

FEDERAL TRADE COMMISSION DECISIONS

FINDING, OPINIONS, AND ORDERS

PUBLISHED BY THE COMMISSION

VOLUME 152



Compiled by
The Office of the Secretary

April J. Tabor, Editor

**MEMBERS OF THE FEDERAL TRADE COMMISSION
DURING THE PERIOD
JULY 1, 2011 TO DECEMBER 31, 2011**

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Took oath of office September 3, 2004.

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Took oath of office January 4, 2006.

J. THOMAS ROSCH, *Commissioner*

Took oath of office January 5, 2006.

EDITH RAMIREZ, *Commissioner*

Took oath of office April 5, 2010.

JULIE BRILL, *Commissioner*

Took oath of office April 6, 2010.

DONALD S. CLARK, *Secretary*

Appointed August 28, 1988.

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FEDERAL TRADE COMMISSION DECISIONS

FINDINGS, OPINIONS, AND ORDERS
JULY 1, 2011, TO DECEMBER 31, 2011

IN THE MATTER OF

SOUTHWEST HEALTH ALLIANCES, INC. D/B/A BSA PROVIDER NETWORK

CONSENT ORDER, ETC. IN REGARD TO ALLEGED VIOLATIONS OF
SEC. 5 OF THE FEDERAL TRADE COMMISSION ACT

*Docket No. C-4327; File No. 091 0013
Filed, July 8, 2011 — Decision, July 8, 2011*

This consent order addresses allegations that BSA Provider Network violated Section 5 of the Federal Trade Commission Act, 15 U.S.C. § 45, by fixing prices charged to those offering coverage for health care services (“payors”) in the Amarillo, Texas, area. The complaint alleges that BSA Provider Network, a multi-specialty independent practice association with a total of approximately 900 physician members in the Amarillo, Texas area, has acted to restrain competition by facilitating, entering into, and implementing agreements to fix the prices and other terms at which it would contract with payers; and to engage in collective negotiations over terms and conditions of dealing with payers. The consent order prohibits Respondent from entering into or facilitating agreements between or among any health care providers (1) to negotiate on behalf of any physician with payer; (2) to negotiate with any physician as a payer; (3) to deal, refuse to deal, or threaten to refuse to deal with any payer; (4) regarding any term, condition, or requirement upon which any physician deals, or is willing to deal, with any payer, including, but not limited to price terms; or (5) not to deal individually with any payer, or not to deal with any payer except through BSA Provider Network.

Participants

For the *Commission*: *John P. Wiegand.*

Complaint

For the *Respondent: William Pakalka and Dan Wellington,
Fulbright & Jaworski.*

COMPLAINT

Pursuant to the provisions of the Federal Trade Commission Act, as amended, 15 U.S.C. § 41 *et seq.* ("FTC Act"), and by virtue of the authority vested in it by said Act, the Federal Trade Commission ("Commission"), having reason to believe that Respondent Southwest Health Alliances, Inc., dba BSA Provider Network ("BSAPN"), hereinafter sometimes referred to as "Respondent," has violated Section 5 of the FTC Act, 15 U.S.C. § 45, and it appearing to the Commission that a proceeding by it in respect thereof would be in the public interest, hereby issues this Complaint stating its charges in that respect as follows:

NATURE OF THE CASE

1. This matter concerns horizontal agreements among competing physicians, acting through Respondent, to fix prices charged to those offering coverage for health care services ("payers") in the Amarillo, Texas, area.

RESPONDENT

2. BSAPN, a physician hospital organization ("PHO"), is a for-profit corporation, organized, existing, and doing business under and by virtue of the laws of the State of Texas, with its principal address at 600 S. Tyler St., Amarillo, TX 79101. BSAPN consists of 25 hospitals; approximately 35 physicians employed by BSAPN's affiliated Health Network, of which approximately 20 are devoted to primary care; and multiple, independent medical practices with a total of approximately 900 physician members, of which approximately 300 are devoted to primary care.

Complaint

THE FTC HAS JURISDICTION OVER RESPONDENT

3. At all times relevant to this Complaint, Respondent has been engaged in the business of negotiating or attempting to negotiate contracts with payers for the provision of physician services on behalf, and for the pecuniary benefit, of its members.

4. Except to the extent that competition has been restrained as alleged herein, BSAPN's physician members have been, and are now, in competition with each other for the provision of physician services in the Amarillo, Texas, area.

5. Respondent is a "person," "partnership," or "corporation" within the meaning of Section 5 of the Federal Trade Commission Act, as amended, 15 U.S.C. § 44.

6. Respondent's general business practices, including the acts and practices herein alleged, are in or affecting "commerce" as defined in the Federal Trade Commission Act, as amended, 15 U.S.C. § 44.

OVERVIEW OF PHYSICIAN CONTRACTING WITH
PAYERS

7. Individual physicians and physician group practices contract with payers of healthcare services and benefits, health maintenance organizations (HMOs), preferred provider organizations (PPOs), self-insured employers, and others, to establish the terms and conditions, including price terms, under which the physicians will render their professional medical services to the payers' subscribers or covered employees and dependents.

8. Physicians and physician group practices sometimes form or participate in financially-integrated or clinically-integrated joint ventures to provide physician services under agreements

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with payers willingly seeking such arrangements. Under such arrangements, the physicians and physician group practices may share financial risks and rewards based on their collective success in achieving pre-established targets or goals regarding aggregate utilization and costs of the services provided to covered individuals or they may engage in other behavior to obtain efficiencies.

9. A PHO that employs physicians may, if it is financially-integrated or clinically-integrated, organize and operate its own HMO or PPO by contracting with its non-employed members, as well as with other hospitals and physician group practices, concerning the terms and conditions, including price terms, under which each provider will render services to the HMO's or PPO's covered lives and dependents.

10. Physicians and physician group practices entering into contracts with payers often agree to accept lower compensation from payers in order to obtain access to additional patients made available by the payers' relationship with the covered individuals. These contracts may reduce payers' costs and enable them to lower the price of insurance or of providing health benefits, thereby resulting in lower medical costs for covered individuals.

11. Competing physicians sometimes use a "messenger" to facilitate their contracting with payers, in ways that do not constitute an unlawful agreement on prices and other competitively significant terms. Messenger arrangements can reduce contracting costs between payers and physicians. For example, a payer may submit a contract offer to the messenger, with the understanding that the messenger will transmit that offer to a group of physicians and inform the payer how many physicians across specialties accept the offer or have a counteroffer. Alternatively, the messenger may receive authority from the individual physicians to accept contract offers that meet certain criteria.

Complaint

12. Other than through their participation in integrated joint ventures, and absent anticompetitive agreements among them, otherwise competing physicians and physician group practices unilaterally decide whether to enter into contracts with payers to provide services to individuals covered by a payer's programs, and what prices they will accept as payment for their services pursuant to such contracts.

RESPONDENT'S OPERATION

13. Since its formation, BSAPN has purportedly administered contracts with payers for and on behalf of its respective physician members through a "messenger model," under which BSAPN received offers from payers and messengered those offers to its physician members who each made a unilateral, independent decision to accept or reject a payer's offer.

14. Since its formation, BSAPN also has purportedly administered contracts with payers for and on behalf of its respective physician members through a "reverse messenger model," under which BSAPN surveyed its respective member physicians on a unilateral, independent basis to determine at what price level each of them would agree to contract with payers. From the results of this survey, BSAPN constructed its own fee schedule which it offered to payers as a contract in which all its physician members would participate.

15. Since its formation, BSAPN has used its own fee schedule to offer a non-risk-bearing PPO to self-insured or independently-insured employers.

16. The member physicians' participation in BSAPN and their offering of services through BSAPN's administered contracts, was not, however, the member physicians' exclusive method of selling their professional medical services. Rather, the member

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physicians also continued to sell their medical services individually, on a fee-for-service basis, outside of BSAPN, to individual patients and through contracts individually and directly entered into with payers.

ANTICOMPETITIVE CONDUCT

17. Since at least 2000, BSAPN, acting as a combination of its physician members, and in conspiracy with its members, has acted to restrain competition by, among other things, facilitating, entering into, and implementing agreements, express or implied, to fix the prices and other terms at which they would contract with payers; and to engage in collective negotiations over terms and conditions of dealing with payers.

18. Since at least 2000, BSAPN has established its own fee schedule through direct negotiations with its physician members.

19. Since at least 2000, BSAPN has used the prices in its own fee schedule as a signaling device as to whether its members should accept or reject offers it messengered on behalf of some payers.

20. Since at least 2000, BSAPN, with some payers, has renegotiated contracts that were originally administered through a messenger model. In these renegotiations, price was increased based on a demand BSAPN made on behalf of its physician members. The physician members received a new, higher reimbursement rate and did not make a unilateral, independent decision to accept or reject a payer's offer.

21. Since at least 2000, BSAPN has periodically increased the rates of its own fee schedule in contracts administered through a reverse messenger model. In implementing these rate increases, BSAPN did not survey its physician members on a unilateral,

Complaint

independent basis to determine at what price level each of them would agree to contract with payers.

RESPONDENT'S CONDUCT IS NOT LEGALLY JUSTIFIED

22. Respondent's joint negotiation of fees and other competitively significant terms, and the agreements, acts, and practices described above, have not been, and are not, reasonably related to any efficiency-enhancing integration among the physician members of BSAPN.

RESPONDENT'S ACTIONS HAVE HAD, OR COULD BE EXPECTED TO HAVE, SUBSTANTIAL ANTICOMPETITIVE EFFECTS

23. Respondent's actions described in Paragraphs 14 through 16 of this Complaint have had, have tended to have, or if successful would have had, the effect of restraining trade unreasonably and hindering competition in the provision of physician services in the Amarillo, Texas, area in the following ways, among others:

- a. unreasonably restraining price and other forms of competition among physicians who are members of BSAPN;
- b. increasing prices for physician services;
- c. depriving payers, including insurers and employers, and individual consumers, of the benefits of competition among physicians; and
- d. depriving consumers of the benefits of competition among payers.

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24. The combination, conspiracy, acts, and practices described above constitute unfair methods of competition in violation of Section 5 of the Federal Trade Commission Act, as amended, 15 U.S.C. § 45. Such combination, conspiracy, acts, and practices, or the effects thereof, are continuing and will continue or recur in the absence of the relief herein requested.

WHEREFORE, THE PREMISES CONSIDERED, the Federal Trade Commission on this eighth day of July, 2011, issues its Complaint against Respondent BSAPN.

By the Commission.

DECISION AND ORDER

The Federal Trade Commission (“Commission”), having initiated an investigation of certain acts and practices of Southwest Health Alliances, Inc., dba BSA Provider Network (“BSAPN”), herein sometimes referred to as “Respondent,” and Respondent having been furnished thereafter with a copy of the draft Complaint that counsel for the Commission proposed to present to the Commission for its consideration and which, if issued, would charge Respondent with violations of Section 5 of the Federal Trade Commission Act (“Act”), as amended, 15 U.S.C. § 45; and

Respondent, its attorney, and counsel for the Commission having thereafter executed an Agreement Containing Consent Order to Cease and Desist (“Consent Agreement”), containing an admission by Respondent of all the jurisdictional facts set forth in

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the aforesaid draft Complaint, a statement that the signing of said Consent Agreement is for settlement purposes only and does not constitute an admission by Respondent that the law has been violated as alleged in such Complaint, or that the facts as alleged in such Complaint, other than jurisdictional facts, are true, and waivers and other provisions as required by the Commission's Rules; and

The Commission having thereafter considered the matter and having determined that it had reason to believe that Respondent has violated the Act, and that a Complaint should issue stating its charges in that respect, and having accepted the executed Consent Agreement and placed such Consent Agreement on the public record for a period of thirty (30) days for the receipt and consideration of public comments, now in further conformity with the procedure described in Commission Rule 2.34, 16 C.F.R. § 2.34, the Commission hereby issues its Complaint, makes the following jurisdictional findings and issues the following Order:

1. Respondent BSAPN is a for-profit corporation, organized, existing, and doing business under and by virtue of the laws of the State of Texas, with its principal address at 600 South Tyler St., Amarillo, TX 79101.
2. The Federal Trade Commission has jurisdiction of the subject matter of this proceeding and of Respondent, and this proceeding is in the public interest.

ORDER**I.**

IT IS ORDERED that, as used in this Order, the following definitions shall apply:

Decision and Order

- A. “Respondent” means Southwest Health Alliances, Inc., dba BSA Provider Network ("BSAPN"), its officers, directors, employees, agents, attorneys, representatives, successors, and assigns; and the subsidiaries, divisions, groups, and affiliates controlled by it, and the respective officers, directors, employees, agents, attorneys, representatives, successors, and assigns of each.
- B. “Medical Group Practice” means a bona fide, integrated firm in which physicians practice medicine together as partners, shareholders, owners, members, or employees, or in which only one Physician practices medicine.
- C. “Participate” in an entity means (1) to be a partner, shareholder, owner, member, or employee of such entity, or (2) to provide services, agree to provide services, or offer to provide services, to a Payer through such entity. This definition also applies to all tenses and forms of the word “participate,” including, but not limited to, “participating,” “participated,” and “participation.”
- D. “Payer” means any Person that pays, or arranges for the payment, for all or any part of any Physician services for itself or for any other Person, as well as any Person that develops, leases, or sells access to networks of Physicians.
- E. “Person” means both natural Persons and artificial Persons, including, but not limited to, corporations, unincorporated entities, and governments.
- F. “Physician” means a doctor of allopathic medicine (“M.D.”) or a doctor of osteopathic medicine (“D.O.”).

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- G. “Preexisting Contract” means a contract for the provision of Physician services that was in effect on the date of the receipt by a Payer that is a party to such contract of notice sent by Respondent BSAPN, pursuant to Paragraph VII.A.2 of this Order, of such Payer’s right to terminate such contract.
- H. “Qualified Clinically-Integrated Joint Arrangement” means an arrangement to provide Physician services in which:
1. all Physicians who Participate in the arrangement Participate in active and ongoing programs of the arrangement to evaluate and modify the practice patterns of, and create a high degree of interdependence and cooperation among, the Physicians who Participate in the arrangement, in order to control costs and ensure the quality of services provided through the arrangement; and
 2. any agreement concerning price or other terms or conditions of dealing entered into by or within the arrangement is reasonably necessary to obtain significant efficiencies that result from such integration through the arrangement.
- I. “Qualified Risk-Sharing Joint Arrangement” means an arrangement to provide Physician services in which:
1. all Physicians who Participate in the arrangement share substantial financial risk through their Participation in the arrangement and thereby create incentives for the Physicians who Participate jointly to control costs and improve quality by

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managing the provision of Physician services such as risk-sharing involving:

- a. the provision of Physician services at a capitated rate;
 - b. the provision of Physician services for a predetermined percentage of premium or revenue from Payers;
 - c. the use of significant financial incentives (e.g., substantial withholds) for Physicians who Participate to achieve, as a group, specified cost-containment goals; or
 - d. the provision of a complex or extended course of treatment that requires the substantial coordination of care by Physicians in different specialties offering a complementary mix of services, for a fixed, predetermined price, when the costs of that course of treatment for any individual patient can vary greatly due to the individual patient's condition, the choice, complexity, or length of treatment, or other factors; and
2. any agreement concerning price or other terms or conditions of dealing entered into by or within the arrangement is reasonably necessary to obtain significant efficiencies that result from such integration through the arrangement.
- J. "Qualified Arrangement" means a Qualified Clinically-Integrated Joint Arrangement or a Qualified Risk-Sharing Joint Arrangement.

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II.

IT IS FURTHER ORDERED that Respondent, directly or indirectly, or through any corporate or other device, in connection with the provision of Physician services in or affecting commerce, as “commerce” is defined in Section 4 of the Federal Trade Commission Act, 15 U.S.C. § 44, cease and desist from:

- A. Entering into, adhering to, Participating in, maintaining, organizing, implementing, enforcing, or otherwise facilitating any combination, conspiracy, agreement, or understanding between or among any Physicians with respect to its provision of Physician services:
1. To negotiate on behalf of any Physician with any Payer, including Respondent when operating as a Payer;
 2. To negotiate with any Physician as a Payer;
 3. To refuse to deal, or threaten to refuse to deal, with any Payer, in furtherance of any conduct or agreement that is prohibited by any other provision of Paragraph II of this Order;
 4. Regarding any term, condition, or requirement upon which any Physician deals, or is willing to deal, with any Payer, including, but not limited to, price terms; or
 5. Not to deal individually with any Payer, or not to deal with any Payer other than through Respondent;

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- B. Exchanging or facilitating in any manner the exchange or transfer of information among Physicians concerning any Physician's willingness to deal with a Payer, or the terms or conditions, including price terms, on which the Physician is willing to deal with a Payer;
- C. Attempting to engage in any action prohibited by Paragraphs II.A or II.B above; and
- D. Encouraging, suggesting, advising, pressuring, inducing, or attempting to induce any Person to engage in any action that would be prohibited by Paragraphs II.A through II.C above.

Provided, however, that nothing in this Paragraph II shall prohibit any agreement or conduct involving Respondent that, subject to the requirements of Paragraph V of this Order, is reasonably necessary to form, Participate in, or take any action in furtherance of, a Qualified Arrangement.

III.

IT IS FURTHER ORDERED that, for five (5) years from the date this Order becomes final, for any arrangement under which Respondent would act as an agent, or as a messenger, on behalf of any Physician or any Medical Group Practice with any Payer regarding contracts, except for those contracts under which Respondent is, or will be, paid on a capitated (per member per month) rate by the Payer, Respondent shall notify the Commission in writing ("Paragraph III Notification") at least sixty (60) days prior to entering into the arrangement for which Paragraph III Notification is required. The Paragraph III Notification shall include the number of proposed Physician Participants in the proposed arrangement; the proposed geographic area in which the proposed arrangement would

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operate; a copy of any proposed Physician Participation agreement; a description of the proposed arrangement's purpose and function; a description of any resulting efficiencies expected to be obtained through the proposed arrangement; and a description of procedures to be implemented to limit possible anticompetitive effects of the proposed arrangement, such as those prohibited by this Order.

IV.**IT IS FURTHER ORDERED** that:

- A. If, within sixty (60) days from the date of the Commission's receipt of the Paragraph III Notification, a representative of the Commission makes a written request to the Respondent for additional information, then Respondent shall not participate in the proposed arrangement prior to the expiration of thirty (30) days after substantially complying with such request, or such shorter waiting period as may be granted in writing from the Bureau of Competition;
- B. The expiration of any waiting period described herein without a request for additional information, or without the initiation of an enforcement proceeding, shall not be construed as a determination by the Commission, or its staff, that the proposed arrangement does or does not violate this Order or any law enforced by the Commission;
- C. The absence of notice that the proposed arrangement has been rejected, regardless of a request for additional information, shall not be construed as a determination by the Commission, or its staff, that the proposed arrangement has been approved;

Decision and Order

- D. Receipt by the Commission of any Paragraph III Notification is not to be construed as a determination by the Commission, or its staff, that the proposed arrangement does or does not violate this Order or any law enforced by the Commission; and
- E. Paragraph III Notification shall not be required prior to participating in any arrangement for which Paragraph III Notification has previously been given.

V.

IT IS FURTHER ORDERED that for five (5) years from the date this Order becomes final, pursuant to each Qualified Arrangement in which Respondent is a Participant, except for those contracts under which Respondent is, or will be, paid on a capitated (per member per month) rate by the Payer, (“Paragraph V Arrangement”), Respondent shall notify the Commission in writing (“Paragraph V Notification”) at least sixty (60) days prior to:

- A. Participating in, organizing, or facilitating any discussion or understanding with or among any Physicians or Medical Group Practices in such Arrangement relating to price terms or conditions of dealing with any Payer; or
- B. Contacting a payer, pursuant to an Arrangement to negotiate or enter into any agreement concerning price or other terms or conditions of dealing with any Payer, on behalf of any Physician or Medical Group Practice in such Arrangement.

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VI.**IT IS FURTHER ORDERED** that:

- A. Paragraph V Notification shall include the following information regarding the Qualified Arrangement pursuant to which the Respondent intends to engage in the above identified conduct:
1. the total number of Physicians and the number of Physicians in each specialty participating in the Qualified Arrangement;
 2. a description of the Qualified Arrangement, including its purpose and geographic area of operation;
 3. a description of the nature and extent of the integration and the efficiencies resulting from the Qualified Arrangement;
 4. an explanation of the relationship of any agreement on prices, or contract terms related to price, to furthering the integration and achieving the efficiencies of the Qualified Arrangement;
 5. a description of any procedures proposed to be implemented to limit possible anticompetitive effects resulting from the Qualified Arrangement or its activities; and
 6. all studies, analyses, and reports that were prepared for the purpose of evaluating or analyzing competition for Physician services in any relevant market, including, but not limited to, the market share of Physician services in any relevant market.

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- B. If, within sixty (60) days from the Commission's receipt of the Paragraph V Notification, a representative of the Commission makes a written request to Respondent for additional information, then Respondent shall not participate in any arrangement described in Paragraph V.A or Paragraph V.B of this Order prior to the expiration of thirty (30) days after substantially complying with such request for additional information, or such shorter waiting period as may be granted in writing from the Bureau of Competition;
- C. The expiration of any waiting period described herein without a request for additional information, or without the initiation of an enforcement proceeding, shall not be construed as a determination by the Commission, or its staff, that the proposed Qualified Arrangement does or does not violate this Order or any law enforced by the Commission;
- D. The absence of notice that the proposed Qualified Arrangement has been rejected, regardless of a request for additional information, shall not be construed as a determination by the Commission, or its staff, that the proposed Qualified Arrangement has been approved;
- E. Receipt by the Commission of any Paragraph V Notification regarding participation pursuant to a proposed Qualified Arrangement is not to be construed as a determination by the Commission that any such proposed Qualified Arrangement does or does not violate this Order or any law enforced by the Commission; and

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- F. Paragraph V Notification shall not be required prior to participating in any Qualified Arrangement for which Paragraph V Notification has previously been given.

VII.

IT IS FURTHER ORDERED that Respondent shall:

- A. Within thirty (30) days from the date on which this Order becomes final:
1. send by first-class mail with delivery confirmation or return receipt requested, or electronic mail with return confirmation, a copy of this Order and the Complaint to:
 - a. every Physician who Participates, or has Participated, in Respondent at any time since January 1, 2006; and
 - b. each current officer, director, manager, and employee of Respondent; and
 2. send by first-class mail, return receipt requested, a copy of this Order, the Complaint, and the letter attached as Appendix A to this Order to the chief executive officer of each Payer that has contracted with Respondent for the provision of Physician services at any time since January 1, 2006 regarding contracting for the provision of Physician services, except for those contracts under which Respondent is, or will be, paid a capitated (per member per month) rate by the Payer;
- B. Terminate, without penalty or charge, and in compliance with any applicable laws, any Preexisting

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Contract with any Payer who is sent the letter required by Paragraph VII.A.2 of this Order, at the earlier of: (1) receipt by Respondent BSAPN of a written request to terminate such contract from any Payer that is a party to the contract, or (2) the earliest termination date, renewal date (including any automatic renewal date), or the anniversary date of such contract.

Provided, however, a Preexisting Contract for Physician services may extend beyond any such termination or renewal date no later than one (1) year from the date that the Order becomes final if, prior to such termination or renewal date:

(a) the Payer submits to Respondent BSAPN a written request to extend such contract to a specific date no later than one (1) year from the date that this Order becomes final, and

(b) Respondent BSAPN has determined not to exercise any right to terminate.

Provided further, that any Payer making such request to extend a contract retains the right, pursuant to Paragraph VII.B of this Order, to terminate the Preexisting Contract at any time.

- C. Within ten (10) days of receiving a written request to terminate from a Payer, pursuant to Paragraph VII.B of this Order, distribute, by first-class mail, return receipt requested, or electronic mail with return confirmation, a copy of that request to each Physician Participating in such contract as of the date that Respondent BSAPN receives such request to terminate.

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- D. For five (5) years from the date this Order becomes final:
1. Distribute a copy of this Order and the Complaint to:
 - a. each Physician who begins Participating in Respondent, and who did not previously receive a copy of this Order and the Complaint from Respondent, by first-class mail, return receipt requested, or electronic mail with return confirmation, within thirty (30) days of the time that such Participation begins;
 - b. each payer who contracts with Respondent for the provision of Physician services, except for those Payers who contract with Respondent solely for Physician services that are, or will be, paid on a capitated (per member per month) rate by the Payer, and who did not previously receive a copy of this Order and the Complaint from Respondent, by first-class mail, return receipt requested, within thirty (30) days of the time that such Payer enters into such contract; and
 - c. Each Person who becomes an officer, director, manager, or employee of Respondent, and who did not previously receive a copy of this Order and the Complaint from Respondent, by first-class mail, return receipt requested, or electronic mail with return confirmation, within thirty (30) days of the time that he or she assumes such position with Respondent; and

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1. Annually publish in an official annual report or newsletter sent to all Physicians who Participate in Respondent, a copy of this Order and the Complaint with such prominence as is given to regularly featured articles.
- E. File verified written reports within sixty (60) days from the date this Order becomes final, annually thereafter for five (5) years on the anniversary of the date this Order becomes final, and at such other times as the Commission may by written notice require. Each report shall include:
1. a detailed description of the manner and form in which the Respondent has complied and is complying with this Order;
 2. the name, address, and telephone number of each Payer with which the Respondent has had any contact, during the one (1) year period preceding the date for filing such report, except for Payers whose sole contacts with Respondent relate to contracts under which Respondent is, or will be, paid a capitated (per member per month) rate by the Payer;
 3. the identity of each Payer sent a copy of the letter attached as Appendix A, the response of each Payer to that letter, and the status of each contract to be terminated pursuant to that letter; and
 4. copies of the delivery confirmations, signed return receipts, or electronic mail with return confirmations required by Paragraph VII.A.I, and copies of the signed return receipts required by Paragraphs VII.A.2, VII.C, and VII.D.

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VIII.

IT IS FURTHER ORDERED that Respondent shall notify the Commission:

- A. of any change in its principal address within twenty (20) days of such change in address; and
- B. at least thirty (30) days prior to any proposed: (1) dissolution of Respondent; (2) acquisition, merger, or consolidation of Respondent; or (3) any other change in Respondent including, but not limited to, assignment and the creation or dissolution of subsidiaries, if such change might affect compliance obligations arising out of this Order.

IX.

IT IS FURTHER ORDERED that, for the purpose of determining or securing compliance with this Order, and subject to any legally recognized privilege, and upon written request and upon five (5) days notice to Respondent, Respondent shall, without restraint or interference, permit any duly authorized representative of the Commission:

- A. Access, during office hours of Respondent, and in the presence of counsel, to all facilities and access to inspect and copy all books, ledgers, accounts, correspondence, memoranda, and all other records and documents in the possession, or under the control, of Respondent relating to compliance with this Order, which copying services shall be provided by Respondent at its expense; and

Decision and Order

- B. To interview officers, directors, or employees of Respondent, who may have counsel present, regarding such matters.

X.

IT IS FURTHER ORDERED that this Order shall terminate on July 8, 2031.

By the Commission.

Decision and Order

APPENDIX A

[Respondent's Letterhead]

[Name of Payer's CEO]

[Address]

Dear _____:

Enclosed is a copy of a complaint and a consent order ("Order") issued by the Federal Trade Commission against BSAPN.

Pursuant to Paragraph VII.B of the Order, BSAPN must allow you to terminate, upon your written request without any penalty or charge, any contracts with BSAPN for the provision of physician services that were in effect prior to your receipt of this letter.

Paragraph VII.B of the Order also provides that, if you do not terminate your contract, the contract will terminate at the earlier of [date one year from the date the Order becomes final] or its earliest termination or renewal date (including any automatic renewal date). If the termination or renewal date occurs prior to [date one year from the date the Order becomes final], you may request BSAPN to extend that date to a date no later than [date one year from the date the Order becomes final]. If you choose to extend the term of the contract, you may nevertheless still terminate the contract at any time. At the end of any contract extensions you may, of course, elect to enter into a new contract with BSAPN in a manner consistent with the terms of the Order.

Sincerely,

[BSAPN to fill in information in brackets]

Analysis to Aid Public Comment

**ANALYSIS OF AGREEMENT CONTAINING CONSENT
ORDER TO AID PUBLIC COMMENT**

The Federal Trade Commission has accepted, subject to final approval, an agreement containing a proposed Consent Order with Southwest Health Alliances, Inc., dba BSA Provider Network (“BSA Provider Network” or “Respondent”). The agreement settles charges that BSA Provider Network violated Section 5 of the Federal Trade Commission Act, 15 U.S.C. § 45, by fixing prices charged to those offering coverage for health care services (“payors”) in the Amarillo, Texas, area. The proposed Consent Order has been placed on the public record for 30 days to receive comments from interested persons. Comments received during this period will become part of the public record. After 30 days, the Commission will review the agreement and the comments received, and will decide whether it should withdraw from the agreement or make the proposed Consent Order final.

The purpose of this analysis is to facilitate public comment on the proposed Consent Order. The analysis is not intended to constitute an official interpretation of the agreement and proposed Consent Order or to modify their terms in any way. Further, the proposed Consent Order has been entered into for settlement purposes only and does not constitute an admission by Respondent that it violated the law or that the facts alleged in the Complaint (other than jurisdictional facts) are true.

The Complaint’s Allegations

BSA Provider Network is a multi-specialty independent practice association consisting of multiple, independent medical practices with a total of approximately 900 physician members, of which approximately 300 are devoted to primary care, in the Amarillo, Texas, area.

Analysis to Aid Public Comment

Since at least 2000, BSA Provider Network has acted to restrain competition by facilitating, entering into, and implementing agreements to fix the prices and other terms at which it would contract with payers; and to engage in collective negotiations over terms and conditions of dealing with payers.

BSA Provider Network did not engage in any activity that might justify collective agreements on the prices its members would accept for their services. For example, the physicians in BSA Provider Network have not clinically or financially integrated their practices to create efficiencies sufficient to justify their acts and practices. The Respondent's actions have restrained price and other forms of competition among physicians in the Amarillo, Texas, area and thereby harmed consumers (including health plans, employers, and individual consumers) by increasing the prices for physician services.

The Proposed Consent Order

The proposed Consent Order is designed to prevent the continuance and recurrence of the illegal conduct alleged in the complaint while it allows BSA Provider Network to engage in legitimate, joint conduct. The proposed Consent Order does not affect BSA Provider Network's activities in contracting with payers on a capitated basis.

Paragraph II.A prohibits Respondent from entering into or facilitating agreements between or among any health care providers: (1) to negotiate on behalf of any physician with payer; (2) to negotiate with any physician as a payer; (3) to deal, refuse to deal, or threaten to refuse to deal with any payer; (4) regarding any term, condition, or requirement upon which any physician deals, or is willing to deal, with any payer, including, but not limited to price terms; or (5) not to deal individually with any payer, or not to deal with any payer except through BSA Provider Network.

Analysis to Aid Public Comment

The other parts of Paragraph II reinforce these general prohibitions. Paragraph II.B prohibits Respondent from facilitating exchanges of information between health care providers concerning whether, or on what terms, to contract with a payer. Paragraph II.C bars attempts to engage in any action prohibited by Paragraph II.A or II.B, and Paragraph II.D proscribes encouraging, suggesting, advising, pressuring, inducing, or attempting to induce any person to engage in any action that would be prohibited by Paragraphs II.A through II.C.

As in other Commission orders addressing health care providers' collective bargaining with health care purchasers, certain kinds of agreements are excluded from the general bar on joint negotiations. Paragraph II does not preclude BSA Provider Network from engaging in conduct that is reasonably necessary to form or participate in legitimate "qualified risk-sharing" or "qualified clinically-integrated" joint arrangements, as defined in the proposed Consent Order. Also, Paragraph II would not bar agreements that only involve physicians who are part of the same medical group practice, defined in Paragraph I.B, because it is intended to reach agreements between and among independent competitors.

Paragraphs III-VI require BSA Provider Network to notify the Commission before it initiates certain contacts regarding contracts with payers. Paragraphs III and IV apply to arrangements under which BSA Provider Network would be acting as a messenger on behalf of its member physicians. Paragraphs V and VI apply to arrangements under which BSA Provider Network plans to achieve financial or clinical integration.

Paragraph VII.A requires BSA Provider Network to send a copy of the Complaint and Consent Order to its physician members, its management and staff, and any payers who communicated with BSA Provider Network, or with whom BSA

Analysis to Aid Public Comment

Provider Network communicated, with regard to any interest in contracting for physician services.

Paragraph VII.B allows for contract termination if a payer voluntarily submits a request to BSA Provider Network to terminate its contract. Pursuant to such a request, Paragraph VII.B requires BSA Provider Network to terminate, without penalty, any payer contracts that they had entered into since it began its alleged restraint of trade in 2000. This provision is intended to eliminate the effects of BSA Provider Network's joint price setting behavior. Paragraph VII.C requires that BSA Provider Network send a copy of any payer's request for termination to every physician who participates in each group.

Paragraph VII.D contains notification provisions relating to future contact with physicians, payers, management, and staff. These provisions require BSA Provider Network to distribute a copy of the Complaint and Consent Order to each physician who begins participating in each group; each payer who contacts each group regarding the provision of physician services; and each person who becomes an officer, director, manager, or employee for three years after the date on which the Consent Order becomes final. In addition, Paragraph VII.D requires BSA Provider Network to publish a copy of the Complaint and Consent Order, for three years, in any official publication that it sends to its participating physicians

Paragraphs VII.E and VIII-IX impose various obligations on BSA Provider Network to report or to provide access to information to the Commission to facilitate monitoring its compliance with the Consent Order.

Pursuant to Paragraph X, the proposed Consent Order will expire 20 years from the date it is issued.

IN THE MATTER OF

Complaint

**IRVING OIL LIMITED AND IRVING OIL TERMINALS
INC.**CONSENT ORDER, ETC. IN REGARD TO ALLEGED VIOLATIONS OF
SEC. 5(A) OF THE FEDERAL TRADE COMMISSION ACT AND SEC. 7
OF THE CLAYTON ACT*Docket No. C-4328; File No. 101 0021
Filed, July 12, 2011 — Decision, July 12, 2011*

This consent order addresses allegations relating to the proposed acquisition by Irving and Irving Oil Transportation Company LLC (collectively, “Irving”) of certain petroleum products storage and transportation assets located in Maine from ExxonMobil Oil Corporation (“ExxonMobil”). The complaint alleges that the acquisition, if consummated, would substantially lessen competition in the gasoline and distillates terminaling services markets in the South Portland and Bangor/Penobscot Bay areas of Maine, in violation of Section 7 of the Clayton Act and Section 5 of the Federal Trade Commission Act. The consent order requires Irving to divest its acquisition rights to the ExxonMobil Bangor terminal and intrastate pipeline, as well as 50% of ExxonMobil’s South Portland terminal, to Buckeye Partners, L.P. and its affiliate Buckeye Pipe Line Holdings, L.P. Irving will form a joint venture that will purchase ExxonMobil’s South Portland terminal and Buckeye will manage and operate this terminal on behalf of the Irving-Buckeye joint venture. The consent order also requires that Irving enter into a throughput agreement with Buckeye at each of the petroleum products terminals.

Participants

For the *Commission*: *Robert E. Friedman, Brian Telpner,*
and *Michelle Wyant.*

For the *Respondents*: *Joel Grosberg, Raymond A. Jacobsen,*
Jr., and Joseph Winterscheid, McDermott Will & Emery LLP; and
John S. Upton, Perkins Thompson.

Complaint

COMPLAINT

Pursuant to the provisions of the Federal Trade Commission Act, and by virtue of the authority vested in it by said Act, the Federal Trade Commission, having reason to believe that Irving Oil Limited and Irving Oil Terminals Inc. (collectively “Irving”) and ExxonMobil Oil Corporation and Mobil Pipe Line Company (collectively “ExxonMobil”) have entered into an acquisition agreement which, if consummated, would violate Section 7 of the Clayton Act, as amended, 15 U.S.C. § 18, and Section 5 of the Federal Trade Commission Act, as amended, 15 U.S.C. § 45, and it appearing to the Federal Trade Commission that a proceeding by it in respect thereof would be in the public interest, hereby issues its complaint stating its charges as follows:

I. RESPONDENTS

3. Respondent Irving Oil Limited is a privately-held energy processing, transporting, and marketing company organized, existing, and doing business under, and by virtue of, the laws of Canada, with its office and principal place of business located at 10 Sydney Street, Saint John, New Brunswick, Canada E2L 4K1. Irving Oil Limited is the ultimate parent entity of Irving Oil Terminals Inc.

4. Respondent Irving Oil Terminals Inc. is a corporation organized, existing, and doing business under, and by virtue of, the laws of the State of Delaware, with its office and principal place of business located at 190 Commerce Way, Portsmouth, New Hampshire 03801.

5. Respondent Irving Oil Terminals Inc. supplies branded and unbranded petroleum products throughout New England to third-party distributors, retailers, various other re-sellers, and governmental and commercial end-users. Irving, through other subsidiaries, also owns retail travel plazas that sell gasoline and

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diesel petroleum products. In Maine, Irving Oil Terminals Inc. owns a petroleum products terminal in Searsport and co-owns a petroleum products terminal with CITGO in South Portland.

II. JURISDICTION

6. Respondents Irving Oil Limited and Irving Oil Terminals Inc. are, and at all relevant times have been, engaged in commerce, as “commerce” is defined in Section 1 of the Clayton Act, as amended, 15 U.S.C. § 12, and are companies whose businesses are in or affecting commerce as “commerce” is defined in Section 4 of the Federal Trade Commission Act, as amended, 15 U.S.C. § 44.

III. PROPOSED ACQUISITIONS

7. On November 3, 2009, Irving announced it would acquire ExxonMobil’s petroleum products terminals located in Bangor and South Portland, Maine and pipeline connecting the two terminals (collectively “Proposed Acquisitions”).

IV. TRADE AND COMMERCE

Relevant Product Markets

8. For purposes of this complaint, the relevant lines of commerce in which to analyze the effects of the Proposed Acquisitions are gasoline terminaling services and distillates terminaling services.

9. Terminals generally consist of several storage tanks and loading racks that pump fuels into tanker trucks for further delivery. Terminals are specialized facilities connected to one or more fuel supply sources, have the capacity to store fuel shipments, and must be configured properly to distribute the fuel to customers. Light petroleum products terminals are specialized facilities that receive gasoline, diesel fuel, heating oil, kerosene,

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and jet fuel, among other products, by pipeline, by water, by rail, or directly from refinery production. These products are stored or redistributed by pipeline, water, rail, or truck. Terminals are critical to the sale and distribution of transportation fuels.

10. Terminaling services consist of a cluster of services related to the bulk receipt, storage, and throughput of petroleum products. Terminals also perform value-added services, such as handling and injection of motor fuel additives (including ethanol) as petroleum products are redelivered across the truck rack.

11. Only terminals with vapor recovery equipment, internal floating roofs, and specialized environmental and safety permits can store gasoline. However, tanks configured and permitted to store gasoline can always store distillates. Thus terminals that store gasoline compete in both the gasoline terminaling services and distillates terminaling services markets. Terminals that store only distillates compete only in the distillates terminaling services market.

Relevant Geographic Markets

12. For purposes of this complaint, the relevant geographic areas in which to analyze the effects of the Proposed Acquisitions on terminaling services are the Bangor/Penobscot Bay and the South Portland areas of Maine.

13. The Bangor/Penobscot Bay area encompasses the state of Maine north of Waterville, including Bangor, Searsport, and Bucksport.

14. The South Portland area encompasses the state of Maine south of Waterville, including South Portland.

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V. AFFECTED MARKETS**Gasoline Terminaling Services in the
Bangor/Penobscot Bay Area**

15. Irving's terminal in Searsport and ExxonMobil's terminal in Bangor are two of three terminals in the Bangor/Penobscot Bay area capable of independently offering gasoline terminaling services. Only ExxonMobil and Irving independently offer gasoline terminaling services today.

16. If the Proposed Acquisitions are consummated, Irving will control the infrastructure that delivers bulk gasoline to the Bangor/Penobscot Bay area. This control would allow Irving unilaterally to raise the price for or restrict the availability of gasoline terminaling services in the Bangor/Penobscot Bay area and raise gasoline prices to customers served from Bangor/Penobscot Bay area terminals.

**Distillates Terminaling Services in the
Bangor/Penobscot Bay Area**

17. There are five petroleum products terminals in the Bangor/Penobscot Bay area, owned by Irving (Searsport), ExxonMobil (Bangor), Coldbrook (Bangor), Webber (Bucksport), and Sprague (Searsport).

18. Four terminals in the Bangor/Penobscot Bay area independently provide, or could provide, distillates terminaling services. The Proposed Acquisitions reduce the number of independent distillates terminaling services competitors from four to three in the Bangor/Penobscot Bay market.

19. Post-acquisition, without competition from ExxonMobil, the remaining three independent firms would be substantially more likely to coordinate in raising fees or reducing the quality and

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availability of distillates terminaling services in the Bangor/Penobscot Bay market.

Gasoline Terminaling Services in the
South Portland Area

20. Six firms own five terminals in the South Portland area, with Irving and CITGO sharing ownership of one of these terminals. Only three of these terminals are capable of storing gasoline. These terminals are owned by Irving and CITGO (sharing ownership of one terminal), ExxonMobil, and Gulf Oil LP (“Gulf”). The terminals owned by Sprague Energy Corporation and Global Partners LP terminals in South Portland do not store gasoline.

21. The Proposed Acquisitions reduce the number of participants in the South Portland gasoline terminaling services market from four to three and enhance the ability and incentive of the remaining participants to coordinate to increase gasoline terminaling services fees.

22. Maine receives gasoline virtually exclusively via marine vessels. Importing gasoline from Europe on large cargo vessels is less costly than the alternative of shipping it from domestic ports on smaller barges. Therefore, most Maine gasoline is imported from outside the United States. Post-acquisition, Irving will control sufficient terminal capacity in Maine to constrain the ability of others to import gasoline into South Portland terminals at current prices.

23. Because the Bangor terminals receive gasoline via the ExxonMobil pipeline from South Portland, Irving’s control of this pipeline, its Searsport terminal, and the ExxonMobil South Portland terminal gives Irving the unfettered ability to raise the cost of gasoline supplied from Bangor/Penobscot Bay area terminals to retail stations and other consumers.

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Distillates Terminaling Services in the
South Portland Area

24. There are five petroleum products terminals in the South Portland area. Each of the five terminals in the South Portland area participates in the distillates terminaling services market. Irving and CITGO share ownership of one of these terminals. ExxonMobil, Global, Gulf, and Sprague each own one of the remaining four terminals.

25. The acquisition reduces the number of participants in the South Portland distillates terminaling services market from six to five. Post-acquisition, without competition from ExxonMobil, the remaining five firms would be substantially more likely to coordinate in raising fees for and reducing the quality and availability of distillates terminaling services in the South Portland area.

VI. ENTRY CONDITIONS

26. Entry into the relevant markets would not be timely, likely, or sufficient to prevent or defeat the anticompetitive effects of the Proposed Acquisitions.

27. Entry into the relevant markets is costly, difficult, and unlikely because of, among other things, the difficulty of obtaining regulatory approvals and the presence of excess terminal capacity in both markets. A new entrant would be unlikely to invest in a new terminal, with substantial sunk costs, in these markets which already have sufficient capacity.

28. A terminal that cannot currently store gasoline is unlikely to reconfigure its tanks to store gasoline in response to an anticompetitive price increase in gasoline terminaling due to the

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significant cost and limited ability to attract large customer volumes.

VII. EFFECTS OF THE PROPOSED ACQUISITIONS

29. The effects of the Proposed Acquisitions, if consummated, may be substantially to lessen competition and to tend to create a monopoly in the relevant markets in violation of Section 7 of the Clayton Act, as amended, 15 U.S.C. § 18, and Section 5 of the Federal Commission Act, as amended, 15 U.S.C. § 45, in the following ways, among others:

- a. by eliminating actual, direct, and substantial competition between Respondents and ExxonMobil;
- b. by increasing the likelihood that Respondents would unilaterally exercise market power in the relevant markets; and
- c. by enhancing the likelihood of collusion or coordinated interaction between or among the remaining firms in the relevant markets.

IX. VIOLATIONS CHARGED

Count I – Illegal Acquisition

30. The allegations of Paragraphs 1 through 27 above are incorporated by reference as though fully set forth here.

31. The transactions described in Paragraph 5 above, if consummated, would substantially lessen competition in the affected markets in violation of Section 7 of the Clayton Act, as amended, 15 U.S.C. § 18, and Section 5 of the Federal Trade Commission Act, as amended, 15 U.S.C. § 45.

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Count II – Illegal Agreement

32. The allegations of Paragraphs 1 through 27 above are incorporated by reference as though fully set forth.

33. Respondent Irving, through the agreements described in Paragraph 5 above, has engaged in unfair methods of competition in or affecting competition in violation of Section 5 of the Federal Trade Commission Act, as amended, 15 U.S.C. § 45.

WHEREFORE, THE PREMISES CONSIDERED, the Federal Trade Commission on this twelfth day of July, 2011, issues its complaint against said Respondents.

By the Commission.

Decision and Order

DECISION AND ORDER

The Federal Trade Commission ("Commission") having initiated an investigation of the proposed acquisition by Irving Oil Limited and Irving Oil Terminals Inc. (collectively "Irving" or "Respondent") of ExxonMobil Oil Corporation and Mobil Pipe Line Company's energy fuel terminal and pipeline assets located in Maine, and Respondent having been furnished thereafter with a copy of the draft of Complaint that the Bureau of Competition proposed to present to the Commission for its consideration and which, if issued by the Commission, would charge Respondent with violations of Section 7 of the Clayton Act, as amended, 15 U.S.C. § 18, and Section 5 of the Federal Trade Commission Act, as amended, 15 U.S.C. § 45; and

Respondent, its attorneys, and counsel for the Commission having thereafter executed an Agreement Containing Consent Order ("Consent Agreement"), containing: an admission by Respondent of all the jurisdictional facts set forth in the aforesaid draft of Complaint; a statement that the signing of said Consent Agreement is for settlement purposes only and does not constitute an admission by Respondent that the law has been violated as alleged in such Complaint, or that the facts as alleged in such Complaint, other than jurisdictional facts, are true; and waivers and other provisions as required by the Commission's Rules; and

The Commission having thereafter considered the matter and having determined that it had reason to believe that Respondent has violated the said Acts, and that a Complaint should issue stating its charges in that respect, and having accepted the executed Consent Agreement and placed such Consent Agreement on the public record for a period of thirty (30) days for the receipt and consideration of public comments, now in further conformity with the procedure described in Commission Rule 2.34, 16 C.F.R. § 2.34, the Commission hereby issues its

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Complaint, makes the following jurisdictional findings and issues the following Decision and Order ("Order"):

1. Respondent Irving Oil Limited is a Canadian corporation organized, existing, and doing business under, and by virtue of, the laws of Canada, with its office and principal place of business located at 10 Sydney Street, Saint John, New Brunswick, Canada E2L 4K1.
2. Respondent Irving Oil Terminals Inc. is a corporation organized, existing, and doing business under, and by virtue of, the laws of Delaware with its office and principal place of business located at 190 Commerce Way, Portsmouth, New Hampshire 03801.
3. The Federal Trade Commission has jurisdiction of the subject matter of this proceeding and of the Respondent and the proceeding is in the public interest.

ORDER**I.**

IT IS HEREBY ORDERED that, as used in this Order, the following definitions shall apply:

- A. "Irving" means Irving Oil Limited and Irving Oil Terminals Inc., their directors, officers, employees, agents, representatives, successors, and assigns; and the joint ventures, subsidiaries, divisions, groups and affiliates controlled by Irving and the respective directors, officers, employees, agents, representatives, successors, and assigns of each.

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- B. "Commission" means the Federal Trade Commission.
- C. "Buckeye" means Buckeye Pipe Line Holdings, L.P., a limited partnership, and Buckeye Partners, L.P., a publicly-traded master limited partnership, both organized, existing, and doing business under and by virtue of the laws of Delaware, with their offices and principal place of business located at One Greenway Plaza, Suite 600, Houston, Texas 77046.
- D. "Buckeye Assignment Agreements" means the (i) Agreement Concerning Assignment of Contracts, dated May 4, 2011, (ii) Assignment And Assumption Agreement For and Amendment To Terminals Sales and Purchase Agreement, dated May 4, 2011, and (iii) Assignment And Assumption Agreement For and Amendment To Pipeline Sale and Purchase Agreement, dated May 4, 2011, including all exhibits, attachments, agree-ments, and schedules attached to each agreement; *provided, however*, that for purposes of Paragraph II.E., the Buckeye Assignment Agreements shall not include Exhibits D or E of the Agreement Concerning Assignment of Contracts.
- E. "Financial Statements" means income statements, balance sheets, cash flow statements, cash distribution statements, and capital account statements that contain aggregate information only.
- F. "Irving Divestiture Team" means (i) the Irving JV Oversight Team and (ii) one senior manager of Irving appointed by the Irving General Manager, the Irving Executive Team and/or the board of directors of Irving to oversee and manage a divestiture of Irving's interest in the Portland Terminal Joint Venture and no more than three (3) of his or her direct subordinates.

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- G. "Irving Executive Team" means Irving's senior-most team of executive managers that is directly subordinate and accountable to the board of directors of Irving.
- H. "Irving General Manager" means Irving's senior-most manager that is directly subordinate and accountable to the Irving Executive Team.
- I. "Irving JV Oversight Team" means (i) Irving's JV Representative, (ii) Irving's inside legal counsel and their direct administrative subordinates, (iii) Irving's finance director and no more than one of his or her direct administrative subordinates, (iv) the Irving General Manager and no more than one of his or her direct administrative subordinates, (v) the Irving Executive Team, and (vi) Irving's board of directors.
- J. "Irving's JV Representative" means the person (and no more than one alternative) appointed by Irving pursuant to the Portland Terminal Agreement and through whom Irving will act as a member of the Portland Terminal Joint Venture.
- K. "Irving's Maine Business" means any Irving business relating to the marketing, transportation, or storage of energy products in the State of Maine.
- L. "Irving Non-Public Information" means competitively sensitive, proprietary and all other business information of any kind owned by or pertaining to Respondent, other than Portland Terminal JV Non-Public Information (including, but not limited to, product nominations; shipment volumes, scheduling, and customer identification information; receipt, rates, storage, and inventory of products; financial

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statements, plans and forecasts; operating plans; price lists and cost information; supplier and vendor contracts; marketing analyses; customer lists and contracts; employee lists, salary and benefits information; and technologies, processes, and other trade secrets), except for any information that Respondent demonstrates (i) was or becomes generally available to the public other than as a result of a disclosure by Respondent or (ii) was available, or becomes available, to Respondent on a non-confidential basis, but only if, to the knowledge of Respondent, the source of such information is not in breach of a contractual, legal, fiduciary, or other obligation to maintain the confidentiality of the information.

- M. "Manager" means the Person who manages the business and affairs of the Portland Terminal Joint Venture pursuant to the Portland Terminal Agreement.
- N. "Person" means any individual, partnership, firm, trust, association, corporation, joint venture, unincorporated organization, or other business or governmental entity.
- O. "Portland Terminal" means ExxonMobil Oil Corporation's energy fuels terminal and business located at or about 170 Lincoln Street, South Portland, Maine 04108.
- P. "Portland Terminal Agreement" means the Limited Liability Company Agreement of South Portland Terminal LLC, between Buckeye and Irving, dated May __, 2011.
- Q. "Portland Terminal Joint Venture" means the joint venture entered into by Irving and Buckeye for the

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purpose of acquiring the Portland Terminal pursuant to the Portland Terminal Agreement.

- R. "Operator" means the Person who conducts the day-to-day operations of the Portland Terminal Joint Venture pursuant to the Portland Terminal Agreement and under a management, operations, and maintenance agreement.
- S. "Terminal & Pipeline Assets" means all of the right, title, and interest in and to all property and assets that Irving agreed to purchase from (i) ExxonMobil Oil Corporation pursuant to a certain Terminals Sale and Purchase Agreement, dated November 2, 2009, and (ii) Mobil Pipe Line Company pursuant to a certain Sale and Purchase Agreement for Portland to Bangor Refined Products Pipeline System, dated November 2, 2009; *provided, however*, that the Terminal & Pipeline Assets shall not include an interest in the Portland Terminal that Irving may acquire through the Portland Terminal Joint Venture pursuant to the Buckeye Assignment Agreements.
- T. "Portland Terminal JV Non-Public Information" means competitively sensitive, proprietary and all other business information of any kind owned by or pertaining to the Portland Terminal Joint Venture or Portland Terminal assets (including, but not limited to, product nominations; shipment volumes, scheduling, and customer identification information; receipt, rates, storage, and inventory of products; financial statements, plans and forecasts; operating plans; price lists and cost information; supplier and vendor contracts; marketing analyses; customer lists and contracts; employee lists, salary and benefits information; and technologies, processes, and other

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trade secrets), except for any information that Respondent demonstrates (i) was or becomes generally available to the public other than as a result of a disclosure by Respondent or (ii) was available, or becomes available, to Respondent on a non-confidential basis, but only if, to the knowledge of Respondent, the source of such information is not in breach of a contractual, legal, fiduciary, or other obligation to maintain the confidentiality of the information.

II.**IT IS FURTHER ORDERED** that:

- A. Respondent shall divest all rights to acquire the Terminal & Pipeline Assets, absolutely and in good faith, to Buckeye pursuant to the Buckeye Assignment Agreements, no later than five (5) days after the Commission accepts the Consent Agreement for public comment; *provided, however*, that:
 - 1. If, at the time the Commission determines to make this Order final, the Commission determines that Buckeye is not acceptable as the assignee of Respondent's rights to acquire the Terminal & Pipeline Assets, or that the Buckeye Assignment Agreements are not an acceptable manner of divestiture, and so notifies Respondent, Respondent shall immediately terminate or rescind the Buckeye Assignment Agreements and shall not enter into any other agreement to assign its rights to acquire the Terminal & Pipeline Assets without obtaining the prior approval of the Commission.

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2. In the event that the Buckeye Assignment Agreements are rescinded pursuant to Paragraph II.A.1. of this Order, or if Buckeye does not acquire the Terminal & Pipeline Assets for any other reason, Respondent shall not acquire, directly or indirectly, any interest, in whole or in part, in the Terminal & Pipeline Assets without obtaining the prior approval of the Commission.
- B. With respect to the organization, structure, and management of the Portland Terminal Joint Venture and the Portland Terminal, Respondent shall not, without obtaining the prior approval of the Commission:
1. Serve as either Manager or Operator, *provided however*, that in the event that Buckeye is unable (or is legally declared to be unable) to serve as Operator, Respondent shall notify the Commission and may serve as Operator, for an interim period of up to sixty (60) days without obtaining the prior approval of the Commission, when reasonably necessary to provide for the continuous operation of the Portland Terminal;
 2. Acquire storage or throughput rights in the Portland Terminal that exceed those Respondent will have pursuant to the Buckeye Assignment Agreements; *provided, however*, that Respondent may acquire such additional rights for terms of up to one (1) month without prior approval; or
 3. Acquire, directly or indirectly, through subsidiaries or otherwise, any additional ownership interest, or any other interest, in whole or in part, in the Portland Terminal Joint Venture.

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- C. Respondent shall not invite, enter into, implement, continue, enforce, or attempt to enter into, implement, continue or enforce, any condition, policy, practice, agreement, contract understanding, or any other requirement that discourages or prevents the Operator from offering the same terms and conditions to any other Person that it offers Respondent for the handling and throughput of energy fuels at the Portland Terminal.
- D. Irving's JV Representative shall not (i) have any responsibilities (other than as Irving's representative to the Portland Terminal Joint Venture) relating to Irving's Maine Business or (ii) access to Irving Non-Public Information relating to Irving's Maine Business.
- E. Respondent shall comply with all terms of the Buckeye Assignment Agreements, and any breach of the Buckeye Assignment Agreements shall constitute a violation of this Order. If any term of the Buckeye Assignment Agreements varies from or contradicts any term of this Order ("Order Term"), then to the extent that Respondent cannot fully comply with both terms, the Order Term shall determine Respondent's obligations under this Order. Any modification of the Buckeye Assignment Agreements, without the approval of the Commission, shall constitute a failure to comply with this Order.
- F. The purpose of the divestiture of the Terminal & Pipeline Assets and of the related obligations imposed by this Order is to (i) ensure the continued use of the assets in the same businesses in which the Terminal & Pipeline Assets were engaged at the time of

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assignment to Buckeye, (ii) ensure that the Portland Terminal is operated independently of, and in competition with, other Maine terminals, and (iii) remedy the lessening of competition resulting from the acquisition as alleged in the Commission's Complaint.

III.**IT IS FURTHER ORDERED** that:

- A. Respondent shall not (i) receive any Portland Terminal JV Non-Public Information, (ii) provide, disclose or otherwise make available such information to any Person, or (iii) use such information for any reason or purpose; *provided, however*, that:
1. The Irving JV Representative may receive and use Portland Terminal JV Non-Public Information for the purpose of (i) conducting his or her duties as Irving's JV Representative, (ii) exercising Irving's rights as a member under the Portland Terminal Agreement or applicable law, and (iii) evaluating the Operator's compliance with applicable performance metrics or standards established by the Portland Terminal Joint Venture.
 2. The Irving JV Oversight Team may receive and use the following Portland Terminal JV Non-Public Information:
 - (a) Monthly, quarterly, and annual Financial Statements relating to the Portland Terminal Joint Venture solely for the purpose of evaluating Irving's participation in the Portland Terminal Joint Venture;

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- (b) Aggregate financial information (including estimated cash flows, return on investment, and net present value) relating to any proposed new investment in the Portland Terminal Joint Venture solely for the purpose of evaluating such proposal; and
 - (c) Information describing any capital contribution to the Portland Terminal Joint Venture required by the Portland Terminal Agreement that exceeds \$50,000 solely for the purpose of approving disbursement.
3. Respondent may receive, disclose, or use the following Portland Terminal JV Non-Public Information:
- (a) Information relating solely to Irving and its own transactions in the course of conducting its business as a (i) throughput customer of the Portland Terminal or (ii) bulk supplier of energy fuels and additives through the Portland Terminal.
 - (b) Information that Respondent is required to include in its corporate financial, accounting, or tax documents, *provided, however*, that such information shall be disclosed under the direction of Irving's JV Representative and only to those persons who need it to prepare such consolidated documents;
 - (c) Information that Respondent requires in the course of obtaining legal advice or defending or prosecuting any dispute, claim, or litigation pertaining to the Portland Terminal Joint

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Venture, *provided, however*, that such information shall be disclosed under the direction of Irving's JV Representative and only to those persons who need it to provide legal advice or to prosecute or defend any such dispute;

- (d) Information that Respondent requires in operating or managing the Portland Terminal on an emergency basis pursuant to Paragraph II.B.1. of this Order, *provided, however*, that such information shall be disclosed under the direction of Irving's JV Representative and only to those persons who need it to operate the Portland Terminal, *provided further*, that Irving's JV Representative may also describe the general circumstances of the emergency to the Irving JV Oversight Team; and
- (e) Information that Respondent requires to comply with any legal requirement, *provided, however*, that such information shall be disclosed under the direction of Irving's JV Representative and only to those persons who need it to comply with such legal requirement.

Provided further, that Irving's JV Representative shall require that each Person who may be permitted to receive, use, or disclose any Portland Terminal JV Non-Public Information under this Paragraph III.A.3. to sign a statement in which such Person agrees to maintain the confidentiality of the information.

4. The Irving Divestiture Team may receive and use the following Portland Terminal JV Non-Public

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Information solely for the purpose of marketing Irving's interest in the Portland Terminal Joint Venture (should Respondent wish to sell its interest), evaluating offers received, negotiating transaction terms, and executing a sale of Respondent's interest in the Portland Terminal Joint Venture to any Person:

- (a) Financial Statements relating to the Portland Terminal Joint Venture, and
 - (b) Non-financial information and documents pertaining to the Portland Terminal Joint Venture relating to real estate, improvements and personal property; environmental; safety and operations; permits and licenses; human resources; information technology; litigation and disputes; agreements among Irving, the Portland Terminal Joint Venture, the Manager or the Operator; insurance information properly in Irving's possession; and other proprietary or business information not of a competitively sensitive nature in the possession or control of the Manager, Operator or Irving.
5. Respondent may engage outside attorneys, accountants, independent consultants and/or auditors to review on Respondent's behalf Portland Terminal JV Non-Public Information provided that those attorneys, accountants, independent consultants and/or auditors shall not make such information available to Respondent except to the extent Respondent is permitted to receive the information under this Order.
- Provided further*, that prior to receiving and using any Portland Terminal JV Non-Public Information

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under this Paragraph III.A., Irving's JV Representative, the Irving JV Oversight Team, the Irving Divestiture Team, and outside attorneys, accountants independent consultants and/or auditors shall agree in writing to maintain the confidentiality of such information.

- B. Respondent shall not provide, disclose or otherwise make available any Irving Non-Public Information to any Person employed by or associated with the Portland Terminal Joint Venture; *provided, however*, that Respondent may provide or disclose such information to:
1. Irving's JV Representative, except for any such information relating to Irving's Maine Business; and
 2. The Operator relating solely to Irving and its own transactions in the course of conducting its business as a (i) throughput customer of the Portland Terminal, or (ii) a bulk supplier of energy fuels and additives through the Portland Terminal.
- C. Respondent shall within sixty (60) days of the date this Order becomes final, and in consultation with the Monitor appointed pursuant to Paragraph V of this Order, develop and implement procedures to insure compliance with this Paragraph III, including training Respondent's employees.

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IV.**IT IS FURTHER ORDERED** that:

- A. For a period of ten (10) years from the date this Order becomes final, Respondent shall not, without providing advance written notification to the Commission, acquire, directly or indirectly, through subsidiaries or otherwise, any leasehold, ownership interest, or any other interest, in whole or in part, in any concern, corporate or non-corporate, or in any assets engaged in the transportation or storage of energy fuels in Maine; *provided, however*, that this Paragraph IV.A. shall not apply to a single asset acquisition (or group of asset acquisitions within any six month period) with a value of less than \$5,000,000.
- B. The prior notification required by this Paragraph IV shall be given on the Notification and Report Form set forth in the Appendix to Part 803 of Title 16 of the Code of Federal Regulations as amended (hereinafter referred to as "the Notification"), and shall be prepared and transmitted in accordance with the requirements of that part, except that no filing fee will be required for any such notification, notification shall be filed with the Secretary of the Commission, notification need not be made to the United States Department of Justice, and notification is required only by the Respondent and not by any other party to the transaction. Respondent shall provide the Notification to the Commission at least thirty (30) days prior to consummating the transaction (hereinafter referred to as the "first waiting period"). If, within the first waiting period, representatives of the Commission make a written request for additional information or documentary material (within the meaning of 16

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C.F.R. § 803.20), Respondent shall not consummate the transaction until thirty (30) days after submitting such additional information or documentary material. Early termination of the waiting periods in this Paragraph IV may be requested and, where appropriate, granted by letter from the Bureau of Competition. *Provided, however*, that prior notification shall not be required by this Paragraph for a transaction for which notification is required to be made, and has been made, pursuant to Section 7A of the Clayton Act, 15 U.S.C. § 18a.

V.**IT IS FURTHER ORDERED** that:

- A. Kevin Sudy shall serve as Monitor to monitor Respondent's implementation of the confidentiality and nondisclosure requirements of Paragraph III and of this Order.
1. Within three (3) days after this Order becomes final, Respondent shall, pursuant to the Monitor Agreement (attached to this Order as Confidential Appendix B) and this Order, transfer to the Monitor all rights, powers, and authorities necessary to permit the Monitor to perform his duties and responsibilities pursuant to this Order.
 2. If at any time the Commission determines that the Monitor has ceased to act or failed to act diligently, or is unwilling or unable to continue to serve, the Commission may appoint a substitute to serve as Monitor. The Commission shall select a substitute Monitor subject to the consent of Respondent, which consent shall not be unreasonably withheld.

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If Respondent has not opposed, in writing, including the reasons for opposing, the selection of any proposed Monitor within ten days after notice by the staff of the Commission to Respondent (by delivery receipt acknowledged, to Respondent's counsel of record) of the identity of any proposed substitute Monitor, Respondent shall be deemed to have consented to the selection of the proposed substitute. Respondent shall execute the agreement with the substitute Monitor within ten days after the Commission appoints a substitute Monitor. The substitute Monitor shall serve according to the terms and conditions of this Paragraph V.

- B. Respondent shall consent to the following terms and conditions regarding the powers, duties, authorities, and responsibilities of the Monitor:
1. The Monitor shall have the power and authority to monitor Respondent's compliance with Paragraph III of this Order and shall exercise such power and authority and carry out the duties and responsibilities of the Monitor pursuant to the terms of this Order and in consultation with the Commission.
 2. The Monitor's power and duties under this Paragraph V shall continue until the Monitor reports to the Commission that Respondent has put in place adequate procedures in accordance with Paragraph III.C. of this Order, and Commission staff has notified Respondent that such procedures are acceptable.
 3. The Monitor shall have full and complete access to Respondent's books, records, documents,

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personnel, facilities and technical information relating to compliance with this Order, or to any other relevant information, as the Monitor may reasonably request. Respondent shall cooperate with any reasonable request of the Monitor. Respondent shall take no action to interfere with or impede the Monitor's ability to monitor Respondent's compliance with this Order.

4. The Monitor shall serve, without bond or other security, at the expense of Respondent, on such reasonable and customary terms and conditions as the Commission may set. The Monitor shall have authority to employ, at the expense of Respondent, such consultants, accountants, attorneys and other representatives and assistants as are reasonably necessary to carry out the Monitor's duties and responsibilities. The Monitor shall account for all expenses incurred, including fees for his or her services, subject to the approval of the Commission.
5. Respondent shall indemnify the Monitor and hold the Monitor harmless against any losses, claims, damages, liabilities, or expenses arising out of, or in connection with, the performance of the Monitor's duties, including all reasonable fees of counsel and other expenses incurred in connection with the preparation for, or defense of, any claim, whether or not resulting in any liability, except to the extent that such losses, claims, damages, liabilities, or expenses result from the Monitor's gross negligence or wilful misconduct. For purposes of this Paragraph V.B.5., the term "Monitor" shall include all Persons retained by the

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Monitor pursuant to Paragraph V.B.4. of this Order.

6. The Monitor shall report in writing to the Commission every thirty (30) days from the date this Order becomes final, and at any other time as requested by the staff of the Commission, concerning Respondent's compliance with this Order.
 7. Respondent may require the Monitor and each of the Monitor's consultants, accountants, attorneys, and other representatives and assistants to sign an appropriate confidentiality agreement; *provided, however,* such agreement shall not restrict the Monitor from providing any information to the Commission.
- C. The Commission may on its own initiative or at the request of the Monitor issue such additional orders or directions as may be necessary or appropriate to assure compliance with the requirements of this Order.

VI.**IT IS FURTHER ORDERED** that:

- A. If Respondent has not divested all of the Terminal & Pipeline Assets as required by Paragraph II.A. of this Order, the Commission may appoint one or more Persons as Divestiture Trustee to divest the Terminal & Pipeline Assets in a manner that satisfies the requirements of this Order. The Divestiture Trustee appointed pursuant to this Paragraph may be the same Person appointed as the monitor pursuant to Paragraph V of this Order.

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- B. In the event that the Commission or the Attorney General brings an action pursuant to § 5(l) of the Federal Trade Commission Act, 15 U.S.C. § 45(l), or any other statute enforced by the Commission, Respondent shall consent to the appointment of a Divestiture Trustee in such action to divest the relevant assets in accordance with the terms of this Order. Neither the appointment of a Divestiture Trustee nor a decision not to appoint a Divestiture Trustee under this Paragraph shall preclude the Commission or the Attorney General from seeking civil penalties or any other relief available to it, including a court-appointed Divestiture Trustee, pursuant to § 5(l) of the Federal Trade Commission Act, or any other statute enforced by the Commission, for any failure by the Respondent to comply with this Order.
- C. The Commission shall select the Divestiture Trustee, subject to the consent of Respondent, which consent shall not be unreasonably withheld. The Divestiture Trustee shall be a person with experience and expertise in acquisitions and divestitures. If Respondent has not opposed, in writing, including the reasons for opposing, the selection of any proposed Divestiture Trustee within ten (10) days after notice by the staff of the Commission to Respondent of the identity of any proposed Divestiture Trustee, Respondent shall be deemed to have consented to the selection of the proposed Divestiture Trustee.
- D. Within ten (10) days after appointment of a Divestiture Trustee, Respondent shall execute a trust agreement that, subject to the prior approval of the Commission, transfers to the Divestiture Trustee all rights and powers necessary to permit the Divestiture Trustee to

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effect the relevant divestiture or transfer required by the Order.

- E. If a Divestiture Trustee is appointed by the Commission or a court pursuant to this Order, Respondent shall consent to the following terms and conditions regarding the Divestiture Trustee's powers, duties, authority, and responsibilities:
1. Subject to the prior approval of the Commission, the Divestiture Trustee shall have the exclusive power and authority to assign, grant, license, divest, transfer, deliver or otherwise convey the relevant assets that are required by this Order to be assigned, granted, licensed, divested, transferred, delivered or otherwise conveyed.
 2. The Divestiture Trustee shall have twelve (12) months from the date the Commission approves the trust agreement described herein to accomplish the divestiture, which shall be subject to the prior approval of the Commission. If, however, at the end of the twelve (12) month period, the Divestiture Trustee has submitted a plan of divestiture or believes that the divestiture can be achieved within a reasonable time, the divestiture period may be extended by the Commission.
 3. Subject to any demonstrated legally recognized privilege, the Divestiture Trustee shall have full and complete access to the personnel, books, records, and facilities related to the relevant assets that are required to be assigned, granted, licensed, divested, delivered or otherwise conveyed by this Order and to any other relevant information, as the Divestiture Trustee may request. Respondent shall

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develop such financial or other information as the Divestiture Trustee may request and shall cooperate with the Divestiture Trustee. Respondent shall take no action to interfere with or impede the Divestiture Trustee's accomplishment of the divestiture. Any delays in divestiture caused by Respondent shall extend the time for divestiture under this Paragraph VI in an amount equal to the delay, as determined by the Commission or, for a court-appointed Divestiture Trustee, by the court.

4. The Divestiture Trustee shall use commercially reasonable best efforts to negotiate the most favorable price and terms available in each contract that is submitted to the Commission, subject to Respondent's absolute and unconditional obligation to divest expeditiously and at no minimum price. The divestiture shall be made in the manner and to an Acquirer as required by this Order; *provided, however*, that if the Divestiture Trustee receives bona fide offers from more than one acquiring entity, and if the Commission determines to approve more than one such acquiring entity, the Divestiture Trustee shall divest to the acquiring entity selected by Respondent from among those approved by the Commission; *provided further, however*, that Respondent shall select such entity within five (5) days of receiving notification of the Commission's approval.
5. The Divestiture Trustee shall serve, without bond or other security, at the cost and expense of Respondent, on such reasonable and customary terms and conditions as the Commission or a court may set. The Divestiture Trustee shall have the

Decision and Order

authority to employ, at the cost and expense of Respondent, such consultants, accountants, attorneys, investment bankers, business brokers, appraisers, and other representatives and assistants as are necessary to carry out the Divestiture Trustee's duties and responsibilities. The Divestiture Trustee shall account for all monies derived from the divestiture and all expenses incurred. After approval by the Commission and, in the case of a court-appointed Divestiture Trustee, by the court, of the account of the Divestiture Trustee, including fees for the Divestiture Trustee's services, all remaining monies shall be paid at the direction of the Respondent, and the Divestiture Trustee's power shall be terminated. The compensation of the Divestiture Trustee shall be based at least in significant part on a commission arrangement contingent on the divestiture of all of the relevant assets that are required to be divested by this Order.

6. Respondent shall indemnify the Divestiture Trustee and hold the Divestiture Trustee harmless against any losses, claims, damages, liabilities, or expenses arising out of, or in connection with, the performance of the Divestiture Trustee's duties, including all reasonable fees of counsel and other expenses incurred in connection with the preparation for, or defense of, any claim, whether or not resulting in any liability, except to the extent that such losses, claims, damages, liabilities, or expenses result from gross negligence or willful misconduct by the Divestiture Trustee. For purposes of this Paragraph VI.E.6., the term "Divestiture Trustee" shall include all Persons

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retained by the Divestiture Trustee pursuant to Paragraph VI.E.5. of this Order.

7. The Divestiture Trustee shall have no obligation or authority to operate or maintain the relevant assets required to be divested by this Order.
 8. The Divestiture Trustee shall report in writing to Respondent and to the Commission every sixty (60) days concerning the Divestiture Trustee's efforts to accomplish the divestiture.
 9. Respondent or the Commission may require the Divestiture Trustee and each of the Divestiture Trustee's consultants, accountants, attorneys, and other representatives and assistants to sign a customary confidentiality agreement; *provided, however,* that such agreement required by Respondent shall not restrict the Divestiture Trustee from providing any information to the Commission.
- F. If the Commission determines that a Divestiture Trustee has ceased to act or failed to act diligently, the Commission may appoint a substitute Divestiture Trustee in the same manner as provided in this Paragraph VI.
- G. The Commission or, in the case of a court-appointed Divestiture Trustee, the court, may on its own initiative or at the request of the Divestiture Trustee issue such additional orders or directions as may be necessary or appropriate to accomplish the divestiture required by this Order.

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VII.**IT IS FURTHER ORDERED** that:

- A. Sixty (60) days from the date this Order becomes final, Respondent shall submit to the Commission a verified written report setting forth in detail the manner and form in which it intends to comply, is complying, and has complied with this Order.
- B. One (1) year after the date this Order becomes final, annually thereafter for the next nine (9) years on the anniversary of the date this Order becomes final, and at such other times as the Commission may request, Respondent shall file a verified written report with the Commission setting forth in detail the manner and form in which it has complied and is complying with this Order.
- C. Within thirty (30) days from the date any dispute initiated by a party under the Portland Terminal Agreement becomes subject to arbitration or judicial review under the terms of the Portland Terminal Agreement, Respondent shall submit to the Commission a report setting forth in detail a description of the dispute.

VIII.

IT IS FURTHER ORDERED that Respondent shall notify the Commission at least thirty (30) days prior to any proposed (1) dissolution of the Respondent, (2) acquisition, merger or consolidation of Respondent, or (3) any other change in the Respondent that may affect compliance obligations arising out of this Order, including but not limited to assignment, the creation or dissolution of subsidiaries, or any other change in Respondent.

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IX.

IT IS FURTHER ORDERED that, for the purpose of determining or securing compliance with this Order, and subject to any legally recognized privilege, and upon written request and upon five (5) days notice to Respondent, Respondent shall, without restraint or interference, permit any duly authorized representative(s) of the Commission:

- A. Access, during business office hours of the Respondent and in the presence of counsel, to all facilities and access to inspect and copy all books, ledgers, accounts, correspondence, memoranda and all other records and documents in the possession or under the control of the Respondent, which copying services shall be provided by the Respondent at its expense; and
- B. To interview officers, directors, or employees of the Respondent, who may have counsel present, regarding such matters.

X.

IT IS FURTHER ORDERED that this Order shall terminate on July 12, 2021.

By the Commission.

Decision and Order

CONFIDENTIAL APPENDIX A

**[Redacted From the Public Record Version But Incorporated
By Reference]**

CONFIDENTIAL APPENDIX B

**[Redacted From the Public Record Version But Incorporated
By Reference]**

Analysis to Aid Public Comment

**ANALYSIS OF PROPOSED AGREEMENT CONTAINING
CONSENT ORDER TO AID PUBLIC COMMENT****I. Introduction**

The Federal Trade Commission ("Commission") has accepted for public comment, subject to final approval, an Agreement Containing Consent Order ("Consent Agreement") from Irving Oil Terminals Inc. and Irving Oil Limited (collectively "Irving"). The purpose of the proposed Consent Agreement is to remedy the anticompetitive effects resulting from Irving and Irving Oil Transportation Company LLC's proposed acquisition of certain petroleum products storage and transportation assets located in Maine from ExxonMobil Oil Corporation ("ExxonMobil"). As originally structured, Irving would have acquired ExxonMobil's petroleum products terminals located in South Portland and Bangor, Maine, as well as ExxonMobil's intrastate pipeline connecting these two terminals.

The Commission's Complaint alleges that this, if consummated, would violate Section 7 of the Clayton Act, as amended, 15 U.S.C. § 18, and Section 5 of the Federal Trade Commission Act, as amended, 15 U.S.C. § 45, by lessening competition in the gasoline and distillates terminaling services markets in the South Portland and Bangor/Penobscot Bay areas of Maine. To resolve these competitive concerns raised by the original transaction, Irving will divest its acquisition rights to the ExxonMobil Bangor terminal and intrastate pipeline as well as fifty percent of ExxonMobil's South Portland terminal to Buckeye Partners, L.P. and its affiliate Buckeye Pipe Line Holdings, L.P. (collectively "Buckeye"), retaining only the right to acquire the remaining fifty percent of the South Portland terminal. Buckeye and Irving will form a joint venture that will purchase ExxonMobil's South Portland terminal. Under this proposal, Buckeye alone will manage and operate this terminal on behalf of the Irving-Buckeye joint venture. Buckeye will purchase and

Analysis to Aid Public Comment

operate ExxonMobil's pipeline and Bangor terminal. Irving will enter into a throughput agreement with Buckeye at each of the petroleum products terminals. The Commission's Consent Agreement is intended to assure that Irving does not control the pipeline and terminals and does not threaten Buckeye's ability to competitively operate the South Portland terminal.

The proposed Consent Agreement, to govern for a period of ten years, prevents Irving from acquiring additional share in, managing, or operating the South Portland terminal absent the Commission's prior approval. The Consent Agreement also requires prior notification should Irving acquire any form of additional ownership interests in petroleum products transportation or storage assets located in Maine. Finally, the proposed Consent Agreement imposes firewall and monitor provisions to prevent Irving from accessing and using confidential customer information. This remedy preserves competition in the gasoline and distillates terminaling services markets in both the Bangor/Penobscot Bay and South Portland areas of Maine.

The proposed Consent Agreement has been placed on the public record for thirty days to allow interested persons to comment. Comments received during this period will become part of the public record. After thirty days, the Commission will review the proposed Consent Agreement and the comments received, and will decide whether to withdraw the proposed Consent Agreement, modify it, or make it final.

II. Parties

Irving is a family-owned business based in St. John, New Brunswick, Canada. Irving owns the largest refinery in Canada and owns, in whole or in part, six terminals in Canada and the northeastern United States. Irving supplies branded and unbranded petroleum products in Canada and throughout New England to third-

Analysis to Aid Public Comment

party distributors, retailers, various other re-sellers, and governmental and commercial end users. Irving also owns retail travel plazas that sell gasoline and diesel petroleum products. In Maine, Irving owns a terminal in Searsport and co-owns a terminal with CITGO Petroleum Corporation in South Portland.

ExxonMobil is the world's largest publicly traded petroleum and natural gas company worldwide. ExxonMobil produces crude oil and natural gas, refines petroleum products, and transports and sells crude oil, natural gas, and refined petroleum products. ExxonMobil owns terminals located in South Portland and Bangor, Maine, as well as an intrastate pipeline that connects these two terminals.

Buckeye is a publicly traded partnership that owns and operates one of the largest independent refined petroleum products pipeline systems in the United States. Buckeye owns or manages approximately 7,500 miles of pipeline, owns approximately 70 active refined petroleum products terminals, and markets refined petroleum products in some of the geographic areas served by its pipeline and terminal operations. Buckeye is not a party to the original transaction and does not currently market, transport, or store light petroleum products in Maine.

III. The Relevant Markets and their Structure

The Commission's Complaint alleges that the original transaction would pose substantial antitrust concerns in the gasoline and distillates terminaling services markets in the Bangor/Penobscot Bay and South Portland areas of Maine.

Terminals generally consist of a number of storage tanks and loading "racks" that pump fuels into tanker trucks for further delivery. Terminals are specialized facilities connected to one or more fuel supply sources, have the capacity to store fuel shipments, and must be configured properly to distribute the fuel

Analysis to Aid Public Comment

to customers. Light petroleum products terminals are specialized facilities that receive gasoline, diesel fuel, heating oil, kerosene, and jet fuel, among other products, by pipeline, by water, by rail, or directly from refinery production. These products are stored or redistributed by pipeline, water, rail, or truck. Terminals are critical to the sale and distribution of transportation fuels and perform value-added services, such as handling and injection of motor fuel additives (including ethanol) as petroleum products are redelivered across the truck rack. Terminaling services consist of a cluster of services related to the delivery, storage, and throughput of petroleum products.

The Commission's Complaint alleges that relevant product markets within which to analyze the original transaction are gasoline terminaling services and distillates terminaling services. Terminals that store gasoline compete in both the gasoline terminaling services and distillates terminaling services markets. However, terminals that store only distillates compete only in the distillates terminaling services market. Two relevant geographic areas in which to analyze the effects of the original transaction on gasoline and distillates terminaling services are the Bangor/Penobscot Bay and the South Portland areas of Maine. The Bangor/Penobscot Bay area encompasses the state of Maine north of Waterville, including Bangor, Searsport, and Bucksport, Maine. The South Portland area encompasses the state of Maine south of Waterville, including South Portland.

Irving and ExxonMobil are two of three firms that can independently offer gasoline terminaling services in the Bangor/Penobscot Bay area and two of four in the South Portland area. Additionally, these companies are two of four firms independently offering distillates terminaling services in the Bangor/Penobscot Bay area and two of six in the South Portland area. The original acquisition would have substantially increased concentration in each of the above markets.

Analysis to Aid Public Comment

IV. Effects of the Acquisition

The Commission believes that the original transaction would eliminate the actual, direct, and substantial competition between Irving and ExxonMobil, both: (1) increasing the likelihood that Irving would unilaterally exercise market power in the Bangor/Penobscot Bay area gasoline terminaling services market, and (2) enhancing the likelihood of collusion or coordinated interaction among the remaining firms in the South Portland area gasoline terminaling services market and both the Bangor/Penobscot Bay and South Portland area distillates terminaling services markets.

The ExxonMobil pipeline, which originates in South Portland and whose only access point is the ExxonMobil South Portland terminal, supplies the terminals located in Bangor, Maine. Marine vessels supply the remaining Bangor/Penobscot Bay area terminals as well as the South Portland area terminals. Because importing gasoline from Europe on large cargo vessels is generally less costly than shipping it from domestic ports on smaller barges, most Maine suppliers import gasoline from outside the United States.

Controlling the South Portland terminal would allow Irving to control the price of bulk gasoline deliveries to the Bangor/Penobscot Bay area. Irving would likely be able unilaterally to raise the price for or restrict the availability of gasoline terminaling services in the Bangor/Penobscot Bay area and raise gasoline prices to customers served from this area's terminals. Additionally, the original transaction would provide Irving with sufficient terminal capacity to restrict alternative suppliers' ability to import gasoline into South Portland area terminals at current prices. The ability to restrict these imports would allow Irving to increase the cost of gasoline supplied to retail stations and other consumers from the Bangor/Penobscot Bay area terminals.

Analysis to Aid Public Comment

Because the ExxonMobil assets carry both gasoline and distillates, the original transaction also would likely enhance the likelihood of coordination to raise fees for and reduce the quality and availability of terminaling services among the remaining firms that could independently provide distillates terminaling services in the Bangor/Penobscot Bay area and provide gasoline or distillates terminaling services in South Portland area.

Entry into the gasoline and distillates terminaling services markets in the Bangor/Penobscot Bay and South Portland areas would not be timely, likely, or sufficient to prevent or defeat the anticompetitive effects of the original transaction. Entering these markets is costly, difficult, and unlikely due to, among other things, the difficulty of obtaining regulatory approvals and the presence of excess terminal capacity in both markets. Facing substantial sunk costs, a new entrant would not likely invest in a new terminal in these markets, all of which presently have sufficient capacity. Further, due to the significant cost and limited ability to attract large customer volumes, a terminal that cannot currently store gasoline would not likely reconfigure its tanks to store gasoline in response to a small but significant price increase in gasoline terminaling services.

V. The Proposed Consent Agreement

For a duration of ten years, the proposed Consent Agreement addresses the competitive risk that Irving may: (1) gain control of the Irving-Buckeye South Portland terminal in the future, allowing it to restrict supply to the Bangor terminals and imports into South Portland, or (2) access and use confidential business information in an anticompetitive manner. By imposing certain prior approval and prior notice provisions on Irving and prohibiting it from taking certain actions, the remedy ensures that the Irving-Buckeye South Portland terminal will continue to operate independently of, and in competition with, other Maine

Analysis to Aid Public Comment

terminals. Further, by imposing firewall and monitor provisions, the remedy guards against Irving accessing and using confidential information in an anticompetitive manner.

Pursuant to the proposed Consent Agreement, Irving must obtain Commission approval prior to: (1) acting as either manager of the Irving-Buckeye joint venture or operator of the joint venture terminal, with a limited sixty-day exception in the event that Buckeye is unable to serve in either capacity, (2) acquiring additional storage or throughput rights at the joint venture terminal, with a limited one-month exception, or ownership interests in the joint venture, or (3) modifying its assignment agreements with Buckeye. Paragraphs II.B. and II.E. Further, the Consent Agreement requires Irving to notify the Commission prior to acquiring any form of additional ownership interests in petroleum products transportation or storage assets located in Maine. Paragraph IV. Additionally, the Consent Agreement prohibits Irving from taking action that would discourage or prevent Buckeye from offering third parties terms equal to Irving's terms at the South Portland terminal. Paragraph II.C.

The proposed Consent Agreement also prohibits Irving from receiving, sharing, or using any confidential business information with limited exceptions that allow the information to be shared where required and only to those with written agreements to maintain the information's confidentiality. Paragraph III. To this end, the Consent Agreement places an enforcement obligation on Irving and provides for the appointment of a monitor to oversee the implementation of these provisions. Paragraphs III.C. and V. Such a monitor will review Irving's compliance proposals and assist in evaluating their adequacy. Paragraph V.

The proposed Consent Agreement includes the standard divestiture trustee provision pursuant to which the Commission may appoint a trustee if Irving fails to effectuate the divestiture in

Analysis to Aid Public Comment

a manner that complies with the Consent Order. Paragraph VI.A. In this case, the trustee will divest the assets, subject to Commission prior approval, within twelve months. Paragraph VI.E.

VI. Opportunity for Public Comment

The proposed Consent Agreement has been placed on the public record for thirty days for receipt of comments by interested persons. Comments received during this period will become part of the public record. After thirty days, the Commission will review the comments received, and decide whether to withdraw from the proposed Consent Agreement, modify it, or make it final. By accepting the proposed Consent Agreement subject to final approval, the Commission anticipates that the competitive problems alleged in the complaint will be resolved. The purpose of this analysis is to inform and invite public comment on the proposed Consent Agreement, including the proposed remedy, and to aid the Commission in its determination of whether to make the proposed Consent Agreement final. This analysis is not intended to constitute an official interpretation of the proposed Consent Agreement, nor to modify the terms of the proposed Consent Agreement in any way.

Initial Decision

IN THE MATTER OF

**THE NORTH CAROLINA BOARD OF DENTAL
EXAMINERS**

INITIAL DECISION AND ORDER

Docket No. D-9343; File No. 081 0133
Filed, June 17, 2010 — Initial Decision, July 14, 2011

The Initial Decision holds that respondent North Carolina Board of Dental Examiners ("Board") illegally thwarted competition by working to bar non-dentist providers of teeth whitening goods and services from selling their products to consumers. The Board is an agency created to regulate the practice of dentistry in North Carolina and licenses any person who wants to practice dentistry in the state. The Board lacks authority over non-dentists but may ask a state court to determine that particular conduct constitutes the unauthorized practice of dentistry and issue an injunction. The Administrative Law Judge held that the Board sought to, and did, exclude non-dentist providers from the market for teeth whitening services, in violation of Section 5 of the Federal Trade Commission Act. Further, the Board's actions led to higher prices and reduced choices for consumers. The Administrative Law Judge found that Board's alleged procompetitive justifications were not valid and held that the Board was liable under the law. The Board's order, in part, prohibits the Board from directing a non-dentist provider to stop providing teeth whitening goods or services or prohibiting, restricting, impeding, or discouraging the provision of teeth whitening goods or services by a non-dentist provider.

Participants

For the *Commission*: *Michael Bergman, Michael J. Bloom, Richard B. Dagen, William L. Lanning, Steve J. Osnowitz, Tejasvi Srimashnam, Michael Turner, and Melissa Westman-Cherry.*

For the *Respondent*: *Brenner A. Allen, Noel Allen, Carolin Bakewell, Catherine E. Lee, Jackson S. Nichols, and M. Jackson Nichols, Allen Pinnix & Nichols, P.A.*

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By D. MICHAEL CHAPPELL, Chief Administrative Judge:

I. INTRODUCTION

A. Summary of the Complaint and Answer

The Commission issued an administrative complaint against the North Carolina State Board of Dental Examiners ("Respondent" or "the Board") on June 17, 2010 ("Complaint").¹ The Complaint alleges that "[t]he combination, conspiracy, acts and practices" by Respondent to exclude non-dentists from competing with dentists in the provision of teeth whitening services violates Section 5 of the Federal Trade Commission Act ("FTC Act"). Complaint, ¶ 26. Specifically, the Complaint alleges that the Board, without proper authority, engaged in various types of activities aimed at preventing non-dentists from providing teeth whitening services in North Carolina, including issuing cease and desist orders and other communications to existing and potential non-dentist teeth whitening service providers, manufacturers of products and equipment used by non-dentist providers, and mall owners and operators, asserting that non-dentist teeth whitening services are illegal. Complaint ¶¶ 18-22. The Complaint also alleges that the relevant market in which to evaluate the conduct of the Board is the provision of

¹ The caption of the Complaint issued by the Federal Trade Commission ("Commission") refers to Respondent as "The North Carolina Board of Dental Examiners," and, because there has been no motion to change the title of the caption, Respondent is referred to as "The North Carolina Board of Dental Examiners," in the caption of this Initial Decision. However, the Commission, in its Order Denying Respondent's Motion to Dismiss, Granting Complaint Counsel's Motion for Partial Summary Decision, Denying Respondent's Motion to Disqualify the Commission, and Granting Respondent's Motion for Leave to File Limited Surreply Brief, and Opinion in support thereof, has referred to Respondent as "The North Carolina State Board of Dental Examiners." *In re North Carolina Board of Dental Examiners*, Docket 9343, 2011 WL 549449 (Feb. 8, 2011). In addition, Complaint Counsel agrees that the correct title for Respondent is "The North Carolina State Board of Dental Examiners." (Feb. 17, 2011 Transcript of Final Prehearing Conference, at 63-64).

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teeth whitening services in North Carolina and charges that Respondent has and exercises market power to exclude non-dentists from competing in the relevant market. Complaint ¶¶ 7, 14. The Complaint further charges that the challenged conduct has had, and will have, the effect of restraining competition unreasonably and injuring consumers by preventing and deterring non-dentists from providing teeth whitening services in North Carolina; depriving consumers of the benefits of price competition; and reducing consumer choice in North Carolina for the provision of teeth whitening services. Complaint ¶ 25. The Notice of Contemplated Relief attached to the Complaint seeks an order, including, but not limited to, requiring Respondent to cease and desist from the challenged conduct.

In its Answer, filed on July 7, 2010, Respondent asserts that the Board is a state agency enforcing a North Carolina statute which makes it illegal for non-dentists to provide the service of "removal of stains" from teeth, and that there is no collusion, conspiracy or agreement. Answer, p. 1. Further, Respondent avers, the Board's actions with regard to non-dentist teeth whitening services were taken to enforce North Carolina law, in order to protect the public, and not to suppress competition. Answer, pp. 8-17. In addition, Respondent denies that the Board is acting as a competitor in the teeth whitening market and states that the real competition for teeth whitening services offered by non-dentists comes from over-the-counter ("OTC") sales of teeth whitening kits, which are not regulated by the Board. Answer, pp. 6-8. Respondent charges that the contemplated relief exceeds the FTC's authority and would unconstitutionally impair the ability of the State of North Carolina to protect its citizens under the Tenth and Eleventh Amendments to the Constitution. Answer, pp. 18-21.

B. Procedural History

Prior to the start of trial, Respondent filed with the Federal Trade Commission ("Commission") a Motion to Dismiss based on a claim that its conduct is exempted from antitrust liability by the state action doctrine. Complaint Counsel also filed with the Commission a Motion for Partial Summary Decision on the propriety of the Board's invocation of the state action doctrine as an affirmative defense. The Commission, on February 3, 2011,

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issued an Opinion and Order resolving these and related motions. *In re North Carolina Board of Dental Examiners*, Docket 9343, 2011 WL 549449, at *5 (Feb. 8, 2011) (hereinafter "State Action Opinion").²

In its State Action Opinion, the Commission decided that although the Board is a state regulatory body, the undisputed facts showed that the Board is controlled by North Carolina licensed dentists, and that North Carolina dentists – including the Board's dentist members – perform teeth whitening services. 2011 WL 549449, at *13. The Commission also decided that, because of the possibility that the Board would act in self-interest, pursuant to *California Retail Liquor Dealers Ass'n v. Midcal Aluminum, Inc.*, 445 U.S. 97, 105 (1980), active state supervision of the Board's activities must be demonstrated in order for state action immunity to apply. *Id.* The Commission further determined that the undisputed facts showed that the state did not actively supervise the Board's conduct, and, therefore, state action immunity did not apply. *Id.* at *15-17. The Commission concluded: "[B]ecause the Board is controlled by practicing dentists, the Board's challenged conduct must be actively supervised by the state for it to claim state action exemption from the antitrust laws. Because we find no such supervision, we hold that the antitrust laws reach the Board's conduct." *Id.* Also in its State Action Opinion, the Commission rejected the Board's argument that the Board is not subject to the Commission's jurisdiction. *Id.* at *5.

The administrative trial in this matter began on February 17, 2011. On February 28, 2011, Complaint Counsel rested and Respondent, on the record at trial, made an oral motion to dismiss at the close of Complaint Counsel's evidence, pursuant to

² The Commission, in 2009, amended its Rules of Practice to require that motions to dismiss filed before the evidentiary hearing and motions for summary decision shall be directly referred back to the Commission, rather than to the Administrative Law Judge assigned to adjudicate the complaint and "shall be ruled on by the Commission unless the Commission in its discretion refers the motion to the Administrative Law Judge." 16 C.F.R. § 3.22(a).

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Commission Rule 3.22(a).³ Complaint Counsel stated its opposition to the motion to dismiss on the record at trial on February 28, 2011.⁴ By Order dated March 30, 2011, immediately after the hearing record was closed, Respondent's motion to dismiss made at the close of the evidence was denied on the ground that Respondent failed to demonstrate that the Complaint should be dismissed for failure to establish a prima facie case. The March 30, 2011 Order advised the parties that the issues raised by Respondent's motion to dismiss, to the extent necessary or appropriate in regard to a determination of the merits for the Initial Decision in this case, and to the extent briefed by the parties in their post-trial briefs, would be addressed in the Initial Decision when issued. Those issues have been decided against Respondent, as fully discussed herein.

The administrative trial concluded on March 16, 2011 and the record was closed on March 30, 2011.⁵ Over 800 exhibits were admitted, 16 witnesses testified, either live or by deposition, and there are 3,047 pages of trial transcript. The parties' proposed findings of fact, replies to proposed findings of fact, post-trial briefs, and reply briefs total 1,501 pages.

Rule 3.51(a) of the Commission's Rules of Practice states that "[t]he Administrative Law Judge shall file an initial decision within 70 days after the filing of the last filed initial or reply proposed findings of fact, conclusions of law and order . . ." 16 C.F.R. § 3.51(a). The parties filed concurrent post-trial briefs

³ Respondent's arguments in support of its Motion are set forth in the transcript of the hearing on February 28, 2011, pages 1418-1424.

⁴ Complaint Counsel's arguments in Opposition to the Motion are set forth in the transcript of the hearing on February 28, 2011, pages 1424-1432.

⁵ On the record at trial on March 16, 2011, the parties made a joint motion seeking an order holding open the hearing record until March 30, 2011, in order to allow the parties to submit a written filing in connection with designations and counter-designations of deposition testimony, and objections to designated testimony ("Joint Motion"). On March 16, 2011, on the record at trial, the Joint Motion was granted and the record was held open for purposes of receiving deposition testimony.

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and proposed findings of fact on April 25, 2011. The parties filed replies to the other's proposed findings and briefs on May 5, 2011. Pursuant to Commission Rule 3.41(b)(6), closing arguments were held on May 11, 2011. This Initial Decision is filed in compliance with the timeframe required in Commission Rule 3.51(a).

C. Evidence

This Initial Decision is based on the exhibits properly admitted into evidence, the transcripts of testimony at trial, and the briefs and proposed findings of fact and conclusions of law, and the replies thereto, submitted by the parties. Citations to specific numbered findings of fact in this Initial Decision are designated by "F."⁶

This Initial Decision is also based on a consideration of the whole record relevant to the issues and addresses the material issues of fact and law. Proposed findings of fact not included in this Initial Decision were rejected, either because they were not supported by the evidence or because they were not dispositive or material to the determination of the allegations of the Complaint or the defenses thereto. The Commission has held that Administrative Law Judges are not required to discuss the testimony of each witness or all exhibits that are presented during the administrative adjudication. *In re Amrep Corp.*, No. 9018, 102 F.T.C. 1362, 1670, 1983 FTC LEXIS 17, *566-67 (Nov. 2, 1983). Further, administrative adjudicators are "not required to

⁶ References to the record are abbreviated as follows:

CX – Complaint Counsel's Exhibit

RX – Respondent's Exhibit

JX – Joint Exhibit

Tr. – Transcript of testimony before the Administrative Law Judge

Dep. – Transcript of Deposition

IHT – Investigational Hearing Transcript

CCB – Complaint Counsel's Post-Trial Brief

CCRB – Complaint Counsel's Post-Trial Reply Brief

CCFF – Complaint Counsel's Proposed Findings of Fact

RB – Respondent's Post-Trial Brief

RRB – Respondent's Reply Brief

RFF – Respondent's Proposed Findings of Fact

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make subordinate findings on every collateral contention advanced, but only upon those issues of fact, law, or discretion which are 'material.'" *Minneapolis & St. Louis Ry. Co. v. United States*, 361 U.S. 173, 193-94 (1959). *Accord Stauffer Labs., Inc. v. FTC*, 343 F.2d 75, 89 (9th Cir. 1965). *See also Borek Motor Sales, Inc. v. National Labor Relations Bd.*, 425 F.2d 677, 681 (7th Cir. 1970) (holding that it is adequate for the Board to indicate that it had considered each of the company's exceptions, even if only some of the exceptions were discussed, and stating that "[m]ore than that is not demanded by the [Administrative Procedure Act] and would place a severe burden upon the agency").

Under Commission Rule 3.51(c)(1), "[a]n initial decision shall be based on a consideration of the whole record relevant to the issues decided, and shall be supported by reliable and probative evidence." 16 C.F.R. § 3.51(c)(1); *see In re Chicago Bridge & Iron Co.*, No. 9300, 138 F.T.C. 1024, 1027 n.4, 2005 FTC LEXIS 215, at *3 n.4 (Jan. 6, 2005). Under the Administrative Procedure Act ("APA"), an Administrative Law Judge may not issue an order "except on consideration of the whole record or those parts thereof cited by a party and supported by and in accordance with the reliable, probative, and substantial evidence." 5 U.S.C. § 556(d). All findings of fact in this Initial Decision are supported by reliable, probative, and substantial evidence.

D. Burden of Proof

The parties' burdens of proof are governed by Federal Trade Commission Rule 3.43(a), Section 556(d) of the Administrative Procedure Act ("APA"), and case law. Pursuant to Commission Rule 3.43(a), "[c]ounsel representing the Commission . . . shall have the burden of proof, but the proponent of any factual proposition shall be required to sustain the burden of proof with respect thereto." 16 C.F.R. § 3.43(a). Under the APA, "[e]xcept as otherwise provided by statute, the proponent of a rule or order has the burden of proof." 5 U.S.C. § 556(d). The APA, "which is applicable to administrative adjudicatory proceedings unless otherwise provided by statute, 'establishes . . . [the] preponderance-of-the evidence standard.'" *In re Rambus Inc.*, 2006 FTC LEXIS 101, at *45 (Aug. 20, 2006) (quoting *Steadman*

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v. SEC, 450 U.S. 91, 95-102 (1981)), *rev 'd on other grounds*, 522 F.3d 456 (D.C. Cir. 2008), *cert. denied*, 129 S. Ct. 1318 (2009). See *In re Automotive Breakthrough Sciences, Inc.*, No. 9275, 1998 FTC LEXIS 112, at *37 n.45 (Sept. 9, 1998) (holding that each finding must be supported by a preponderance of the evidence in the record); *In re Adventist Health System/West*, No. 9234, 1994 FTC LEXIS 54, at *28 (Apr. 1, 1994) ("Each element of the case must be established by a preponderance of the evidence.").

E. Summary of Initial Decision

The Commission, who issued the Complaint in this case, has determined in the State Action Opinion that the Respondent has no defense under the state action doctrine. Accordingly, in this Initial Decision, the Administrative Law Judge will conduct no analysis nor provide any Findings of Fact or Conclusions of Law regarding that issue, including whether or not teeth whitening services provided by non-dentists violates North Carolina law.

Complaint Counsel has demonstrated by a preponderance of the evidence that dentist members of the Board had a common scheme or design, and hence an agreement, to exclude non-dentists from the market for teeth whitening services and to deter potential providers of teeth whitening services from entering the market. To achieve this objective, dentist members of the Board agreed, expressly and/or implicitly, to cause the Board to: (a) send letters to non-dentist teeth whitening providers, ordering them to cease and desist from offering teeth whitening services; (b) send letters to manufacturers of products and equipment used by non-dentist providers, and other potential entrants, either ordering them to cease and desist from assisting clients offering teeth whitening services, or otherwise attempting to dissuade them from participating in the teeth whitening services market; (c) send letters to owners or operators of malls to dissuade them from leasing to non-dentist providers of teeth whitening services; and (d) elicit the help of the North Carolina Board of Cosmetic Art Examiners to dissuade its licensees from providing teeth whitening services. The evidence further shows that dentists and non-dentists compete with one another in the relevant market for teeth whitening services in North Carolina, and that the Board's concerted action to exclude non-

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dentist provided teeth whitening services from the market constitutes an agreement to exclude rivals, which by its nature has the tendency to harm competition.

Complaint Counsel further proved by a preponderance of the evidence that the Board had the power to exclude non-dentists from the teeth whitening services market in North Carolina by using its apparent authority as a state agency to declare the practice illegal and direct non-dentists to stop that practice. The Board's power to exclude was also demonstrated by evidence that, as a result of the Board's conduct, non-dentist providers did, in fact, exit the market and mall owners and operators refused to lease space to non-dentist teeth whiteners.

Complaint Counsel also demonstrated by a preponderance of the evidence that the Board's concerted actions to exclude non-dentist teeth whitening in North Carolina resulted in anticompetitive effects, which include: (1) non-dentist teeth whitening providers exited the North Carolina market; (2) consumer choice was limited, by the exclusion of non-dentist teeth whitening providers; (3) manufacturers of products used by non-dentist providers of teeth whitening services lost sales in North Carolina; and (4) mall owners and operators stopped leasing to non-dentist providers.

Based on the foregoing, absent a valid procompetitive justification, the Board's conduct constitutes an unreasonable restraint of trade and an unfair method of competition, in violation of Section 5 of the FTC Act. None of the procompetitive justifications proffered by Respondent is valid under applicable antitrust law.

Respondent's proffered procompetitive justification that, in acting to restrict non-dentist teeth whitening, the Board was acting as a state agency enforcing the North Carolina Dental Practice Act ("Dental Practice Act"), to protect the public interest, and not to promote economic self-interest, is essentially a reiteration of Respondent's claim that the Board's conduct is exempt from antitrust liability by the state action doctrine, which has been decided against Respondent by the Commission. State Action Opinion, 2011 WL 549449, at *1, 17.

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Respondent's proffered procompetitive justification that the Board's actions to exclude non-dentist provided teeth whitening services were intended to promote social welfare and/or public safety, *inter alia* by protecting consumers from dangerous or unsafe teeth whitening services, is also not a valid justification under applicable antitrust law. A restraint on competition cannot be justified solely on the basis of social welfare concerns, including concerns about health hazards. Accordingly, this Initial Decision will not analyze, or provide any Findings of Fact or Conclusions of Law regarding, whether or not non-dentist teeth whitening is harmful or unsafe for consumers.

Another of Respondent's proffered procompetitive justifications, that the restraints the Board placed upon non-dentist teeth whitening are procompetitive because they will ensure that teeth whitening services are offered at a cost that reflects the higher skills of dentist-providers, rather than at a cost reflecting the assertedly lower skills of non-dentists, is also rejected as invalid under applicable antitrust law. The risk that an inferior product will be marketed to, and chosen by, consumers is inherent in the nature of competition. To justify a restraint on the ground that competition itself is harmful contradicts the basic policy of the antitrust laws.

Finally, Respondent's proffered procompetitive justification that the Board's restraints on non-dentist provided teeth whitening services are procompetitive because they will promote legal competition between dentists in the teeth whitening services market, rather than the allegedly illegal practice of non-dentist teeth whitening services, is without merit. Respondent cites no case holding that non-dentist teeth whitening is a violation of North Carolina law, and this Initial Decision need not and does not decide that issue. Moreover, that a particular practice may be unlawful is not, in itself, a sufficient justification for collusion among competitors to prevent it.

Accordingly, because Respondent's proffered procompetitive justifications are invalid under applicable antitrust law, the Board's concerted action to exclude non-dentists from the market for teeth whitening services in North Carolina, in which North

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Carolina dentists and dentist Board members compete, constitutes an unreasonable restraint of trade and an unfair method of competition in violation of Section 5 of the FTC Act. The Board's arguments that the relief sought in this case violates the Tenth Amendment to the United States Constitution and exceeds the federal government's Commerce Clause powers are rejected. Having found such violation, an order will be entered, the provisions of which are designed to ensure an end to the unlawful conduct, rectify past violations, and prevent reoccurrence, and are reasonably related to the violations found to exist.

II. FINDINGS OF FACT**A. The North Carolina State Board of Dental Examiners**

1. The North Carolina State Board of Dental Examiners (the "Board") is an agency of the State of North Carolina and is charged with regulating the practice of dentistry in the interest of the public health, safety, and welfare of the citizens of North Carolina. The Board is organized, exists, and transacts business under and by virtue of the laws of the State of North Carolina. Its principal office and place of business is located at 507 Airport Blvd., Suite 105, Morrisville, NC 27560. (Joint Stipulations of Law and Fact ¶ 1).

1. Composition and election/selection of Board members*a. Composition of the Board*

2. The Board consists of eight members: six licensed dentists, one licensed dental hygienist, and one consumer member. The consumer member is neither a dentist nor a dental hygienist. (CX0019 at 001, N.C. Gen. Stat. § 90-22(b) (hereafter "Dental Practice Act § __"); Joint Stipulations of Law and Fact ¶ 2; White, Tr. 2194).

3. The dental hygienist member of the Board is elected to the Board by the licensed dental hygienists of North Carolina. (CX0019 at 001, Dental Practice Act § 90-22(b); White, Tr. 2242-2243).

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4. The consumer member of the Board is appointed by the Governor. (Joint Stipulations of Law and Fact ¶ 3; White, Tr. 2243).

5. The consumer member was added to the Board to look out for the welfare of the consumer and to ensure that dentist Board members act in the public interest, even when such action may be unpopular with dentists. (CX0449 at 005; CX0219 at 005; CX0242 at 005; CX0028 at 005; CX0559 at 008 (Efird, Dep. at 23)).

b. Dentist members of the Board are practicing dentists

6. Each dentist elected to the Board must be licensed and actively engaged in the practice of dentistry while serving on the Board. (CX0019 at 001, Dental Practice Act § 90-22(b); CX0574 at 007 (White, IHT at 25)).

7. Since June 2002, all dentists serving on the Board have been full-time practicing dentists in North Carolina. (CX0563 at 003-004, 010 (Goode, IHT at 9-10, 34)). Board members Allen, Burnham, Brown, Feingold, Hardesty, Holland, Morgan, Owens, and Wester (more fully defined in Section II.B.1 *infra*) were actively practicing when they served on the Board. (CX0554 at 006 (Allen, Dep. at 17); CX0555 at 004 (Brown, Dep. at 8); CX0556 at 004 (Burnham, Dep. 9); CX0560 at 004 (Feingold, Dep. at 9); Hardesty, Tr. 2760-2761; CX0567 at 006 (Holland, Dep. at 14); CX0569 at 004 (Morgan, Dep. at 9); Owens, Tr. 1435; CX0572 at 004 (Wester, Dep. at 7)).

8. During their tenure as Board members, dentist Board members continue to provide for-profit dental services, including teeth whitening services. (CX0560 at 48 (Feingold, Dep. at 183-184); CX0567 at 017 (Holland, Dep. at 58); CX0572 at 009 (Wester, Dep. 26-28); CX0554 at 007 (Allen, Dep. at 18-19)).

9. Many of the dentist Board members provide teeth whitening services through their private practices and derive income from it. (CX0467 at 001 (Dr. Owens); CX0340 at 002 (Dr. Morgan); CX0606 at 005 (Dr. Burnham); CX0614 at 001

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(Dr. Wester); CX0554 at 006 (Allen, Dep. at 18); CX0556 at 038 (Burnham, Dep. at 145-146); CX0560 at 004-005 (Feingold, Dep. at 9-10); CX0564 at 011 (Hall, Dep. at 33-34); CX0565 at 005 (Hardesty, Dep. at 15); CX0567 at 017 (Holland, Dep. at 56-58); CX0569 at 009 (Morgan, Dep. at 27-30); CX0572 at 009 (Wester, Dep. at 20-21, 26-27)).

10. Dr. Owens and his partner earned over \$75,000 from teeth whitening services from 2005 through 2010. (CX0467 at 001; Owens, Tr. at 1589-1590). Dr. Owens earned revenue from teeth whitening during the period of time when he assigned teeth whitening investigations to himself, in his capacity as Secretary-Treasurer of the Board. (Owens, Tr. 1579). Dr. Owens is also the case officer on most of the teeth whitening cases. (White, Tr. 2224).

11. Dr. Hardesty earned over \$40,000 from teeth whitening services from 2005 through 2010. (CX0378 at 012).

12. Board members have a significant, nontrivial financial interest in the business of their profession, including teeth whitening. (F. 9-11; Kwoka, Tr. 1114; CX0826 at 029 (Baumer, Dep. at 106-107) (Board members "may well be influenced by the impact on the bottom line," including the financial interest of dentists, in deciding whether to ban non-dentist teeth whitening)). They are in a position to enhance their incomes and their constituents' incomes. (Kwoka, Tr. 1115-1116; F. 13-15, 101-104, 108 (dentists earn income from teeth whitening services)).

c. The Board is funded by licensees

13. The Board is funded by the dues or fees paid by licensed dentists and dental hygienists in North Carolina. (CX0577 at 009 (Oyster, Dep. at 26); CX0556 at 061 (Burnham, Dep. at 237)).

14. The operating budget for the Board comes from license fees paid by North Carolina dentists and hygienists. (Joint Stipulations of Law and Fact ¶ 11).

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d. Dentists elect dentists for positions on the Board

15. The six dentist members of the Board are elected to the Board directly by other licensed dentists in North Carolina. (CX0019 at 001, Dental Practice Act § 90-22(b), (c); Joint Stipulations of Law and Fact ¶ 6; White, Tr. 2242).

16. Only licensed dentists from North Carolina are eligible voters in Board elections of dentists. (Joint Stipulations of Law and Fact ¶ 4).

17. Board members seek support from other dentists when they run for a position on the Board. (CX0574 at 008 (White, IHT at 28-29); Hardesty, Tr. 2796-2798).

18. If an election is contested, candidates may distribute letters and make speeches that discuss the reasons they want to serve on the Board, including their positions on issues that may come before the Board. (Joint Stipulations of Law and Fact ¶ 9). An election is "contested" when there are more candidates running for election than there are available Board positions. (Joint Stipulations of Law and Fact ¶ 8).

19. Board member Dr. Hardesty's efforts to get elected included sending a letter to all the licensed dentists in the state and asking for their vote, and meeting and talking with dentists at local dental society meetings. (CX0566 at 009 (Hardesty, IHT at 32-33)).

20. Board member Dr. Feingold sent a letter to all licensed dentists in North Carolina expressing his desire to be elected to the Board and solicited support for his election to the Board at the three-day annual convention of the North Carolina Dental Society ("NCDS"). (CX0560 at 011 (Feingold, Dep. at 34-35)).

21. Board member Dr. Burnham sent letters to all of the licensed dentists in North Carolina each time that he ran for a Board position telling them that he would appreciate their vote. (CX0556 at 017-018 (Burnham, Dep. at 61-62)).

22. Board member Dr. Brown sent a letter to dentists in North Carolina stating that he was interested in continuing the Board's

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practice of dentists' governing themselves when he ran in his first contested election. (CX0555 at 037 (Brown, Dep. at 140-141)).

23. Board member Dr. Stanley Allen sent letters to North Carolina dentists during his campaigns for a Board position in which explained his qualifications and why he should be elected. (CX0554 at 017 (Allen, Dep. at 58-59)).

e. Board member terms

28. The dentist members of the Board are elected for three-year terms and can run for reelection, but no person shall be nominated, elected, or appointed to serve more than two consecutive terms on the Board. (CX0019 at 001, Dental Practice Act § 90-22(b); Joint Stipulations of Law and Fact ¶ 7).

29. Some of the dentist members of the Board have served two or more terms. Drs. Allen, Brown, Burnham, Hardesty, and Owens have served two terms on the Board. (CX0554 at 004 (Allen, Dep. at 7); CX0555 at 004 (Brown, Dep. at 9); CX0556 at 007 (Burnham, Dep. at 20); CX0565 at 007 (Hardesty, Dep. at 20-21); CX0570 at 005 (Owens, Dep. at 11-12)). Drs. Morgan and Holland have served three or more terms on the Board. (CX0569 at 004-005 (Morgan, Dep. at 9-12); CX0567 at 005 (Holland, Dep. at 10-11)).

f. Members of the Board from 2005 through 2010

30. The officers of the Board are elected by the Board members. (White, Tr. 2202).

31. For the Board term year starting in August 2005, the Board consisted of Stanley L. Allen (President), Benjamin W. Brown (Immediate Past President), Joseph S. Burnham, (Secretary-Treasurer), Neplus H. Hall (Dental Hygienist Member), Zannie Poplin Efird (Consumer Member), Clifford O. Feingold, W. Stan Hardesty, and Ronald K. Owens. (CX0086 at 002, Annual Report to the Governor – 2006).

32. For the Board term year starting in August 2006, the Board consisted of Joseph S. Burnham (President), Stanley L.

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Allen (Immediate Past President), W. Stan Hardesty (Secretary-Treasurer), Neplus H. Hall (Dental Hygienist Member), Zannie Poplin Efird (Consumer Member), Clifford O. Feingold, C. Wayne Holland, and Ronald K. Owens. (CX0088 at 002, Annual Report to the Governor, 2007).

33. For the Board term year starting in August 2007, the Board consisted of W. Stan Hardesty (President), Joseph S. Burnham (Immediate Past President), Ronald K. Owens (Secretary-Treasurer), Neplus H. Hall (Dental Hygienist Member), Zannie Poplin Efird (Consumer Member), Clifford O. Feingold, C. Wayne Holland, and Brad C. Morgan. (CX0089 at 002, Annual Report to the Governor, 2008).

34. For the Board term year starting in August 2008, the Board consisted of Ronald K. Owens (President), W. Stan Hardesty (Immediate Past President), C. Wayne Holland (Secretary-Treasurer), Jennifer A. Sheppard (Dental Hygienist Member), Zannie Poplin Efird (Consumer Member), Joseph S. Burnham, Brad C. Morgan, and Millard W. Wester. (CX0091 at 002, Annual Report to the Governor, 2009).

35. For the Board term year starting in August 2009 and ending in July 2010, the Board consisted of C. Wayne Holland (President), Ronald K. Owens (Immediate Past President), Brad C. Morgan (Secretary-Treasurer), Jennifer A. Sheppard (Dental Hygienist Member), James B. Hemby, Jr. (Consumer Member), W. Stan Hardesty, Kenneth M. Sadler, and Millard W. Wester. (CX0091 at 002-005, Annual Report to the Governor – 2009).

36. The following chart shows the Board members from 2005 to July 2010. (F. 27-31).

BOARD OF DENTAL EXAMINERS	Term 2005-06	Term 2006-07	Term 2007-08	Term 2008-09	Term 2009-10
President	Allen	Burnham	Hardesty	Owens	Holland
Immediate Past President	Brown	Allen	Burnham	Hardesty	Owens
Secretary- Treasurer	Burnham	Hardesty	Owens	Holland	Morgan

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Dentist Members	Feingold Hardesty Owens	Feingold Holland Owens	Feingold Holland Morgan	Burnham Morgan Wester	Hardesty Wester Sadler
Hygienist Member	Hall	Hall	Hall	Sheppard	Sheppard
Consumer Member	Efrid	Efird	Efird	Efrid	Hemby

2. The authority and duties of the Board

33. The Board is authorized and empowered by the Legislature of North Carolina to enforce the provisions of the Dental Practice Act. (Joint Stipulations of Law and Fact ¶ 12).

34. The Board generally meets once a month for three days. (White, Tr. 2194; CX0562 at 004 (Friddle, IHT at 12)).

a. The Board's authority over North Carolina dentists

35. The Board is the sole licensing authority for dentists in North Carolina. (CX0019 at 007, Dental Practice Act § 90-29(a)). The Board has the authority to issue licenses, renew licenses, and take disciplinary actions against dentists practicing in North Carolina. (CX0019 at 013, 015, 020, 021, Dental Practice Act §§ 90-30, 31, 34, 40, 40.1, 41).

36. The dental hygienist member and consumer member of the Board cannot participate or vote on Board matters concerning the issuance, renewal, or revocation of a dentist's license. The consumer member of the Board cannot participate or vote on Board matters concerning the issuance, renewal, or revocation of a dental hygienist's license. (CX0019 at 001, Dental Practice Act § 90-22(b)).

37. The Dental Practice Act provides that the consumer member and the dental hygienist member are excluded from participating or voting on matters involving the "issuance, renewal or revocation of the license to practice dentistry," and, in

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the case of the consumer member, the license to practice dental hygiene. (CX0019 at 001, Dental Practice Act § 90-22(b)).

38. The Dental Practice Act does not prohibit the consumer member or the hygienist member from serving as the case officer in a non-dentist teeth whitening investigation. (Hardesty, Tr. 2838).

39. The Dental Practice Act does not prohibit the consumer member or the hygienist member from participating in investigations of unlicensed practice of dentistry by non-dentist teeth whiteners. (Wester, Tr. 1334-1335).

40. Despite the facts set forth above in F. 37-39, the dental hygienist member and consumer member of the Board were excluded from participating in investigations of the unlicensed practice of dentistry, including investigations of non-dental teeth whitening. (Hardesty, Tr. 2838) (case officer assignments in teeth whitening investigations are reserved for dentists); CX0554 at 013 (Allen, Dep. at 44) (Dr. Allen never appointed the consumer member or the hygienist member to be on an investigative panel for an unauthorized practice of dentistry investigation); CX0559 at 008 (Efird, Dep. at 23) (consumer member of the Board did not participate in unauthorized practice of dentistry matters); CX0564 at 005 (Hall, Dep. at 12-13) (dental hygienist member did not participate in unlicensed practice of dentistry investigations).

b. The Board's authority relating to non-dentists

41. The Dental Practice Act provides that it is unlawful for an individual to practice dentistry in North Carolina without a current license to practice dentistry issued by the Board. (CX0019 at 007, 020, Dental Practice Act § 90-29(a), 40, 40.1(a)).

42. The Dental Practice Act sets forth practices that constitute the practice of dentistry. (CX0019 at 007-008, Dental Practice Act § 90-29(b)). Under the Dental Practice Act, a person shall be deemed to be practicing dentistry if that person "[r]emoves stains,

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accretions or deposits from the human teeth." (CX0019 at 007-008, Dental Practice Act § 90-29(b)(2)).

43. Under the Dental Practice Act, the North Carolina State Board of Dental Examiners may bring an action to enjoin the practice of dentistry by any person who has not been duly licensed in the superior court of any county in which the acts occurred or in which the defendant resides. (CX0019 at 020-021, Dental Practice Act § 90-40.1(c)).

44. The Dental Practice Act states that in the event of suspected instances of the unlicensed practice of dentistry: the Board may petition a state court for an injunction, (CX0019 at 020-021, Dental Practice Act § 90-40.1). The Board may not prosecute criminally for unlicensed practice of dentistry; however, it may refer matters to the District Attorney for criminal prosecution. (CX0581 at 021-022 (Bakewell, Dep. at 76-79)).

45. The Board has no authority over non-dentists, and its only authorized recourse against non-dentists engaged in what the Board believes to be the practice of dentistry is to go through the courts. (CX0554 at 034 (Allen, Dep. at 129); CX0019 at 006, 007, 020-021, Dental Practice Act § 90-27, 29, 40, 40.1).

46. The Board's authority to hold administrative hearings under the Dental Practice Act is limited to addressing conduct of its licensees or applicants for such a license. (CX0019 at 023, Dental Practice Act § 90-41.1(a)). The Board's authority to hold administrative hearings under the Dental Practice Act does not include claims that a non-licensee is engaging in the unlicensed practice of dentistry. (CX0019 at 023, Dental Practice Act § 90-41.1(a)).

47. The Board does not conduct hearings for unlicensed practice of dentistry matters. (CX0554 at 013 (Allen, Dep. at 43); CX0574 at 011 (White, IHT at 39)).

48. The Board does not have authority to discipline unlicensed individuals. (Owens, Tr. 1443, 1516).

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49. The Board does not have the legal authority to order anyone to stop violating the Dental Practice Act. (White, Tr. 2284-2288).

B. The Witnesses

1. Fact witnesses

50. Set forth below, in alphabetical order, are the identities of the witnesses who testified either in person at the hearing or through deposition testimony:

Dentist Board members

51. Dr. Stanley L. Allen, Jr. served two three-year terms on the Board, from August 2001 through July 2007. Dr. Allen has also been a member of the NCDS since he arrived in North Carolina. (CX0554 at 004-006 (Allen, Dep. at 7-8, 13-14)).

52. Dr. Benjamin W. Brown served two terms on the Board and was President from 2005 through 2006. He has also held the position of Board Secretary/Treasurer twice and was the chair of the sedation and general anesthesia committee for the Board. Dr. Brown has been in practice since 1967 and has a specialty in endodontics. (CX0555 at 003-005 (Brown, Dep. at 7-12)).

53. Dr. Joseph S. Burnham, Jr., a general dentist who has been in practice for 42 years, was first elected to the Board in 2003 for a three-year term. Dr. Burnham ran for a second term on the Board in 2006, was reelected, and served another three-year term. (CX0556 at 004-005, 007, 009 (Burnham, Dep. at 9-10, 20-21, 28)). While he was a member of the Board, Dr. Burnham would give reports about what the Board was doing to the Second District Dental Society's executive meetings as an ex-officio member. Dr. Burnham has occasionally sat as a delegate in the house of representatives at the NCDS. (CX0556 at 005 (Burnham, Dep. at 12)).

54. Dr. Clifford Feingold is a general dentist who has been in practice for 34 years. Dr. Feingold became a Board member in

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August 2005 and served through August 2008. (CX0560 at 004-005 (Feingold, Dep. at 9, 12)).

55. Dr. Willis Stanton Hardesty, Jr. is a licensed dentist in Raleigh, North Carolina. He served two terms on the Board, from August 2004 through July 2010. He served as President of the Board from August 2007 through August 2008. (Hardesty, Tr. 2759, 2761-2762; CX0565 at 007 (Hardesty, Dep. at 20-21)). Dr. Hardesty was a member of the Academy of General Dentistry, the North Carolina Academy of General Dentistry, and the American Academy of Cosmetic Dentistry. At the North Carolina Academy of General Dentistry, Dr. Hardesty held "every office beginning with a delegate through presidency and on to the past presidency", and was a delegate to the House of Delegates of the Academy of General Dentistry. The North Carolina Academy of General Dentistry has as one of its purposes the furthering of interest of dentists in the dental profession. There was a multi-year overlap between Dr. Hardesty's service in officer positions at the North Carolina Academy of General Dentistry and a delegate to the House of Delegates of the Academy of General Dentistry and Dr. Hardesty's service on the Board. (Hardesty, Tr. 2798-2800).

56. Dr. Bradley C. Morgan is currently serving on the Board and has had a general dentistry practice in Canton, North Carolina since December 1981. Dr. Morgan also has been a member of the American Dental Association and the NCDS. Dr. Morgan believes he served on the legislation committee and the dental education committee of the NCDS. (CX0569 at 004-007 (Morgan, Dep. at 9-10, 16-19, 21)).

57. Dr. Ronald K. Owens is a general dentist who has been licensed in the State of North Carolina since 1996. His dental practice is currently located in Winston-Salem, North Carolina. Dr. Owens has been a member of the Board since August 2005 and is the current President of the Board until his term expires on July 31, 2011. (Owens, Tr. 1434-1435, 1439-1440).

58. Dr. Millard W. Wester III is a general dentist practicing in Henderson, North Carolina. He became licensed to practice dentistry in North Carolina in August 1980. Dr. Wester has been

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a member of the Board since 2008, and became Secretary-Treasurer in August 2010. His first term will expire in July 2011. (Wester, Tr. 1276-1278, 1281, 1315-1316).

Non-dentist Board members

59. Ms. Zannie Poplin Efird was the Consumer Representative on the Board from August 2003 until August 2009, serving two terms. (CX0559 at 004 (Efird, Dep. at 7)). Although she was a voting member of the Board, she did not vote on disciplinary matters involving dentists and hygienists, did not participate in any Board matters relating to the unlicensed practice of dentistry, and did not participate in any votes on teeth whitening matters. (CX0559 at 004-008 (Efird, Dep. at 7, 16, 23)).

60. Ms. Neplus S. Hall was the dental hygiene representative of the Board from 2002 through 2008. Ms. Hall did not participate in any discussions relating to teeth whitening and was not involved in any manner with the Board's investigations of teeth whitening. (CX0564 at 005 (Hall, Dep. at 12-13)).

Other witnesses associated with the Board

61. Ms. Carolin Bakewell has served as outside counsel to the Board through her own firm, Carolin Bakewell PLLC, since January 2010. Previously, from September 2006, Ms. Bakewell was in-house counsel for the Board. (CX0581 at 005 (Bakewell, Dep. at 10)).

62. Ms. Casie Smith Goode is the Assistant Director of Investigations for the Board, and has held this position since approximately 2004. She began working for the Board in June 2002 as an executive assistant. As Assistant Director of Investigations, Goode assists the director of investigations, Terry Friddle (F. 64), in overseeing investigations. Goode sets up files, drafts correspondence, makes copies, and communicates with case officers (*see* F. 178). (CX0563 at 003-004 (Goode, IHT at 9-10)). Goode and Friddle both work with three of the six dentist Board members in their roles as case officers. (CX0563 at 004, 027-028 (Goode, IHT at 10-11, 105-107)).

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63. Mr. William Linebaugh Dempsey has been employed as an investigator with the Board since June 2003. Mr. Dempsey investigates teeth whitening complaints by observing the kiosk or salon at which the teeth whitening services are performed. (*See* F. 186, 188). He often takes pictures and may write notes on topics including, if chairs or LED lights were set up, or if providers were wearing lab coats. (CX0557 at 004, 009 (Dempsey, Dep. at 8, 28-29); CX0558 at 003 (Dempsey, IHT at 7)).

64. Ms. Terry W. Friddle is the Deputy Operations Officer for the Board and has worked for the Board for 29 years. As Deputy Operations Officer she is "second in command" at the Board and considers herself the director of investigations. Ms. Friddle reports to both the Board's Chief Operating Officer ("COO") Bobby White and the individual Board members. She oversees the investigative process and makes preparations for the Board's meetings. (CX0561 at 004-005, 006 (Friddle, Dep. at 8-10, 15); CX0562 at 006 (Friddle, IHT at 18)).

65. Dr. Larry Tilley practices general dentistry in Raleigh, North Carolina. Dr. Tilley has worked as a paid consultant for the Board for about twenty years. Dr. Tilley evaluates complaints, examines complainants, and reports back to the Board. Dr. Tilley acts as a consultant for the Board two or three times a year, on issues such as dentures, decay, crowns, and general dental procedures. Dr. Tilley has consulted for the Board on one teeth whitening complaint. (Tilley, Tr. 1997, 2004-2007).

66. Mr. Bobby White is the Chief Operating Officer of the Board. He has had this position since February 2004. He is a licensed attorney in North Carolina. Mr. White's duties include human resources, payroll, insurance, contract negotiations, and advising the Board with regard to disciplinary and legal matters. As part of his duties, he has been designated as the media contact for the Board, and the Board's representative with the North Carolina legislature and serves as liaison with the NCDS. (White, Tr. 2189-2190, 2256-2257; CX0574 at 004, 020 (White IHT at 11-12, 77)).

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Other dentists

67. Dr. William M. Litaker has practiced dentistry for 25 years. He is a member of the NCDS, and acts as an NCDS delegate to the American Dental Association and also is a member of the NCDS legislative committee. Dr. Litaker was a trustee of the NCDS from 1999 through 2005. Additionally, from 2006 through 2009, in successive one-year terms, he was Secretary/Treasurer, President-elect, President, and Past President of the NCDS. (CX0576 at 004-005 (Litaker, Dep. at 7, 11)).

68. Dr. Gary D. Oyster has practiced general dentistry for 37 years. Dr. Oyster's practice is located in Raleigh, North Carolina. Dr. Oyster has been the chairman of the legislative committee of the NCDS since approximately 1996. As chairman of the NCDS legislative committee, Dr. Oyster works with the committee to construct an agenda, which is for presentation to the NCDS board of trustees, and enlists the political priorities of the NCDS. (CX0577 at 004-006, 027 (Oyster, Dep. at 7-8, 13-15, 99)).

69. Dr. M. Alec Parker practiced general dentistry from 1979 through 2007. Dr. Parker ceased his dental practice in 2007 and became an employee of the NCDS. He initially acted in an associative or assistive position to the NCDS executive director until January 2008, when he became executive director. Dr. Parker remains the executive director of the NCDS. (CX0578 at 004-005 (Parker, Dep. at 9-13)).

Teeth whitening manufacturers or marketers

70. Mr. George Nelson is the President of WhiteScience, a teeth whitening manufacturing and marketing business located in Alpharetta, Georgia. WhiteScience manufactures and sells a teeth whitening system called SpaWhite. SpaWhite is principally marketed to spas, salons, fitness centers, trade shows, and mall locations. WhiteScience also sells a teeth whitening product to dentists called Artiste. (Nelson Tr. 721-722, 725-726, 729, 800).

71. Ms. Joyce Osborn is the president and founder of BEKS, Inc., which manufactures and distributes the BriteWhite Teeth

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Whitening System ("BriteWhite System"). BEKS, Inc., is located in Jasper, Alabama and has been in operation since 2004. Ms. Osborn is also the President of the Council for Cosmetic Teeth Whitening ("CCTW"), created in 2007 and incorporated in 2008, which is a trade association that promotes the cosmetic teeth whitening industry and provides a self-administered teeth whitening protocol for use by manufacturers and distributors of non-dentist teeth whitening systems. In addition, Ms. Osborn has operated a beauty salon and spa for more than 26 years. (Osborn, Tr. 646-647, 675, 687).

72. Mr. James Valentine is a co-founder of WhiteSmile USA, a manufacturer and marketer of teeth whitening products, founded in 2007. By 2008, WhiteSmile USA earned revenues of ten million dollars, had 125 to 130 employees, and operated in more than 60 Sam's Club stores across the United States. In its first three years of operation, WhiteSmile oversaw more than 100,000 in-store bleachings. (Valentine, Tr. 515, 546-548, 574-575).

Kiosk or salon operators

73. Mrs. Margie Hughes has been a licensed esthetician since 2005. Mrs. Hughes' training as an esthetician has included a 600-hour course at Central Carolina Community College in Sanford, North Carolina, and continuing education courses of at least eight hours per year. Mrs. Hughes operates her business as SheShe Skin, currently located within the Hair Republic Salon in Dunn, North Carolina. (Hughes, Tr. 928-933).

74. Mr. Brian Wyant opened a WhiteScience kiosk in 2007 after asking questions about the business over the phone and traveling to WhiteScience's headquarters in Atlanta for training. He received training on the protocol relating to teeth whitening, product information, issues relating to documentation, utilizing a consent form, and procedures for safety and cleanliness. (Wyant, Tr. 860, 864-866, 876-884, 892; CX0629 at 001-003).

Mall owner

75. Mr. John Gibson is a partner and Chief Operations Officer of Hull Storey Gibson Companies, L.L.C., also known as HSG.

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Mr. Gibson oversees the operations of HSG, a retail property management company that owns and operates 11.5 million square feet of retail space in seven states, including the management of five enclosed malls in North Carolina. (Gibson, Tr. 613-615).

Consumer

76. Mr. Brian Runsick is a consumer who underwent teeth bleaching at the BleachBright facility at Crabtree Valley Mall in February 2008. He testified regarding a complaint he filed with the Board in which he claimed injury as a result of the teeth bleaching. (Runsick, Tr. 2105-2106).

2. Expert witnesses

a. Complaint Counsel's expert witnesses

i. Dr. John Kwoka, Ph.D.

77. Dr. John Kwoka is a Professor of Economics at Northeastern University. He has a bachelor's degree in economics from Brown University and a Ph.D. in economics from the University of Pennsylvania. Dr. Kwoka has taught economics, at various institutions, for over 30 years. (Kwoka, Tr. 969-972).

78. Dr. Kwoka worked for six years in the Bureau of Economics at the Federal Trade Commission, and one year each in the Antitrust Division of the Department of Justice and as a Special Assistant to the Director of the Common Carrier Bureau of the Federal Communications Commission. (Kwoka, Tr. 972-973).

79. Dr. Kwoka offered these opinions, in summary: that dentist and non-dentist providers of teeth whitening services compete with one another in the provision of teeth whitening services and are close substitutes for each other; that the Board represents licensed dentists in North Carolina and that such dentists have a material interest in prohibiting non-dentist teeth whitening; that the Board acted to prohibit non-dentist teeth whitening services in North Carolina; that exclusion of

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non-dentist teeth whitening service providers is harmful to consumers because it denies some consumers of options they prefer and likely increases the prices of the remaining options; that complete exclusion is not justified by any economic argument of the Board; that the Board's claims of harm from non-dentist teeth whitening have little evidentiary support; and that if such problems of harm do exist, they can be resolved through less restrictive remedies than exclusion of teeth whitening service providers. (CX0654 at 001; Kwoka, Tr. 982, 994, 996-997, 998, 1001-1002, 1114-1116).

ii. Dr. Martin Giniger

80. Dr. Martin Giniger has been a licensed dentist since 1984. He also has a master's degree in oral medicine and a Ph.D. in biomedical science, specializing in oral biology. (Giniger, Tr. 78-79). Dr. Giniger has also been a teacher and researcher. (CX0653 at 001-002).

81. Dr. Giniger has worked and consulted for numerous oral care companies, and has been involved in developing and/or testing the safety and effectiveness of a variety of oral care products, including teeth bleaching products. Dr. Giniger has been involved in the development of teeth bleaching products such as Colgate's Whitening Toothpastes and Systems, Discus' Dental NiteWhite with ACP at-home teeth whitening product, and Discus' Dental Zoom2 teeth whitening system for in-office use. (Giniger, Tr. 96-98; CX0653 at 002-003).

82. Dr. Giniger offered these opinions, in summary: that teeth bleaching, also commonly known as teeth whitening, is safe and effective regardless of whether it is provided by dentists or non-dentists; that teeth whitening is not the same thing as stain removal; that the Board's materials submitted as supporting exclusion of non-dentist teeth whitening service providers for reasons of actual or potential harm were not persuasive; that the operating protocols for non-dentist teeth whitening establishments that he reviewed indicated that there was no reason that appropriate sanitary conditions could not be maintained, even absent running water; that there is no evidence that non-dentist provided teeth whitening poses any greater risk than dentist

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provided teeth whitening; that consumers benefit from having a variety of safe alternatives for teeth whitening; and that the actions of the Board in excluding non-dentists from teeth whitening has needlessly harmed consumers. (CX0653 at 006-009).

*b. Respondent's expert witnesses**i. Dr. Van B. Haywood*

83. Dr. Van B. Haywood has a D.M.D. from the Medical College of Georgia School of Dentistry, where he is now a professor of oral rehabilitation. He practiced dentistry for seven years in Georgia, and also taught at the University of North Carolina School of Dentistry before moving to the Medical College of Georgia. Dr. Haywood is also the director of continuing education at the Medical College of Georgia School of Dentistry. Dr. Haywood has researched and published on the safety and effects of tray bleaching, including the use of Nightguard Vital Bleaching at-home tray bleaching. (RX0077 at 002-003).

84. Dr. Haywood offered these opinions, in summary: that for safety reasons teeth whitening should always be preceded by a proper dental examination to determine the cause of discoloration or staining; that teeth whitening involves bleaching, which constitutes stain removal from teeth; that non-dentist teeth whiteners present themselves as health professionals with the requisite training and skill to diagnose and treat dental conditions; that the safety and quality of certain teeth whitening products is unknown; that teeth whitening without a prior dental exam may be wasteful, result in the masking of a clinical problem, or create an unsightly aesthetic; and that teeth whitening is the practice of dentistry, and is illegal under the North Carolina Dental Practice Act. (RX0077 at 004-006; Haywood, Tr. 2398, 2403-2404, 2545, 2571-2573).

ii. Dr. David L. Baumer, Ph.D.

85. Dr. David L. Baumer has a Ph.D. in economics from the University of Virginia and a J.D. from the University of Miami.

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He is a Professor and Head of the Business Management Department at North Carolina State University, College of Management. He also has a consulting practice related to academics. Most of his work has been in the area of governmental regulation. Dr. Baumer was retained to review the expert report of Dr. John Kwoka. (RX0078 at 002, 005-006; Baumer, Tr. 1693-1694).

86. Dr. Baumer offered these opinions, in summary: Dr. Kwoka's opinions that the Board has a material interest in prohibiting non-dentist teeth whitening and that the Board's conduct has harmed consumers would apply to virtually every federal, state, or local professional and occupational licensing board; that a cartel model is an inappropriate method for evaluating governmental licensing boards; that the cartel model ignores evidence that licensing requirements curb fraud and protect public health and safety by preventing consumer harm at the hands of unqualified practitioners; and that Dr. Kwoka cites no evidence that prices charged by dentists for teeth whitening were or are being affected by the non-availability of non-dentist teeth whitening. Dr. Baumer also opined, in summary, that there is a rational basis for regulating the dental profession based on the health and safety of North Carolina citizens and for North Carolina law to require the majority of Board members to be practicing dentists; that restricting the unlicensed practice of dentistry is an obvious and desirable consequence of regulation; and that the Board is not a cartel, but rather excludes unqualified practitioners. (RX0078 at 002-005; Baumer, Tr. 1708; 1696-1697).

C. Jurisdictional Issues

87. The Board is an agency of the State of North Carolina, and is charged with regulating the practice of dentistry in the interest of the public health, safety, and welfare of the citizens of North Carolina. (Joint Stipulations of Law and Fact ¶ 1).

88. Manufacturers of teeth whitening equipment and products used by dentist and non-dentist teeth whiteners are located outside the State of North Carolina. *See* Joint Stipulations of Law and Fact ¶ 21 (non-dentist teeth whiteners in North Carolina bought

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brand name products, including WhiteSmileUSA, BriteWhite, Beyond White Spa, Beyond Dental & Health, and SpaWhite) and ¶ 25 (dentist teeth whiteners in North Carolina used products by Zoom and Bright Smile); (F. 89-92).

89. WhiteSmile sells and licenses a teeth whitening system manufactured by DaVinci in California, and once operated in North Carolina. (Valentine, Tr. 520, 561, 567).

90. WhiteScience, a manufacturer of non-dentist teeth whitening systems located in Alpharetta, Georgia, sells its products nationally, and has sold some of its products into North Carolina. (Nelson, Tr. 733-734). WhiteScience operates in over 40 states. (Nelson, Tr. 800).

91. BriteWhite, a manufacturer of non-dentist teeth whitening systems located in Jasper, Alabama, sells its products nationally, and has sold some of its products into North Carolina. BriteWhite's products have been sold to customers in Florida, California, New York, Illinois, Ohio, Indiana, Texas, North Carolina and other states. (Osborn, Tr. 645, 668-670).

92. Board member Dr. Hardesty purchased the Zoom in-office teeth whitening system from Discus Dental, headquartered in Culver City, California, in 2002 or 2003, although he no longer uses this product in his office. (CX0535 at 001; CX0565 at 027 (Hardesty, Dep. at 98-100)).

93. Dentist and non-dentist teeth whiteners in North Carolina use instrumentalities of interstate communication in the conduct of their businesses, including without limitation, the telephone and the internet to communicate with manufacturers of teeth whitening equipment and products located outside the State of North Carolina. (E.g., CX0268 at 001-002; CX0313 at 001-002; CX0605 at 003-004; CX0610 at 001-005; CX0036 at 003; CX0119 at 001-002; CX0620 at 001; CX0045 at 003; CX0054 at 006; CX0281 at 001; CX0312 at 001; Hughes, Tr. 934-936; Wyant, Tr. 861, 863-866).

94. Dentist and non-dentist teeth whiteners in North Carolina purchase and receive products and equipment that are shipped

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across state lines by manufacturers and suppliers located outside the State of North Carolina. (CX0050 at 001; CX0565 at 027 (Hardesty, Dep. at 98-100); Osborn, Tr. 668-670; Nelson, Tr. 733-734; Hughes, Tr. 934-936; CX0655 at 001-003; Wyant, Tr. 861, 863-864, 868-869, 891).

95. Dentist and non-dentist teeth whiteners in the State of North Carolina transfer money and other instruments of payment across state lines to pay for teeth whitening equipment and products received from manufacturers located outside the State of North Carolina. (CX0050 at 001; CX0565 at 027 (Hardesty, Dep. at 98-100); Osborn, Tr. 668-670; Nelson, Tr. 733-734; Wyant, Tr. 861, 863-864, 868-869, 891).

96. The Board sent at least 40 cease and desist letters to non-dentist teeth whiteners in North Carolina that contained various headings directing non-dentists to cease and desist offering teeth whitening services. (Joint Stipulations of Law and Fact ¶ 30; CX0042 at 001 to 041; Kwoka, Tr. 990; RX0078 at 008; CX0050 at 002-003; CX0069 at 001-002; CX0074 at 001-002; CX0077 at 001-002; CX0096 at 001-002; CX0097 at 001-002; CX0153; CX0155; CX0156; CX0386 at 001-002). Some recipients of cease and desist letters sent copies of those letters to their out-of-state suppliers of products, equipment, or facilities. (CX0119 at 001-002).

97. The Board sent at least eleven letters to third parties, including out-of-state property management companies that indicated that teeth whitening services offered at mall kiosks that are not supervised by a licensed North Carolina dentist is illegal. (Joint Stipulations of Law and Fact ¶ 31; CX0203 at 001; CX0204 at 001 (CBL & Associates, Chattanooga, Tennessee); CX0260 at 001 (General Growth Properties, Chicago, Illinois); CX0261 at 001 (Hendon Properties, Atlanta, Georgia); *see also* CX0205 at 001; CX0259 at 001; CX0260 at 001; CX0262 at 001; CX0263 at 001; CX0323 at 001; CX0324 at 001; CX0325 at 001).

98. The eleven letters referred to in F. 97 impacted out-of-state mall operators' decisions whether to rent kiosks or stores to non-dentist teeth whiteners in North Carolina. (Gibson,

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Tr. 627-628, 632-633; Wyant, Tr. 876-884; CX0629 at 001-002; CX0525 at 001).

99. The Board sent letters titled Notice to Cease and Desist to out-of-state manufacturers of teeth whitening products used by non-dentist teeth whiteners in North Carolina. (CX0100 at 001 (December 4, 2007, Notice to Cease and Desist to WhiteScience, Roswell, GA); CX0122 at 001-002 (October 7, 2008, Notice and Order to Cease and Desist to Florida WhiteSmile in Orlando, FL)).

D. The Relevant Market is Dentist Provided and Non-Dentist Provided Teeth Whitening Services

1. Teeth whitening services generally

100. Teeth whitening can be achieved in one of three methods: (1) bleaching or lightening, through the application of some form of peroxide - hydrogen peroxide or carbamide peroxide; (2) through the use of aesthetic or prosthetic dental restorations, such as crowns, caps or veneers; and (3) through dental stain removal, either through the application of toothpaste or by going to the dentist to have stains scraped off, including by the use of rotary instruments to polish teeth. (Giniger, Tr. 128-132).⁷

101. A 1989 article publicized the discovery that the use of low level concentrations of hydrogen peroxide, if held against the teeth in a tray or other mechanism, could whiten teeth. A few years later, various companies started developing products for the purpose of whitening teeth and dentists began using this method to whiten patients' teeth. (Giniger, Tr. 149-150; CX0653 at 024; CX0550 at 002-003; CX0392 at 002).

102. The American Academy of Cosmetic Dentistry ("AACD") reported in 2004 and the American Dental

⁷ The Complaint challenges conduct relating only to the first method of teeth whitening. Complaint ¶¶ 8, 10. The term "teeth whitening" is used herein to refer to the first method of teeth whitening, bleaching or lightening through the application of some form of peroxide.

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Association's ("ADA") Counsel for Scientific Affairs reported in 2009 that teeth whitening or bleaching has become one of the most popular esthetic dental treatments over the past two decades.

The AACD reported in 2004 that teeth whitening or bleaching is the number one requested cosmetic dentistry procedure, and had increased more than 300% since 1996. (CX0397 at 001; CX0392 at 002).

103. A 2008 national Gallup Poll reported that over 80% of dentists nationwide engage in the practice of teeth whitening. (CX0513 at 007).

104. Some dentists in North Carolina earned thousands of dollars annually in revenue from the provision of teeth whitening procedures during the period from 2005 through August of 2010. (CX0599 at 003; CX0605 at 003; CX0616 at 021; CX0601 at 008; CX0608 at 002; CX0602 at 002; CX0600 at 003; CX0603 at 003).

2. Teeth whitening products and services methods

105. There are four categories of teeth whitening services or products available in North Carolina: (1) dentist in-office teeth whitening services; (2) dentist provided take-home teeth whitening products; (3) over-the-counter ("OTC") teeth whitening products; and (4) non-dentist teeth whitening services in salons, retail stores, and mall kiosks. (Kwoka, Tr. 981-984, 1168; Baumer, Tr. 1845; CX0392 at 002; CX0053 at 004-005; Osborn, Tr. 650; Valentine, Tr. 515).

106. The four alternative methods of teeth whitening (F.105) have a number of common characteristics. All of the methods use some form of peroxide - hydrogen peroxide or carbamide peroxide - and all involve application of that chemical in gel or strip form directly onto the teeth. All of the methods trigger the same chemical process that results in whiter teeth. (Kwoka, Tr. 997; Baumer, Tr. 1925-1926).

107. The four alternative methods of teeth whitening (F. 105) differ in ways that are important to consumers, including immediacy of results, ease of use, provider support, and price.

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(Giniger, Tr. 118-121; Haywood Tr. 2915-2917; Kwoka, Tr. 994-995; CX0653 at 005).

a. Dentist in-office teeth whitening services

108. Dentists offer and provide teeth whitening services in North Carolina. (CX0467 at 001; CX0578 at 007 (Parker Dep. at 12-14); CX0566 at 003 (Hardesty, IHT at 9); CX0576 at 005 (Litaker, Dep. at 11-12); CX0577 at 009 (Oyster, Dep. at 28); Wester, Tr. 1289; CX0554 at 007 (Allen, Dep. at 18-19); CX0641 at 001-067).

109. The teeth whitening products used by dentists for in-office teeth whitening generally have a higher concentration of the active ingredients hydrogen peroxide or carbamide peroxide than that typically available in non-dentist teeth whitening. Dentist provided in-office bleaching typically uses highly concentrated hydrogen peroxide (25% to 35%), applied multiple times during a single office visit. (Joint Stipulations of Law and Fact ¶ 24; Giniger, Tr. 169, 172; CX0653 at 021; RX0078 at 006).

110. Dental chair-side bleaching is performed by a dentist or supervised assistant in a dental chair at the dentist's office. The procedure includes a dental exam by the dentist to identify whether or not a patient is an appropriate candidate for teeth whitening services. (Giniger, Tr. 179-180; Haywood, Tr. 2472; CX0653 at 039).

111. During a preparatory time of up to 30 minutes, the patient's teeth are exposed using cheek retractors. Due to the high concentration of peroxide used in professional bleaching products (up to 38%), a protective barrier is applied to prevent the gums from burning. (Joint Stipulations of Law and Fact ¶ 24; Giniger, Tr. 168-169; Haywood Tr. 2692). The peroxide solution is thereafter painted directly on the teeth and a curing light is often placed in front of the teeth to activate the bleaching gel or expedite the whitening effect. After 30 minutes, the gel is usually suctioned off the teeth using a dental vacuum. The gel is reapplied, the light (if used) is set again, and the treatment is repeated up to two more times for a total of 60-120 minutes of

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actual bleaching time. (CX076 at 007 (Parker, Dep. at 21); CX0596 at 002; Giniger, Tr. 164-172; CX0653 at 040).

112. Dental chair-side bleaching can be done with or without the use of an accelerator light, which emits heat and ultra-violet radiation (UV) to accelerate whitening. (Giniger, Tr. 169; CX0653 at 021, 027).

113. To complement the accelerator light, dental chair-side formulations may also contain a photo or thermal activator, a chemical designed to interact with the light or heat to cause the peroxide to break down more quickly. (Giniger, Tr. 169, 172; CX0653 at 021; CX0809A; CX0809B).

114. Many dentists today use lights, such as light emitting diode (LED) lights, which generate neither appreciable UV nor heat, above the ambient temperature. (Giniger, Tr. 187-188; CX0632 at 011).

115. Patients having in-office teeth whitening wear protective glasses to prevent eye injury from the spatter of hydrogen peroxide as it is applied directly to the teeth or from UV in the event the dentist uses a UV-emitting light. (Giniger, Tr. 181-191).

116. Dentist in-office teeth whitening services provide results in one to three hours. (CX0601 at 026; CX0598 at 001; CX0641 at 040).

117. Dentist in-office teeth whitening services range widely in price, but charges between \$400 and \$500 are common. (Kwoka, Tr. 982; RX0078 at 006-007; CX0560 at 048 (Feingold Dep. at 183 (\$500)); CX0053 at 001-002 (\$400); CX0108 at 008 (\$400-\$900); CX0096 at 004 (\$400-\$600); Hardesty, Tr. at 2805-2806 (\$675-\$750); CX0578 at 005 (Parker, Dep. at 12-13 (\$350)); CX0601 at 009 (\$550); CX0609 at 002 (regularly \$350); CX0611 at 004 (\$400); CX0616 at 034 (averaged \$537 for in-office bleaching); CX0653 at 040 (\$500 to \$800); CX0570 at 043-044 (Owens, Dep. at 167-168) (approximately \$500)).

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118. Dentist provided chair-side bleaching is the most costly bleaching alternative, of the four options described in F. 105, often costing between \$400 and \$700. (Giniger, Tr. 119-120).

119. The principal benefits of dentist in-office teeth whitening are that it is quick and effective, providing immediate results in one visit to the dentist. Additional benefits include professional service, guidance, and support. (Giniger, Tr. 180-181; Kwoka, Tr. 981-982).

120. The disadvantages to dentist in-office teeth whitening are that it is relatively expensive compared to the alternatives, and it requires making an appointment with the dentist that may not be at a convenient time for the consumer. (Kwoka, Tr. 981-982).

b. Take-home kits provided by dentists

121. Dentists in North Carolina also offer take-home teeth whitening kits that consumers self-administer after a consultation with the dentist. (Giniger, Tr. 119-121; CX0652 at 019-020; CX0571 at 006 (Owens, IHT at 20-21); CX0570 at 023 (Owens, Dep. at 84); CX0560 at 004-005, 048 (Feingold, Dep. at 9-10; 183); Hardesty, Tr. at 2775; CX0565 at 006 (Hardesty, Dep. at 15); CX0578 at 005 (Parker, Dep. at 11-12); CX0580 at 006-007 (Tilley, Dep. at 14-15, 19); CX0641 at 001-067).

122. Take-home kits provided by dentists include a custom-made whitening tray and whitening gel. The tray is created either by the dentist, hygienist or technician, and takes roughly 30 to 45 minutes to fabricate. (CX0580 at 006 (Tilley, Dep. at 14); CX0554 at 007 (Allen, Dep. at 18-19); CX0566 at 003 (Hardesty, IHT at 9); CX0566 at 019 (Hardesty, IHT at 72); Wester, Tr. 1289; Giniger, Tr. 200).

123. Take-home kits provided by dentists can either be used as a follow-up to in-office treatment or as the sole teeth whitening service. (Joint Stipulations of Law and Fact ¶ 26).

124. Take-home kits provided by dentists usually require at least two visits to the dentist. Typically, in the first visit, the

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dentist examines the patient and takes an impression used to make a customized teeth whitening tray. Usually, in the second visit, the dentist delivers the tray and whitening solution, and provides instructions for whitening to the patient. (Joint Stipulations of Law and Fact ¶ 28).

125. Take-home kits provided by dentists typically use low concentrations of hydrogen peroxide or carbamide peroxide and require the consumer to reapply the whitening solution to his or her own teeth multiple times over a period of weeks or months. (Joint Stipulations of Law and Fact ¶ 27; Giniger, Tr. 119-121; CX0571 at 006 (Owens, IHT at 20-21)).

126. Take-home kits provided by dentists typically cost hundreds of dollars, in part because the dentist performs a diagnostic examination, charges to fabricate the custom tray, provides instruction on its use, and supplies the whitening product and kit. (CX0576 at 005-006 (Litaker, Dep. at 16-17 (\$380 per arch/\$760 for full mouth)); CX0577 at 009 (Oyster, Dep. at 29 (\$300)); CX0578 at 005 (Parker, Dep. at 12-13 (\$250))).

127. Take-home kits provided by dentists are usually more expensive than any non-dentist provided products. (Compare CX0653 at 043 (non-dentist take home product costs between \$40 and \$80) with Giniger, Tr. 201 (typical price of dentist provided take home kit is \$350 to \$500)).

128. Take-home kits provided by dentists are less expensive than the dentist in-office procedure and are also relatively effective at whitening teeth. On the other hand, the consumer is required to apply the product at home a number of times without assistance. (Kwoka, Tr. 982-983; CX0654 at 004).

c. Over-the-counter products

129. Manufacturers recently developed unique trayless methods for over-the-counter ("OTC") at-home bleaching. Available OTC products include gels, rinses, chewing gums, trays, and strips. In a 2006 report, NBC's *Today* correspondent Janice Liebennan reported that in 2005, the U.S. market for OTC

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products was \$41.4 billion. (CX0653 at 041; Joint Stipulations of Law and Fact ¶ 22).

130. OTC products typically use relatively low concentrations of hydrogen peroxide or carbamide peroxide, that are applied daily for an extended period of time. OTC products are sold in a variety of locations including pharmacies, groceries, over the internet, and even by dentists. (Giniger, Tr. 204-207).

131. Crest Whitestrips from Proctor and Gamble (P&G) was one of the first OTC teeth bleaching products on the market, and it remains the number one selling product today. When first made available to consumers in 2001, Whitestrips contained approximately 5% hydrogen peroxide. Now, the most popular Whitestrips contain a greater concentration of bleaching agents. Other manufacturers have also developed generic whitening strips as well, and the concentration of hydrogen peroxide in these strips has also increased significantly over the years. (CX0653 at 041; CX0566 at 016 (Hardesty, IHT at 58-59); CX0555 at 019 (Brown Dep. at 67); CX0560 at 030 (Feingold, Dep. 111-112); CX0570 at 020 (Owens, Dep. 71-72)).

132. Consumers self-apply the OTC strips directly to their teeth. (Kwoka, Tr. 983; CX0654 at 004).

133. In order to whiten teeth, OTC strips must be reapplied multiple times over multiple days. (Joint Stipulations of Law and Fact ¶ 29).

134. OTC strips and trays typically cost between \$15 and \$50, depending on brand, quantity, and concentration. (CX0382 at 001 (Crest 3D - \$43.97); CX0394 at 001 (Crest 3D White Strips Professional Effects - \$47.99, Plus White 5 Minute Speed Whitening System - \$10.99, DenTek Complete White Professional Whitening - \$14.99)).

135. The whitening results with OTC strips are highly variable because user compliance is variable. A great many consumers will not complete the whitening regimen, which may require up to 30 days of daily use. (CX0653 at 041-042).

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136. The OTC strips have the advantages of the convenience of at-home treatment as well as low cost compared to the other alternatives. The OTC strips are effective when used over a period of days or weeks. The disadvantage is that OTC strips require diligent and repeated application by the consumer. (Kwoka, Tr. 983; CX0654 at 004).

d. Non-dentist teeth whitening service providers

137. Teeth whitening services are offered by non-dentists, including in North Carolina, and have been offered since approximately 2003 or 2004. (Hughes, Tr. 934-936; Nelson, Tr. 733-734; Osborn, Tr. 646-47, 668-670; Wyant Tr., 860-63, 870-871; Valentine, Tr. 567).

138. Teeth whitening services by non-dentists are offered in kiosks, spas, retail stores, and salons. (Hughes, Tr. 934-936; Nelson, Tr. 733-734; Osborn, Tr. 668-670; Valentine, Tr. 519-520; Wyant Tr. 870-871).

139. Teeth whitening products used by non-dentists fall under many brand names, including WhiteSmile USA, BriteWhite, Beyond White Spa, Beyond Dental & Health, and SpaWhite. (Joint Stipulations of Law and Fact ¶ 21).

140. Non-dentist teeth whitening providers typically use a mid-level hydrogen peroxide or carbamide peroxide concentration, typically equating to 16% or less of hydrogen peroxide. The product is usually applied once during a single visit. (Giniger, Tr. 182-183; CX0653 at 021).

141. A gingival barrier is not required in a non-dentist bleaching procedure because the concentration of peroxide used is non-caustic, and often the delivery system, such as a sponge in the mouthpiece that is pre-impregnated with peroxide, prevents unwanted dispersal of peroxide into the oral cavity. (Giniger, Tr. 192; CX0653 at 020-021).

142. Typically, but not always, a non-dentist provider will follow a protocol provided by a teeth whitening manufacturer or

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distributor. While each protocol is slightly different, all require the operator to provide the customer with literature, and some require the customer to answer questions before the procedure begins. (CX0108 at 009; CX0049 at 056-067; Valentine, Tr. 545-546; Osborn, Tr. 653, 707; Nelson, Tr. 796-797).

143. In a typical non-dentist bleaching procedure, the operator generally will: (1) have the client sit in a chair; (2) put on protective gloves; (3) place a bib around the client's neck; (4) take a tray from a sealed package, which is either pre-filled with peroxide solution or which the operator fills with the peroxide solution, and hand it to the customer, who places the tray into his or her mouth; (5) adjust the light, if used; and (6) start the timer. At the end of the procedure, the customer will remove the tray and hand it to the provider, who disposes of it. (Giniger, Tr. 188-189; CX0108 at 010-012; CX0049 at 056-067; Osborn, Tr. 653, 655, 707-708; Nelson, Tr. 750, 757, 770, 796-797; Valentine, Tr. 533-534).

144. Non-dentist bleaching centers may use lights during the procedure. However, unlike dentists, these facilities use LED lights, which produce no UV radiation and little heat above the ambient temperature. (Giniger, Tr. 182-183, 479; CX0653 at 021).

145. Most manufactures use a tray delivery system, which is often pre-impregnated with peroxide. (Giniger, Tr. 187, 385).

146. Teeth whitening services offered in kiosks, spas, retail stores, and salons typically take one hour or less to whiten the customer's teeth. (Nelson, Tr. 740 (whitening process took 20 minutes using SpaWhite); Osborn, Tr. 653-656 (whitening process took 20 minutes after placement of the BriteWhite whitening tray); Valentine, Tr. 532-533 (once a customer had a tray inside his mouth, the session with the light would last 15 minutes with WhiteSmile)).

147. The cost of non-dentist teeth whitening varies, but ranges between \$75 and \$150. (Kwoka, Tr. 984; CX0654 at 004).

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148. Non-dentist teeth whitening services are typically priced below dentist provided services (\$400 to \$500 (F. 117)) and above OTC teeth whitening products (\$15 to \$50 (F. 134)). (Baumer, Tr. 1926; CX0826 at 034 (Baumer, Dep. at 128)).

149. Non-dentist chair-side bleaching is accessible, located most often in large shopping malls, and does not require an appointment. (CX0653 at 042; Valentine, Tr. 532; Tilley, Tr. 1973).

150. Non-dentist teeth whitening can be completed in a single bleaching session. It is effective at whitening teeth but with a significantly lower cost in comparison to in-office dentist teeth whitening. (Kwoka, Tr. 983-984; CX0654 at 004).

3. Dentist and non-dentist provided teeth whitening services are a relevant market

a. Dentist and non-dentist provided teeth whitening services are reasonable substitutes for one another

151. Non-dentist and dentist teeth whitening services have common characteristics, including quick and efficient service, provision of instruction, provision of a tray, loading of the peroxide, and use of a light activator. (*Compare* F. 109-114 with F. 140-146).

152. If a consumer wants effective "one-shot" teeth whitening, the only ways to achieve such immediate results would be to go to a dentist or a non-dentist provider of teeth whitening services, such as those located in mall kiosks. (Kwoka, Tr. 982-984, 998; CX0560 at 048 (Feingold, Dep. at 184); Nelson, Tr. 766-767).

153. If a consumer wants teeth whitening within 24 hours, and has not previously made an appointment with a dentist, he or she would turn to a non-dentist provider of teeth whitening services because they have similar attributes as dentist provided services. (Baumer, Tr. 1975-1976; CX0826 at 034 (Baumer, Dep. at 126-27)).

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154. Cross-elasticity is an economic term measuring the degree of substitution between alternative products, defined as the percentage change in quantity and demand of one product as the price of a different product changes. (Kwoka, Tr. 999-1000).

155. There is substantial cross-elasticity between dentist and non- dentist teeth whitening services. (Kwoka, Tr. 999; Baumer, Tr. 1842).

156. Dentist provided and non-dentist provided teeth whitening services are reasonable substitutes for one another. (F. 151-155).

b. Dentists and non-dentists compete with one another

157. Dentists are aware that there is commonality and substitution between the methods of teeth whitening. (Kwoka, Tr. 997-998; CX0392 at 002).

158. Dentists and non-dentist teeth whiteners in North Carolina compete to provide teeth whitening services to consumers in North Carolina. (Kwoka, Tr. 994-998; RX0078 at 010).

159. Dr. Burnham discussed with other Board members that consumers may choose to go to a kiosk teeth whitener to get their teeth whitened rather than to a dentist. (CX0556 at 040 (Burnham, Dep. at 152)).

160. A non-dentist teeth whitener operating within two miles of a dentist could affect the volume of teeth whitening services provided by the dentist. (CX0565 at 024 (Hardesty, Dep. at 87)).

161. A dental practice that sought to perform teeth whitening as an important part of its revenue stream might react to the price charged by a nearby non-dentist teeth whitener by reducing its own prices for teeth whitening. (CX0565 at 024 (Hardesty, Dep. at 87-88)).

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162. Dr. Baumer agrees that a reduction in supply of teeth whitening services will have an upward impact on price. (Baumer, Tr. 1700).

163. Dentists in North Carolina have made claims in advertisements that they practice "Cosmetic Dentistry," including the provision of teeth whitening services. (CX0641 at 001-002, 004, 013, 015-018, 020, 024-027, 029-032, 039, 043-044, 048-049, 052, 059-060, 063-067).

164. Non-dentist providers of teeth whitening services target advertisements to consumers who would or are considering going to the dentist for teeth whitening. The advertisements boast similar results as dentists but for a lower price, indicating a belief that consumers will substitute between these two alternatives. (Kwoka, Tr. 999).

165. Non-dentist providers of teeth whitening services in North Carolina have advertised that they charge lower prices for their services than dentists charge for their teeth whitening services. (Kwoka, Tr. 999; CX0556 at 040 (Burnham, Dep. at 151-152); *see also* CX0096 at 004; CX0103 at 014-015; CX0043 at 005; CX0108 at 009; CX0054 at 006; CX0198 at 002).

166. Non-dentist providers of teeth whitening services in North Carolina have compared their services to teeth whitening provided by dentists with respect to efficacy. (CX0041 at 006-007; CX0096 at 004; CX0108 at 008-009).

167. Non-dentist teeth whiteners in North Carolina have compared themselves to dentists in terms of time and convenience. (CX0108 at 009).

168. Non-dentist providers of teeth whitening services have advertised that they can whiten teeth in one hour or less. (CX0308 at 007; CX0043 at 002; CX0078 at 002; CX0108 at 008; CX0054 at 006; CX0103 at 009).

169. Discus Dental, the largest manufacturer of whitening products for dentists, maker of Zoom and BriteSmile, has included salon/mall operations in its consumer surveys, indicating

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industry recognition of non-dentist competition. The survey found that on several different attributes, including convenience, value, and pain, consumers rate these non-dentist teeth whitening operations between OTC products and dentist provided products. (CX0489 at 013, 031-032, 044-045, 050, 052).

4. The relevant market does not include self administered teeth whitening products

170. Take-home products do not contain as much hydrogen peroxide as contained in the products used by dentists and non-dentists providing teeth whitening services. (Giniger, Tr. 204-205; CX0653 at 020, 041).

171. Take-home products require numerous bleaching sessions over many days or weeks. By contrast, chair-side bleaching, whether provided by dentists or non-dentists, is usually limited to a single session. (Giniger, Tr. 118-119; CX0653 at 005).

172. The amount of time it takes to whiten the teeth is important to some consumers of teeth whitening services or products. (Hardesty, Tr. 2812-2813; Nelson, Tr. 766).

173. OTC products come only with instructions. By comparison, dentists provide professional service, support, and advice and non-dentists typically provide service based on training provided to them by the manufacturers of the bleaching products/services and their own experience. (Giniger, Tr. 119; CX0653 at 005).

174. OTC products (\$20-\$60) are the least expensive alternative for consumers. These products are good for cost-conscious consumers who are willing to self-apply bleaching products over several days or weeks aided only by written instructions. However, they are not a good substitute for chair-side teeth bleaching for those consumers intent on quick results or wary about self-application of OTC products without supervision or support. (Giniger, Tr. 120-121; CX0653 at 005-006).

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E. The Board's Cease and Desist Letters⁸

1. Background

a. The Board's process for handling complaints and investigations of unauthorized practice of dentistry

175. The Board conducts investigations of allegations that persons are engaged in the unauthorized practice of dentistry. (CX0236 at 001-002; Owens, Tr. 1440-1441; 21 N.C.A.C. 16 U.0101; 21 N.C.A.C. 16 U.0102 (21 N.C.A.C. 16 *et seq.* contains the Board's Rules)).

176. The Board's process for handling complaints and investigations in non-licensee cases, including those regarding teeth whitening, is set forth in the Board's investigations manual. (CX0527 at 008-010, 029-031; White, Tr. 2220-2221).

177. The process for handling non-licensee cases includes the receipt of a complaint, an investigation, and a decision by the case officer about how to proceed after the investigation. (CX0556 at 064 (Burnham, Dep. at 247-248)).

178. All complaints to the Board initially go to the Board's Deputy Operations Officer, Terry Friddle. (CX0562 at 011 (Friddle, IHT at 38-39)). Ms. Friddle assigns case numbers to the complaints and forwards the complaints to the Secretary-Treasurer. (White, Tr. 2219).

179. The Board's Secretary-Treasurer, a dentist, receives all complaints filed with the Board and assigns them to a case officer. (White, Tr. 2202-2203; Wester, Tr. 1281).

⁸ The testimony and exhibits refer to communications sent by the Board interchangeably as "cease and desist orders" and "cease and desist letters." Findings as to whether these communications constituted "letters" or "orders" are set forth in F. 207-226. Based on these findings, except where the term "cease and desist order" is specifically used in the testimony or exhibit, the communications sent by the Board are referred to herein as "cease and desist letters."

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180. The Secretary-Treasurer has discretion in assigning cases or investigations. (White, Tr. 2203). The Secretary-Treasurer may keep a case or assign the case to another Board member. The assigned Board member is referred to as the case officer for that investigation. (CX0562 at 011 (Friddle, IHT at 38-39); CX0556 at 007-008 (Burnham, Dep. at 21-22); Owens, Tr. 1440-1441).

181. The investigative panel conducts investigations of alleged instances of the unlawful practice of dentistry. (Owens, Tr. 1440-1441; CX0527 at 006, 009-010, 015; CX0234 at 001-011).

182. A Board investigative panel consists of the case officer, the Deputy Operations Officer or Board designee, and the Investigator assigned to the investigation. The Board's legal counsel may participate in the panel meetings as needed. (CX0527 at 006; Owens, Tr. 1441; CX0554 at 012 (Allen, Dep. at 39)).

183. The case officer is the Board member assigned by the Board President or Secretary-Treasurer whose duty it is to oversee an investigation. (CX0527 at 006). Deputy Operations Officer Friddle assigns an investigator (either Mr. Kurdys or Mr. Dempsey) and a case manager (either Ms. Friddle or Ms. Goode) to the case. (CX0562 at 011 (Friddle, IHT at 38-39)).

184. Only dentists serve as case officers for teeth whitening investigations. (Hardesty, Tr. 2838; CX0563 at 009-010 (Goode, IHT at 33-34); CX0571 at 016 (Owens, IHT at 62); CX0566 at 008 (Hardesty, IHT at 27-28); CX0555 at 031-032 (Brown, Dep. at 117-118) (hygienist Board member cannot be assigned as a case officer)).

185. The case officer directs the investigation of instances of teeth whitening services performed by non-dentists and is assisted by other Board staff members. (Owens, Tr. 1441-1442; CX0571 at 014 (Owens, IHT at 50-51)).

186. At the direction of the case officer, Board investigators perform undercover investigations in non-dentist teeth whitening

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cases posing as prospective clients. (CX0558 at 017 (Dempsey, IHT at 64); (CX0038 at 004) (Hardesty directed Friddle to do a "sting" of a non-dentist teeth whitener where Board investigators posed as clients to have impressions made); CX0070 at 001; CX0367 at 001; CX0284 at 001; CX0201 at 001).

187. Board investigators also perform investigations, at the direction of the case officer, where they identify themselves as Board employees and ask questions about the processes used by non-dentist teeth whiteners. (CX0367 at 001; CX0228 at 001-002; CX0247 at 001).

188. Board investigator Dempsey often takes pictures and may write notes indicating whether non-dentist teeth whiteners had [dental] chairs set up, whether there were LED lights set up and if the providers were wearing lab coats. (CX0557 at 009 (Dempsey, Dep. at 28-29)).

189. The case officer is authorized by the Board to make enforcement decisions and take enforcement actions on its behalf. (CX0570 at 011 (Owens, Dep. at 37); CX0571 at 014 (Owens, IHT at 50-51); White, Tr. 2224).

190. At the conclusion of the investigation in an unlicensed practice of dentistry case, the case officer has two options. The case officer can direct the Board attorney to take civil action or recommend a criminal prosecution to a local district attorney. If that happens, the Board would be informed at the next Board meeting. (White, Tr. 2224).

191. The case officer in an unlicensed practice of dentistry case may decide to authorize a cease and desist letter to the target of the investigation. (CX0556 at 064 (Burnham, Dep. at 248)).

192. Ms. Efird, the consumer member of the Board, was a voting member of the Board. However, she did not vote on disciplinary matters involving dentists and hygienists. She did not participate in any votes on teeth whitening matters. (F. 59; CX0559 at 006 (Efird, Dep. at 16)).

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193. Ms. Hall, the hygienist member, was not involved in any manner with the Board's investigations of teeth whitening services. Ms. Hall did not participate in any discussions relating to teeth whitening while on the Board. (CX0564 at 006 (Hall, Dep. at 15-16)).

b. Complaints about non-dentist providers of teeth whitening services made by dentists

194. In or around 2003, the Board received its first complaints about non-dentist providers of teeth whitening services. (CX0562 at 006 (Friddle, IHT at 21)).

195. Dr. Benjamin Brown opened an investigation of Great White Smiles in September 2003 after Dr. Richard Yeager complained that his staff had informed him that Great White Smiles was selling teeth whitening gel and making impressions for bleach trays at the "Southern Women's Show" in Charlotte, North Carolina. (CX0033 at 001-005). Dr. Brown subsequently directed Ms. Friddle to close the investigation for "lack of evidence." (CX0032 at 001-005).

196. Between August and September 2, 2004, four North Carolina dentists complained to the Board about Edie's Salon Panache. The complaints noted that the salon advertised that it was the second "salon in North Carolina to offer teeth whitening" and that it offered a price of \$149, which was lower than the amount dentists charge. (CX0036 at 002-004).

197. On September 11, 2006, Dr. Luiz Arzola faxed the Board a complaint noting that "increasingly large number[s] of spas in the Hickory area are offering their clients dental bleaching." He inquired whether that procedure is legal when performed by unlicensed persons. (CX0619 at 001).

198. The Board met on February 9, 2007, and discussed the increasing number of complaints regarding non-dental teeth whitening services being provided in spas. (CX0056 at 005).

199. By February and March of 2008, Board employees Ms. Bakewell and Ms. Goode recognized that there were

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non-dentist teeth whitening service providers or "bleaching kiosks" and teeth whitening companies throughout the State of North Carolina. (CX0231 at 001; CX0092 at 001).

200. On November 19, 2007, Dr. Harald Heymann complained to the Board about a non-dentist bleaching salon in Southpoint Mall in North Carolina, emphasizing that the salon operator stated that they use 44% carbamide peroxide administered in a gel tray and that they charge \$100. (CX0365 at 002).

201. After receiving a February 18, 2008 complaint from Dr. Mark Casey of Raleigh, North Carolina about a teeth whitening kiosk in Crabtree Valley Mall, Bobby White, the Board's COO, responded that the Crabtree Valley whitening kiosk "is one of many such 'bleaching kiosks' with which we are currently going forth to do battle," and that the Board had sent out "numerous cease and desist orders throughout the state." (CX0404 at 001-002).

202. In a letter dated February 27, 2008, Dr. Nicole LeCann complained to the Board about a bleaching kiosk in Crabtree Valley Mall. Dr. LeCann noted that the kiosk's prices started at \$99 and wrote that the presence of kiosks "cheapens and degrades the dental profession." Dr. LeCann requested that the Board investigate the matter "quickly." (CX0278 at 001; White, Tr. 2317-2319).

203. The tripartite meeting is a meeting held between the North Carolina State Board of Dental Examiners, the North Carolina Dental Society ("NCDS") and the UNC School of Dentistry. The meeting is held once every year and hosted by each one of these groups on a rotating basis. (Hardesty, Tr. 2866).

204. The NCDS is a professional association of North Carolina Dentists that promotes, among other things, the interests of North Carolina dentists. (CX0578 at 010 (Parker, Dep. 32); CX0577 at 006 (Oyster, Dep. at 15)).

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205. At the April 4, 2008 tripartite meeting, the NCDS members in attendance complained about the proliferation of non-dentist teeth whitening kiosks and asked the Board what it was going to do about it. The Board assured the NCDS that it was investigating complaints about non-dentist teeth whiteners. (CX0565 at 067 (Hardesty, Dep. at 259-261); CX0109 at 003).

206. At a general meeting of the Board attended by Ms. Hall, it was mentioned that the Board would be investigating complaints about teeth whitening services. (CX0564 at 006 (Hall, Dep. at 15-16)).

2. Origins and numbers of cease and desist letters

207. On September 30, 2005, Board Investigator Dempsey sent an e-mail to Board member Dr. Brown and several Board staff regarding an investigation into jewelry stores fabricating decorative gold teeth. In the email he noted that he and Casie Smith [Goode], had previously developed a cease and desist letter to "deal with dentists practicing without a license" and he believed it would be useful in the jewelry case. He noted that he was working on a similar jewelry case in another part of the state and that he had written to the case officer in that case:

In an email to the Case Officer, I stated: "I also must say that I really do like the Cease and Desist Letter . . . I think in the past, we have had several of these type of cases [person is allegedly treating patients without a license] that ended up getting closed because we didn't have evidence . . . at least now we can put them on notice that we know something is going on. This might work well with the "gold teeth" type cases as well. With them, they may not know that it is against the law to take impressions . . . this informs them and lets them know we are investigating them (or at least they think we are constantly watching them, sending in undercover agents, etc . . . when we aren't). Hopefully, it causes them to modify their behavior.

(CX0080 at 002 (alterations in original); White Tr. 2335-2336).

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208. In 2006, the Board sent two cease and desist letters to non-dentist teeth whitening providers. (CX0038 at 001; CX0044 at 004-005). The first letter was to Serenity Day Spa, located at 814 C Old Spartanburg Highway, Hendersonville, North Carolina. (CX0038 at 001). The second letter was to Stephanie Keith of Star-Bright Whitening Systems at her place of business known as the Cutting Crib Hair Salon in Sanford, North Carolina. (CX0044 at 003-005).

209. In 2007, the Board sent at least 12 cease and desist letters to non-dentist teeth whitening providers. (CX0050 at 001-003; CX0069 at 001-002; CX0074 at 001-002; CX0077 at 001-002; CX0094 at 005-006; CX0096 at 001-002; CX0097 at 001-002; CX0279 at 001-002; CX0386 at 001-002). Of these 12 letters, several are addressed to the same establishment. (CX0065 and CX0097; CX0074 and CX0256).

210. Beginning in 2007, because the volume of complaints had increased, it became the policy of the Board to issue cease and desist letters on the basis of the complaint, without any investigation. (CX0070; CX0562 at 013 (Friddle, IHT at 43-44, 47)).

211. On March 22, 2007, Ms. Friddle sent an e-mail to Dr. Holland regarding the difficulty in getting the time to send staff to "perform these undercover spa deals." Ms. Friddle explained to Dr. Holland: "Dr. Hardesty has pretty much taken the stance that we write them a cease and desist letter the first go round." The Board would only "move in with the big guns," if the Board discovered that a cease and desist letter recipient persisted in providing non-dentist teeth whitening services. (CX0070 at 001; CX0561 at 022-023 (Friddle, Dep. at 81-83)).

212. When Dr. Hardesty directed Ms. Friddle around March 2007 to "write [non-dentist teeth whitening businesses] a cease and desist letter the first go round," Ms. Friddle understood that to mean to send a cease and desist letter when a complaint initially came in. On at least five occasions, she followed Dr. Hardesty's directions. (CX0070 at 001; CX0561 at 022-023 (Friddle, Dep. at 81-84)).

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213. In 2007 and 2008, cease and desist letters were sent "fairly quickly, like shortly after the case was set up." (CX0562 at 013 (Friddle, IHT at 47)). According to Ms. Friddle, "if it is unclear as to whether or not, or if it appears that there's a violation, then we would send a cease and desist." (CX0562 at 012 (Friddle, IHT at 43-44)).

214. Dr. Hardesty authorized sending a cease and desist letter to a business without having first sent an investigator to determine precisely what that business was doing. (Hardesty, Tr. 2856). Dr. Hardesty also authorized the sending of a cease and desist letter to a salon based solely on an e-mail from a dentist and his review of the website for the whitening product that the salon was considering using. (CX0565 at 043 (Hardesty, Dep. at 163-165); CX0293 at 001).

215. Dr. Owens sent out cease and desist letters within minutes or hours of receiving notice of a complaint, and at times without any investigation. (CX0297 at 001 (Dec. 1, 2008) (Dr. Owens authorized cease and desist 12 minutes after being assigned case); CX0311 at 001 (Dr. Owens authorized cease and desist letter same day as receiving assignment)).

216. In 2008, the Board sent at least 12 cease and desist letters to non-dentist teeth whitening providers. (CX0042 at 039-041; CX0059 at 001-002; CX0068 at 001-002; CX0079 at 001-002; CX0120 at 001-002; CX0122 at 001-002; CX0123 at 001-002; CX0387 at 001-002; CX0388 at 001-002; CX0389 at 001-002; CX0390 at 001-002; CX0391 at 001-002).

217. In 2009, the Board sent at least 22 cease and desist letters to non-dentist teeth whitening providers. (CX0042 at 001-002; CX0042 at 005-006; CX0042 at 008-009; CX0042 at 010-011; CX0042 at 012-013; CX0042 at 014-015; CX0042 at 016-017; CX0042 at 018-019; CX0042 at 020-021; CX0042 at 022-023; CX0042 at 024-025; CX0042 at 026-027; CX0042 at 028-029; CX0042 at 030-031; CX0042 at 032-033; CX0042 at 034-035; CX0058 at 001-002; CX0112 at 001-002; CX0153 at 001-002; CX0155 at 001-002; CX0156 at 001-002; CX0272 at 001-002). Several of these letters were sent to the same recipients. (CX0042 at 001-002 and CX0042 at 039-041).

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218. The Board has sent at least 47 cease and desist letters to non-dental teeth whitening manufacturers and providers since it began the practice in 2006. (CX0038 at 001; CX0042 at 001-002, 005-007, 008-009, 010-011, 012-013, 014-015, 016-017, 018-019, 020-021, 022-023, 024-025, 026-027, 028-029, 030-031, 032-033, 034-035; CX0044 at 004-005; CX0050 at 002-003; CX0058 at 001-002; CX0059 at 001-002; CX0065 at 001-002; CX0068 at 001-002; CX0069 at 001-002; CX0074 at 001-002; CX0077 at 001-002; CX0079 at 001-002; CX0094 at 005; CX0096 at 001-002; CX0097 at 001-002; CX0100 at 001-002; CX0112 at 001-002; CX0120 at 001-002; CX0122 at 001-002; CX0123 at 001-002; CX0153 at 001-002; CX0155 at 001-002; CX0156 at 001-002; CX0272 at 001-002; CX0279 at 001-002; CX0351 at 001-002; CX0386 at 001-002; CX0387 at 001-002; CX0388 at 001-002; CX0389 at 001-002; CX0390 at 001-002; CX0391 at 001-002; *see also* Joint Stipulations of Law and Fact ¶ 30 (stipulating to at least 40 cease and desist letters).

3. Content of cease and desist letters

219. The 47 cease and desist letters sent to non-dentist teeth whitening service providers or manufacturers were sent on the letterhead of the North Carolina State Board of Dental Examiners.

The letterhead also contains each Board members name, the Past President of the Board and the name of the Chief Operations Officer. (CX0038 at 001; CX0042 at 001-002, 005-007, 008-009, 010-011, 012-013, 014-015, 016-017, 018-019, 020-021, 022-023, 024-025, 026-027, 028-029, 030-031, 032-033, 034-035; CX0044 at 004-005; CX0050 at 002-003; CX0058 at 001-002; CX0059 at 001-002; CX0065 at 001-002; CX0068 at 001-002; CX0069 at 001-002; CX0074 at 001-002; CX0077 at 001-002; CX0079 at 001-002; CX0094 at 005; CX0096 at 001-002; CX0097 at 001-002; CX0100 at 001-002; CX0112 at 001-002; CX0120 at 001-002; CX0122 at 001-002; CX0123 at 001-002; CX0153 at 001-002; CX0155 at 001-002; CX0156 at 001-002; CX0272 at 001-002; CX0279 at 001-002; CX0351 at 001-002; CX0386 at 001-002; CX0387 at 001-002; CX0388 at 001-002; CX0389 at 001-002; CX0390 at 001-002; CX0391 at 001-002).

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220. At least 40 of the cease and desist letters sent to non-dentist teeth whitening service providers contain bold, capitalized headings that state: "NOTICE AND ORDER TO CEASE AND DESIST" or "NOTICE TO CEASE AND DESIST." (CX0038 at 001; CX0042 at 001-002, 005-007, 008-009, 010-011, 012-013, 014-015, 016-017, 018-019, 020-021, 022-023; 024-025, 026-027, 028-029, 030-031, 032-033; 034-035; CX0050 at 002-003; CX0058 at 001-002; CX0059 at 001-002; CX0065 at 001-002) or have a heading that states: "CEASE AND DESIST NOTICE." (CX0068 at 001-002; CX0069 at 001-002; CX0074 at 001-002; CX0077 at 001-002; CX0079 at 001-002; CX0094 at 005; CX0096 at 001-002; CX0097 at 001-002; CX0100 at 001-002; CX0112 at 001-002; CX0120 at 001-002; CX0122 at 001-002; CX0123 at 001-002; CX0272 at 001-002; CX0279 at 001-002; CX0351 at 001-002; CX0386 at 001-002; CX0387 at 001-002; CX0388 at 001-002; CX0389 at 001-002; CX0390 at 001-002; CX0391 at 001-002; Joint Stipulations of Law and Fact ¶ 30 (stipulating to at least 40 cease and desist letters)).

221. In addition to cease and desist headings, the cease and desist letters sent to 39 non-dentist teeth whitening service providers or manufacturers state:

You are hereby ordered to CEASE AND DESIST any and all activity constituting the practice of dentistry or dental hygiene as defined by North Carolina General Statutes § 90-29 and § 90-233 and the Dental Board Rules promulgated thereunder.

Specifically, G.S. 90-29(b) states that "A person shall be deemed to be practicing dentistry in this State who does, undertakes or attempts to do, or claims the ability to do any one or more of the following acts or things which, for the purposes of this Article, constitute the practice of dentistry:"

"(2) Removes stains, accretions or deposits from the human teeth;"

"(7) Takes or makes an impression of the human teeth, gums or jaws:"

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"(10) Performs or engages in any of the clinical practices included in the curricula of recognized dental schools or colleges."

(CX0042 at 001-002, 005-007, 008-009, 010-011, 012-013, 014-015, 016-017, 018-019, 020-021, 022-023, 024-025, 026-027, 028-029, 030-031, 032-033, 034-035; CX0050 at 002-003; CX0058 at 001-002; CX0059 at 001-002; CX0068 at 001-002; CX0069 at 001-002; CX0077 at 001-002; CX0079 at 001-002; CX0094 at 005; CX0096 at 001-002; CX0097 at 001-002; CX0112 at 001-002; CX0120 at 001-002; CX0122 at 001-002; CX0123 at 001-002; CX0272 at 001-002; CX0279 at 001-002; CX0351 at 001-002; CX0386 at 001-002; CX0387 at 001-002; CX0388 at 001-002; CX0389 at 001-002; CX0390 at 001-002; CX0391 at 001-002).

222. Three of the cease and desist letters contain a bold, capitalized heading that states: "NOTICE OF APPARENT VIOLATION AND DEMAND TO CEASE AND DESIST." These three letters also state:

The Dental Board hereby demands that you CEASE AND DESIST any and all activity constituting the practice of dentistry as defined by North Carolina General Statutes § 90-29 and the Dental Board Rules promulgated thereunder.

Specifically, G.S. 90-29(b) states that . . . "A person shall be deemed to be practicing dentistry in this State who does, undertakes or attempts to do, or claims the ability to do any one or more of the following acts or things which, for the purposes of this Article, constitute the practice of dentistry:"

"(2) Removes stains, accretions or deposits from the human teeth;"

"(7) Takes or makes an impression of the human teeth, gums or jaws:"

"(10) Performs or engages in any of the clinical practices included in the curricula of recognized dental schools or colleges."

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(CX0153 at 001-002; CX0155 at 001-002; CX0156 at 001-002).

223. The last three cease and desist letters sent in 2009 contained slightly different language than the other cease and desist letters sent in 2009 and in 2008. (CX0153 at 001-002; CX0155 at 001-002; CX0156 at 001-002). These three cease and desist letters were captioned, "NOTICE OF APPARENT VIOLATION AND DEMAND TO CEASE AND DESIST" instead of being captioned "NOTICE AND ORDER TO CEASE AND DESIST." In addition, rather than stating "you are hereby ordered to CEASE AND DESIST any and all activity constituting the practice of dentistry . . . ," these three cease and desist letters stated that the Board "hereby demands that you CEASE AND DESIST any and all activity constituting the practice of dentistry" (CX0153 at 001-002; CX0155 at 001-002; CX0156 at 001-002).

224. All 47 of the cease and desist letters sent to non-dentist teeth whitening service providers or manufacturers were signed by the Board's Deputy Operations Officer Friddle, the Board's Attorney, or the Board's Assistant Director of Investigations. (CX0038-001; CX0042 at 001-002, 005-007, 008-009, 010-011, 012-013, 014-015, 016-017, 018-019, 020-021, 022-023, 024-025, 026-027, 028-029, 030-031, 032-033, 034-035; CX0044 at 004-005; CX0050 at 002- 003; CX0058 at 001-002; CX0059 at 001-002; CX0065 at 001-002; CX0068 at 001-002; CX0069 at 001-002; CX0074 at 001-002; CX0077 at 001-002; CX0079 at 001-002; CX0094 at 005; CX0096 at 001-002; CX0097 at 001-002; CX0100 at 001-002; CX0112 at 001-002; CX0120 at 001-002; CX0122 at 001-002; CX0123 at 001-002; CX0153 at 001-002; CX0155 at 001-002; CX0156 at 001-002; CX0272 at 001-002; CX0279 at 001-002; CX0351 at 001-002; CX0386 at 001-002; CX0387 at 001-002; CX0388 at 001-002; CX0389 at 001-002; CX0390 at 001-002; CX0391 at 001-002).

225. All but 1 of the 47 cease and desist letters sent to non-dentist teeth whitening service providers or manufacturers indicate that the case officer and the Board's Attorney were copied on the letter. (CX0042 at 001-002, 005-007, 008-009, 010-011, 012-013, 014-015, 016-017, 018-019, 020-021, 022-023,

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024-025, 026-027, 028-029, 030-031, 032-033, 034-035; CX0044 at 004-005; CX0050 at 002-003; CX0058 at 001-002; CX0059 at 001-002; CX0065 at 001- 002; CX0068 at 001-002; CX0069 at 001-002; CX0074 at 001-002; CX0077 at 001-002; CX0079 at 001-002; CX0094 at 005; CX0096 at 001-002; CX0097 at 001-002; CX0100 at 001-002; CX0112 at 001-002; CX0120 at 001-002; CX0122 at 001-002; CX0123 at 001-002; CX0153 at 001-002; CX0155 at 001-002; CX0156 at 001-002; CX0272 at 001-002; CX0279 at 001-002; CX0351 at 001-002; CX0386 at 001-002; CX0387 at 001-002; CX0388 at 001-002; CX0389 at 001-002; CX0390 at 001-002; CX0391 at 001-002). Only the very first identified cease and desist letter, sent to Serenity Day Spa in Hendersonville, North Carolina dated January 11, 2006, does not indicate that the case officer and the Board's Attorney were copied on the letter. (CX0038 at 001).

226. Cease and desist letters sent to non-dentist teeth whiteners were formally served either by return receipt mail (CX0042 at 001-002), by sheriff's service, (CX0095), by hand-delivery by a private investigator (CX0094 at 005) or personal service by a Board investigator. (CX0044 at 004-005).

4. Relationship between cease and desist letters and dentist complaints

227. Almost all of the complaints to the Board about non-dentist teeth whitening service providers have come from licensed North Carolina dentists or their employees. (CX0276 at 001; Owens Tr. 1576-1579 (approximately 90% of teeth whitening complaints are from dentists or employees of dentists)).

228. The Board admits that "only three investigations it opened included a report of harm or injury to an individual." (Response to RFA ¶ 22). Two of these stem from consumer complaints and one from a dentist on behalf of his patient. (RX0005 at 002-005; RX0017 at 001-021; RX0021 at 004-007; *see also* RPF 100-237 (listing by case name 28 investigations the Board has taken in response to complaints and including in these proposed findings only 3 investigations based on complaints claiming harm from teeth whitening services by non-dentists)).

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229. At least 47 individual dentists filed complaints with the Board about non-dentist teeth whitening operations. (CX0032 at 001-008; CX0035 at 001-002; CX0036 at 002-018; CX0043 at 001-013; CX0045 at 002-006; CX0054 at 002-006; CX0092 at 001; CX0102 at 001-003; CX0111 at 002-004; CX0198 at 001-002; CX0245 at 001; CX0251 at 001-002; CX0265 at 001; CX0276 at 001-002; CX0278 at 001; CX0281 at 001; CX0282 at 001; CX0293 at 001-002; CX0304 at 001; CX0365 at 001-022; CX0404 at 001-003; CX0411 at 001-004; CX0465 at 001; CX0477 at 003-005; CX0524 at 001-003; CX0619 at 001-002; CX0620 at 001).

230. At least 29 non-dentist teeth whitening providers were sent cease and desist letters by the Board in instances where a North Carolina dentist had filed a complaint with the Board.

Complaints: CX0043 at 001-013 (BleachBright); CX0092 at 001 (Port City Tanning); CX0245 at 001 (Celebrity Smiles); CX0251 at 001-002 (Inspire Skin & Body); CX0198 at 001-002 (Movie Star Smile); CX0276 at 001 (*various*); CX0278 at 001 (BleachBright); CX0281 at 001 (Champagne Taste/Lash Lady); CX0304 at 001-002 (Bailey's Lightning Whitening); CX0365 at 001-002 (Celebrity Smiles); CX0404 at 001-003 (BleachBright); CX0411 at 003 (Whitening on Wheels).

Cease and desist letters: CX0042 at 001-002 (BleachBright/James & Linda Holder); CX0042 at 005-007 (BleachBright/Skin Sense); CX0042 at 008-009 (BleachBright/Electric Beach Pleasant Valley); CX0042 at 010-011 (BleachBright/Exotic Tan); CX0042 at 012-013 (BleachBright/Skin Sense Apex); CX0042 at 014-015 (BleachBright/Cris Scott Hair Studio); CX0042 at 016-017 (BleachBright/Douglas Carroll Salon); CX0042 at 018-019 (BleachBright/Electric Beach Cary); CX0042 at 020-021 (BleachBright/Electric Beach Mission Valley); CX0042 at 022-023 (BleachBright/Electric Beach North Market Drive); CX0042 at 024-025 (BleachBright/Cary Massage Therapy Center); CX0042 at 026-027 (BleachBright/Skin Sense Falls of Neuse Road); CX0042 at 028-029 (BleachBright/Modern Enhancement); CX0042 at 030-031 (BleachBright/Life's Little Pleasures); CX0042 at 032-033 (BleachBright/La Therapie Spa); CX0042 at 034-035 (BleachBright/Electric Beach Six Forks);

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CX0059 at 001-002 (Port City Tanning); CX0077 at 001-002 (Champagne Taste/Lash Lady); CX0079 at 001-002 (Movie Star Smile); CX0112 at 001-002 (BleachBright/Jason & Shanon Rabon); CX0120 at 001-002 (Fantiaticians); CX0153 at 001-002 (Serenity Total Body Care/BleachBright); CX0272 at 001-002 (Inspire Skin & Body); CX0351 at 001-002 (Celebrity Smiles at The Street of Southpoint); CX0386 at 001-002 (Details, Inc); CX0387 at 001-002 (Bailey's Lightning Whitening); CX0389 at 001-002 (Triad Body Secrets); CX0390 at 001-002 (Whitening on Wheels); CX0391 at 001-002 (The Extra Smile, Inc.).

231. With one exception, CX0477, dentists' complaints to the Board about non-dentist teeth whitening do not state that any consumer had been harmed by the procedure. (CX0032 at 001-002; CX0035 at 003; CX0036 at 001-002, 005-006, 007-018; CX0043 at 004-008, 009-010, 011-013; CX0054 at 002-006; CX0092 at 001-002; CX0111 at 001-004; CX0198 at 001-002; CX0245 at 001-002; CX0251 at 001-002; CX0278 at 001; CX0281 at 001; CX0293 at 001-002; CX0304 at 001; CX0365 at 001; CX0404 at 001-003; CX0411 at 001, 003; CX0465 at 001; CX0524 at 001-003; CX0619 at 001-002; CX0620 at 001-002).

232. Many of the dentists' complaints to the Board about non-dentist teeth whitening referenced, or attached advertisements, showing the prices charged by non-dentist teeth whitening service providers. (CX0035 at 003; CX0036 at 001-002, 005-006, 007-018; CX0043 at 004-008, 009-010, 011-013; CX0054 at 002-006; CX0198 at 001-002; CX0619 at 001-002).

233. North Carolina dentists who filed complaints or inquiries that led to Board investigations of the unauthorized practice of dentistry derived income from the provision of teeth whitening services in recent years. The following dentists, whose identities have been shielded from disclosure, were in dental practices that earned the following amounts of income from teeth whitening services from 2005 through 2010: Dentist A (CX0600 at 003; CX0304 at 001) (over \$150,000); Dentist B (CX0599 at 003; CX0524 at 001) (over \$100,000); Dentist C (CX0602 at 002; CX0035 at 001-002) (over \$100,000); Dentist D (CX0603 at 003; CX0092 at 001) (over \$100,000); Dentist E

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(CX0605 at 003; CX0245 at 001) (over \$50,000); Dentist F (CX0616 at 021; CX0043 at 011-013) (over \$50,000); Dentist G (CX0601 at 008; CX0276 at 001) (over \$50,000); Dr. H (CX0608 at 002; CX0276 at 001) (over \$50,000); Dentist I (CX0611 at 002, 004; CX0576 at 007-008 (Dep. at 20-22, 24-25)); (CX0054 at 003) (over \$50,000); Dentist J (CX0617 at 001, 012; CX0111 at 001-006) (over \$50,000); Dentist K (CX0610 at 002; CX0265 at 001) (over \$15,000); Dentist L (CX0607 at 001; CX0276 at 001) (over \$15,000); Dentist M (CX0609 at 001-002; CX0043 at 003-010) (over \$15,000); Dentist N (CX0613 at 004-005; CX0102 at 001-002) (over \$15,000).

5. Meaning and purpose of cease and desist letters

a. Testimony of Board members confirms the intent of the cease and desist letters was to make non-dentists stop providing teeth whitening services

234. Dr. Wester testified that the cease and desist letter was a message to the recipient that "they should stop" or "cease and desist" from engaging in teeth whitening activities. (CX0572 at 016 (Wester, Dep. at 57)).

235. Dr. Allen testified that through a cease and desist letter, the "[B]oard [is] saying that you not only are ordered but you have the responsibility to comply with this order." (CX0554 at 034 (Allen, Dep. at 126-127)).

236. Dr. Allen further testified that a cease and desist letter from the Board is "an order in the same sense that the board as the State's designee to regulate the practice of dentistry and protect the public is – is telling you not to do this anymore I mean, the letter implies that if you continue to do it you'll either be fined or in prison if you continue." (CX0554 at 034 (Allen, Dep. at 127-128)).

237. Dr. Wester testified that he treats a cease and desist letter sent by a case officer as essentially the same thing as an injunction or a court order, because the expected impact of a cease and desist order is that the recipient will stop doing what the

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Board wants them to stop doing. (Wester, Tr. 1337-1338, 1352-1353).

238. Mr. White testified that a cease and desist letter issued by the Board is "ordering [the recipient] either to stop whatever that activity is or to demonstrate why what they're doing is not a violation of the Act." (CX0573 at 007 (White, Dep. 19-20)).

239. Mr. White testified that he understands that in common parlance, "an order is viewed as a command to stop." (CX0573 at 010 (White, Dep. at 31)).

b. Contemporaneous documents of the Board members and staff refer to the cease and desist letters as "orders"

240. Contemporaneous e-mails, letters, and reports drafted by Board members and Board staff confirm that while the documents sent to non-dentist teeth whiteners are sometimes referred to as "letters," they are also referred to by Board members and staff as "Cease and Desist Orders." (E.g., CX0070 at 001; CX0254 at 001; CX0258 at 001-002; CX0347 at 001; CX0404 at 001-002; CX0462 at 003-005; RX0019 at 005; RX0028 at 001).

241. On November 26, 2007, Board Investigator Dempsey wrote in an e-mail to Dr. Owens, Terry Friddle, Carolin Bakewell, Bobby White and Casie Smith Goode, that he "was able to serve the Cease and Desist Order to Ms. Heather York" of Celebrity Smiles. The next day, on November 27, 2007, Ms. Bakewell wrote in an e-mail that the Board "has recently issued Cease and Desist Orders to an out of state company that has been providing bleaching services in a number of malls in the state." (CX0350 at 001; CX0254 at 001).

242. On January 18, 2007, Board Investigator Dempsey wrote that the Amazing Grace Spa was sent "a Cease and Desist Order." (CX0347 at 001).

243. On January 17, 2008, Board Investigator Dempsey wrote in an Investigative Memo regarding a kiosk teeth whitening vendor that "Mr. Cogan explained that . . . he had not officially

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received a Cease & Desist Order. I explained that Mr. Nelson [the President of the company that manufactured Mr. Cogan's teeth whitening products] said that he had, and I was informing him verbally that he needed to cease and desist Before leaving, I explained, once again, that I was a representative of the North Carolina State Board of Dental Examiners and that he was practicing dentistry without a license and that he should cease and desist." (CX0258 at 001-002).

244. On February 20, 2008, Mr. Bobby White wrote in an e-mail in response to a dentist's complaint, "We've sent out numerous Cease and Desist Orders throughout the state." (CX0404 at 001).

245. Board members intended and understood that the cease and desist letters were intended to stop the recipients from providing teeth whitening services. (F. 234-244).

6. Effects of cease and desist letters

246. Some recipients of the cease and desist letters believed that the communication they received was an order from a state agency to stop teeth whitening activities. (F. 247-256).

247. In a letter from Tonya Norwood, received by the Board on February 9, 2009, the owner of Modern Enhancement Salon stated that she would "no longer perform this service as per your order to stop and will no longer perform teeth whitening services unless told otherwise by the North Carolina Board of Dental Examiners." (CX0162 at 001).

248. On March 27, 2007, Ms. Pamela Weaver of the Amazing Grace Spa responded to a cease and desist letter from the Board by stating that she had removed the teeth whitening machine from her salon. (CX0347 at 001; CX0050 at 001).

249. Mr. George Nelson of WhiteScience understood the cease and desist letters sent by the Board as "ordering businesses to close. [The Board] issue[s] a cease and desist and they order [non-dentist teeth whitening operations] to close and not to continue in the teeth whitening business with no other discussion

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or options . . . I personally haven't heard and been advised about any type of permitting or other type of option. I've only heard about ordering the close of the business." (Nelson, Tr. 850).

250. As a result of the Board's cease and desist letter, Triad Body Secret ceased offering teeth whitening services it had previously provided using the WhiteScience product. (Nelson, Tr. 785-786; CX0389 at 001-002).

251. After receiving a cease and desist letter from the Board dated February 8, 2007, the owner of Champagne Taste Salon, also known as "Lash Lady", wrote to the Board stating that "they have now stopped offering [teeth whitening] service[s]." (CX0622 at 003).

252. By February 29, 2008, according to a Memorandum to Members of the Board from Terry Friddle regarding Closed Investigative Files, after receiving a cease and desist letter from the Board, Savage Tan Salon no longer offered teeth whitening services at the location visited by the Board's investigator. (CX0623 at 003-004).

253. Margie Hughes of SheShe Studio Spa stopped offering teeth whitening services to the public after receiving the Board's cease and desist letter. (Hughes, Tr. 943, 946).

254. After receiving a cease and desist letter from the Board dated January 31, 2007, Details, Inc. notified the Board that it had sold its teeth whitening equipment and was no longer providing teeth whitening services. (CX0660 at 003).

255. After receiving a cease and desist letter from the Board dated July 17, 2008, the owner of Bailey's Lightning Whitening wrote to the Board that "due to [the Board's] letter[, she] had disposed of the [teeth whitening] product" and "would not be providing any teeth whitening services at her salon." (CX0658 at 005).

256. The Board's cease and desist letters were effective in causing non-dentists to cease providing teeth whitening services in North Carolina. (F. 247-255; Kwoka, Tr. 1007-1008; RX0078

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at 008 (Respondent's expert stating, "[n]ot surprisingly, the actions of the State Board were effective and many kiosk and spa operators complied with state law by ceasing their actions that were clearly in violation of state law.").

257. When non-dentists ceased providing teeth whitening services in North Carolina, consumers were denied the ability to choose a non-dentist teeth whitening service provider. (Kwoka, Tr. 1136-1137, 1219; CX0654 at 005-006). *See also* CX0826 (Baumer, Dep. at 122-123 ("Yes, there's no doubt that, you know, if you reduce products, other things being equal, that there's a loss in consumer welfare or consumer surplus.")).

7. Board alternatives

258. Bobby White does not believe that the Board's ability to enforce the Dental Practice Act would be impacted if the letters that the Board sent out to non-dentist teeth whitening businesses stated that the Board believes that the recipient violated the law and may take the recipient to court to get an injunction or other relief, instead of stating "you are hereby ordered to cease and desist." (CX0573 at 010 (White, Dep. at 30)).

259. In October 2000, a letter sent to Ortho Depot regarding alleged unauthorized practice of dentistry had no heading stating "Cease and Desist," nor did the body of the letter state "You are hereby ordered to cease and desist." Instead, the Board letter stated "This is to advise you that the North Carolina State Board of Dental Examiners is considering initiating a civil suit to enjoin you from the unlawful practice of dentistry." (CX0136 at 001 (October 3, 2000)).

260. A December 2001 letter notified the recipient that "[i]t has come to the attention of the North Carolina State Board of Dental Examiners that you may be setting up a dental practice in conjunction with the Dowd Central YMCA. This is to advise you that the Board is conducting an inquiry based on this knowledge." This letter neither had a heading stating "Cease and Desist," nor did the body of the letter state "You are hereby ordered to cease and desist." (CX0139 at 001 (December 10, 2001)). When the Board did not receive a response to its letter, it

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sent a follow-up letter, which is similarly void of any "cease and desist" language, and simply reiterates the request for the recipient to respond. (CX0138 at 001 (February 12, 2002)).

F. The Board and Teeth Whitening Manufacturers and Distributors, and Potential Entrants

261. The Board communicated to manufacturers and distributors of teeth whitening products and equipment that the provision of teeth whitening services by non-dentists is, constitutes, or may constitute, the unauthorized practice of dentistry in North Carolina, which is a misdemeanor. (CX0100 at 001; CX0122 at 001; Nelson, Tr. 850; CX0371 at 001; CX0110 at 001; CX0066 at 001).

262. Of the 47 cease and desist letters sent by the Board (F. 219), two were sent to manufacturers of teeth whitening products used by non-dentists. (CX0100 at 001 (WhiteScience); CX0122 at 001-002 (Florida WhiteSmile)).

263. On February 13, 2007, Ms. Bakewell wrote WhiteScience, regarding its present and future sales of non-dentist teeth whitening systems in North Carolina. On behalf of the Board, Ms. Bakewell represented to WhiteScience that those who purchased and provided WhiteScience's systems to the public may be practicing unlicensed dentistry, which is a misdemeanor, and that WhiteScience should "accurately inform current and potential customers of the limitations on the provision of teeth whitening services in North Carolina." (CX0110 at 001).

264. During the August 10 and 11, 2007 Board meeting, the Board discussed an inquiry by Frank Recker, an attorney representing WhiteScience, into whether WhiteScience could market its teeth whitening product to spas and salons operated by non-dentists. The Board's meeting minutes state with respect to WhiteScience's inquiry: "Upon review of the literature, it was determined that the application of bleaching gels or similar materials to human teeth and the use of a light to speed the curing process constituted the practice of dentistry Staff was directed to respond." (CX0106 at 005; CX0206 at 005).

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265. The Board issued a "Notice to Cease and Desist" letter to WhiteScience on December 4, 2007 advising that "assisting clients to accelerate the whitening process with an LED light . . . constitutes the unauthorized practice of dentistry. This is a misdemeanor. The Board hereby directs your company to cease its activities unless they are performed or supervised by a properly licensed North Carolina dentist." The letter was signed by Ms. Bakewell as Board counsel. (CX0100 at 001).

266. George Nelson of WhiteScience understood from the letter he received from the Board, described in F. 265, that the people WhiteScience was selling to in North Carolina would be committing a misdemeanor. (Nelson, Tr. 775; CX0110).

267. Mr. Nelson of WhiteScience understood from his salon operators in North Carolina that the Board was ordering the salons to close their teeth whitening businesses. (Nelson, Tr. 776-777, 786, 789). "They issue a cease and desist and they order them to close and not to continue on the teeth whitening business with no other discussion or options . . . I personally haven't heard and been advised about any type of permitting or other type of option. I've only heard about ordering the closing of the business." (Nelson, Tr. 850).

268. Before being what Mr. Nelson described as "shut down" by the Board, WhiteScience was making close to \$200,000 a year in sales of teeth whitening products in North Carolina. After the Board's actions with respect to WhiteScience, WhiteScience retail sales in North Carolina evaporated to nothing, from over a million dollars yearly. (Nelson, Tr. 734-736.)

269. As a result of WhiteScience's salon clients receiving cease and desist letters from the Board, the salon clients severed their relationships with WhiteScience. (Nelson, Tr. 785-786; CX0389 at 001-002).

270. Pam Helme-dollar, with Savvy Salon and Spa in North Carolina informed WhiteScience that she stopped providing teeth whitening services at her business because she believed that the North Carolina Board of Cosmetic Arts Examiners deemed it unlawful for salons to provide teeth whitening services. She

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offered to give her remaining two whitening systems back to WhiteScience. (Nelson, Tr. 786-787; CX0814 at 001).

271. WhiteSmile first marketed its products and services in North Carolina in the spring of 2007 through a trade show in Raleigh and Charlotte, North Carolina. Jim Valentine, co-founder of WhiteSmile considered these trade show experiences to be very successful. (Valentine, Tr. 561).

272. WhiteSmile chose not to pursue locating within Sam's Clubs in North Carolina in late 2007, even though North Carolina would have been a good market with a large number of Sam's Clubs. This was because both WhiteSmile and Sam's Club were aware of the actions taken by the Board in North Carolina against non-dentist teeth whiteners. (Valentine, Tr. 562-563).

273. WhiteSmile became aware of the Board's position regarding non-dentist teeth whitening through his contacts with potential investors in North Carolina. WhiteSmile learned of the Board's use of cease and desist letters, and counsel for the investors was told by the Board that WhiteSmile's operations would be considered the practice of dentistry, even though providers would not touch their customers' mouths. (Valentine, Tr. 562-564).

274. On October 7, 2008, the Board issued a "Notice and Order to Cease and Desist," to Florida WhiteSmile, Orlando, Florida, stating that it was "investigating a report that you are engaged in the unlicensed practice of dentistry. Practicing dentistry without a license in North Carolina is a crime. . . . You are hereby ordered to CEASE AND DESIST any and all activity constituting the practice of dentistry" (CX0122 at 001-002).

275. When Mr. Valentine contacted the Board to inquire as to whether WhiteSmile could market its self-applied system to non-dentists in North Carolina, the Board advised him that the Board considered WhiteSmile's product and procedures to be the practice of dentistry, which must be performed by a licensed dentist. (Valentine, Tr. 564-567; CX0108; CX0206 at 004-005).

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276. Mr. Valentine's inquiry (F. 275) was discussed in the Board's minutes of its meeting on August 10 and 11, 2007. The minutes state with regard to WhiteSmile: "Upon review of the literature, it was determined that the application of this product constituted the practice of dentistry and must be provided by a licensed dentist Only dentists and properly licensed and supervised auxiliaries may assist in the removal of stains, accretions or deposits from the teeth of other humans. This would include the application of bleaching gels or similar materials to a customer's teeth and using curing lights or similar methods to speed the process." Staff was directed to respond to Mr. Valentine's request. (CX0206 at 004-005; Valentine, Tr. 564-567; *see also* CX0106 at 005).

277. WhiteSmile's negotiations with potential investors in North Carolina fell apart due to the investors' and their attorneys' concerns over whether the Board would allow non-dentist teeth whitening. (Valentine, Tr. 563-564).

278. WhiteSmile eventually entered the North Carolina market in 2009 inside Sam's Clubs, after The News & Observer newspaper reported that North Carolina was going to look at teeth whitening on a case by case basis. This report satisfied Sam's Clubs that WhiteSmile could use their space. (Valentine, Tr. 567; CX0158).

279. WhiteSmile delayed its entry into the North Carolina market as a result of the Board's opposition, described in F. 276. WhiteSmile would have entered the North Carolina market in January 2008 had it not been for the Board's opposition to non-dentist provided teeth whitening services. As a result of the one and one-half year delay in entering the market, WhiteSmile estimates a loss of a one and one-half million dollars. (Valentine, Tr. 567-570).

280. On February 13, 2007, Ms. Bakewell, as counsel to the Board, wrote Enhanced Light Technologies stating that it had come to the attention of the Board that representatives of the firm "have sold and/or attempted to sell teeth whitening systems to non-dental professionals in North Carolina, such as spa and salon owners" and advising that "[i]ndividuals who use your products to

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provide teeth whitening services to the public may be engaging in the unauthorized practice of dentistry, which is a misdemeanor." The letter further stated that Enhanced Light Technologies should "accurately inform current and potential customers of the limitations on the provision of teeth whitening services in North Carolina." (CX0371 at 001).

281. As a result of the Dental Board's actions, including the issuance of cease and desist letters to non-dentist teeth whitening service providers in North Carolina, manufacturers of teeth whitening products used by non-dentist teeth whiteners have lost sales in North Carolina. (Nelson, Tr. 734-736, 774-778, 785-786; CX0814 at 001; CX0389 at 001-002 (WhiteScience); Valentine, Tr. 562-564, 567-570, 575 (WhiteSmile USA); Osborn, Tr. 671-675 (BriteWhite)).

282. Ms. Joyce Osborn of BEKS, Inc., which sells the BriteWhite System, stopped selling her products in North Carolina in 2008, because she was afraid of the risk of getting a cease and desist letter. Ms. Osborn was aware of the Board's cease and desist letters, and that one of her purchasers, Signature Spas, had been sued by the Board and went out of business. (Osborn, Tr. 670-674).

283. BriteWhite products have not been sold in North Carolina since 2008, even though there have been requests for its product from people in North Carolina, and even though Ms. Osborn would like to be selling in North Carolina. (Osborn, Tr. 671-675).

284. In an e-mail dated January 17, 2008, Board counsel Carolin Bakewell informed a non-dentist teeth whitener – in response to the teeth whitener's inquiries into the legality of teeth whitening in North Carolina – that the Dental Practice Act defines the practice of dentistry to include the "removal of stains and accretions." Ms. Bakewell informed the inquiring teeth whitener that his or her whitening business, which provides customers with a personal tray with a whitening solution and use of a whitening light, violated the statute because it was designed to remove stains from human teeth. Ms. Bakewell further told the inquiring teeth

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whitener that the statute is not limited to situations where the non-dentist touches the customer's mouth. (CX0291 at 002-003).

285. On February 12, 2008, Board counsel Carolin Bakewell responded to an e-mail from Craig Francis inquiring about what he needed to do in order to lawfully operate a mall whitening kiosk. Ms. Bakewell informed Mr. Francis he "may not operate a whitening kiosk except under the direct supervision of a licensed North Carolina dentist. The prohibition remains the same even if the customer inserts the whitening tray themselves." (CX0523 at 001).

286. The purpose and effect of the communications described in F. 261-265, 274-276 was to discourage or prevent manufacturers and distributors of teeth whitening products and equipment from providing products and equipment to non-dentist teeth whitening service providers in North Carolina. (F. 266-273, 277-279, 281-283).

287. The purpose of the communications described in F. 284-285 was to dissuade the recipients from entering the teeth whitening market in North Carolina.

G. The Board and Property Owners and Mall Operators

1. Letters to mall operators regarding non-dentist teeth whitening service providers

288. On November 21, 2007, the Board sent 11 nearly identical letters to third parties, including mall management and out-of-state mall property management companies. These letters stated:

The N.C. State Board of Dental Examiners is the agency created by the North Carolina legislature to enforce the dental laws in this state. The Dental Board has learned that an out of state company has leased kiosks in a number of shopping malls in North Carolina for the purpose of offering tooth whitening services to the public.

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North Carolina law specifically provides that the removal of stains from human teeth constitutes the practice of dentistry. See N.C. Gen. Stat. 90-29(b)(2), a copy of which is enclosed. The unauthorized practice of dentistry is a misdemeanor. See N.C. Gen. Stat. 90-40, a copy of which is also enclosed.

It is our information that the teeth whitening services offered at these kiosks are not supervised by a licensed North Carolina dentist. Consequently, this activity is illegal.

The Dental Board would be most grateful if your company would assist us in ensuring that the property owned or managed by your company is not being used for improper activity that could create a risk to the public health and safety.

(CX0203 at 001; CX0204 at 001-002; CX0205 at 001-002; CX0259 at 001-002; CX0260 at 001-002; CX0261 at 001-002; CX0262 at 001-002; CX0263 at 001-002; CX0323 at 001-002; CX0324 at 001-002; CX0325 at 001-002; CX0326 at 001-002; (Joint Stipulations of Law and Fact ¶ 31; CX0560 at 051 (Feingold, Dep. at 195-196)).

289. The Board members unanimously approved sending the November 21, 2007 letters to mall operators described in F. 288. (Hardesty, Tr. 2864; CX0565 at 054-055 (Hardesty, Dep. at 206-208, 210)).

290. It was the Board's intention to send "quite a number" of letters to mall operators warning them that kiosk teeth whiteners were violating the Dental Practice Act by offering teeth whitening services. (CX0565 at 055 (Hardesty, Dep. at 210); CX0203 at 001).

291. In separate letters, dated January 23, 2008, Board counsel Carolin Bakewell informed Dr. Kyle Taylor and Dr. Michael Catanese – dentists who each had alerted the Board of a teeth whitening kiosk in Carolina Place Mall – of the actions that the Board had taken in regard to teeth whitening kiosks in Carolina Place Mall. Ms. Bakewell enclosed in each letter a copy of the November 21, 2007 letter that the Board had sent to General Growth Properties – the company that owned Carolina

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Place Mall – informing them that the Board viewed the teeth whitening services being performed in Carolina Place Mall to be illegal. (CX0102 at 001-003; CX0524 at 001-003).

292. The purpose of the November 21, 2007 letter sent by the Board to mall operators (F. 288) was to induce the malls to refuse to rent space to non-dentist teeth whiteners, because they were "breaking the law." (CX0560 at 052 (Feingold, Dep. at 199-200); *see also* CX0581 at 067-071 (Bakewell, Dep. at 262-263 (one purpose was to let mall operators know that non-dentist teeth whiteners were breaking the law, and if the Board took action against the kiosk owner, the kiosk owner might leave the mall and lessor would be left with a bad lease))).

293. The Board sent the letters to malls and mall property management groups in response to the complaints the Board had received and "in hopes of trying to prevent further expansion" of non-dentist teeth whitening kiosks in malls. (CX0562 at 019-020 (Friddle, IHT at 71-72, 75-76 ("So not to have them there"))).

2. Effects of the letters to mall operators

294. As a result of the Board's November 21, 2007 letters to malls, mall companies, and mall management companies, (F. 288) mall operators were reluctant to lease space to non-dentist teeth whitening service providers in North Carolina and some companies refused to lease space and cancelled existing leases. (Wyant, Tr. 876-884; Gibson, Tr. 627-628, 632-633; CX0255 at 001; CX0525 at 001; CX0629 at 001-002; CX0647 at 002). *See also* RX0078 at 008 (Respondent's expert stating, "Mall operators cooperated [with the Board's actions to enforce state law] by refusing to renew leases or rent to operators of teeth whitening services.").

a. Hull Storey Gibson Companies

295. John Gibson is a partner and Chief Operating Officer ("COO") of Hull Storey Gibson Companies, L.L.C. ("HSG"). HSG is a retail property management company that owns 11.5 million square feet of retail space in seven states, including North

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Carolina. Mr. Gibson became the COO of HSG in 1999. (Gibson, Tr. 613, 615).

296. Cathy Mosley is the Specialty Leasing Manager and Leasing Representative of HSG. She reports to Mr. Gibson indirectly through the Vice President for Leasing. Because Mr. Gibson signs all the leases, he has frequent direct contact with Ms. Mosley. (Gibson, Tr. 616).

297. HSG operates five malls in North Carolina, including the Blue Ridge Mall in Hendersonville, North Carolina; the Cleveland Mall in Shelby, North Carolina; the Carolina Mall in Concord, North Carolina; the New Bern Mall in New Bern, North Carolina; and the Wilson Mall in Wilson, North Carolina. (Gibson, Tr. 613-614).

298. HSG held a non-dentist teeth whitening event at its Lake City Mall. (Gibson, Tr. 625).

299. HSG's Blue Ridge Mall received a letter dated November 21, 2007, "Re: Tooth Whitening Kiosks," that was brought to Mr. Gibson's attention by Ms. Mosley. HSG's Cleveland Mall received a virtually identical letter. (Gibson, Tr. 626-627; CX0203 at 001-002; CX0259 at 001-002).

300. The content of the November 21, 2007 letters received by HSG is set forth in F. 288.

301. Mr. Gibson understood from these letters that the Board took the position that the person operating the kiosks and providing non-dentist teeth whitening services would be violating North Carolina law. (Gibson, Tr. 629; CX0203 at 001-002; CX0259 at 001-002).

302. On March 21, 2008, Lisa Schaak of HSG sent an e-mail to Ms. Mosley indicating that Mr. Craig of BleachBright of Carolina wanted to talk to her about space for teeth whitening. On March 21, 2008, Ms. Mosley replied to Ms. Schaak stating "Mr. Craig will need to provide us with proof that the Board of Dental Examiners will approve this. I have had feedback from several Developers letting me know that this use is illegal in

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several states and that their operations have been shut down in their malls." (CX0255 at 001-002).

303. Ms. Mosley brought the mall letter (F. 288; CX0203 at 001-002) to Mr. Gibson's attention because she had been told that a prospective kiosk tenant insisted that the Board had approved its teeth whitening procedure. (Gibson, Tr. 627-631; CX0525 at 001).

304. On March 21, 2008, Ms. Mosley e-mailed Ms. Bakewell to confirm representations that she had received from BleachBright of Carolina to the effect that its teeth bleaching process had been approved by the Board. (Gibson, Tr. 629-631; CX0525 at 001).

305. Ms. Bakewell's March 24, 2008 response told Ms. Mosley that the Board had not issued an approval for the operation of teeth whitening kiosks by BleachBright. (CX0525 at 001; Gibson, Tr. 631-632).

306. HSG would have leased retail space to non-dentist teeth whiteners in North Carolina had they not received the Board's letter to the mall operators and Ms. Bakewell's e-mail to Ms. Mosley. (Gibson, Tr. 622-623, 632-633).

307. HSG would be willing to rent in-line or specialty space in its North Carolina malls today, if the Board withdrew its letters to HSG. (Gibson, Tr. 624).

308. HSG has continued to receive inquiries from non-dentist teeth whiteners, but it has declined to consider leasing space to them. (Gibson, Tr. 633).

b. General Growth Properties and Simon Group Properties

309. On December 7, 2007, Angela Wyant signed a license agreement to rent kiosk space for Brian Wyant's business, a non-dental teeth whitening service using the WhiteScience system, in Carolina Place Mall with General Growth Properties, owner of the mall. (Wyant, Tr. 871-872, 875-876; CX0665; CX0668).

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310. In late January 2008, General Growth Properties' leasing agent informed Mr. Wyant that his month-to-month licensing agreement would not be renewed and that his teeth whitening business would have to leave Carolina Place Mall by February 1, 2008. Mr. Wyant was told that the North Carolina State Board of Dental Examiners had sent a letter stating that the business was the illegal practice of dentistry. In a subsequent meeting with Carolina Place Mall General Manager Michael Payton, Mr. Wyant was shown the Board's letter to General Growth Properties and was told that General Growth Properties' legal team had advised them not to allow Mr. Wyant to stay in business at the mall. (Wyant, Tr. 876- 880, 884; CX0260; CX0629).

311. On January 28, 2008, Mr. Wyant called Concord Mills Mall in Concord, North Carolina, a Simon Group Properties Mall, to inquire about the possibility of locating his business there. Mr. Wyant was told by Ms. Christy Sparks that the Concord Mills Mall would not rent to non-dentist teeth whiteners due to the North Carolina State Board of Dental Examiners' letter (F. 288). Mr. Wyant also contacted SouthPark Mall, another Simon mall, about relocating his business there, and was advised by Ada Nosowicz that moving to a Simon mall was not an option. (Wyant, Tr. 881-884; CX0629).

c. Southpoint Mall

312. On February 11, 2008, Craig Francis e-mailed Bobby White at the Board inquiring about what approvals he would need from the Board to lawfully open up a teeth whitening kiosk. Mr. Francis was intending to sell the BleachBright teeth whitening system. He stated he was seeking information from the Board because the leasing office at Southpoint Mall "mentioned something about the board and the laws associated with the kiosk." (CX0542 at 001). See F. 285 for the Board's response.

313. In an e-mail dated February 13, 2008, Alissa Neal told Board investigator Line Dempsey that she wanted to talk to him "about the teeth whitening businesses that are growing in malls and salons in our area." Ms. Neal related that she had spoken to

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The Streets at Southpoint Mall, which had informed her that the previous teeth whitening business at that location had been "shut down very quickly" and she wanted to know why that business had been ordered to leave. (CX0354 at 001).

H. The Board⁹ and the North Carolina Board of Cosmetic Art Examiners

314. Dr. Hardesty came to the realization that many of the non-dentist teeth whitening complaints were against salons and spas regulated by the North Carolina Board of Cosmetic Art Examiners ("Cosmetology Board"). (CX0565 at 060, 062 (Hardesty, Dep. at 233, 238)).

315. Dr. Hardesty believed that because a lot of the non-dentist teeth whitening providers were licensees of the Cosmetology Board, it was logical that the Cosmetology Board might be willing to assist the Board in its efforts regarding non-dentist teeth whitening services. (CX0565 at 060-061 (Hardesty, Dep. at 231-233, 236)).

316. Dr. Hardesty instructed Board counsel Carolin Bakewell to prepare an article for the Cosmetology Board to post regarding teeth whitening after discussing the issue with the other Board members at a Board meeting. (Hardesty, Tr. 2861-2862).

317. At the next Board meeting after Dr. Hardesty's realization referred in F. 315, Dr. Hardesty asked to go into closed session, and the Board had a general discussion regarding enlisting the assistance of the Cosmetology Board by allowing the Board to publish a letter to them. The Board, upon motion, formally approved the idea of having Ms. Bakewell write a letter to the Cosmetology Board. (CX0565 at 062 (Hardesty, Dep. at 238-240)).

318. At the Board's February 2007 meeting, the Board discussed the increase in complaints involving spas that are offering teeth whitening procedures. The Board also discussed

⁹ As defined in F. 1, "the Board" refers to the North Carolina State Board and not the Cosmetology Board.

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advising the Cosmetology Board to let their licensees know that they should not engage in any unlawful teeth whitening procedures. (CX0566 at 030 (Hardesty, IHT at 115-116); CX0056 at 005).

319. In February 2007, Ms. Bakewell forwarded a draft article for the Cosmetology Board's newsletter. The text of the draft would have been reviewed by at least Mr. Bobby White before it was sent out. (CX0067 at 001, 003; CX0581 at 079-081 (Bakewell, Dep. at 308-310, 311-316)).

320. In February 2007, the Board contacted the Cosmetology Board about the subject of non-dentist teeth whitening services and approved providing the Cosmetology Board with a notice that, consistent with the draft forwarded by Ms. Bakewell, stated:

Cosmetologists should be aware that any device or process that "removes stains, accretions or deposits from the human teeth" constitutes the practice of dentistry as defined by North Carolina General Statutes 90-29(b)(2). Taking impressions for bleaching trays also constitutes the practice of dentistry as defined by North Carolina General Statutes 90-29(b)(7).

Only a licensed dentist or dental hygienist acting under the supervision of a licensed dentist may provide these services. The unlicensed practice of dentistry in our state is a misdemeanor.

(Joint Stipulations of Law and Fact ¶ 33; CX0067 at 001, 003; CX0565 at 060 (Hardesty, Dep. at 231-232)).

321. The Board approved sending the letter to the Cosmetology Board regarding unlicensed teeth whitening by consensus after a five minute discussion with Board counsel. (CX0565 at 062 (Hardesty, Dep. at 238-240)).

322. In February 2007, the Cosmetology Board posted the Dental Board's notice on the Cosmetology Board's website. (Hughes, Tr. 940-941).

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323. The purpose of the notice referred to in F. 320, posted on the Cosmetology Board's website, was to encourage the Cosmetology Board's licensees to cease providing teeth whitening services. (F. 314-321).

324. In March 2007, a cosmetologist advised the Board that they had ceased providing teeth whitening services, after learning from the Cosmetology Board on February 15, 2007 that it was not legal to do so. (CX0050 at 001 (letter from Ms. Pamela Weaver, dated March 27, 2007: "I found out . . . that it was not legal to use [a teeth whitening machine] from the state board of cosmetology and immediately removed it from the salon where I rent and have not used it since that time"); CX0347 (January 16, 2008 e-mail from Mr. Dempsey to Board members confirming that he made an on-site visit to confirm that Ms. Weaver no longer offered teeth whitening services)).

325. Other Cosmetology Board licensees also saw the statement against non-dentists performing teeth whitening services on the Cosmetology Board's website. (Hughes Tr. 940-943).

326. In an e-mail dated August 31, 2010, Pat Helmandollar notified WhiteScience that her salon "will no longer be doing teeth whitening in our salon/spa as the North Carolina board of cosmetic arts has deemed it unlawful to perform this service in a salon." (CX0814; Nelson, Tr. 786-787).

327. A direct result of the Board's actions with respect to the Cosmetology Board was to cause non-dentists to stop providing teeth whitening services. (F. 324-326; Hughes Tr. 941-943).

III. ANALYSIS

Complaint Counsel asserts that dentists and non-dentists compete with one another in the teeth whitening market. CCB at 70. Complaint Counsel states that salons, spas, and kiosks in shopping malls ("non-dentist providers") offer teeth whitening services to consumers, as do dentists, and that non-dentist teeth whitening services are a less costly alternative to going to a

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dentist to have one's teeth whitened quickly and efficiently. CCB at 70. Complaint Counsel argues that because the Board is a combination of competitors, its concerted actions to prevent non-dentists from offering teeth whitening services constitute an unreasonable restraint of trade. CCB at 72-74. Complaint Counsel further contends that the Board embarked upon a campaign to exclude non-dentist teeth whitening service providers from the market, using a variety of methods, including issuing cease and desist orders to non-dentist providers; issuing cease and desist orders to manufacturers of products and equipment used by non-dentist providers; dissuading mall owners from leasing to non-dentist providers; dissuading potential entrants from starting non-dentist teeth whitening businesses; and enlisting the North Carolina Board of Cosmetic Art Examiners also to discourage non-dentist providers. Complaint ¶¶ 20-22; CCB at 70 (hereafter referred to collectively, as the "challenged conduct"). Complaint Counsel further asserts that this conduct was likely to, and did in fact, result in anticompetitive effects, and that there is no procompetitive justification for the Board's conduct. CCB at 89-102. Therefore, Complaint Counsel concludes, the Board's conduct constitutes a combination, contract or conspiracy in restraint of trade, in violation of Section 5 of the Federal Trade Commission ("FTC") Act. As a remedy, Complaint Counsel requests an order enjoining Respondent from ordering non-dentists to discontinue providing teeth whitening goods and services, and from engaging in other conduct and communications to prevent or discourage non-dentists from providing teeth whitening services, and teeth whitening goods provided in conjunction with those services.

The North Carolina Dental Practice Act, N.C. Gen. Stat. § 90-22, *et seq.* ("Dental Practice Act") provides that certain activities, including "remov[ing] stains, accretions or deposits from human teeth," constitute the practice of dentistry, and must be performed or supervised by a licensed dentist. N.C. Gen. Stat. § 90-29(b); F. 41-42. Respondent asserts that the provision of teeth whitening services by non-dentists equates to the "remov[al of] stains, accretions or deposits from human teeth," and thereby constitutes the illegal practice of dentistry without a license. RB at 9, 28-29. According to Respondent, the Board was therefore authorized, as an agent of the state enforcing the Dental Practice

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Act, to take steps to prevent non-dentists from providing teeth whitening services. RB at 3. Accordingly, Respondent argues, because the Board was acting in the public interest, as an agent of the state enforcing the Dental Practice Act, its conduct cannot be deemed unlawful under the rule of reason. RB at 9-11; *see also* RRB at 28-30, 37-43. In addition, Respondent argues that its actions were intended to promote social welfare, by ensuring that teeth whitening services are supervised by licensed dentists and by protecting consumers from dangerous or unsafe teeth whitening services. RB at 1, 12-14. Further, Respondent argues that the restraints on non-dentist teeth whitening providers are procompetitive because they will serve to "protect legal competition within the marketplace," RB at 1; "promote competition between qualified, legal teeth whitening service providers," RB at 13; and will ensure that teeth whitening services are offered at a cost that reflects the higher skills of dentist providers, rather than at the lower cost alternative offered by assertedly lesser skilled, non-dentist teeth whitening service providers. RRB at 6, 12.

Before evaluating whether the conduct challenged in the Complaint is a violation of the FTC Act, the jurisdiction of the Commission must first be established. (Section III.A). The Initial Decision next provides an overview of the applicable legal standards for cases brought under Section 5 of the FTC Act. (Section III.B). Then, the analysis turns to a determination of the relevant market in which to evaluate the challenged conduct (Section III.C) and whether the challenged conduct constitutes "concerted action." (Section III.D). The analysis then examines whether the challenged conduct constitutes an unreasonable restraint of trade (Section III.E) and analyzes Respondent's proffered procompetitive justifications and defenses. (Section III.F). Finally, the nature and extent of an appropriate remedy is addressed. (Section III.G).

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A. Jurisdiction

1. The Board is a "person" within the meaning of the FTC Act

The Complaint charges Respondent with violating Section 5 of the FTC Act. Section 5(a)(2) of the FTC Act gives the Commission jurisdiction "to prevent persons, partnerships, or corporations . . . from using unfair methods of competition in or affecting commerce" 15 U.S.C. § 45(a)(2); *Kaiser Aluminum & Chem. Corp. v. FTC*, 652 F.2d 1324, 1327 n.2 (7th Cir. 1981). Complaint Counsel asserts that the Board is a "person" within the meaning of Section 5 of the FTC Act. CCF 404. Respondent, at this stage of the proceeding, does not dispute that it is a "person" within the meaning of Section 5 of the FTC Act.

The Commission, in its decision denying Respondent's Motion to Dismiss, rejected the Board's argument that it was not subject to the Commission's jurisdiction and held that the Commission has many times exercised jurisdiction over state boards as "persons" under the FTC Act. *In re North Carolina Board of Dental Examiners*, Docket 9343, 2011 WL 549449, at *5 (Feb. 8, 2011) (hereinafter "State Action Opinion") (citing *Va. Bd. of Funeral Dirs. & Embalmers*, 138 F.T.C. 645 (2004); *In re South Carolina State Bd. of Dentistry*, 138 F.T.C. 229 (2004); *In re Mass. Board of Registration in Optometry*, 110 F.T.C. 549, 1988 FTC LEXIS 34 (1988)). In *Mass. Board*, the Commission reasoned that because the Supreme Court had held local governments, as agents of the state, to be persons within the meaning of the Sherman Act and the Clayton Act, they should also be considered persons under the FTC Act and concluded that a state board is a "person" for purposes of jurisdiction under the FTC Act. 1988 FTC LEXIS 34, at *25. Consistent with this precedent, Respondent is a "person" within the meaning of Section 5 of the FTC Act.

2. The Board's acts are in or affecting commerce

To establish jurisdiction, Complaint Counsel must also demonstrate that the acts of Respondent are in or affect

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commerce. 15 U.S.C. § 45(a)(1) (prohibiting unfair methods of competition "in or affecting commerce"); *McLain v. Real Estate Board*, 444 U.S. 232, 242 (1980). The Commission utilizes cases interpreting jurisdiction under the Sherman Act in analyzing its jurisdiction under Section 5 of the FTC Act. *In re North Texas Specialty Physicians*, 140 F.T.C. 715, 726-27 & n.9 (2005). Such approach was upheld in *North Texas Specialty Physicians v. FTC*, 528 F.3d 346, 354-55 (5th Cir. 2008).

"The Supreme Court on numerous occasions has emphasized the breadth of federal antitrust jurisdiction, even when wholly intrastate conduct of local actors is challenged." *In re North Texas Specialty Physicians*, 140 F.T.C. at 727 (citing *Summit Health, Ltd. v. Pinhas*, 500 U.S. 322, 328-31 (1991); *McLain v. Real Estate Bd. of New Orleans, Inc.*, 444 U.S. 232, 241 (1980); *Hosp. Bldg. Co. v. Trs. of Rex Hosp.*, 425 U.S. 738, 743-45 (1976); *Goldfarb v. Virginia State Bar*, 421 U.S. 773, 784-85 (1975)). "Wholly local business restraints can produce the effects condemned by the Sherman Act." *Rex Hosp.*, 425 U.S. at 743 (citation omitted). Indeed, the jurisdictional reach of the Sherman Act (and, thus, the FTC Act), "is coextensive with the broad-ranging power of Congress under the Commerce Clause." *Chatham Condo. Ass'n v. Century Village, Inc.*, 597 F.2d 1002, 1007 (5th Cir. 1979) (citing *Burke v. Ford*, 389 U.S. 320, 321-22 (1967) ("When competition is reduced, prices increase and unit sales decrease Thus, the state-wide wholesalers' market division inevitably affected interstate commerce.")).

Purchases by a defendant of out-of-state goods are a factor in evaluating whether an activity substantially affects interstate commerce. *E.g.*, *Rex Hosp.*, 425 U.S. at 744 (petitioner's purchases of out-of-state medicines and supplies considered in determining "substantial effect" on interstate commerce); *Miller v. Indiana Hosp.*, 843 F.2d 139, 144 n.5 (3rd Cir. 1988) (defendant hospital's treatment of out-of-state patients, purchase of medical supplies from out-of-state, and receipt of money from out-of-state, including federal funds, satisfies the requirement of affecting interstate commerce); *Oksanen v. Page Mem. Hosp.*, 945 F.2d 696, 702 (4th Cir. 1991) (same). *See also United States v. Robertson*, 514 U.S. 669, 672 (1995) ("[A] corporation is generally 'engaged "in commerce"' when it is itself 'directly

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engaged in the production, distribution, or acquisition of goods or services in interstate commerce.'") (per curiam) (quoting *United States v. Am. Bldg. Maint. Indust.*, 422 U.S. 271, 283 (1975)).

The Supreme Court has explained with regard to jurisdiction under the Sherman Act that the plaintiff "need not allege, or prove, an actual effect on interstate commerce to support federal jurisdiction." *Summit Health*, 500 U.S. at 330 (citations omitted).

"Nor is jurisdiction defeated in a case relying on anticompetitive effects by plaintiff's failure to quantify the adverse impact of defendant's conduct." *McLain*, 444 U.S. at 243.

The evidence in this case establishes that manufacturers of teeth whitening equipment and products used by dentist and non-dentist teeth whiteners are located outside the State of North Carolina. F. 88-92. Dentist and non-dentist teeth whiteners in North Carolina use instrumentalities of interstate commerce and communication in the conduct of their businesses, including without limitation, the telephone and the internet to communicate with manufacturers of teeth whitening equipment and products located outside the State of North Carolina. F. 93. Dentist and non-dentist teeth whiteners in North Carolina purchase and receive products and equipment that are shipped across state lines by manufacturers and suppliers located outside the State of North Carolina. F. 94. Dentist and non-dentist teeth whiteners in the State of North Carolina transfer money and other instruments of payment across state lines to pay for teeth whitening equipment and products received from manufacturers located outside the State of North Carolina. F. 95.

In addition, the Board sent at least 40 letters to non-dentist teeth whiteners in North Carolina ordering them to cease and desist from providing teeth whitening services (discussed *infra* Section III.E.2) and some recipients of these letters sent copies of those letters to their out-of-state suppliers of products, equipment, or facilities. F. 96. The Board also sent at least 11 letters to third parties, including out-of-state property management companies (discussed *infra* Section III E.2) which impacted some of those recipients' decisions whether to rent to non-dentist teeth whitening service providers in North Carolina. F. 97-98. Two of the cease and desist letters were sent to out-of-state

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manufactures of teeth whitening products used by non-dentist teeth whiteners in North Carolina. F. 99.

Respondent argues that jurisdiction does not exist because the interstate commerce allegedly affected is the "illegal" interstate commerce of non-dentist teeth whitening. RB at 15. Respondent cites no authority for this argument. Moreover, the argument assumes that non-dentist teeth whitening has been held illegal, although Respondent cites no case that has interpreted the North Carolina Dental Practice Act in this way. Accordingly, Respondent's jurisdiction argument is without merit.

Under the broad jurisdictional scope of "a substantial effect on interstate commerce," the activities of Respondent are in or affect commerce. Thus, the Commission has jurisdiction over the Board, and the conduct challenged in the Complaint, under Sections 4 and 5 of the FTC Act. 15 U.S.C. §§ 44, 45.

B. Overview of Applicable Legal Standards

The FTC Act's prohibition of unfair methods of competition encompasses violations of Section 1 of the Sherman Act. *See, e.g., Cal. Dental Ass'n v. FTC*, 526 U.S. 756, 762 & n.3 (1999); *FTC v. Cement Inst.*, 333 U.S. 683, 694 (1948). "[T]he analysis under § 5 of the FTC Act is the same . . . as it would be under § 1 of the Sherman Act." *Polygram Holding, Inc. v. FTC*, 416 F.3d 29, 32 (D.C. Cir. 2005); *see also FTC v. Indiana Fed'n of Dentists*, 476 U.S. 447, 451-52 (1986). Accordingly, it is appropriate to rely upon Sherman Act jurisprudence in determining whether the challenged conduct violated Section 5 of the FTC Act. *Cal. Dental Ass'n*, 526 U.S. at 762 n.3; *see Indiana Federation*, 476 U.S. at 454-55 (noting that the same analysis applies to both violations of Section 1 of the Sherman Act and Section 5 of the FTC Act); *Realcomp II, Ltd. v. FTC*, 635 F.3d 815, 824 (6th Cir. 2011) (same).

Section 1 of the Sherman Act prohibits "every contract, combination in the form of trust or otherwise, or conspiracy, in restraint of trade or commerce among the several States . . ." 15 U.S.C. § 1. Despite its broad language, the ban on contracts in restraint of trade extends only to unreasonable restraints of trade,

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i.e., restraints that impair competition. *State Oil Co. v. Khan*, 522 U.S. 3, 10 (1997). Thus, a Section 1 violation requires a determination of "(1) whether there was a contract, combination, or conspiracy -- or, more simply, an agreement; and, if so, (2) whether the contract, combination, or conspiracy 'unreasonably restrained trade in the relevant market.'" *Realcomp*, 635 F.2d at 824 (citations omitted); *Law v. NCAA*, 134 F.3d 1010, 1016 (10th Cir. 1998).

The analysis, thus, turns first to a determination of the relevant market that the challenged conduct is alleged to have affected. Next, whether there was a contract, combination or conspiracy is evaluated. Following that determination is an evaluation of whether the restraint unreasonably restrained trade and, then, an evaluation of the procompetitive justifications offered by Respondent.

C. Relevant Market

1. Framework

An antitrust violation requires proof that defendants (1) participated in an agreement that (2) unreasonably restrained trade in the relevant market. *Wampler v. Southwestern Bell Tel. Co.*, 597 F.3d 741, 744 (5th Cir. 2010); *NHL Players' Ass'n v. Plymouth Whalers Hockey Club*, 325 F.3d 712, 718-19 (6th Cir. 2003). "The first step in this analysis is determining the relevant market, which itself is a function of the relevant product market and the relevant geographic market." *Wampler*, 597 F.3d at 744.

The Complaint alleges that "the relevant market in which to evaluate the conduct of the Dental Board is the provision of teeth whitening services in North Carolina" and that "[t]eeth whitening services are offered by dentists and non-dentists." Complaint ¶ 7. The Complaint does not include in the relevant market "[t]eeth whitening products (such as toothpaste and OTC whitening strips)." Complaint ¶ 12.

Respondent argues that Complaint Counsel failed to establish the relevant market because "the teeth whitening market should include over-the-counter products – which are not regulated by

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the State Board – and should exclude illegal non-dentist provided services." RB at 16.

In its Reply Brief, Complaint Counsel asserts "market definition is not a prerequisite to establishing liability under the rule of reason." CCRB at 10. This assertion is contrary to established law. *E.g.*, *Ark. Carpenters Health & Welfare Fund v. Bayer AG (In re Ciprofloxacin Hydrochloride Antitrust Litig.)*, 544 F.3d 1323, 1331-32 (Fed. Cir. 2008) (The first step in rule of reason analysis is for plaintiff to show that the challenged action has had an actual adverse effect on competition as a whole in the relevant market.); *Geneva Pharms. Tech. Corp. v. Barr Labs., Inc.*, 386 F.3d 485, 506-07 (2d Cir. 2004) ("Under the rule of reason, the plaintiffs bear an initial burden to demonstrate the defendants' challenged behavior 'had an actual adverse effect on competition as a whole in the relevant market.'"); *Worldwide Basketball & Sport Tours, Inc. v. NCAA*, 388 F.3d 955, 959 (6th Cir. 2004) ("Under the rule of reason analysis, the plaintiff bears the burden of establishing that the conduct complained of 'produces significant anticompetitive effects within the relevant product and geographic markets.'). Although in some circumstances no "elaborate industry analysis" is necessary to find an unreasonable restraint of trade (see discussion *infra* Section III.E.1 on legal framework; *Cal. Dental Ass'n*, 526 U.S. at 770), the market in which competition has been allegedly affected must nevertheless be defined. *See Queen City Pizza, Inc. v. Domino's Pizza, Inc.*, 124 F.3d 430, 436 (3d Cir. 1997) (affirming dismissal of complaint for failure to sufficiently allege relevant market, stating "[p]laintiffs have the burden of defining the relevant market").

The relevant market has two components, a geographic market and a product market. *H.J., Inc. v. Int'l Tel. & Tel.*, 867 F.2d 1531, 1537 (8th Cir. 1989). The relevant geographic market is the region "in which the seller operates, and to which the purchaser can practicably turn for supplies." *Tampa Elec. Co. v. Nashville Coal Co.*, 365 U.S. 320, 327 (1961). That North Carolina is the relevant geographic market in which to assess the challenged conduct is not disputed. *See* RB at 15-19.

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The relevant product or service market is "composed of products [or services] that have reasonable interchangeability for the purposes for which they are produced – price, use and qualities considered." *United States v. E.I. du Pont de Nemours & Co.*, 351 U.S. 377, 404 (1956); *Eastman Kodak Co. v. Image Technical Services, Inc.*, 504 U.S. 451, 481-82 (1992) (noting that relevant market is determined by the choices of products or services available to consumers). Relying on *du Pont*, courts have found the "reasonable interchangeability" standard to be the essential test for ascertaining the relevant product market. *Worldwide Basketball & Sport Tours*, 388 F.3d at 961; *Hornsby Oil Co. v. Champion Spark Plug Co.*, 714 F.2d 1384, 1393 (5th Cir. 1983). "Reasonable interchangeability 'may be gauged by (1) the product uses, i.e., whether the substitute products or services can perform the same function, and/or (2) consumer response (cross-elasticity); that is, consumer sensitivity to price levels at which they elect substitutes for the defendant's product or service.'" *Worldwide Basketball & Sport Tours*, 388 F.3d at 961 (citation omitted).

The evidence shows that there are four methods of teeth whitening, but that only dentist provided teeth whitening services and non-dentist teeth whitening services are reasonably interchangeable. Before discussing the four methods and their interchangeability, a brief overview of teeth whitening is provided below.

2. Overview of the methods for teeth whitening

There are three methods of whitening teeth: (1) the use of aesthetic or prosthetic dental restorations, such as crowns, caps or veneers; (2) dental stain removal, either through the application of toothpaste or by going to the dentist to have stains scraped off, including by the use of rotary instruments to polish teeth; and (3) bleaching, using peroxide-containing gels or serums that are applied to the teeth using a variety of delivery systems. F. 100. The challenged conduct in this case relates only to the third method of whitening, the use of peroxide-containing gels or serums. F. 100. The terms bleaching and whitening are used synonymously in this opinion.

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Regarding whitening through the use of peroxide containing gels or serums, four methods are or were available in North Carolina: (1) dentist in-office teeth whitening services; (2) dentist provided take-home teeth whitening products; (3) over-the-counter ("OTC") teeth whitening products; and (4) non-dentist teeth whitening services in salons, retail stores, and mall kiosks. F. 105. Each of these methods uses some form of peroxide, either hydrogen peroxide or carbamide peroxide, and each involves application of that chemical in gel or strip form directly onto the teeth. F. 106. These four alternatives for obtaining teeth whitening differ in ways that are important to consumers, including immediacy of results, ease of use, provider support, and price, and are discussed below. F. 107.

Dentists began offering an in-office process of bleaching living teeth in the early 1990s. F. 101. This in-office process, also known as dental chairside bleaching, uses highly concentrated hydrogen peroxide (25% to 35%). F. 109. Around 2001, Proctor & Gamble introduced Crest White Strips: clear, thin, flexible pieces of plastic (polyethylene) that are coated on one side with a thin film of a low level of hydrogen peroxide bleaching agent. F. 131. This and similar products can be purchased by consumers over-the-counter ("OTC") and are self-applied by the consumer, but, as discussed below, do not achieve teeth whitening results quickly. F. 131-32, 135.

Beginning around 2003, non-dentists began offering teeth whitening services, operating primarily in beauty salons, spas, warehouse clubs, fitness centers and kiosks at malls. F. 137-38. These non-dental providers of teeth whitening services use concentrations typically equivalent to 16% or less of hydrogen peroxide. F. 140. As further explained below, teeth whitening services provided by non-dentists achieve teeth whitening results in one visit, and, in this way, are similar to the teeth whitening services provided by dentists. F. 146, 150.

a. Dentist in-office teeth whitening services

Dentists in North Carolina provide teeth whitening services. F. 108. Dentist provided services typically use highly concentrated hydrogen peroxide, applied multiple times during a

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single office visit. F. 109. Dentists use protective barriers to prevent the gums from burning, paint the peroxide solution onto the teeth, and often use a curing light to activate the bleaching gel or expedite the process. F. 111-12. Dentist in-office teeth whitening provides results in one to three hours. F. 111. This service ranges widely in price, often costing between \$400 and \$700. F. 117-18. The principal benefits of dentist in-office teeth whitening services are that it is applied by a professional dentist, after an examination and determination that it is medically appropriate, and that it is quick and effective, providing immediate results in one visit to the dentist. F. 119. The disadvantages to dentist in-office teeth whitening are that it is relatively expensive compared to the alternatives, and it requires making an appointment with the dentist that may not be at a convenient time for the consumer. F. 120.

b. Take-home teeth whitening kits provided by dentists

Dentists in North Carolina also offer take-home teeth whitening kits that patients self-administer after a consultation with the dentist. F. 121. Take-home kits provided by dentists include a custom-made whitening tray and whitening gel. F. 122. Take-home kits provided by dentists typically use low concentrations of hydrogen peroxide or carbamide peroxide and require the consumer to reapply the whitening solution to his or her own teeth multiple times over a period of weeks or months. F. 125. Dentist provided take-home kits typically cost hundreds of dollars, in part, because the dentist performs a diagnostic examination, charges to fabricate the custom tray, provides instruction on its use, and supplies the whitening product and kit. F. 126. Take-home kits provided by dentists are usually more expensive than over-the-counter kits, discussed below. F. 127. Take-home kits provided by dentists are less expensive than the dentist in-office procedure and are also relatively effective at whitening teeth. F. 128. However, the consumer is required to apply the product at home a number of times without assistance. F. 128.

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c. Over-the-counter products

Over-the-counter ("OTC") products include tray-less methods, such as gels, rinses, chewing gums, trays, and strips, for at-home bleaching. F. 129. These products typically use relatively low concentrations of hydrogen peroxide or carbamide peroxide and must be applied daily for an extended period of time. F. 130. OTC products are sold in a variety of locations including pharmacies, groceries, and over the internet. F. 130. Consumers self-apply the OTC strips directly to their teeth and must reapply them multiple times over multiple days. F. 132-33. OTC strips and trays typically cost between \$15 and \$50, depending on brand, quantity, and concentration. F. 134. The whitening results with OTC strips are highly variable because user compliance is variable; a great many consumers will not complete the whitening regimen, which may require as much as 30 days of daily use. F. 135. OTC strips have the advantages of the convenience of at-home treatment and low cost compared to the other alternatives. F. 136. The disadvantage is that OTC strips require diligent and repeated application by the consumer. F. 136.

d. Non-dentist teeth whitening services

Non-dentists offer teeth whitening services in mall kiosks, spas, retail stores, and salons. F. 138. Non-dentist teeth whitening typically uses a mid-level hydrogen peroxide/carbamide peroxide concentration, which is usually applied once during a single visit. F. 140. In a typical non-dentist bleaching procedure, the operator generally will: (1) have the client sit in a chair; (2) put on protective gloves; (3) place a bib around the client's neck; (4) take a tray from a sealed package, which is either pre-filled with peroxide solution or which the operator fills with the peroxide solution, and hand it to the customer, who places the tray into his or her mouth; (5) adjust the light, if used; and (6) start the timer. F. 143. At the end of the procedure, the customer will remove the tray and hand it to the provider, who disposes of it. F. 143. Teeth whitening services offered in mall kiosks, spas, retail stores, and salons typically take one hour or less to whiten the customer's teeth. F. 146. The cost of non-dentist teeth whitening services varies, but ranges

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between \$75 and \$150. F. 147. Non-dentist chair-side bleaching is accessible, located most often in large shopping malls, and does not require an appointment. F. 149. Importantly, non-dentist whitening teeth whitening services can be completed in a single session. F. 150.

2. Interchangeability of the methods for teeth whitening

a. Interchangeability of products and services

Take-home products do not contain as much hydrogen peroxide as is contained in the products used by dentists and non-dentists in providing teeth whitening services. F. 170. Therefore, take-home products, whether provided by a dentist, non-dentist, or purchased over-the-counter, require numerous bleaching sessions over many days or weeks. F. 171. By contrast, chair-side bleaching, whether provided by dentists or non-dentists, is usually limited to a single bleaching session. F. 171.

The amount of time it takes to whiten teeth is important to some consumers of teeth whitening services or products. F. 172.

If consumers want teeth whitening within 24 hours because, for example, they have a special event the next day, their choices are to go either to a dentist or to a non-dentist kiosk or salon for whitening. F. 153. OTC products do not achieve the same whitening results that quickly. F. 133, 136, 171.

OTC products are the least expensive alternative for consumers who are willing to self-apply bleaching products over several days or weeks, aided only by written instructions. F. 133, 136, 171. However, they are not a good substitute for chair-side teeth bleaching for consumers who want quick results or are concerned about self-application of OTC products. F. 174. Therefore, teeth whitening products, whether sold by dentists or OTC, are not reasonable substitutes for teeth whitening services. *See* F. 170-74.

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b. Interchangeability of services offered by dentists and non-dentists

If a consumer wants same day teeth whitening, the only ways to achieve that are to go to a dentist or to a non-dentist provider of teeth whitening services, such as those located in mall kiosks. F. 152-53. Dentists and non-dentist providers of teeth whitening services use higher peroxide concentrations than used in typical OTC products available in drug stores and supermarkets and, thus, work faster. F. 109, 140, 170-71. Non-dentist and dentist teeth whitening services have common characteristics, including higher concentrations of peroxide, provision of instruction, provision of a tray, loading of the peroxide, use of a light activator, and convenience of achieving results in one session. F. 151.

Cross-elasticity measures the degree of substitution between alternative products, defined as the percentage change in quantity and demand of one product as the price of a different product changes. *FTC v. Swedish Match*, 131 F. Supp. 2d 151, 157 (D.D.C. 2000) ("Interchangeability of use and cross-elasticity of demand look to the availability of products that are similar in character or use to the product in question and the degree to which buyers are willing to substitute those similar products for the product."); *see also* F. 154.

The expert testimony in this case establishes that there is substantial cross-elasticity of demand between dentist and non-dentist teeth whitening services, as testified to by Complaint Counsel's economic expert, Dr. John Kwoka, and agreed to by Respondent's expert, Dr. David Baumer. F. 155 (Dr. Kwoka concluding there is substantial cross-elasticity of demand between dentist and non-dentist teeth-whitening services and Dr. Baumer agreeing that there is a high cross-elasticity between dentist and non-dentist teeth-whitening services). Respondent's expert further agreed that a reduction in the supply of teeth whitening services would have an upward impact on price. F. 162.

Dentists are aware that there is commonality between the services they provide and the services non-dentists provide. F. 157. Dentists have acknowledged that consumers may choose to go to a kiosk teeth whitener to get their teeth whitened rather than

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to a dentist and that a non-dentist teeth whitener operating within two miles of a dentist could affect the volume of teeth whitening services provided by the dentist. F. 159-60. The fact that complaints sent to the Board about non-dentist teeth whitening services focus on the amount being charged by non-dentists also indicates a concern by dentists about competition from non-dentists. F. 196-97, 228, 231-32.

Non-dentist providers of teeth whitening services target advertisements to consumers who would or are considering going to the dentist for teeth whitening. F. 164. The advertisements boast similar results as dentists, but for a lower price. F. 164-65. In addition, Discus Dental, the largest manufacturer of whitening products for dentists, maker of Zoom and BriteSmile, has included salon/mall operations in its consumer surveys, showing industry recognition of interchangeability between dentists and non-dentist providers of teeth whitening services. F. 169.

4. Analysis

The geographic market is the State of North Carolina, because North Carolina is the region in which the dentists who comprise the North Carolina State Board of Dental Examiners operate (F. 7) and where consumers in North Carolina turn for teeth whitening services.

The product market is the provision of teeth whitening services by dentists and non-dentists and does not include self-administered teeth whitening products. The evidence, set forth at F. 151-53 and summarized above, establishes that dentists and non-dentist teeth whitening services are viewed by consumers as performing the same function – effective teeth whitening performed in one session – and, thus, are reasonably interchangeable. Dentists and non-dentist providers also view themselves as offering comparable services. F. 157-68. Expert testimony confirms the cross-elasticity of demand between dentist and non-dentist teeth whitening services. F. 154-55. The evidence also establishes that self-administered teeth whitening products are not reasonably interchangeable with dentist and non-dentist providers of teeth whitening services because the

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products do not achieve the same results sought by consumers. F. 170-74. Accordingly, the relevant market in which to assess the challenged restraint of trade is the provision of teeth whitening services in North Carolina.

D. Concerted Action

The first element of a Sherman Act Section 1 violation requires proof of a contract, combination, or conspiracy among two or more separate entities. *Valuepest.com of Charlotte, Inc. v. Bayer Corp.*, 561 F.3d 282, 286 (4th Cir. 2009); *Law v. NCAA*, 134 F.3d at 1016. "Independent action is not proscribed." *Monsanto Co. v. Spray-Rite Service Co.*, 465 U.S. 752, 761 (1984). "The fundamental prerequisite is unlawful conduct by two or more parties pursuant to an agreement, explicit or implied. Solely unilateral conduct, regardless of its anticompetitive effects, is not prohibited by Section 1. Rather, to establish an unlawful combination or conspiracy, there must be evidence that two or more parties have knowingly participated in a common scheme or design." *Mass. Board*, 1988 FTC LEXIS 34, at *28 (quoting *Contractor Utility Sales Co. v. Certain-Teed Products Corp.*, 638 F.2d 1061, 1074 (7th Cir. 1981)). "The term 'concerted action' is often used as shorthand for any form of activity meeting the section 1 'contract, combination or conspiracy' requirement." *Alvord-Polk v. F. Schumacher & Co.*, 37 F.3d 996, 999 n.1 (3rd Cir. 1994). *See, e.g., Viazis v. Am. Ass'n of Orthodontists*, 314 F.3d 758, 761 (5th Cir. 2002) ("[t]o establish a § 1 violation, a plaintiff must demonstrate concerted action").

In the instant case, Complaint Counsel alleges that the Board's efforts to prevent or eliminate non-dentist teeth whitening services, through issuing cease and desist letters and other communications to providers, manufacturers, potential entrants, and mall operators (collectively, the "challenged conduct"), constituted concerted actions of the Board. Complaint ¶¶ 18-22, 26. Complaint Counsel argues that it has established the element of concerted action, as a matter of law, because the Board, although ostensibly a single legal entity, is controlled by six independent dentist members, each with a distinct and

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independent economic interest, who compete in the industry they regulate. CCB at 72-73; CCRB at 27-28.

In support of this argument, Complaint Counsel notes that courts and the Commission have treated contracts and other agreements made by professional organizations and trade groups as "concerted action" of the controlling members, for purposes of Section 1, despite such a group's organization as single, distinct legal entity. CCB at 72-72, citing, *e.g.*, *American Needle, Inc. v. NFL*, 130 S. Ct. 2201 (2010) and *Mass. Board*, 110 F.T.C. 549 (1988). However, in both of the foregoing cases, there was no factual issue as to whether there had been "a contract or other agreement" made by the organization. In *American Needle*, the member teams of the NFL voted to cause its licensing entity, which the NFL had formed, to enter into an exclusive license agreement with one company and to terminate a previous license agreement with American Needle. In *Mass. Board*, the respondent's members collectively voted to promulgate regulations that restricted advertising by optometrists. *See also FTC v. Indiana Federation of Dentists*, 476 U.S. 447 (1986) (defendant dentists' union promulgated a work rule requiring member dentists to withhold x-rays requested by dental insurers); *Arizona v. Maricopa County Med. Soc.*, 457 U.S. 332 (1982) (medical fees were set by majority vote of medical foundation members, and contracts were made that bound members to abide by set fees); *National Soc'y of Professional Engineers v. United States*, 435 U.S. 679 (1978) (professional society adopted code of ethics prohibiting engineers from engaging in competitive bidding). The issue in both *American Needle* and *Mass. Board* was whether, given the membership composition of each organization, the organization was legally "*capable* of engaging in a 'contract, combination . . . , or conspiracy' as defined by § 1 of the Sherman Act, 15 U.S.C. § 1, or, . . . whether the alleged activity . . . 'must be viewed as that of a single enterprise for purposes of § 1.'" *American Needle*, 103 S. Ct. at 2208 (emphasis added); *see also Mass. Board*, 1988 FTC LEXIS 34, at *28-30.

Contrary to Complaint Counsel's argument, case law does not hold that the membership composition of a group, by itself, establishes the element of "concerted action" for a Section 1

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violation. As the Commission stated in *Mass. Board*, Section 1 requires proof that that the members comprising the group "agree to a common design . . . The fundamental prerequisite of [Section 1] is unlawful conduct by two or more parties pursuant to an agreement, explicit or implied. . . . [T]o establish an unlawful combination or conspiracy, there must be evidence that two or more parties have knowingly participated in a common scheme or design." 1988 FTC LEXIS 34, at *28 (quoting in part *Contractor Utility Sales Co. v. Certain-Teed Products Corp.*, 638 F.2d 1061, 1074 (7th Cir. 1981)) (emphasis added). See *Copperweld Corp. v. Indep. Tube Corp.*, 467 U.S. 752, 771 (1984) (holding that agreement under Section 1 of the Sherman Act may be found from "a unity of purpose or a common design and understanding, or a meeting of minds"). Accordingly, a finding of a legal capacity to conspire does not resolve the issue of whether a conspiracy actually occurred. "The mere opportunity to conspire does not by itself support the inference that such an illegal combination actually occurred." *Capital Imaging v. Mohawk Valley Medical Associates, Inc.*, 996 F.2d 537, 545 (2d Cir. 1993).

Consistent with the foregoing authorities, it must first be determined whether the Board is legally capable of concerted action. Following that determination, the analysis next examines whether the Board's conduct with regard to non-dentist teeth whitening service providers was, in fact, concerted action, under the law.

1. The Board's capacity for concerted action

Complaint Counsel contends that the Board is controlled by six independent dentist members, who are practicing dentists with distinct and independent economic interests, and who compete in the industry they regulate. CCB at 72. Respondent claims that the Board's dentist members, although practicing dentists, have little, if any, economic interest in the challenged conduct of non-dentist teeth whitening services; are in any event ethically bound not to let their economic interests interfere with their work on the Board; and, in taking action with regard to non-dentist teeth whitening services, were pursuing the common business purpose of enforcing North Carolina law. RB at 24-26; RRB at 3-4. Accordingly, Respondent claims, the evidence indicates that

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the Board is not composed of competing economic actors, but rather constitutes a "unitary business enterprise" within the rule of *Copperweld Corp. v. Indep. Tube Corp.*, 467 U.S. 752 (1984) (holding that parent company and wholly owned subsidiary were a "single aggregation of economic power" that could not conspire within the meaning of Sherman Act § 1).

"[S]ubstance, not form, should determine whether a[n] . . . entity is capable of conspiring under § 1." *Copperweld*, 467 U.S. at 773 n.21; *American Needle*, 130 S. Ct. at 2211. The relevant inquiry is not whether the defendant is a single legal entity, but whether the entity's decision-makers consist of "separate economic actors" with "separate economic interests," whose joint decision could deprive the marketplace of actual or potential competition. *American Needle*, 130 S. Ct. at 2212-13. Accordingly, both the courts and the Commission have held that "when an organization is controlled by a group of competitors, the organization is viewed as a combination of its members, and their concerted actions will violate the antitrust laws if [those actions constitute] an unreasonable restraint of trade." *North Texas Specialty Physicians*, 140 F.T.C. at 738 (citing *In re Michigan State Med. Soc'y*, 101 F.T.C. 191, 286 (1983)). See, e.g., *American Needle*, 130 S. Ct. at 2212-13 (holding that NFL was capable of conspiracy where it was controlled by competing member teams that were each independently owned and managed); *United States v. Sealy, Inc.*, 388 U.S. 350, 353-54 (1967) (holding that licensing entity operated and controlled by group of manufacturer-licensees was not a single actor for purposes of Sherman Act Section 1); *Capital Imaging*, 996 F.2d at 544 (holding that multi-member association of competing doctors, all of whom were in private practice for themselves, was capable of conspiring); *Mass. Board*, 110 F.T.C. 549, 1988 FTC LEXIS 34, at *29-30 (1988) (rejecting argument that Board conduct was unilateral action, where member optometrists were each principally engaged in private practice, and had separate economic identities). The rationale for such "jurisprudence is sound. Without it, any group of competitors could avoid antitrust liability . . . by acting through single organizations that they control. . . ." *North Texas Specialty Physicians*, 140 F.T.C. at 738. Indeed, antitrust law "has been particularly watchful of organizations of the various trades or professions. See, e.g.,

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National Soc’y of Professional Engineers v. United States, 435 U.S. 679, 98 S. Ct. 1355, 55 L. Ed. 2d 637 (1978); *Goldfarb v. Virginia State Bar*, 421 U.S. 773, 95 S. Ct. 2004, 44 L. Ed. 2d 572 (1975). . . ." *Virginia Academy of Clinical Psychologists v. Blue Shield of Virginia*, 624 F.2d 476, 481 (4th Cir. 1980) (other citations omitted).

In the instant case, the evidence shows that the Board is controlled by member dentists, who hold six of the eight seats on the Board. F. 2, 15; *see also* F. 184 (only dentist members serve as case officers in non-dentist teeth whitening investigations). The remaining two seats, held by the consumer and hygienist members, have only limited authority, and virtually no role in or power over the Board activities affecting non-dentist teeth whitening. F. 36-40, 59-60, 192-93. Moreover, at all relevant times, each dentist Board member has been engaged in the full-time practice of dentistry while serving on the Board. F. 6-7.

Thus, the evidence shows that the Board is controlled by dentist members who are each "separate economic entities." *See Capital Imaging Associates*, 996 F.2d at 544 (holding that where each doctor in independent practice association practiced medicine in his or her own individual capacity, each was a separate economic entity); *Mass. Board*, 1988 FTC LEXIS 34, at *29 (affirming Administrative Law Judge’s ruling that, where Optometry Board members were practicing optometrists, they had separate economic identities).

Respondent’s claim that the dentists controlling the Board did not have competing economic interests with respect to non-dentist teeth whitening services is not borne out by the evidence. Many of the Board members provide teeth whitening services through their private practices and derive income from it. F. 8-11. Some dentists in North Carolina earned thousands of dollars annually in revenue from the provision of teeth whitening procedures during the period from 2005 until August of 2010. F. 104, 233. In addition, dentist members of the Board are elected by fellow dentists in North Carolina, and they campaign for their Board positions. F. 15-23. Moreover, the Board is funded by fees paid by dentists. F. 13-14. These facts support an inference that Board members have a financial interest in the business of teeth whitening. F. 12 (Board members "may well be influenced by

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the impact on the bottom line," including the financial interest of dentists, in deciding whether to ban non-dentist teeth whitening). Board members are in a position to enhance their incomes and those of their constituents by preventing or eliminating non-dentist teeth whitening services. F. 12. The Board's assertion that it is subject to ethical rules against conflicts of interest on the part of its dentist members, RB at 31, and the fact that the members are obliged to enforce North Carolina law (F. 1, 33), do not transform the dentists' separate economic interests into a unity of economic interest as would negate the legal capacity to engage in concerted action.

Respondent's reliance on *Oksanen v. Page Mem'l Hosp.*, 945 F.2d 696 (4th Cir. 1991) and *Amer. Chiropractic v. Trigon Healthcare*, 367 F.3d 212 (4th Cir. 2004) (RB at 24-26) is misplaced. In *Oksanen*, the court held that a hospital and its peer review committee were not legally capable of conspiring with one another, due to the hospital's management structure and authority to overrule the committee's recommendations. 945 F. 2d at 702-05. See also *Trigon Healthcare*, 367 F.3d at 224-25 (holding that insurance company and managed care advisory panel were not separate entities capable of conspiring together). In the instant case, unlike both *Oksanen* and *Trigon*, the claim is that the Board *itself* engaged in concerted action.¹⁰ In this regard, it is significant that the court in *Oksanen*, in evaluating the claim that the members of the peer review committee conspired among themselves, specifically recognized that when "physicians with independent and at times competing economic interests . . . join together to take action among themselves, they are unlike a single

¹⁰ Although the introduction to the Complaint states that "[d]entists in North Carolina, acting through the instrument of" the Board "are colluding to exclude non-dentists from competing with dentists" in the teeth whitening services market, Complaint, p. 1, Complaint Counsel has apparently abandoned that claim in favor of the theory that the Board *itself* engaged in unlawful concerted action. CCB at 72-73 (stating that the conduct of the Board constitutes concerted action within the meaning of antitrust law and that because the Board's conduct constitutes concerted action, whether the Board conspired with non-Board dentists is immaterial).

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entity and therefore they have the capacity to conspire as a matter of law." *Oksanen*, 945 F.2d at 706.¹¹

Consistent with the foregoing authorities, and based on the evidence, the Board is indeed legally capable of concerted action.

2. The Board's concerted action with regard to non-dentist teeth whitening services in North Carolina

Complaint Counsel argues that the Board can only act through its agents, that the dentist members are agents of the Board, and that the dentist members' actions against non-dentist teeth whitening service providers, such as sending out cease and desist letters on behalf of the Board, were taken with the actual or apparent authority of the Board. CCRB 30-32. Therefore, Complaint Counsel concludes, it has proven the element of "concerted action" in this case because the conduct of the individual dentist members is attributable to the Board. CCRB at 31-32 (citing *Am. Soc'y of Mechanical Eng'rs v. Hydrolevel*, 456 U.S. 556 (1982); *NAACP v. Claiborne Hardware Co.*, 458 U.S. 886 (1982); and *Viazis v. American Ass'n of Orthodontists*, 314 F.3d 758 (5th Cir. 2002)). Complaint Counsel's theory is inapposite.

In *Hydrolevel*, the issue was whether the American Society of Mechanical Engineers (ASME) could be held liable under

¹¹ Moreover, the facts underlying the holdings in *Oksanen* and *Trigon* are readily distinguishable. In *Oksanen*, the peer review committee had been specifically tasked by the hospital's Board of Trustees to conduct a peer review and make recommendations. In addition, the Board of Trustees could modify the committee's recommendations at any time and, pursuant to by-laws, retained ultimate responsibilities for all credentialing decisions. Because of the committee's limited role as an agent of the hospital, with the hospital exercising control and authority over the committee, the court concluded that the peer review committee was akin to a corporation's officers, or members of an autonomous corporate unit, and was not a separate entity capable of conspiring with the hospital. 945 F.2d at 702-05. In *Trigon*, the insurer created the panel, held 6 of its 15 seats, including the chair, and the recommendations of the panel were not binding on the insurer. *Trigon*, 367 F.3d at 224-25. The facts of these cases are simply not analogous to the facts of this case.

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Sherman Act Section 1 for conspiring with two other entities to interpret and apply a certain influential ASME code in a way that competitively disadvantaged Hydrolevel's product. *Am. Soc'y of Mechanical Eng'rs v. Hydrolevel*, 456 U.S. 556 (1982). The Supreme Court held that ASME could be held liable as a participant in the conspiracy with the other entities because the ASME members that participated in the challenged conduct were agents of ASME, acting with the apparent authority of ASME, and that it was not necessary to show that ASME ratified its agents' conduct. *Id.* at 573. In the instant case, however, Complaint Counsel contends that the Board *itself* conspired to remove non-dentist teeth whitening service providers from the market, not that the Board conspired with other persons or entities. *See* fn.10, *supra*. Compare *NAACP v. Claiborne Hardware Co.* (addressing whether NAACP, by a vote of its members, conspired with other organizations and non-member individuals in a boycott of white merchants); *Viazis v. American Ass'n of Orthodontists* (deciding, *inter alia*, whether the American Association of Orthodontists, through the conduct of some of its members, conspired with three other entities and one individual to keep Viazis' orthodontic appliance out of the market). Thus, whether the Board can be held liable as a participant in a conspiracy with other entities, because of the acts of its member-agents, is immaterial to determining whether the Board's conduct constitutes the concerted action of its members.

As explained above, to establish the element of concerted action, Complaint Counsel must show that the dentist members of the Board had an express or implied agreement to exclude non-dentist teeth whitening services from the market. An agreement results from two or more parties knowingly participating in a common scheme or design. *Mass. Board*, 1988 FTC LEXIS 34, at *28. *See Copperweld*, 467 U.S. at 771 (holding that agreement under Section 1 of the Sherman Act may be found from "a unity of purpose or a common design and understanding, or a meeting of minds"). Moreover, contrary to Respondent's argument, RB at 20-21, RRB at 4-6, "it is settled that 'no formal agreement is necessary to constitute an unlawful conspiracy,' *American Tobacco Co. v. United States*, 328 U.S. 781, 809, and that 'business behavior is admissible circumstantial evidence from which the fact finder may infer agreement.'"

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Norfolk Monument Co. v. Woodlawn Memorial Gardens, Inc., 394 U.S. 700, 703-04 (1969) (quoting *Theatre Enterprises, Inc. v. Paramount Film Distributing Corp.*, 346 U.S. 537, 540). See *Alvord-Polk*, 37 F.3d at 1000 ("An agreement need not be explicit to result in section 1 liability . . . direct evidence of concerted action is not required.") (citations omitted). Thus, in *Realcomp*, the court held that the defendant's website policy, adopted by its governing members, constituted an agreement of its governing members. 635 F.3d at 824-25. In *Mass. Board*, 1988 FTC LEXIS 34, at *32, the Board's promulgation of regulations, after discussion and vote of the Board's members, was sufficient to demonstrate concerted action of the Board's members.

Applying the foregoing legal principles, the evidence in this case shows that the Board had a common scheme or design, and therefore an agreement, to prevent or eliminate non-dentist teeth whitening services in North Carolina. This agreement is readily inferable from the Board's course of conduct in issuing cease and desist letters and similar Board communications designed to discourage non-dentist teeth whitening. See F. 207-45 (providers and manufacturers), 261-80 (manufacturers and entrants), 288-93 (mall owners and operators), 314-23 (North Carolina Board of Cosmetic Art Examiners). The consistency and frequency of the Board's message regarding non-dentist teeth whitening, over the course of several years and across the tenures of varying Board members, is highly probative circumstantial evidence of an agreement among Board members as to the content and purpose of that message. *Id.*; see also F. 32 (Board members from 2005 to 2010). Indeed, with respect to some of the Board's communications targeting non-dentist teeth whitening, there is direct evidence of advance discussion and formal approval by Board members. F. 264, 276, 289, 317, 321.

The Board's form letter issued to various mall operators stating that non-dentist teeth whitening was illegal was designed to prevent the expansion of mall-based teeth whitening kiosks, by inducing malls to refuse to rent space to non-dentist providers. F. 288, 290-93. The Board members discussed and unanimously approved this letter in advance. F. 289. In addition, the Board members expressly agreed to request the North Carolina Board of Cosmetic Art Examiners ("Cosmetology Board") to post a notice

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of the Board's position against non-dentist teeth whitening, in order to encourage the Cosmetology Board's licensees to stop providing teeth-whitening services. F. 317, 321. As with the mall letters, it is also significant that the content of the notice, as well as its purpose, was discussed and unanimously approved by Board members in advance. *See id.* A similar message of the Board's position against non-dentist teeth whitening service providers was also sent to manufacturers of teeth whitening systems, after discussion and approval at a Board meeting. F. 264, 276.

The Board members' common design, and hence agreement, to prevent or eliminate the provision of non-dentist teeth whitening services in North Carolina is further demonstrated by the Board's issuance of cease and desist letters to non-dentist teeth whitening service providers. The cease and desist letters contained nearly identical messages and were issued over the course of multiple years and across the tenures of varying Board members, including at times upon receipt of a complaint without any additional investigation. F. 32, 210-26. These facts support the inference that the Board's issuance of these letters was an agreed policy of the Board's members, in response to complaints from dentists (F.194-206), in furtherance of the dentist members' common purpose to eliminate non-dentist teeth whitening. *See also* F.201 (The Board's executive director responding to a complainant in February of 2008, referred to the Board's "going forth to do battle" with mall "bleaching kiosks" and its issuing "numerous cease and desist orders throughout the state"). Moreover, the cease and desist letters sent to teeth whitening product manufacturers and distributors were virtually identical to those sent to non-dentist teeth whitening service providers. F. 220, 262. This fact further supports the inference that the use of such letters was an agreed policy, in furtherance of the Board members' common purpose of discouraging the expansion of non-dentist teeth-whitening services.

Respondent argues that Complaint Counsel has failed to produce evidence to exclude the possibility that, in issuing the cease and desist letters, the Board members were acting independently. RRB at 7. *See Toys "R" Us v. FTC*, 221 F.3d 928, 934 (7th Cir. 2000) ("When circumstantial evidence is used,

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there must be some evidence that ‘tends to exclude the possibility’ that the alleged conspirators acted independently.” (quoting *Matsushita Elec. Indus. Co. v. Zenith Radio Corp.*, 475 U.S. 574, 588 (1986)). For example, according to Respondent, evidence that the Board approached investigations into allegations of unlawful teeth whitening services in the same manner as it approached its other investigations into the unauthorized practice of dentistry supports an inference of independent conduct, rather than conspiracy. RRB at 23, relying on *Merck-Medco Managed Care, LLC v. Rite Aid Corp.*, 1999 U.S. App. LEXIS 21487, at *25-27, 30 (4th Cir. 1999). While *Medco* notes that evidence of departure from normal business practices can be valuable proof of conspiracy, 1999 U.S. App. LEXIS 21487, at *30, *Medco* does not stand for the proposition that such proof is required to prove conspiracy.

Moreover, unlike *Medco*, the evidence in this case shows more than mere parallel conduct among Board members that could just as well be independent action, as contended by Respondent. RB at 27. Rather, as set forth above, the evidence shows a consistent, and persistent, course of conduct, using virtually identical language, over an extended period of time, during which the dentist Board members shifted and changed. See F. 27-32. Such facts tend to negate the possibility that the Board members were acting independently, “in parallel.” In any event, the law does not require that the evidence exclude *all* possibility that the alleged conspirators acted independently of one another. *Toys “R” Us*, 221 F.3d at 934-35. Furthermore, it is not necessary to demonstrate that every Board member participated in the conspiracy. See *In re Mich. State Med. Soc’y*, No. 9129, 101 F.T.C. 191, 1983 FTC LEXIS 113, at *222 (Feb. 17, 1983) (holding that even if less than all members of an organization or association agree to participate, that fact does not negate the presence of a conspiracy or combination as to those who do participate). Similarly, proof of concerted action does not require a showing of simultaneous agreement by the alleged conspirators. *Interstate Circuit, Inc. v. United States*, 306 U.S. 208, 227 (1939) (“It is elementary that an unlawful conspiracy may be and often is formed without simultaneous action or agreement on the part of the conspirators.”).

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Finally, Respondent contends that, even if the Board is capable of concerted action, and even if it took concerted action with regard to the challenged conduct, such concerted action is not unlawful because the dentist Board members were acting to enforce the Dental Practice Act, and not to suppress competition. RB at 27-29; RRB at 7-8. Because this argument is not material to whether or not the Board's conduct was "concerted action," but rather to whether that conduct constitutes an unreasonable restraint of trade, it is addressed in Section III.E below.

E. Restraint of Trade

Complaint Counsel alleges that the Board's campaign to exclude non-dentist teeth whitening providers from offering teeth whitening services constitutes an unreasonable restraint of trade. CCRB at 6. Complaint Counsel charges that the "methods of exclusion employed by the Board include issuing cease and desist orders to non-dentist providers; issuing cease and desist orders to manufacturers of products and equipment used by non-dentist providers; dissuading mall owners from leasing to non-dentist providers; and enlisting the Cosmetology Board also to threaten non-dentist providers." CCB at 70.

The Dental Practice Act provides that certain activities, including "remov[ing] stains, accretions or deposits from human teeth," constitute the practice of dentistry, and must be performed or supervised by a licensed dentist. N.C. Gen. Stat. § 90-29(b); F. 41-42. Respondent asserts that the Dental Practice Act limits the offering and provision of stain removal services to licensed dentists and authorizes the Board to take action to enforce this limitation. RB at 3. Because it is enforcing the Dental Practice Act, Respondent argues, the Board's actions against non-dentist teeth whitening service providers cannot properly be deemed an "unreasonable" restraint of trade. RB at 3.

The Commission has decided in this case that the Board, although an agency of the State, is not entitled to state action immunity for its alleged anticompetitive conduct. State Action Opinion, 2011 WL 549449, at *1. The Commission reasoned: "[T]he Board has presented no evidence to suggest that its decision to classify teeth whitening as the practice of dentistry and

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to enforce this decision with cease and desist orders was subject to any state supervision, let alone sufficient supervision to convert the Board's conduct into the conduct of the state of North Carolina." State Action Opinion, 2011 WL 549449, at *17. Respondent's contention, summarized above, that its conduct cannot be deemed an antitrust violation because it acted as a state agency enforcing state law, is logically indistinguishable from its argument to the Commission that, as a state agency enforcing state law, the Board is immune from antitrust liability. *See, e.g.*, Answer, pp. 8-17; Respondent's Motion to Dismiss, Nov. 3, 2010. Accordingly, the Commission's decision that the Board's actions are not protected from antitrust liability based on the state action doctrine effectively precludes the Administrative Law Judge from considering that issue, and forecloses Respondent from defending its conduct on the ground that the Board is a state agency enforcing state law. Similarly, the Commission's holding that the Board's conduct is not immunized as state action renders immaterial whether or not non-dentist teeth whitening services constitute a violation of the Dental Practice Act. Thus, whether non-dentist teeth whitening constitutes the "remov[al of] stains, accretions or deposits from human teeth," and, thereby, constitutes the illegal unlicensed practice of dentistry, need not and will not be addressed.

With that background, the analysis turns to whether the concerted actions of the Board constitute an unreasonable restraint of trade. The legal framework for such analysis is set forth below.

1. Legal framework

In analyzing whether an agreement unreasonably restrains trade, the Supreme Court has explained that "a restraint may be adjudged unreasonable either because it fits within a class of restraints that has been held to be '*per se*' unreasonable, or because it violates what has come to be known as the 'Rule of Reason.'" *Indiana Federation*, 476 U.S. at 457-58; *Realcomp*, 635 F.3d at 825. Complaint Counsel does not contend that the challenged conduct of the Board is unreasonable *per se*. Accordingly, the challenged conduct is analyzed pursuant to a rule of reason inquiry.

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The conventional rule of reason approach requires courts to engage in a thorough analysis of the relevant market and the effects of the restraint in that market. *Realcomp*, 635 F.3d at 825 (citing *Indiana Federation*, 476 U.S. at 461). As the court in *Realcomp* explained:

A full rule-of-reason inquiry "may extend to a 'plenary market examination,'" *Continental Airlines, Inc. v. United Airlines, Inc.*, 277 F.3d 499, 509 (4th Cir. 2002) (quoting *Cal. Dental Ass'n*, 526 U.S. at 779), which may include the analysis of "the facts peculiar to the business, the history of the restraint, and the reasons why it was imposed," *id.* (quoting *Nat'l Soc'y of Prof'l Eng'rs v. United States*, 435 U.S. 679 (1978)), "as well as the availability of reasonable, less restrictive alternatives," *id.*

Realcomp, 635 F.3d at 825. If the challenged restraint is shown to have actual anticompetitive effects, then the burden shifts to the proponent of the challenged restraint to provide procompetitive justifications for it. *Id.* In addition, "[m]arket power and the anticompetitive nature of the restraint are sufficient to show the potential for anticompetitive effects under a rule-of-reason analysis, and once this showing has been made, [the proponent of the policies] must offer procompetitive justifications." *Id.* at 827.

However, proof of actual detrimental effects can obviate the need for an inquiry into market power, which is but a "surrogate for detrimental effects." *Indiana Federation*, 476 U.S. at 460-61, quoting 7 P. Areeda, *Antitrust Law* P1511, at 429 (1986).

A "quick look," or abbreviated rule of reason analysis applies to those arrangements that "an observer with even a rudimentary understanding of economics could conclude . . . would have an anticompetitive effect on customers and markets." *Cal. Dental Ass'n*, 526 U.S. at 770. In such cases, the nature of the restraint is such that the likelihood of anticompetitive effects "can easily be ascertained," or is "comparably obvious" and no elaborate or detailed market analysis is necessary. *See id.* at 769-71. If the nature of the restraint is deemed facially anticompetitive pursuant to this "quick-look," "the proponent of the restraint must provide 'some competitive justification' for it, 'even in the absence of a

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detailed market analysis' showing market power or market effects." *Realcomp*, 635 F.3d at 825 (quoting *Cal. Dental Ass'n*, 526 U.S. at 769-71).

The Commission has held that an abbreviated rule of reason analysis is appropriate in cases where "the conduct at issue is inherently suspect owing to its likely tendency to suppress competition. Such conduct ordinarily encompasses behavior that past judicial experience and current economic learning have shown to warrant summary condemnation. If the plaintiff makes such an initial showing, and the defendant makes no effort to advance any competitive justification for its practices, then the case is at an end and the practices are condemned." *In re Polygram Holding, Inc.*, 136 F.T.C. 310, 344-45 (2003), *aff'd Polygram Holding, Inc. v. FTC*, 416 F.3d 29 (D.C. Cir. 2005). *Accord In re North Texas Specialty Physicians*, 140 F.T.C. at 733-36; *In re Realcomp II Ltd.*, No. 9320, 2009 FTC LEXIS 250, at *52-55 (Oct. 30, 2009). The Commission's "inherently suspect" framework is essentially a "'quick-look' rule-of-reason analysis." *North Texas Specialty Physicians*, 528 F.3d at 360-61; *see also Polygram*, 416 F.3d at 36-37 ("Although the Commission uses the term 'inherently suspect' to describe those restraints that judicial experience and economic learning have shown to be likely to harm consumers, . . . the rebuttable presumption of illegality arises . . . from the close family resemblance between the suspect practice and another practice that already stands convicted in the court of consumer welfare.").

While there are varying modes of inquiry, the ultimate test of legality "is whether the restraint imposed is such as merely regulates and perhaps thereby promotes competition or whether it is such as may suppress or even destroy competition." *Polygram*, 136 F.T.C. at 327 n.14, quoting *Chicago Board of Trade v. United States*, 246 U.S. 231, 238 (1918). As the court explained in *Realcomp*:

Despite these different methods, "no categorical line" separates those "restraints that give rise to an intuitively obvious inference of anticompetitive effect and those that call for more detailed treatment." *Cal. Dental Ass'n*, 526 U.S. at 780-81. Rather, the Supreme Court has

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emphasized that "whether the ultimate finding is the product of a presumption or actual market analysis, the essential inquiry remains the same -- whether or not the challenged restraint enhances competition." *Id.* at 779-80 (quoting *NCAA v. Bd. of Regents of Univ. of Okla.*, 468 U.S. 85, 104 (1984)). Accordingly, the Court has moved "away from . . . reliance upon fixed categories and toward a continuum," *Polygram Holding, Inc. v. FTC*, 416 F.3d 29, 35 (D.C. Cir. 2005), within which "the extent of the inquiry is tailored to the suspect conduct in each particular case," *id.* at 34; *see also* 7 Phillip E. Areeda & Herbert Hovenkamp, *Antitrust Law* ¶ 1507 (3d ed. 2010) . . . ("[T]he quality of proof required should vary with the circumstances."). Therefore, we must make "an enquiry meet for the case, looking to the circumstances, details, and logic of a restraint." *Cal. Dental Ass'n*, 526 U.S. at 781.

635 F.3d at 826.

Applying a rule of reason analysis, the challenged conduct of the Board constitutes concerted action which, absent a valid procompetitive justification, unreasonably restrains trade. As fully explained in detail below, the evidence shows that the challenged conduct is, by its nature, anticompetitive. (Section III.E.2.a). The evidence further shows that Respondent has market power. (Section III.E.2.b). The evidence additionally shows that the challenged conduct has had actual anticompetitive effects. (Section III.E.3). Respondent's asserted procompetitive justifications and defenses are analyzed in Section III.F.

2. Potential adverse effects

a. Anticompetitive nature

The challenged conduct has been addressed in a summary fashion above, in the context of showing that the actions of Respondent constituted concerted action. Additional details of this course of conduct are described here in order to assess the anticompetitive nature of Respondent's conduct. "[T]he facts peculiar to the business, the history of the restraint, and the reasons why it was imposed," *National Soc'y of Professional*

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Engineers, 435 U.S. at 692, are reviewed first, however, to put the anticompetitive nature of the challenged conduct in context.

i. Context for the challenged conduct

(a) Teeth whitening popularity

Teeth whitening or bleaching has become one of the most popular esthetic dental treatments over the past two decades. *See* F. 102-03. In 2004, the American Academy of Cosmetic Dentistry reported that teeth whitening services had increased more than 300% since 1996. F. 102. A 2008 national Gallup Poll reported that over 80% of dentists nationwide engage in the practice of teeth whitening. F. 103.

Realizing the popularity of teeth whitening, non-dentists began offering teeth whitening services to consumers in salons, spas, or kiosks at malls, in North Carolina in approximately 2003 or 2004.

F. 137. Non-dentist providers of teeth whitening services have advertised that: they are comparable to dentists in terms of time and convenience; they can whiten teeth in one hour or less; and they charge lower prices than dentists for their services. F. 164-68. And indeed, the evidence shows that these services are a less costly alternative to going to a dentist to have one's teeth whitened quickly and efficiently. F. 148. Whereas dentist provided teeth whitening services commonly cost around \$400 to \$500, non-dentist provided teeth whitening services commonly cost between \$75 and \$150. F. 117, 147; *see also* F. 150. For consumers who want their teeth whitened quickly, teeth whitening services provided at salons, spas or kiosks at malls are the only reasonable substitute for teeth whitening services provided by dentists. F. 151-53.

(b) Dentists' responses to non-dentist provided teeth whitening services

Dentists became aware that individuals who sought quick and inexpensive teeth whitening services saw salons, spas or mall kiosks as an alternative to going to the dentist. F. 157; *see also* F. 194-206. For example, Board member Dr. Burnham discussed with other Board members that individuals may choose to go to a

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kiosk teeth whitener rather than to a dentist to get their teeth whitened, and Board member Dr. Hardesty acknowledged that a non-dentist teeth whitener operating within two miles of a dentist could affect the volume of teeth whitening services provided by the dentist. F. 159-61.

In or around 2003, the Board received its first complaints about non-dentists providing teeth whitening services. F. 194. Between August and September 2, 2004, four North Carolina dentists complained to the Board about Edie's Salon Panache. The complaints noted that the salon advertised that it was the second "salon in North Carolina to offer teeth whitening" and that it offered a price of \$149, which was lower than the amount dentists charge. F. 196. On September 11, 2006, another dentist faxed the Board a complaint noting that "increasingly large number[s] of spas in the Hickory area are offering their clients dental bleaching." F. 197.

At least 47 individual dentists filed complaints with the Board about non-dentist teeth whitening operations. F. 229. At least 29 non-dentist teeth whitening providers were sent cease and desist letters by the Board in instances where a North Carolina dentist had filed a complaint with the Board. F. 230. With one exception, dentists' complaints to the Board about non-dentist teeth whitening do not state that any individual had been harmed by the procedure. F. 231. The Board admits that "only three investigations it opened included a report of harm or injury to an individual." F. 228. Two of these investigations stem from consumer complaints and one stems from a dentist on behalf of his patient. F. 228; *see also* RFF 100-237 (listing by case name 28 investigations the Board has taken in response to complaints and including in these proposed findings only three investigations based on complaints claiming harm from teeth whitening services by non-dentists).

Many of the dentists' complaints to the Board about non-dentist teeth whitening referenced the price being charged by, or attached advertisements showing the prices charged by, non-dentist teeth whitening service providers. F. 232. *See also* F. 196, 200, 202. Moreover, many of the dentists who filed complaints or inquiries that led to the Board investigations of

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non-dentist teeth whitening service providers derived income from the provision of teeth whitening services in recent years. F. 233. Some dentists in North Carolina earned thousands of dollars annually in revenue from the provision of teeth whitening procedures during the period of 2005 until August of 2010. F. 104, 233. Furthermore, many of the Board members provide teeth whitening services through their private practices and derive income from it. F. 9-11.

(c) Summary of context

The evidence shows that non-dentists began to offer teeth whitening services at mall kiosks, salons and spas in approximately 2003 and, thus, recently entered the market for teeth whitening services. The evidence further shows that the overwhelming number of complaints to the Board from dentists reference the price charged by non-dentists, rather than the harm caused by this procedure.

In addition, the evidence shows that dentists and some Board members had an economic interest in preventing non-dentists from offering teeth whitening services. The expert testimony, from both Complaint Counsel's and Respondent's experts, confirms that Board members have a significant, nontrivial financial interest in the business of their profession, including teeth whitening. F. 12.

As stated in *Realcomp* by the Commission: "The circumstances surrounding the establishment of the policies, and Realcomp's evident aim of retarding the emergence of a new business model, underscore the exclusionary impact of those policies." 2009 FTC LEXIS 250, at *64. Here too, the circumstances of non-dentists recently entering the teeth whitening services market, and the Board's evident aim to prevent non-dentists from offering teeth whitening services (discussed below) underscore the exclusionary impact of the challenged conduct. It is from this backdrop that the challenged conduct is assessed below.

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ii. The challenged conduct

The evidence shows that Respondent engaged in a concerted effort to exclude non-dentists from the market for teeth whitening services and to deter potential providers of teeth whitening services from entering the market. Respondent pursued its objective through the following course of conduct: (a) sending letters to non-dentist teeth whitening providers, ordering them to cease and desist from offering teeth whitening services; (b) sending letters to manufacturers of products and equipment used by non-dentist providers, and other potential entrants, either ordering them to cease and desist from assisting clients offering teeth whitening services, or otherwise attempting to dissuade them from participating in the teeth whitening services market; (c) sending letters to owners or operators of malls to dissuade them from leasing to non-dentist providers of teeth whitening services; and (d) eliciting the help of the North Carolina Board of Cosmetic Art Examiners ("Cosmetology Board") to dissuade its licensees from providing teeth whitening services.

(a) Letters to non-dentist providers

The Board has sent at least 47 cease and desist letters to non-dental teeth whitening providers and manufacturers since it began the practice in 2006. F. 218. These 47 cease and desist letters were sent on the letterhead of the North Carolina State Board of Dental Examiners. F. 219. At least 40 of the cease and desist letters sent to non-dentist teeth whiteners contain bold, capitalized headings that state: "NOTICE AND ORDER TO CEASE AND DESIST" or "NOTICE TO CEASE AND DESIST" or a heading that states: "CEASE AND DESIST NOTICE." F. 220. The text of the majority (39 of 47) of these letters states:

You are hereby ordered to CEASE AND DESIST any and all activity constituting the practice of dentistry or dental hygiene as defined by North Carolina General Statutes § 90-29 and § 90-233 and the Dental Board Rules promulgated thereunder.

Specifically, G.S. 90-29(b) states that . . . "A person shall be deemed to be practicing dentistry in this State who does,

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undertakes or attempts to do, or claims the ability to do any one or more of the following acts or things which, for the purposes of this Article, constitute the practice of dentistry:"

"(2) Removes stains, accretions or deposits from the human teeth;"

"(7) Takes or makes an impression of the human teeth, gums or jaws:"

"(10) Performs or engages in any of the clinical practices included in the curricula of recognized dental schools or colleges."

F. 221.

The Board's objective in sending the cease and desist letters was to order the recipients to stop providing teeth whitening services. *See* F. 234-45. This is borne out by testimony of Board members and staff and by contemporaneous Board documents. *Id.* For example, Dr. Allen testified that through a cease and desist letter, the "[B]oard [is] saying that you not only are ordered but you have the responsibility to comply with this order." F. 235. Mr. White, the Board's Chief Operating Officer, testified that through a cease and desist letter "the Board is ordering [the recipient] either to stop whatever that activity is or to demonstrate why what they're doing is not a violation of the Act." F. 238.

Contemporaneous e-mails, letters, and reports drafted by Board members and Board staff confirm that while the documents sent to non-dentist teeth whitening service providers are sometimes referred to as "letters," they are also referred to by Board members and staff as "Cease and Desist Orders." F. 240. For example, on November 26, 2007, Board Investigator Dempsey wrote in an e-mail to Dr. Owens, Terry Friddle, Carolin Bakewell, Bobby White and Casie Smith Goode, that he "was able to serve the Cease and Desist Order to Ms. Heather York" of Celebrity Smiles. F. 241. The next day, on November 27, 2007, Ms. Bakewell, Board counsel, wrote in an e-mail that the Board

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"has recently issued Cease and Desist Orders to an out of state company that has been providing bleaching services in a number of malls in the state." F. 241. On February 20, 2008, Mr. White wrote in an e-mail in response to a dentist's complaint, "We've sent out numerous Cease and Desist Orders throughout the state." F. 244.

(b) Letters to manufacturers and potential entrants

Two of the 47 cease and desist letters discussed above were sent to teeth whitening product manufacturers. F. 262. On December 4, 2007, the Board issued a "Notice to Cease and Desist" to WhiteScience, advising it that assisting clients to accelerate the teeth whitening process with an LED light constitutes the unauthorized practice of dentistry, which is a misdemeanor. F. 265. The Board further directed WhiteScience to "cease its activities unless they are performed or supervised by a properly licensed North Carolina dentist." F. 265. On October 7, 2008, the Board issued a "Notice and Order to Cease and Desist," to Florida WhiteSmile, stating it was "investigating a report that you are engaged in the unlicensed practice of dentistry.

Practicing dentistry without a license in North Carolina is a crime. . . . You are hereby ordered to CEASE AND DESIST any and all activity constituting the practice of dentistry . . ." F. 274. In addition, on February 13, 2007, Ms. Bakewell wrote Enhanced Light Technologies, stating that it had come to the attention of the Board that representatives of the firm "have sold and/or attempted to sell teeth whitening systems to non-dental professionals in North Carolina, such as spa and salon owners" and advising that "[i]ndividuals who use your products to provide teeth whitening services to the public may be engaging in the unauthorized practice of dentistry, which is a misdemeanor." F. 280. The letter further directed that Enhanced Light Technologies should "accurately inform current and potential customers of the limitations on the provision of teeth whitening services in North Carolina." F. 280.

Moreover, the Board took action to dissuade potential non-dentist providers of teeth whitening services from entering the teeth whitening services market. In an e-mail dated January

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17, 2008, Board counsel Carolin Bakewell informed a non-dentist teeth whitener – in response to the teeth whitener's inquiries into the legality of teeth whitening in North Carolina – that the Dental Practice Act defines the practice of dentistry to include the "removal of stains and accretions." F. 284. Ms. Bakewell informed the inquiring teeth whitener that his or her whitening business, which provides customers with a personal tray with a whitening solution and use of a whitening light, violated the statute because it was designed to remove stains from human teeth. F. 284. Ms. Bakewell further told the inquiring teeth whitener that the statute is not limited to situations where the non-dentist touches the customer's mouth. F. 284. In another instance, on February 12, 2008, Carolin Bakewell responded to an e-mail from Craig Francis inquiring about what he needed to do in order to lawfully operate a mall whitening kiosk. F. 285. Ms. Bakewell informed Mr. Francis that he "may not operate a whitening kiosk except under the direct supervision of a licensed North Carolina dentist. The prohibition remains the same even if the customer inserts the whitening tray themselves." F. 285.

(c) Letters to owners and operators of malls

On November 21, 2007, the Board sent 11 nearly identical letters to third parties, including mall management and out-of-state mall property management companies. F. 288. These letters stated:

The N.C. State Board of Dental Examiners is the agency created by the North Carolina legislature to enforce the dental laws in this state. The Dental Board has learned that an out of state company has leased kiosks in a number of shopping malls in North Carolina for the purpose of offering tooth whitening services to the public.

North Carolina law specifically provides that the removal of stains from human teeth constitutes the practice of dentistry. See N.C. Gen. Stat. 90-29(b)(2), a copy of which is enclosed. The unauthorized practice of dentistry is a misdemeanor. See N.C. Gen. Stat. 90-40, a copy of which is also enclosed.

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It is our information that the teeth whitening services offered at these kiosks are not supervised by a licensed North Carolina dentist. Consequently, this activity is illegal.

The Dental Board would be most grateful if your company would assist us in ensuring that the property owned or managed by your company is not being used for improper activity that could create a risk to the public health and safety.

F. 288. As noted in Section III.D.2, the Board members unanimously approved sending the November 21, 2007 letters to mall operators. F. 289. The objective of the November 21, 2007 letter sent by the Board to mall operators was to induce the malls to refuse to rent space to non-dentist teeth whitening service providers. F. 290-93.

(d) Notice to Cosmetology Board

Many of the complaints about non-dentist teeth whitening service providers were against salons and spas regulated by the North Carolina Board of Cosmetic Art Examiners. F. 314. Dr. Hardesty believed that because many of the non-dentist teeth whitening service providers were licensees of the Cosmetology Board, it was logical that the Cosmetology Board might be willing to assist the Board in its efforts regarding non-dentist teeth whitening services. F. 315.

In February 2007, the Board provided the Cosmetology Board with a notice that stated:

Cosmetologists should be aware that any device or process that "removes stains, accretions or deposits from the human teeth" constitutes the practice of dentistry as defined by North Carolina General Statutes 90-29(b)(2). Taking impressions for bleaching trays also constitutes the practice of dentistry as defined by North Carolina General Statutes 90-29(b)(7).

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Only a licensed dentist or dental hygienist acting under the supervision of a licensed dentist may provide these services. The unlicensed practice of dentistry in our state is a misdemeanor.

F. 320. Shortly thereafter, the Cosmetology Board posted the Dental Board's notice on the Cosmetology Board's website. F. 322. The Board's objective in providing that notice was to encourage the Cosmetology Board's licensees to cease providing teeth-whitening services. F. 323.

iii. Tendency to harm competition

As summarized above, the evidence shows that the nature of the challenged conduct was to prevent non-dentists from offering teeth whitening services and thereby to exclude these competitors from the market. Agreements to exclude competitors from the market have long been held to violate antitrust laws. In *Fashion Originators' Guild v. FTC*, 312 U.S. 457 (1941), a combination of manufacturers of women's garments and manufacturers of textiles used in their making who claimed that the designs of their products, though not protected by patent or copyright, were original and distinctive, took actions aimed at preventing manufacturers who copied their designs from selling garments. The Supreme Court found that "the aim of petitioners' combination was the intentional destruction of one type of manufacturer and sale which competed with Guild members. The purpose and object of this combination, its potential power, its tendency to monopoly, the coercion it could and did practice upon a rival method of competition, all brought it within the policy of the prohibition declared by the Sherman and Clayton Acts." *Fashion Originators' Guild*, 312 U.S. at 467-68. In the instant case as well, the aim of the Board was to eliminate non-dentist teeth whitening service providers that competed with Board dentist members and the Board's constituents, and, therefore, the Board's conduct is well within the policy of the prohibition declared by the Sherman Act.

The Supreme Court in *Fashion Originators' Guild* further stated, "even if copying were an acknowledged tort under the law of every state, that situation would not justify petitioners in

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combining together to regulate and restrain interstate commerce in violation of federal law." 312 U.S. at 468. Similarly here, even if teeth whitening is the unauthorized practice of dentistry, that does not justify Respondent's concerted action to restrain commerce if, as the Commission has decided in this case, the Board's actions are not protected by state action immunity.

Other Supreme Court cases confirm the serious competitive harm from agreements to exclude competitors. *E.g.*, *Radiant Burners, Inc. v. Peoples Gas Light & Coke Co.*, 364 U.S. 656, 658, 660 (1961) (concerted refusal by a trade association to provide certification with result that plaintiff was "effectively excluded from the market," "clearly has, by its 'nature' and 'character,' a 'monopolistic tendency,'" and hence was per se unlawful); *Allied Tube & Conduit Corp. v. Indian Head*, 486 U.S. 492, 496, 500, 501 n.5 (1988) (where association of manufacturers of building materials that developed a model code for electrical wiring systems "collectively agreed to exclude respondent's product" from the code, Supreme Court recognized the "serious potential for anticompetitive harm" of industry standard setting, including that "'it might deprive some consumers of a desired product . . . [or] exclude rival producers.'") (quoting 7 P. Areeda, *Antitrust Law* ¶ 1503, p. 373 (1986)).

The anticompetitive nature of concerted action to exclude rivals from the market was recently addressed in the Sixth Circuit's opinion in *Realcomp*. There, the evidence showed that the respondent, an association of full service real estate brokers, implemented policies that significantly curtailed the ability of limited-service brokers to access websites controlled by the association and utilized by consumers looking to purchase real estate. *Realcomp*, 635 F.3d at 830. The court of appeals held that this evidence revealed "'a concerted refusal to deal with [limited-service brokers] on substantially equal terms' and establishe[d] that the [challenged practice was] likely to protect its [members] from competitive pricing pressure." *Id.* (quoting *Northwest Wholesale Stationers, Inc. v. Pacific Stationery & Printing Co.*, 472 U.S. 284, 295 n.6 (1985)). The Sixth Circuit then stated, "[c]ombining these findings with *Realcomp*'s substantial market power, the Commission reasonably concluded

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that Realcomp's website policy is likely to be anticompetitive." *Id.* at 830.

The evidence in this case, summarized above, also shows that the stated objective of the Board – to stop unlicensed persons from providing teeth whitening services – had the tendency to prevent consumers from getting a particular service they desire: teeth whitening in a quick, one-time session. The Supreme Court, in *Indiana Federation* held, "[a]bsent some countervailing procompetitive virtue . . . an agreement limiting consumer choice by impeding the 'ordinary give and take of the market place,' *National Society of Professional Engineers, supra*, at 692, cannot be sustained under the Rule of Reason." 476 U.S. at 459. There, a group of dentists agreed to withhold x-rays from dental insurance companies that requested their use in benefits determinations. The Supreme Court condemned the restraint as "a horizontal agreement among the participating dentists to withhold from their customers a particular service that they desire." *Id.* at 459. Here, the concerted action of the Board is to prevent non-dentists from offering teeth whitening services, which thereby withholds from consumers the choice of where they can go to get their teeth whitened quickly and less expensively than a dentist. F. 257.

The context in which Respondent's course of conduct arose and the nature of the challenged conduct reveals a tendency to harm competition. In summary, the Board has an interest in serving the interests of dentists, including dentists' financial interests. Dentists and some Board members engage in teeth whitening, in competition with non-dentists. Dentists and some Board members perceived that non-dentists were offering teeth whitening services at cheaper prices than dentists. The Board engaged in a course of conduct to prevent non-dentists from offering teeth whitening services. The Board used its status as a state agency to direct non-dentists to cease and desist from offering teeth whitening services and to direct manufacturers of products used for teeth whitening services to cease and desist from selling such products to non-dentists. The Board also used its status as a state agency to inform owners or operators of malls that it viewed the practice of non-dentist teeth whitening as an illegal practice, in order to dissuade them from leasing to

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non-dentist teeth whitening providers. Although in *Indiana Federation* the challenged restraint was condemned without an analysis of market power, 476 U.S. at 460-61, an assessment of the Board's market power in this case follows. See *Realcomp*, 635 F.3d at 828-29.

b. Market power

Market power is defined as the ability to raise prices or the ability to exclude competition. *E.I. du Pont de Nemours & Co.*, 351 U.S. 377, 391 (1956). In the instant case, the evidence shows that the Board has the power to exclude competition.

The Board was created by the Dental Practice Act "as the agency of the State for the regulation of the practice of dentistry in this State." N.C. Gen. Stat. § 90-22(a); F. 1, 33. The Board is responsible for enforcing the Dental Practice Act, including its prohibition against practicing dentistry without a license. F. 33, 41-44. Stating that it was acting pursuant to this state statute, the Board sent letters on Board letterhead, in most instances with bold, capitalized headings of: "NOTICE AND ORDER TO CEASE AND DESIST" or "NOTICE TO CEASE AND DESIST." F. 219-25. Recipients of these letters believed, and reasonably so, that they were being ordered by a state agency to stop providing teeth whitening services. F. 246-56, 266-67.

Similar evidence in *Mass. Board of Optometry* supported a finding that the respondent, also a state agency, possessed market power. Finding that the Massachusetts Board of Registration in Optometry "can impose its restraints on the market for optometric goods and services throughout Massachusetts" and its "disciplinary powers give it the ability to impose sanctions on any optometrist who fails to obey its rules and regulations," the Administrative Law Judge found that the Massachusetts Board "has market power." *In re Mass. Board of Registration in Optometry*, 1986 FTC LEXIS 39, at *78, 110 F.T.C. 549 (June 20, 1986), *aff'd* 110 F.T.C. 549 (June 13, 1988). Here, although the Board did not have disciplinary power over non-dentists, it was nevertheless able to impose restraints on the market for teeth whitening services through its course of conduct, as shown in Section III.E.3 below.

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Moreover, in cases involving standard-setting organizations ("SSOs"), defendants have been found to have the power to exclude because the SSO's decision to disapprove a product strongly influenced the market. For example, in *Hydrolevel*, where the codes and standards of the American Society of Mechanical Engineers, Inc. ("ASME") were found to "influence the policies of numerous States and cities," the Supreme Court stated:

ASME wields great power in the Nation's economy. . . . [A]s has been said about "so-called voluntary standards" generally, its interpretations of its guidelines "may result in economic prosperity or economic failure, for a number of businesses of all sizes throughout the country," as well as entire segments of an industry. ASME can be said to be "in reality an extra-governmental agency, which prescribes rules for the regulation and restraint of interstate commerce." . . . [ASME's agents have] the power to frustrate competition in the marketplace.

Hydrolevel, 456 U.S. at 570-71 (citations omitted). In *Allied Tube*, the Supreme Court also acknowledged "the setting of the Association's Code . . . in part involves the exercise of market power." *Allied Tube*, 486 U.S. at 507.

Like an SSO, the Board undertook, on its own, to set a standard that teeth whitening could only be performed by, or supervised by, a dentist, and then undertook, extra-judicially, to enforce that standard through sending letters ordering recipients to cease and desist. Moreover, Respondent's expert witness acknowledged that the Board has the power to drive from the marketplace non-dentist teeth whitening businesses. (CX0826 at 036 (Baumer, Dep. at 136-137 (The Board has "the power to exclude competition")). As more fully discussed in Section III.E.3 below, the exercise of that power resulted in actual exclusion, and restriction of consumer access to the market. Accordingly, the Board had the power to exclude.

A finding of market power, coupled with the determination that the nature of the challenged policies was to exclude

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competitors from the market, supports an inference of actual or likely adverse competitive effects. *In re Realcomp*, 2009 FTC LEXIS 250, at *95 (citing *e.g.*, *Law v. NCAA*, 134 F.3d at 1019; *Tops Markets*, 142 F.3d at 96; *Levine v. Central Florida Medical Affiliates, Inc.*, 72 F.3d 1538, 1551 (11th Cir. 1996); *Brown Univ.*, 5 F.3d at 669). As the Commission stated in *Realcomp*, "if the tribunal finds that the defendants had market power and that their conduct tended to reduce competition, it is unnecessary to demonstrate directly that their practices had adverse effects on competition." *In re Realcomp*, 2009 FTC LEXIS 250, at *47 (citing *e.g.*, *United States v. Brown Univ.*, 5 F.3d 658, 668 (3d Cir. 1993); *Flegel v. Christian Hospital*, 4 F.3d 682, 688 (8th Cir. 1993); *Gordon v. Lewistown Hosp.*, 423 F.3d 184, 210 (3d Cir. 2005); *Law v. NCAA*, 134 F.3d at 1019; *Toys "R" Us, Inc. v. FTC*, 221 F.3d 928, 937 (7th Cir. 2000)). In light of the Board's market power and the facially restrictive nature of the challenged conduct, no more is required to find that the challenged conduct constitutes an unreasonable restraint of trade because the challenged conduct will predictably result in harm to competition. Nevertheless, an analysis of the effects of the challenged conduct follows.

3. Actual adverse effects

a. Summary of facts

i. Manufacturers lost sales

The evidence shows that manufacturers of the products used by non-dentist providers of teeth whitening services have lost sales in North Carolina. F. 268-70, 279, 281-83. Two of the 47 cease and desist letters summarized above were sent to manufacturers of teeth whitening products used by non-dentists, WhiteScience and White Smile. F. 262. George Nelson of WhiteScience understood that the Board was ordering non-dentist teeth whitening businesses to close, and that the people to whom WhiteScience was selling in North Carolina would be committing a misdemeanor. F. 266-67. After the Board's actions with respect to WhiteScience and its customer-teeth whitening service providers, WhiteScience's retail sales in North Carolina evaporated to nothing, from over one million dollars yearly. F.

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268. Similarly, WhiteSmile's negotiations with potential investors in WhiteSmile operations in North Carolina fell apart due to the investors' and their attorneys' concerns over whether the Board would allow non-dentist teeth whitening. F. 273, 277. WhiteSmile eventually was able to enter the North Carolina market, but the delay in entering resulted in an estimated loss of revenue for WhiteSmile of one and one-half million dollars. F. 278-79.

ii. Owners and operators of malls stopped leasing to non-dentist providers

The evidence also shows that as a result of the Board's November 21, 2007 letters to mall companies, mall management companies, and malls (F. 288), mall operators have been reluctant to lease space to non-dentist teeth whitening service providers in North Carolina, and some companies refused to lease space and cancelled existing leases. F. 294. Respondent's expert agrees, stating "[m]all operators cooperated [with the Board's actions to enforce state law] by refusing to renew leases or rent to operators of teeth whitening services." F. 294.

As an example, Hull Storey Gibson Companies, L.L.C. ("HSG"), a retail property management company that operates five malls in North Carolina, understood from the November 21, 2007 letter it received (F. 288) that the Board took the position that the person operating the kiosks and providing non-dentist teeth whitening services would be violating North Carolina law. F. 295-301. When a non-dentist sought to lease space in an HSG mall, HSG stated that the non-dentist provider would "need to provide us with proof that the Board of Dental Examiners will approve this." F. 302. HSG contacted the Board to determine if BleachBright's teeth bleaching process had been approved by the Board and was told by Board counsel, Ms. Bakewell, that the Board had not issued an approval. F. 304-05. HSG would have leased retail space to non-dentist teeth whiteners in North Carolina had they not received these communications and would be willing to rent space to non-dentist providers if the Board were to withdraw its opposition. F. 306-08.

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As another example, a non-dental provider using the WhiteScience system in Carolina Place Mall, owned by General Growth Properties, was told that his month-to-month rental agreement would not be renewed and that his teeth whitening business would have to leave Carolina Place Mall. F. 309-11. He was further told that, based on the Board's November 21, 2007 letter, General Growth Properties' legal team advised him not to allow the non-dentist to stay in business at the mall. F. 310. Thus, the Board's letters to owners and operators of malls also resulted in excluding non-dentist teeth whiteners from the market.

iii. Non-dentist providers exited the market

Finally, the evidence shows that, as a result of the Board's actions, non-dentist providers who were operating in North Carolina ceased offering teeth whitening services. F. 246-56. For example, the owner of Modern Enhancement Salon stated in a letter to the Board, that "per your order to stop," she would "no longer perform teeth whitening services unless told otherwise by the North Carolina Board of Dental Examiners." F. 247; *see also* F. 248, 254, 255 (letters from Amazing Grace Spa, Details, Inc., and Bailey's Lightning Whitening, respectively, notifying the Board that they were no longer providing teeth whitening services). As a result of the Board's cease and desist letters, Champagne Taste Salon, Savage Tan, SheShe Studio Spa, and Triad Body Secret also ceased offering teeth whitening services. F. 250-53. Respondent's expert acknowledged the effectiveness of the letter: "[n]ot surprisingly, the actions of the State Board were effective and many kiosk and spa operators complied with state law by ceasing their actions that were clearly in violation of state law." F. 256.

A direct result of the Board's actions with respect to the Cosmetology Board was to cause non-dentists to stop providing teeth whitening services. F. 324-27. For example, one salon owner notified WhiteScience that her salon "will no longer be doing teeth whitening . . . as the North Carolina board of cosmetic arts has deemed it unlawful to perform this service in a salon." F. 326. Another salon notified the Board that they had ceased providing teeth whitening services, after learning from the Cosmetology Board that it was not legal to do so. F. 324. In

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summary, the Board has forced non-dentist teeth whitening operators to terminate their businesses, and deterred others from entering.

b. Analysis

The evidence summarized above shows that the actions of the Board caused non-dentists to cease and desist from offering teeth whitening services and prevented potential non-dentists from opening up salons or kiosks to offer the services. The Board's actions thereby: (1) excluded non-dentists from the teeth whitening service market; and (2) deprived consumers of a reasonable alternative to dentist provided teeth whitening services. "[A]n observer with even a rudimentary understanding of economics" could readily conclude that the exclusion of a rival service "would have an anticompetitive effect on customers and markets." *Cal. Dental Ass'n*, 468 U.S. at 770.

i. Exclusion of competitors and potential entrants

Respondent asserts that the Board's conduct did not have any effect on the *legal* sales of teeth whitening; instead, the Board's action affected only *illegal* teeth whitening services and was therefore reasonable under the rule of reason. RB at 7-8 (emphasis added). Respondent cites no case in which a court has held that non-dentist teeth whitening is illegal in North Carolina. Moreover, the Board's argument essentially claims that it is permitted to engage in anticompetitive conduct because it was enforcing state law. As previously discussed, issues regarding whether the Board was enforcing state law were rendered immaterial by the State Action Opinion. The Commission decided: "Absent some form of state supervision, we lack assurance that the Board's efforts to exclude non-dentists from providing teeth whitening services in North Carolina represent a sovereign policy choice to supplant competition rather than an effort to benefit the dental profession." State Action Opinion, 2011 WL 549449, at *13. Accordingly, Respondent's argument that its actions should be deemed reasonable under the rule of reason because the actions affected only "illegal" services is not considered further.

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Respondent next asserts that the evidence fails to show that the Board was able to force any kiosk, spa, or other provider of non-dentist teeth whitening services to stop operations based solely on the Board's cease and desist letters. Indeed, Respondent admits: "In order to close such a business, a court order or court judgment would be required. The State Board does not have the statutory authority to independently enforce an order requiring any person or entity to cease or desist their violations of the N.C. Dental Practice Act." RB at 8. A similar argument was rejected in *Goldfarb v. Virginia State Bar*, 421 U.S. 773 (1975).

In *Goldfarb*, the County Bar, which published a minimum fee schedule for common legal services, argued that because the fee schedule was merely advisory, the schedule and its enforcement mechanism did not constitute price fixing. *Id.* at 781. The County Bar further contended "that in practice the schedule has not had the effect of producing fixed fees." *Id.* The Supreme Court rejected those arguments, observing that, because of the prospect of disciplinary actions by the State Bar and "the desire of attorneys to comply with the announced professional norms," bar members did, in fact, comply with the schedule. *Id.* at 781-82. Although the Board here does not have the power to take disciplinary actions against non-dentists, as summarized in Section III.E.2.b, the Board projected an apparent state power of enforcement. Furthermore, just as the County Bar's argument that the schedule was "merely advisory" was rejected because the lawyers did in fact comply with the schedule, here the Board's argument that it did not have authority to enforce an order against any non-dentist teeth whitening service provider is similarly rejected because non-dentists did in fact comply with the letters directing them to cease and desist from offering teeth whitening services.

Moreover, even though Respondent admits that it does not have the authority to enforce an order for a non-dentist entity to cease or desist from violations of the Dental Practice Act, the letters that it sent did in fact order recipients to cease and desist. F. 220-22 (letters with headings including "NOTICE AND ORDER TO CEASE AND DESIST" and text stating: "You are hereby ordered to CEASE AND DESIST any and all activity

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constituting the practice of dentistry or dental hygiene as defined by North Carolina General Statutes § 90-29 and § 90-233 and the Dental Board Rules promulgated thereunder."). As summarized above, recipients interpreted these letters as ordering them to cease and desist from providing teeth whitening services or to stop selling products for use by non-dentist teeth whiteners. And, as a result of these letters and other communications issued by the Board, non-dentists did, in fact, cease and desist from providing teeth whitening services and potential entrants decided not to enter such market. Manufacturers of two teeth whitening products used by non-dentists lost sales in North Carolina, of approximately one and one half million dollars in one case and one million dollars in the other, as a result of the Board's efforts and actions to stop non-dentists from offering teeth whitening services.

Thus, the evidence shows that the concerted action of Respondent excluded non-dentists from competition, conduct that the Supreme Court has long held to be anticompetitive. For example, in *Associated Press v. United States*, 326 U.S. 1, 9, 13-14 (1945), it was held that the effect of a challenged restraint by a news association composed of member newspapers (Associated Press) was to block all newspaper non-members from any opportunity to buy news from Associated Press or any of its publisher members. The Supreme Court found the challenged restraint "hindered and restrained the sale of interstate news to non-members who competed with members" and held: "[t]rade restraints of this character, aimed at the destruction of competition, tend to block the initiative which brings newcomers into a field of business and to frustrate the free enterprise system which it was the purpose of the Sherman Act to protect." *Id.* at 13-14. See also, e.g., *Silver v. N.Y. Stock Exchange*, 373 U.S. 341, 347-49 (1963) (holding that collective action of the New York Stock Exchange and its members that excluded petitioners from a valuable business service that petitioners needed in order to compete effectively falls into "forbidden category of restraints which 'because of their inherent nature or effect injuriously restrained trade'"); *Hydrolevel*, 456 U.S. at 564, 571 (holding that defendant SSO that promulgated and published codes and standards for areas of engineering liable for harm to competition where one entity was able to use an "unofficial" response from the

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SSO on an interpretation of a code "to injure seriously the business of a competitor" which, after that response, "continued to suffer from market resistance").

Despite the evidence, Respondent asserts that because recipients of the Board's letters had alternatives to ceasing operations, "the letters did not have the immediate, irreversible, and unreasonable effect of shutting down businesses." RB at 8. The alternatives to shutting down that Respondent poses are that recipients could have offered evidence to the Board showing that no violation of the Dental Practice Act had occurred; could have hired a licensed dentist to oversee teeth whitening services; could have ceased offering such services until they could convince the North Carolina legislature that it was not in the public's interest to restrict the removal of stains from teeth to licensees; or could have requested an administrative hearing or other relief from North Carolina courts. RB at 8. But arguments as to what the non-dentists "could have done" is not as compelling as the evidence of what they actually did, which was to cease and desist from offering teeth whitening services. The Commission made a similar ruling in *Realcomp*. There, an association of real estate brokers, operated a computer database used by its members to disseminate and search for information about houses available for sale (multiple listing service or MLS). Realcomp adopted a "Search Function Policy," whereby the default setting on the association's MLS searched only full service/full price listings, and omitted listings where the broker had agreed to accept a discounted rate. Realcomp argued that the Search Function Policy did not harm competition "because users of the Realcomp MLS could override the default settings" in order to secure information about discounted listings. *Id.* at *98-100. The Commission rejected this argument, explaining: "[D]ata and broker testimony show that many brokers did not override the default search parameters. On this point we rely upon the record evidence showing what brokers actually do." *Id.* at *100. Thus, in the instant case, Respondent's speculation of what the non-dentists could have done does not defeat the record evidence showing what the non-dentists actually did in response to the Board's course of conduct. Indeed, the non-dentists' response in ceasing to provide teeth-whitening services was precisely the response intended by the Board. F. 234-45.

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ii. Limited consumer choice

In addition to excluding rivals from the market, Respondent has harmed competition by depriving consumers of a choice. F. 257. In *Indiana Federation*, the Supreme Court condemned the "horizontal agreement among the participating dentists to withhold from their customers a particular service that they desire – the forwarding of x-rays to insurance companies along with claim forms." *Id.* at 459. In this case, while the Board has not withheld services offered by dentists, its concerted activities have deprived consumers of the services of others – that of non-dentist teeth whitening service providers. By causing non-dentists to cease and desist from offering teeth whitening services, the Board has deprived consumers of the option of going to a mall, spa or salon for teeth whitening services. Thus, as in *Indiana Federation*, Respondent has "disrupted the proper functioning" of the market.¹²

In *Realcomp*, where an association of full service real estate brokers instituted a website policy that "severely restricted consumers' access to limited service listings" (offered by the full service brokers' competitors), the court of appeals upheld the "Commission's conclusion that Realcomp's website policy is likely to have an adverse impact on competition by restricting consumer access to discount listings." 635 F.3d at 829, 831. The Commission had held, "as a matter of law, there is liability under the Rule of Reason cases insofar as Realcomp's Policies operated to narrow consumer choice or hinder the competitive process." *In re Realcomp*, 2009 FTC LEXIS 250, at *111. In addition, the Commission, drawing on record evidence and

¹² In *Indiana Federation*, the Supreme Court "did not require proof of actual anticompetitive effects, such as higher prices, because the agreement was 'likely enough to disrupt the proper functioning of the price-setting mechanism of the market that it may be condemned even absent proof that it resulted in higher prices or, as here, the purchase of higher priced services, than would occur in its absence.'" *Realcomp*, 2009 FTC LEXIS 250 at *66 (quoting *Indiana Federation*, 476 U.S. at 461-62). Just as in *Realcomp*, where Complaint Counsel was not required to proffer "elaborate econometric 'proof that [the restraint] resulted in higher prices,'" *id.* at *46, it is not required to do so here.

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testimony from Complaint Counsel's expert, found that the reduction of "choices available to consumers of brokerage services," among other factors, led to the conclusion that the challenged policies "had a substantial restrictive effect on competition" in the relevant market. *Id.* at *126.

The expert testimony in this case also confirms the conclusion that Respondent's course of conduct harmed consumers and had a substantial restrictive effect on competition. Complaint Counsel's expert, Dr. Kwoka, concluded that exclusion of a product desired by consumers is presumed in economics to be anticompetitive, absent some compelling justification and Respondent's economic expert, Dr. Baumer, agreed with Dr. Kwoka's conclusion. F. 257. Respondent points out, however, that Dr. Baumer's testimony is taken out of context. According to Respondent, "Dr. Baumer's important conclusion [is] that the exclusion of a selection of teeth whitening options did not occur in a vacuum; it was necessitated by state law and public interest." RRB at 11. The issue of whether the Board's exclusion of a selection of teeth whitening options was necessitated by state law has been rendered immaterial by the decision of the Commission that state action immunity does not apply and, therefore, will not be addressed. The issue of whether the exclusion was in the public interest is evaluated in Section III.F below, addressing Respondent's procompetitive justifications.

Having determined that Respondent's course of conduct had direct adverse effects on competition, Respondent's procompetitive justifications are next considered.

F. Procompetitive Justifications and Defenses

Respondent's concerted action to exclude non-dentists and limit consumer choice cannot be sustained under a rule of reason analysis "[a]bsent some countervailing procompetitive virtue." *Indiana Federation*, 476 U.S. at 459. Respondent bears the burden of "establishing an affirmative defense which competitively justifies this apparent deviation from the operations of a free market." *National Collegiate Athletic Ass'n*, 468 U.S. at 113; *Realcomp*, 635 F.3d at 825. *See also Realcomp*, 2009 FTC LEXIS 250, at *126 (stating that "defendants generally may be

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able to defeat a finding of liability if their practices can be 'justified by plausible arguments that they were intended to enhance overall efficiency and make markets more competitive'" (quoting *Northwest Wholesale Stationers*, 472 U.S. at 294)). The Initial Decision turns now to Respondent's proffered justifications and defenses.

Respondent contends that its efforts to restrict non-dentist teeth whitening services, even if amounting to restraints, were not "unreasonable" restraints under the rule of reason because it was acting to protect the citizens of North Carolina from the unauthorized practice of dentistry. This contention is raised by Respondent in defense of its course of conduct and is therefore analyzed herein as a proffered procompetitive justification.

In support of this contention, Respondent first argues that it was acting as a state agency or occupational licensing board enforcing the Dental Practice Act, to protect the public interest, and not to promote economic self-interest. RB at 9-11; *see also* RRB at 28-30, 37-43. As noted earlier in Section III.E., this argument is essentially a reiteration of Respondent's claim that the Board's conduct is exempt from antitrust liability by the state action doctrine that has been decided against Respondent by the Commission and will not be considered.

In *Indiana Federation*, the Supreme Court held that, where there was no active state supervision, the Federation's concerted action in withholding x-rays from insurance companies was subject to condemnation under the Sherman Act "whether or not the policy the Federation has taken upon itself to advance is consistent with the policy of the State of Indiana" *Indiana Federation*, 476 U.S. at 465. In the instant case as well, because the Commission decided that there was no active state supervision, regardless of whether the conduct of the Board is aimed at preventing unauthorized dentistry and is consistent with the Dental Practice Act, Respondent has no state action immunity defense and the conduct is "anticompetitive collusion among private actors . . . subject to Sherman Act condemnation." *Id.*

Second, Respondent argues that its actions were intended to promote social welfare, by ensuring that teeth whitening services

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are supervised by licensed dentists and by protecting consumers from dangerous or unsafe teeth-whitening services. RB at 1, 12-14. Specifically, Respondent contends that the Board's enforcement of the Dental Practice Act was necessitated by serious and well-known concerns over the dangers of unsupervised teeth whitening. RB at 12. It is well established, however, that a restraint on competition cannot be justified solely on the basis of social welfare concerns, including concerns about health hazards.

The Supreme Court, in *National Society of Professional Engineers v. United States*, 435 U.S. 679 (1978), rejected as a matter of law a trade association's defense that it had restrained trade in order to protect the public from the danger of inferior engineering work. There, a trade association of engineers adopted an ethics rule that prohibited association members from engaging in competitive bidding for their engineering services. In its defense, the association claimed that "competitive pressure to offer engineering services at the lowest possible price would adversely affect the quality of engineering" and "the practice of awarding engineering contracts to the lowest bidder, regardless of quality, would be dangerous to the public health, safety, and welfare." *Id.* at 685. The district court rejected this justification "without making any findings on the likelihood that competition would produce the dire consequences foreseen by the association." *Id.* at 681. The court of appeals affirmed and the Supreme Court granted certiorari to decide whether the district court should have considered the factual basis for the proffered justification before rejecting it. *Id.* In affirming, the Supreme Court held:

The Sherman Act reflects a legislative judgment that ultimately competition will produce not only lower prices, but also better goods and services. . . . The assumption that competition is the best method of allocating resources in a free market recognizes that all elements of a bargain -- quality, service, safety, and durability -- and not just the immediate cost, are favorably affected by the free opportunity to select among alternative offers. Even assuming occasional exceptions to the presumed consequences of competition, the statutory policy precludes

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inquiry into the question whether competition is good or bad.

The fact that engineers are often involved in large-scale projects significantly affecting the public safety does not alter our analysis. Exceptions to the Sherman Act for potentially dangerous goods and services would be tantamount to a repeal of the statute. In our complex economy the number of items that may cause serious harm is almost endless – automobiles, drugs, foods, aircraft components, heavy equipment, and countless others, cause serious harm to individuals or to the public at large if defectively made.

Id. at 695. Thus, the Supreme Court held, even if the challenged restraint "ultimately inure[d] to public benefit by preventing the production of inferior work," this reason did not "satisfy the Rule [of Reason]." *Id.* at 693-94.

Such a public safety defense has also been rejected in the medical field. In *Wilk v. Am. Med. Assoc.*, 719 F.2d 207, 214 (7th Cir. 1983), through various mechanisms physicians were discouraged from cooperating with chiropractors in patient treatment, educational activities, and interpreting electrocardiograms, and chiropractors were denied access to the hospital facilities they considered necessary to practice their profession. Defendant physicians argued that their conduct had been undertaken in the interest of public health, safety, and welfare and that their conduct had been non-commercial. 719 F.2d at 216. The court of appeals rejected this argument, holding:

It is true that medical doctors are better qualified than most members of the public to form an opinion whether chiropractic poses a threat to public health, safety and welfare. They are free to attempt to persuade legislatures and administrative agencies. But a generalized concern for the health, safety and welfare of members of the public as to whom a medical doctor has assumed no specific professional responsibility, however genuine and well-informed such a concern may be, affords no legal

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justification for economic measures to diminish competition with some medical doctors by chiropractors.

Id. at 228. *See also Indiana Federation*, 476 U.S. at 463 (the argument "that an unrestrained market in which consumers are given access to the information they believe to be relevant to their choices will lead them to make unwise and even dangerous choices . . . amounts to 'nothing less than a frontal assault on the basic policy of the Sherman Act.'"); *Patrick v. Burget*, 486 U.S. 94, 105 (1988) (rejecting claim that threat of antitrust liability for physician peer- review activities will discourage participation in the process to the detriment of patient care, stating that such argument "essentially challenges the wisdom of applying the antitrust laws to the sphere of medical care, and as such is properly directed to the legislative branch").

Thus, in this case, even if the Board was acting to prevent the public from physical harm that could result from teeth whitening services provided by non-dentists, such an argument does not, under applicable antitrust law, constitute a valid justification for the Board's conduct. For this reason, expert testimony on whether teeth whitening services performed by non-dentists is safe and other testimony on harm purported to have been caused by non-dentist teeth whitening need not and will not be addressed.

Rather than alleged public welfare benefits, to avoid liability Respondent must demonstrate that the restraints have "some countervailing procompetitive virtue -- such as, for example, the creation of efficiencies in the operation of a market or the provision of goods and services . . ." *Indiana Federation*, 476 U.S. at 459; *accord Realcomp*, 2009 FTC LEXIS 250, at *127 ("The requisite beneficial effect ordinarily is one that stems from measures that increase output or improve product quality, service, or innovation." (citing *Polygram*, 136 F.T.C. at 345-46)).

Third, Respondent argues that the challenged restraints upon non-dentist teeth whitening are procompetitive because they will ensure that teeth whitening services are offered at a cost that reflects the higher skills of dentist providers, RRB at 6, 12, rather than at the lower cost alternative offered by assertedly lesser skilled, non-dentist teeth whitening providers. This argument is analogous to the argument that was made, and rejected, in

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National Society of Professional Engineers. As the Court stated in that case, "[i]t may be, as petitioner argues, that competition tends to force prices down and that an inexpensive item may be inferior to one that is more costly. There is some risk, therefore, that competition will cause some suppliers to market a defective product." *National Soc'y of Professional Engineers*, 435 U.S. at 694. However, to attempt to justify the restraint on this basis – that competition is harmful – "is nothing less than a frontal assault on the basic policy of the Sherman Act." *Id.* at 695.

In the instant case, as in *National Society of Professional Engineers*, the Board claims that permitting non-dentists to provide teeth whitening services in competition with dentists risks the production of an inferior service that consumers will choose due to lower cost. As in *National Society of Professional Engineers*, such claim runs counter to the policy of the Sherman Act and must be rejected. Respondent's argument that withholding a lower cost service from consumers is ultimately beneficial to consumers is also similar to the argument rejected in *Indiana Federation*, 476 U.S. at 462-63 (rejecting claim that withholding x-rays from insurers will prevent insurers from permitting only lower cost, inadequate treatment).

Fourth, Respondent contends that the challenged restraints are procompetitive because they will serve to "protect legal competition within the marketplace," RB at 1, and "promote competition between qualified, legal teeth whitening service providers." RB at 13. However, this argument presumes that only dentist provided teeth whitening is legal. Respondent cites no case that has held that non-dentist teeth whitening constitutes the unlawful practice of dentistry under the Dental Practice Act, as previously discussed, this Initial Decision need not and does not decide that issue. Moreover, "[t]hat a particular practice may be unlawful is not, in itself, a sufficient justification for collusion among competitors to prevent it." *Indiana Federation*, 476 U.S. at 465.

In support of its claim that the challenged restraints are procompetitive, and therefore not an unreasonable restraint of trade, Respondent relies upon *United States v. Brown Univ., et al.*, 5 F.3d 658 (3rd Cir. 1993). In *Brown*, a group of Ivy League

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colleges and universities agreed to distribute financial aid based exclusively on need and to collectively determine the amount of financial assistance that each school would offer to the commonly admitted students. The schools acknowledged that the purpose and effect of this agreement was to eliminate price competition for talented students among member institutions. However, they proffered the justification, *inter alia*, that by removing financial obstacles for needy students, the schools were expanding the choice of schools that students might attend and thereby enhancing consumer choice. The court concluded that, while the financial aid program had social benefits, the claimed enhancement of consumer choice was an economic benefit, which distinguished the case from the social welfare justifications rejected in both *National Society of Professional Engineers* and *Indiana Federation*. 5 F.3d at 676-77. Thus, the court concluded that the lower court erred in refusing, on the basis of *National Society of Professional Engineers* and *Indiana Federation*, to consider the schools' justifications as part of a full rule of reason analysis. *Id.* at 677. Respondent's reliance on *Brown* is misplaced. Respondent's restraints on non-dentist provided teeth whitening services tend to and did remove the service from the market, (*e.g.*, F.246-56, 324-27), thereby restricting consumer choice. F. 257. By contrast, the restraint in *Brown* enhanced consumer choice as well as provided social welfare benefits. As demonstrated above, Respondent's proffered "procompetitive" justifications are far more analogous to those rejected as anticompetitive in *National Society of Professional Engineers* and *Indiana Federation*.¹³

¹³ Respondent also relies on *Hospital Building. Co. v. Trustees of Rex Hospital*, 691 F.2d 678 (4th Cir. 1982), and *Pocono Invitational Sports Camp, Inc. v. NCAA*, 371 F. Supp. 2d 569 (E.D. Pa. 2004) for the proposition that courts recognize procompetitive, public interest justifications for state regulatory schemes. Neither case stands for such proposition. *Rex* held that the rule of reason permitted defendants the opportunity to demonstrate that a federal certificate of need statute, upon which they relied to justify their conduct, effectively created an exemption to the antitrust laws. *Id.* at 685. *Pocono* held that the regulations in question were not "trade or commerce" within the meaning of the Sherman Act. 317 F. Supp. 2d at 583-84.

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For the foregoing reasons, Respondent's defenses are insufficient to justify the Board's anticompetitive restraints. Accordingly, Complaint Counsel has demonstrated that the challenged conduct is an unreasonable restraint of trade, in violation of Section 5 of the FTC Act.

G. Remedy

1. Applicable legal standards

Pursuant to Section 5 of the Federal Trade Commission Act, upon determination that the challenged practice is an unfair method of competition, the Commission "shall issue . . . an order requiring such person . . . to cease and desist from using such method of competition or such act or practice." 15 U.S.C. § 45(b); *FTC v. National Lead Co.*, 352 U.S. 419, 428 (1957). The Commission's authority to issue remedial orders also includes requiring respondents to make affirmative disclosures, including sending notices to affected parties. *See, e.g., Am. Med. Ass'n*, 94 F.T.C. 701, 1979 FTC LEXIS 182, at *368, *373-79 (1979) (requiring respondent to notify its members and others of prohibition against, *inter alia*, certain advertising restrictions), *aff'd*, 638 F.2d 443 (2d Cir. 1980), *aff'd by an equally divided court*, 452 U.S. 960 (1982); *Southwest Sunsites, Inc. v. FTC*, 785 F.2d 1431, 1439 (9th Cir. 1986) (corrective advertising); *Amrep Corp. v. FTC*, 768 F.2d 1171, 1180 (10th Cir. 1985) (same). Courts have long recognized that the Commission has considerable discretion in fashioning an appropriate remedial order, subject to the constraint that the order must bear a reasonable relationship to the unlawful acts or practices. *See, e.g., FTC v. Colgate-Palmolive Co.*, 380 U.S. 374, 394-95 (1965); *FTC v. Ruberoid Co.*, 343 U.S. 470, 473 (1952); *Jacob Siegel Co. v. FTC*, 327 U.S. 608, 612-13 (1946).

In this case, Complaint Counsel has proven that Respondent took concerted action to eliminate or prevent the provision of non-dentist teeth whitening services in North Carolina, and that its actions constitute an unreasonable restraint of trade and an unfair method of competition under Section 5 of the FTC Act. The appropriate remedy is to bring an end to this conduct, rectify past violations, and prevent reoccurrence. The provisions of the

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attached order (hereafter, "Order"), more fully discussed below, accomplish these objectives and are reasonably related to the proven violations. Thus, the Order is necessary and appropriate to remedy the violations of law found to exist.

2. Cease and desist provisions

The Order requires the Board to cease and desist from directing a non-dentist teeth whitening provider to cease providing teeth whitening services, or teeth whitening goods provided in conjunction with those services (collectively, "teeth whitening goods and services"), II. A., as well as from prohibiting, restricting, impeding or discouraging the provision of such goods and services. II.B. Complaint Counsel requested language for Paragraph II.B. that would prohibit the Board from "engaging in any action that restrains, restricts, inhibits, deters or otherwise excludes" the provision of teeth whitening goods or services. Complaint Counsel's proposed prohibition is overbroad. For example, the proposed provision could be interpreted to prohibit the Board's filing a lawsuit for a suspected violation by a non-dentist teeth whitening provider, or notifying such a provider of its intention to do so, both of which are not prohibited by the Order. *See* Paragraph II.F. As modified, the language of Paragraph II.B. is consistent with the Order entered in *Mass. Board*, 1988 FTC LEXIS 34, at *83 (ordering the Board to cease and desist from, *inter alia*: "Prohibiting, restricting, impeding, or discouraging the advertising or publishing of the name of an optometrist or the availability of an optometrist's services by a person or organization not licensed to practice optometry"). Similarly, certain language proposed by Complaint Counsel for Paragraph II.G. is rejected, as unduly vague and overbroad, in favor of language used by the Commission in the order entered in *Mass. Board* (prohibiting the Board from "[i]nducing, urging, encouraging, or assisting any person or organization to take any of the actions prohibited by" the order).¹⁴

¹⁴ Section II G as proposed by Complaint Counsel would have prohibited Respondent from "[e]ncouraging, suggesting, advising, pressuring, or inducing, . . ." anyone to violate the terms of the Order.

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The Order also requires the Board to cease and desist from communicating to any current or prospective non-dentist providers, lessor of commercial property, or actual or prospective manufacturer, distributor or seller of teeth whitening goods or services, that a non-dentist's teeth whitening goods or services violate the Dental Practice Act. Section II., Paragraphs C.-F. As found above, the Board's communications to these parties that non-dentist teeth whitening was illegal were intended to prevent or eliminate non-dentist teeth whitening; had the tendency and effect of excluding non-dentist providers; and have been determined to be part of Respondent's anticompetitive course of conduct. Accordingly, prohibiting these communications is directly related to the violation. Moreover, prohibiting such communications as set forth in Section II, Paragraphs C-F will strengthen and support the Order's requirements in Section II, Paragraphs A and B, that Respondent cease actions to eliminate, restrain, or discourage the provision of non-dentist teeth whitening services.

Complaint Counsel requested language that would also prohibit Respondent from communicating that a non-dentist provider's teeth whitening goods or services "may be" in violation of the Dental Practice Act. Such a prohibition would conflict with provisions, also proposed by Complaint Counsel, and provided in the Order, which expressly permit the Board, notwithstanding the provisions of Paragraphs II.C-G, to communicate that it is investigating a suspected violation, to provide notice of intent to file a lawsuit for a suspected violation, and to file a lawsuit for an "alleged" violation. Communicating a "suspected" or "alleged" violation is the equivalent of communicating that there "may be" a violation. Accordingly, the Order does not prohibit communicating that a non-dentist provider "may be" violating the Dental Practice Act.

Section II also contains important provisions that nothing in the Order prohibits the Board from engaging in certain conduct and communications, including: (i) investigating a non-dentist provider for suspected violations of the Dental Practice Act; (ii) filing or causing to be filed, a court action against a Non-Dentist Provider for an alleged violation of the Dental Practice Act pursuant to N.C. Gen. Stat. §§ 90-40, 90-40.1, or 90-233.1; (iii)

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pursuing any administrative remedies against a non-dentist; (iv) communicating notice of "its bona fide intention to file a court action" for a suspected violation of the Dental Practice Act with regard to teeth whitening goods or services; or (v) communicating "its bona fide intention to pursue administrative remedies" with regard to teeth whitening goods or services. Although not proposed by either party, the Order extends the provision protecting certain communications to notice of the Board's "belief or opinion regarding whether a particular method of providing Teeth Whitening Goods or Teeth Whitening Services may violate the Dental Practice Act." This additional provision is necessary to give full effect to the rights retained by the Board to investigate, issue notifications, and pursue bona fide remedies regarding teeth whitening goods and services.

These communication rights retained by the Board under Section II, described above, are conditioned upon the Board's including "with equal prominence" certain affirmative disclosures, set forth in Appendix A to the Order. As noted above, requiring such affirmative disclosures are well within the Commission's remedial authority. Appendix A advises the recipient that the opinion of the Board with regard to the legality of the recipient's teeth whitening goods or services is not a legal determination; that the Board cannot order the recipient to discontinue providing the teeth whitening goods or services; and that such matters are for a court to decide. The notice also advises the recipient of potential rights to obtain a declaratory ruling under North Carolina law. These provisions are designed to ensure that the recipient of a permitted communication from the Board regarding an investigation, administrative action, or intended court action for a suspected violation, fully understands the scope or effect of the Board's communication.

3. Affirmative disclosures

Section III of the Order requires the Board to send notices and other affirmative disclosures to parties affected by the Order. As explained above, such notices are well within the Commission's remedial authority. Paragraphs A and B of Section III require the Board to send a copy of the Complaint and the Order to all present, and future, Board members, officers, directors,

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employees and agents. Paragraph C requires the Board to send a letter, in the form of Appendix B, to each person to whom the Board previously sent a "cease and desist" communication or to whom the Board otherwise communicated that a non-dentist provider of teeth whitening goods or services was violating the law. Appendix B briefly summarizes the Complaint and Order in this matter, and then sets forth substantially the same information as that set forth in Appendix A regarding the scope and effect of the Board's prior communication and the potential right to a declaratory judgment under North Carolina law. *See also* Paragraph III.C. and Appendix C (requiring the same information be provided to licensees of the Cosmetology Board, either directly or through the Cosmetology Board's website). Such affirmative disclosures serve to clarify, and remedy, impressions created by the Board's prior anticompetitive communications and conduct. In this regard, the required communications are analogous to corrective advertising.

Complaint Counsel also requested that the Order require the Board, for a period of five years, to publish in reports and post on its website, a notice containing the following affirmative disclosures:

As of the date the record closed in the Federal Trade Commission proceeding, the Board was not aware of any scientific, clinical or empirical, studies anywhere in this country that showed that teeth whitening services provided by non-dentists were any less safe than teeth whitening services provided by dentists. The harms that had been reported to the Board by consumers of non-dentist teeth whitening services were not substantiated, and the Board was not aware of any other systemic report of such harm from anywhere else in this country at that time. The FTC has ordered the Board to post this notice in response to the anticompetitive practices enumerated in the FTC Complaint. To read the FTC Order and Complaint click [here](#) [required links].

Proposed Order, Paragraph III.E. Paragraph III.E. addresses matters that are outside the scope of the violations alleged in the Complaint and outside the scope of the notice of contemplated

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relief attached to the Complaint. Moreover, as noted in Section III.E of this Initial Decision, no determination is made as to whether non-dentist teeth whitening is unsafe or injurious to consumers because that issue is not material to whether Respondent's conduct constitutes an unlawful restraint of trade. Accordingly, Complaint Counsel's proposed disclosure improperly overreaches and is not included in the Order.

4. Miscellaneous provisions

The remainder of the Order addresses various reporting and record-keeping requirements that will enable the Commission to verify compliance with the Order, and are appropriate ancillary provisions. *See* Sections IV.-VI.

5. Respondent's objections

a. Tenth Amendment

Respondent contends that the relief sought in this case violates the Tenth Amendment to the United States Constitution by "direct[ing] the actions of state officials." RB at 30-31. Respondent relies on *New York v. United States*, 505 U.S. 144 (1992) and *Printz v. United States*, 521 U.S. 898 (1997). In *New York*, the Court held that certain provisions of the Low-Level Radioactive Waste Policy Amendments Act of 1985, which required States either to enact legislation providing for the disposal of radioactive waste generated within their borders, or to take title to, and possession of, the waste, effectively required States either to legislate, or enact administrative rules, in accordance with the dictates of Congress. According to the Court, such provisions violated the sovereignty of the States because: "[t]he Federal Government may not compel the States to enact or administer a federal regulatory program." *New York v. United States*, 505 U.S. at 188. In *Printz*, the Court held that state chief law enforcement officers could not, consistent with the Constitution's provisions for state sovereignty, be compelled by the Brady Act to administer background checks on prospective handgun purchasers.

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Neither *New York* nor *Printz* applies to the instant case. First, unlike either the challenged provisions of the Low-Level Radioactive Waste Policy Amendments Act or the Brady Act, the FTC Act is not directed at state governments or state officials. Rather, it is a statute of general applicability. Respondent cites no case in which the Tenth Amendment barred a statute of general applicability from being applied to state governments or state officials, particularly where as here, the statute regulates interstate commerce. Legislation of general applicability does not violate the Tenth Amendment simply because it may have the effect of regulating a state activity. *South Carolina v. Baker*, 485 U.S. 505, 512 (1988) (holding that federal legislation prohibiting bearer bonds did not implicate Tenth Amendment because "[t]he Tenth Amendment limits on Congress' authority to regulate state activities . . . are structural, not substantive – i.e., . . . States must find their protection from congressional regulation through the national political process, not through judicially defined spheres of unregulable state activity"); *Garcia v. San Antonio Metropolitan Transit Authority*, 469 U.S. 528 (1985) (holding that the Tenth Amendment did not bar application of Fair Labor Standards Act to state employers).

Respondent further argues that the requested relief violates the Tenth Amendment by impermissibly prescribing the qualifications of state officials. RB at 31-32. Respondent argues that because the antitrust violation in this case is related to the Board's being composed of licensed dentists, pursuant to North Carolina law, the State of North Carolina "must either change its statutes so that the State Board is not 'dominated' by licensed dentists, or North Carolina must take steps to provide additional oversight to the State Board's enforcement activities." RB at 32. In this regard, Respondent restates the bases for the Commission's decision that the state action doctrine did not immunize the Board from antitrust liability, State Action Opinion, 2011 WL 549449; however, nothing in the Order requires North Carolina to take such steps to immunize the Board against the consequences of anticompetitive conduct in the future. Rather, the Order is designed to prevent the Board from repeating or engaging in what has been found to be anticompetitive conduct.

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Similarly, nothing in the Order dictates the manner of enforcing the Dental Practice Act, as claimed by Respondent. RB at 32-34. In fact, the Order is clear that none of its provisions bars the Board from fulfilling its duties to investigate, issue notifications, and pursue bona fide remedies regarding teeth whitening goods and services. *See* Section II., at 3. The Order does, however, require that the Board execute its duties without repeating the conduct that has been proven to violate the antitrust laws. The limitations on the Board's conduct provided in the Order do not interfere with the Board's enforcement of the Dental Practice Act. *See* F. 258 (Board's Chief Operating Officer stating that Board's ability to enforce the Dental Practice Act would not be impacted if the letters that the Board sent out to non-dentist teeth whitening businesses stated that it was a notice that the Board believes there is a violation and may take the recipient to court); *see also* F. 259-60 (In 2000 and 2001, Board letters did not include cease and desist language.). Accordingly, Respondent provides no basis for concluding that such limitations on the Board's activities violate the Tenth Amendment.

b. Commerce Clause

Respondent next contends that the Commerce Clause, U.S. CONST. art. I § 8, cl. 3, prohibits relief in this case because the regulation of dentistry is a state function and, therefore, outside the reach of the federal government's commerce clause powers. RB at 34-36. Respondent's argument lacks merit. First, the Order does not regulate the practice of dentistry. Rather, as noted above, the Order is designed to ensure that the Board executes its regulatory duties without repeating the activities that have been proven to violate the antitrust laws. Moreover, preventing unfair competition in or affecting interstate commerce is expressly delegated to the FTC pursuant to the FTC Act. 5 U.S.C. § 45(a). The issue of whether the Board's conduct in this case is nevertheless exempt, as state regulatory conduct, has been decided against the Board and is not addressed. *State Action Opinion*, 2011 WL 549449, at *17. For all these reasons, the Commerce Clause does not bar the entry of the Order in this case. IV.

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IV. SUMMARY OF CONCLUSIONS OF LAW

1. The Federal Trade Commission ("FTC") has jurisdiction over Respondent North Carolina State Board of Dental Examiners ("Respondent" or the "Board") and the subject matter of this proceeding pursuant to Section 5 of the Federal Trade Commission Act ("FTC Act"), 15 U.S.C. § 45.
2. Respondent is a "person" within the meaning of Section 5 of the FTC Act. 15 U.S.C. § 45.
3. The activities of Respondent challenged in the Complaint are in or affecting commerce, within the meaning of Sections 4 and 5 of the FTC Act. 15 U.S.C. §§ 44, 45.
4. The FTC Act's prohibition of unfair methods of competition under Section 5 of the FTC Act encompasses violations of Section 1 of the Sherman Act. 15 U.S.C. § 45; 15 U.S.C. § 1.
5. The legal analysis to determine a violation of Section 5 of the FTC Act is the same as it would be under Section 1 of the Sherman Act (hereafter, "Section 1").
6. A Section 1 violation requires a determination of (1) whether there was a contract, combination, or conspiracy or, more simply, an agreement; and, if so, (2) whether the contract, combination, or conspiracy unreasonably restrained trade in the relevant market.
7. Complaint Counsel has the burden of proving the relevant market in which the challenged conduct occurred.
8. The relevant product market is the provision of teeth whitening services by dentists and non-dentists.
9. The relevant geographic market is the State of North Carolina.

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10. The fundamental prerequisite under Section 1 is unlawful conduct by two or more parties pursuant to an agreement, explicit or implied. An agreement results from two or more parties knowingly participating in a common scheme or design.
11. There need not be direct evidence of an agreement to find an unlawful conspiracy under Section 1. An agreement may be inferred from circumstantial evidence, such as business behavior.
12. Membership composition of a group, by itself, does not establish the element of concerted action for a Section 1 violation. The mere opportunity to conspire does not by itself support the inference that such an illegal combination actually occurred.
13. Although a single legal entity, the Board is capable of concerted action under Section 1 because it is controlled by six practicing dentist members who are each separate economic entities and who are in a position to enhance their own incomes and/or the incomes of their dentist constituents by preventing or eliminating non-dentist teeth whitening.
14. The evidence shows a common scheme or design, and therefore an agreement, of the Board's dentist members to prevent or eliminate non-dentist teeth whitening services in North Carolina. This agreement is readily inferable from the Board's course of conduct in issuing cease and desist letters and similar Board communications designed to stop non-dentist teeth whitening in North Carolina.
15. Evidence of the Board's consistent, and persistent, course of conduct, using virtually identical language, over an extended period of time, tends to negate the possibility that Board members were acting independently.
16. The law does not require that the evidence exclude all possibility that the alleged conspirators acted independently of one another.

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17. It is not necessary to demonstrate that every Board member participated in the conspiracy.
18. Proof of concerted action does not require a showing of simultaneous agreement by the alleged conspirators.
19. Complaint Counsel has met its burden of showing that Respondent engaged in concerted action to exclude non-dentists from the market for teeth whitening services and to deter potential providers of teeth whitening services from entering the market.
20. A restraint may be adjudged unreasonable either because it fits within a class of restraints that has been held to be "*per se*" unreasonable, or because it violates the "rule of reason."
21. The conventional rule-of-reason approach requires courts to engage in a thorough analysis of the relevant market and the effects of the restraint in that market.
22. A "quick look," or abbreviated rule of reason analysis applies to those arrangements that an observer with even a rudimentary understanding of economics could conclude would have an anticompetitive effect on customers and markets.
23. An abbreviated rule of reason analysis is appropriate in cases where the conduct at issue is inherently suspect owing to its likely tendency to suppress competition, including behavior that past judicial experience and current economic learning have shown to warrant summary condemnation.
24. If the nature of the restraint is deemed facially anticompetitive pursuant to an abbreviated rule of reason analysis, the proponent of the restraint must provide some competitive justification for it, even in the absence of a detailed market analysis showing market power or market effects.

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25. Proof of market power and the anticompetitive nature of the restraint are sufficient to show the potential for anticompetitive effects under a rule of reason analysis, and once this showing has been made, the proponent of the policies must offer procompetitive justifications.
26. Proof of actual detrimental effects from the challenged practice can obviate the need for an inquiry into market power, which is but a surrogate for detrimental effects.
27. If the challenged restraint is shown to have actual anticompetitive effects, then the burden shifts to the proponent of the challenged restraint to provide procompetitive justifications for it.
28. While there are varying modes of inquiry, the ultimate test of legality under Section 1 is whether the restraint imposed is such as merely regulates and perhaps thereby promotes competition or whether it is such as may suppress or even destroy competition.
29. An agreement to exclude competitors, by its nature, has the tendency to harm competition.
30. Absent some countervailing procompetitive virtue, an agreement limiting consumer choice by excluding competitors from the market impedes the ordinary give and take of the marketplace and cannot be sustained under the rule of reason.
31. Market power is defined as the ability to raise prices or the ability to exclude competition.
32. The Board's power to exclude competition is demonstrated by the fact that non-dentist teeth whitening providers exited the market in response to the Board's cease and desist letters.
33. Complaint Counsel has met its burden of showing that Respondent engaged in concerted action to exclude

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non-dentists from the teeth whitening services market and deterred potential non-dentist providers from entering that market through the following course of conduct: (a) sending letters to non-dentist teeth whitening providers, ordering them to cease and desist from offering teeth whitening services; (b) sending letters to manufacturers of products and equipment used by non-dentist providers, and other potential entrants, either ordering them to cease and desist from assisting clients offering teeth whitening services, or otherwise attempting to dissuade them from participating in the teeth whitening services market; (c) sending letters to owners or operators of malls to dissuade them from leasing to non-dentist providers of teeth whitening services; and (d) eliciting the help of the North Carolina Board of Cosmetic Art Examiners ("Cosmetology Board") to dissuade its licensees from providing teeth whitening services.

34. The Board's concerted actions to exclude non-dentist teeth whitening in North Carolina resulted in anticompetitive effects, including: the exit of non-dentist teeth whitening services providers from the North Carolina market; the limitation of consumer choice through exclusion of non-dentist teeth whitening service providers in North Carolina; lost sales by manufacturers of products used by non-dentist providers of teeth whitening services in North Carolina; and the decision of mall owners and operators to stop leasing to non-dentist teeth whitening service providers in North Carolina.
35. Respondent bears the burden of establishing an affirmative defense that competitively justifies the apparent deviation from the operations of a free market caused by its concerted actions to exclude non-dentist teeth whitening.
36. Respondent's proffered justification that in acting to restrict non-dentist teeth whitening, it was acting as a state agency or occupational licensing board enforcing the North Carolina Dental Practice Act, to protect the public interest, and not to promote economic self-interest, is essentially a reiteration of Respondent's claim that the

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Board's conduct is exempt from antitrust liability by the state action doctrine, which was decided against Respondent by the Commission. Commission State Action Opinion, 2011 WL 549449, at *1, 17.

37. It is well established that a restraint on competition cannot be justified solely on the basis of social welfare concerns, including concerns about health hazards.
38. A generalized concern for the health, safety and welfare of members of the public, however genuine and well-informed such a concern may be, affords no legal justification for economic measures to diminish competition.
39. To avoid liability, Respondent must demonstrate that the challenged restraints have some countervailing procompetitive virtue, such as the creation of efficiencies in the operation of a market or the provision of goods and services, increases in output, or improvements in product quality, service, or innovation.
40. Respondent's proffered justification that its actions to exclude non-dentist teeth whitening service providers were intended to promote social welfare or public safety, by ensuring that teeth whitening services are supervised by licensed dentists and by protecting consumers from dangerous or unsafe teeth whitening services is not a valid justification under applicable antitrust law.
41. Respondent's proffered justification that its actions to exclude non-dentist teeth whitening are procompetitive because they will ensure that teeth whitening services are offered at a cost that reflects the higher skills of dentist providers, rather than at the lower cost alternative offered by assertedly lesser skilled, non-dentist teeth whitening providers is not a valid justification under applicable antitrust law. Competition cannot be restrained based upon the risk that competition may result in the marketing of inferior products.

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42. Respondent's proffered justification that its actions to exclude non-dentist teeth whitening are procompetitive because they will serve to protect "legal competition" between qualified, legal teeth whitening service providers is not a valid justification under applicable antitrust law. Even if non-dentist teeth whitening were illegal in North Carolina, which has not been decided, the fact that a practice may be unlawful is not, in itself, a sufficient justification for collusion among competitors to prevent it.
43. Respondent's actions to exclude non-dentist teeth whitening, as described in paragraphs 19 and 33 above, constitute a contract, combination or conspiracy, that unreasonably restrained trade in the market for teeth whitening services in North Carolina, which violates Section 1 of the Sherman Act and constitutes an unfair method of competition in violation of Section 5 of the FTC Act. 15 U.S.C. § 45.
44. Upon determination that a challenged practice is an unfair method of competition, the Commission "shall issue . . . an order requiring such person . . . to cease and desist from using such method of competition or such act or practice." 15 U.S.C. § 45(b).
45. The Commission's authority to issue remedial orders also includes requiring Respondents to make affirmative disclosures, including sending notices to affected parties.
46. The Commission has considerable discretion in fashioning an appropriate remedial order, subject to the constraint that the order must bear a reasonable relationship to the unlawful acts or practices.
47. The appropriate remedy is to bring an end to this conduct, rectify past violations, and prevent reoccurrence.
48. The Order entered herein is necessary and appropriate to remedy the violation of law found to exist.

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ORDER

I.

IT IS ORDERED that, as used in this Order, the following definitions shall apply:

- A. "Board" means the North Carolina State Board of Dental Examiners ("NCSBDE"), its officers, directors, members, employees, agents, attorneys, representatives, successors, and assigns; and the subsidiaries, divisions, groups, and affiliates controlled by it; and the respective officers, directors, members, employees, agents, attorneys, representatives, successors, and assigns of each.
- B. "Communicate" or "Communicating" means exchanging, transferring, or disseminating any information, without regard to the manner or means by which it is accomplished.
- C. "Communication" means any information exchange, transfer, or dissemination, without regard to the means by which it is accomplished, including, without limitation, oral or written, in any manner, form, or transmission medium.
- D. "Dental Practice Act" means any legislation that is administered by the Board, including, North Carolina General Statutes, Chapter 90, Article 2 (Dentistry) (N.C. Gen. Stat. §§ 90-22 - 90-48.3 (2010)) and Article 16 (Dental Hygiene Act) (N.C. Gen. Stat. §§ 90-221 - 90-233.1 (2010)).
- E. "Dentist" means any individual holding a license, issued by the Board, to practice dentistry in North Carolina.
- F. "Direct" or "Directing" means to order, direct, command or instruct.

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- G. "Non-Dentist Provider" means any Person other than a Dentist engaged in the provision, distribution or sale of any Teeth Whitening Goods or Teeth Whitening Services.
- H. "Person" means both natural persons and artificial persons, including, but not limited to, corporations, and unincorporated entities.
- I. "Principal Address" means either (i) primary business address, if there is a business address, or (ii) primary residential address, if there is no business address.
- J. "Teeth Whitening Goods" means any formulation containing a peroxide bleaching agent, whether or not used in conjunction with an LED light source, and any other ancillary products used in the provision of Teeth Whitening Services.
- K. "Teeth Whitening Services" means whitening teeth through the use of a formulation containing a peroxide bleaching agent, whether or not used in conjunction with an LED light source.
- L. "Third Party" means any Person other than NCSBDE.

II.

IT IS FURTHER ORDERED that Respondent, directly or indirectly, or through any corporate or other device, in connection with the provision of Teeth Whitening Services in or affecting commerce, as "commerce" is defined in Section 4 of the Federal Trade Commission Act, 15 U.S.C. § 44, cease and desist from:

- A. Directing a Non-Dentist Provider to cease providing Teeth Whitening Goods or Teeth Whitening Services;
- B. Prohibiting, restricting, impeding, or discouraging the provision of Teeth Whitening Goods or Teeth Whitening Services by a Non-Dentist Provider;

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- C. Communicating to a Non-Dentist Provider that: (i) such Non-Dentist Provider is violating, or has violated the Dental Practice Act by providing Teeth Whitening Goods or Teeth Whitening Services; or (ii) the provision of Teeth Whitening Goods or Teeth Whitening Services by a Non-Dentist Provider is a violation of the Dental Practice Act;
- D. Communicating to a prospective Non-Dentist Provider that: (i) a Non-Dentist Provider would violate the Dental Practice Act by providing Teeth Whitening Goods or Teeth Whitening Services; or (ii) the provision of Teeth Whitening Goods or Teeth Whitening Services by a Non-Dentist Provider would violate the Dental Practice Act;
- E. Communicating to a lessor of commercial property or any other Third Party that (i) the provision of Teeth Whitening Goods or Teeth Whitening Services by a Non-Dentist Provider is a violation of the Dental Practice Act, or (ii) that any Non-Dentist Provider is violating or has violated the Dental Practice Act by providing Teeth Whitening Goods or Teeth Whitening Services;
- F. Communicating to an actual or prospective manufacturer, distributor, or seller of Teeth Whitening Goods used by Non-Dentist Providers, or to any other Third Party that (i) the provision of Teeth Whitening Goods or Teeth Whitening Services by a Non-Dentist Provider is a violation of the Dental Practice Act, or (ii) that any Non-Dentist Provider is violating or has violated the Dental Practice Act by providing Teeth Whitening Goods or Teeth Whitening Services; and
- G. Inducing, urging, encouraging, assisting or attempting to induce, any Person to engage in any action that would be prohibited to Respondent by Paragraphs II.A through II.F above;

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Provided, however, that nothing in this Order prohibits the Board from:

- (i) investigating a Non-Dentist Provider for suspected violations of the Dental Practice Act;
- (ii) filing or causing to be filed, a court action against a Non-Dentist Provider for an alleged violation of the Dental Practice Act pursuant to N.C. Gen. Stat. §§ 90-40, 90-40.1, or 90-233.1; or
- (iii) pursuing any administrative remedies against a Non-Dentist Provider pursuant to and in accordance with the North Carolina Annotated Code;

Provided further, that nothing in this Order prohibits the Board from Communicating to a Third Party:

- (i) notice of its belief or opinion regarding whether a particular method of providing Teeth Whitening Goods or Teeth Whitening Services may violate the Dental Practice Act;
- (ii) notice of its bona fide intention to file a court action against that Person for a suspected violation of the Dental Practice Act with regard to Teeth Whitening Goods or Teeth Whitening Services; or
- (iii) notice of its bona fide intention to pursue administrative remedies with regard to Teeth Whitening Goods or Teeth Whitening Services,

so long as such Communication includes, with equal prominence, the paragraph included in Appendix A to this Order.

III.

IT IS FURTHER ORDERED that Respondent shall:

- A. Within thirty (30) days from the date this Order becomes final, send a copy of this Order and the

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Complaint by first-class mail with delivery confirmation or electronic mail with return confirmation to:

1. each Board member; and
 2. each officer, director, manager, representative, agent, attorney, and employee of the Board;
- B. Distribute by first-class mail, return receipt requested, a copy of this Order and the Complaint to each individual who becomes a Board member, or an officer, director, manager, attorney, representative, agent or employee of Board, and who did not previously receive a copy of this Order and the Complaint from Respondent, within ten (10) days of the time that he or she assumes such position;
- C. Within thirty (30) days from the date this Order becomes final, send a copy of the letter, on the Board's official letterhead, with the text included in Appendix B to this Order by first-class mail with delivery confirmation or electronic mail with return confirmation to:
1. each Person, including without limitation actual or prospective Non-Dentist Providers, manufacturers of goods and services used by Non-Dentists Providers, or any other Third Party, to whom the Board Communicated a cease-and-desist order, letter; or other similar Communication;
 2. each Person, including without limitation actual or prospective lessors of commercial property or any other Third Party, to whom the Board Communicated that (i) the provision of Teeth Whitening Goods or Teeth Whitening Services by a Non-Dentist Provider is a violation of the Dental Practice Act, or (ii) that any Non-Dentist Provider is violating, has violated, or may be violating the

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Dental Practice Act by providing Teeth Whitening Goods or Teeth Whitening Services; and

3. any other Third Party to whom, or with whom, the Board Communicated substantially the same information set forth in C.1 and 2 of this Paragraph III;
- D. Within sixty (60) days from the date this Order becomes final, Respondent shall arrange with the North Carolina Board of Cosmetic Art Examiners for the notice included as Appendix C to this Order to appear on the website of that Board for a period of six (6) months;

Provided, however, should Respondent be unable within sixty (60) days to arrange with the North Carolina Board of Cosmetic Art Examiners for such notice to appear on that Board's website, Respondent shall within ninety (90) days from the date this Order becomes final: (1) obtain from the North Carolina Board of Cosmetic Art Examiners its most current list of licensees; and (2) send the Appendix C notification by first-class mail with delivery confirmation or electronic mail with return confirmation to each licensee on that current list;

IV.

IT IS FURTHER ORDERED that Respondent shall file verified written reports within sixty (60) days from the date this Order becomes final, annually thereafter for three (3) years on the anniversary of the date this Order becomes final, and at such other times as the Commission may by written notice require. Each report shall include, among other information that may be necessary:

- A. The identity, including address and telephone number, of each Non-Dentist Provider, and any other Third Party, that the Board Communicated with during the relevant reporting period regarding Teeth Whitening Goods or Teeth Whitening Services;

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- B. Copies of all Communications with any Non-Dentist Provider, and any other Third Party regarding the provision of Teeth Whitening Goods or Teeth Whitening Services;
- C. Copies of the delivery confirmations or electronic mail with return confirmations required by Paragraph III. A and B; and
- D. A detailed description of the manner and form in which Respondent has complied, and is complying, with this Order.

V.

IT IS FURTHER ORDERED that Respondent shall notify the Commission of any change in its principal address within twenty (20) days of such change in address.

VI.

IT IS FURTHER ORDERED that, for the purpose of determining or securing compliance with this Order, and subject to any legally recognized privilege, and upon written request and upon five (5) days notice to NCSBDE, that NCSBDE shall, without restraint or interference, permit any duly authorized representative of the Commission:

- A. Access, during office hours of NCSBDE and in the presence of counsel, to all facilities and access to inspect and copy all books, ledgers, accounts, correspondence, memoranda, and all other records and documents in the possession, or under the control, of NCSBDE relating to compliance with this Order, which copying services shall be provided by NCSBDE at its expense; and
- B. To interview officers, directors, or employees of NCSBDE, who may have counsel present, regarding such matters.

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VII.

IT IS FURTHER ORDERED that this Order shall terminate twenty (20) years from the date it is issued.

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APPENDIX A

The Federal Trade Commission, by its Order of _____, 2011, has directed the Board to provide you with the following Notice. The Board hereby notifies you that the opinion of the Board expressed in this communication is not a legal determination. The Board does not have the authority to order you to discontinue providing Teeth Whitening Goods or Teeth Whitening Services. Only a court may determine that you have violated, or are violating, any law, and, if appropriate, impose a remedy or penalty for such violation.

Further, pursuant to 21 N.C.A.C. 16N .0400 and N.C. Gen. Stat. § 150B-4, you may have the right, prior to the initiation of any court action by the Board, to request a declaratory ruling regarding whether your method of providing teeth whitening goods or services is lawful.

You are further notified that any right to a declaratory ruling from the Board is additional to any other legal rights that you may already have to establish the legality of your teeth whitening goods or services. A complete copy of the Federal Trade Commission's Complaint and Decision and Order are available on the Commission's website, <http://www.ftc.gov>.

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APPENDIX B

(Letterhead of NCSBDE)

(Name and Address of the Recipient)

Dear (Recipient):

As you may know, the Federal Trade Commission issued an administrative complaint in 2010 against the Board challenging the legality of the Board's activities directed at the elimination of dental teeth whitening services in North Carolina by non-dentists.

At the conclusion of that administrative proceeding, the Commission issued a Decision and Order directing that the Board, among other things, cease and desist from certain activities involving teeth whitening by non-dentists and take certain remedial actions, of which this letter is one part. A complete copy of the Federal Trade Commission's Complaint and Decision and Order are available on the Commission's website, <http://www.ftc.gov>.

You are receiving this letter because you previously received from the Board either: (1) a letter directing, or ordering, you to cease and desist the unlicensed provision of dental teeth whitening services, or selling dental teeth whitening goods or services to non-dentist teeth whiteners in violation of the Dental Practice Act, N.C. Gen. Stat. §§ 90-29(b)(2), 90-40, and/or 90-40.1; or (2) a letter advising you that (i) a non-dentist would or might be violating the Dental Practice Act by providing teeth whitening goods or services; or (ii) the provision of teeth whitening goods or services by a non-dentist would or might be a violation of the Dental Practice Act, N.C. Gen. Stat. §§ 90-29(b)(2), 90-40, and/or 90-40.1.

The Board hereby notifies you that the prior letter you received from the Board only expressed the opinion of the Board, and that such opinion is not a legal determination. The Board does not have the authority to order that you discontinue providing Teeth Whitening Goods or Teeth Whitening Services. Only a court may determine that you are violating, or have

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violated, any law and, if appropriate, impose a remedy or penalty for such violation. Further, you may have the right to request a declaratory ruling from the Board, pursuant to 21 N.C.A.C. 16N .0400 and N.C. Gen. Stat. § 150B-4, regarding whether a particular method of providing teeth whitening goods or services is lawful. You are further notified that any right to a declaratory ruling from the Board is additional to any other legal rights that you may already have to establish the legality of any particular method of providing teeth whitening goods or services.

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APPENDIX C**Teeth Whitening Notice**

As you may know, the Federal Trade Commission issued an administrative complaint in 2010 against the North Carolina State Board of Dental Examiners challenging the legality of the Dental Board's activities directed at the elimination of dental teeth whitening services in North Carolina by non-dentists. At the conclusion of that administrative proceeding, the Commission issued a Decision and Order directing that the Dental Board, among other things, cease and desist from certain activities involving teeth whitening by non-dentists and take certain remedial actions, of which this Notice is one part. A complete copy of the Federal Trade Commission's Complaint and Decision and Order are available on the Commission's website, <http://www.ftc.gov>.

In 2007, the Cosmetology Board, at the request of the Dental Board, displayed a "Teeth Whitening Bulletin" on the Cosmetology Board's website advising cosmetologists and estheticians "that any process that 'removes stains, accretions or deposits from human teeth' constitutes the practice of dentistry. . . Taking impressions for bleaching trays also constitutes the practice of dentistry. . ." That Bulletin further advised that it was a misdemeanor for anyone other than a licensed dentist to provide those services.

The Dental Board hereby notifies you that the prior Bulletin, described above, only expressed the opinion of the Dental Board, and that such opinion is not a legal determination. The Dental Board does not have the authority to order that you discontinue providing Teeth Whitening Goods or Teeth Whitening Services. Only a court may determine that you have violated, or are violating, any law and, if appropriate, to impose a remedy or penalty for such violation. Further, you may have the right to request a declaratory ruling from the Dental Board, pursuant to 21 N.C.A.C. 16N .0400 and N.C. Gen. Stat. § 150B-4, regarding whether a particular method of providing teeth whitening goods or services is lawful. You are further notified that any right to a declaratory ruling from the Dental Board is additional to any other

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legal rights that you may already have to establish the legality of any particular method of providing teeth whitening goods or services.

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COMPLAINT

Pursuant to the provisions of the Federal Trade Commission Act, and by virtue of the authority vested in it by said Act, the Federal Trade Commission (“Commission”), having reason to believe that the Respondent, North Carolina Board of Dental Examiners, has violated the provisions of said Act, and it appearing to the Commission that a proceeding in respect thereof would be in the public interest, hereby issues this Complaint stating its charges as follows:

NATURE OF THE CASE

Dentists in North Carolina, acting through the instrument of the North Carolina Board of Dental Examiners (“Dental Board”), are colluding to exclude non-dentists from competing with dentists in the provision of teeth whitening services. The actions of the Dental Board prevent and deter non-dentists from providing or expanding teeth whitening services, increase prices and reduce consumer choice without any legitimate justification or defense, including the “state action” defense. The actions of the Dental Board unreasonably restrain competition and violate Section 5 of the Federal Trade Commission Act.

RESPONDENT

1. The Dental Board is an agency of the State of North Carolina, and is charged with regulating the practice of dentistry in the interest of the public health, safety, and welfare of the citizens of North Carolina. The Dental Board is organized, exists, and transacts business under and by virtue of the laws of the State of North Carolina, with its principal office and place of business located at 507 Airport Blvd., Suite 105, Morrisville, NC 27560.

2. The Dental Board consists of six licensed dentists, one licensed hygienist, and one “consumer member,” who is neither a dentist nor a hygienist. Each dentist member is elected to this position by the licensed dentists of North Carolina, and serves a three-year term. Collectively, the six dentist members can and do control the operation of the Dental Board. Each dentist member

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is financially interested in decisions reached by the Dental Board because, while serving on the Dental Board, each dentist member continues to engage in the for-profit business of providing dental services.

3. The conduct of the Dental Board constitutes concerted action by its members and the dentists of North Carolina.

4. The Dental Board is the sole licensing authority for dentists in North Carolina. It is unlawful for an individual to practice dentistry in North Carolina without holding a current license to practice issued by the Dental Board. The Dental Board is also tasked with policing instances of unauthorized practice of dentistry (“UPD”) as defined by and pursuant to the North Carolina dental statute.

JURISDICTION

5. The Dental Board is a “person” within the meaning of Section 5 of the Federal Trade Commission Act, as amended, 15 U.S.C. § 45.

6. The acts and practices of the Dental Board, including the acts and practices alleged herein, are in commerce or affect commerce, as “commerce” is defined in Section 4 of the Federal Trade Commission Act, as amended, 15 U.S.C. § 44. In particular, dentists and non-dentist providers of teeth whitening services in North Carolina purchase and receive products and equipment that are shipped across state lines by manufacturers and suppliers located out of state, and transfer money across state lines in payment for these products and equipment. Further, the actions alleged herein deter persons from other states from providing teeth whitening services in North Carolina.

THE RELEVANT MARKET

7. The relevant market in which to evaluate the conduct of the Dental Board is the provision of teeth whitening services in North Carolina. Teeth whitening services are offered by dentists and non-dentists.

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8. Many dentists offer patients both in-office teeth whitening services and take-home teeth whitening kits. The most common in-office procedure consists of covering the gums with a protective material, applying to the teeth a hydrogen peroxide solution in the 20-35 percent range, and then exposing the teeth to a light source. Take home kits include a custom-made whitening tray, and a whitening gel that is generally a 15-20 percent carbamide peroxide solution. The consumer self-applies the gel in essentially the same manner as when using an over-the counter (“OTC”) teeth whitening product purchased at, for example, a pharmacy.

9. During the last several years, in much of the United States, there has been an expansion of teeth whitening operations by non-dentists. Entrepreneurs have begun offering teeth-whitening services in salons, retail stores, and mall kiosks.

10. Typically, a non-dentist provider operates in the following way. The provider hands a strip or tray containing peroxide to the customer, who applies it to his or her own teeth. The customer’s teeth are then exposed to a light-emitting diode (“LED”) light source for 15 to 30 minutes. The amount of hydrogen peroxide applied to the teeth at non-dentist outlets generally falls into the 10-15 percent range. This is a greater concentration than OTC products (usually 10 percent or less), but less than the concentration employed in dentist-applied products (approximately 20-35 percent). The non-dentist provider generally does not touch the customer’s mouth.

11. Teeth whitening services performed by non-dentists are much less expensive than those performed by dentists. A non-dentist typically charges \$100 to \$200 per session, whereas dentists typically charge \$300 to \$700, with some procedures costing as much as \$1,000.

12. Teeth whitening products (such as toothpaste and OTC whitening strips) are generally viewed by consumers as inadequate substitutes for teeth whitening services, due to differences in the nature of the product, quality, cost, and convenience.

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13. Except to the extent that competition has been restrained as alleged below, and depending upon their geographic location, the dentist members of the Dental Board and the dentists of North Carolina compete with each other, and also compete with non-dentist providers of teeth whitening services.

14. The Dental Board has and exercises the power to exclude dentists and non-dentists from competing in the relevant market.

**THE DENTAL BOARD IS ACTING TO SUPPRESS
COMPETITION**

15. The North Carolina dental statute does not expressly address whether, or under what circumstances, a non-dentist may engage in teeth whitening.

16. The Dental Board has decided that the provision of teeth whitening services by non-dentists constitutes UPD. As detailed herein, the Dental Board has acted in various ways to eliminate the provision of teeth whitening services by non-dentists.

17. The Dental Board interprets the North Carolina dental statute as permitting non-dentists to engage in the retail sale of teeth whitening products for use at home. However, the Dental Board has determined that any service provided along with a teeth whitening product, including advice, guidance, providing a customer with a personal tray, whitening solution, mouth piece and/or LED light, or providing a location to use the whitening product, constitutes the practice of dentistry.

18. The Dental Board has engaged in several types of activities aimed at preventing non-dentists from providing teeth whitening services in North Carolina.

19. In particular, the Dental Board has engaged in extra-judicial activities aimed at preventing non-dentists from providing teeth whitening services in North Carolina. These activities are not authorized by statute and circumvent any review or oversight by the State.

Complaint

20. On 42 occasions, the Dental Board transmitted letters to non-dentist teeth whitening providers, communicating to the recipients that they were illegally practicing dentistry without a license and ordering the recipients to cease and desist from providing teeth whitening services.

21. On at least six occasions, agents of the Dental Board also threatened and discouraged non-dentists who were considering opening teeth whitening businesses by communicating to them that teeth whitening services could be provided only under the direct supervision of a dentist.

22. Furthermore, the Dental Board issued at least 11 letters to third parties, including mall owners and property management companies, with interests in approximately 27 malls, stating that teeth whitening services offered at mall kiosks are illegal. The purpose of these letters was to block the expansion of teeth whitening kiosks in shopping malls.

23. The Dental Board's exclusion of the provision of teeth whitening services by non-dentists does not qualify for a state action defense nor is it reasonably related to any efficiencies or other benefits sufficient to justify its harmful effect on competition.

ANTICOMPETITIVE EFFECTS OF THE DENTAL BOARD'S ACTIONS

24. The exclusionary course of conduct of the Dental Board as alleged in Paragraphs 18-22 of the Complaint may be expected to continue in the absence of effective relief. As a consequence of the challenged actions and course of conduct of the Dental Board, the availability of non-dentist teeth whitening services in North Carolina has been and will be significantly diminished. Numerous businesses have closed down entirely or have ceased to sell teeth whitening products and/or services. Additional teeth whitening businesses have curtailed their advertising or are unable to provide the types of services desired by customers. Several malls in North Carolina have declined to permit the operation therein of non-dentist teeth whitening businesses.

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25. The challenged actions and course of conduct of the Dental Board have had and will have the effect of restraining competition unreasonably and injuring consumers in the following ways, among others:

- a. preventing and deterring non-dentists from providing teeth whitening services in North Carolina;
- b. depriving consumers of the benefits of price competition; and
- c. reducing consumer choice in North Carolina for the provision of teeth whitening services.

VIOLATIONS ALLEGED

26. The combination, conspiracy, acts and practices described above, constitute anticompetitive and unfair methods of competition in or affecting commerce in violation of Section 5 of the Federal Trade Commission Act, as amended, 15 U.S.C. § 45. Such combination, conspiracy, acts and practices, or the effects thereof, are continuing and will continue or recur in the absence of appropriate relief.

NOTICE

Notice is hereby given to the respondent that the seventeenth day of February, 2011, at 10:00 a.m., is hereby fixed as the time and Federal Trade Commission offices, 600 Pennsylvania Avenue, NW, Washington D.C. 20580, as the place when and where a hearing will be had before an Administrative Law Judge of the Federal Trade Commission, on the charges set forth in this complaint, at which time and place you will have the right under the Federal Trade Commission Act to appear and show cause why an order should not be entered requiring you to cease and desist from the violations of law charged in the complaint.

You are notified that the opportunity is afforded you to file with the Commission an answer to this complaint on or before the fourteenth (14th) day after service of it upon you. An answer in which the allegations of the complaint are contested shall contain

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a concise statement of the facts constituting each ground of defense; and specific admission, denial, or explanation of each fact alleged in the complaint or, if you are without knowledge thereof, a statement to that effect. Allegations of the complaint not thus answered shall be deemed to have been admitted.

If you elect not to contest the allegations of fact set forth in the complaint, the answer shall consist of a statement that you admit all of the material allegations to be true. Such an answer shall constitute a waiver of hearings as to the facts alleged in the complaint and, together with the complaint, will provide a record basis on which the Commission shall issue a final decision containing appropriate findings and conclusions and a final order disposing of the proceeding. In such answer, you may, however, reserve the right to submit proposed findings of fact and conclusions of law under 3.46 of said Rules.

Failure to file an answer within the time above provided shall be deemed to constitute a waiver of your right to appear and to contest the allegations of the complaint, and shall authorize the Commission, without further notice to you, to find the facts to be as alleged in the complaint and to enter a final decision containing appropriate findings and conclusions and a final order disposing of the proceeding.

The Administrative Law Judge shall hold a prehearing scheduling conference not later than ten (10) days after an answer is filed by the respondent. Unless otherwise directed by the Administrative Law Judge, the scheduling conference and further proceedings will take place at the Federal Trade Commission, 600 Pennsylvania Avenue, N.W., Washington DC 20580. Rule 3.21(a) requires a meeting of the parties' counsel as early as practicable before the prehearing scheduling conference, and Rule 3.31(b) obligates counsel for each party, within five days of receiving respondent's answer, to make certain initial disclosures without awaiting a formal discovery request.

NOTICE OF CONTEMPLATED RELIEF

Should the Commission conclude from the record developed in any adjudicative proceedings in this matter that respondent's

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conduct violated Section 5 of the Federal Trade Commission Act as alleged in the complaint, the Commission may order such relief as is supported by the record and is necessary and appropriate, including but not limited to:

1. Requiring respondent to provide appropriate notification to an independent state authority of any proposed or contemplated action of the Dental Board that may, if implemented by the Dental Board, restrain the provision of teeth whitening services by non-dentist providers.
2. Requiring respondent to secure the prior and appropriate approval of an independent state authority before taking any action that may restrain the provision of teeth whitening services by non-dentist providers.
3. Requiring respondent to cease and desist from directing any non-dentist provider of teeth whitening services to cease providing teeth whitening services.
4. Requiring respondent to cease and desist communicating to any non-dentist provider of teeth whitening services that: (i) such non-dentist provider is violating, has violated, or may be violating the North Carolina Dental Practice Act by providing teeth whitening services; or (ii) the provision of teeth whitening services by a non-dentist provider is a violation of the North Carolina Dental Practice Act.
5. Requiring respondent to include in all correspondence with any non-dentist provider of teeth whitening services, including any threat to file a law suit, that the Board does not have the authority to determine whether the law has been violated, and that only a court can make that determination and then assess penalties, if judged appropriate.
6. Requiring respondent to cease and desist communicating to a lessor of commercial property or

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other third party that (i) the provision of teeth whitening services by a non-dentist provider is a violation of the North Carolina Dental Practice Act, or (ii) that any non-dentist provider of teeth whitening services is violating, has violated, or may be violating the North Carolina Dental Practice Act by providing teeth whitening services.

7. Requiring respondent to distribute a copy of the Commission's order to each and every current and future Dental Board member; officer, manager, representative, agent, and employee of the Dental Board.
8. Such additional relief as is necessary to correct or remedy the violations alleged in the complaint.

WHEREFORE, THE PREMISES CONSIDERED, the Federal Trade Commission on this seventeenth day of June, 2010, issues its complaint against the Dental Board.

By the Commission, Commissioner Brill recused.

Complaint

IN THE MATTER OF

**GRIFOLS, S.A. AND TALECRIS BIOTHERAPEUTICS
HOLDINGS CORPORATION**CONSENT ORDER, ETC. IN REGARD TO ALLEGED VIOLATIONS OF
SEC. 5(A) OF THE FEDERAL TRADE COMMISSION ACT AND SEC. 7
OF THE CLAYTON ACT

*Docket No. C-4322; File No. 101 0153
Filed, May 31, 2011 — Decision, July 20, 2011*

This consent order addresses the proposed \$3.4 billion acquisition by Grifols, S.A. ("Grifols"), of Talecris Biotherapeutics Holdings Corp. ("Talecris"). The complaint alleges that the acquisition, if consummated, would substantially lessen competition in the U.S. markets for Ig, albumin, and pdFVII. Ig is a protein replacement therapy largely used to treat immune deficient patients. Albumin is a plasma-derived substance used to expand blood volume, prime heart valves during cardiac surgery, treat burn patients, and replace proteins in treating liver failure. Under the consent order, Grifols is required to divest Talecris's Melville facility, plasma-derived business, and plasma collection centers, to a pre-approved buyer. Grifols is also required to toll manufacture Ig, albumin and PdFVII for the pre-approved buyer for seven years.

Participants

For the *Commission*: *Katherine Ambrogi, Alexander Ansaldo, Maria DiMoscato, Karen Espaldon, Peggy Bayer Femenella, Michelle Fetterman, Ken Field, Peter Herrick, Victoria Jeffries, Albert Kim, Jeremy Morrison, Paul Nolan, Eric Rohlck, Jennifer Schwab, and Nicholas Widnell.*

For the *Respondents*: *William Baer, Deborah Feinstein, and Frank Liss, Arnold & Porter LLP; and Alicia Batts and Rhett Krulla, Proskauer Rose LLP.*

COMPLAINT

Pursuant to the provisions of the Federal Trade Commission Act ("FTC Act"), and by virtue of the authority vested in it by said Act, the Federal Trade Commission ("Commission"), having reason to believe that Respondent Grifols, S.A. ("Grifols"), a corporation subject to the jurisdiction of the Commission, has

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agreed to acquire Respondent Talecris Biotherapeutics Holdings Corp. ("Talecris"), a corporation subject to the jurisdiction of the Commission, in violation of Section 7 of the Clayton Act, as amended, 15 U.S.C. § 18, and Section 5 of the FTC Act, as amended, 15 U.S.C. § 45, and it appearing to the Commission that a proceeding in respect thereof would be in the public interest, hereby issues its Complaint, stating its charges as follows:

I. RESPONDENTS

1. Respondent Grifols is a public company, headquartered in Barcelona, Spain. With its primary production facilities in Barcelona and Los Angeles, California, Grifols develops, manufactures, and sells human blood plasma-derived products. Grifols also owns a network of U.S. plasma collection centers to supply its production facilities. Grifols employs approximately 6,000 people worldwide and had global 2009 revenues of \$1.3 billion, roughly one-third of which came from sales in the United States.

2. Respondent Talecris is a public company – owned in part by the private investment firm Cerberus Capital Management, L.P. – that specializes in the development, manufacture, and sale of human blood plasma-derived products. Talecris is headquartered in Research Triangle Park, North Carolina, with additional regional headquarters in Canada and Germany. Talecris has production facilities in Clayton, North Carolina, and Melville, New York, and like Grifols, Talecris owns a network of U.S. plasma collection centers to supply those facilities. Talecris employs approximately 5,000 people worldwide and had global 2009 revenues of approximately \$1.5 billion, roughly two-thirds of which came from sales in the United States.

3. The plasma-derived products manufactured and sold by Respondents are life-sustaining and life-enhancing biologics indicated for, among other things, the treatment of primary immune deficiency diseases, neurological conditions, severe burns, liver failure, and blood coagulation disorders.

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II. THE ACQUISITION

4. Pursuant to an Agreement and Plan of Merger dated June 6, 2010, Grifols agreed to acquire Talecris for \$3.4 billion in cash and stock (the "Acquisition"). The Acquisition would combine two of the largest manufacturers of life-sustaining plasma-derived products.

III. JURISDICTION

5. Respondents, and each of their relevant operating subsidiaries and parent entities are, and at all relevant times have been, engaged in activities in or affecting "commerce" as defined in Section 4 of the FTC Act, 15 U.S.C. § 44, and Section 1 of the Clayton Act, 15 U.S.C. § 12. The Acquisition constitutes an acquisition under Section 7 of the Clayton Act.

IV. THE RELEVANT PRODUCTS

6. The relevant product markets in which to analyze the Acquisition are: (i) Ig, (ii) albumin, and (iii) plasma-derived Factor VIII ("pdFVIII").

A. Ig

7. Ig is a widely used drug that can be administered intravenously ("IVIG" or "IGIV") or subcutaneously ("SCIG"). IVIG, the more predominant form, has numerous indications approved by the U.S. Food and Drug Administration ("FDA"), and as many as 150 off-label uses. The most common uses involve the treatment of Primary Immunodeficiency Diseases and neurological conditions – *e.g.*, Guillain-Barré Syndrome and Chronic Inflammatory Demyelinating Polyneuropathy.

8. There are no substitutes for Ig for certain indications. For other indications, physicians and hospitals regard Ig as far superior to all potential substitutes.

9. Ig constitutes a relevant product market in which to analyze the Acquisition's effects.

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B. Albumin

10. Albumin is used as a blood volume expander and to prime heart valves during surgery, treat burn victims, and replace proteins in treating liver failure.

11. There are no good substitutes for albumin. Physicians and hospitals regard albumin as far superior from a clinical standpoint to any potential alternatives, such as hetastarch and saline products.

12. Albumin constitutes a relevant product market in which to analyze the Acquisition's effects.

C. Plasma-Derived Factor VIII

13. pdFVIII is an essential protein responsible for blood coagulation (*i.e.*, clotting), and products containing pdFVIII are FDA-approved to treat individuals with either Hemophilia A or von Willebrand Disease, or in some instances, both.

14. Recombinant Factor VIII ("rFVIII") is made from non-human sources and can also be used to treat Hemophilia A. Due to perceived differences in safety, rFVIII is the standard of care for previously untreated Hemophilia A patients.

15. For certain treatments, neither rFVIII nor any other product is a clinical substitute for pdFVIII. For example, rFVIII products do not contain von Willebrand Factor and therefore cannot be used to treat von Willebrand disease. Purchasers and patients would not switch from pdFVIII to rFVIII in response to a small but significant and non-transitory increase in price of pdFVIII.

16. pdFVIII constitutes a relevant product market in which to analyze the Acquisition's effects.

V. THE RELEVANT GEOGRAPHIC MARKET

17. The United States is the relevant geographic market in which to analyze the Acquisition's effects. To compete in the

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relevant product markets in the United States, a firm must establish a local sales force, service infrastructure, and reputation among purchasers.

18. Like pharmaceutical products, Ig, albumin, and pdFVIII must be FDA-approved for sale in the United States. To obtain approval, the products must be made from plasma collected in the United States at FDA-approved collection centers. These products must also be manufactured at FDA-approved facilities.

19. Performing the necessary clinical trials and navigating the FDA approval process for plasma and plasma-derived products takes well in excess of two years. Thus, Ig, albumin, and pdFVIII currently sold outside of the United States are not viable competitive alternatives for U.S. customers, who cannot and do not turn to these products even in the event of a price increase for products currently available in the United States.

VI. MARKET STRUCTURE

20. Under the 2010 Department of Justice and Federal Trade Commission Horizontal Merger Guidelines ("Merger Guidelines") and relevant case law, the Acquisition is presumptively unlawful in the Ig and albumin markets. Under the Herfindahl-Hirschman Index ("HHI"), which is the standard measure of market concentration under the Merger Guidelines, an acquisition is presumed to enhance market power if it increases the HHI by more than 200 points and results in a post-acquisition HHI that exceeds 2,500 points. The Acquisition creates market concentration levels well in excess of these thresholds for Ig and albumin.

- a. Based on 2009 sales volume, the combined firm would have approximately 31.2% of the Ig market and face meaningful competition from only two firms: Baxter International, Inc. ("Baxter") and CSL Limited ("CSL"). As of 2009, Baxter and CSL commanded approximately 35% and 25% of the Ig market, respectively, meaning the three largest suppliers would control more than 91% of the market after the Acquisition. According to 2009 sales volume, the

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Acquisition would increase the HHI in the Ig market by 383 points, from 2,518 to 2,901.

- b. In September 2010, another Ig supplier, Octapharma AG ("Octapharma"), withdrew its Ig product from the U.S. market because of concerns about serious adverse events. Before the withdrawal, Octapharma accounted for approximately 8.8% of the Ig market. Now, Octapharma is not selling any Ig in the United States, and its future competitive significance is uncertain.
- c. In addition, the Acquisition would also increase concentration in the albumin market by 333 points, from 2,743 to 3,076, leaving only four meaningful competitors.

21. Under the Merger Guidelines, acquisitions that increase the HHI by between 100 and 200 points and result in a post-acquisition HHI that exceeds 2,500 points raise potentially significant competitive concerns and often warrant scrutiny. Here, the Acquisition would increase the HHI in the pdFVIII market by 166 points, from 3,491 to 3,657, leaving only three meaningful competitors controlling nearly 100% of the market.

VII. ENTRY CONDITIONS

22. Entry into the relevant markets would not be timely, likely, or sufficient to prevent or defeat the Acquisition's likely anticompetitive effects.

23. The manufacturing process for plasma-derived products is complex and highly regulated and involves technical know-how and proprietary processes involving (i) plasma collection, (ii) plasma testing, (iii) fractionation (*i.e.*, precipitation of solids by manipulation of solution pH, temperature, etc.), (iv) finishing or purification, (v) quality control, and (vi) lot release.

24. Currently, the U.S. markets for Ig, albumin, and pdFVIII are controlled by a handful of vertically integrated manufacturers, each of which has its own plasma collection, fractionation, and purification facilities. To be successful, a new entrant must

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develop and produce a product that is at least on par with the incumbent products in terms of safety, efficacy, and reliability. A new entrant – including existing manufacturers outside the United States – also must establish a U.S. sales force, plasma supply, support, manufacturing capability, and a reputation for safety, efficacy, and reliability.

25. Building the necessary facilities and infrastructure to manufacture Ig, albumin, and pdFVIII takes years and costs tens of millions of dollars. In particular, entry into the relevant product markets *de novo* requires a massive commitment of time and resources.

VIII. INDUSTRY BACKGROUND AND THE ACQUISITION'S EFFECTS

26. Historically, the plasma-derived products industry has operated as a tight oligopoly, characterized by a high level of transparency and coordination. Absent relief, Grifols' acquisition of Talecris would eliminate a significant threat to that dynamic.

- a. A decade ago, there was robust competition in the plasma-derived products industry. After supply increases in the early 2000s led to lower prices, producers "rationalized" production and plasma collection capacity and began to vertically integrate, placing plasma collection almost entirely in the control of the few remaining firms in the market. Manufacturers also underwent horizontal consolidation, leading to an industry dominated by three large firms – Baxter, CSL, and Talecris – and two smaller ones – Grifols and Octapharma. In the years that followed, the market saw supply shortages and dramatic year-over-year price increases.
- b. Signaling among suppliers – *i.e.*, intentional sharing of competitive information for purposes of securing accommodating reactions from other firms – allows them to gain real time insight into each other's strategies and plans. Sensitive competitive information is widely available from a vast array of reports, market

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analyses, discussions with downstream purchasers, and the suppliers themselves, as firms collect and catalog an extraordinary wealth of timely "competitive intelligence."

- c. The industry's primary trade group, the Plasma Protein Therapeutics Association ("PPTA"), facilitates this free exchange of competitive intelligence. The PPTA regularly publicizes aggregated plasma collection, inventory, and throughput data for IVIG, albumin, and pdFVIII, among other products.
- d. Manufacturers routinely use PPTA data and other competitive intelligence to calibrate their own collections, output, and pricing decisions and avoid "irrational" behavior, such as oversupplying the market or starting a price war. When this information is combined with the long production cycle for plasma-derived products, suppliers have little opportunity to "cheat" by increasing output, without being detected and potentially punished by other suppliers well in advance of realizing any benefits from such cheating.

27. The Acquisition would substantially lessen competition in the relevant markets in violation of Section 7 of the Clayton Act, as amended, 15 U.S.C. § 18, and Section 5 of the FTC Act, as amended, 15 U.S.C. § 45, in the following ways, among others:

- a. eliminating actual, direct, and substantial competition between Respondents for the sale of Ig, albumin, and pdFVIII in the United States;
- b. enabling the combined firm and other firms selling Ig, albumin, and pdFVIII to engage more successfully and completely in coordinated interaction that harms consumers;
- c. increasing the likelihood that U.S. consumers would be forced to pay higher prices for Ig, albumin, and pdFVIII; and

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- d. increasing the likelihood that consumers would experience lower levels of innovation and service in the U.S. markets for Ig, albumin, and pdFVIII.

IX. VIOLATIONS CHARGED

28. The allegations of Paragraphs 1 through 27 above are incorporated by reference as though fully set forth here.

29. The Acquisition constitutes a violation of Section 5 of the FTC Act, as amended, 15 U.S.C. § 45.

30. The Acquisition, if consummated, would constitute a violation of Section 7 of the Clayton Act, as amended, 15 U.S.C. § 18, and Section 5 of the FTC Act, as amended, 15 U.S.C. § 45.

IN WITNESS WHEREOF, the Federal Trade Commission has caused this Complaint to be signed by its Secretary and its official seal to be hereto affixed, at Washington, D.C., this thirty-first day of May, 2011.

By the Commission, Commissioner Kovacic recused.

DECISION AND ORDER

The Federal Trade Commission ("Commission"), having initiated an investigation of the proposed acquisition of Talecris Biotherapeutics Holdings Corp. ("Respondent Talecris") by Grifols, S.A. ("Respondent Grifols"), and Respondent Grifols and Respondent Talecris having been furnished thereafter with a copy of a draft Complaint that the Bureau of Competition proposed to present to the Commission for its consideration and which, if issued by the Commission, would charge Respondent Grifols and Respondent Talecris with violations of Section 7 of the Clayton

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Act, as amended, 15 U.S.C. § 18, and Section 5 of the Federal Trade Commission Act, as amended, 15 U.S.C. § 45; and

Respondent Grifols and Respondent Talecris, their attorneys, and counsel for the Commission having thereafter executed an Agreement Containing Consent Orders ("Consent Agreement"), containing an admission by Respondent Grifols and Respondent Talecris of all the jurisdictional facts set forth in the aforesaid draft Complaint, a statement that the signing of said Consent Agreement is for settlement purposes only and does not constitute an admission by Respondent Grifols and Respondent Talecris that the law has been violated as alleged in such Complaint, or that the facts as alleged in such Complaint, other than jurisdictional facts, are true, and waivers and other provisions as required by the Commission's Rules; and

The Commission having thereafter considered the matter and having determined that it had reason to believe that Respondent Grifols and Respondent Talecris have violated the said Acts, and that a Complaint should issue stating its charges in that respect, and having thereupon issued its Complaint and an Order to Maintain Assets, and having accepted the executed Consent Agreement and placed such Consent Agreement on the public record for a period of thirty (30) days for the receipt and consideration of public comments, now in further conformity with the procedure described in Commission Rule 2.34, 16 C.F.R. § 2.34, the Commission hereby makes the following jurisdictional findings and issues the following Decision and Order ("Order").

1. Respondent Grifols is a corporation organized, existing and doing business under and by virtue of the laws of Spain with its office and principal place of business at Avinguda de la Generalitat, 152, Parque empresarial Can Sant Joan, 08174 Sant Cugat del Valles, Barcelona, Spain, and with its office and principal place of business in the United States located at 2410 Lillyvale Avenue, Los Angeles, CA 90032.
2. Respondent Talecris is a corporation organized, existing and doing business under and by virtue of the

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laws of Delaware, with its office and principal place of business located at 4101 Research Commons, 79 T.W. Alexander Drive, Research Triangle Park, North Carolina 27709.

3. The Federal Trade Commission has jurisdiction of the subject matter of this proceeding and of Respondent, and the proceeding is in the public interest.

ORDER**I.**

IT IS ORDERED that, as used in this Order, the following definitions shall apply:

- A. "Grifols" means Grifols, S.A., its directors, officers, employees, agents, representatives, successors, and assigns; and its joint ventures, subsidiaries, divisions, groups, and affiliates controlled by Grifols, S.A. (including Talecris, after the Acquisition Date), and the respective directors, officers, employees, agents, representatives, successors, and assigns of each.
- B. "Talecris" means Talecris Biotherapeutics Holdings Corp. its directors, officers, employees, agents, representatives, successors, and assigns; and its joint ventures, subsidiaries, divisions, groups, and affiliates controlled by Talecris Biotherapeutics Holdings Corporation, and the respective directors, officers, employees, agents, representatives, successors, and assigns of each.
- C. "Commission" means the Federal Trade Commission.
- D. "Acquisition" means Respondent Grifols' acquisition of Talecris.
- E. "Acquisition Date" means the date on which the Acquisition is consummated.

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- F. "Acquirer" means the Person specified by name in this Order, or the Person approved by the Commission, to acquire the Divested Business pursuant to Paragraph II or Paragraph VI of this Order.
- G. "Branded Supply Date" means the date that is one hundred twenty (120) days after the Acquisition Date.
- H. "Confidential Business Information" means competitively sensitive, proprietary, and all other information, solely Relating To the Divested Business, that is not in the public domain, owned by or pertaining to a Person or a Person's business, and includes, but is not limited to, all customer lists, price lists, contracts, cost information, marketing methods, technologies, processes, or other trade secrets.
- I. "Contract Manufacturing Agreement" means the agreement that has been approved by the Commission and become a part of the Divestiture Agreement, under which Respondent Grifols and Kedrion have agreed to, among other things, various terms regarding the Manufacturing of Products by Respondent Grifols and the sale of Products by Kedrion.
- J. "Designated Amount of Products" means the confidential amount of liter equivalent Products included in Confidential Exhibit A to this Order.
- K. "Designated Employee" means the named employee, or person filling a particular job description, listed in Confidential Exhibit B to this Order.
- L. "Designated Melville Employee" means the named employee, or person filling a particular job description, listed in Confidential Exhibit B-1 to this Order.
- M. "Development" means all research and development activities, including, without limitation, the following: test method development; stability testing; process development; manufacturing scale-up;

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development-stage manufacturing; quality assurance/quality control development; statistical analysis and report writing; and conducting experiments for the purpose of obtaining any and all product approvals or certifications. "Develop" means to engage in Development.

- N. "Divested Business" means:
1. The Melville Facility;
 2. The Grifols Plasma Centers;
 3. Grifols Plasma;
 4. The Contract Manufacturing Agreement; and
 5. All assets, tangible and intangible, property, facilities, equipment, contracts, and all other requirements necessary to fulfill Grifols' obligations under the Contract Manufacturing Agreement, the Product Agreement, and the Divestiture Agreement.
- O. "Divestiture Agreement" means all the divestiture agreements, licenses, assignments, and other agreements entered into by Respondent Grifols and Kedrion for the sale of the Melville Facility, the Grifols Plasma Centers, Grifols Plasma, the Products Supply Agreements, and all other agreements, leases, transfers, and licenses required by this Order. The Divestiture Agreement is attached as Confidential Exhibit C to this Order.
- P. "Effective Date" means the date on which the divestitures, licensing, and assignments pursuant to Paragraph II or Paragraph VI of this Order, are consummated.
- Q. "FDA Approval Date" means the date on which the FDA grants all approvals necessary for Kedrion to market and sell Private Label Albumin Product and

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Private Label IVIG Product. In the event the FDA approves the marketing and sale by Kedrion of one of the two products before the other, the FDA Approval Date shall be the latter of those two approval dates.

- R. "Grifols Plasma" means normal source plasma, approved by the U.S. Food & Drug Administration ("FDA"), supplied by Grifols, which meets the specifications set forth in Exhibit B to the Contract Manufacturing Agreement.
- S. "Grifols Plasma Centers" means the plasma collection facilities owned and operated by Respondent Grifols at the locations identified in Exhibit D to this Order.
- T. "Kedrion" means Kedrion S.p.A. a corporation organized, existing and doing business under and by virtue of the laws of Italy with its international headquarters located at Loc. Ai Conti, 55051 Castelrechhio Pascoli, Barga (Lucca), Italy and its principal place of business in the United States located at Parker Plaza, 40 Kelby Street, Fort Lee, NJ 07024.
- U. "Manufacture" or "Manufactured" means some or all of the fractionation, purification, formulation, filling, packaging, inspecting, validating and testing of Products, and does not include the commercialization activities including, but not limited to, pricing and price-reporting, sales, marketing, and/or distribution.
- V. "Melville Facility" means the facility owned and operated by Talecris at 155 Duryea Road, Melville, New York 11747, and all machinery, fixtures, equipment, vehicles, transportation and storage facilities, furniture, tools, supplies, stores, spare parts, and other tangible property located at or Relating To that facility.
- W. "Melville Lease Agreement" means any agreement between Respondent Grifols and Kedrion for the lease of the Melville Facility.

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- X. "Melville Lease Termination Date" means the date on which Respondent Grifols terminates its lease of the Melville Facility from Kedrion pursuant to the Melville Lease Agreement.
- Y. "Patents" means all patents, patent applications, including provisional patent applications, invention disclosures, certificates of invention and applications for certificates of invention and statutory invention registrations, in each case existing as of the Acquisition Date, and includes all reissues, additions, divisions, continuations, continuations-in-part, supplementary protection certificates, extensions and reexaminations thereof, all inventions disclosed therein, and all rights therein provided by international treaties and conventions, Related To any product of or owned by Respondent Grifols as of the Acquisition Date.
- Z. "Person" means any natural person, partnership, corporation, association, trust, joint venture, government, government agency, division, or department, or other business or legal entity.
- AA. "Plasma Sales Agreement" means an agreement between Grifols and Kedrion under which Grifols will sell blood plasma to Kedrion.
- BB. "Products" means:
1. Private Label IVIG Product, Koate, or Private Label Albumin Product, in each case that is intended for human use, Manufactured by Grifols, pursuant to instructions by Kedrion and under the terms and conditions of the Contract Manufacturing Agreement; and
 2. Fraction V Paste or Cryoprecipitate, derived from plasma, Manufactured by Grifols for Kedrion pursuant to the Contract Manufacturing

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Agreement, and delivered as intermediates to Kedrion by Grifols.

- CC. "Relating To" or "Related To" means pertaining in any way to, and is not limited to that which pertains exclusively to or primarily to.
- DD. "Remedial Agreement" means the following:
1. the Divestiture Agreement if such agreement has not been rejected by the Commission pursuant to Paragraph II of this Order; and
 2. any agreement between Respondent Grifols and a Commission-approved Acquirer (or between a Divestiture Trustee and a Commission-approved Acquirer) that has been approved by the Commission to accomplish the requirements of this Order, and all amendments, exhibits, attachments, agreements, and schedules thereto, related to the relevant assets to be granted, licensed, delivered or otherwise conveyed, that have been approved by the Commission to accomplish the requirements of this Order.
- EE. "Third Party(ies)" means any Person other than Respondent Grifols, Talecris, Kedrion, or the Acquirer.
- FF. "Trade Dress" means the current trade dress of a particular product or Person including, without limitation, product packaging, logos, and the lettering of the product trade name, brand name, or corporate name.
- GG. "Trademark(s)" means all proprietary names or designations, trademarks, service marks, trade names, and brand names, including registrations and applications for registration therefor (and all renewals, modifications, and extensions thereof) and all common

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law rights, and the goodwill symbolized thereby and associated therewith, for Koate.

[Albumin Definitions]

- HH. "Albumin Manufacturing Agreement" means an agreement between Kedrion and Respondent Grifols, that has been approved by the Commission and become a part of the Divestiture Agreement, under which Respondent Grifols will provide Private Label Albumin Product and Fraction V for Kedrion.
- II. "Albumin Product" means an albumin factor derived from human blood plasma and used, among other things, as a blood volume expander.
- JJ. "Designated Amount of Talecris Albumin Product" means the minimum amount of Talecris Albumin Product to be produced by Respondent Grifols during the Contract Manufacturing Agreement and made available for sale by Kedrion, attached in Confidential Exhibit E-1.
- KK. "Fraction V" means plasma protein factor that predominantly contains albumin.
- LL. "Fraction V Paste" means a plasma intermediate used in the Manufacture of Albumin Product.
- MM. "Plasbumin" means branded Talecris Albumin Product and includes Plasbumin®-5, Albumin (Human) 5%, USP (PDF); Plasbumin®-20, Albumin (Human) 20%, USP (PDF); and Plasbumin®-25, Albumin (Human) 25%, USP (PDF).
- NN. "Private Label Albumin Product" means an Albumin Product identical to, and manufactured according to the FDA-approved process used in the production of, the Talecris Albumin Product.

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- OO. "Talecris Albumin Customer Contracts" means contracts between Talecris and Third Parties, including group purchasing organizations and hospitals, for the sale and purchase of, at a minimum, the Designated Amount of Talecris Albumin Product, including but not limited to, the contracts identified in Confidential Exhibit E.
- PP. "Talecris Albumin Product" means the Albumin Product Developed, manufactured and sold by Talecris in the United States under the brand name Plasbumin.

[IVIG Definitions]

- QQ. "IVIG Product" means an intravenous immune globulin derived from human blood plasma.
- RR. "Designated Amount of Talecris IVIG Product" means minimum amount of Talecris IVIG Product to be produced by Respondent Grifols during the Contract Manufacturing Agreement and made available for sale by Kedrion, and designated in Confidential Exhibit F-1.
- SS. "Gamunex" means branded Talecris IVIG Product.
- TT. "Private Label IVIG Product" means intravenous immune globulin derived from human blood plasma identical to, and manufactured according to the FDA-approved process used in the production of, the Talecris IVIG Product.
- UU. "Talecris IVIG Customer Contracts" means contracts between Talecris and Third Parties, including group purchasing organizations and hospitals, for the sale and purchase of at least the Designated Amount of Talecris IVIG Product including, but not limited to, the contracts identified in Confidential Exhibit F.

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- VV. "Talecris IVIG Product" means the IVIG Product Developed, manufactured and sold by Talecris in the United States under the brand name Gamunex.

[Koate Definitions]

- WW. "Cryoprecipitate" means a product derived from fresh frozen plasma containing coagulation factors.
- XX. "Factor VIII Product" means an antihemophilic factor derived from Cryoprecipitate used in the treatment of, among other things, hemophilia A.
- YY. "Koate" means the Factor VIII Product sold under the Talecris registered brand name Koate.
- ZZ. "Koate Option, License and Sale Agreement" means the agreement between Respondent Grifols and Kedrion granting to Kedrion, among other things, the exclusive rights to sell branded Koate in the United States and the option to acquire non-exclusive rights to manufacture branded Koate in the United States, Italy, and Hungary.
- AAA. "Koate Customer Contracts" means all contracts between Talecris and a third party for the purchase and sale of Koate in the United States including, but not limited to, the contracts identified in Confidential Exhibit G.
- BBB. "Koate Intellectual Property" means all of the following Related To Koate:
1. all Talecris intellectual property used in the Development, manufacturing, storage, distribution and sale of Koate including, but not limited to:
 - a. Koate Manufacturing Copyrights;
 - b. Software;

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- c. computer programs;
 - d. Patents including, but not limited to, the right to obtain and file for Patents and Koate Sales and Manufacturing Copyrights, and registrations thereof;
 - e. licenses including, but not limited to, licenses to third-party Software if transferable and sub-licenses to Software modified by Respondent Talecris;
 - f. know-how (including, but not limited to, flow sheets, process and instrumentation), diagrams, risk analysis, certificates of analysis, goodwill, technology (including, but not limited to, equipment specifications), drawings, utility models, designs, design rights, techniques, data, inventions, practices, recipes, raw material specifications, process descriptions;
 - g. technical information (including, but not limited to, material and final product specifications);
 - h. protocols (including, but not limited to, operational manuals);
 - i. quality control information and methods, and other confidential or proprietary technical, business, Development and other information;
 - j. trade secrets; and
 - k. all rights to limit the use or disclosure thereof trade names, service marks, logos, and the modifications or improvements to such intellectual property; and
2. rights to sue and recover damages or obtain injunctive relief for infringement, dilution,

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misappropriation, violation or breach of any of the foregoing.

- CCC. "Koate Manufacturing Copyrights" means copyrights in all process development data and reports Relating To the research and development of Koate, or of any materials used in the research, Development, manufacture, manufacturing records, manufacturing processes, and supplier lists; all copyrights in data contained in laboratory notebooks Relating To Koate; all copyrights in analytical and quality control data; and all correspondence with governmental agencies.
- DDD. "Koate Sales Copyrights" means rights to all original works of authorship of any kind directly Related To the sale of Koate in the United States, and any registrations and applications for registrations thereof, including, but not limited to, the following: all such rights with respect to all promotional, marketing, sales, and advertising materials, educational and training materials for the sales force, and sales forecasting models; marketing or sale of Koate including copyrights in all raw data, statistical programs developed (or modified in a manner material to the use or function thereof (other than through user preferences)) to analyze research data, market research data, market intelligence reports and statistical programs (if any) used for marketing and sales research; all copyrights in customer information; all copyrights in records, including customer lists, sales force call activity reports, vendor lists, and sales data.

II.

IT IS FURTHER ORDERED that:

- A. Within ten (10) days of the Acquisition Date, Respondent Grifols shall divest the Melville Facility, the Grifols Plasma Centers, and Grifols Plasma, enter into the Contract Manufacturing Agreement, the Product Agreement, the Koate Option, License and

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Sale Agreement, assign or extend rights and obligations under the Koate Customer Contracts, the Talecris Albumin Customer Contracts, and the Talecris IVIG Customer Contracts, absolutely and in good faith, to Kedrion, pursuant to, and in accordance with, the Divestiture Agreement. The Divestiture Agreement (which shall include, among other things, the sale and purchase agreements for the Melville Facility, the Grifols Plasma Centers, and Grifols Plasma, the assignments, licenses, supply agreements, and all other agreements between Respondent Grifols and Kedrion) between Respondent Grifols and Kedrion shall not vary or contradict, or be construed to vary or contradict, the terms of this Order, it being understood that nothing in this Order shall be construed to reduce any rights or benefits of Kedrion, or to reduce any obligations of Respondent Grifols under such agreements, and such agreements, if approved by the Commission, shall be incorporated by reference into this Order and made a part hereof.

Provided, however, that Respondent Grifols shall be allowed, pursuant to the Divestiture Agreement, to enter into a Melville Facility Lease Agreement with Kedrion under which, for a period of no more than four (4) years from the Acquisition Date, Respondent Grifols will lease back the Melville Facility from Kedrion. Such agreement, if approved by the Commission, shall be a part of the Divestiture Agreement and incorporated into this Order and made a part hereof.

Provided, however, if, at the time the Commission determines to make this Order final, the Commission notifies Respondent Grifols that Kedrion is not an acceptable Acquirer then, after receipt of such written notification: (1) Respondent Grifols shall immediately notify Kedrion of the notice received from the Commission and shall as soon as practicable effect the rescission of the Divestiture Agreement; and (2) Respondent Grifols shall, within one-hundred-fifty

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(150) days from the date this Order becomes final, divest the Divested Business, enter into manufacturing and distribution agreements, assign or extend rights and obligations under customer contracts, and divest any other assets or enter into any other relief required to satisfy the purposes of this Order, absolutely and in good faith, at no minimum price, to or with an Acquirer, that receives the prior approval of the Commission, and in a manner that receives the prior approval of the Commission;

Provided further, however, that if Respondent Grifols has complied with the terms of Paragraphs II.A., II.B., and II.C. before the date on which this Order becomes final, and if, at the time the Commission determines to make this Order final, the Commission notifies Respondent Grifols that the manner in which the divestiture and assignments were accomplished is not acceptable, the Commission may direct Respondent Grifols, or appoint a Divestiture Trustee, to effect such modifications to the manner of divestiture and assignments including, but not limited to, entering into additional agreements or arrangements, as the Commission may determine are necessary to satisfy the requirements of this Order.

- B. Prior to the Effective Date, Respondent Grifols shall secure all consents and waivers from all Third Parties, other than the FDA, including customers whose contracts are being assigned or extended to Kedrion pursuant to Paragraph II.A., that are necessary to permit Kedrion to sell Private Label Albumin Product, Private Label IVIG Product, and Koate.

Provided, however, Respondent may satisfy this requirement by certifying that the Acquirer has executed all such agreements directly with each of the relevant Third Parties.

- C. Respondent Grifols shall Manufacture the Designated Amount of Products, as set forth in Confidential

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Exhibits A, E-1, and F-1, annually for Kedrion to market and sell such Products, and Kedrion will take or pay for such Designated Amount of Products Manufactured by Grifols for seven (7) years beginning the day after the FDA Approval Date or the Effective Date, which ever date is later;

Provided, however, that in the event Kedrion is not approved by the FDA to market and sell Private Label Albumin Product or Private Label IVIG Product by the Branded Supply Date, then, for purposes of Paragraph II.C., Respondent Grifols shall: (1) Manufacture Plasbumin and Gamunex for Kedrion; (2) supply Kedrion with sufficient inventory of Plasbumin and Gamunex so it can begin supplying customers with Plasbumin and Gamunex no later than three days after the Branded Supply Date, and (3) continue to supply Kedrion with Plasbumin and Gamunex so it can market and sell in the amounts set forth in Confidential Exhibits A, E-1, and F-1 of this Order.

Provided further, however, that in the event Respondent Grifols is required to supply Kedrion with Plasbumin and Gamunex, the requirements of Paragraph II.C. shall begin no later than the Branded Supply Date, and continue until the earlier of (a) the FDA Approval Date, or (b) seven (7) years after the Branded Supply Date. In the event the Branded Supply Date occurs before the Effective Date, then, for purposes of section (b) of this proviso, it shall be seven (7) years after the Effective Date. If FDA Approval is granted for Kedrion to market and sell the Private Label Albumin Product or the Private Label IVIG Product, then Respondent Grifols shall begin supplying Kedrion those private label products pursuant to Paragraph II.C. in place of Plasbumin or Gamunex, respectively.

Provided further, however, that in no event shall the seven (7) year obligations of Paragraph II.C. extend

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longer than seven (7) years after the Branded Supply Date or the Effective Date, whichever is later.

Provided further, however, that respondent grifols and respondent talecris, with assistance from the monitor, shall use all reasonable efforts to expedite all fda approvals necessary for kedrion to market and sell private label albumin product and private label ivig product.

- D. Respondent Grifols shall divest or otherwise transfer to Kedrion:
1. The exclusive right to sell Koate in the United States;
 2. The exclusive rights to the use of all Trade Dress, brand names, Trademarks, and Koate Sales Copyrights Relating To Koate in the United States, including the exclusive rights to use the brand name Koate and its derivatives in the United States;
 3. All sales and promotional materials used in the United States for the sale of Koate in the United States;
 4. At Kedrion's option and within five (5) years of the Acquisition Date, a non-exclusive license to Koate Intellectual Property for use in Koate at a price agreed to in the Divestiture Agreement;
 5. The right to sell the Private Label Albumin Product, or Plasbumin, if required pursuant to the Order, in the United States;
 6. The right to rebrand and use all current Talecris marketing materials Relating To Talecris Albumin Product;

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7. The right to sell the Private Label IVIG Product, or Gamunex, if required pursuant to the Order, in the United States; and
 8. The right to rebrand and use all current Talecris marketing materials Relating To the Talecris IVIG Product.
- E. Respondent Grifols shall include, as part of the Divestiture Agreement, any service agreement in which Respondent Grifols contemplates providing services or assistance it will provide Kedrion for the duration of the period described in Paragraph II.C., including scope of services, term, prices, and personnel involved.
- F. Any Remedial Agreement that has been approved by the Commission between Respondent Grifols (or a Divestiture Trustee) and a Commission-approved Acquirer shall be deemed incorporated into this Order, and any failure by Respondent Grifols to comply with any term of such Remedial Agreement shall constitute a failure to comply with this Order.
- G. Respondent Grifols shall not terminate any agreement that is part of the Divestiture Agreement before the end of the term approved by the Commission without:
1. the written agreement of Kedrion or the Acquirer and thirty (30) days prior notice to the Commission; or,
 2. in the case of a proposed unilateral termination by Respondent Grifols due to an alleged breach of an agreement by the Kedrion or the Acquirer, sixty (60) days notice of such termination. *Provided, however,* such sixty (60) days notice shall be given only after the parties have:
 - a. attempted to settle the dispute between themselves, and

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- b. either engaged in arbitration and received an arbitrator's decision, or received a final court decision after all appeals.
- H. The purposes of this Paragraph II of the Order are: (1) to ensure that the Acquirer will have the intention and ability to produce and sell Koate, Private Label Albumin Product, and Private Label IVIG Product independently of Respondent Grifols; (2) to ensure continued sales and distribution of Koate until such time as the Acquirer has the ability to produce a Factor VIII Product at its own facilities; (3) to ensure that the Acquirer has the ability to sell and distribute Private Label Albumin Product and Private Label IVIG Product until such time as the Acquirer has the ability to produce an Albumin Product and an IVIG Product at its own facilities; and (4) to remedy the lessening of competition resulting from the Acquisition as alleged in the Commission's Complaint.

III.**IT IS FURTHER ORDERED** that:

- A. Except in the course of performing its obligations under the Divestiture Agreement or as expressly allowed pursuant to this Order, Respondent Grifols and Respondent Talecris shall not
 1. Interfere with any suppliers, distributors, resellers, or customers of the Persons who will acquire or have acquired the Divested Business;
 2. Interfere with any contracts that will be divested, have been divested, will be assigned or extended to the Acquirer, or have been assigned or extended to the Acquirer pursuant to this Order; or
 3. Interfere in any other way with the Persons who will acquire or have acquired the Divested

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Business pursuant to this Order or with the businesses that will be divested or have been divested pursuant to this Order.

Provided however, that unless otherwise prohibited by the Order as part of contract assignments, nothing in this Paragraph III.A. shall prevent Respondent Grifols from competing for contracts or for the trade of suppliers, distributors, resellers, or customers.

- B. During the time period before the Effective Date and before the Designated Employees are hired pursuant to Paragraph VII , Respondent Grifols and Respondent Talecris shall:
1. take such actions as are necessary to maintain the full economic viability, marketability and competitiveness of the Divested Business to minimize any risk of loss of competitive potential for the Divested Business, and to prevent the destruction, removal, wasting, deterioration, or impairment of the Divested Business, except for ordinary wear and tear. Respondent Grifols and Respondent Talecris shall not sell, transfer, encumber or otherwise impair the Divested Business (other than in the manner prescribed in this Order), nor take any action that lessens the full economic viability, marketability or competitiveness of the Divested Business. Respondent Talecris shall take all actions reasonably necessary to protect its Trademarks and trade dress to be transferred to Kedrion from Third Party complaints or challenges.
 2. retain all of Respondent Grifols' and Respondent Talecris' rights, title, and interest in the Divested Business;
 3. maintain the operations of the Divested Business in the regular and ordinary course of business and in accordance with past practice (including regular

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repair and maintenance of the assets, as necessary) and/or as may be necessary to preserve the marketability, viability, and competitiveness of the Divested Business and shall use its best efforts to preserve the existing relationships with the following: suppliers, vendors, distributors, customers, governmental agencies, employees, and others having business relations with the Divested Business.

4. maintain a work force as large as, and with equivalent or better training and expertise to, what has been associated with the Divested Business as of the Acquisition Date.
 5. provide Designated Employees with reasonable financial incentives to continue in their positions and to Develop, and manufacture the Divested Products consistent with past practices and/or as may be necessary to preserve the marketability, viability and competitiveness of the Divested Products pending divestiture. Such incentives shall include a continuation of all employee benefits offered by Respondent Grifols and Respondent Talecris until the Effective Date has occurred, including regularly scheduled raises, bonuses, vesting of pension benefits (as permitted by law), and additional incentives as may be necessary to prevent any diminution of the competitiveness of the Divested Business.
- C. During the time period before the Melville Lease Termination Date, Respondent Grifols and Respondent Talecris shall provide Designated Melville Employees with reasonable financial incentives to continue in their positions. Such incentives shall include a continuation of all employee benefits offered by Respondent Grifols and Respondent Talecris until the Melville Lease Termination Date has occurred, including regularly scheduled raises, bonuses, vesting of pension benefits (as permitted by law), and

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additional incentives as may be necessary to prevent any diminution of the competitiveness of the Melville Facility.

- D. The purpose of this Paragraph III is to maintain the full economic viability, marketability and competitiveness of the Divested Business until the Effective Date, to minimize any risk of loss of competitive potential for the Divested Business, and to prevent the destruction, removal, wasting, deterioration, or impairment of the Divested Business, except for ordinary wear and tear.

IV.**IT IS FURTHER ORDERED** that:

- A. Except in the course of performing its obligations under the Divestiture Agreement, or as expressly allowed pursuant to this Order:
1. Respondent Grifols shall not provide, disclose or otherwise make available any Confidential Business Information, including the terms of the Divestiture Agreement, to any Person; and
 2. Respondent Grifols shall not use any Confidential Business Information, including the terms of the Divestiture Agreement, for any reason or purpose. Among other things, Respondent Grifols shall not use such Confidential Business Information:
 - a. to assist or inform Respondent Grifols employees who Develop, manufacture, solicit for sale, sell, or service Respondent Grifols products that compete with the products divested, sold, or distributed pursuant to this Order;
 - b. to interfere with any suppliers, distributors, resellers, or customers of the Persons who acquired the divested businesses;

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- c. to interfere with any contracts divested, assigned, or extended to the Acquirer pursuant to this Order; or
 - d. to interfere in any other way with the Persons who acquired the divested businesses pursuant to this Order or with the businesses divested pursuant to this Order.
- B. The requirements of this Paragraph IV do not apply to Confidential Business Information that Respondent Grifols demonstrates to the satisfaction of the Commission, in its sole discretion:
1. was or becomes generally available to the public other than as a result of a disclosure by Respondent Grifols;
 2. is necessary to be included in mandatory regulatory filings; *provided, however*, that Respondent Grifols shall make all reasonable efforts to maintain the confidentiality of such information in the regulatory filings;
 3. was available, or becomes available, to Respondent Grifols on a non-confidential basis, but only if, to the knowledge of Respondent Grifols, the source of such information is not in breach of a contractual, legal, fiduciary, or other obligation to maintain the confidentiality of the information;
 4. is consented to by the Acquirer;
 5. is necessary information exchanged in the course of consummating the Acquisition;
 6. is disclosed in complying with this Order;
 7. is information the disclosure of which is necessary to allow Respondents to comply with the

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requirements and obligations of the laws of the United States and other countries;

8. is disclosed in defending legal claims, investigations or enforcement actions threatened or brought against Respondents or the Divested Business; or
9. is disclosed in obtaining legal advice.

V.**IT IS FURTHER ORDERED** that:

- A. Mr. R. Owen Richards, President of Quantic Regulatory Services, LLC, shall serve as the Monitor pursuant to the agreement executed by the Monitor and Respondent Grifols and attached as Exhibit H ("Monitor Agreement") and Confidential Exhibit H-1 (Monitor Compensation). The Monitor is appointed to assure that Respondent Grifols expeditiously complies with all of its obligations and performs all of its responsibilities as required by this Order.
- B. The Monitor Agreement shall require that, no later than one (1) day after the Acquisition Date, Respondent Grifols transfers to the Monitor all rights, powers, and authorities necessary to permit the Monitor to perform his duties and responsibilities, pursuant to this Order and the Asset Maintenance Order, and consistent with the purposes of this Order.
- C. No later than one (1) day after the Acquisition Date, Respondent Grifols shall, pursuant to the Monitor Agreement, transfer to the Monitor all rights, powers, and authorities necessary to permit the Monitor to perform his duties and responsibilities, pursuant to and consistent with, the purposes of the Decision and Order.

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- D. Respondent Grifols shall consent to the following terms and conditions regarding the powers, duties, authorities, and responsibilities of the Monitor:
1. The Monitor shall have the power and authority to monitor Respondent Grifols' compliance with the terms of the Order, and shall exercise such power and authority and carry out the duties and responsibilities of the Monitor in a manner consistent with the purposes of the Order and in consultation with the Commission including, but not limited to:
 - a. Assuring that Respondent Grifols expeditiously complies with all of its obligations and performs all of its responsibilities as required by this Order; and
 - b. Monitoring any agreements between Respondent Grifols and the Acquirer.
 2. The Monitor shall act in a fiduciary capacity for the benefit of the Commission.
 3. Subject to any demonstrated legally recognized privilege, the Monitor shall have full and complete access to Respondent Grifols' personnel, books, documents, records kept in the normal course of business, facilities and technical information, and such other relevant information as the Monitor may reasonably request, Related To Respondent Grifols' compliance with its obligations under the Order. Respondent Grifols shall cooperate with any reasonable request of the Monitor and shall take no action to interfere with or impede the Monitor's ability to monitor Respondent Grifols' compliance with the Order.
 4. The Monitor shall serve, without bond or other security, at the expense of Respondent Grifols on such reasonable and customary terms and

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conditions as the Commission may set. The Monitor shall have authority to employ, at the expense of Respondent Grifols, such consultants, accountants, attorneys and other representatives and assistants as are reasonably necessary to carry out the Monitor's duties and responsibilities. The Monitor shall account for all expenses incurred, including fees for services rendered, subject to the approval of the Commission.

5. Respondent Grifols shall indemnify the Monitor and hold the Monitor harmless against any losses, claims, damages, liabilities, or expenses arising out of, or in connection with, the performance of the Monitor's duties, including all reasonable fees of counsel and other reasonable expenses incurred in connection with the preparations for, or defense of, any claim, whether or not resulting in any liability, except to the extent that such losses, claims, damages, liabilities, or expenses result from gross negligence, malfeasance, willful or wanton acts, or bad faith by the Monitor.
 6. The Monitor Agreement shall provide that within one (1) month from the date the Monitor is appointed pursuant to this paragraph, and every sixty (60) days thereafter, the Monitor shall report in writing to the Commission concerning performance by Respondent Grifols of its obligations under the Order.
 7. Respondent Grifols may require the Monitor and each of the Monitor's consultants, accountants, attorneys, and other representatives and assistants to sign a customary confidentiality agreement; *provided, however*, such agreement shall not restrict the Monitor from providing any information to the Commission.
- E. The Commission may, among other things, require the Monitor and each of the Monitor's consultants,

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accountants, attorneys, and other representatives and assistants to sign an appropriate confidentiality agreement relating to Commission materials and information received in connection with the performance of the Monitor's duties.

- F. If the Commission determines that the Monitor has ceased to act or failed to act diligently, the Commission may appoint a substitute Monitor:
1. The Commission shall select the substitute Monitor, subject to the consent of Respondent Grifols, which consent shall not be unreasonably withheld. If Respondent Grifols has not opposed, in writing, including the reasons for opposing, the selection of a proposed Monitor within ten (10) days after notice by the staff of the Commission to Respondent Grifols of the identity of any proposed Monitor, Respondent Grifols shall be deemed to have consented to the selection of the proposed Monitor.
 2. Not later than ten (10) days after appointment of the substitute Monitor, Respondent Grifols shall execute an agreement that, subject to the prior approval of the Commission, confers on the Monitor all the rights and powers necessary to permit the Monitor to monitor Respondent Grifols' compliance with the relevant terms of the Order in a manner consistent with the purposes of the Order.
- G. The Commission may on its own initiative, or at the request of the Monitor, issue such additional orders or directions as may be necessary or appropriate to assure compliance with the requirements of the Order.
- H. A Monitor appointed pursuant to this Order may be the same person appointed as the Divestiture Trustee pursuant to the relevant provisions of this Order.

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VI.**IT IS FURTHER ORDERED** that:

- A. If Respondent Grifols has not fully complied with the obligations as required by Paragraph II of this Order, the Commission may appoint a Divestiture Trustee to divest the Melville Facility and the Grifols Plasma Centers (if not divested), enter into a Plasma Sales Contract, Product Manufacturing Agreements, and any other agreements, assignments, and licenses, in a manner that satisfies the requirements of this Order. In the event that the Commission or the Attorney General brings an action pursuant to § 5(l) of the Federal Trade Commission Act, 15 U.S.C. § 45(l), or any other statute enforced by the Commission, Respondent Grifols shall consent to the appointment of a Divestiture Trustee in such action to effectuate the divestitures and other obligations as described in Paragraphs II, III, and IV. Neither the appointment of a Divestiture Trustee nor a decision not to appoint a Divestiture Trustee under this Paragraph VI shall preclude the Commission or the Attorney General from seeking civil penalties or any other relief available to it, including a court-appointed Divestiture Trustee, pursuant to § 5(l) of the Federal Trade Commission Act, or any other statute enforced by the Commission, for any failure by Respondent Grifols to comply with this Order.
- B. The Commission shall select the Divestiture Trustee, subject to the consent of Respondent Grifols, which consent shall not be unreasonably withheld. The Divestiture Trustee shall be a person with experience and expertise in acquisitions and divestitures. If Respondent Grifols has not opposed, in writing, including the reasons for opposing, the selection of any proposed Divestiture Trustee within ten (10) days after notice by the staff of the Commission to Respondent Grifols of the identity of any proposed Divestiture Trustee, Respondent Grifols shall be deemed to have

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consented to the selection of the proposed Divestiture Trustee.

- C. Not later than ten (10) days after the appointment of a Divestiture Trustee, Respondent Grifols shall execute a trust agreement that, subject to the prior approval of the Commission, transfers to the Divestiture Trustee all rights and powers necessary to permit the Divestiture Trustee to effectuate the divestitures required by this Order.
- D. If a Divestiture Trustee is appointed by the Commission or a court pursuant to this Paragraph VI, Respondent Grifols shall consent to the following terms and conditions regarding the Divestiture Trustee's powers, duties, authority, and responsibilities:
1. Subject to the prior approval of the Commission, the Divestiture Trustee shall have the exclusive power and authority to divest the Melville Facility and the Grifols Plasma Centers, enter into a Plasma Sales Contract, Product Manufacturing Agreements, and all other agreements, licenses and assignments as described in Paragraph II of this Order.
 2. The Divestiture Trustee shall have one (1) year after the date the Commission approves the trust agreement described herein to divest the Melville Facility and the Grifols Plasma Centers, enter into a Plasma Sales Contract, Product Manufacturing Agreements, and all other agreements, licenses and assignments as described in Paragraph II of this Order, absolutely and in good faith, at no minimum price, to one or more acquirers that receive the prior approval of the Commission and in a manner that receives the prior approval of the Commission. If, however, at the end of the one (1) year period, the Divestiture Trustee has submitted a plan of divestiture or believes that the divestiture can be

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achieved within a reasonable time, the divestiture period or periods may be extended by the Commission; *provided, however*, the Commission may extend the divestiture period only two (2) times.

3. Subject to any demonstrated legally recognized privilege, the Divestiture Trustee shall have full and complete access to the personnel, books, records and facilities related to the relevant assets that are required to be divested by this Order and to any other relevant information, as the Divestiture Trustee may request. Respondent Grifols shall develop such financial or other information as the Divestiture Trustee may request and shall cooperate with the Divestiture Trustee. Respondent Grifols shall take no action to interfere with or impede the Divestiture Trustee's accomplishment of the divestiture. Any delays in divestiture caused by Respondent Grifols shall extend the time for divestiture under this Paragraph VI in an amount equal to the delay, as determined by the Commission.
4. The Divestiture Trustee shall use best efforts to negotiate the most favorable price and terms available in each contract that is submitted to the Commission, subject to Respondent Grifols' absolute and unconditional obligation to divest expeditiously and at no minimum price. The divestiture shall be made in the manner and to an acquirer as required by this Order.

Provided, however, if the Divestiture Trustee receives bona fide offers from more than one acquiring entity for assets and businesses to be divested pursuant to Paragraph II and if the Commission determines to approve more than one such acquiring entity, the Divestiture Trustee shall divest to the acquiring entity selected by

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Respondent Grifols from among those approved by the Commission;

Provided further, however, that Respondent Grifols shall select such entity within five (5) days after receiving notification of the Commission's approval.

5. The Divestiture Trustee shall serve, without bond or other security, at the cost and expense of Respondent Grifols, on such reasonable and customary terms and conditions as the Commission or a court may set. The Divestiture Trustee shall have the authority to employ, at the cost and expense of Respondent Grifols, such consultants, accountants, attorneys, investment bankers, business brokers, appraisers, and other representatives and assistants as are necessary to carry out the Divestiture Trustee's duties and responsibilities. The Divestiture Trustee shall account for all monies derived from the divestiture and all expenses incurred. After approval by the Commission of the account of the Divestiture Trustee, including fees for the Divestiture Trustee's services, all remaining monies shall be paid at the direction of Respondent Grifols, and the Divestiture Trustee's power shall be terminated. The compensation of the Divestiture Trustee shall be based at least in significant part on a commission arrangement contingent on the divestiture of all of the relevant assets that are required to be divested by this Order.
6. Respondent Grifols shall indemnify the Divestiture Trustee and hold the Divestiture Trustee harmless against any losses, claims, damages, liabilities, or expenses arising out of, or in connection with, the performance of the Divestiture Trustee's duties, including all reasonable fees of counsel and other expenses incurred in connection with the preparation for, or defense of, any claim, whether

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or not resulting in any liability, except to the extent that such losses, claims, damages, liabilities, or expenses result from gross negligence, malfeasance, willful or wanton acts, or bad faith by the Divestiture Trustee.

7. The Divestiture Trustee shall have no obligation or authority to operate or maintain the relevant assets required to be divested by this Order.
 8. The Divestiture Trustee shall act in a fiduciary capacity for the benefit of the Commission.
 9. The Divestiture Trustee shall report in writing to Respondent Grifols and to the Commission every sixty (60) days concerning the Divestiture Trustee's efforts to accomplish the divestiture.
 10. Respondent Grifols may require the Divestiture Trustee and each of the Divestiture Trustee's consultants, accountants, attorneys and other representatives and assistants to sign a customary confidentiality agreement; *provided, however*, such agreement shall not restrict the Divestiture Trustee from providing any information to the Commission.
 11. The Commission may, among other things, require the Divestiture Trustee and each of the Divestiture Trustee's consultants, accountants, attorneys, and other representatives and assistants to sign an appropriate confidentiality agreement relating to Commission materials and information received in connection with the performance of the Divestiture Trustee's duties.
- E. If the Commission determines that a Divestiture Trustee has ceased to act or failed to act diligently, the Commission may appoint a substitute Divestiture Trustee in the same manner as provided in this Paragraph VI.

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- F. The Commission or, in the case of a court-appointed Divestiture Trustee, the court, may on its own initiative or at the request of the Divestiture Trustee issue such additional orders or directions as may be necessary or appropriate to accomplish the obligations under Paragraph II of this Order.
- G. The Divestiture Trustee(s) appointed pursuant to Paragraph VI of this Order may be the same Person appointed as the Monitor pursuant to Paragraph V of this Order.

VII.**IT IS FURTHER ORDERED** that:

- A. Beginning no later than: (a) the Acquisition Date and continuing until ninety (90) days after the Effective Date for Designated Employees, and (b) ninety (90) days before the Melville Lease Termination Date for Designated Melville Employees, Respondent Grifols shall, in a manner consistent with local labor laws:
 - 1. facilitate employment interviews between each Designated Employee or Designated Melville Employee, as applicable, and the Acquirer, including providing the names and contact information for such employees and allowing such employees reasonable opportunity to interview with the Acquirer and shall not discourage such employee from participating in such interviews;
 - 2. not interfere in employment negotiations between each Designated Employee or Designated Melville Employee, as applicable, and the Acquirer;
 - 3. with respect to each Designated Employee or Designated Melville Employee, as applicable, who receives an offer of employment from the Acquirer:

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- a. not prevent, prohibit, or restrict, or threaten to prevent, prohibit, or restrict the Designated Employee or Designated Melville Employee, as applicable, from being employed by the Acquirer, and shall not offer any incentive to the Designated Employee or Designated Melville Employee, as applicable, to decline employment with the Acquirer.
- b. cooperate with the Acquirer in effecting transfer of the Designated Employee or Designated Melville Employee, as applicable, to the employ of the Acquirer, if the Designated Employee or Designated Melville Employee, as applicable, accepts an offer of employment from the Acquirer.
- c. eliminate any contractual provisions, non-compete, or other restrictions entered into or imposed by Respondent Grifols that would otherwise prevent or discourage the Designated Employee or Designated Melville Employee, as applicable, from being employed by the Acquirer.
- d. eliminate any confidentiality restrictions that would prevent the Designated Employee or Designated Melville Employee, as applicable, who accepts employment with the Acquirer from using or transferring to the Acquirer any information Relating To the production and sales of Koate, the Private Label Albumin Product, or the Private Label IVIG Product.
- e. unless alternative arrangements are agreed upon with the Acquirer, retain the obligation to pay the benefits of any Designated Employee or Designated Melville Employee, as applicable, who accepts employment with the Acquirer including, but not limited to, all

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accrued bonuses, vested pensions, and other accrued benefits.

- B. Respondent Grifols shall not, for a period of two (2) years following the Effective Date for Designated Employees, or the Melville Lease Termination Date for Designated Melville Employees, respectively, directly or indirectly, solicit, induce, or attempt to solicit or induce any Designated Employee or Designated Melville Employee, as applicable, who is employed by the Acquirer to terminate his or her employment relationship with the Acquirer;

Provided, however, Respondent Grifols may place general advertisements for employees including, but not limited to, in newspapers, trade publications, websites, or other media not targeted specifically at the Acquirer's employees;

Provided further, however, Respondent Grifols may hire Designated Employees or Designated Melville Employee who apply for employment with Respondent Grifols as long as such employees were not solicited by Respondent Grifols in violation of this Paragraph.

VIII.

IT IS FURTHER ORDERED that for a period of ten (10) years from the date this Order becomes final, Respondent Grifols shall not, without providing advance written notification to the Commission in the manner described in this Paragraph VIII, directly or indirectly, acquire:

- A. any stock, share capital, equity, or other interest in any Person, corporate or non-corporate, that produces, designs, manufactures, or sells Factor VIII Product, Albumin Product, or IVIG Product in or into the United States; or

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- B. any assets used at any time after the acquisition, or during the six (6) month period prior to the acquisition, in the design, manufacture, production, or sale of Factor VIII Product, Albumin Product, or IVIG Product in or into the United States.

Said notification shall be given on the Notification and Report Form set forth in the Appendix to Part 803 of Title 16 of the Code of Federal Regulations as amended (herein referred to as "the Notification"), and shall be prepared and transmitted in accordance with the requirements of that part, except that no filing fee will be required for any such notification, notification shall be filed with the Secretary of the Commission, notification need not be made to the United States Department of Justice, and notification is required only of Respondent Grifols and not of any other party to the transaction. Respondent Grifols shall provide the Notification to the Commission at least thirty days prior to consummating the transaction (hereinafter referred to as the "first waiting period"). If, within the first waiting period, representatives of the Commission make a written request for additional information or documentary material (within the meaning of 16 C.F.R. § 803.20), Respondent Grifols shall not consummate the transaction until thirty days after submitting such additional information or documentary material. Early termination of the waiting periods in this paragraph may be requested and, where appropriate, granted by letter from the Bureau of Competition.

Provided, however, that prior notification shall not be required by this paragraph for a transaction for which Notification is required to be made, and has been made, pursuant to Section 7A of the Clayton Act, 15 U.S.C. § 18a.

Provided further, however, that prior notification shall not be required by this Paragraph VIII for any acquisition after which Respondent Grifols would hold no more than one percent of the outstanding securities or other equity interest in any Person described in this Paragraph VIII.

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IX.**IT IS FURTHER ORDERED** that:

- A. Within thirty (30) days after the date this Order becomes final, and every thirty (30) days thereafter until Respondent Grifols has fully complied with Paragraph II.A. of this Order, Respondent Grifols shall submit to the Commission a verified written report setting forth in detail the manner and form in which it intends to comply, is complying, and has complied with this Order. Respondent Grifols shall submit at the same time a copy of its report concerning compliance with this Order to the Monitor or Divestiture Trustee, if any Divestiture Trustee has been appointed pursuant to this Order. Respondent Grifols shall include in its report, among other things that are required from time to time, a full description of the efforts being made to comply with the relevant Paragraphs of the Order, including a description of all substantive contacts or negotiations related to the divestiture of the relevant assets and the identity of all parties contacted. Respondent Grifols shall include in its report copies of all written communications to and from such parties, all internal memoranda, and all reports and recommendations concerning completing the obligations.
- B. Beginning twelve (12) months after the date this Order becomes final, and annually thereafter on the anniversary of the date this Order becomes final, for the next nine (9) years, Respondent Grifols shall submit to the Commission a verified written report setting forth in detail the manner and form in which it has complied, is complying, and will comply with this Order. Respondent Grifols shall include in its compliance reports, among other things that are required from time to time, a full description of the efforts being made to comply with the Order and copies of all written communications to and from all persons Relating To this Order. Additionally,

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Respondent Grifols shall include in its compliance report whether or not it made any notifiable acquisitions pursuant to Paragraph VIII. Respondent Grifols shall include a description of such acquisitions including, but not limited to, the identity of the Person or assets acquired, the location of the Person or assets, and a detailed description of the assets or Person and its Factor VIII Product, Albumin Product, or IVIG Product sales or manufacturing.

X.

IT IS FURTHER ORDERED that Respondent Grifols shall notify the Commission at least thirty (30) days prior to any proposed:

- A. dissolution of the Respondent Grifols;
- B. acquisition of, merger with, or consolidation by Respondent Grifols; or
- C. other change in the Respondent Grifols, including, but not limited to, assignment and the creation or dissolution of subsidiaries, if such change might affect compliance obligations arising out of this Order.

XI.

IT IS FURTHER ORDERED that, for purposes of determining or securing compliance with this Order, and subject to any legally recognized privilege, and upon written request and upon five (5) days' notice to Respondent Grifols, Respondent Grifols shall, without restraint or interference, permit any duly authorized representative(s) of the Commission:

- A. access, during business office hours of Respondent Grifols and in the presence of counsel, to all facilities and access to inspect and copy all books, ledgers, accounts, correspondence, memoranda and all other records and documents in the possession or under the control of Respondent Grifols Relating To

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compliance with this Order, which copying services shall be provided by Respondent Grifols at its expense; and

- B. to interview officers, directors, or employees of Respondent Grifols, who may have counsel present, regarding such matters.

XII.

IT IS FURTHER ORDERED that this Order shall terminate ten (10) years after the date on which this Order becomes final.

By the Commission.

CONFIDENTIAL EXHIBIT A

DESIGNATED AMOUNT OF PRODUCTS

[Redacted From the Public Record Version
But Incorporated By Reference]

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CONFIDENTIAL EXHIBIT B

**DESIGNATED PLASMA CENTER AND
SALES & MARKETING EMPLOYEES**

[Redacted From the Public Record Version
But Incorporated By Reference]

CONFIDENTIAL EXHIBIT B-1

DESIGNATED MELVILLE EMPLOYEES

[Redacted From the Public Record Version
But Incorporated By Reference]

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CONFIDENTIAL EXHIBIT C

DIVESTITURE AGREEMENT

[Redacted From the Public Record Version
But Incorporated By Reference]

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EXHIBIT D

GRIFOLS PLASMA CENTERS

PLASMA COLLECTION CENTERS

Talecris
5301 Moffett Road, Suite 230
Mobile, Alabama 36618

Talecris
250 YWCA Way
Winston-Salem, North Carolina 27101

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CONFIDENTIAL EXHIBIT E
TALECRIS ALBUMIN CUSTOMER CONTRACTS

[Redacted From the Public Record Version
But Incorporated By Reference]

CONFIDENTIAL EXHIBIT E-1

**DESIGNATED AMOUNT OF
TALECRIS ALBUMIN**

[Redacted From the Public Record Version
But Incorporated By Reference]

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CONFIDENTIAL EXHIBIT F

TALECRIS IVIG CUSTOMER CONTRACTS

[Redacted From the Public Record Version
But Incorporated By Reference]

CONFIDENTIAL EXHIBIT F-1

**DESIGNATED AMOUNT OF
TALECRIS IVIG PRODUCT**

[Redacted From the Public Record Version
But Incorporated By Reference]

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CONFIDENTIAL EXHIBIT G

KOATE CUSTOMER CONTRACTS

[Redacted From the Public Record Version
But Incorporated By Reference]

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EXHIBIT H
MONITOR AGREEMENT**MONITOR AGREEMENT**

MONITOR AGREEMENT (the "Agreement"), dated as of April 22, 2011, between Grifols, Inc. ("Grifols"), Talecris Biotherapeutics Holdings Corp. ("Talecris"), and R. Owen Richards, President of Quantic Regulatory Services, LLC, 5N Regent Street, Suite 502, Livingston, N.J. 07039 (the "Monitor").

PRELIMINARY STATEMENTS

On April 18, 2011, Grifols and Kedrion S.p.A. ("Kedrion") entered into Divestiture Agreements, which Agreements are attached hereto as Confidential Exhibit A.

Grifols and Talecris will enter into an Agreement Containing Consent Orders ("Consent Agreement") with the Staff of the United States Federal Trade Commission (the "Commission"). The Consent Agreement is subject to approval by the Commission. If the Commission determines to accept for public comment the executed Consent Agreement containing the proposed Decision and Order (collectively, the "Order"), attached hereto as Exhibit B, it is anticipated that the Commission will issue the Order to Maintain Assets, attached hereto as Exhibit C. The Order requires Grifols to divest to Kedrion the Melville Facility, the Grifols Plasma Centers, and Grifols Plasma, enter into the Contract Manufacturing Agreement, the Product Agreement, the Koate Option, License and Sale Agreement, assign, or extend to Kedrion the rights, benefits and obligations under, the Koate Customer Contracts, assign, or extend to Kedrion the rights, benefits and obligations under, the Talecris Albumin Customer Contracts, assign, or extend to Kedrion the rights, benefits and obligations under, the Talecris IVIG Customer Contracts; allows Grifols to enter into a Melville Facility Lease Agreement with Kedrion under which, for a period of no more than four (4) years from the Acquisition Date, Grifols will lease back the Melville Facility from Kedrion; and provides for the appointment of a monitor to ensure that Grifols complies with its obligations under the Order. The Order to Maintain Assets requires Grifols and Talecris to maintain and preserve, pending divestiture, the assets that are subject to the Order.

WHEREAS, the Commission may appoint R. Owen Richards, President of Quantic Regulatory Services, LLC, as the monitor pursuant to the Order to monitor Grifols' and Talecris' compliance with the terms of the Order and the Order to Maintain Assets, and R. Owen Richards has consented to such appointment;

WHEREAS, the Order further provides that Grifols shall execute a Monitor Agreement, subject to the prior approval of the Commission, conferring all the rights, powers and authority necessary to permit the Monitor to carry out such duties and responsibilities pursuant to the Order;

WHEREAS, this Monitor Agreement, although executed by the Monitor, Grifols, and Talecris, is not effective for any purpose, including but not limited to imposing rights and

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responsibilities on Grifols, Talecris, or the Monitor under the Order, until it has been approved by the Commission;

WHEREAS, upon such approval by the Commission, the Monitor, Grifols, and Talecris intend to be legally bound by this Monitor Agreement; and

NOW, THEREFORE, the parties agree as follows:

DEFINITIONS

- A. "Grifols" means Grifols, Inc., its directors, officers, employees, agents, representatives, successors, and assigns; and its joint ventures, subsidiaries, divisions, groups and affiliates in each case controlled by Grifols, and the respective directors, officers, employees, agents, representatives, successors, and assigns of each.
- B. "Talecris" means Talecris Biotherapeutics Holdings Corp., its directors, officers, employees, agents, representatives, successors, and assigns; and its joint ventures, subsidiaries, divisions, groups and affiliates in each case controlled by Talecris, and the respective directors, officers, employees, agents, representatives, successors, and assigns of each.
- C. All other capitalized words or phrases appearing in this Agreement that are not otherwise defined herein are deemed to have the defined meanings assigned to them in the Order.

ARTICLE I

1.1 Powers of the Monitor. The Monitor shall have the rights, duties, powers and authority conferred upon the Monitor by the Order, attached as Exhibit B, and by the Order to Maintain Assets, attached as Exhibit C, that are necessary for the Monitor to monitor Grifols' and Talecris' compliance with the requirements of the Order and the Order to Maintain Assets. Grifols and Talecris hereby transfer to the Monitor all rights, powers, and authorities necessary to permit the Monitor to perform his duties and responsibilities pursuant to and consistent with the purposes of the Order and the Order to Maintain Assets. Any descriptions thereof contained in this Agreement in no way modify the Monitor's powers and authority or Grifols' and Talecris' obligations under the Order and the Order to Maintain Assets.

1.2 Monitor's Duties. The Monitor shall monitor Grifols' and Talecris' compliance with the Order. The Monitor's duties shall include monitoring Grifols' and Talecris' compliance with the terms of the Order and the Order to Maintain Assets including monitoring:

- a. preserving the assets to be divested pending the divestiture;
- b. divesting the Melville Facility;
- c. divesting the Grifols Plasma Centers;

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- d. divesting the Grifols Plasma;
- e. entering into and complying with the Contract Manufacturing Agreement;
- f. entering into and complying with the Product Agreement;
- g. entering into and complying with the Koate Option, License and Sale Agreement;
- h. assigning, or extending to Kedrion the rights, benefits and obligations under, the Koate Customer Contracts;
- i. assigning, or extending to Kedrion the rights, benefits and obligations under, the Talecris Albumin Customer Contracts;
- j. assigning, or extending to Kedrion the rights, benefits and obligations under, the Talecris IVIG Customer Contracts;
- k. carrying out all other duties of the Monitor specified in the Order and the Order to Maintain Assets.

The Monitor shall act in a fiduciary capacity for the benefit of the Commission only; it is understood and agreed that no such fiduciary relationship exists between the Monitor and Grifols or Talecris.

1.3 Duration of Monitor's Authority. The Monitor shall have all powers and duties described above and consistent with the Order and the Order to Maintain Assets until Grifols has completed the divestitures required by the Order and has completed the supply obligations under the Contract Manufacturing Agreement; provided, however, that the Commission may extend or modify this period as may be necessary or appropriate to accomplish the purposes of the Order.

1.4 Confidential and Proprietary Information. The Monitor shall enter into a confidentiality agreement, attached hereto as Confidential Exhibit D.

1.5 Access to records, documents and facilities. Subject to any demonstrated legally recognized privilege, the Monitor shall have full and complete access to Grifols' and Talecris' personnel, books, documents, records kept in the ordinary course of business, facilities and technical information, and such other relevant information as the Monitor may reasonably request, related to Grifols' and Talecris' compliance with its obligations under the Order and the Order to Maintain Assets. Grifols and Talecris shall cooperate with any reasonable request of the Monitor and shall take no action to interfere with or impede the Monitor's ability to monitor Grifols' and Talecris' compliance with the Order and the Order to Maintain Assets.

1.6 Grifols' and Talecris' Duties. Grifols agrees that:

- a. no later than one (1) day after the Acquisition Date, Grifols and Talecris will transfer to the Monitor all rights, powers, and authorities necessary to permit the Monitor to perform his duties and responsibilities, pursuant to the Order and the Order to Maintain Assets consistent with the purposes of the Order.
- b. Grifols and Talecris will provide the Monitor with information that the Monitor reasonably requests to carry out his duties and responsibilities under the Order.

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c. Grifols and Talecris will designate a senior individual as a primary contact for the Monitor.

d. Grifols and Talecris will provide the Monitor with electronic or hard copies, as may be appropriate, of all reports submitted to the Commission pursuant to the Order and the Order to Maintain Assets that are relevant to the Monitor's duties, simultaneous with the submission of such reports to the Commission.

e. Grifols and Talecris will comply with the Monitor's reasonable requests for onsite visits and audits of Grifols' and Talecris' facilities.

f. Grifols and Talecris will comply with the Monitor's reasonable requests for follow-up discussions or supplementary information concerning any reports provided to or requested by the Monitor pursuant to the Order or the Order to Maintain Assets, and will provide the Monitor with access to and copies of other data, records or other information that the Monitor reasonably believes are necessary to the proper discharge of his responsibilities under the Order or the Order to Maintain Assets.

g. Grifols and Talecris consent to the following terms and conditions regarding the powers, duties, authorities, and responsibilities of the Monitor:

1. The Monitor shall have the power and authority to monitor Respondent Grifols' and Talecris' compliance with the terms of the Order and the Order to Maintain Assets, and shall exercise such power and authority and carry out the duties and responsibilities of the Monitor in a manner consistent with the purposes of the Order and in consultation with the Commission including, but not limited to:

a. Monitoring Grifols' and Talecris' compliance with all of their obligations and performance of all of their responsibilities as required by the Order and the Order to Maintain Assets; and

b. Monitoring any agreements between Respondent Grifols and the Acquirer.

2. Within one (1) month from the date the Monitor is appointed and every sixty (60) days thereafter, the Monitor shall report in writing to the Commission concerning performance by Grifols and Talecris of their obligations under the Order and the Order to Maintain Assets.

3. The Monitor and each of the Monitor's consultants, accountants, attorneys, and other representatives and assistants shall sign a confidentiality agreement; PROVIDED, HOWEVER, such agreement shall not restrict the Monitor from providing any information to the Commission.

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1.7 **Effective Date.** This Monitor Agreement shall become effective only upon Commission approval of the Monitor.

ARTICLE II

2.1 **Retention and payment of Counsel, Consultants, and other Assistants.** The Monitor shall have the authority to employ, at the cost and expense of Grifols and Talecris, such attorneys, consultants, accountants, and other representatives and assistants as are reasonably necessary to carry out the Monitor's duties and responsibilities as allowed pursuant to the Order and the Order to Maintain Assets provided that such individuals enter into a confidentiality agreement that requires the same standard of care and obligations of confidentiality to which the Monitor must adhere. Before hiring any legal counsel, the Monitor shall confirm with counsel that there is no conflict of interest if that counsel represents the Monitor.

2.2 **Compensation of the Monitor.** Grifols and Talecris will pay the Monitor within thirty (30) days of receipt of an invoice in accordance with the hourly fee schedule attached hereto as Confidential Exhibit E for all time spent in the performance of the Monitor's duties including all monitoring activities related to the Order and the Order to Maintain Assets (including any and all such activities performed prior to the date of this Agreement), all work in connection with the negotiation and preparation of this Monitor Agreement, and all reasonable and necessary travel time.

- a. In addition, Grifols and Talecris will pay within such thirty (30) days (i) all out-of-pocket expenses incurred by the Monitor in the performance of the Monitor's duties, including, without limitation, any auto, train or air travel in the performance of the Monitor's duties, international telephone calls, and (ii) all fees and disbursements reasonably incurred by such consultants, accountants, attorneys and other representatives and assistants as are reasonably necessary to carry out the Monitor's duties.
- b. The Monitor shall have full and direct responsibility for compliance with all applicable laws, regulations and requirements pertaining to income and social security taxes, unemployment insurance, worker's compensation, disability insurance, and the like.

ARTICLE III

3.1 **Monitor's liabilities and indemnification.** Grifols and Talecris hereby agree to indemnify the Monitor and his employees, consultants, accountants, attorneys and other representatives and assistants (collectively the "Indemnified Parties") and hold the Indemnified Parties harmless in accordance with and to the extent required by the Order and the Order to Maintain Assets. Without in any way limiting the generality of the foregoing, Grifols and Talecris shall indemnify the Indemnified Parties and hold the

Decision and Order

Indemnified Parties harmless against any losses, claims, damages, liabilities, or expenses arising out of, or in connection with, the performance of the Monitor's duties, including, without limitation, all reasonable fees of counsel (of Monitor's choosing) and other reasonable expenses incurred in connection with the preparations for, or defense of, any claim or inquiry, whether or not resulting in any liability, except to the extent that such losses, claims, damages, liabilities, or expenses result from gross negligence, willful or wanton acts, or bad faith by the Monitor. The Monitor's maximum liability to Grifols or Talecris relating to services rendered pursuant to this Agreement (regardless of the form of the action, whether in contract, statutory law, tort, or otherwise) shall be limited to the total sum of the fees paid to the Monitor by Grifols and Talecris, respectively, except to the extent that any losses, claims, damages, liabilities, or expenses result from gross negligence, willful or wanton actions, or bad faith by the Monitor. IN NO CIRCUMSTANCES WHATSOEVER SHALL MONITOR BE LIABLE FOR ANY SPECIAL, INCIDENTAL, CONSEQUENTIAL OR PUNITIVE DAMAGES.

Grifols and Talecris agree that their obligations to indemnify the Monitor extend to any agreement or relationship between the Monitor and Kedrion and relates to the Monitor's responsibilities under the Monitor Agreement and/or the Order or the Order to Maintain Assets.

3.2 Monitor's removal. If the Monitor materially breaches his responsibilities under the Order, the Commission may terminate this Agreement and appoint a substitute Monitor.

3.3 Approval by the Commission. This Agreement shall have no force or effect until approved by the Commission.

3.4 Termination: This Agreement shall terminate the earlier of: (a) the date set forth in the Order; (b) Grifols' and Talecris' receipt of written notice from the Commission that the Commission has determined that the Monitor has ceased to act or failed to act diligently, or is unwilling or unable to continue to serve as Monitor; or (c) with at least thirty (30) days advance notice to be provided by the Monitor to Grifols, Talecris and the Commission, upon resignation of the Monitor. The Monitor may resign at any time during the term of this Agreement for any reason by providing such 30 days written notice to Grifols, Talecris and the Commission and Monitor shall have no liability as a result of his resignation. If this Agreement is terminated for any reason, the confidentiality obligations set forth in this Agreement will remain in force.

3.5 Conflicts of Interest: If the Monitor becomes aware during the term of this Agreement that he has or may have a conflict of interest that may affect or could have the appearance of affecting performance by the Monitor of any of his duties under this Agreement, the Monitor shall promptly inform Grifols, Talecris and the Commission of any such conflict.

3.6 Independent Contractor. It is understood that the Monitor will be serving under this Monitor Agreement as an independent contractor and that the relationship of employer and employee shall not exist between Monitor and Grifols or Talecris. The Monitor will

Decision and Order

not be entitled to participate in any employee benefit plans or accrue any employee benefits as a result of providing services under this Agreement.

3.7 Choice of Law. This Monitor Agreement shall be subject to the substantive law of the State of New York (regardless of any other jurisdiction's choice of law principles). This Monitor Agreement is for the sole benefit of the parties hereto and their permitted assigns and the Commission, and nothing herein express or implied shall give or be construed to give any other person any legal or equitable rights hereunder. This Monitor Agreement contains the entire agreement between the parties hereto with respect to the matters described herein and replaces any and all prior agreements or understandings, whether written or oral.

3.8 Notices. Any notices or other communication required to be given hereunder shall be deemed to have been properly given if sent by mail or reputable overnight courier, to the applicable party at its address below (or to such other address as to which such party shall hereafter notify the other party):

If to the Monitor:

R. Owen Richards, President
Quantic Regulatory Services, LLC
5N Regent Street, Suite 502
Livingston, N.J. 07039
Fax: 973.535.1734

If to Grifols:

Grifols, Inc.
2410 Lillyvale Avenue
Los Angeles, CA 90032-3514
Fax: 323.441.7151
Attention: David Ian Bell, General Counsel

With copies to:

Proskauer Rose LLP
1001 Pennsylvania Avenue, N.W.
Suite 400 South
Washington, D.C. 20004-2533
Fax: 202.416.6899
Attention: Alicia J. Batts and
Rhett R. Krulla

and

Decision and Order

Osborne Clarke S.L.P.
Avenida Diagonal, 477
Planta 20
08036 Barcelona
Spain
Fax: +34.93.410.2513
Attention: Tomás Dagá
Raimon Grifols

If to Talecris:

Talecris Biotherapeutics Holdings Corp.
4101 Research Commons
79 T.W. Alexander Drive
Research Triangle Park
North Carolina 27709
Fax: 1-919-287-2807
Attention: John F. Gaither, Jr.

With a copy to:

Arnold & Porter LLP
555 Twelfth Street, N.W.
Washington, D.C. 20004-1206
Fax: 202.942.5999
Attention: Deborah L. Feinstein

If to the Commission:

Federal Trade Commission
600 Pennsylvania Avenue, N.W.
Washington, D.C. 20580
Attention: Eric D. Rohlck

IN WITNESS WHEREOF, the parties hereto have caused this Agreement to be executed
as of the date first above written.

**R. OWEN RICHARDS, PRESIDENT
QUANTIC REGULATORY SERVICES, LLC
MONITOR:**

R. Owen Richards
President

Decision and Order

Osborne Clarke S.L.P.
Avenida Diagonal, 477
Planta 20
08036 Barcelona
Spain
Fax: +34.93.410.2513
Attention: Tomás Dagá
Raimon Grifols

If to Talecris:

Talecris Biotherapeutics Holdings Corp.
4101 Research Commons
79 T.W. Alexander Drive
Research Triangle Park
North Carolina 27709
Fax: _____
Attention:

With a copy to:

Arnold & Porter LLP
555 Twelfth Street, N.W.
Washington, D.C. 20004-1206
Fax: 202.942.5999
Attention: Deborah L. Feinstein

If to the Commission:

Federal Trade Commission
600 Pennsylvania Avenue, N.W.
Washington, D.C. 20580
Attention: Eric D. Rohlek

IN WITNESS WHEREOF, the parties hereto have caused this Agreement to be executed
as of the date first above written.

R. OWEN RICHARDS, PRESIDENT
QUANTIC REGULATORY SERVICES, LLC
MONITOR:



R. Owen Richards
President

Decision and Order

GRIFOLS:

BY:  _____

NAME: David Bell
Vice President, Corporate Operations

TITLE: General Counsel

TALECRIS:

BY: _____

NAME: _____

TITLE: _____

Decision and Order

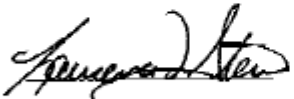
GRIFOLS:

BY: _____

NAME: _____

TITLE: _____

TALECRIS:

BY: 

NAME: Lawrence D. Stern

TITLE: Chairman and Chief Executive Officer



Decision and Order

CONFIDENTIAL EXHIBIT A

DIVESTITURE AGREEMENT

[Redacted From the Public Record Version
But Incorporated By Reference]

EXHIBIT B

**AGREEMENT CONTAINING CONSENT ORDER AND
DECISION AND ORDER**

EXHIBIT C

ORDER TO MAINTAIN ASSETS

CONFIDENTIAL EXHIBIT D

CONFIDENTIALITY AGREEMENT

[Redacted From the Public Record Version
But Incorporated By Reference]

CONFIDENTIAL EXHIBIT H-1
EXHIBIT E TO MONITOR AGREEMENT
(COMPENSATION)

[Redacted From the Public Record Version
But Incorporated By Reference]

Order to Maintain Assets

ORDER TO MAINTAIN ASSETS

The Federal Trade Commission ("Commission") having initiated an investigation of the proposed acquisition of Talecris Biotherapeutics Corp. ("Respondent Talecris") by Grifols, S.A. ("Respondent Grifols") and Respondents having been furnished thereafter with a copy of the draft of Complaint that the Bureau of Competition proposed to present to the Commission for its consideration and which, if issued by the Commission, would charge Respondent Grifols and Respondent Talecris with violations of Section 7 of the Clayton Act, as amended, 15 U.S.C. § 18, and Section 5 of the Federal Trade Commission Act, as amended, 15 U.S.C. § 45; and

Respondent Grifols and Respondent Talecris, their attorneys, and counsel for the Commission having thereafter executed an Agreement Containing Consent Orders ("Consent Agreement"), containing an admission by Respondents of all the jurisdictional facts set forth in the aforesaid draft Complaint, a statement that the signing of said Consent Agreement is for settlement purposes only and does not constitute an admission by Respondent Grifols or Respondent Talecris that the law has been violated as alleged in such Complaint, or that the facts as alleged in such Complaint, other than jurisdictional facts, are true, and waivers and other provisions as required by the Commission's Rules; and

The Commission having thereafter considered the matter and having determined that it had reason to believe that Respondents have violated the said Acts, and that a Complaint should issue stating its charges in that respect, and having determined to accept the executed Consent Agreement and to place such Consent Agreement containing the Decision and Order on the public record for a period of thirty (30) days for the receipt and consideration of public comments, now in further conformity with the procedure described in Commission Rule 2.34, 16 C.F.R. § 2.34, the Commission hereby issues its Complaint, makes the following jurisdictional findings and issues this Order to Maintain Assets:

1. Respondent Grifols is a corporation organized, existing and doing business under and by virtue of the laws of

Order to Maintain Assets

Spain with its office and principal place of business located at Avinguda de la Generalitat, 152, Parque empresarial Can Sant Joan, 08174 Sant Cugat del Valles, Barcelona, Spain, and with its office and principal place of business in the United States located at 2410 Lillyvale Avenue, Los Angeles, CA 90032.

2. Respondent Talecris is a corporation organized, existing and doing business under and by virtue of the laws of Delaware, with its office and principal place of business located at 4101 Research Commons, 79 T.W. Alexander Drive, Research Triangle Park, North Carolina 27709.
3. The Federal Trade Commission has jurisdiction of the subject matter of this proceeding and of Respondents, and the proceeding is in the public interest.

ORDER**I.**

IT IS ORDERED that, as used in this Order to Maintain Assets, the following definitions and the definitions used in the Consent Agreement and the proposed Decision and Order (and when made final, the Decision and Order), which are incorporated herein by reference and made a part hereof, shall apply:

- A. "Grifols" means Grifols, S.A., its directors, officers, employees, agents, representatives, successors, and assigns; and its joint ventures, subsidiaries, divisions, groups, and affiliates controlled by Grifols, S.A. (including Talecris, after the Acquisition Date), and the respective directors, officers, employees, agents, representatives, successors, and assigns of each.
- B. "Talecris" means Talecris Biotherapeutics Holdings Corp., its directors, officers, employees, agents, representatives, successors, and assigns; and its joint ventures, subsidiaries, divisions, groups, and affiliates controlled by Talecris Biotherapeutics Holdings Corp.,

Order to Maintain Assets

and the respective directors, officers, employees, agents, representatives, successors, and assigns of each.

- C. "Commission" means the Federal Trade Commission.
- D. "Decision and Order" means the:
 - 1. Proposed Decision and Order contained in the Consent Agreement in this matter until the issuance of a final Decision and Order by the Commission; and
 - 2. Final Decision and Order issued by the Commission following the issuance and service of a final Decision and Order by the Commission.
- E. "Orders" means the Decision and Order and this Order to Maintain Assets.

II.**IT IS FURTHER ORDERED** that:

- A. From the date on which Respondent Grifols and Respondent Talecris sign the Consent Agreement and until the Effective Date, Respondent Grifols and Respondent Talecris shall take such actions as are necessary to maintain the full economic viability, marketability and competitiveness of each of their assets included within the Divested Business to minimize any risk of loss of competitive potential for the Divested Business, and to prevent the destruction, removal, wasting, deterioration, or impairment of the Divested Business, except for ordinary wear and tear. Respondent Grifols and Respondent Talecris shall not sell, transfer, encumber or otherwise impair any of their assets included within the Divested Business (other than in the manner prescribed in the Decision and Order) nor take any action that lessens the full economic viability, marketability or competitiveness

Order to Maintain Assets

of any of their assets included within the Divested Business.

- B. Respondent Grifols and Respondent Talecris shall retain all rights, title, and interest in each of their assets included within the Divested Business.
- C. Respondent Grifols and Respondent Talecris shall maintain the operations of each of their assets included within the Divested Business in the regular and ordinary course of business and in accordance with past practice (including regular repair and maintenance of the assets, as necessary) and/or as may be necessary to preserve the marketability, viability, and competitiveness of the Divested Business, and shall use their best efforts to preserve the existing relationships with the following: suppliers, vendors, distributors, customers, governmental agencies, employees, and others having business relations with the Divested Business. Respondent Grifols and Respondent Talecris, for each of their assets included within the Divested Business, shall be responsible for, among other things:
 - 1. Providing sufficient working capital to operate at least at current rates of operation, to meet all capital calls with respect to such business and to carry on, at least at their scheduled pace, all capital projects, business plans and promotional activities;
 - 2. Continuing, at least at their scheduled pace, any additional expenditures authorized prior to the date the Consent Agreement was signed by Respondent Grifols and Respondent Talecris including, but not limited to, all research, development, manufacture, distribution, marketing and sales expenditures;
 - 3. Providing such resources as may be necessary to respond to competition and/or to prevent any diminution in sales of the Divested Business prior to the Effective Date;

Order to Maintain Assets

4. Providing such resources as may be necessary to maintain the competitive strength and positioning of the Divested Business;
 5. Making available for use by the Divested Business funds sufficient to perform all routine maintenance and all other maintenance as may be necessary to, and all replacements of, the assets related to such business;
 6. Providing the Divested Business with such funds as are necessary to maintain the full economic viability, marketability and competitiveness of the Divested Business; and
 7. Providing such support services to the Divested business as of the date the Consent Agreement was signed by Respondent Grifols and Respondent Talecris.
- D. Respondent Grifols and Respondent Talecris shall maintain a work force at the equivalent or larger size, and with equivalent or better training and expertise, to what has been associated with each of their assets included within the Divested Business as of the date the Consent Agreement was signed by Respondents.
1. Respondent Grifols shall provide all of the Designated Employees with reasonable financial incentives to continue in their positions consistent with past practices and/or as may be necessary to preserve the marketability, viability and competitiveness of Respondents Grifols' assets within the Divested Business pending divestiture. Such incentives shall include a continuation of all employee benefits offered by Respondent Grifols until the Effective Date has occurred, including regularly scheduled raises, bonuses, vesting of pension benefits (as permitted by law), and additional incentives as may be necessary to

Order to Maintain Assets

prevent any diminution of the Divested Business' competitiveness.

2. Respondent Talecris shall provide all of the Designated Melville Employees with reasonable financial incentives to continue in their positions consistent with past practices and/or as may be necessary to preserve the marketability, viability and competitiveness of Talecris' assets within the Divested Business pending divestiture. Such incentives shall include a continuation of all employee benefits offered by Respondent Talecris until the Effective Date has occurred, including regularly scheduled raises, bonuses, vesting of pension benefits (as permitted by law), and additional incentives as may be necessary to prevent any diminution of the Divested Business' competitiveness.
- E. Respondent Grifols and Respondent Talecris shall not interfere with the hiring or employing of the Designated Employees or the Designated Melville Employees, respectively, as described in Paragraph VII of the proposed Decision and Order, and shall remove any impediments within the control of Respondent Grifols or Respondent Talecris that may deter these employees from accepting employment with the Acquirer including, but not limited to, any noncompete provisions of employment or other contracts with Respondent Grifols or Respondent Talecris that would affect the ability or incentive of those individuals to be employed by the Acquirer. In addition, Respondent Grifols and Respondent Talecris shall not make any counteroffer to a Designated Employee or a Designated Melville Employee, respectively, who receives a written offer of employment from the Acquirer.

Provided, however, subject to the conditions of continued employment prescribed in this Order to Maintain Assets, this Paragraph II.E. shall not prohibit

Order to Maintain Assets

Respondent Grifols or Respondent Talecris from continuing to employ any Designated Employee or Designated Melville Employee, respectively, under the terms of such employee's employment with Respondent Grifols or Respondent Talecris prior to the date of the written offer of employment from the Acquirer to such employee.

- F. Unless specifically authorized by the Acquirer, Respondent Grifols and Respondent Talecris shall not use, directly or indirectly, any Confidential Business Information other than as necessary to:
1. comply with the requirements of the Orders;
 2. comply with applicable law;
 3. consummate the Acquisition;
 4. defend legal claims, investigations or enforcement actions threatened or brought against Respondents or the Divested Business; and
 5. obtain legal advice.
- G. Respondent Grifols and Respondent Talecris shall not disclose or convey any such Confidential Business Information, directly or indirectly, to any person except the Acquirer or other persons specifically authorized by the Acquirer to receive such information, other than as necessary to:
1. comply with the requirements of the Orders;
 2. comply with applicable law;
 3. defend legal claims, investigations or enforcement actions threatened or brought against Respondents or the Divested Business; and
 4. obtain legal advice.

Order to Maintain Assets

- H. Respondent Grifols and Respondent Talecris shall institute procedures and requirements to ensure that:
1. Employees of Respondent Grifols or Respondent Talecris with access to Confidential Business Information do not provide, disclose or otherwise make available, directly or indirectly, any Confidential Business Information in contravention of this Order to Maintain Assets; and
 2. Employees of Respondent Grifols and Respondent Talecris do not solicit, access or use any Confidential Business Information that they are prohibited under this Order to Maintain Assets from receiving for any reason or purpose.
- I. Respondent Grifols shall require any agents and employees of Grifols who have access to Confidential Business Information to enter into agreements, within ten (10) days after the date this Order to Maintain Assets becomes final, not to disclose any Confidential Business Information to Respondent Grifols or to any third party except as otherwise permitted by this Order to Maintain Assets. Copies of such agreements shall be retained by Respondent Grifols and provided to the Commission.
- J. Respondent Talecris shall require any agents and employees of Talecris who have access to Confidential Business Information to enter into agreements, within ten (10) days after the date this Order to Maintain Assets becomes final, not to disclose any Confidential Business Information Relating To the Divested Business to Respondent Talecris or to any third party except as otherwise permitted by this Order to Maintain Assets. Copies of such agreements shall be retained by Respondent Talecris and provided to the Commission.

Order to Maintain Assets

- K. The purpose of this Order to Maintain Assets is to maintain the full economic viability, marketability and competitiveness of the Divested Business until the Effective Date, to minimize any risk of loss of competitive potential for the Divested Business, and to prevent the destruction, removal, wasting, deterioration, or impairment of the Divested Business, except for ordinary wear and tear.

III.**IT IS FURTHER ORDERED** that:

- A. At any time after Respondent Grifols and Respondent Talecris sign the Consent Agreement in this matter, the Commission may appoint a Monitor to assure that Respondent Grifols and Respondent Talecris expeditiously comply with all of their obligations and perform all of their responsibilities as required by this Order.
- B. The Commission shall select the Monitor, subject to the consent of Respondent Grifols and Respondent Talecris, which consent shall not be unreasonably withheld. If Respondent Grifols or Respondent Talecris has not opposed, in writing, including the reasons for opposing, the selection of a proposed Monitor within ten (10) days after notice by the staff of the Commission to Respondent Grifols and Respondent Talecris of the identity of any proposed Monitor, Respondent Grifols and Respondent Talecris shall be deemed to have consented to the selection of the proposed Monitor.
- C. Not later than ten (10) days after appointment of the Monitor, Respondent Grifols and Respondent Talecris shall execute an agreement that, subject to the prior approval of the Commission, confers on the Monitor all the rights and powers necessary to permit the Monitor to monitor Respondent Grifols' and Respondent Talecris' compliance with the relevant

Order to Maintain Assets

terms of the Orders in a manner consistent with the purposes of the Orders.

- D. Respondent Grifols and Respondent Talecris shall consent to the following terms and conditions regarding the powers, duties, authorities, and responsibilities of the Monitor:
1. The Monitor shall have the power and authority to monitor Respondent Grifols' and Respondent Talecris' compliance with the terms of the Orders, and shall exercise such power and authority and carry out the duties and responsibilities of the Monitor in a manner consistent with the purposes of the Orders and in consultation with the Commission including, but not limited to:
 - a. Assuring that Respondent Grifols and Respondent Talecris expeditiously comply with all of their obligations and perform all of their responsibilities as required by the Orders; and
 - b. Monitoring any agreements between Respondent Grifols and the Acquirer.
 2. The Monitor shall act in a fiduciary capacity for the benefit of the Commission.
 3. Subject to any demonstrated legally recognized privilege, the Monitor shall have full and complete access to Respondent Grifols' and Respondent Talecris' personnel, books, documents, records kept in the normal course of business, facilities and technical information, and such other relevant information as the Monitor may reasonably request Related To Respondent Grifols' and Respondent Talecris' compliance with their obligations under the Orders. Respondent Grifols and Respondent Talecris shall cooperate with any reasonable request of the Monitor and shall take no action to interfere with or impede the Monitor's ability to

Order to Maintain Assets

monitor Respondent Grifols' or Respondent Talecris' compliance with the Orders.

4. The Monitor shall serve, without bond or other security, at the expense of Respondent Grifols and Respondent Talecris on such reasonable and customary terms and conditions as the Commission may set. The Monitor shall have authority to employ, at the expense of Respondent Grifols and Respondent Talecris, such consultants, accountants, attorneys and other representatives and assistants as are reasonably necessary to carry out the Monitor's duties and responsibilities. The Monitor shall account for all expenses incurred, including fees for services rendered, subject to the approval of the Commission.
5. Respondent Grifols and Respondent Talecris shall indemnify the Monitor and hold the Monitor harmless against any losses, claims, damages, liabilities, or expenses arising out of, or in connection with, the performance of the Monitor's duties, including all reasonable fees of counsel and other reasonable expenses incurred in connection with the preparations for, or defense of, any claim, whether or not resulting in any liability, except to the extent that such losses, claims, damages, liabilities, or expenses result from gross negligence, malfeasance, willful or wanton acts, or bad faith by the Monitor.
6. The Monitor Agreement shall provide that within one (1) month from the date the Monitor is appointed pursuant to this paragraph, and every sixty (60) days thereafter, the Monitor shall report in writing to the Commission concerning performance by Respondent Grifols and Respondent Talecris of its obligations under the Orders.

Order to Maintain Assets

7. Respondent Grifols and Respondent Talecris may require the Monitor and each of the Monitor's consultants, accountants, attorneys, and other representatives and assistants to sign a customary confidentiality agreement; *provided, however*, such agreement shall not restrict the Monitor from providing any information to the Commission.
- E. The Commission may, among other things, require the Monitor and each of the Monitor's consultants, accountants, attorneys, and other representatives and assistants to sign an appropriate confidentiality agreement relating to Commission materials and information received in connection with the performance of the Monitor's duties.
- F. If the Commission determines that the Monitor has ceased to act or failed to act diligently, the Commission may appoint a substitute Monitor:
1. The Commission shall select the substitute Monitor, subject to the consent of Respondent Grifols and Respondent Talecris, which consent shall not be unreasonably withheld. If Respondent Grifols and Respondent Talecris have not opposed, in writing, including the reasons for opposing, the selection of a proposed Monitor within ten (10) days after notice by the staff of the Commission to Respondent Grifols and Respondent Talecris of the identity of any proposed Monitor, Respondent Grifols and Respondent Talecris shall be deemed to have consented to the selection of the proposed Monitor.
 2. Not later than ten (10) days after appointment of the substitute Monitor, Respondent Grifols and Respondent Talecris shall execute an agreement that, subject to the prior approval of the Commission, confers on the Monitor all the rights and powers necessary to permit the Monitor to monitor Respondent Grifols' and Respondent

Order to Maintain Assets

Talecris' compliance with the relevant terms of the Orders in a manner consistent with the purposes of the Orders.

- G. The Commission may on its own initiative, or at the request of the Monitor, issue such additional orders or directions as may be necessary or appropriate to assure compliance with the requirements of the Orders.
- H. A Monitor appointed pursuant to this Order may be the same person appointed as the Monitor pursuant to the Decision and Order and the Divestiture Trustee pursuant to the relevant provisions of the Decision and Order.

IV.

IT IS FURTHER ORDERED that within thirty (30) days after the date this Order to Maintain Assets becomes final, and every sixty (60) days thereafter until Respondent Grifols and Respondent Talecris have fully complied with their obligations under Paragraphs II, III, IV, VI, and VII of the related Decision and Order in this matter, Respondent Grifols and Respondent Talecris shall submit to the Commission a verified written report setting forth in detail the manner and form in which it intends to comply, is complying, and has complied with this Order to Maintain Assets and the related Decision and Order; *provided, however,* that, after the Decision and Order in this matter becomes final, the reports due under this Order to Maintain Assets shall be consolidated with, and submitted to the Commission at the same time as, the reports required to be submitted by Respondent Grifols pursuant to Paragraph IX.A. of the Decision and Order.

V.

IT IS FURTHER ORDERED that Respondent Grifols shall notify the Commission at least thirty (30) days prior to any proposed:

- A. dissolution of the Respondent Grifols;

Order to Maintain Assets

- B. acquisition, merger or consolidation of Respondent Grifols; or
- C. other change in the Respondent Grifols, including, but not limited to, assignment and the creation or dissolution of subsidiaries, if such change might affect compliance obligations arising out of this Order to Maintain Assets.

VI.

IT IS FURTHER ORDERED that, for purposes of determining or securing compliance with this Order to Maintain Assets, and subject to any legally recognized privilege, and upon written request and upon five (5) days notice to Respondent Grifols, Respondent Grifols, shall, without restraint or interference, permit any duly authorized representative(s) of the Commission:

- A. access, during business office hours of Respondent Grifols and in the presence of counsel, to all facilities and access to inspect and copy all books, ledgers, accounts, correspondence, memoranda and all other records and documents in the possession or under the control of Respondent Grifols related to compliance with this Order to Maintain Assets, which copying services shall be provided by Respondent Grifols at its expense; and
- B. to interview officers, directors, or employees of Respondent Grifols, who may have counsel present, regarding such matters.

VII.

IT IS FURTHER ORDERED that this Order to Maintain Assets shall terminate on the earlier of:

- A. Three (3) days after the Commission withdraws its acceptance of the Consent Agreement pursuant to the

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provisions of Commission Rule 2.34, 16 C.F.R. § 2.34;
or

- B. The latter of:
1. the day after the Effective Date;
 2. the day the related Decision and Order becomes final; or
- C. The day after the Commission otherwise directs that this Order to Maintain Assets is terminated.

By the Commission, Commissioner Kovacic recused.

ANALYSIS OF AGREEMENT CONTAINING CONSENT ORDERS TO AID PUBLIC COMMENT

I. Introduction

The Federal Trade Commission ("Commission") has accepted from Grifols, S.A. ("Grifols") and Talecris Biotherapeutics Holdings Corp. ("Talecris"), subject to final approval, an Agreement Containing Consent Orders ("Consent Agreement") and Decision and Order, and has issued a Complaint and the Order to Maintain Assets ("OMA") contained in the Consent Agreement. The Consent Agreement is designed to remedy the anticompetitive effects resulting from Grifols' proposed acquisition of Talecris (the "Acquisition"). Under the Consent Agreement, Grifols will: (i) divest the fractionation facility currently owned by Talecris in Melville, New York, to Kedrion S.p.A. ("Kedrion"); (ii) divest plasma collection centers to Kedrion; (iii) divest to Kedrion Talecris' Koate DVI plasma-derived Factor VIII ("pdFVIII") business, including the Koate brand name, in the United States; and (iv) for a seven-year

Analysis to Aid Public Comment

period, manufacture immune globulin ("Ig"), albumin, and Koate for Kedrion to sell in the United States.

The proposed Consent Agreement has been placed on the public record for 30 days to solicit comments from interested persons. Comments received during this period will become part of the public record. After 30 days, the Commission will again review the proposed Consent Agreement and will decide whether it should withdraw from the proposed Consent Agreement, modify it, or make it final.

On June 6, 2010, Grifols entered into an agreement to acquire Talecris for approximately \$3.4 billion in cash and stock. The Commission's Complaint alleges that the Acquisition violates Section 5 of the FTC Act, as amended, 15 U.S.C. § 45, and if consummated, would violate Section 7 of the Clayton Act, as amended, 15 U.S.C. § 18, and Section 5 of the FTC Act by lessening competition in the U.S. markets for Ig, albumin, and pdFVIII (the "Relevant Products").

II. The Parties

Grifols is a public company, headquartered in Barcelona, Spain. Its bioscience division develops and manufactures human blood plasma-derived products with manufacturing facilities in Barcelona and Los Angeles, California. Grifols entered the U.S. market in 2002, when it acquired the assets of a U.S. manufacturer, Alpha Therapeutics Corporation, and 42 plasma collection centers from SeraCare. Since then, Grifols has acquired additional plasma centers and is now vertically integrated, making it the second largest plasma collector in the world. Grifols employs approximately 6,000 people worldwide and had global 2009 revenues of \$1.3 billion.

Talecris is also a public company – owned in part by the private investment firm Cerberus Capital Management, L.P. ("Cerberus") – that specializes in the development, manufacture, and worldwide sale of human blood plasma-derived products. Talecris began its U.S. operations in 2005, when Cerberus acquired Bayer AG's global plasma business and Precision Pharma in the same year. Talecris is headquartered in Research

Analysis to Aid Public Comment

Triangle Park, North Carolina, with additional regional headquarters in Canada and Germany. Like Grifols, Talecris is a vertically integrated company, owning numerous plasma collection centers, as well as manufacturing facilities in Clayton, North Carolina, and Melville, New York. It employs approximately 5,000 people worldwide and had global 2009 revenues of approximately \$1.5 billion.

III. Market Structure and Relevant Products

A. Relevant Geographic Market

The relevant geographic market in which to analyze the Acquisition's effects is the United States. Plasma-derived products must be FDA-approved for sale in the United States, which requires that these products be made solely from plasma collected in the United States in FDA-approved collection centers and manufactured in FDA-approved plants. Thus, plasma products not approved for sale in the United States do not provide viable competitive alternatives for U.S. consumers in the face of an increase in price for U.S. products.

B. Relevant Product Markets

i. Ig

Ig is a plasma protein replacement therapy largely used to treat immune deficient patients. The relevant product market for Ig includes all brands, concentrations (*i.e.*, 5% and 10%), formulations (*i.e.*, liquid and lyophilized/powder), and means of administration (*i.e.*, intravenous and subcutaneous). Because intravenous Ig ("IVIG") accounts for the overwhelming majority of Ig sales in the United States, industry participants often refer to the Ig market as the IVIG market. Although IVIG is available in two concentrations (5% and 10%), they are therapeutically equivalent. The main difference is one of convenience: a 10% IVIG requires less volume, meaning treatment typically takes less time. Ig has numerous FDA-approved indications (*e.g.*, primary immunodeficiencies and Chronic Inflammatory Demyelinating Polyneuropathy), and there is a significant amount of off-label use.

Analysis to Aid Public Comment

Hospitals, physicians, and patients would not switch, and historically have not switched, from Ig products to non-Ig products in response to a small but significant and non-transitory increase in price ("SSNIP"). Although Ig products differ somewhat (*e.g.*, based on sucrose levels, immunoglobulin A content, or concentration), ample evidence demonstrates that the brands and products are largely interchangeable. Grifols and Talecris account for approximately 8.4% and 22.8% of the U.S. Ig market, respectively, and their merger would leave three manufacturers with nearly 100% of current U.S. Ig sales.

Physicians use albumin to expand blood volume, prime heart valves during cardiac surgery, treat burn victims, and replace proteins in treating liver failure. In the United States, the parties compete in the sale of two different albumin concentrations: 5% and 25% liquid. The 5% and 25% concentrations have different clinical uses, but if a 5% product is unavailable, hospitals can dilute a 25% product to a 5% concentration if necessary. On the manufacturing side, there are no significant costs associated with shifting production between 5% and 25% albumin, and manufacturers can make such changes in a matter of days. Because competitive conditions – including the number and identity of suppliers – for 5% and 25% albumin solutions are the same, it is appropriate to analyze albumin as a single market comprising both 5% and 25% products.

In most circumstances where it is used, albumin has no viable substitutes. While starches and salines can act as volume expanders like 5% albumin, those non-albumin products cannot substitute for albumin in the great majority of uses and do not meaningfully constrain albumin prices and, hence, are not included in the relevant product market. Even for those few indications for which there might be a potential alternative therapy, hospitals generally prefer albumin and would not switch from albumin to another product in response to a SSNIP. Grifols and Talecris have U.S. albumin market shares of approximately 13% each, and the Acquisition would leave only four meaningful competitors in that market.

Analysis to Aid Public Comment

Physicians use pdFVIII to treat bleeding disorders, namely Hemophilia A and von Willebrand Disease ("VWD"). While both pdFVIII and its non-plasma counterpart, recombinant Factor VIII ("rFVIII"), can be used to treat Hemophilia A, rFVIII and pdFVIII have limited interchangeability and, hence, limited ability to constrain each other's prices. For instance, although rFVIII is the standard of care for previously untreated patients with Hemophilia A (due to the perception that pdFVIII carries an increased risk of viral transmission), evidence suggests that patients using rFVIII are more likely to develop inhibitors – antibodies that impede the treatment's effectiveness. Thus, for some Hemophilia A patients, pdFVIII is the only viable treatment. Likewise, patients with severe VWD are treated with pdFVIII products containing von Willebrand Factor ("VWF"). No recombinant products contain VWF, so those patients also may have no choice but to use pdFVIII.

Clinical considerations, not price, determine whether a particular patient is given pdFVIII or rFVIII, and hospitals would not switch from pdFVIII to rFVIII in response to an increase in the price of pdFVIII. Grifols and Talecris account for approximately 23% and 3.6% of the U.S. pdFVIII market, respectively, and their merger would leave only three meaningful competitors in that market.

IV. Industry Background and the Acquisition's Effects

A decade ago, there was robust competition in the plasma-derived products industry. After supply increases in the early 2000s led to lower prices, suppliers reduced production and plasma collection capacity and began to vertically integrate, placing plasma collection almost entirely in the control of the few remaining firms in the market. Manufacturers also engaged in horizontal consolidation, leading to an industry dominated by three large firms, including Talecris. In the years that followed that consolidation, the Ig market in particular experienced a tightening of supply and dramatic year-over-year price increases.

The relevant markets have characteristics that allow manufacturers to promote stability and rational, coordinated

Analysis to Aid Public Comment

behavior. *First*, the markets are transparent, with firms monitoring each other's collections, output, pricing, and future expansion plans. *Second*, firms have engaged in signaling to limit supply levels and maintain higher prices. *Third*, if a firm were to "break ranks" from a coordinated scheme, the other manufacturers can detect any "cheating" over the course of the long manufacturing period and inflict punishment in other geographic markets. *Fourth*, the relevant markets are characterized by highly inelastic demand, increasing the firms' incentives to coordinate because even a small change in supply can have a large effect on price.

The Acquisition would substantially lessen competition in the relevant markets. It would eliminate actual, direct, and substantial competition between Grifols and Talecris. Moreover, given that each of the relevant markets already is highly concentrated, the Acquisition would facilitate successful coordinated interaction among the few remaining meaningful competitors, leading to reduced supply and higher prices for consumers. In addition, the Acquisition increases the likelihood that consumers would experience lower levels of innovation and service in the markets for the Relevant Products.

V. Entry Conditions

Neither new entry nor expansion sufficient to deter or counteract the Acquisition's anticompetitive effects is likely to occur within two years. The barriers to entering the plasma fractionation industry are extraordinary, with costs reaching hundreds of millions of dollars. Indeed, the barriers are so immense that *de novo* entry is unrealistic in less than five years. For example, an entrant must develop a product and secure all necessary regulatory approvals, with the required clinical trials alone taking up to three years. Additionally, the time and capital investment required to build and obtain regulatory clearance for a fractionation facility are significant, taking four to eight years and costing \$100 million or more. Finally, entrants must navigate a substantial body of intellectual property in the field, including trade secrets relating to purification and safety, and must incur substantial product research and development costs before bringing a product to market. Accordingly, new entry by a

Analysis to Aid Public Comment

domestic or foreign firm would not be timely, likely, or sufficient to counteract the Acquisition's anticompetitive effects.

VI. The Consent Agreement

The proposed Consent Agreement requires Grifols to divest certain assets to Kedrion and take other actions to alleviate the Acquisition's effects. In particular, the Consent Agreement expedites the entry of an additional competitor into each of the relevant markets, making a potential industry-wide coordinated scheme more difficult, and limiting the combined firm's ability to raise prices.

Kedrion possesses the resources and ability to be an effective competitor and meaningful constraint on any potential coordination in the industry. Created in 2001, Kedrion is the seventh largest fractionator in the world. Specializing in the development, production, and distribution of plasma-derived products, Kedrion actively sells plasma-derived products in more than 30 countries. Kedrion currently sells IVIG in a number of European and other markets and has started the process for FDA approval of its own IVIG product for sale in the United States. Kedrion also expects final FDA approval to sell a new albumin product in the United States in 2011. It currently operates two plants in Italy and is nearing completion of an expansion to its manufacturing facility in Godollo, Hungary.

Under the Consent Agreement, Grifols will enter into a sale-and-leaseback agreement with Kedrion for Talecris' Melville fractionation facility. Specifically, Kedrion will acquire the Melville facility and lease it back to Grifols for three to four years to ensure continuity of operations; at the end of the lease term, Kedrion can assume Melville operations and fractionate its own plasma. Additionally, Grifols will divest to Kedrion plasma collection centers and sell Kedrion an initial supply of raw plasma, ensuring that Kedrion will have an independent and reliable source of raw plasma.

In addition, Grifols will manufacture and supply Kedrion with FDA-approved and established IVIG, albumin, and pdFVIII products. Kedrion will market and sell private-label versions of

Analysis to Aid Public Comment

Talecris' Gamunex IVIG and Plasbumin albumin for a period of seven years. And Grifols will transfer to Kedrion all commercial agreements and rights to sell Koate pdFVIII in the U.S. market, making Kedrion the sole provider of Koate in the United States. Kedrion will also have the option to purchase the rights to manufacture Koate for sale in the United States.

Through the Consent Agreement, Kedrion will have immediate market access and the ability to supply customers with established products in all three product markets. Kedrion's presence in the U.S. market will add incremental supply of these life-saving products while still allowing the combined firm to take full advantage of the Acquisition's expected efficiencies. In addition, Kedrion will also have the opportunity to hire Grifols and Talecris employees to facilitate its entry and ensure continuity in the manufacture and sale of its products. By eliminating many of the industry's immense barriers to entry, the Consent Agreement will facilitate Kedrion's current and future entry with its own IVIG and albumin products and position Kedrion to replace the competition lost as a result of the Acquisition.

To ensure that the Commission remains informed about the status of the proposed divestitures, the Consent Agreement also requires the parties to file periodic reports with the Commission until the divestitures are accomplished. Furthermore, the OMA requires that the parties maintain all assets scheduled to transfer to Kedrion and authorizes the Commission to appoint a monitor to oversee the various agreements between Kedrion and Grifols. Under the OMA, Grifols and Talecris must maintain the full economic viability, marketability, and competitiveness of the proposed divested business and assets. This includes, among other things, retaining all rights, title, and interest in the divested assets, maintaining operations in their regular course, and not interfering in Kedrion's hiring of designated Grifols and Talecris employees. If Grifols does not comply with the OMA or any of the Consent Agreement's other terms, the Commission may appoint a divestiture trustee to divest the assets and enter into a product manufacturing agreement with a Commission-approved acquirer.

Concurring Statement

The purpose of this analysis is to facilitate public comment on the Consent Agreement. It is not intended to constitute an official interpretation of the proposed Decision and Order or to modify its terms in any way.

**CONCURRING STATEMENT OF COMMISSIONER
JULIE BRILL**

I concur in the Commission's decision to issue a complaint against Grifols challenging its acquisition of Talecris. I write separately to express my view that whether to resolve this matter through the proposed consent order is a close call, though I ultimately concur in that decision as well.

The vitally important plasma protein industry has seen considerable consolidation in recent years. Today, only four significant active competitors remain as to immune globulin ("Ig"), the largest product by sales at issue in this merger: Grifols, Talecris, CSL and Baxter.¹ In the meantime, prices have increased substantially. Just two years ago, when CSL tried to buy Talecris, the Commission alleged that these "price increases have been caused by the consolidation of competitors and the resulting increases in concentration."² The industry has operated as a "tight oligopoly," in the words of a 2007 Department of Health and Human Services report, carefully controlling supply, avoiding robust price competition, and engaging in signaling of future competitive moves.³

¹ A fifth competitor, Octapharma, withdrew its Ig product from the market in September 2010 due to safety concerns. As the Commission alleges in its complaint, "its future competitive significance is uncertain."

² Compl. ¶ 33, *FTC v. CSL Ltd.*, No. 09-1000 (D.D.C., filed May 28, 2009), available at <http://www.ftc.gov/os/caselist/0810255/091110csl-cerberusunsealedcmplt.pdf>.

³ *Id.* ¶¶ 37-44.

Analysis to Aid Public Comment

One outgrowth of the supply limitations and coordinated behavior described in the Commission's CSL complaint has been the difficulty safety-net providers have had in obtaining Ig under the 340B Drug Pricing Program. This Congressionally-mandated program is designed to provide pharmaceuticals at reduced prices to health care providers serving indigent and other at-risk patients.

All too often, however, plasma-derivative manufacturers have not made their products available at statutorily-mandated prices.⁴ This subverts Congress's goal of ensuring access to life-saving pharmaceuticals and increases costs to the health care system overall.

Against this backdrop, almost any merger in this industry would merit the significant scrutiny this one has received at the FTC. Although Grifols is today one of the smaller firms in the U.S. market, with a roughly 9% share of Ig sales, it recently launched a new 10% concentration intravenous Ig product that could threaten the industry-leading products offered by Talecris, Baxter and CSL. In addition, as alleged in the Commission's current complaint, the Ig market is highly concentrated and the change in market concentration effected by this merger easily raises a presumption of enhanced market power under the antitrust agencies' 2010 Merger Guidelines.⁵ Finally, as also alleged in the complaint, the risk of post-merger coordinated behavior is very real, given the history of coordination in this industry and the fact that the immediate post-merger U.S. Ig market will consist of three firms of roughly equal size. Given these and other significant facts, I strongly support issuance of the Commission's complaint.

Whether the consent order does enough to remedy competition concerns is a much closer call. On the one hand, the consent allows for the near-term introduction of product into the

⁴ See, e.g., Public Hospital Pharmacy Coalition, "Access to IVIG by Safety Net Hospitals Participating in the 340B Drug Discount Program" (Sept. 2006), available at http://www.phpcrx.org/public/documents/pdfs/IVIG_report.pdf.

⁵ The Ig market share and HHI figures in the Commission's complaint date from 2009 and are thus conservative, as they count Octapharma as a market participant, which it currently is not.

Concurring Statement

market from a new competitor, Kedrion. The consent should also facilitate Kedrion's entry into the U.S. market with its own Ig product in several years. On the other hand, Grifols will keep 67 of Talecris's 69 plasma collection centers, as well as its own 80 centers, while divesting two to Kedrion. In addition, the Melville, NY, manufacturing plant that Grifols is divesting to Kedrion is a smaller facility that is not currently outfitted to purify fractionated plasma into finished product. While Grifols will fractionate and purify a "Designated Amount of [finished] Product" for Kedrion for several years under the consent order, Kedrion may need to build or purchase a new facility in order to effectively compete over the longer term.⁶

In the end, given the particular facts and circumstances of this matter, I support the consent because it provides some degree of immediate, sure relief to consumers. I expect, though, that the Commission, other federal and state agencies, and affected purchasers will closely monitor these markets, both as to future proposed consolidations and potential coordinated behavior, including behavior that may adversely impact indigent and other at-risk patients through the critical 340B program.

⁶ Compare *In re Polypore Int'l, Inc.*, 2010-2 Trade Cas. ¶ 77,267, 2010 FTC LEXIS 97, at *108-110 (F.T.C. 2010) (requiring divestiture of second manufacturing plant to ensure that divestiture assets constituted viable ongoing business).

Complaint

IN THE MATTER OF
SETTLEMENTONE CREDIT CORPORATION
AND
SACKETT NATIONAL HOLDINGS, INC.

CONSENT ORDER, ETC. IN REGARD TO ALLEGED VIOLATIONS OF
SEC. 5(A) OF THE FEDERAL TRADE COMMISSION ACT, SECS. 604
AND 607(A) OF THE FAIR CREDIT REPORTING ACT, AND THE
GRAMM-LEACH-BLILEY SAFEGUARDS RULE

Docket No. C-4330; File No. 082 3208
Filed, August 17, 2011 — Decision, August 17, 2011

This consent order addresses allegations that SettlementOne Credit Corporation and its parent corporation Sackett National Holdings, Inc. (“Respondents”) failed to provide reasonable and appropriate security for consumers’ personal information. According to the complaint, Respondents obtained sensitive consumer information, much of which is not publicly available, from the three nationwide consumer reporting agencies, Equifax, Experian, and TransUnion. Respondents then used this information to create “trimerge reports,” which it sold to mortgage brokers and others to determine consumers’ eligibility for credit. The complaint alleges that Respondents, among other things, failed to develop comprehensive written information security policies; to implement reasonable steps to maintain an effective system of monitoring access to consumer reports by end users; and take appropriate action to correct existing vulnerabilities or threats to personal information in light of known risks. As a result, hackers were able to exploit vulnerabilities and access hundreds of consumer reports. The order requires Respondents to establish and maintain a comprehensive information security program reasonably designed to protect consumer information. The order further requires Respondents to maintain procedures to ensure that its consumer reports are given only to those persons or entities that will use it for a permissible purpose under the Fair Credit Reporting Act. The order further requires Respondents to obtain an independent, third-party assessment of its security procedures on a biennial basis for the next 20 years.

Participants

For the *Commission*: *Anthony Rodriguez and Katherine White.*

For the *Respondents*: *Patrice A. Ficklin, Relman, Dane & Colfax, PLLC.*

Complaint

COMPLAINT

The Federal Trade Commission (“FTC” or “Commission”), having reason to believe that SettlementOne Credit Corporation and Sackett National Holdings, Inc. have violated the Commission’s Standards for Safeguarding Customer Information Rule (“Safeguards Rule”), 16 C.F.R. Part 314, issued pursuant to Title V, Subtitle A of the Gramm-Leach-Bliley Act (“GLB Act”); 15 U.S.C. §§ 6801-6809, the Fair Credit Reporting Act (“FCRA”), 15 U.S.C. § 1681 et seq.; and Section 5 of the Federal Trade Commission Act (“FTC Act”), 15 U.S.C. § 45(a), and it appearing to the Commission that this proceeding is in the public interest, alleges:

1. Respondent SettlementOne Credit Corporation (“SettlementOne”) is a California corporation with its principal office or place of business at 2605 Camino Del Rio South, San Diego, California 92108. Respondent SettlementOne is a wholly-owned subsidiary of respondent Sackett National Holdings, Inc.

2. Respondent Sackett National Holdings, Inc. (“SNH”) is a corporation with its principal office or place of business at 2605 Camino Del Rio South, San Diego, California 92108. SNH conducts business through its ten wholly-owned subsidiaries, including SettlementOne. During all times material to this complaint, SNH controlled the practices alleged in this complaint.

3. The acts and practices of respondents as alleged in this complaint have been in or affecting commerce, as “commerce” is defined in Section 4 of the FTC Act, 15 U.S.C. § 44.

4. SettlementOne contracts with the three nationwide consumer reporting agencies, Equifax, Experian, and TransUnion (“nationwide CRAs”) to obtain consumer reports that it assembles and merges into a single “trimerge report.” The trimerge reports contain sensitive consumer information such as full name, current and former addresses, Social Security number, date of birth, employer history, credit account histories and information, and even account numbers. Much of this sensitive information is not publicly available. These “trimerge reports” are “consumer

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reports” as defined in Section 603(d) of the FCRA, 15 U.S.C. § 1681a(d).

5. Respondents sell these trimerge reports to mortgage brokers and others to determine consumers’ eligibility for credit. In creating and selling the trimerge reports to end user clients, respondent SettlementOne is a consumer reporting agency as that term is defined in Section 603(f) of the FCRA, 15 U.S.C. § 1681(f).

6. Respondent SettlementOne is a “financial institution” as that term is defined by Section 509(3)(A) of the GLB Act, 15 U.S.C. § 6809(3)(A), and is therefore subject to the requirements of the Safeguards Rule.

RESPONDENTS’ COURSE OF CONDUCT

7. SettlementOne furnishes its end user clients with trimerge reports through an online portal. It issues credentials to its clients, which consist of a user name and password. The end user clients use these credentials to access SettlementOne’s online portal and receive trimerged reports.

8. From at least February 2008, respondents have engaged in a number of practices that, taken together, failed to provide reasonable and appropriate security for consumers’ personal information. Among other things, respondents failed to:

- a. develop and disseminate information security policies for SettlementOne and its end user clients;
- b. assess the risks of allowing end users with unverified or inadequate security to access consumer reports through SettlementOne’s portal;
- c. implement reasonable steps to address these risks by, for example, evaluating the security of end user’s computer networks, requiring appropriate information security measures, and training end user clients;

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- d. implement reasonable steps to maintain an effective system of monitoring access to consumer reports by SettlementOne's end users, including by monitoring to detect anomalies and other suspicious activity; and
- e. take appropriate action to correct existing vulnerabilities or threats to personal information in light of known risks.

9. Because of SettlementOne's lack of information security policies and procedures, respondents allow clients without basic security measures in place, such as firewalls and updated antivirus software, to have access to their trimerge reports. The lack of such security measures directly caused highly-sensitive consumer reports to be available to hackers, as explained below.

THE BREACHES

10. As a direct result of these failures, between February and June 2008, hackers were able to exploit vulnerabilities in the computer networks of multiple SettlementOne end user clients, putting consumer reports in those networks at risk. In multiple breaches, hackers accessed at least 784 consumer reports without authorization. Additionally, the hackers had the ability to view any consumer report that the end user client had pulled in the previous 90 days.

11. Following each of the breaches, respondents did not make reasonable efforts to determine the cause(s) of the breaches and protect against future breaches. Although respondents did terminate some of the affected end users after learning of the security breaches, in other cases respondents did nothing. Respondents, for example, did not require end user clients to submit any documentation demonstrating that the clients' computer systems were virus free and otherwise properly protected. In one instance, despite the lack of documentation, the respondents restored access to an end user whose credentials had been stolen.

12. In addition, respondents have made no effort to warn their other end users of a known threat, or to suggest they make any efforts to ensure their systems were adequately secured.

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Respondents continue to give access to consumer reports to end user clients whose information security has not been adequately verified.

VIOLATIONS OF THE SAFEGUARDS RULE

13. The Safeguards Rule, which implements Section 501(b) of the GLB Act, 15 U.S.C. § 6801(b), was promulgated by the Commission on May 23, 2002, and became effective on May 23, 2003. The Rule requires financial institutions to protect the security, confidentiality, and integrity of customer information by developing a comprehensive written information security program that contains reasonable administrative, technical, and physical safeguards that include: (1) designating one or more employees to coordinate the information security program; (2) identifying reasonably foreseeable internal and external risks to the security, confidentiality, and integrity of customer information, and assessing the sufficiency of any safeguards in place to control those risks; (3) designing and implementing information safeguards to control the risks identified through risk assessment, and regularly testing or otherwise monitoring the effectiveness of the safeguards' key controls, systems, and procedures; (4) overseeing service providers and requiring them by contract to protect the security and confidentiality of customer information; and (5) evaluating and adjusting the information security program in light of the results of testing and monitoring, changes to the business operation, and other relevant circumstances. 16 C.F.R. §§ 314.3, 314.4.

14. As described in Paragraphs 7 through 12, respondents failed to implement reasonable security policies and procedures to protect sensitive consumer information, and have thereby engaged in violations of the Safeguards Rule by, among other things:

- a. failing to design and implement information safeguards to control the risks to customer information;
- b. failing to regularly test or monitor the effectiveness of its existing controls and procedures;

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- c. failing to evaluate and adjust the information security program in light of known or identified risks; and
- d. failing to develop, implement, and maintain a comprehensive information security program.

VIOLATIONS OF THE FCRA

15. Section 604 of the FCRA, 15 U.S.C. § 1681b, prohibits a consumer reporting agency from furnishing a consumer report except for specified “permissible purposes.” As described in Paragraph 10, in multiple instances, respondents furnished consumer reports to hackers that did not have a permissible purpose to obtain a consumer report. By and through the acts and practices described in Paragraphs 7 through 12, respondents have violated Section 604 of the FCRA, 15 U.S.C. § 1681b.

16. Section 607(a) of the FCRA, 15 U.S.C. § 1681e(a), requires every consumer reporting agency to maintain reasonable procedures to limit the furnishing of consumer reports to the purposes listed under Section 604 of the FCRA, 15 U.S.C. § 1681b. As described in Paragraphs 7 through 12, respondents failed to maintain reasonable procedures to limit the furnishing of consumer reports to the purposes listed under Section 604 of the FCRA. By and through the acts and practices described in Paragraphs 7 through 12, respondents have violated Section 607(a) of the FCRA, 15 U.S.C. § 1681e(a).

17. Section 607(a) of the FCRA, 15 U.S.C. § 1681e(a), prohibits a consumer reporting agency from furnishing a consumer report to any person if it has reasonable grounds for believing that the consumer report will not be used for a permissible purpose. As described in Paragraphs 10 through 12, in numerous instances, respondents furnished consumer reports under circumstances in which they had reasonable grounds for believing that the reports would not be used for a permissible purpose. By and through the acts and practices described in Paragraphs 10 through 12, respondents have violated Section 607(a) of the FCRA, 15 U.S.C. § 1681e(a).

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18. By their violations of Sections 604 and 607(a) of the FCRA, and pursuant to Section 621(a) thereof, 15 U.S.C. § 1681s, respondents have engaged in unfair and deceptive acts and practices in or affecting commerce, in violation of Section 5(a) of the FTC Act, 15 U.S.C. § 45(a).

VIOLATIONS OF THE FTC ACT

19. As described in Paragraphs 7 through 12, respondents have not employed reasonable and appropriate measures to secure the personal information they maintain and sell. Respondents' failure to employ reasonable and appropriate security measures to protect consumers' personal information has caused or is likely to cause substantial injury to consumers that is not offset by countervailing benefits to consumers or competition and is not reasonably avoidable by consumers. This practice was, and is, an unfair act or practice in or affecting commerce in violation of Section 5(a) of the Federal Trade Commission Act, 15 U.S.C. § 45(a).

THEREFORE, the Federal Trade Commission this seventeenth day of August, 2011, has issued this complaint against respondents.

By the Commission.

DECISION AND ORDER

The Federal Trade Commission having initiated an investigation of certain acts and practices of the Respondents named in the caption hereof, and the Respondents having been furnished thereafter with a copy of a draft Complaint that the Bureau of Consumer Protection proposed to present to the Commission for its consideration and which, if issued by the Commission, would charge the Respondents with violation of the Federal Trade Commission Act, 15 U.S.C. § 45 *et seq*; the Fair Credit Reporting Act, 15 U.S.C. § 1681 *et seq*; and the

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Commission's Standards for Safeguarding Customer Information Rule, 16 C.F.R. Part 314, issued pursuant to Title V, Subtitle A of the Gramm-Leach-Bliley Act, 15 U.S.C. §§ 6801-6809.

The Respondents, their attorney, and counsel for the Commission having thereafter executed an Agreement Containing Consent Order ("Consent Agreement"), an admission by the Respondents of all the jurisdictional facts set forth in the aforesaid draft Complaint, a statement that the signing of said Consent Agreement is for settlement purposes only and does not constitute an admission by Respondents that the law has been violated as alleged in such Complaint, or that the facts as alleged in such Complaint, other than jurisdictional facts, are true, and waivers and other provisions as required by the Commission's Rules; and

The Commission having thereafter considered the matter and having determined that it has reason to believe that the Respondents have violated the Federal Trade Commission Act, the Fair Credit Reporting Act, and the Gramm-Leach-Bliley Act's Safeguards Rule, and that a Complaint should issue stating its charges in that respect, and having thereupon accepted the executed Consent Agreement and placed such Consent Agreement on the public record for a period of thirty (30) days for the receipt and consideration of public comments, and having duly considered the comments received from interested persons, now in further conformity with the procedure described in Section 2.34 of its Rules, 16 C.F.R. § 2.34, the Commission hereby issues its Complaint, makes the following jurisdictional findings, and enters the following Order:

- 1a. Respondent SettlementOne is a California corporation with its principal office or place of business at 2605 Camino Del Rio South, Suite 400, San Diego, CA 92108. SettlementOne is a wholly-owned subsidiary of Sackett National Holdings, Inc.
- 1b. Respondent Sackett National Holdings, Inc. is a corporation with its principal office or place of business at 2605 Camino Del Rio South, San Diego, CA 92108. SNH conducts business through its ten wholly-owned subsidiaries, including SettlementOne.

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2. The Federal Trade Commission has jurisdiction of the subject matter of this proceeding and of the Respondents, and the proceeding is in the public interest.

ORDER**DEFINITIONS**

For purposes of this order, the following definitions shall apply:

1. “Personal information” shall mean individually identifiable information from or about an individual consumer including, but not limited to: (a) a first and last name; (b) a home or other physical address, including street name and name of city or town; (c) an email address or other online contact information; (d) a telephone number; (e) a Social Security number; (f) a credit card or debit card account number; (g) checking account information, (h) a driver’s license, military or state identification number; (i) a persistent identifier, such as a customer number, that is combined with other available data that identifies an individual consumer; or (j) any information that is combined with any of (a) through (i) above.
2. “Gramm-Leach-Bliley Act” or “GLB Act” refers to 15 U.S.C. §§ 6801-6809, as amended, the “Safeguards Rule” or the “Standards for Safeguarding Customer Information Rule” refers to 16 C.F.R. Part 314, issued pursuant to Title V, Subtitle A of the GLB Act, 15 U.S.C. §§ 6801-6809.
3. “Financial institution” shall mean as defined in Section 509(3)(A) of the GLB Act, 15 U.S.C. § 6809(3)(A).
4. “The Fair Credit Reporting Act” or “FCRA” refers to 15 U.S.C. § 1681 *et seq.*

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5. “Consumer report” shall mean as defined in Section 603(d)(1) of the FCRA, 15 U.S.C. § 1681a(d)(1).
6. Unless otherwise specified, “respondents” shall mean Sackett National Holdings and SettlementOne Credit Corporation, and their subsidiaries, divisions, affiliates, successors and assigns.
7. “Commerce” shall mean as defined in Section 4 of the Federal Trade Commission Act, 15 U.S.C. § 44.

I.

IT IS ORDERED that respondents shall, no later than the date of service of this order, establish and implement, and thereafter maintain, a comprehensive information security program that is reasonably designed to protect the security, confidentiality, and integrity of personal information collected from or about consumers, including the security, confidentiality, and integrity of personal information accessible to end users. Such program, the content and implementation of which must be fully documented in writing, shall contain administrative, technical, and physical safeguards appropriate to the respondents’ size and complexity, the nature and scope of the respondents’ activities, and the sensitivity of the personal information collected from or about consumers. The information security program must include:

- A. the designation of an employee or employees to coordinate and be accountable for the information security program;
- B. the identification of material internal and external risks to the security, confidentiality, and integrity of personal information that could result in the unauthorized disclosure, misuse, loss, alteration, destruction, or other compromise of such information, and assessment of the sufficiency of any safeguards in place to control these risks. At a minimum, this risk assessment should include consideration of risks in each area of relevant operation, including, but not

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limited to: (1) employee training and management; (2) information systems, including network and software design, access, information processing, storage, transmission, and disposal; and (3) prevention, detection, and response to attacks, intrusions, or other systems failures;

- C. the design and implementation of reasonable safeguards to control the risks identified through risk assessment and regular testing or monitoring of the effectiveness of the safeguards' key controls, systems, and procedures;
- D. the development and use of reasonable steps to select and retain service providers capable of appropriately safeguarding personal information they receive from the respondents, and requiring service providers by contract to implement and maintain appropriate safeguards; and
- E. the evaluation and adjustment of the respondents' information security program in light of the results of the testing and monitoring required by sub-Part C, any material changes to respondents' operations or business arrangements, or any other circumstances that respondents know or have reason to know may have a material impact on the effectiveness of their information security program.

II.

IT IS FURTHER ORDERED that respondents and their officers, agents, representatives, and employees, shall not, directly or through any corporation, subsidiary, division, website, or other device, violate any provision of the Safeguards Rule, 16 C.F.R. Part 314. In the event that this Rule is hereafter amended or modified, respondents' compliance with that Rule as so amended or modified shall not be a violation of this order.

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III.

IT IS FURTHER ORDERED that respondents, in connection with the compilation, creation, sale, or dissemination of any consumer report shall:

- A. Furnish such consumer report only to those persons which it has reason to believe have a permissible purpose as described in Section 604(a)(3) of the Fair Credit Reporting Act, 15 U.S.C. § 1681b(a)(3), or under such other circumstances as set forth in Section 604 of the Fair Credit Reporting Act, 15 U.S.C. § 1681b;
- B. Maintain reasonable procedures to limit the furnishing of such consumer report to those with a permissible purpose and ensure that no consumer report is furnished to any person when there are reasonable grounds to believe that the consumer report will not be used for a permissible purpose, as required by Section 607(a) of the Fair Credit Reporting Act, 15 U.S.C. § 1681e(a).

IV.

IT IS FURTHER ORDERED that respondents shall, in connection with their compliance with Part I of this order, obtain initial and biennial assessments and reports (“Assessments”) from a qualified, objective, independent third-party professional, who uses procedures and standards generally accepted in the profession, provided however, that except for SettlementOne Credit Corporation for which such Assessments are always required, Sackett National Holdings, Inc. shall not be required to obtain such Assessments for any subsidiary, division, affiliate, successor or assign if the personal information such entities collect, maintain, or store from or about consumers is limited to a first and last name; a home or other physical address, including street name and name of city or town; an email address; a telephone number; or publicly available information regarding property ownership and appraised home value. Each Assessment shall be prepared and completed within sixty (60) days after the

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end of the reporting period to which the Assessment applies by a person qualified as a Certified Information System Security Professional (CISSP) or as a Certified Information Systems Auditor (CISA); a person holding Global Information Assurance Certification (GIAC) from the SysAdmin, Audit, Network, Security (SANS) Institute; or a similarly qualified person or organization approved by the Associate Director for Enforcement, Bureau of Consumer Protection, Federal Trade Commission, 600 Pennsylvania Avenue NW, Washington, D.C. 20580. The reporting period for the Assessments shall cover: (1) the first one hundred and eighty (180) days after service of the order for the initial Assessment, and (2) each two (2) year period thereafter for twenty (20) years after service of the order for the biennial Assessments. Each Assessment shall:

- A. set forth the specific administrative, technical, and physical safeguards that respondents have implemented and maintained during the reporting period;
- B. explain how such safeguards are appropriate to respondents' size and complexity, the nature and scope of respondents' activities, and the sensitivity of the personal information collected from or about consumers;
- C. explain how the safeguards that have been implemented meet or exceed the protections required by the Safeguards Rule; and
- D. certify that respondents' security program is operating with sufficient effectiveness to provide reasonable assurance that the security, confidentiality, and integrity of personal information is protected and has so operated throughout the reporting period.

Respondents shall provide the initial Assessment to the Associate Director for Enforcement, Bureau of Consumer Protection, Federal Trade Commission, 600 Pennsylvania Avenue NW, Washington, D.C. 20580, within ten (10) days after the Assessment has been prepared. All subsequent biennial

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Assessments shall be retained by respondents until the order is terminated and provided to the Associate Director of Enforcement within ten (10) days after respondents receive such request.

V.

IT IS FURTHER ORDERED that respondents shall maintain, and upon request make available to the Federal Trade Commission for inspection and copying:

- A. for a period of five (5) years, a print or electronic copy of each document relating to compliance, including but not limited to documents, prepared by or on behalf of respondents, that contradict, qualify, or call into question respondents' compliance with this order;
- B. for a period of five (5) years, copies of all subpoenas and other communications with law enforcement entities or personnel, whether in written or electronic form, if such documents bear in any respect on respondents' collection, maintenance, or furnishing of consumer reports or other personal information of consumers; and
- C. for a period of three (3) years after the date of preparation of each Assessment required under Part IV of this order, all materials relied upon to prepare the Assessment, whether prepared by or on behalf of the respondents, including but not limited to all plans, reports, studies, reviews, audits, audit trails, policies, training materials, and assessments, and any other materials relating to respondents' compliance with Parts I and II of this order, for the compliance period covered by such Assessment.

VI.

IT IS FURTHER ORDERED, that for a period of five (5) years from the date of entry of this Order, respondents shall deliver copies of the Order as directed below:

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- A. Respondents must deliver a copy of this order to (1) all current and future principals, officers, directors and managers, (2) all employees, agents and representatives who engage in conduct related to the subject matter of the order, and (3) any business entity resulting from any change in structure set forth in Part VII. For current personnel, delivery shall be within five (5) days of service of this Order. For new personnel, delivery shall occur prior to them assuming their responsibilities. For any business entity resulting from any change in structure set forth in Part VII, delivery shall be at least ten (10) days prior to the change in structure.
- B. Respondents must secure a signed and dated statement acknowledging receipt of this Order, within thirty (30) days of delivery, from all persons receiving a copy of the Order pursuant to this section.

VII.

IT IS FURTHER ORDERED that respondents shall notify the Commission at least thirty (30) days prior to any change in the corporations that may affect compliance obligations arising under this order, including, but not limited to, a dissolution, assignment, sale, merger, or other action that would result in the emergence of a successor corporation; the creation or dissolution of a subsidiary, parent, or affiliate that engages in any acts or practices subject to this order; the proposed filing of a bankruptcy petition; or a change in the corporate name or address. *Provided, however,* that with respect to any proposed change in the corporations about which respondents learns less than thirty (30) days prior to the date such action is to take place, respondents shall notify the Commission as soon as is practicable after obtaining such knowledge. Unless otherwise directed by a representative of the Commission, all notices required by this Part shall be sent by overnight courier (not the U.S. Postal Service) to the Associate Director of Enforcement, Bureau of Consumer Protection, Federal Trade Commission, 600 Pennsylvania Avenue NW, Washington, D.C. 20580, with the subject line FTC v. SettlementOne Credit Corporation, and Sackett National

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Holdings, Inc. *Provided, however,* that, in lieu of overnight courier, notices may be sent by first-class mail, but only if an electronic version of such notices is contemporaneously sent to the Commission at DEbrief@ftc.gov.

VIII.

IT IS FURTHER ORDERED that respondents and their successors and assigns, within sixty (60) days after the date of service of this order, shall file with the Commission a true and accurate report, in writing, setting forth in detail the manner and form of their own compliance with this order. Within ten (10) day of receipt of written notice from a representative of the Commission, they shall submit additional true and accurate written reports.

IX.

This order will terminate on August 17, 2031, or twenty (20) years from the most recent date that the United States or the Federal Trade Commission files a complaint (with or without an accompanying consent decree) in federal court alleging any violation of the order, whichever comes later; *provided, however,* that the filing of such a complaint will not affect the duration of:

- A. any Part in this order that terminates in less than twenty (20) years;
- B. this order's application to any respondent that is not named as a defendant in such complaint; and
- C. this order if such complaint is filed after the order has terminated pursuant to this Part.

Provided further, that if such complaint is dismissed or a federal court rules that respondents did not violate any provision of the order, and the dismissal or ruling is either not appealed or upheld on appeal, then the order will terminate according to this Part as though the complaint had never been filed, except that the order will not terminate between the date such complaint is filed and the

Analysis to Aid Public Comment

later of the deadline for appealing such dismissal or ruling and the date such dismissal or ruling is upheld on appeal.

By the Commission.

ANALYSIS OF CONSENT ORDER TO AID PUBLIC COMMENT

The Federal Trade Commission has accepted, subject to final approval, three agreements containing consent orders from ACRAnet, Inc. (“ACRAnet”); SettlementOne, Inc. (“SettlementOne”), and its parent corporation Sackett National Holdings, Inc.; and Fajilan and Associates, Inc. d/b/a Statewide Credit Services (“Statewide”) and its principal Robert Fajilan (collectively “respondents”).

The proposed consent orders have been placed on the public record for thirty (30) days for receipt of comments by interested persons. Comments received during this period will become part of the public record. After thirty (30) days, the Commission will again review the agreements and the comments received, and will decide whether it should withdraw from the agreements and take appropriate action or make final the agreements’ proposed orders.

According to the Commission’s proposed complaints, respondents contract with the three nationwide consumer reporting agencies, Experian, Equifax, and TransUnion to obtain consumer reports that they assemble and merge into a single “trimerge report.” The trimerge reports contain sensitive consumer information such as full name, current and former addresses, social security number, date of birth, employer history, credit account histories and information, and account numbers. Respondents provides the trimerge reports to end user clients through an online portal. Respondents issue credentials to their clients, which consist of a user name and password. The end user

Analysis to Aid Public Comment

clients use these credentials to access respondents' online portals and receive trimerged reports.

The Commission's complaints allege that respondents engaged in a number of practices that, taken together, failed to provide reasonable and appropriate security for consumers' personal information. Among other things, they failed to: (a) develop and disseminate comprehensive written information security policies; (b) assess the risks of allowing end users with unverified or inadequate security to access consumer reports through their online portals; (c) implement reasonable steps to address these risks by, for example, evaluating the security of end users' computer networks, requiring appropriate information security measures, and training end user clients; (d) implement reasonable steps to maintain an effective system of monitoring access to consumer reports by end users, including by monitoring to detect anomalies and other suspicious activity; and (e) take appropriate action to correct existing vulnerabilities or threats to personal information in light of known risks.

The complaints further allege that hackers were able to exploit vulnerabilities in the computer networks of multiple end user clients, putting all consumer reports in those networks at risk. In multiple breaches, hackers accessed hundreds of consumer reports.

According to the proposed complaints, respondents' practices violated the Gramm-Leach-Bliley ("GLB") Safeguards Rule by, among other things: (1) failing to design and implement information safeguards to control the risks to customer information; (2) failing to regularly test or monitor the effectiveness of existing controls and procedures; (3) failing to evaluate and adjust the information security programs in light of known or identified risks; and (4) failing to develop, implement, and maintain comprehensive information security programs. In addition, the proposed complaints allege that respondents' conduct violated sections 604 and 607(e) of the Fair Credit Reporting Act ("FCRA"). Further, the proposed complaints allege that respondents' failure to employ reasonable and appropriate measures to secure the personal information they maintain and sell is an unfair practice in violation of Section 5 of the Federal Trade Commission Act.

Analysis to Aid Public Comment

The proposed orders contain provisions designed to prevent respondents from engaging in similar practices in the future. They also apply to personal information respondents collect from or about consumers. The orders name the resellers themselves, ACRAnet, SettlementOne, and Statewide; in the case of SettlementOne, its parent corporation Sackett National Holdings; and in the case of Statewide, its principal Robert Fajilan.

Part I of the proposed orders requires respondents to establish and maintain a comprehensive information security program that is reasonably designed to protect the security, confidentiality, and integrity of personal information collected from or about consumers, including the security, confidentiality, and integrity of personal information accessible to end users.¹ The security program must contain administrative, technical, and physical safeguards appropriate to each respondent's size and complexity, the nature and scope of its activities, and the sensitivity of the personal information collected from or about consumers. Specifically, the orders require respondents to:

- Designate an employee or employees to coordinate and be accountable for the information security program.
- Identify material internal and external risks to the security, confidentiality, and integrity of personal information that could result in the unauthorized disclosure, misuse, loss, alteration, destruction, or other compromise of such information, and assess the sufficiency of any safeguards in place to control these risks.
- Design and implement reasonable safeguards to control the risks identified through risk assessment, and regularly test or monitor the effectiveness of the safeguards' key controls, systems, and procedures.

¹ The proposed order against Statewide includes an individual respondent, Robert Fajilan. Parts I-VI of this order apply to any business entity that Mr. Fajilan controls.

Analysis to Aid Public Comment

- Develop and use reasonable steps to select and retain service providers capable of appropriately safeguarding personal information they receive from respondents, and require service providers by contract to implement and maintain appropriate safeguards.
- Evaluate and adjust the information security program in light of the results of the testing and monitoring, any material changes to the company's operations or business arrangements, or any other circumstances that they know or have reason to know may have a material impact on the effectiveness of their information security program.

Part II of the proposed orders prohibits respondents from violating any provision of the GLB Safeguards Rule.

Part III of the proposed orders requires that respondents, in connection with the compilation, creation, sale or dissemination of any consumer report shall: (1) furnish such consumer report only to those persons it has reason to believe have a permissible purpose as described in Section 604(a)(3) of the FCRA, or under such other circumstances as set forth in Section 604 of the FCRA; and (2) maintain reasonable procedures to limit the furnishing of such consumer reports to those with a permissible purpose and ensure that no consumer report is furnished to any person when there are reasonable grounds to believe that the consumer report will not be used for a permissible purpose.

Part IV of the proposed orders requires that respondents obtain within 180 days, and on a biennial basis thereafter for twenty (20) years, an assessment and report from a qualified, objective, independent third-party professional, certifying, among other things, that they have in place a security program that provides protections that meet or exceed the protections required by Part I of the proposed order; and their security program is operating with sufficient effectiveness to provide reasonable assurance that the security, confidentiality, and integrity of consumers' personal information is protected.²

² The proposed order against SettlementOne and Sackett National Holdings does not require Sackett National Holdings to obtain an assessment for any subsidiary, division, affiliate, successor or assign if the personal

Analysis to Aid Public Comment

Parts V through IX of the proposed orders are reporting and compliance provisions. Part V requires respondents to retain documents relating to their compliance with the orders. For most records, the orders require that the documents be retained for a five-year period. For the third-party assessments and supporting documents, respondents must retain the documents for a period of three years after the date that each assessment is prepared. Part VI requires dissemination of the orders now and in the future to principals, officers, directors, and managers, and all employees, agents and representatives who engage in conduct related to the subject matter of the order. In the ACRAnet and SettlementOne orders, Part VII ensures notification to the FTC of changes in corporate status. In the Statewide order, Part VII requires the individual respondent to notify the FTC of changes in contact information, business or employment status, and Part VIII requires the corporate respondent to notify the FTC of changes in corporate status. Part VIII of the ACRAnet and SettlementOne orders and Part XI of the Statewide order mandates that respondents submit an initial compliance report to the FTC, and make available to the FTC subsequent reports. The last provision of the orders is a provision “sunsetting” the orders after twenty (20) years, with certain exceptions.

The purpose of the analysis is to aid public comment on the proposed orders. It is not intended to constitute an official interpretation of the proposed orders or to modify their terms in any way.

information such entities collect, maintain, or store from or about consumers is limited to a first and last name; a home or other physical address, including street name and name of city or town; an email address; a telephone number; or publicly available information regarding property ownership and appraised home value.

Concurring Statement

**STATEMENT OF COMMISSIONER BRILL, IN WHICH
CHAIRMAN LEIBOWITZ AND COMMISSIONERS
ROSCH AND RAMIREZ JOIN**

The respondents in these three matters are resellers of consumer reports who failed to take reasonable measures to protect sensitive consumer credit information. We fully support staff's work on these matters. We write separately to emphasize that in the future we will call for imposition of civil penalties against resellers of consumer reports who do not take adequate measures to fulfill their obligations to protect information contained in consumer reports, as required by the Fair Credit Reporting Act ("FCRA").

The respondents in these three matters treated their legal obligations to protect consumer information as a paper exercise. Respondents provided only a cursory review of security measures. Thereafter, respondents took no further action to ensure that their customers' security measures adequately protected the information in the consumer reports. Nor did they provide training on security measures to end users. Even after discovering security breaches that should have alerted them to problems with the data security of some customers, respondents failed to implement measures to check the security practices of other clients.

The FCRA requires respondents to take reasonable measures to ensure that consumer reports are given only to entities using the reports for purposes authorized by the statute.¹ As a result of respondents' failure to comply with the FCRA, nearly 2,000 credit reports were improperly accessed. There is no doubt that such unauthorized access can result in grave consumer harm through identity theft.

The significant impact and cost of identity theft are well documented. Although reports regarding the impact of identity theft do not always agree on specific figures, they do reveal tremendous economic and non-economic consequences for both consumers and the economy. The Commission itself issued

¹ 15 U.S.C. § 1681b; 15 U.S.C. § 1681e(a).

Concurring Statement

reports in both 2003² and 2007.³ Our 2007 report estimated that in 2005 alone 8.3 million consumers fell victim to identity theft. We found that 1.8 million of those victims had new accounts opened in their names. One-quarter of the “new account victims” incurred more than \$1,000 in out-of-pocket expenses and five percent spent 1,200 hours in dealing with the consequences of the theft. The report concluded that total losses from identity theft in 2006 totaled \$15.6 billion. Beyond these financial impacts, we also identified non-economic harm to victims in many forms: denial of new credit or loans, harassment from collection agencies, the loss the time involved in resolving the problems, and being subjected to criminal investigation. In view of the hardships and costs brought on by identity theft, measures to prevent it must be rigorously enforced.

While we view the breaches in these cases with alarm, we are also cognizant of the fact that these are the first cases in which the Commission has held resellers responsible for downstream data protection failures.⁴ Looking forward, the actions we announce today should put resellers — indeed, all of those in the chain of handling consumer data — on notice of the seriousness with which we view their legal obligations to proactively protect consumers’ data. The Commission should use all of the tools at its disposal to protect consumers from the enormous risks posed by security breaches that may lead to identity theft. In the future, we should not hesitate to use our authority to seek civil penalties under the FCRA⁵ to make the protection of consumer data a top priority for those who profit from its collection and dissemination.

² Fed. Trade Comm’n. *Identity Theft Survey Report* (2003), available at <http://www.ftc.gov/os/2003/09/synovaterreport.pdf>.

³ Fed. Trade Comm’n, *2006 Identity Theft Survey Report* (2007), available at <http://www.ftc.gov/os/2007/11/SynovateFinalReportIDTheft2006.pdf>.

⁴ The Commission has previously taken action where the credit reporting agency failed to adequately screen purchasers of consumer credit information. For instance, in *United States v. ChoicePoint, Inc.*, 09-CV-0198 (N.D. Ga. Oct. 19, 2009), the Commission alleged that the failure to screen customers led to the sale of 160,000 credit reports to identity thieves posing as customers of ChoicePoint.

⁵ The Fair Credit Reporting Act authorizes the Commission to seek civil penalties for violations of the Act. 15 U.S.C. § 1681s(a)(2)(A).

Complaint

IN THE MATTER OF**ACRANET, INC.****CONSENT ORDER, ETC. IN REGARD TO ALLEGED VIOLATIONS OF
SEC. 5(A) OF THE FEDERAL TRADE COMMISSION ACT, SECS. 604
AND 607(A) OF THE FAIR CREDIT REPORTING ACT, AND THE
GRAMM-LEACH-BLILEY SAFEGUARDS RULE**

*Docket No. C-4331; File No. 092 3088
Filed, August 17, 2011 — Decision, August 17, 2011*

This consent order addresses allegations that ACRANet, Inc. (“Respondent”) failed to provide reasonable and appropriate security for consumers’ personal information. According to the complaint, Respondent obtained sensitive consumer information, much of which is not publicly available, from the three nationwide consumer reporting agencies, Equifax, Experian, and TransUnion. Respondent then used this information to create “trimerge reports,” which it sold to mortgage brokers and others to determine consumers’ eligibility for credit. The complaint alleges that Respondent, among other things, failed to develop comprehensive written information security policies; to implement reasonable steps to maintain an effective system of monitoring access to consumer reports by end users; and take appropriate action to correct existing vulnerabilities or threats to personal information in light of known risks. As a result, hackers were able to exploit vulnerabilities and access hundreds of consumer reports. The order requires Respondent to establish and maintain a comprehensive information security program reasonably designed to protect consumer information. The order further requires Respondent to maintain procedures to ensure that its consumer reports are given only to those persons or entities that will use it for a permissible purpose under the Fair Credit Reporting Act. The order further requires Respondent to obtain an independent, third-party assessment of its security procedures on a biennial basis for the next 20 years.

Participants

For the *Commission*: *Anthony Rodriguez* and *Katherine White*.

For the *Respondent*: *Jed W. Morris, Lukins & Annis*.

Complaint

COMPLAINT

The Federal Trade Commission (“FTC” or “Commission”), having reason to believe that ACRAnet, Inc. has violated the Commission’s Standards for Safeguarding Customer Information Rule (“Safeguards Rule”), 16 C.F.R. Part 314, issued pursuant to Title V, Subtitle A of the Gramm-Leach-Bliley Act (“GLB Act”); 15 U.S.C. §§ 6801- 6809, the Fair Credit Reporting Act (“FCRA”), 15 U.S.C. § 1681 et seq.; and Section 5 of the Federal Trade Commission Act (“FTC Act”), 15 U.S.C. § 45(a), and it appearing to the Commission that this proceeding is in the public interest, alleges:

1. Respondent ACRAnet, Inc. (“ACRAnet”) is a Nevada corporation with its principal office or place of business at 521 W. Maxwell, Spokane, Washington 99201.

2. The acts and practices of respondent as alleged in this complaint have been in or affecting commerce, as “commerce” is defined in Section 4 of the FTC Act, 15 U.S.C. § 44.

3. ACRAnet contracts with the three nationwide consumer reporting agencies, Equifax, Experian, and TransUnion (“nationwide CRAs”) to obtain consumer reports that it assembles and merges into a single “trimerge report.” The trimerge reports contain sensitive consumer information such as full name, current and former addresses, Social Security number, date of birth, employer history, trade lines, and even account numbers. Much of this sensitive information is not publicly available. These “trimerge reports” are “consumer reports” as defined in Section 603(d) of the FCRA, 15 U.S.C. § 1681a(d).

4. Respondent sells these trimerge reports to mortgage brokers and others to determine consumers’ eligibility for credit. In creating and selling the trimerge reports to end user clients, respondent ACRAnet is a consumer reporting agency as that term is defined in Section 603(f) of the FCRA, 15 U.S.C. § 1681(f).

5. Respondent ACRAnet is a “financial institution” as that term is defined by Section 509(3)(A) of the GLB Act, 15 U.S.C. §

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6809 (3)(A), and is therefore subject to the requirements of the Safeguards Rule.

RESPONDENTS' COURSE OF CONDUCT

6. ACRAnet furnishes its end user clients with trimerge reports through an online portal. It issues credentials to its clients, which consist of a user name and password. The end user clients use these credentials to access ACRAnet's online portal and receive trimerge reports.

7. From at least December 2007, respondent has engaged in a number of practices that, taken together, failed to provide reasonable and appropriate security for consumers' personal information. Among other things, respondent failed to:

- a. develop and disseminate comprehensive information security policies;
- b. assess the risks of allowing end users with unverified or inadequate security to access consumer reports through ACRAnet's portal;
- c. implement reasonable steps to address these risks by, for example, evaluating the security of end user's computer networks, requiring appropriate information security measures, and training end user clients;
- d. implement reasonable steps to maintain an effective system of monitoring access to consumer reports by ACRAnet's end users, including by monitoring to detect anomalies and other suspicious activity; and
- e. take appropriate action to correct existing vulnerabilities or threats to personal information in light of known risks.

8. Because of ACRAnet's lack of information security policies and procedures, respondent allows clients without basic security measures in place, such as firewalls and updated antivirus software, to have access to its trimerge reports. The lack of such

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security measures directly caused highly-sensitive consumer reports to be available to hackers, as explained below.

THE BREACHES

9. As a direct result of these failures, between December 2007 and November 2008, hackers were able to exploit vulnerabilities in the computer networks of multiple ACRA net end user clients, putting consumer reports in those networks at risk. In multiple breaches, hackers accessed at least 694 consumer reports without authorization. Additionally, the hackers had the ability to view any consumer report that the end user client had pulled in the previous 90 days.

10. Following each of the breaches, respondent did not make reasonable efforts to protect against future breaches. For example, respondent did not change any of its policies for screening new end users and did not require that new and existing end user clients submit any documentation demonstrating that the clients' computer systems were virus free and otherwise properly protected. Respondent continues to give access to consumer reports to end user clients whose information security has not been adequately verified.

VIOLATIONS OF THE SAFEGUARDS RULE

11. The Safeguards Rule, which implements Section 501(b) of the GLB Act, 15 U.S.C. § 6801(b), was promulgated by the Commission on May 23, 2002, and became effective on May 23, 2003. The Rule requires financial institutions to protect the security, confidentiality, and integrity of customer information by developing a comprehensive written information security program that contains reasonable administrative, technical, and physical safeguards that include: (1) designating one or more employees to coordinate the information security program; (2) identifying reasonably foreseeable internal and external risks to the security, confidentiality, and integrity of customer information, and assessing the sufficiency of any safeguards in place to control those risks; (3) designing and implementing information safeguards to control the risks identified through risk assessment, and regularly testing or otherwise monitoring the effectiveness of

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the safeguards' key controls, systems, and procedures; (4) overseeing service providers and requiring them by contract to protect the security and confidentiality of customer information; and (5) evaluating and adjusting the information security program in light of the results of testing and monitoring, changes to the business operation, and other relevant circumstances. 16 C.F.R. §§ 314.3, 314.4.

12. As described in Paragraphs 6 through 10, respondent failed to implement reasonable security policies and procedures to protect sensitive consumer information, and has thereby engaged in violations of the Safeguards Rule by, among other things:

- a. failing to design and implement information safeguards to control the risks to customer information;
- b. failing to regularly test or monitor the effectiveness of its existing controls and procedures;
- c. failing to evaluate and adjust the information security program in light of known or identified risks; and
- d. failing to develop, implement, and maintain a comprehensive information security program.

VIOLATIONS OF THE FCRA

13. Section 604 of the FCRA, 15 U.S.C. § 1681b, prohibits a consumer reporting agency from furnishing a consumer report except for specified "permissible purposes." As described in Paragraph 9, in multiple instances, respondent furnished consumer reports to hackers that did not have a permissible purpose to obtain a consumer report. By and through the acts and practices described in Paragraphs 6 through 10, respondent has violated Section 604 of the FCRA, 15 U.S.C. § 1681b.

14. Section 607(a) of the FCRA, 15 U.S.C. § 1681e(a), requires every consumer reporting agency to maintain reasonable procedures to limit the furnishing of consumer reports to the purposes listed under Section 604 of the FCRA, 15 U.S.C. §

Complaint

1681b. As described in Paragraphs 6 through 10, respondent failed to maintain reasonable procedures to limit the furnishing of consumer reports to the purposes listed under Section 604 of the FCRA. By and through the acts and practices described in Paragraphs 6 through 10, respondent has violated Section 607(a) of the FCRA, 15 U.S.C. § 1681e(a).

15. Section 607(a) of the FCRA, 15 U.S.C. § 1681e(a), prohibits a consumer reporting agency from furnishing a consumer report to any person if it has reasonable grounds for believing that the consumer report will not be used for a permissible purpose. As described in Paragraphs 9 and 10, in numerous instances, respondent furnished consumer reports under circumstances in which it had reasonable grounds for believing that the reports would not be used for a permissible purpose. By and through the acts and practices described in Paragraphs 9 and 10, respondent has violated Section 607(a) of the FCRA, 15 U.S.C. § 1681e(a).

16. By its violations of Sections 604 and 607(a) of the FCRA, and pursuant to Section 621(a) thereof, 15 U.S.C. § 1681s, respondent has engaged in unfair and deceptive acts and practices in or affecting commerce, in violation of Section 5(a) of the FTC Act, 15 U.S.C. § 45(a).

VIOLATIONS OF THE FTC ACT

17. As described in Paragraphs 6 through 10, respondent has not employed reasonable and appropriate measures to secure the personal information it maintains and sells. Respondent's failure to employ reasonable and appropriate security measures to protect consumers' personal information has caused or is likely to cause substantial injury to consumers that is not offset by countervailing benefits to consumers or competition and is not reasonably avoidable by consumers. This practice was, and is, an unfair act or practice in or affecting commerce in violation of Section 5(a) of the Federal Trade Commission Act, 15 U.S.C. § 45(a).

Decision and Order

THEREFORE, the Federal Trade Commission this seventeenth day of August, 2011, has issued this complaint against respondent.

By the Commission.

DECISION AND ORDER

The Federal Trade Commission having initiated an investigation of certain acts and practices of the Respondent named in the caption hereof, and the Respondent having been furnished thereafter with a copy of a draft Complaint that the Bureau of Consumer Protection proposed to present to the Commission for its consideration and which, if issued by the Commission, would charge the Respondent with violation of the Federal Trade Commission Act, 15 U.S.C. § 45 et seq; the Fair Credit Reporting Act, 15 U.S.C. § 1681 et seq; and the Commission's Standards for Safeguarding Customer Information Rule, 16 C.F.R. Part 314, issued pursuant to Title V, Subtitle A of the Gramm-Leach-Bliley Act, 15 U.S.C. §§ 6801-6809.

The Respondent, its attorney, and counsel for the Commission having thereafter executed an Agreement Containing Consent Order ("Consent Agreement"), an admission by the Respondent of all the jurisdictional facts set forth in the aforesaid draft Complaint, a statement that the signing of said Consent Agreement is for settlement purposes only and does not constitute an admission by Respondent that the law has been violated as alleged in such Complaint, or that the facts as alleged in such Complaint, other than jurisdictional facts, are true, and waives and other provisions as required by the Commission's Rules; and

The Commission having thereafter considered the matter and having determined that it has reason to believe that the Respondent has violated the Federal Trade Commission Act, Fair

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Credit Reporting Act, and the Gramm-Leach-Bliley Act's Safeguards Rule and that a Complaint should issue stating its charges in that respect, and having thereupon accepted the executed Consent Agreement and placed such Consent Agreement on the public record for a period of thirty (30) days for the receipt and consideration of public comments, and having duly considered the comments received from interested persons, now in further conformity with the procedure described in Section 2.34 of its Rules, 16 C.F.R. § 2.34, the Commission hereby issues its Complaint, makes the following jurisdictional findings, and enters the following Order:

1. Respondent ACRAnet, Inc. is a Nevada corporation with its principal office or place of business at 521 W. Maxwell, Spokane, Washington 99201.
2. The Federal Trade Commission has jurisdiction of the subject matter of this proceeding and of the Respondents, and the proceeding is in the public interest.

ORDER**DEFINITIONS**

For purposes of this order, the following definitions shall apply:

1. "Personal information" shall mean individually identifiable information from or about an individual consumer including, but not limited to: (a) a first and last name; (b) a home or other physical address, including street name and name of city or town; (c) an email address or other online contact information; (d) a telephone number; (e) a Social Security number; (f) a credit card or debit card account number; (g) checking account information, (h) a driver's license, military or state identification number; (i) a persistent identifier, such as a customer number, that is combined with other available data that identifies an individual

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consumer; or (j) any information that is combined with any of (a) through (i) above.

2. “Gramm-Leach-Bliley Act” or “GLB Act” refers to 15 U.S.C. §§ 6801-6809, as amended, the “Safeguards Rule” or the “Standards for Safeguarding Customer Information Rule” refers to 16 C.F.R. Part 314, issued pursuant to Title V, Subtitle A of the GLB Act, 15 U.S.C. §§ 6801-6809.
3. “Financial institution” shall mean as defined in Section 509(3)(A) of the GLB Act, 15 U.S.C. § 6809(3)(A).
4. “The Fair Credit Reporting Act” or “FCRA” refers to 15 U.S.C. § 1681 et seq.
5. “Consumer report” shall mean as defined in Section 603(d)(1) of the FCRA, 15 U.S.C. § 1681a(d)(1).
6. Unless otherwise specified, “respondent” shall mean ACRAnet, Inc. and its subsidiaries, divisions, affiliates, successors and assigns.
7. “Commerce” shall mean as defined in Section 4 of the Federal Trade Commission Act, 15 U.S.C. § 44.

I.

IT IS ORDERED that respondent shall, no later than the date of service of this order, establish and implement, and thereafter maintain, a comprehensive information security program that is reasonably designed to protect the security, confidentiality, and integrity of personal information collected from or about consumers, including the security, confidentiality, and integrity of personal information accessible to end users. Such program, the content and implementation of which must be fully documented in writing, shall contain administrative, technical, and physical safeguards appropriate to respondent’s size and complexity, the nature and scope of respondent’s activities, and the sensitivity of the personal information collected from or about consumers. The information security program must include:

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- A. the designation of an employee or employees to coordinate and be accountable for the information security program;
- B. the identification of material internal and external risks to the security, confidentiality, and integrity of personal information that could result in the unauthorized disclosure, misuse, loss, alteration, destruction, or other compromise of such information, and assessment of the sufficiency of any safeguards in place to control these risks. At a minimum, this risk assessment should include consideration of risks in each area of relevant operation, including, but not limited to: (1) employee training and management; (2) information systems, including network and software design, access, information processing, storage, transmission, and disposal; and (3) prevention, detection, and response to attacks, intrusions, or other systems failures;
- C. the design and implementation of reasonable safeguards to control the risks identified through risk assessment and regular testing or monitoring of the effectiveness of the safeguards' key controls, systems, and procedures;
- D. the development and use of reasonable steps to select and retain service providers capable of appropriately safeguarding personal information they receive from the respondent, and requiring service providers by contract to implement and maintain appropriate safeguards; and
- E. the evaluation and adjustment of respondent's information security program in light of the results of the testing and monitoring required by sub-Part C, any material changes to respondent's operations or business arrangements, or any other circumstances that respondent knows or has reason to know may have a

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material impact on the effectiveness of its information security program.

II.

IT IS FURTHER ORDERED that respondent and its officers, agents, representatives, and employees, shall not, directly or through any corporation, subsidiary, division, website, or other device, violate any provision of the Safeguards Rule, 16 C.F.R. Part 314. In the event that this Rule is hereafter amended or modified, respondent's compliance with that Rule as so amended or modified shall not be a violation of this order.

III.

IT IS FURTHER ORDERED that respondent, in connection with the compilation, creation, sale, or dissemination of any consumer report shall:

- A. Furnish such consumer report only to those persons which it has reason to believe have a permissible purpose as described in Section 604(a)(3) of the Fair Credit Reporting Act, 15 U.S.C. § 1681b(a)(3), or in such other circumstances as set forth in Section 604 of the Fair Credit Reporting Act, 15 U.S.C. § 1681b; and
- B. Maintain reasonable procedures to limit the furnishing of such consumer report to those with a permissible purpose and ensure that no consumer report is furnished to any person when there are reasonable grounds to believe that the consumer report will not be used for a permissible purpose, as required by Section 607(a) of the Fair Credit Reporting Act, 15 U.S.C. § 1681e(a).

IV.

IT IS FURTHER ORDERED that respondent shall, in connection with its compliance with Part I of this order, obtain initial and biennial assessments and reports ("Assessments") from a qualified, objective, independent third-party professional, who

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uses procedures and standards generally accepted in the profession. Each Assessment shall be prepared and completed within sixty (60) days after the end of the reporting period to which the Assessment applies by a person qualified as a Certified Information System Security Professional (CISSP) or as a Certified Information Systems Auditor (CISA); a person holding Global Information Assurance Certification (GIAC) from the SysAdmin, Audit, Network, Security (SANS) Institute; or a similarly qualified person or organization approved by the Associate Director for Enforcement, Bureau of Consumer Protection, 600 Pennsylvania Avenue NW, Federal Trade Commission, Washington, D.C. 20580. The reporting period for the Assessments shall cover: (1) the first one hundred and eighty (180) days after service of the order for the initial Assessment, and (2) each two (2) year period thereafter for twenty (20) years after service of the order for the biennial Assessments. Each Assessment shall:

- A. set forth the specific administrative, technical, and physical safeguards that respondent has implemented and maintained during the reporting period;
- B. explain how such safeguards are appropriate to respondent's size and complexity, the nature and scope of respondent's activities, and the sensitivity of the personal information collected from or about consumers;
- C. explain how the safeguards that have been implemented meet or exceed the protections required by the Safeguards Rule; and
- D. certify that respondent's security program is operating with sufficient effectiveness to provide reasonable assurance that the security, confidentiality, and integrity of personal information is protected and has so operated throughout the reporting period.

Respondent shall provide the initial Assessment to the Associate Director for Enforcement, Bureau of Consumer Protection, Federal Trade Commission, 600 Pennsylvania Avenue NW, Washington, D.C. 20580, within ten (10) days after the

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Assessment has been prepared. All subsequent biennial Assessments shall be retained by respondent until the order is terminated and provided to the Associate Director of Enforcement within ten (10) days after respondent receives such request.

V.

IT IS FURTHER ORDERED that respondent shall maintain, and upon request make available to the Federal Trade Commission for inspection and copying:

- A. for a period of five (5) years, a print or electronic copy of each document relating to compliance, including but not limited to documents, prepared by or on behalf of respondent, that contradict, qualify, or call into question respondent's compliance with this order;
- B. for a period of five (5) years, copies of all subpoenas and other communications with law enforcement entities or personnel, whether in written or electronic form, if such documents bear in any respect on respondent's collection, maintenance, or furnishing of consumer reports or other personal information of consumers; and
- C. for a period of three (3) years after the date of preparation of each Assessment required under Part IV of this order, all materials relied upon to prepare the Assessment, whether prepared by or on behalf of the respondent, including but not limited to all plans, reports, studies, reviews, audits, audit trails, policies, training materials, and assessments, and any other materials relating to the respondent's compliance with Parts I and II of this order, for the compliance period covered by such Assessment.

VI.

IT IS FURTHER ORDERED that for a period of five (5) years from the date of entry of this Order, respondent shall deliver copies of the Order as directed below:

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- A. Respondent must deliver a copy of this Order to (1) all current and future principals, officers, directors, and managers, (2) all employees, agents and representatives who engage in conduct related to the subject matter of the Order, and (3) any business entity resulting from any change in structure set forth in Part VII. For current personnel, delivery shall be within five (5) days of service of this Order. For new personnel, delivery shall occur prior to them assuming their responsibilities. For any business entity resulting from any change in structure set forth in Part VII, delivery shall be at least ten (10) days prior to the change in structure.
- B. Respondent must secure a signed and dated statement acknowledging receipt of this Order, within thirty (30) days of delivery, from all persons receiving a copy of the Order pursuant to this section.

VII.

IT IS FURTHER ORDERED that respondent shall notify the Commission at least thirty (30) days prior to any change in the corporation that may affect compliance obligations arising under this order, including, but not limited to, a dissolution, assignment, sale, merger, or other action that would result in the emergence of a successor corporation; the creation or dissolution of a subsidiary, parent, or affiliate that engages in any acts or practices subject to this Order; the proposed filing of a bankruptcy petition; or a change in the corporate name or address. *Provided, however*, that with respect to any proposed change in the corporation about which respondent learns less than thirty (30) days prior to the date such action is to take place, respondent shall notify the Commission as soon as is practicable after obtaining such knowledge. Unless otherwise directed by a representative of the Commission, all notices required by this Part shall be sent by overnight courier (not the U.S. Postal Service) to the Associate Director of Enforcement, Bureau of Consumer Protection, Federal Trade Commission, 600 Pennsylvania Avenue NW, Washington, D.C. 20580, with the subject line FTC v. ACRAnet, Inc.

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Provided, however, that, in lieu of overnight courier, notices may be sent by first-class mail, but only if an electronic version of such notices is contemporaneously sent to the Commission at DEbrief@ftc.gov.

VIII.

IT IS FURTHER ORDERED that respondent, and its successors and assigns, within sixty (60) days after the date of service of this order, shall file with the Commission a true and accurate report, in writing, setting forth in detail the manner and form of their own compliance with this order. Within ten (10) days of receipt of written notice from a representative of the Commission, they shall submit additional true and accurate written reports.

IX.

This order will terminate on August 17, 2031, or twenty (20) years from the most recent date that the United States or the Federal Trade Commission files a complaint (with or without an accompanying consent decree) in federal court alleging any violation of the order, whichever comes later; *provided, however,* that the filing of such a complaint will not affect the duration of:

- A. any Part in this order that terminates in less than twenty (20) years;
- B. this order's application to any respondent that is not named as a defendant in such complaint; and
- C. this order if such complaint is filed after the order has terminated pursuant to this Part.

Provided, further, that if such complaint is dismissed or a federal court rules that respondent did not violate any provision of the order, and the dismissal or ruling is either not appealed or upheld on appeal, then the order will terminate according to this Part as though the complaint had never been filed, except that the order will not terminate between the date such complaint is filed and the

Analysis to Aid Public Comment

later of the deadline for appealing such dismissal or ruling and the date such dismissal or ruling is upheld on appeal.

By the Commission.

**ANALYSIS OF CONSENT ORDER TO AID PUBLIC
COMMENT**

The Federal Trade Commission has accepted, subject to final approval, three agreements containing consent orders from ACRAnet, Inc. (“ACRAnet”); SettlementOne, Inc. (“SettlementOne”), and its parent corporation Sackett National Holdings, Inc.; and Fajilan and Associates, Inc. d/b/a Statewide Credit Services (“Statewide”) and its principal Robert Fajilan (collectively “respondents”).

The proposed consent orders have been placed on the public record for thirty (30) days for receipt of comments by interested persons. Comments received during this period will become part of the public record. After thirty (30) days, the Commission will again review the agreements and the comments received, and will decide whether it should withdraw from the agreements and take appropriate action or make final the agreements’ proposed orders.

According to the Commission’s proposed complaints, respondents contract with the three nationwide consumer reporting agencies, Experian, Equifax, and TransUnion to obtain consumer reports that they assemble and merge into a single “trimerge report.” The trimerge reports contain sensitive consumer information such as full name, current and former addresses, social security number, date of birth, employer history, credit account histories and information, and account numbers. Respondents provides the trimerge reports to end user clients through an online portal. Respondents issue credentials to their clients, which consist of a user name and password. The end user

Analysis to Aid Public Comment

clients use these credentials to access respondents' online portals and receive trimerged reports.

The Commission's complaints allege that respondents engaged in a number of practices that, taken together, failed to provide reasonable and appropriate security for consumers' personal information. Among other things, they failed to: (a) develop and disseminate comprehensive written information security policies; (b) assess the risks of allowing end users with unverified or inadequate security to access consumer reports through their online portals; (c) implement reasonable steps to address these risks by, for example, evaluating the security of end users' computer networks, requiring appropriate information security measures, and training end user clients; (d) implement reasonable steps to maintain an effective system of monitoring access to consumer reports by end users, including by monitoring to detect anomalies and other suspicious activity; and (e) take appropriate action to correct existing vulnerabilities or threats to personal information in light of known risks.

The complaints further allege that hackers were able to exploit vulnerabilities in the computer networks of multiple end user clients, putting all consumer reports in those networks at risk. In multiple breaches, hackers accessed hundreds of consumer reports.

According to the proposed complaints, respondents' practices violated the Gramm-Leach-Bliley ("GLB") Safeguards Rule by, among other things: (1) failing to design and implement information safeguards to control the risks to customer information; (2) failing to regularly test or monitor the effectiveness of existing controls and procedures; (3) failing to evaluate and adjust the information security programs in light of known or identified risks; and (4) failing to develop, implement, and maintain comprehensive information security programs. In addition, the proposed complaints allege that respondents' conduct violated sections 604 and 607(e) of the Fair Credit Reporting Act ("FCRA"). Further, the proposed complaints allege that respondents' failure to employ reasonable and appropriate measures to secure the personal information they maintain and sell is an unfair practice in violation of Section 5 of the Federal Trade Commission Act.

Analysis to Aid Public Comment

The proposed orders contain provisions designed to prevent respondents from engaging in similar practices in the future. They also apply to personal information respondents collect from or about consumers. The orders name the resellers themselves, ACRAnet, SettlementOne, and Statewide; in the case of SettlementOne, its parent corporation Sackett National Holdings; and in the case of Statewide, its principal Robert Fajilan.

Part I of the proposed orders requires respondents to establish and maintain a comprehensive information security program that is reasonably designed to protect the security, confidentiality, and integrity of personal information collected from or about consumers, including the security, confidentiality, and integrity of personal information accessible to end users.¹ The security program must contain administrative, technical, and physical safeguards appropriate to each respondent's size and complexity, the nature and scope of its activities, and the sensitivity of the personal information collected from or about consumers. Specifically, the orders require respondents to:

- Designate an employee or employees to coordinate and be accountable for the information security program.
- Identify material internal and external risks to the security, confidentiality, and integrity of personal information that could result in the unauthorized disclosure, misuse, loss, alteration, destruction, or other compromise of such information, and assess the sufficiency of any safeguards in place to control these risks.
- Design and implement reasonable safeguards to control the risks identified through risk assessment, and regularly test or monitor the effectiveness of the safeguards' key controls, systems, and procedures.

¹ The proposed order against Statewide includes an individual respondent, Robert Fajilan. Parts I-VI of this order apply to any business entity that Mr. Fajilan controls.

Analysis to Aid Public Comment

- Develop and use reasonable steps to select and retain service providers capable of appropriately safeguarding personal information they receive from respondents, and require service providers by contract to implement and maintain appropriate safeguards.
- Evaluate and adjust the information security program in light of the results of the testing and monitoring, any material changes to the company's operations or business arrangements, or any other circumstances that they know or have reason to know may have a material impact on the effectiveness of their information security program.

Part II of the proposed orders prohibits respondents from violating any provision of the GLB Safeguards Rule.

Part III of the proposed orders requires that respondents, in connection with the compilation, creation, sale or dissemination of any consumer report shall: (1) furnish such consumer report only to those persons it has reason to believe have a permissible purpose as described in Section 604(a)(3) of the FCRA, or under such other circumstances as set forth in Section 604 of the FCRA; and (2) maintain reasonable procedures to limit the furnishing of such consumer reports to those with a permissible purpose and ensure that no consumer report is furnished to any person when there are reasonable grounds to believe that the consumer report will not be used for a permissible purpose.

Part IV of the proposed orders requires that respondents obtain within 180 days, and on a biennial basis thereafter for twenty (20) years, an assessment and report from a qualified, objective, independent third-party professional, certifying, among other things, that they have in place a security program that provides protections that meet or exceed the protections required by Part I of the proposed order; and their security program is operating with sufficient effectiveness to provide reasonable assurance that the security, confidentiality, and integrity of consumers' personal information is protected.²

² The proposed order against SettlementOne and Sackett National Holdings does not require Sackett National Holdings to obtain an assessment

Analysis to Aid Public Comment

Parts V through IX of the proposed orders are reporting and compliance provisions. Part V requires respondents to retain documents relating to their compliance with the orders. For most records, the orders require that the documents be retained for a five-year period. For the third-party assessments and supporting documents, respondents must retain the documents for a period of three years after the date that each assessment is prepared. Part VI requires dissemination of the orders now and in the future to principals, officers, directors, and managers, and all employees, agents and representatives who engage in conduct related to the subject matter of the order. In the ACRAnet and SettlementOne orders, Part VII ensures notification to the FTC of changes in corporate status. In the Statewide order, Part VII requires the individual respondent to notify the FTC of changes in contact information, business or employment status, and Part VIII requires the corporate respondent to notify the FTC of changes in corporate status. Part VIII of the ACRAnet and SettlementOne orders and Part XI of the Statewide order mandates that respondents submit an initial compliance report to the FTC, and make available to the FTC subsequent reports. The last provision of the orders is a provision “sunsetting” the orders after twenty (20) years, with certain exceptions.

The purpose of the analysis is to aid public comment on the proposed orders. It is not intended to constitute an official interpretation of the proposed orders or to modify their terms in any way.

for any subsidiary, division, affiliate, successor or assign if the personal information such entities collect, maintain, or store from or about consumers is limited to a first and last name; a home or other physical address, including street name and name of city or town; an email address; a telephone number; or publicly available information regarding property ownership and appraised home value.

Concurring Statement

**STATEMENT OF COMMISSIONER BRILL, IN WHICH
CHAIRMAN LEIBOWITZ AND COMMISSIONERS
ROSCH AND RAMIREZ JOIN**

The respondents in these three matters are resellers of consumer reports who failed to take reasonable measures to protect sensitive consumer credit information. We fully support staff's work on these matters. We write separately to emphasize that in the future we will call for imposition of civil penalties against resellers of consumer reports who do not take adequate measures to fulfill their obligations to protect information contained in consumer reports, as required by the Fair Credit Reporting Act ("FCRA").

The respondents in these three matters treated their legal obligations to protect consumer information as a paper exercise. Respondents provided only a cursory review of security measures. Thereafter, respondents took no further action to ensure that their customers' security measures adequately protected the information in the consumer reports. Nor did they provide training on security measures to end users. Even after discovering security breaches that should have alerted them to problems with the data security of some customers, respondents failed to implement measures to check the security practices of other clients.

The FCRA requires respondents to take reasonable measures to ensure that consumer reports are given only to entities using the reports for purposes authorized by the statute.¹ As a result of respondents' failure to comply with the FCRA, nearly 2,000 credit reports were improperly accessed. There is not doubt that such unauthorized access can result in grave consumer harm through identity theft.

The significant impact and cost of identity theft are well documented. Although reports regarding the impact of identity theft do not always agree on specific figures, they do reveal tremendous economic and non-economic consequences for both consumers and the economy. The Commission itself issued

¹ 15 U.S.C. § 1681b; 15 U.S.C. § 1681e(a).

Concurring Statement

reports in both 2003² and 2007.³ Our 2007 report estimated that in 2005 alone 8.3 million consumers fell victim to identity theft. We found that 1.8 million of those victims had new accounts opened in their names. One-quarter of the “new account victims” incurred more than \$1,000 in out-of-pocket expenses and five percent spent 1,200 hours in dealing with the consequences of the theft. The report concluded that total losses from identity theft in 2006 totaled \$15.6 billion. Beyond these financial impacts, we also identified non-economic harm to victims in many forms: denial of new credit or loans, harassment from collection agencies, the loss the time involved in resolving the problems, and being subjected to criminal investigation. In view of the hardships and costs brought on by identity theft, measures to prevent it must be rigorously enforced.

While we view the breaches in these cases with alarm, we are also cognizant of the fact that these are the first cases in which the Commission has held resellers responsible for downstream data protection failures.⁴ Looking forward, the actions we announce today should put resellers — indeed, all of those in the chain of handling consumer data — on notice of the seriousness with which we view their legal obligations to proactively protect consumers’ data. The Commission should use all of the tools at its disposal to protect consumers from the enormous risks posed by security breaches that may lead to identity theft. In the future, we should not hesitate to use our authority to seek civil penalties under the FCRA⁵ to make the protection of consumer data a top priority for those who profit from its collection and dissemination.

² Fed. Trade Comm’n. *Identity Theft Survey Report* (2003), available at <http://www.ftc.gov/os/2003/09/synovaterreport.pdf>.

³ Fed. Trade Comm’n, *2006 Identity Theft Survey Report* (2007), available at <http://www.ftc.gov/os/2007/11/SynovateFinalReportIDTheft2006.pdf>.

⁴ The Commission has previously taken action where the credit reporting agency failed to adequately screen purchasers of consumer credit information. For instance, in *United States v. ChoicePoint, Inc.*, 09-CV-0198 (N.D. Ga. Oct. 19, 2009), the Commission alleged that the failure to screen customers led to the sale of 160,000 credit reports to identity thieves posing as customers of ChoicePoint.

⁵ The Fair Credit Reporting Act authorizes the Commission to seek civil penalties for violations of the Act. 15 U.S.C. § 1681s(a)(2)(A).

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IN THE MATTER OF

**FAJILAN AND ASSOCIATES, INC.
D/B/A STATEWIDE CREDIT SERVICES
AND
ROBERT FAJILAN**

CONSENT ORDER, ETC. IN REGARD TO ALLEGED VIOLATIONS OF
SEC. 5(A) OF THE FEDERAL TRADE COMMISSION ACT, SECS. 604
AND 607(A) OF THE FAIR CREDIT REPORTING ACT, AND THE
GRAMM-LEACH-BLILEY SAFEGUARDS RULE

*Docket No. C-4332; File No. 092 3089
Filed, August 17, 2011 — Decision, August 17, 2011*

This consent order addresses allegations that Fajilan and Associates, Inc., doing business as Statewide Credit Services, and its owner Robert Fajilan (“Respondents”) failed to provide reasonable and appropriate security for consumers’ personal information. According to the complaint, Respondents obtained sensitive consumer information, much of which is not publicly available, from the three nationwide consumer reporting agencies, Equifax, Experian, and TransUnion. Respondents then used this information to create “trimerge reports,” which it sold to mortgage brokers and others to determine consumers’ eligibility for credit. The complaint alleges that Respondents, among other things, failed to develop comprehensive written information security policies; to implement reasonable steps to maintain an effective system of monitoring access to consumer reports by end users; and take appropriate action to correct existing vulnerabilities or threats to personal information in light of known risks. As a result, hackers were able to exploit vulnerabilities and access hundreds of consumer reports. The order requires Respondents to establish and maintain a comprehensive information security program reasonably designed to protect consumer information. The order further requires Respondents to maintain procedures to ensure that its consumer reports are given only to those persons or entities that will use it for a permissible purpose under the Fair Credit Reporting Act. The order further requires Respondents to obtain an independent, third-party assessment of its security procedures on a biennial basis for the next 20 years.

Participants

For the *Commission*: *Anthony Rodriguez* and *Katherine White*.

For the *Respondents*: *Pro Se*.

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COMPLAINT

The Federal Trade Commission (“FTC” or “Commission”), having reason to believe that Fajilan and Associates, Inc. also d/b/a Statewide Credit Services, and Robert Fajilan have violated the Commission’s Standards for Safeguarding Customer Information Rule (“Safeguards Rule”), 16 C.F.R. Part 314, issued pursuant to Title V, Subtitle A of the Gramm-Leach-Bliley Act (“GLB Act”); 15 U.S.C. §§ 6801-6809, the Fair Credit Reporting Act (“FCRA”), 15 U.S.C. § 1681 et seq.; and Section 5 of the Federal Trade Commission Act (“FTC Act”), 15 U.S.C. § 45(a), and it appearing to the Commission that this proceeding is in the public interest, alleges:

1. Respondent Fajilan and Associates, Inc. also d/b/a Statewide Credit Services (“Statewide”) is a California corporation with its principal office or place of business at 2690 South White Road, Suite 235, San Jose, California 95148.

2. Respondent Robert Fajilan (“Fajilan”) is owner and President of Statewide. At all times material to this complaint, acting alone or in concert with others, Robert Fajilan has formulated, directed, or controlled the acts or practices of Statewide, including the various acts or practices alleged in this complaint. His principal office or place of business is the same as Statewide.

3. The acts and practices of respondents as alleged in this complaint have been in or affecting commerce, as “commerce” is defined in Section 4 of the FTC Act, 15 U.S.C. § 44.

4. Statewide contracts with the three nationwide consumer reporting agencies, Equifax, Experian, and TransUnion (“nationwide CRAs”) to obtain consumer reports that it assembles and merges into a single “trimerge report.” The trimerge reports contain sensitive consumer information such as full name, current and former addresses, Social Security number, date of birth, employer history, credit account histories and information, and even account numbers. Much of this sensitive information is not publicly available. These “trimerge reports” are “consumer

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reports” as defined in Section 603(d) of the FCRA, 15 U.S.C. § 1681a(d).

5. Respondents sell these trimerge reports to mortgage brokers and others to determine consumers’ eligibility for credit. In creating and selling the trimerge reports to end user clients, respondent Statewide is a “consumer reporting agency” as that term is defined in Section 603(f) of the FCRA, 15 U.S.C. § 1681(f).

6. Respondent Statewide is a “financial institution” as that term is defined by Section 509(3)(A) of the GLB Act, 15 U.S.C. § 6809(3)(A), and is therefore subject to the requirements of the Safeguards Rule.

RESPONDENTS’ COURSE OF CONDUCT

7. Statewide furnishes its end user clients with trimerge reports through an online portal. It issues credentials to its clients, which consist of a user name and password. The end user clients use these credentials to access Statewide’s online portal and receive trimerged reports.

8. From at least October 2006, respondents have engaged in a number of practices that, taken together, failed to provide reasonable and appropriate security for consumers’ personal information. Among other things, respondents failed to:

- a. develop and disseminate information security policies for Statewide and its end user clients;
- b. assess the risks of allowing end users with unverified or inadequate security to access consumer reports through Statewide’s portal;
- c. implement reasonable steps to address these risks by, for example, evaluating the security of end user’s computer networks, requiring appropriate information security measures, and training end user clients;

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- d. implement reasonable steps to maintain an effective system of monitoring access to consumer reports by Statewide's end users, including by monitoring to detect anomalies and other suspicious activity; and
- e. take appropriate action to correct existing vulnerabilities or threats to personal information in light of known risks.

9. Because of Statewide's lack of information security policies and procedures, respondents allow clients without basic security measures in place, such as firewalls and updated antivirus software, to have access to their trimerge reports. The lack of such security measures directly caused highly-sensitive consumer reports to be available to hackers, as explained below.

THE BREACHES

10. As a direct result of these failures, between October 2006 and November 2007, hackers were able to exploit vulnerabilities in the computer networks of Statewide and multiple Statewide end user clients, putting consumer reports in those networks at risk. In multiple breaches, hackers accessed at least 323 consumer reports without authorization. Additionally, the hackers had the ability to view any consumer report that the end user client had pulled in the previous 90 days.

11. Following each of the breaches, respondents did not make reasonable efforts to determine the cause(s) of the breaches and protect against future breaches. For example, respondents did not perform a comprehensive assessment of Statewide's computer system, and made no efforts to identify and patch any vulnerabilities. Nor did respondents change any of their policies for screening new end users or require that new and existing end user clients submit any documentation demonstrating that the clients' computer systems were virus free and otherwise properly protected.

12. In addition, respondents have made no effort to warn their other end users of a known threat, or to suggest they make any efforts to ensure their systems were adequately secured.

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Respondents continue to give access to consumer reports to end user clients whose information security has not been adequately verified.

VIOLATIONS OF THE SAFEGUARDS RULE

13. The Safeguards Rule, which implements Section 501(b) of the GLB Act, 15 U.S.C. § 6801(b), was promulgated by the Commission on May 23, 2002, and became effective on May 23, 2003. The Rule requires financial institutions to protect the security, confidentiality, and integrity of customer information by developing a comprehensive written information security program that contains reasonable administrative, technical, and physical safeguards that include: (1) designating one or more employees to coordinate the information security program; (2) identifying reasonably foreseeable internal and external risks to the security, confidentiality, and integrity of customer information, and assessing the sufficiency of any safeguards in place to control those risks; (3) designing and implementing information safeguards to control the risks identified through risk assessment, and regularly testing or otherwise monitoring the effectiveness of the safeguards' key controls, systems, and procedures; (4) overseeing service providers and requiring them by contract to protect the security and confidentiality of customer information; and (5) evaluating and adjusting the information security program in light of the results of testing and monitoring, changes to the business operation, and other relevant circumstances. 16 C.F.R. §§ 314.3, 314.4.

14. As described in Paragraphs 7 through 12, respondents failed to implement reasonable security policies and procedures to protect sensitive consumer information, and have thereby engaged in violations of the Safeguards Rule by, among other things:

- a. failing to design and implement information safeguards to control the risks to customer information;
- b. failing to regularly test or monitor the effectiveness of its existing controls and procedures;

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- c. failing to evaluate and adjust the information security program in light of known or identified risks; and
- d. failing to develop, implement, and maintain a comprehensive information security program.

VIOLATIONS OF THE FCRA

15. Section 604 of the FCRA, 15 U.S.C. § 1681b, prohibits a consumer reporting agency from furnishing a consumer report except for specified “permissible purposes.” As described in Paragraph 10, in multiple instances, respondents furnished consumer reports to hackers that did not have a permissible purpose to obtain a consumer report. By and through the acts and practices described in Paragraphs 7 through 12, respondents have violated Section 604 of the FCRA, 15 U.S.C. § 1681b.

16. Section 607(a) of the FCRA, 15 U.S.C. § 1681e(a), requires every consumer reporting agency to maintain reasonable procedures to limit the furnishing of consumer reports to the purposes listed under Section 604 of the FCRA, 15 U.S.C. § 1681b. As described in Paragraphs 7 through 12, respondents failed to maintain reasonable procedures to limit the furnishing of consumer reports to the purposes listed under Section 604 of the FCRA. By and through the acts and practices described in Paragraphs 7 through 12, respondents have violated Section 607(a) of the FCRA, 15 U.S.C. § 1681e(a).

17. Section 607(a) of the FCRA, 15 U.S.C. § 1681e(a), prohibits a consumer reporting agency from furnishing a consumer report to any person if it has reasonable grounds for believing that the consumer report will not be used for a permissible purpose. As described in Paragraphs 10 through 12, in numerous instances, respondents furnished consumer reports under circumstances in which they had reasonable grounds for believing that the reports would not be used for a permissible purpose. By and through the acts and practices described in Paragraphs 10 through 12, respondents have violated Section 607(a) of the FCRA, 15 U.S.C. § 1681e(a).

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18. By their violations of Sections 604 and 607(a) of the FCRA, and pursuant to Section 621(a) thereof, 15 U.S.C. § 1681s, respondents have engaged in unfair and deceptive acts and practices in or affecting commerce, in violation of Section 5(a) of the FTC Act, 15 U.S.C. § 45(a).

VIOLATIONS OF THE FTC ACT

19. As described in Paragraphs 7 through 12, respondents have not employed reasonable and appropriate measures to secure the personal information they maintain and sell. Respondents' failure to employ reasonable and appropriate security measures to protect consumers' personal information has caused or is likely to cause substantial injury to consumers that is not offset by countervailing benefits to consumers or competition and is not reasonably avoidable by consumers. This practice was, and is, an unfair act or practice in or affecting commerce in violation of Section 5(a) of the Federal Trade Commission Act, 15 U.S.C. § 45(a).

THEREFORE, the Federal Trade Commission this seventeenth day of August, 2011, has issued this complaint against respondents.

By the Commission.

DECISION AND ORDER

The Federal Trade Commission having initiated an investigation of certain acts and practices of the Respondents named in the caption hereof, and the Respondents having been furnished thereafter with a copy of a draft Complaint that the Bureau of Consumer Protection proposed to present to the Commission for its consideration and which, if issued by the

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Commission, would charge the Respondents with violation of the Federal Trade Commission Act, 15 U.S.C. § 45 *et seq*; the Fair Credit Reporting Act, 15 U.S.C. § 1681 *et seq*; and the Commission's Standards for Safeguarding Customer Information Rule, 16 C.F.R. Part 314, issued pursuant to Title V, Subtitle A of the Gramm-Leach-Bliley Act, 15 U.S.C. §§ 6801-6809.

The Respondents and counsel for the Commission having thereafter executed an Agreement Containing Consent Order ("Consent Agreement"), an admission by the Respondents of all the jurisdictional facts set forth in the aforesaid draft Complaint, a statement that the signing of said Consent Agreement is for settlement purposes only and does not constitute an admission by Respondents that the law has been violated as alleged in such Complaint, or that the facts as alleged in such Complaint, other than jurisdictional facts, are true, and waivers and other provisions as required by the Commission's Rules; and

The Commission having thereafter considered the matter and having determined that it has reason to believe that the Respondents have violated the Federal Trade Commission Act, the Fair Credit Reporting Act, and the Gramm-Leach Bliley Act's Safeguards Rule, and that a Complaint should issue stating its charges in that respect, and having thereupon accepted the executed Consent Agreement and placed such Consent Agreement on the public record for a period of thirty (30) days for the receipt and consideration of public comments, and having duly considered the comments received from interested persons, now in further conformity with the procedure described in Section 2.34 of its Rules, 16 C.F.R. § 2.34, the Commission hereby issues its Complaint, makes the following jurisdictional findings, and enters the following Order:

- 1a. Respondent Statewide is a California corporation with its principal office or place of business at 2690 South White Road, Suite 235, San Jose, CA 95148.
- 1b. Respondent Robert Fajilan ("Fajilan") is owner and President of Statewide. Individually, or in concert with others, he formulates, directs, or controls the policies, acts, or practices of respondent Statewide.

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His principal place of business is the same as Statewide.

2. The Federal Trade Commission has jurisdiction of the subject matter of this proceeding and of the Respondents, and the proceeding is in the public interest.

ORDER**DEFINITIONS**

For purposes of this order, the following definitions shall apply:

1. “Personal information” shall mean individually identifiable information from or about an individual consumer including, but not limited to: (a) a first and last name; (b) a home or other physical address, including street name and name of city or town; (c) an email address or other online contact information; (d) a telephone number; (e) a Social Security number; (f) a credit card or debit card account number; (g) checking account information, (h) a driver’s license, military or state identification number; (i) a persistent identifier, such as a customer number, that is combined with other available data that identifies an individual consumer; or (j) any information that is combined with any of (a) through (i) above.
2. “Gramm-Leach-Bliley Act” or “GLB Act” refers to 15 U.S.C. §§ 6801-6809, as amended, the “Safeguards Rule” or the “Standards for Safeguarding Customer Information Rule” refers to 16 C.F.R. Part 314, issued pursuant to Title V, Subtitle A of the GLB Act, 15 U.S.C. §§ 6801-6809.
3. “Financial institution” shall mean as defined in Section 509(3)(A) of the GLB Act, 15 U.S.C. § 6809(3)(A).

Decision and Order

4. “The Fair Credit Reporting Act” or “FCRA” refers to 15 U.S.C. § 1681 et seq.
5. “Consumer report” shall mean as defined in Section 603(d)(1) of the FCRA, 15 U.S.C. § 1681a(d)(1).
6. Unless otherwise specified, “Corporate respondent” shall mean Statewide Credit Services, Inc. and its subsidiaries, divisions, affiliates, successors and assigns. “Individual respondent” means Robert Fajilan. “Respondents” means the Individual respondent and Corporate respondent, individually, collectively, or in any combination.
7. “Commerce” shall mean as defined in Section 4 of the Federal Trade Commission Act, 15 U.S.C. § 44.

I.

IT IS ORDERED that Corporate respondent and any business entity that Individual respondent, Robert Fajilan, controls, directly or indirectly, which collects, maintains, or stores personal information from or about consumers, shall, no later than the date of service of this order, establish and implement, and thereafter maintain, a comprehensive information security program that is reasonably designed to protect the security, confidentiality, and integrity of personal information collected from or about consumers, including the security, confidentiality, and integrity of personal information accessible to end users. Such program, the content and implementation of which must be fully documented in writing, shall contain administrative, technical, and physical safeguards appropriate to Corporate respondent’s or the entity’s size and complexity, the nature and scope of Corporate respondent’s or the entity’s activities, and the sensitivity of the personal information collected from or about consumers. The information security program must include:

- A. the designation of an employee or employees to coordinate and be accountable for the information security program;

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- B. the identification of material internal and external risks to the security, confidentiality, and integrity of personal information that could result in the unauthorized disclosure, misuse, loss, alteration, destruction, or other compromise of such information, and assessment of the sufficiency of any safeguards in place to control these risks. At a minimum, this risk assessment should include consideration of risks in each area of relevant operation, including, but not limited to: (1) employee training and management; (2) information systems, including network and software design, access, information processing, storage, transmission, and disposal; and (3) prevention, detection, and response to attacks, intrusions, or other systems failures;
- C. the design and implementation of reasonable safeguards to control the risks identified through risk assessment and regular testing or monitoring of the effectiveness of the safeguards' key controls, systems, and procedures;
- D. the development and use of reasonable steps to select and retain service providers capable of appropriately safeguarding personal information they receive from the Corporate respondent or the entity, and requiring service providers by contract to implement and maintain appropriate safeguards; and
- E. the evaluation and adjustment of respondent's or the entity's information security program in light of the results of the testing and monitoring required by sub-Part C, any material changes to Corporate respondent's or the entity's operations or business arrangements, or any other circumstances that Corporate respondent or the entity know or have reason to know may have a material impact on the effectiveness of their information security program.

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II.

IT IS FURTHER ORDERED that Corporate respondent and any business entity that Individual respondent, Robert Fajilan controls, directly or indirectly, and their officers, agents, representatives, and employees, shall not, directly or through any corporation, subsidiary, division, website, or other device, violate any provision of the Safeguards Rule, 16 C.F.R. Part 314. In the event that this Rule is hereafter amended or modified, respondents' compliance with that Rule as so amended or modified shall not be a violation of this order.

III.

IT IS FURTHER ORDERED that Corporate respondent and any business entity that Individual respondent, Robert Fajilan, controls, directly or indirectly, in connection with the compilation, creation, sale, or dissemination of any consumer report shall:

- A. furnish such consumer report only to those with a permissible purpose as described in Section 604 of the Fair Credit Reporting Act, 15 U.S.C. § 1681b;
- B. maintain reasonable procedures to limit the furnishing of such consumer report to those with a permissible purpose and ensure that no consumer report is furnished to any person when there are reasonable grounds to believe that the consumer report will not be used for a permissible purpose, as required by Section 607(a) of the Fair Credit Reporting Act, 15 U.S.C. § 1681e(a).

IV.

IT IS FURTHER ORDERED that, Corporate respondent and any business entity that Individual respondent, Robert Fajilan, controls, directly or indirectly, which collects, maintains, or stores personal information from or about consumers, shall, in connection with their compliance with Part I of this order, obtain initial and biennial assessments and reports ("Assessments") from a qualified, objective, independent third-party professional, who

Decision and Order

uses procedures and standards generally accepted in the profession. Each Assessment shall be prepared and completed within sixty (60) days after the end of the reporting period to which the Assessment applies by a person qualified as a Certified Information System Security Professional (CISSP) or as a Certified Information Systems Auditor (CISA); a person holding Global Information Assurance Certification (GIAC) from the SysAdmin, Audit, Network, Security (SANS) Institute; or a similarly qualified person or organization approved by the Associate Director for Enforcement, Bureau of Consumer Protection, Federal Trade Commission, 600 Pennsylvania Avenue NW, Washington, D.C. 20580. The reporting period for the Assessments shall cover: (1) the first one hundred and eighty (180) days after service of the order for the initial Assessment, and (2) each two (2) year period thereafter for twenty (20) years after service of the order for the biennial Assessments. Each Assessment shall:

- A. set forth the specific administrative, technical, and physical safeguards that Corporate respondent or the entity have implemented and maintained during the reporting period;
- B. explain how such safeguards are appropriate to Corporate respondent's or the entity's size and complexity, the nature and scope of Corporate respondent's or the entity's activities, and the sensitivity of the personal information collected from or about consumers;
- C. explain how the safeguards that have been implemented meet or exceed the protections required by the Safeguards Rule; and
- D. certify that Corporate respondent's or the entity's security program is operating with sufficient effectiveness to provide reasonable assurance that the security, confidentiality, and integrity of personal information is protected and has so operated throughout the reporting period.

Decision and Order

Respondents shall provide the initial Assessment to the Associate Director for Enforcement, Bureau of Consumer Protection, Federal Trade Commission, Washington, D.C. 20580, within ten (10) days after the Assessment has been prepared. All subsequent biennial Assessments shall be retained by respondents until the order is terminated and provided to the Associate Director of Enforcement within ten (10) days after respondents receive such request.

V.

IT IS FURTHER ORDERED that Corporate respondent, and Individual respondent, Robert Fajilan, for any business entity that he controls, directly or indirectly, which collects, maintains or stores personal information from or about consumers, shall maintain, and upon request make available to the Federal Trade Commission for inspection and copying:

- A. for a period of five (5) years, a print or electronic copy of each document relating to compliance, including but not limited to documents, prepared by or on behalf of Corporate respondent or the entity, that contradict, qualify, or call into question Corporate respondent's or the entity's compliance with this order;
- B. for a period of five (5) years, copies of all subpoenas and other communications with law enforcement entities or personnel, whether in written or electronic form, if such documents bear in any respect on Corporate respondent's or the entity's collection, maintenance, or furnishing of consumer reports or other personal information of consumers; and
- C. for a period of three (3) years after the date of preparation of each Assessment required under Part IV of this order, all materials relied upon to prepare the Assessment, whether prepared by or on behalf of the Corporate respondent or the entity, including but not limited to all plans, reports, studies, reviews, audits, audit trails, policies, training materials, and assessments, and any other materials relating to the

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Corporate respondent's or the entity's compliance with Parts I and II of this order, for the compliance period covered by such Assessment.

VI.

IT IS FURTHER ORDERED that for a period of five (5) years from the date of entry of this Order, respondents shall deliver copies of the Order as directed below:

- A. Corporate respondent must deliver a copy of this Order to (1) all current and future principals, officers, directors, and managers, (2) all employees, agents and representatives who engage in conduct related to the subject matter of the Order, and (3) any business entity resulting from any change in structure set forth in Part VIII. For current personnel, delivery shall be within five (5) days of service of this Order. For new personnel, delivery shall occur prior to them assuming their responsibilities. For any business entity resulting from any change in structure set forth in Part VIII, delivery shall be at least ten (10) days prior to the change in structure.
- B. For any business that Individual respondent, Robert Fajilan, controls, directly or indirectly, which collects, maintains, or stores personal information from or about consumers, Individual respondent must deliver a copy of this Order to (1) all principals, officers, directors, and managers of that business, (2) all employees, agents, and representatives of that business who engage in conduct related to the subject matter of the Order, and (3) any business entity resulting from any change in structure set forth in Part VII. For current personnel, delivery shall be within five (5) days of service of this Order. For new personnel, delivery shall occur prior to them assuming their responsibilities. For any business entity resulting from any change in structure set forth in Part VII, delivery shall be at least ten (10) days prior to the change in structure.

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- C. For any business that collects, maintains, or stores personal information from or about consumers, where Individual respondent, Robert Fajilan, is not a controlling person of the business, but he otherwise has responsibility, in whole or in part, for developing or overseeing the implementation of policies and procedures to protect the privacy, security, confidentiality, or integrity of personal information collected from or about consumers by the business, Individual respondent must deliver a copy of this Order to all principals and managers of such business before engaging in such conduct.
- D. Respondents must secure a signed and dated statement acknowledging receipt of this Order, within thirty (30) days of delivery, from all persons receiving a copy of the Order pursuant to this section.

VII.

IT IS FURTHER ORDERED that Individual respondent Fajilan, for a period of ten (10) years from the date of entry of this Order, shall notify the Commission of the following:

- A. Any changes in Individual respondent's residence, mailing address, and or telephone numbers, within ten (10) days of such a change;
- B. Any changes in Individual respondent's business or employment status (including self-employment), and any changes in his ownership in any business entity, within ten (10) days of such a change. Such notice shall include the name and address of each business that respondent is affiliated with, employed by, created or forms, or performs services for; a detailed description of the nature of the business or employment; and a detailed description of the respondent's duties and responsibilities in connection with such business or employment; and

Decision and Order

- C. Any changes in Individual respondent's name or use of any aliases or fictitious names, including "doing business as" names.

Unless otherwise directed by a representative of the Commission, all notices required by this Part shall be sent by overnight courier (not the U.S. Postal Service) to the Associate Director of Enforcement, Bureau of Consumer Protection, Federal Trade Commission, 600 Pennsylvania Avenue NW, Washington, D.C. 20580, with the subject line FTC v. Fajilan and Associates, Inc. also d/b/a Statewide Credit Services, and Robert Fajilan. *Provided, however,* that, in lieu of overnight courier, notices may be sent by first-class mail, but only if an electronic version of such notices is contemporaneously sent to the Commission at DEbrief@ftc.gov.

VIII.

IT IS FURTHER ORDERED that Corporate respondent shall notify the Commission at least thirty (30) days prior to any change in the corporation that may affect compliance obligations arising under this order, including, but not limited to, a dissolution, assignment, sale, merger, or other action that would result in the emergence of a successor corporation; the creation or dissolution of a subsidiary, parent, or affiliate that engages in any acts or practices subject to this Order; the proposed filing of a bankruptcy petition; or a change in the corporate name or address. *Provided, however,* that with respect to any proposed change in the corporation about which Corporate respondent learns less than thirty (30) days prior to the date such action is to take place, Corporate respondent shall notify the Commission as soon as is practicable after obtaining such knowledge. Unless otherwise directed by a representative of the Commission, all notices required by this Part shall be sent by overnight courier (not the U.S. Postal Service) to the Associate Director of Enforcement, Bureau of Consumer Protection, Federal Trade Commission, 600 Pennsylvania Avenue NW, Washington, D.C. 20580, with the subject line FTC v. Fajilan and Associates Inc., d/b/a Statewide Credit Services, and Robert Fajilan. *Provided, however,* that, in lieu of overnight courier, notices may be sent by first-class mail,

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but only if an electronic version of such notices is contemporaneously sent to the Commission at DEbrief@ftc.gov.

IX.

IT IS FURTHER ORDERED that Corporate respondent, and its successors and assigns, and Individual respondent Robert Fajilan, within sixty (60) days after the date of service of this order, shall file with the Commission a true and accurate report, in writing, setting forth in detail the manner and form of their own compliance with this order. Within ten (10) days of receipt of written notice from a representative of the Commission, they shall submit additional true and accurate written reports.

X.

This order will terminate on August 17, 2031, or twenty (20) years from the most recent date that the United States or the Federal Trade Commission files a complaint (with or without an accompanying consent decree) in federal court alleging any violation of the order, whichever comes later; *provided, however*, that the filing of such a complaint will not affect the duration of:

- A. any Part in this order that terminates in less than twenty (20) years;
- B. this order's application to any respondent that is not named as a defendant in such complaint; and
- C. this order if such complaint is filed after the order has terminated pursuant to this Part.

Provided, further, that if such complaint is dismissed or a federal court rules that respondents did not violate any provision of the order, and the dismissal or ruling is either not appealed or upheld on appeal, then the order will terminate according to this Part as though the complaint had never been filed, except that the order will not terminate between the date such complaint is filed and the

Analysis to Aid Public Comment

later of the deadline for appealing such dismissal or ruling and the date such dismissal or ruling is upheld on appeal.

By the Commission.

ANALYSIS OF CONSENT ORDER TO AID PUBLIC COMMENT

The Federal Trade Commission has accepted, subject to final approval, three agreements containing consent orders from ACRAnet, Inc. (“ACRAnet”); SettlementOne, Inc. (“SettlementOne”), and its parent corporation Sackett National Holdings, Inc.; and Fajilan and Associates, Inc. d/b/a Statewide Credit Services (“Statewide”) and its principal Robert Fajilan (collectively “respondents”).

The proposed consent orders have been placed on the public record for thirty (30) days for receipt of comments by interested persons. Comments received during this period will become part of the public record. After thirty (30) days, the Commission will again review the agreements and the comments received, and will decide whether it should withdraw from the agreements and take appropriate action or make final the agreements’ proposed orders.

According to the Commission’s proposed complaints, respondents contract with the three nationwide consumer reporting agencies, Experian, Equifax, and TransUnion to obtain consumer reports that they assemble and merge into a single “trimerge report.” The trimerge reports contain sensitive consumer information such as full name, current and former addresses, social security number, date of birth, employer history, credit account histories and information, and account numbers. Respondents provides the trimerge reports to end user clients through an online portal. Respondents issue credentials to their clients, which consist of a user name and password. The end user

Analysis to Aid Public Comment

clients use these credentials to access respondents' online portals and receive trimerged reports.

The Commission's complaints allege that respondents engaged in a number of practices that, taken together, failed to provide reasonable and appropriate security for consumers' personal information. Among other things, they failed to: (a) develop and disseminate comprehensive written information security policies; (b) assess the risks of allowing end users with unverified or inadequate security to access consumer reports through their online portals; (c) implement reasonable steps to address these risks by, for example, evaluating the security of end users' computer networks, requiring appropriate information security measures, and training end user clients; (d) implement reasonable steps to maintain an effective system of monitoring access to consumer reports by end users, including by monitoring to detect anomalies and other suspicious activity; and (e) take appropriate action to correct existing vulnerabilities or threats to personal information in light of known risks.

The complaints further allege that hackers were able to exploit vulnerabilities in the computer networks of multiple end user clients, putting all consumer reports in those networks at risk. In multiple breaches, hackers accessed hundreds of consumer reports.

According to the proposed complaints, respondents' practices violated the Gramm-Leach-Bliley ("GLB") Safeguards Rule by, among other things: (1) failing to design and implement information safeguards to control the risks to customer information; (2) failing to regularly test or monitor the effectiveness of existing controls and procedures; (3) failing to evaluate and adjust the information security programs in light of known or identified risks; and (4) failing to develop, implement, and maintain comprehensive information security programs. In addition, the proposed complaints allege that respondents' conduct violated sections 604 and 607(e) of the Fair Credit Reporting Act ("FCRA"). Further, the proposed complaints allege that respondents' failure to employ reasonable and appropriate measures to secure the personal information they maintain and sell is an unfair practice in violation of Section 5 of the Federal Trade Commission Act.

Analysis to Aid Public Comment

The proposed orders contain provisions designed to prevent respondents from engaging in similar practices in the future. They also apply to personal information respondents collect from or about consumers. The orders name the resellers themselves, ACRAnet, SettlementOne, and Statewide; in the case of SettlementOne, its parent corporation Sackett National Holdings; and in the case of Statewide, its principal Robert Fajilan.

Part I of the proposed orders requires respondents to establish and maintain a comprehensive information security program that is reasonably designed to protect the security, confidentiality, and integrity of personal information collected from or about consumers, including the security, confidentiality, and integrity of personal information accessible to end users.¹ The security program must contain administrative, technical, and physical safeguards appropriate to each respondent's size and complexity, the nature and scope of its activities, and the sensitivity of the personal information collected from or about consumers. Specifically, the orders require respondents to:

- Designate an employee or employees to coordinate and be accountable for the information security program.
- Identify material internal and external risks to the security, confidentiality, and integrity of personal information that could result in the unauthorized disclosure, misuse, loss, alteration, destruction, or other compromise of such information, and assess the sufficiency of any safeguards in place to control these risks.
- Design and implement reasonable safeguards to control the risks identified through risk assessment, and regularly test or monitor the effectiveness of the safeguards' key controls, systems, and procedures.

¹ The proposed order against Statewide includes an individual respondent, Robert Fajilan. Parts I-VI of this order apply to any business entity that Mr. Fajilan controls.

Analysis to Aid Public Comment

- Develop and use reasonable steps to select and retain service providers capable of appropriately safeguarding personal information they receive from respondents, and require service providers by contract to implement and maintain appropriate safeguards.
- Evaluate and adjust the information security program in light of the results of the testing and monitoring, any material changes to the company's operations or business arrangements, or any other circumstances that they know or have reason to know may have a material impact on the effectiveness of their information security program.

Part II of the proposed orders prohibits respondents from violating any provision of the GLB Safeguards Rule.

Part III of the proposed orders requires that respondents, in connection with the compilation, creation, sale or dissemination of any consumer report shall: (1) furnish such consumer report only to those persons it has reason to believe have a permissible purpose as described in Section 604(a)(3) of the FCRA, or under such other circumstances as set forth in Section 604 of the FCRA; and (2) maintain reasonable procedures to limit the furnishing of such consumer reports to those with a permissible purpose and ensure that no consumer report is furnished to any person when there are reasonable grounds to believe that the consumer report will not be used for a permissible purpose.

Part IV of the proposed orders requires that respondents obtain within 180 days, and on a biennial basis thereafter for twenty (20) years, an assessment and report from a qualified, objective, independent third-party professional, certifying, among other things, that they have in place a security program that provides protections that meet or exceed the protections required by Part I of the proposed order; and their security program is operating with sufficient effectiveness to provide reasonable assurance that the security, confidentiality, and integrity of consumers' personal information is protected.²

² The proposed order against SettlementOne and Sackett National Holdings does not require Sackett National Holdings to obtain an assessment for any subsidiary, division, affiliate, successor or assign if the personal

Analysis to Aid Public Comment

Parts V through IX of the proposed orders are reporting and compliance provisions. Part V requires respondents to retain documents relating to their compliance with the orders. For most records, the orders require that the documents be retained for a five-year period. For the third-party assessments and supporting documents, respondents must retain the documents for a period of three years after the date that each assessment is prepared. Part VI requires dissemination of the orders now and in the future to principals, officers, directors, and managers, and all employees, agents and representatives who engage in conduct related to the subject matter of the order. In the ACRAnet and SettlementOne orders, Part VII ensures notification to the FTC of changes in corporate status. In the Statewide order, Part VII requires the individual respondent to notify the FTC of changes in contact information, business or employment status, and Part VIII requires the corporate respondent to notify the FTC of changes in corporate status. Part VIII of the ACRAnet and SettlementOne orders and Part XI of the Statewide order mandates that respondents submit an initial compliance report to the FTC, and make available to the FTC subsequent reports. The last provision of the orders is a provision “sunsetting” the orders after twenty (20) years, with certain exceptions.

The purpose of the analysis is to aid public comment on the proposed orders. It is not intended to constitute an official interpretation of the proposed orders or to modify their terms in any way.

information such entities collect, maintain, or store from or about consumers is limited to a first and last name; a home or other physical address, including street name and name of city or town; an email address; a telephone number; or publicly available information regarding property ownership and appraised home value.

Concurring Statement

**STATEMENT OF COMMISSIONER BRILL, IN WHICH
CHAIRMAN LEIBOWITZ AND COMMISSIONERS
ROSCH AND RAMIREZ JOIN**

The respondents in these three matters are resellers of consumer reports who failed to take reasonable measures to protect sensitive consumer credit information. We fully support staff's work on these matters. We write separately to emphasize that in the future we will call for imposition of civil penalties against resellers of consumer reports who do not take adequate measures to fulfill their obligations to protect information contained in consumer reports, as required by the Fair Credit Reporting Act ("FCRA").

The respondents in these three matters treated their legal obligations to protect consumer information as a paper exercise. Respondents provided only a cursory review of security measures. Thereafter, respondents took no further action to ensure that their customers' security measures adequately protected the information in the consumer reports. Nor did they provide training on security measures to end users. Even after discovering security breaches that should have alerted them to problems with the data security of some customers, respondents failed to implement measures to check the security practices of other clients.

The FCRA requires respondents to take reasonable measures to ensure that consumer reports are given only to entities using the reports for purposes authorized by the statute.¹ As a result of respondents' failure to comply with the FCRA, nearly 2,000 credit reports were improperly accessed. There is no doubt that such unauthorized access can result in grave consumer harm through identity theft.

The significant impact and cost of identity theft are well documented. Although reports regarding the impact of identity theft do not always agree on specific figures, they do reveal tremendous economic and non-economic consequences for both consumers and the economy. The Commission itself issued

¹ 15 U.S.C. § 1681b; 15 U.S.C. § 1681e(a).

Concurring Statement

reports in both 2003² and 2007.³ Our 2007 report estimated that in 2005 alone 8.3 million consumers fell victim to identity theft. We found that 1.8 million of those victims had new accounts opened in their names. One-quarter of the “new account victims” incurred more than \$1,000 in out-of-pocket expenses and five percent spent 1,200 hours in dealing with the consequences of the theft. The report concluded that total losses from identity theft in 2006 totaled \$15.6 billion. Beyond these financial impacts, we also identified non-economic harm to victims in many forms: denial of new credit or loans, harassment from collection agencies, the loss the time involved in resolving the problems, and being subjected to criminal investigation. In view of the hardships and costs brought on by identity theft, measures to prevent it must be rigorously enforced.

While we view the breaches in these cases with alarm, we are also cognizant of the fact that these are the first cases in which the Commission has held resellers responsible for downstream data protection failures.⁴ Looking forward, the actions we announce today should put resellers — indeed, all of those in the chain of handling consumer data — on notice of the seriousness with which we view their legal obligations to proactively protect consumers’ data. The Commission should use all of the tools at its disposal to protect consumers from the enormous risks posed by security breaches that may lead to identity theft. In the future, we should not hesitate to use our authority to seek civil penalties under the FCRA⁵ to make the protection of consumer data a top priority for those who profit from its collection and dissemination.

² Fed. Trade Comm’n. *Identity Theft Survey Report* (2003), available at <http://www.ftc.gov/os/2003/09/synovaterreport.pdf>.

³ Fed. Trade Comm’n, *2006 Identity Theft Survey Report* (2007), available at <http://www.ftc.gov/os/2007/11/SynovateFinalReportIDTheft2006.pdf>.

⁴ The Commission has previously taken action where the credit reporting agency failed to adequately screen purchasers of consumer credit information. For instance, in *United States v. ChoicePoint, Inc.*, 09-CV-0198 (N.D. Ga. Oct. 19, 2009), the Commission alleged that the failure to screen customers led to the sale of 160,000 credit reports to identity thieves posing as customers of ChoicePoint.

⁵ The Fair Credit Reporting Act authorizes the Commission to seek civil penalties for violations of the Act. 15 U.S.C. § 1681s(a)(2)(A).

Complaint

IN THE MATTER OF

BEIERSDORF, INC.CONSENT ORDER, ETC. IN REGARD TO ALLEGED VIOLATIONS OF
SECS. 5(A) AND 12 OF THE FEDERAL TRADE COMMISSION ACT

Docket No. C-4333; File No. 092 3194
Filed, August 17, 2011 — Decision, August 17, 2011

This consent order addresses allegations that Beiersdorf, Inc.'s ("Respondent") advertising, marketing, and sale of its "Nivea My Silhouette! Redefining Gel-Cream" skin cream ("My Silhouette") violates the FTC Act. According to the complaint, Respondent advertised that regular use of My Silhouette results in significant reductions in body size. The complaint alleged this claim was false and violated the FTC Act. The order prohibits Respondent from claiming that My Silhouette or any other topically applied product causes substantial weight loss, fat loss, or reduction in body size. The order further prohibits Respondent from making any representations that a drug, dietary supplement, or cosmetic causes weight or fat loss or a reduction in body size without competent and reliable scientific evidence substantiating the representation. The order further requires Respondent to pay \$900,000 to the Commission to be distributed as equitable relief, including restitution, to consumers.

Participants

For the *Commission*: *Matthew D. Gold and Evan Rose.*

For the *Respondent*: *John Fleder, Paul Hyman, and Susan J. Matthees, Hyman, Phelps & McNamara PC.*

COMPLAINT

The Federal Trade Commission, having reason to believe that Beiersdorf, Inc., a corporation ("respondent"), has violated the provisions of the Federal Trade Commission Act, and it appearing to the Commission that this proceeding is in the public interest, alleges:

1. Respondent Beiersdorf, Inc., is a Delaware corporation with its principal office or place of business at Wilton Corporate Center, 187 Danbury Road, Wilton, Connecticut 06897.

Complaint

2. Respondent has manufactured, advertised, labeled, offered for sale, sold, and distributed products to the public, including Nivea My Silhouette! Redefining Gel-Cream (“My Silhouette”). My Silhouette is a “drug” and/or “cosmetic” within the meaning of Sections 12 and 15 of the Federal Trade Commission Act.

3. The acts and practices of respondent alleged in this complaint have been in or affecting commerce, as “commerce” is defined in Section 4 of the Federal Trade Commission Act.

4. My Silhouette is a skin cream that contains “Bio-slim Complex,” a combination of ingredients that includes white tea and anise. Respondent promoted My Silhouette as able to slim and reshape the body.

5. Respondent has disseminated or has caused to be disseminated advertisements for My Silhouette, including but not necessarily limited to the attached Exhibits A to C. These advertisements contained the following statements and depictions:

- A. TV advertisement (Exhibit A, transcript, and Exhibit B, DVD containing ad)

“[Narrator]: New Nivea My Silhouette! with Bio-Slim Complex helps redefine the appearance of your silhouette and noticeably firm skin in just four weeks. [Depicts woman getting jeans out of rear of closet, and trying them on to discover that they fit.] So you can rediscover your favorite jeans. And how they still get his attention. New Nivea My Silhouette! with Bio-Slim Complex. Touch and be touched.”

- B. Sponsored Search Engine Keywords (Exhibit C)

Respondents also entered into agreements with Google, an Internet search engine, to preferentially identify a webpage marketing My Silhouette in response to consumer searches for information relating to body size. As a result, if a consumer entered the terms “stomach fat,” “nivea slim silhouette,” or “thin waist” into Google, a link to

Complaint

this My Silhouette webpage would appear as a sponsored result at the top of the search results, such as follows:

Excerpts from Google sponsored search results

[User search term: “stomach fat”]

Want a Toned **Stomach**? Sponsored Link
[URL] NIVEA My Silhouette Can Redefine The Appearance of Your Curves!

[User search term: “nivea slim silhouette”]

Want to **Slim Down**? Sponsored Link
[URL] NIVEA My Silhouette Redefines the Appearance of the Body’s Contours!

[User search term: “thin waist”]

Thin Waist Sponsored Link
[URL] Try NIVEA My Silhouette Body Gel-Cream and Redefine Your Curves!

6. Through the means described in Paragraph 5, respondent represented, expressly or by implication, that regular use of My Silhouette results in significant reductions in body size.

7. In truth and in fact, regular use of My Silhouette does not result in significant reductions in body size. Therefore, the representation set forth in Paragraph 6 was, and is, false or misleading.

8. The acts and practices of respondent as alleged in this complaint constitute unfair or deceptive acts or practices, and the making of false advertisements, in or affecting commerce in violation of Sections 5(a) and 12 of the Federal Trade Commission Act.

Complaint

THEREFORE, the Federal Trade Commission this seventeenth day of August, 2011, has issued this complaint against respondent.

By the Commission.

Complaint

EXHIBIT A**My Silhouette! :30 TV
3.23.09****Revised Based on R&D 3.23.09**

ANNCR: New NIVEA My Silhouette with Bio-Slim complex helps redefine the appearance of your silhouette and noticeably firms skin in just four weeks.

So you can rediscover your favorite jeans and how they still get his attention.

New Nivea My Silhouette with Bio-Slim complex.

Touch and be touched.

Complaint

EXHIBIT B

**DVD OF NIVEA MY SILHOUETTE! "MIRROR" TV
COMMERCIAL**

Complaint

EXHIBIT C-1

The screenshot shows a Google search interface with the search term "stomach fat" entered in the search bar. The search results are displayed on a white background with a blue header. The NIVEA logo is visible in the top right corner. The search results include several links to articles and videos, such as "Want a Toned Stomach?", "The Truth About Belly Fat", "Belly fat in men, why weight loss matters", "Fat Stomach Exercises and Diet Tips", "WikiAnswers - What's the easiest way to get rid of lower stomach fat?", "How to Lose Belly Fat - wikiHow", "Lose Belly Fat: Get Flat Six Pack Abs, Ab Workouts, Abdominal", "Causes of Belly Fat - It's Not Just Lack of Exercise!", "How to Reduce a Fat Belly or Stomach", and "Burn Stomach Fat - Burn Stomach Fat". The search results are sorted by relevance, and the page number "6" is visible at the bottom right.

Exhibit C-1

Complaint

EXHIBIT C-2

The screenshot shows a Google search interface with the search term "nivea slim silhouette" entered in the search bar. The search results are displayed below the search bar, including sponsored links and organic search results. The Nivea logo is visible in the top right corner of the browser window. The search results include links to Nivea USA, Nivea Slim Silhouette product pages, and various retailers like Amazon and Walmart. The search results are organized into sections like "Sponsored Links" and "Shopping results for nivea slim silhouette".

Google Search

Web Images Maps News Videos Gmail more Sign in

Google Search Advanced Search Feedback

Web Shopping Results 1 - 10 of about 12,600 for nivea slim silhouette. (0.24 seconds)

Want to Slim Down? **Nivea My Silhouette Redefines the Appearance of the Body's Contours!** **Slim Silhouette**

[NiveaUSA.com/SlimYearsChallenge](#) [Nivea My Silhouette Redefines the Appearance of the Body's Contours!](#) [Slim Silhouette](#)

[www.eligible.com/nivea](#) See Reviews on Nivea Skin Care Free Shipping with Minimum Purchase. [Go!](#) [Contact](#)

Shopping results for nivea slim silhouette

[Nivea My Silhouette Redefining Gel Cream with...](#) \$12.13 - American.com

[Nivea My Silhouette Reshaping Gel Cream with...](#) \$12.13 - Underdog

[Nivea Slimming & Reshaping Gel Cream \(200 ml\)](#) \$18.70 - Sassa.com

My Silhouette - NIVEA review at Kaboodle

Gel-Cream, slims and reshapes your body for you to discover your own feel good silhouette. NIVEA research has developed the natural Bio-Slim Complex that ... [www.kaboodle.com/reviews/my-silhouette-nivea](#) - 5/5 - [Cached](#) - [Similar pages](#)

Shop online Nivea My Silhouette Redefining Gel Cream with Natural ...

Now Nivea My Silhouette Gel-Cream with natural Bio-Slim Complex for a toned and redefined silhouette. **INGREDIENTS:** Water, Glycerin, Alcohol Denat., ... [www.american.com/products/04551.html#456](#) - [Cached](#) - [Similar pages](#)

My Silhouette - NIVEA

Slimming & Reshaping Gel-Cream NIVEA My Silhouette! ... NIVEA research has developed the natural Bio-Slim Complex that combines the high-performance active ... [www.nivea.com/products/nivea/0222](#) - 2/5 - [Cached](#) - [Similar pages](#)

Nivea My Silhouette Redefining Gel Cream with Natural Bio Slim ...

You have additional Nivea My Silhouette Reshaping Gel Cream with Natural Bio-Slim Complex - 7 Oz supplies in our online store supporting garden tools. ... [www.barkyardstore.com/Shop/Health_Beauty/Health_Products/1601](#)

Sponsored Links

Find Slim Silhouette now

Looking for cheap Slim Silhouette? Check \$ 800 shops for great prices! [www.SlimSilhouette.best-price.com](#)

Comparison Shopping Made Easy. Find Slim Silhouette

[BizRate.com](#)

Exhibit C-2

Complaint

EXHIBIT C-3

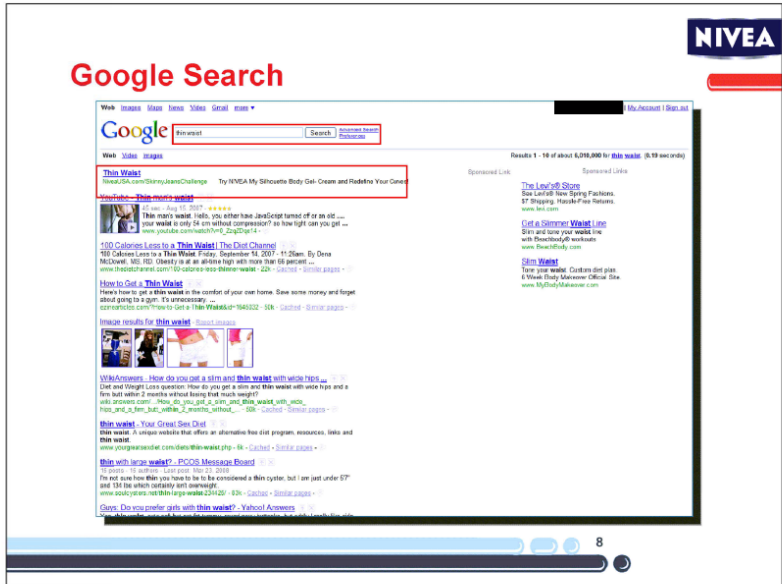


EXHIBIT C-3

Decision and Order

DECISION AND ORDER

The Federal Trade Commission having initiated an investigation of certain acts and practices of the respondent named in the caption hereof, and the respondent having been furnished thereafter with a copy of a draft of complaint which the Western Region-San Francisco proposed to present to the Commission for its consideration and which, if issued by the Commission, would charge respondent with violation of the Federal Trade Commission Act; and

The respondent, its attorneys, and counsel for the Commission having thereafter executed an agreement containing a consent order, an admission by the respondent of all the jurisdictional facts set forth in the aforesaid draft of complaint, a statement that the signing of said agreement is for settlement purposes only and does not constitute an admission by respondent that the law has been violated as alleged in such complaint, or that the facts as alleged in such complaint, other than jurisdictional facts, are true and waivers and other provisions as required by the Commission's Rules; and

The Commission having thereafter considered the matter and having determined that it had reason to believe that the respondents have violated the said Act, and that complaint should issue stating its charges in that respect, and having thereupon accepted the executed consent agreement and placed such agreement on the public record for a period of thirty (30) days, now in further conformity with the procedure prescribed in § 2.34 of its Rules, the Commission hereby issues its complaint, makes the following jurisdictional findings and enters the following order:

1. Respondent Beiersdorf, Inc., is a Delaware corporation with its principal office or place of business at Wilton Corporate Center, 187 Danbury Road, Wilton, Connecticut 06897.
2. The Federal Trade Commission has jurisdiction of the subject matter of this proceeding and of the respondent, and the proceeding is in the public interest.

Decision and Order

ORDER**DEFINITIONS**

For purposes of this order, the following definitions shall apply:

1. Unless otherwise specified, “respondent” shall mean Beiersdorf, Inc., a corporation, its successors and assigns and its officers, agents, representatives, and employees.
2. “Commerce” shall mean as defined in Section 4 of the Federal Trade Commission Act, 15 U.S.C. § 44.
3. “Covered Product” means any drug, dietary supplement, or cosmetic.
4. “Drug” and “cosmetic” mean as defined in Section 15 of the FTC Act, 15 U.S.C. § 55.
5. “Adequate and well-controlled human clinical study” means a human clinical study that is randomized, double-blind, placebo-controlled, and conducted by persons qualified by training and experience to conduct such study.
6. “Dietary supplement” means:
 - A. any product labeled as a dietary supplement or otherwise represented as a dietary supplement; or
 - B. any pill, tablet, capsule, powder, softgel, gelcap, liquid, or other similar form containing one or more ingredients that are a vitamin, mineral, herb or other botanical, amino acid, probiotic, or other dietary substance for use by humans to supplement the diet by increasing the total dietary intake, or a concentrate, metabolite, constituent, extract, or combination of any ingredient described above,

Decision and Order

that is intended to be ingested, and is not represented to be used as a conventional food or as a sole item of a meal or the diet.

7. “Essentially Equivalent Product” means a product that contains the identical ingredients, except for inactive ingredients (e.g., binders, colors, fillers, excipients), in the same form and dosage, and with the same route of administration (e.g., orally, sublingually), as the Covered Product; *provided that*, with regard to Paragraph II of this Order, the Covered Product may contain additional ingredients if reliable scientific evidence generally accepted by experts in the field demonstrates that the amount and combination of additional ingredients is unlikely to impede or inhibit the effectiveness of the ingredients in the Essentially Equivalent Product.

II.

IT IS ORDERED that respondent, directly or through any corporation, subsidiary, division, or other device, in connection with the manufacturing, labeling, advertising, promotion, offering for sale, sale, or distribution of NIVEA My Silhouette! Redefining Gel-Cream, or any other topically applied product, in or affecting commerce, shall not represent, in any manner, expressly or by implication, including through the use of a product name, endorsement, depiction, or illustration, that use of such product causes substantial weight or fat loss or a substantial reduction in body size.

III.

IT IS FURTHER ORDERED that, subject to the provisions of Part I of this order, respondent, directly or through any corporation, subsidiary, division, or other device, in connection with the manufacturing, labeling, advertising, promotion, offering for sale, sale, or distribution of any Covered Product, in or affecting commerce, shall not represent, in any manner, expressly or by implication, including through the use of a product name, endorsement, depiction, or illustration, that use of such product

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causes weight or fat loss or a reduction in body size, unless the representation is non-misleading, and, at the time it is made, respondent possesses and relies upon competent and reliable scientific evidence that substantiates that the representation is true. For purposes of this Part, competent and reliable scientific evidence shall consist of at least two adequate and well-controlled human clinical studies of the Covered Product, or of an Essentially Equivalent Product, conducted by different researchers, independently of each other, that conform to acceptable designs and protocols and whose results, when considered in light of the entire body of relevant and reliable scientific evidence, are sufficient to substantiate that the representation is true. Respondent shall have the burden of proving that a product satisfies the definition of Essentially Equivalent Product.

IV.

IT IS FURTHER ORDERED that respondent, directly or through any corporation, subsidiary, division, or other device, in connection with the manufacturing, labeling, advertising, promotion, offering for sale, sale, or distribution of any Covered Product in or affecting commerce, shall not make any representation, in any manner, expressly or by implication, including through the use of a product name, endorsement, depiction, or illustration, other than representations covered under Parts I and II of this order, about the health benefits of such product, unless the representation is non-misleading, and, at the time of making such representation, the respondent possesses and relies upon competent and reliable scientific evidence that is sufficient in quality and quantity based on standards generally accepted in the relevant scientific fields, when considered in light of the entire body of relevant and reliable scientific evidence, to substantiate that the representation is true. For purposes of this Part, competent and reliable scientific evidence means tests, analyses, research, or studies that have been conducted and evaluated in an objective manner by qualified persons, and that are generally accepted in the profession to yield accurate and reliable results.

Decision and Order

V.

IT IS FURTHER ORDERED that nothing in this order shall prohibit respondent from making any representation for:

- A. Any drug that is permitted in the labeling for such drug under any tentative final or final standard promulgated by the Food and Drug Administration, or under any new drug application approved by the Food and Drug Administration; and
- B. Any product that is specifically permitted in labeling for such product by regulations promulgated by the Food and Drug Administration pursuant to the Nutrition Labeling and Education Act of 1990.

VI.

IT IS FURTHER ORDERED that respondent shall pay to the Federal Trade Commission the sum of nine hundred thousand dollars (\$900,000). This payment shall be made in the following manner:

- A. The payment shall be made by wire transfer made payable to the Federal Trade Commission, the payment to be made no later than five (5) days after the date that this order becomes final.
- B. In the event of default on any obligation to make payment under this order, interest, computed pursuant to 28 U.S.C. § 1961(a), shall accrue from the date of default to the date of payment. In the event such default continues for ten (10) calendar days beyond the date that payment is due, the entire amount shall immediately become due and payable.
- C. All funds paid to the Commission pursuant to this order shall be deposited into an account administered by the Commission or its agents to be used for equitable relief, including restitution, and any attendant expenses for the administration of such

Decision and Order

equitable relief. In the event that direct redress to consumers is wholly or partially impracticable or funds remain after the redress to consumers (which shall be the first priority for dispensing the funds set forth above) is completed, the Commission may apply any remaining funds for such other equitable relief (including consumer information remedies) as it determines to be reasonably related to respondent's practices alleged in the complaint. Any funds not used for such equitable relief shall be deposited in the United States Treasury as disgorgement. Respondent shall be notified as to how the funds are distributed, but shall have no right to challenge the Commission's choice of remedies under this Part. Respondent shall have no right to contest the manner of distribution chosen by the Commission. No portion of any payment under this Part shall be deemed a payment of any fine, penalty, or punitive assessment.

- D. Respondent relinquishes all dominion, control, and title to the funds paid to the fullest extent permitted by law. Respondent shall make no claim to or demand for return of the funds, directly or indirectly, through counsel or otherwise.
- E. Respondent agrees that the facts as alleged in the complaint filed in this action shall be taken as true without further proof in any bankruptcy case or subsequent civil litigation pursued by the Commission to enforce its rights to any payment or money judgment pursuant to this order, including but not limited to a nondischargeability complaint in any bankruptcy case. Respondent further agrees that the facts alleged in the complaint establish all elements necessary to sustain an action by the Commission pursuant to Section 523(a)(2)(A) of the Bankruptcy Code, 11 U.S.C. § 523(a)(2)(A), and that this order shall have collateral estoppel effect for such purposes.
- F. In accordance with 31 U.S.C. § 7701, respondent is hereby required, unless it has done so already, to

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furnish to the Commission its taxpayer identifying number, which shall be used for the purposes of collecting and reporting on any delinquent amount arising out of respondent's relationship with the government.

- G. Proceedings instituted under this Part are in addition to, and not in lieu of, any other civil or criminal remedies that may be provided by law, including any other proceedings the Commission may initiate to enforce this order.

VII.

IT IS FURTHER ORDERED that respondent Beiersdorf, Inc., and its successors and assigns shall, for five (5) years after the last date of dissemination of any representation covered by this order, maintain and, upon reasonable notice and request, make available to the Federal Trade Commission for inspection and copying:

- A. All advertisements and promotional materials containing the representation;
- B. All materials that were relied upon in disseminating the representation; and
- C. All tests, reports, studies, surveys, demonstrations, or other evidence in its possession or control that contradict, qualify, or call into question the representation, or the basis relied upon for the representation, including complaints and other communications with consumers or with governmental or consumer protection organizations.

VIII.

IT IS FURTHER ORDERED that respondent Beiersdorf, Inc., and its successors and assigns shall deliver a copy of this order to all current and, for the next five (5) years, all future principals, officers, directors, and other employees having

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primary responsibilities with respect to the subject matter of this order, and shall secure from each such person a signed and dated statement acknowledging receipt of the order. Respondent Beiersdorf, Inc., and its successors and assigns shall deliver this order to current personnel within thirty (30) days after the date of service of this order, and to future personnel within thirty (30) days after the person assumes such position or responsibilities.

IX.

IT IS FURTHER ORDERED that respondent Beiersdorf, Inc., and its successors and assigns shall notify the Commission at least thirty (30) days prior to any change in the corporation(s) that may affect compliance obligations arising under this order, including but not limited to a dissolution, assignment, sale, merger, or other action that would result in the emergence of a successor corporation; the creation or dissolution of a subsidiary, parent, or affiliate that engages in any acts or practices subject to this order; the proposed filing of a bankruptcy petition; or a change in the corporate name or address. *Provided, however,* that, with respect to any proposed change in the corporation about which respondent learns less than thirty (30) days prior to the date such action is to take place, respondent shall notify the Commission as soon as is practicable after obtaining such knowledge. Unless otherwise directed by a representative of the Commission, all notices required by this Part shall be sent by overnight courier (not the U.S. Postal Service) to the Associate Director of Enforcement, Bureau of Consumer Protection, Federal Trade Commission, 600 Pennsylvania Avenue NW, Washington, DC 20580, with the subject line: In the Matter of Beiersdorf, Inc., FTC File Number 092-3194. *Provided, however,* that, in lieu of overnight courier, notices may be sent by first-class mail, but only if an electronic version of such notices is contemporaneously sent to the Commission at Debrief@ftc.gov.

X.

IT IS FURTHER ORDERED that respondent Beiersdorf, Inc., and its successors and assigns shall, within sixty (60) days after the date of service of this order, file with the Commission a true and accurate report, in writing, setting forth in detail the

Decision and Order

manner and form of its own compliance with this order. Within ten (10) days of receipt of written notice from a representative of the Commission, they shall submit additional true and accurate written reports.

XI.

This order will terminate on August 17, 2031, or twenty (20) years from the most recent date that the United States or the Federal Trade Commission files a complaint (with or without an accompanying consent decree) in federal court alleging any violation of the order, whichever comes later; *provided, however*, that the filing of such a complaint will not affect the duration of:

- A. Any Part in this order that terminates in less than twenty (20) years;
- B. This order's application to any respondent that is not named as a defendant in such complaint; and
- C. This order if such complaint is filed after the order has terminated pursuant to this Part.

Provided, further, that if such complaint is dismissed or a federal court rules that the respondent did not violate any provision of the order, and the dismissal or ruling is either not appealed or upheld on appeal, then the order will terminate according to this Part as though the complaint had never been filed, except that the order will not terminate between the date such complaint is filed and the later of the deadline for appealing such dismissal or ruling and the date such dismissal or ruling is upheld on appeal.

By the Commission.

Analysis to Aid Public Comment

**ANALYSIS OF CONSENT ORDER TO AID PUBLIC
COMMENT**

The Federal Trade Commission (“FTC” or “Commission”) has accepted, subject to final approval, an Agreement Containing Consent Order from Beiersdorf, Inc. (“respondent”). The proposed consent order has been placed on the public record for thirty (30) days for receipt of comments by interested persons. Comments received during this period will become part of the public record. After thirty (30) days, the Commission will again review the agreement and the comments received, and will decide whether it should withdraw from the agreement and take appropriate action or make final the agreement’s proposed order.

This matter involves the advertising, marketing, and sale of “NIVEA My Silhouette! Redefining Gel-Cream” (“My Silhouette”) by respondent. Respondent has marketed My Silhouette to consumers through third-party retail outlets.

My Silhouette is a skin cream that contains “Bio-slim Complex,” a combination of ingredients that includes white tea and anise. According to the FTC complaint, respondent promoted My Silhouette as able to slim and reshape the body.

Specifically, the FTC complaint alleges that respondent represented, in various advertisements, that regular use of My Silhouette results in significant reductions in body size. The complaint alleges that this claim is false and thus violates the FTC Act.

The proposed consent order contains provisions designed to prevent respondent from engaging in similar acts or practices in the future. Specifically, Part I prohibits respondent from claiming that My Silhouette or any other topically applied product causes substantial weight or fat loss or a substantial reduction in body size.

Part II covers any representation that a drug, dietary supplement, or cosmetic causes weight or fat loss or a reduction in body size. Part II prohibits respondent from making such representations unless the representation is non-misleading, and,

Analysis to Aid Public Comment

at the time of making such representation, respondent possesses and relies upon competent and reliable scientific evidence that substantiates that the representation is true. For purposes of Part II, the proposed order defines “competent and reliable scientific evidence” as at least two randomized, double-blind, placebo-controlled human clinical studies that are conducted by independent, qualified researchers and that conform to acceptable designs and protocols, and whose results, when considered in light of the entire body of relevant and reliable scientific evidence, are sufficient to substantiate that the representation is true.

Part III of the proposed order prohibits respondent from making representations, other than representations covered under Parts I or II, about the health benefits of any drug, dietary supplement, or cosmetic, unless the representation is non-misleading, and, at the time of making such representation, respondent possesses and relies upon competent and reliable scientific evidence that is sufficient in quality and quantity based on standards generally accepted in the relevant scientific fields, when considered in light of the entire body of relevant and reliable scientific evidence, to substantiate that the representation is true. For purposes of Part III, the proposed order defines “competent and reliable scientific evidence” as “tests, analyses, research, or studies that have been conducted and evaluated in an objective manner by qualified persons, and that are generally accepted in the profession to yield accurate and reliable results.”

Part IV of the proposed order states that the order does not prohibit respondent from making representations for any drug that are permitted in labeling for that drug under any tentative or final standard promulgated by the Food and Drug Administration (“FDA”), or under any new drug application approved by the FDA. This part of the proposed order also states that the order does not prohibit respondent from making representations for any product that are specifically permitted in labeling for that product by regulations issued by the FDA under the Nutrition Labeling and Education Act of 1990.

Part V of the proposed order requires respondent to pay nine hundred thousand dollars (\$900,000) to the Commission to be used for equitable relief, including restitution, and any attendant

Analysis to Aid Public Comment

expenses for the administration of such equitable relief.

Parts VI, VII, VIII, and IX of the proposed order require respondent to keep copies of relevant advertisements and materials substantiating claims made in the advertisements; to provide copies of the order to its personnel; to notify the Commission of changes in corporate structure that might affect compliance obligations under the order; and to file compliance reports with the Commission. Part X provides that the order will terminate after twenty (20) years, with certain exceptions.

The purpose of this analysis is to facilitate public comment on the proposed order, and it is not intended to constitute an official interpretation of the agreement and proposed order or to modify their terms in any way.

Complaint

IN THE MATTER OF**GOOGLE, INC.****CONSENT ORDER, ETC. IN REGARD TO ALLEGED VIOLATIONS OF
SECS. 5(A) OF THE FEDERAL TRADE COMMISSION ACT**

*Docket No. C-4336; File No. 102 3136
Filed, October 13, 2011 — Decision, October 13, 2011*

This consent order addresses allegations that Google, Inc. provided inadequate privacy disclosures in violation of the FTC Act. In 2010, Google launched a social networking service called Google Buzz that allowed users to share updates, comments, photos, videos, and other information through posts or “buzzes.” The Google Buzz platform was available to consumers who signed up for Gmail, Google’s web-based email product. The complaint alleges that Google violated the FTC Act (1) by failing to advise Gmail users that its information would become public by default through Google Buzz; (2) by deceiving consumers about their ability to decline enrollment in certain features of Google Buzz; and (3) by misrepresenting its compliance with certain international data transfer laws. The order prohibits Google from misrepresenting the privacy and confidentiality of its users’ information. The order further requires Google to provide any user with clear and prominent notice and to obtain express affirmative consent prior to sharing the user’s information with any third party, under certain conditions. The order further requires Google to establish and maintain a comprehensive privacy program., and that Google obtain an independent, third-party assessment of its privacy practices every other year for the next 20 years.

Participants

For the *Commission*: *Katherine Race Brin and Kathryn D. Ratté.*

For the *Respondent*: *Al Gidari, Perkins Coie.*

COMPLAINT

The Federal Trade Commission, having reason to believe that Google Inc. (“Google” or “respondent”), a corporation, has violated the Federal Trade Commission Act (“FTC Act”), and it appearing to the Commission that this proceeding is in the public interest, alleges:

Complaint

1. Respondent Google is a Delaware corporation with its principal office or place of business at 1600 Amphitheatre Parkway, Mountain View, CA 94043.

2. The acts and practices of respondent as alleged in this complaint have been in or affecting commerce, as “commerce” is defined in Section 4 of the FTC Act.

RESPONDENT’S BUSINESS PRACTICES

3. Google is a technology company best known for its web-based search engine, which provides free search results to consumers. Google also provides various free web products to consumers, including its widely used web-based email service, Gmail, which has been available since April 2004. Among other things, Gmail allows consumers to send and receive emails, chat with other users through Google’s instant messaging service, Google Chat, and store email messages, contact lists, and other information on Google’s servers.

4. Google’s free web products for consumers also include: Google Reader, which allows users to subscribe to, read, and share content online; Picasa, which allows users to edit, post, and share digital photos; and Blogger, Google’s weblog publishing tool that allows users to share text, photos, and video.

5. Google also offers consumers the ability to create a “Google profile,” which enables them to make certain information about themselves public and to link to their content on Google product websites, such as the user’s Google Reader shared items, public Picasa Web Albums, and Blogger blog. Information on a consumer’s public Google profile, which may include the consumer’s name, location, and photo, is available on the Internet and may be indexed by search engines.

RESPONDENT’S STATEMENTS

6. Respondent has disseminated or caused to be disseminated statements to consumers on its website regarding its privacy practices, including but not limited to:

Complaint

- a. From approximately October 2004 until October 2010, the following statement in the Gmail Privacy Policy about Google's use of consumer information provided through Gmail:

Gmail stores, processes and maintains your messages, contact lists and other data related to your account in order to provide the service to you.

- b. From approximately October 2005 until October 2010, the following statement in Google's Privacy Policy regarding consumers' choices about the uses of their personal information in all of Google's products, including Gmail:

When you sign up for a particular service that requires registration, we ask you to provide personal information. If we use this information in a manner different than the purpose for which it was collected, then we will ask for your consent prior to such use.

RESPONDENT'S LAUNCH OF GOOGLE BUZZ

7. On February 9, 2010, Google launched a social networking service called Google Buzz ("Google Buzz" or "Buzz") within the Gmail product. Google Buzz is a platform that allows users to share updates, comments, photos, videos, and other information through posts or "buzzes" made either publicly or privately to individuals or groups of users. Google used the information of consumers who signed up for Gmail, including first and last name and email contacts, to populate the social network. Without prior notice or the opportunity to consent, Gmail users were, in many instances, automatically set up with "followers" (people following the user). In addition, after enrolling in Buzz, Gmail users were automatically set up to "follow" other users.

8. On the day Buzz was launched, Gmail users who signed into their accounts were taken to a welcome screen that announced the new service and highlighted features such as: "No set up needed – You're already following the people you email

Complaint

and chat with the most in Gmail.” Gmail users had to elect one of two options to proceed to their inboxes: “Sweet! Check out Buzz” or “Nah, go to my inbox.” Exhibit A shows how the initial Buzz screen appeared to consumers.

- a. If a Gmail user selected “Nah, go to my inbox” from the initial Buzz screen, that user’s information was nonetheless shared in a number of ways:
 - i. The user could be “followed” by other Gmail users who had enrolled in Buzz.
 - ii. If the user had previously created a public Google profile, the user could appear on the public Google profiles of people who had enrolled in Buzz and were following the user.
 - iii. A Buzz link would appear in the list of links on the user’s Gmail page. If the user clicked on the that link, he or she would be taken to the Buzz welcome screen and automatically enrolled in Buzz, without any disclosure of that fact and without any further action on the user’s part. Exhibit B shows how the Buzz welcome screen appeared to consumers. The user would be enrolled in Buzz even if the user did not click the “Okay” button at the bottom of the welcome screen.
- b. Regardless of whether they chose “Sweet! Check out Buzz” or “Nah, go to my inbox,” Gmail users had an option to click a “Turn off Buzz” link, contained in small type at the bottom of the Gmail home page after login. Clicking that link removed the Buzz tab from the user’s Gmail page. Gmail users who had clicked “Sweet! Check out Buzz” or had clicked on the Buzz link in Gmail, then later clicked the “Turn off Buzz” link, nonetheless continued to appear as a “follower” on the Google profiles and Google Buzz pages of the people whom they emailed the most. In addition, on each such profile, a “follow” link was placed next to

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the Gmail user's name, so other individuals could begin following the user.

9. The setup process for Gmail users who enrolled in Buzz did not adequately communicate that certain previously private information would be shared publicly by default. Further, the controls that would allow the user to change the defaults were confusing and difficult to find.

- a. Users who clicked on "Sweet! Check out Buzz" from the Buzz welcome screen, as well as users that selected "Nah, go to my Inbox" and later clicked the Buzz tab, were directed to a Buzz welcome screen that stated: "You're set up to follow the people you email and chat with the most," and listed the users' followers and the people the user was set up to follow. However, there was no disclosure on this screen that, by default, those lists might later be posted on a user's public Google profile, exposing the list of people with whom a user chatted or emailed most often. *See* Exhibit B.
- b. When first attempting to post in Buzz, users were directed to click through a profile creation screen, which explained that users needed to create a public Google profile before participating in Buzz. The profile creation screen contained the following header: "How do you want to appear to others?" The screen also included the following language in prominent, contrasting type: "Before participating in Buzz, you need a public profile with your name and photo. It's visible on the web so friends can find and recognize you. You can post publicly to the world or privately to only the people you choose." The profile creation screen also included the following language in small gray letters against a white background: "Your profile will include your name, photo, people you follow and people who follow you." Exhibit C shows how the profile creation screen appeared to consumers.
- c. In order to find controls that would allow the user to stop following certain individuals, a user had to take the additional step to click a link marked "edit," which

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expanded the profile creation screen. Only after clicking “edit” could users choose not to have their lists of followers and people the user was following shown on the user’s public Google profile. They did so by unchecking a pre-checked box. Users who saw no reason to edit their profile – particularly those who already had created a Google profile and did not realize new information would be added and publicly available by default on that profile – would never have learned that these controls were available. Exhibit D shows how the expanded profile creation screen appeared to consumers.

- d. The default setting for items posted in Google Buzz was “public” – shared with all of a user’s followers – though users had the ability to select “private” from a drop-down menu to post to a more limited group. Public buzzes were added to a user’s public Google profile, which was searchable on the Internet and could be indexed by search engines.
- e. Google Buzz also automatically connected to other information users had made public through Google products such as Picasa and Reader. In many instances, this information was automatically compiled and broadcast in public buzzes that showed up on the user’s public Google profile.

10. Certain personal information of Gmail users was shared without consumers’ permission through the Google Buzz social network.

- a. In some cases, Gmail users had previously blocked certain email contacts from viewing other information about them, but those preferences were not carried over to Buzz. For example, even if a Gmail user blocked an individual in Google Chat or Google Reader, that person was not blocked in Buzz and could show up as a follower of that Gmail user.
- b. Users could not block followers who did not have a public Google profile. Moreover, an individual who

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had not provided a first or last name when setting up a Google account would appear as an “unknown” follower to a user. The user was not only unable to block such an individual from following them, but they had no way of knowing the individual’s identity.

- c. If a Google Buzz user wanted to reply or direct a comment to an individual, the user placed the @ sign in front of the individual’s name, and Google suggested names from a user’s contact list. If the user selected a name or account from the suggest list that was not associated with a Google profile, Buzz filled in the field with that person’s private email address. Using an individual’s private email address in a public reply or comment thus exposed the address to all followers of the user and allowed that email address to be accessed by search engines.

11. In response to the launch of Google Buzz, many users complained about the automatic generation of lists of followers and people to follow from email contact lists that included in some cases: individuals against whom they had obtained restraining orders; abusive ex-husbands; clients of mental health professionals; clients of attorneys; children; and recruiters they had emailed regarding job leads. Further, because of the default settings and the complex and multi-step nature of respondent’s disclosures described in paragraph 9, consumers were confused about what information was made public through Buzz and complained about the potential disclosure of private email addresses.

12. Following widespread public criticism and thousands of consumer complaints, Google made certain changes to the Buzz service. Among other things, Google: (1) gave users the ability to effectively disable or turn off Buzz; (2) switched from setting up Gmail users with an automatic list of people to follow to suggesting a list of people to follow for users to approve; (3) made the process for editing lists of followers and people to follow clearer and more easily accessible; (4) made it possible for users to block any follower, regardless of whether that follower had a public profile; (5) made the option not to show lists of followers on a user’s public profile more prominent; (6)

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discontinued the feature that automatically connected to information from other websites, such as Picasa and Google Reader; and (7) fixed the @ reply function so that private email addresses of users would not be made public.

VIOLATIONS OF THE FTC ACT

13. As set forth in paragraph 6(a), respondent has represented, expressly or by implication, that it used, and would use, information from consumers signing up for Gmail only for the purpose of providing them with a web-based email service.

14. In truth and in fact, as described in paragraphs 7-11, respondent did not use information from consumers signing up for Gmail only for the purpose of providing them with a web-based email service. Instead, Google used this information to populate its new social networking service. Therefore, the representations set forth in paragraph 13 were, and are, false or misleading and constitute a deceptive act or practice.

15. As set forth in paragraph 6(b), respondent has represented, expressly or by implication, that it would seek consumers' consent to use information they provided for a purpose other than that for which it was collected.

16. In truth and in fact, as described in paragraphs 7-11, respondent did not seek consumers' consent before using the information they provided in connection with Gmail for the Google Buzz social networking product. Therefore, the representations set forth in paragraph 15 were, and are, false or misleading and constitute a deceptive act or practice.

17. As set forth in paragraph 8, by offering the option "Nah, go to my inbox," as well as the option to "Turn off Buzz," respondent has represented, expressly or by implication, that consumers who clicked on these options would not be enrolled in Buzz.

18. In truth and in fact, as described in paragraph 8, consumers who clicked on these options were enrolled in certain features of Buzz. Therefore, the representations set forth in

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paragraph 17 were, and are, false and misleading and constitute a deceptive act or practice.

19. As set forth in paragraph 9, respondent represented, expressly or by implication, through the Buzz enrollment screens and statements such as “How do you want to appear to others?” that consumers would be able to exercise control over what information would be made public through their Google public profile. Respondent failed to disclose, or failed to disclose adequately, that in most instances the contacts with whom users emailed and chatted the most would become public by default and that user information submitted through other Google products would be automatically broadcast through Buzz. These facts would be material to consumers in their enrollment in and use of the Google Buzz service. Therefore, respondent’s failure to adequately disclose these facts, in light of the representations made, was, and is, a deceptive act or practice.

U.S.-EU SAFE HARBOR FRAMEWORK

20. The U.S.-EU Safe Harbor Framework provides a method for U.S. companies to transfer personal data outside of the European Union (“EU”) that is consistent with the requirements of the European Union Data Protection Directive (“Directive”). The Directive sets forth EU requirements for privacy and the protection of personal data. Among other things, it requires EU Member States to implement legislation that prohibits the transfer of personal data outside the EU, with exceptions, unless the European Commission (“EC”) has made a determination that the recipient jurisdiction’s laws ensure the protection of such personal data. This determination is commonly referred to as meeting the EU’s “adequacy” standard.

21. To satisfy the EU’s adequacy standard for certain commercial transfers, the U.S. Department of Commerce (“Commerce”) and the EC negotiated the U.S.-EU Safe Harbor Framework, which went into effect in 2000. The Safe Harbor is a voluntary framework that allows U.S. companies to transfer personal data lawfully from the EU to the U.S. To join the Safe Harbor, a company must self-certify to Commerce that it complies with seven principles and related requirements that have been deemed to meet the EU’s adequacy standard.

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22. The Safe Harbor privacy principles, issued by Commerce on July 21, 2000, include the following:

NOTICE: An organization must inform individuals about the purposes for which it collects and uses information about them, how to contact the organization with any inquiries or complaints, the types of third parties to which it discloses the information, and the choices and means the organization offers individuals for limiting its use and disclosure. This notice must be provided in clear and conspicuous language when individuals are first asked to provide personal information to the organization or as soon thereafter as is practicable, but in any event before the organization uses such information for a purpose other than that for which it was originally collected or processed by the transferring organization or discloses it for the first time to a third party.

CHOICE: An organization must offer individuals the opportunity to choose (opt out) whether their personal information is (a) to be disclosed to a third party or (b) to be used for a purpose that is incompatible with the purpose(s) for which it was originally collected or subsequently authorized by the individual. Individuals must be provided with clear and conspicuous, readily available, and affordable mechanisms to exercise choice.

23. From October 2005 until the present, Google has maintained a current self-certification to Commerce and has appeared on the list of Safe Harbor companies on the Commerce website. Prior to the launch of the Buzz social networking product, Google transferred data collected from Gmail users in Europe to the United States for processing.

24. From approximately October 2005 until the present, Google made the following statement in its Privacy Policy regarding its participation in the U.S.-EU Safe Harbor Framework:

Google adheres to the US Safe Harbor Privacy Principles of Notice, Choice, Onward Transfer, Security, Data Integrity, Access and Enforcement, and is registered with

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the U.S. Department of Commerce's Safe Harbor Program.

25. In truth and in fact, as described in paragraph 7, respondent did not adhere to the US Safe Harbor Privacy Principles of Notice and Choice. In particular, respondent did not give Gmail users notice before using the information collected for Gmail for a purpose other than that for which it was originally collected. Respondent also did not give Gmail users choice about using their information for a purpose that was incompatible with the purpose for which it was originally collected. Therefore, the representations set forth in paragraphs 23 and 24 were, and are, false or misleading and constitutes a deceptive act or practice.

26. The acts and practices of respondent as alleged in this complaint constitute unfair or deceptive acts or practices, in or affecting commerce, in violation of Section 5(a) of the Federal Trade Commission Act.

THEREFORE, the Federal Trade Commission this thirteenth day of October, 2011, has issued this complaint against respondent.

By the Commission.

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EXHIBIT A



New! Google Buzz in Gmail

Share updates, photos, videos, and more.
Start conversations about the things you find interesting.



No setup needed

You're already following the people you email and chat with the most in Gmail.



Everything in one place

Follow your friends and get recommended buzz from others — all within Gmail.



Inbox integration

Comments appear right in your inbox so it's easy to keep the conversation going.

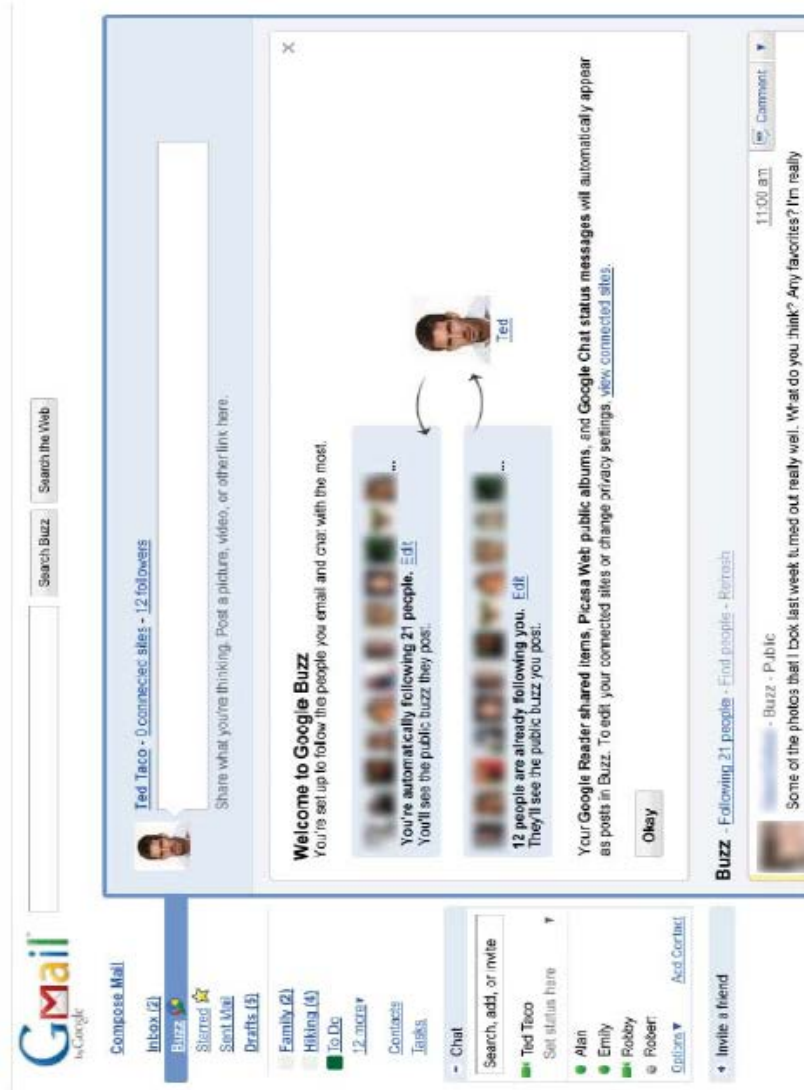
Sweet! Check out Buzz

[Nah...go to my inbox](#)



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EXHIBIT B




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EXHIBIT C

How do you want to appear to others? ✕

Profile preview - [Edit](#)



Ted Taco
[Ted has 12 followers](#)
[Ted is following 19](#)

Your profile will include your name, photo, people you follow, and people who follow you.

Before participating in Buzz, you need a public profile with your name and photo. It's visible on the web so friends can find and recognize you. You can post publicly to the world or privately to only the people you choose. [Why do I need a profile?](#)

[Cancel, don't post buzz](#)

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EXHIBIT D



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DECISION AND ORDER

The Federal Trade Commission, having initiated an investigation of certain acts and practices of the Respondent named in the caption hereof, and the Respondent having been furnished thereafter with a copy of a draft of Complaint which the Bureau of Consumer Protection proposed to present to the Commission for its consideration and which, if issued, would charge the Respondent with violation of the Federal Trade Commission Act; and

The Respondent and counsel for the Commission having thereafter executed an agreement containing a consent order, an admission by the Respondent of all the jurisdictional facts set forth in the aforesaid draft complaint, a statement that the signing of the agreement is for settlement purposes only and does not constitute an admission by the Respondent that the law has been violated as alleged in such complaint, or that any of the facts as alleged in such complaint, other than jurisdictional facts, are true, and waivers and other provisions as required by the Commission's Rules; and

The Commission having thereafter considered the matter and having determined that it had reason to believe that the Respondent has violated the Federal Trade Commission Act, and that a complaint should issue stating its charges in that respect, and having thereupon accepted the executed consent agreement and placed such agreement on the public record for a period of thirty (30) days for the receipt and consideration of public comments, and having duly considered the comments received from interested persons pursuant to Section 2.34 of its Rules, now in further conformity with the procedure prescribed in Section 2.34 of its Rules, 16 C.F.R. § 2.34, the Commission hereby issues its complaint, makes the following jurisdictional findings, and enters the following order:

1. Respondent Google is a Delaware corporation with its principal office or place of business at 1600 Amphitheatre Parkway, Mountain View, CA 94043.

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2. The Federal Trade Commission has jurisdiction of the subject matter of this proceeding and of the Respondent, and the proceeding is in the public interest.

ORDER**DEFINITIONS**

For purposes of this order, the following definitions shall apply:

1. Unless otherwise specified, “respondent” shall mean Google, its successors and assigns, officers, agents, representatives, and employees. For the purpose of Parts I, II, and III of this order, “respondent” shall also mean Google acting directly or through any corporation, subsidiary, division, website, or other device.
2. “Clear(ly) and prominent(ly)” shall mean:
 - a. In textual communications (e.g., printed publications or words displayed on the screen of a computer or mobile device), the required disclosures are of a type, size, and location sufficiently noticeable for an ordinary consumer to read and comprehend them, in print that contrasts highly with the background on which they appear;
 - b. In communications disseminated orally or through audible means (e.g., radio or streaming audio), the required disclosures are delivered in a volume and cadence sufficient for an ordinary consumer to hear and comprehend them;
 - c. In communications disseminated through video means (e.g., television or streaming video), the required disclosures are in writing in a form consistent with subpart (A) of this definition and shall appear on the screen for a duration sufficient

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for an ordinary consumer to read and comprehend them, and in the same language as the predominant language that is used in the communication; and

- d. In all instances, the required disclosures: (1) are presented in an understandable language and syntax; and (2) include nothing contrary to, inconsistent with, or in mitigation of any other statements or disclosures provided by respondent.
3. “Commerce” shall mean as defined in Section 4 of the Federal Trade Commission Act, 15 U.S.C. § 44.
 4. “Google user” shall mean an identified individual from whom respondent has collected information for the purpose of providing access to respondent’s products and services.
 5. “Covered information” shall mean information respondent collects from or about an individual, including, but not limited to, an individual’s: (a) first and last name; (b) home or other physical address, including street name and city or town; (c) email address or other online contact information, such as a user identifier or screen name; (d) persistent identifier, such as IP address; (e) telephone number, including home telephone number and mobile telephone number; (f) list of contacts; (g) physical location; or any other information from or about an individual consumer that is combined with (a) through (g) above.
 6. “Third party” shall mean any individual or entity other than: (1) respondent; (2) a service provider of respondent that: (i) uses or receives covered information collected by or on behalf of respondent for and at the direction of the respondent and no other individual or entity, (ii) does not disclose the data, or any individually identifiable information derived from such data, to any individual or entity other than respondent, and (iii) does not use the data for any other purpose; or (3) any entity that uses covered

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information only as reasonably necessary: (i) to comply with applicable law, regulation, or legal process, (ii) to enforce respondent's terms of use, or (iii) to detect, prevent, or mitigate fraud or security vulnerabilities.

I.

IT IS ORDERED that respondent, in or affecting commerce, shall not misrepresent in any manner, expressly or by implication:

- A. the extent to which respondent maintains and protects the privacy and confidentiality of any covered information, including, but not limited to, misrepresentations related to: (1) the purposes for which it collects and uses covered information, and (2) the extent to which consumers may exercise control over the collection, use, or disclosure of covered information.
- B. the extent to which respondent is a member of, adheres to, complies with, is certified by, is endorsed by, or otherwise participates in any privacy, security, or any other compliance program sponsored by the government or any other entity, including, but not limited to, the U.S. EU Safe Harbor Framework.

II.

IT IS FURTHER ORDERED that respondent, prior to any new or additional sharing by respondent of the Google user's identified information with any third party, that: 1) is a change from stated sharing practices in effect at the time respondent collected such information, and 2) results from any change, addition, or enhancement to a product or service by respondent, in or affecting commerce, shall:

- A. Separate and apart from any final "end user license agreement," "privacy policy," "terms of use" page, or similar document, clearly and prominently disclose: (1) that the Google user's information will be

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disclosed to one or more third parties, (2) the identity or specific categories of such third parties, and (3) the purpose(s) for respondent's sharing; and

- B. Obtain express affirmative consent from the Google user to such sharing.

III.

IT IS FURTHER ORDERED that respondent, in or affecting commerce, shall, no later than the date of service of this order, establish and implement, and thereafter maintain, a comprehensive privacy program that is reasonably designed to: (1) address privacy risks related to the development and management of new and existing products and services for consumers, and (2) protect the privacy and confidentiality of covered information. Such program, the content and implementation of which must be documented in writing, shall contain privacy controls and procedures appropriate to respondent's size and complexity, the nature and scope of respondent's activities, and the sensitivity of the covered information, including:

- A. the designation of an employee or employees to coordinate and be responsible for the privacy program.
- B. the identification of reasonably foreseeable, material risks, both internal and external, that could result in the respondent's unauthorized collection, use, or disclosure of covered information, and an assessment of the sufficiency of any safeguards in place to control these risks. At a minimum, this privacy risk assessment should include consideration of risks in each area of relevant operation, including, but not limited to: (1) employee training and management, including training on the requirements of this order, and (2) product design, development, and research.
- C. the design and implementation of reasonable privacy controls and procedures to address the risks identified through the privacy risk assessment, and regular

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testing or monitoring of the effectiveness of those privacy controls and procedures.

- D. the development and use of reasonable steps to select and retain service providers capable of appropriately protecting the privacy of covered information they receive from respondent, and requiring service providers by contract to implement and maintain appropriate privacy protections.
- E. the evaluation and adjustment of respondent's privacy program in light of the results of the testing and monitoring required by subpart C, any material changes to respondent's operations or business arrangements, or any other circumstances that respondent knows or has reason to know may have a material impact on the effectiveness of its privacy program.

IV.

IT IS FURTHER ORDERED that, in connection with its compliance with Part III of this order, respondent shall obtain initial and biennial assessments and reports ("Assessments") from a qualified, objective, independent third party professional, who uses procedures and standards generally accepted in the profession. A person qualified to prepare such Assessments shall have a minimum of three (3) years of experience in the field of privacy and data protection. All persons conducting such Assessments and preparing such reports shall be approved by the Associate Director for Enforcement, Bureau of Consumer Protection, Federal Trade Commission, Washington, D.C. 20580, in his or her sole discretion. The reporting period for the Assessments shall cover: (1) the first one hundred and eighty (180) days after service of the order for the initial Assessment, and (2) each two (2) year period thereafter for twenty (20) years after service of the order for the biennial Assessments. Each Assessment shall:

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- A. set forth the specific privacy controls that respondent has implemented and maintained during the reporting period;
- B. explain how such privacy controls are appropriate to respondent's size and complexity, the nature and scope of respondent's activities, and the sensitivity of the covered information;
- C. explain how the privacy controls that have been implemented meet or exceed the protections required by Part III of this order; and
- D. certify that the privacy controls are operating with sufficient effectiveness to provide reasonable assurance to protect the privacy of covered information and that the controls have so operated throughout the reporting period.

Each Assessment shall be prepared and completed within sixty (60) days after the end of the reporting period to which the Assessment applies. Respondent shall provide the initial Assessment to the Associate Director for Enforcement, Bureau of Consumer Protection, Federal Trade Commission, Washington, D.C. 20580, within ten (10) days after the Assessment has been prepared. All subsequent biennial Assessments shall be retained by respondent until the order is terminated and provided to the Associate Director of Enforcement within ten (10) days of request.

V.

IT IS FURTHER ORDERED that respondent shall maintain and upon request make available to the Federal Trade Commission for inspection and copying, unless respondent asserts a valid legal privilege, a print or electronic copy of:

- A. for a period of three (3) years from the date of preparation or dissemination, whichever is later, all widely disseminated statements that describe the extent to which respondent maintains and protects the

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privacy and confidentiality of any covered information, with all materials relied upon in making or disseminating such statements;

- B. for a period of six (6) months from the date received, all consumer complaints directed at respondent, or forwarded to respondent by a third party, that allege unauthorized collection, use, or disclosure of covered information and any responses to such complaints;
- C. for a period of five (5) years from the date received, any documents, whether prepared by or on behalf of respondent, that contradict, qualify, or call into question respondent's compliance with this order; and
- D. for a period of three (3) years after the date of preparation of each Assessment required under Part III of this order, all materials relied upon to prepare the Assessment, whether prepared by or on behalf of respondent, including but not limited to all plans, reports, studies, reviews, audits, audit trails, policies, training materials, and assessments, for the compliance period covered by such Assessment.

VI.

IT IS FURTHER ORDERED that respondent shall deliver a copy of this order to all current and future principals, officers, directors, and managers, and to all current and future employees, agents, and representatives having supervisory responsibilities relating to the subject matter of this order. Respondent shall deliver this order to such current personnel within thirty (30) days after service of this order, and to such future personnel within thirty (30) days after the person assumes such position or responsibilities.

VII.

IT IS FURTHER ORDERED that respondent shall notify the Commission at least thirty (30) days prior to any change in the corporation that may affect compliance obligations arising under

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this order, including, but not limited to, a dissolution, assignment, sale, merger, or other action that would result in the emergence of a successor corporation; the creation or dissolution of a subsidiary, parent, or affiliate that engages in any acts or practices subject to this order; the proposed filing of a bankruptcy petition; or a change in either corporate name or address. *Provided, however,* that, with respect to any proposed change in the corporation about which respondent learns less than thirty (30) days prior to the date such action is to take place, respondent shall notify the Commission as soon as is practicable after obtaining such knowledge. All notices required by this Part shall be sent by certified mail to the Associate Director, Division of Enforcement, Bureau of Consumer Protection, Federal Trade Commission, Washington, D.C. 20580.

VIII.

IT IS FURTHER ORDERED that respondent shall, within ninety (90) days after the date of service of this order file with the Commission a true and accurate report, in writing, setting forth in detail the manner and form in which respondent has complied with this order. Within ten (10) days of receipt of written notice from a representative of the Commission, respondent shall submit additional true and accurate written reports.

IX.

This order will terminate on October 13, 2031, or twenty (20) years from the most recent date that the United States or the Commission files a complaint (with or without an accompanying consent decree) in federal court alleging any violation of the order, whichever comes later; *provided, however,* that the filing of such a complaint will not affect the duration of:

- A. any Part in this order that terminates in fewer than twenty (20) years;
- B. this order if such complaint is filed after the order has terminated pursuant to this Part.

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Provided, further, that if such complaint is dismissed or a federal court rules that respondent did not violate any provision of the order, and the dismissal or ruling is either not appealed or upheld on appeal, then the order as to such respondent will terminate according to this Part as though the complaint had never been filed, except that the order will not terminate between the date such complaint is filed and the later of the deadline for appealing such dismissal or ruling and the date such dismissal or ruling is upheld on appeal.

By the Commission.

ANALYSIS OF CONSENT ORDER TO AID PUBLIC COMMENT

The Federal Trade Commission has accepted, subject to final approval, a consent agreement from Google Inc. (“Google”).

The proposed consent order has been placed on the public record for thirty (30) days for receipt of comments by interested persons. Comments received during this period will become part of the public record. After thirty (30) days, the Commission will again review the agreement and the comments received, and will decide whether it should withdraw from the agreement and take appropriate action or make final the agreement’s proposed order.

On February 9, 2010, Google launched a social networking service called Google Buzz (“Google Buzz” or “Buzz”) within Gmail, its web-based email product. Google Buzz is a platform that allows users to share updates, comments, photos, videos, and other information through posts or “buzzes” made either publicly or privately to individuals or groups of users. Google used the information of consumers who signed up for Gmail, including first and last name and email contacts, to populate the social

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network, which, in many instances, resulted in certain previously private information being made public.

The Commission's complaint alleges that Google violated Section 5(a) of the FTC Act by falsely representing to users signing up for Gmail that it would use their information only for the purpose of providing them with web-based email. The complaint also alleges that Google falsely represented to consumers that it would seek their consent before using their information for a purpose other than that for which it was collected. The complaint further alleges that Google deceived consumers about their ability to decline enrollment in certain features of Buzz. In addition, the complaint alleges that Google failed to disclose adequately that certain information would become public by default through the Buzz product. Finally, the complaint alleges that Google misrepresented its compliance with the U.S.-EU Safe Harbor Framework, a mechanism by which U.S. companies may transfer data from the European Union to the United States consistent with European law.

The proposed order contains provisions designed to prevent Google from engaging in the future in practices similar to those alleged in the complaint with respect to all Google products and services, not only Gmail or Buzz.

Part I of the proposed order prohibits Google from misrepresenting the privacy and confidentiality of any "covered information," as well as the company's compliance with any privacy, security, or other compliance program, including but not limited to the U.S.-EU Safe Harbor Framework. "Covered information" is defined broadly to include an individual's: (a) first and last name; (b) home or other physical address, including street name and city or town; (c) email address or other online contact information, such as a user identifier or screen name; (d) persistent identifier, such as IP address; (e) telephone number, including home telephone number and mobile telephone number; (f) list of contacts; (g) physical location; or any other information from or about an individual consumer that is combined with (a) through (g) above.

Analysis to Aid Public Comment

Part II of the proposed order requires Google to give Google users a clear and prominent notice and to obtain express affirmative consent prior to sharing the Google user's information with any third party in connection with a change, addition or enhancement to any product or service, where such sharing is contrary to stated sharing practices in effect at the time the Google user's information was collected. This provision is limited to users of Google's products and services whom Google has identified at the time it shares their information with third parties, for example, users who are logged into a Google product.

Part III of the proposed order requires Google to establish and maintain a comprehensive privacy program that is reasonably designed to: (1) address privacy risks related to the development and management of new and existing products and services, and (2) protect the privacy and confidentiality of covered information.

The privacy program must be documented in writing and must contain privacy controls and procedures appropriate to Google's size and complexity, the nature and scope of its activities, and the sensitivity of covered information. Specifically, the order requires Google to:

- designate an employee or employees to coordinate and be responsible for the privacy program;
- identify reasonably-foreseeable, material risks, both internal and external, that could result in the unauthorized collection, use, or disclosure of covered information and assess the sufficiency of any safeguards in place to control these risks;
- design and implement reasonable privacy controls and procedures to control the risks identified through the privacy risk assessment and regularly test or monitor the effectiveness of the safeguards' key controls and procedures;
- develop and use reasonable steps to select and retain service providers capable of appropriately protecting the privacy of covered information they receive from respondent, and require service providers by contract to

Analysis to Aid Public Comment

implement and maintain appropriate privacy protections;
and

- evaluate and adjust its privacy program in light of the results of the testing and monitoring, any material changes to its operations or business arrangements, or any other circumstances that it knows or has reason to know may have a material impact on the effectiveness of its privacy program.

Part IV of the proposed order requires that Google obtain within 180 days, and on a biennial basis thereafter for twenty (20) years, an assessment and report from a qualified, objective, independent third-party professional, certifying, among other things, that: it has in place a privacy program that provides protections that meet or exceed the protections required by Part III of the proposed order; and its privacy controls are operating with sufficient effectiveness to provide reasonable assurance that the privacy of covered information is protected.

Parts V through IX of the proposed order are reporting and compliance provisions. Part V requires that Google retain all “widely disseminated statements” that describe the extent to which respondent maintains and protects the privacy and confidentiality of any covered information, along with all materials relied upon in making or disseminating such statements, for a period of three (3) years. Part V further requires Google to retain, for a period of six (6) months from the date received, all consumer complaints directed at Google, or forwarded to Google by a third party, that allege unauthorized collection, use, or disclosure of covered information and any responses to such complaints. Part V also requires Google to retain for a period of five (5) years from the date received, documents that contradict, qualify, or call into question its compliance with the proposed order. Finally, Part V requires that Google retain all materials relied upon to prepare the third-party assessments for a period of three (3) years after the date that each assessment is prepared.

Part VI requires dissemination of the order now and in the future to principals, officers, directors, and managers, and to all current and future employees, agents, and representatives having

Concurring Statement

supervisory responsibilities relating to the subject matter of the order. Part VII ensures notification to the FTC of changes in corporate status. Part VIII mandates that Google submit an initial compliance report to the FTC and make available to the FTC subsequent reports. Part IX is a provision “sunsetting” the order after twenty (20) years, with certain exceptions.

The purpose of the analysis is to aid public comment on the proposed order. It is not intended to constitute an official interpretation of the proposed order or to modify its terms in any way.

**CONCURRING STATEMENT OF
COMMISSIONER J. THOMAS ROSCH**

I concur in accepting, subject to final approval, a consent agreement from Google Inc. (“Google”) for public comment. However, it should be emphasized that this consent agreement is being accepted, subject to final approval. I have substantial reservations about Part II of the consent agreement. My concerns are threefold. Before I describe them, however, I want to make clear that I do not mean to defend Google. Google can – and should – speak for itself. However, I believe that, as a Commission, we must always be concerned that a consent agreement, like a litigated decree, is consistent with the public interest. For that reason, I am opposed to accepting consent agreements that may be contrary to the public interest because a party is willing to agree to terms that hurt other competitors as much or more than the terms will hurt that party. That may occur, for example, when a consent agreement is used as “leverage” in dealing with the practices of other competitors. Part II of the proposed consent order may be susceptible to this happening.

Concurring Statement

More specifically, the crux of the violation alleged in the Complaint is that Google represented in its general “Privacy Policy” that “When you sign up for a particular service that requires registration, we ask you to provide personal information. If we use this information in a manner different from the purpose for which it was collected, then we will ask for your consent prior to such use.” However, when Google initiated its social networking service (“Google Buzz”) it used personal information previously collected for other purposes without asking for users’ consent prior to this use. Part II of the proposed consent order prohibits Google, without prior “express affirmative consent” (an “opt-in” requirement) from engaging in any “new or additional sharing” of previously collected personal information “with any third party” that results from “any change, addition, or enhancement” to any Google product or service.

First, Google did not represent in its general “Privacy Policy” (or otherwise, according to the Complaint) that the “consent” it would seek would require consumers to “opt in” as required by Part II. Indeed, the Complaint does not allege that Google ever asked consumers to signify their “consent” by “opting in” (as opposed to “opting out”). To be sure, insofar as Google did not seek “consent” at all, its representation in its general “Privacy Policy” was deceptive in violation of Section 5. But the “opt in” requirement in Part II is seemingly brand new. It does not echo what Google promised to do at the outset. In the separate Statement that I issued when the staff issued its preliminary Privacy Report, I expressed concern about whether an “opt in” requirement in these circumstances might sometimes be contrary to the public interest. Then, as now, I was concerned that it might be used as leverage in consent negotiations with other competitors.

Second, Part II of the proposed consent order applies whenever Google engages in any “new or additional sharing” of previously collected personal information “with any third party” for the next twenty years, not just any “material” new or additional sharing of that information. Because internet business models (and technology) change so rapidly, Google (and its competitors) are bound to engage in “new or additional” sharing of previously collected information with third parties during that

Concurring Statement

period. That means that Part II is certain to apply (and with some frequency) during that period as long as Google does not warn users or consumers in its “general Privacy Policy” that it may engage in such sharing in the future.

Third, Part II applies not just to Google’s social networking services or products, but to every single Google service or product that undergoes some “change, addition, or enhancement” (terms that are not defined in Part II) that results from the sharing of certain information. As a practical matter, this means that Google is at risk that Part II will apply across the board to every existing product or service that Google offers, including any product or service that involves the tracking and sharing of identified Google users’ browsing behavior.

In short, on the face of it, Part II seems to be contrary to Google’s self-interest. I therefore ask myself if Google willingly agreed to it, and if so, why it did so. Surely it did not do so simply to save itself litigation expense. But did it do so because it was being challenged by other government agencies and it wanted to “get the Commission off its back”? Or did it do so in hopes that Part II would be used as leverage in future government challenges to the practices of its competitors? In my judgment, neither of the latter explanations is consistent with the public interest.

Nor am I comforted that the purpose and effect of Part II may be to “fence in” Google. I am aware of the teaching of *Jacob Siegel Co. v. FTC*, 327 U.S. 608 (1946) that a “fencing in” order may cover legal conduct as long as that conduct is “reasonably related” to the violation. Even if Part II may be considered to cover conduct that is “reasonably related” to the violation here, any consent order, whether litigated or negotiated, must be consistent with the public interest. I look forward to public comment about whether Part II of the proposed consent order meets that requirement.

Complaint

IN THE MATTER OF

**KOBY BROWN AND GREGORY PEARSON
DOING BUSINESS AS DERMAPPS**CONSENT ORDER, ETC. IN REGARD TO ALLEGED VIOLATIONS OF
SECS. 5(A) AND 12 OF THE FEDERAL TRADE COMMISSION ACT*Docket No. C-4337; File No. 102 3205**Filed, October 13, 2011 — Decision, October 13, 2011*

This consent order addresses allegations that Koby Brown and Gregory W. Pearson, doing business as DERMAPPS (“Respondents”), violated the FTC Act by misrepresenting the effectiveness of its AcneApp mobile software application. The complaint alleges that Respondents falsely claimed its AcneApp mobile software application effectively treated acne, by holding light-emitting display screen next to the area of skin to be treated for several minutes each day. The complaint alleges Respondents falsely represented a journal study proved that red and blue light therapy was an effective treatment for acne. The order prohibits Respondents from making any representation that AcneApp or any other device provides effective treatment for acne, unless Respondents have competent and reliable scientific evidence to substantiate the claim. The order further requires Respondents to pay approximately \$15,000 towards consumer relief.

Participants

For the *Commission*: *Stacey Ferguson and James A. Prunty.*

For the *Respondents*: *Sesha Kalapatapu.*

COMPLAINT

The Federal Trade Commission, having reason to believe that Koby Brown and Gregory W. Pearson (“respondents”), individually and doing business as DERMAPPS, have violated the provisions of the Federal Trade Commission Act, and it appearing to the Commission that this proceeding is in the public interest, alleges:

1. Respondent Koby Brown (“Brown”) is the developer, and a seller or marketer, of a mobile software application called “AcneApp.” At all times relevant to this complaint, Brown,

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individually or in concert with others, formulated, directed, controlled, or participated in the acts or practices alleged in this complaint. His principal office or place of business is located in Houston, Texas.

2. Respondent Gregory W. Pearson (“Pearson”) is a licensed and board-certified dermatologist, and a seller or marketer of a mobile software application called “AcneApp.” At all times relevant to this complaint, Pearson, individually or in concert with others, formulated, directed, controlled, or participated in the acts or practices alleged in this complaint. His principal office or place of business is located in Houston, Texas.

3. Respondents Brown and Pearson have developed, labeled, advertised, promoted, offered for sale, sold, and distributed AcneApp to consumers, including teens, through the iTunes Store, an electronic retail platform operated by Apple, Inc., from at least September 24, 2009 and continuing thereafter. From September 1, 2009 through March 15, 2011, there were approximately 11,600 downloads of AcneApp.

4. AcneApp is a “device” within the meaning of Sections 12 and 15 of the Federal Trade Commission Act.

5. The acts and practices of respondents, as alleged herein, have been in or affecting commerce, as “commerce” is defined in Section 4 of the Federal Trade Commission Act.

6. Respondents have disseminated or caused to be disseminated advertisements for AcneApp through the iTunes store, including, but not limited to, the advertisement in the attached Exhibit A. This advertisement contains the following statements and depictions:

Pre-Download Advertisement: (Exhibit A - website print screen capture)

On screen: New York Times:

December 30, 2009 “Better Skin to the Touch?” –
Camille Sweeney

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“... a Houston dermatologist has bypassed the hand-held gadget and tried to harness the power of in-office acne treatments in a more familiar form: the iPhone or iPod Touch.”

FOX News:

January 12, 2009 “Can iPhone Application Treat Your Acne?” – Ned Hibberd

“... self esteem emergency? These flashing lights may be their salvation.”

iTunes REVIEWS [*Selected and featured by respondents*]

- “This app is probably the best thing ever to surface. i’ve (sic) had problems with my skin for years. Acne app is easy to use and you can use it any time of the day. My skin started to clear after the first week and it’s noticable (sic). I’ve used pro activ (sic), roaccutane (sic) and every other skin product but this is truly amazing.” (Australia)
- “I will have to say that I was skeptical at first but am amazed by the results of really dedicating time to this.” (US)
- “I was very hesitant to purchase it a (sic) first because I thought it was simply exploiting peoples’ insecurities, but it works! Maybe the best app I’ve bought!” (US)
- “Hormones go crazy when your (sic) pregnant but you can’t use chemicals to dry up your breakouts[.] [T]his app is the solution!” (US)
- This is the best money I have ever spent[.] [I]t works amazing for me[.] [A]lready seeing the difference in 2 days. It stops me form (sic) getting spots and reduces the redness of the present acne. It’s a gotta buy for people suffering with acne. 5 stars :D (United Kingdom)

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IMPORTANT STUFF:

This app was developed by a dermatologist.

A study published by the British Journal of Dermatology showed blue and red light treatments eliminated p-acne bacteria (a major cause of acne) and reduces skin blemishes by 76%. Studies showed that light treatments were almost twice as effective as benzoyl peroxide, the main ingredient in Proactiv and other common over-the-counter blemish treatments.

INSTRUCTIONS:

Begin by choosing a light from the tab bar below.
Blue & Red alternating light is the recommended option.

Rest the iPhone against your skin's acne-prone areas for 2 minutes daily to improve skin health without prescription drugs.

Blue Light: fights bacteria.
Red Light: helps heal skin.

* * *

This app is for entertainment purposes only and is not intended for treatment of any disease or medical condition.

© Copyright DermApps 2009-2010. All Rights Reserved.

AcneApp. Acne therapy without risky medications.

* * *

7. Through the means described in Paragraph 6, respondents have represented, expressly or by implication, that AcneApp is an effective treatment for acne.

8. Through the means described in Paragraph 6, respondents have represented, expressly or by implication, that they possessed

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and relied upon a reasonable basis that substantiated the representation set forth in Paragraph 7, at the time the representation was made.

9. In truth and in fact, respondents did not possess and rely upon a reasonable basis that substantiated the representation set forth in Paragraph 7, at the time the representation was made. Therefore, the representation set forth in Paragraph 8 was, and is, false or misleading.

10. Through the means described in Paragraph 6, respondents have represented, expressly or by implication, that a study published by the British Journal of Dermatology proves that blue and red light therapy such as that provided by AcneApp is an effective treatment for acne.

11. In truth and in fact, the study published by the British Journal of Dermatology does not prove that blue and red light therapy such as that provided by AcneApp is an effective treatment for acne. Therefore, the representation set forth in Paragraph 10 was, and is, false or misleading.

12. The acts and practices of respondents as alleged in this complaint constitute unfair or deceptive acts or practices, and the making of false advertisements, in or affecting commerce, in violation of Sections 5(a) and 12 of the Federal Trade Commission Act, 15 U.S.C. §§ 45(a) and 52.

THEREFORE, the Federal Trade Commission, this thirteenth day of October, 2011, has issued this complaint against respondents.

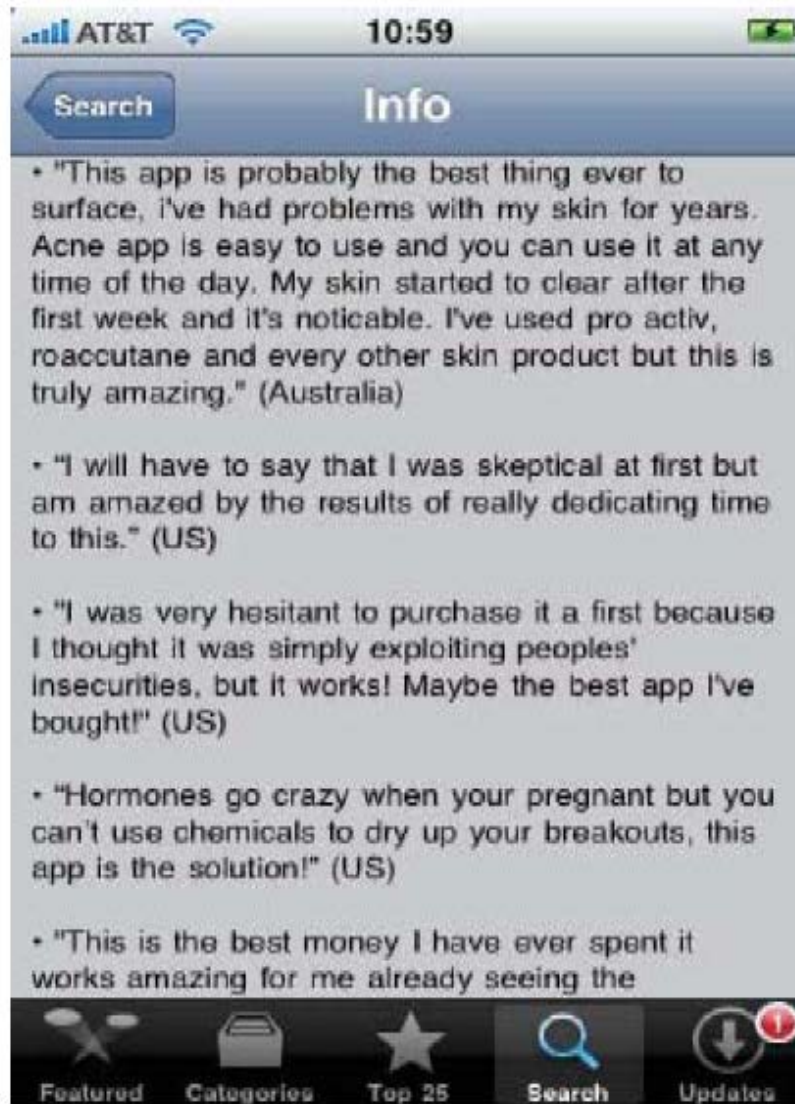
By the Commission.

Complaint

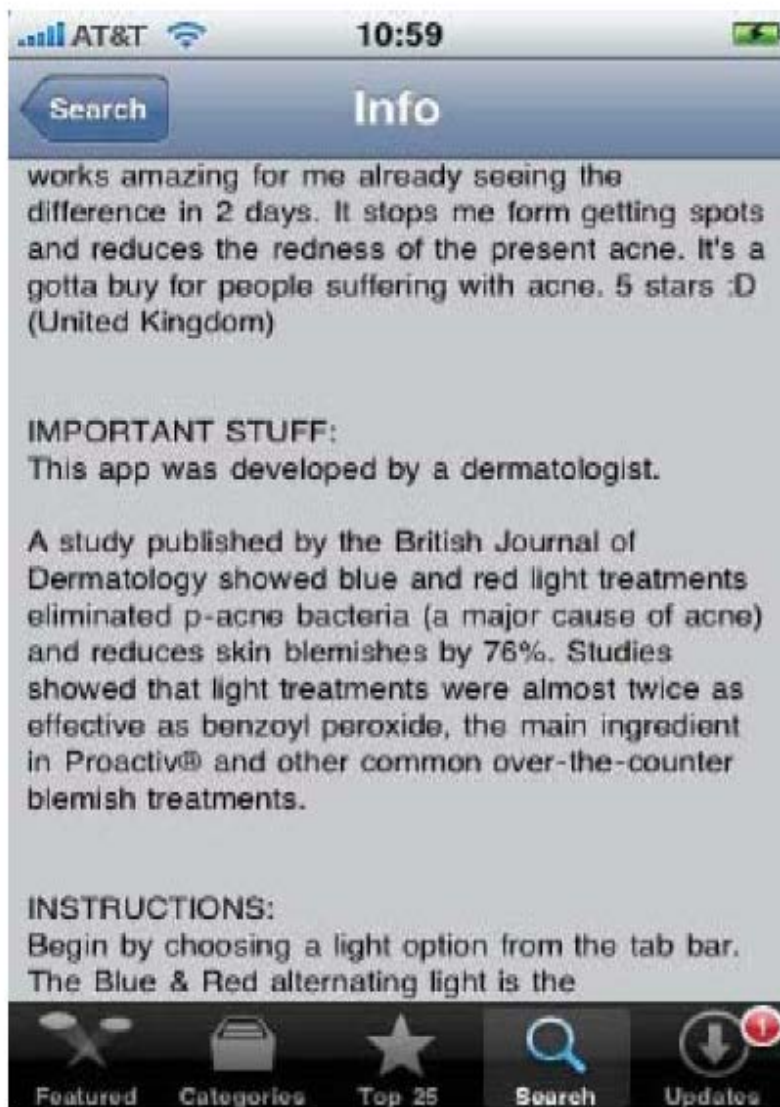
EXHIBIT A



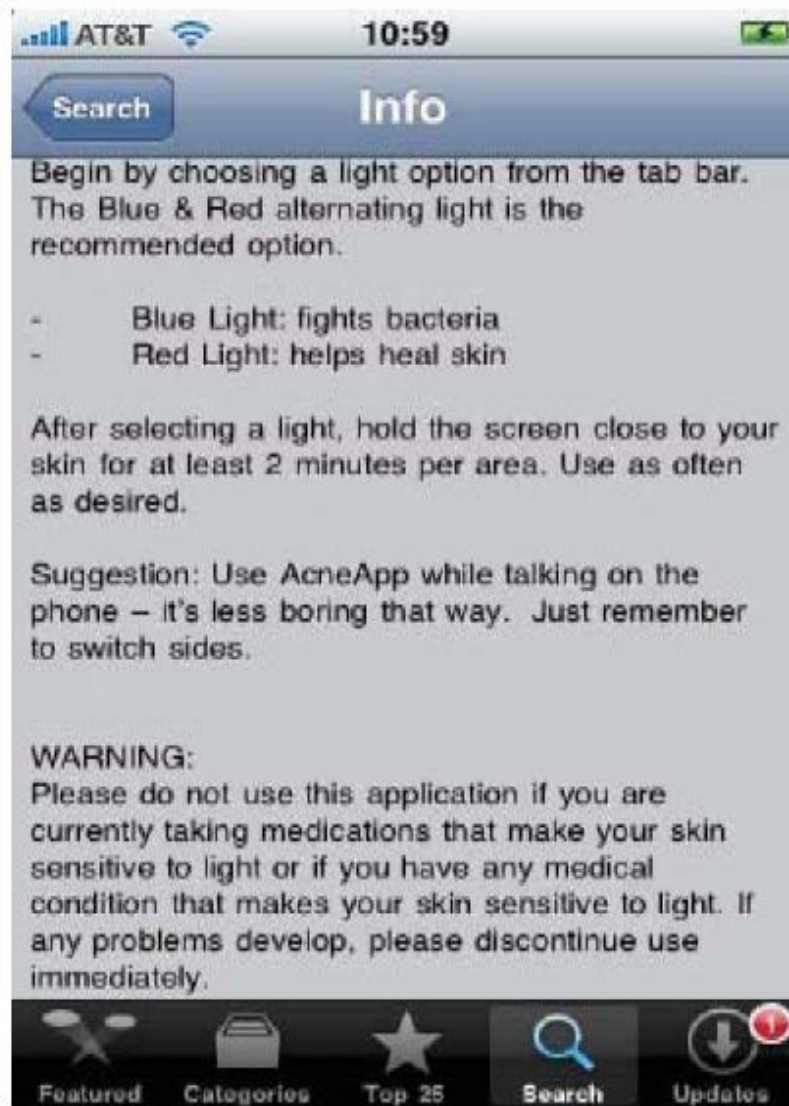
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Complaint



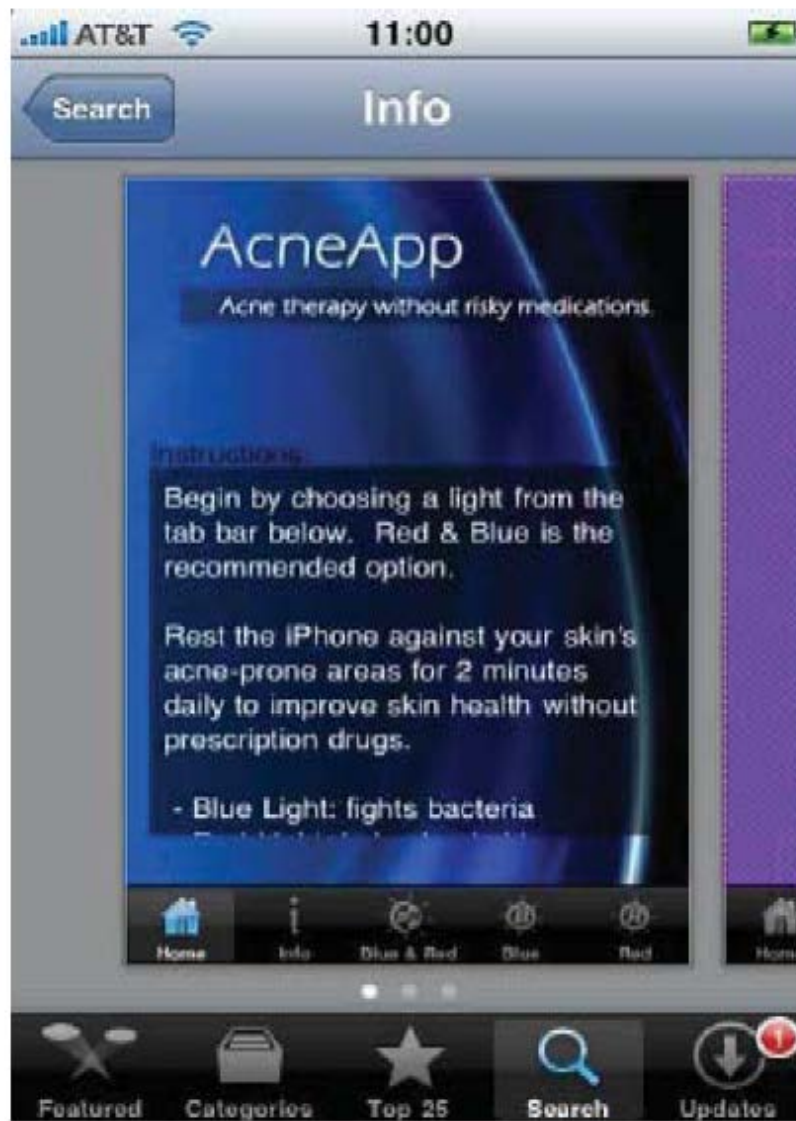
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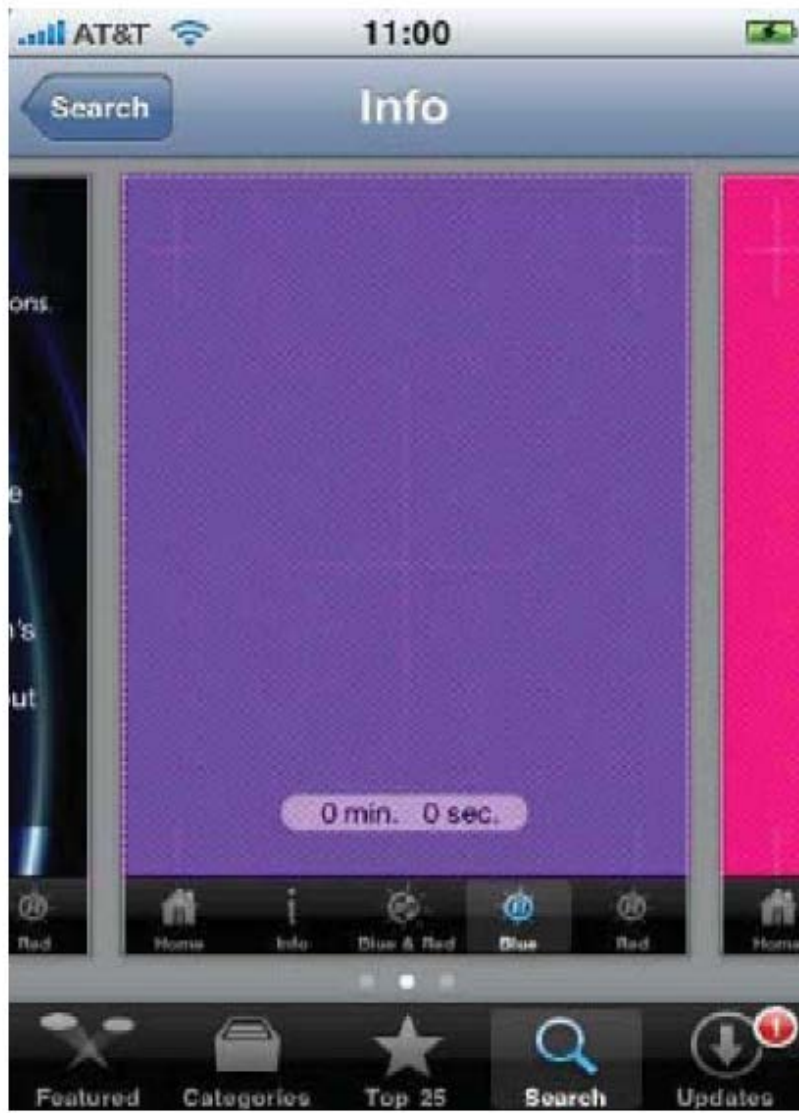
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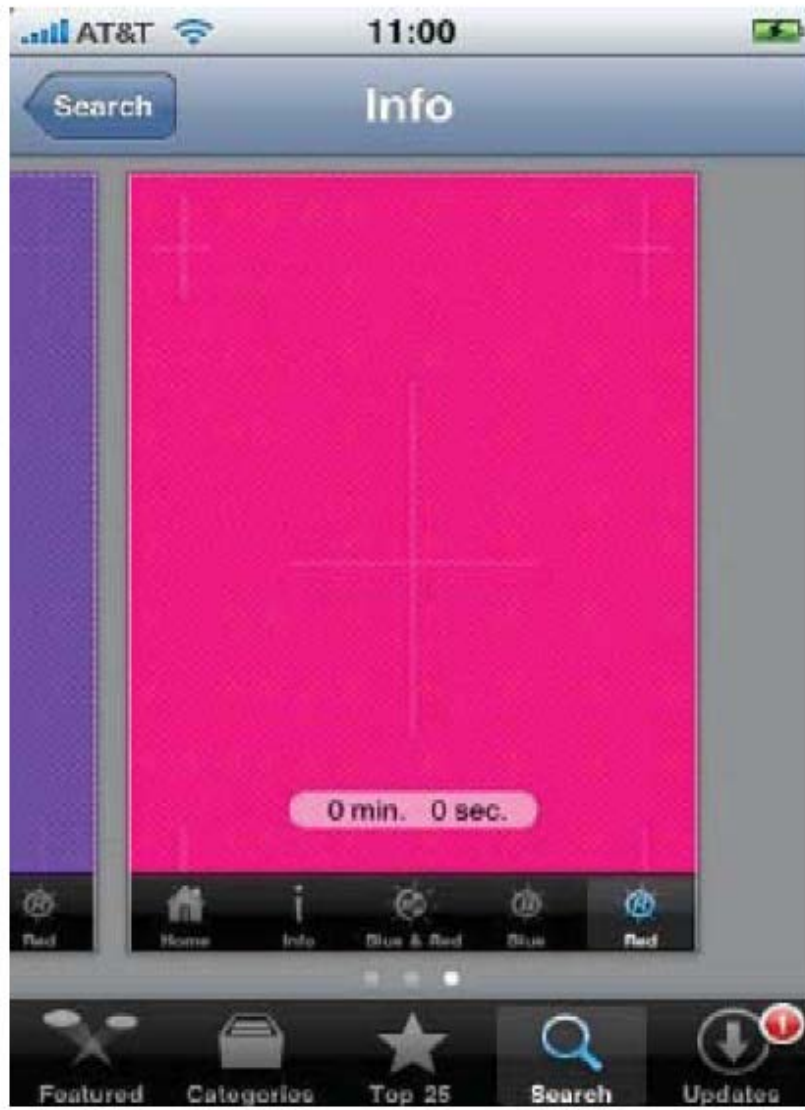
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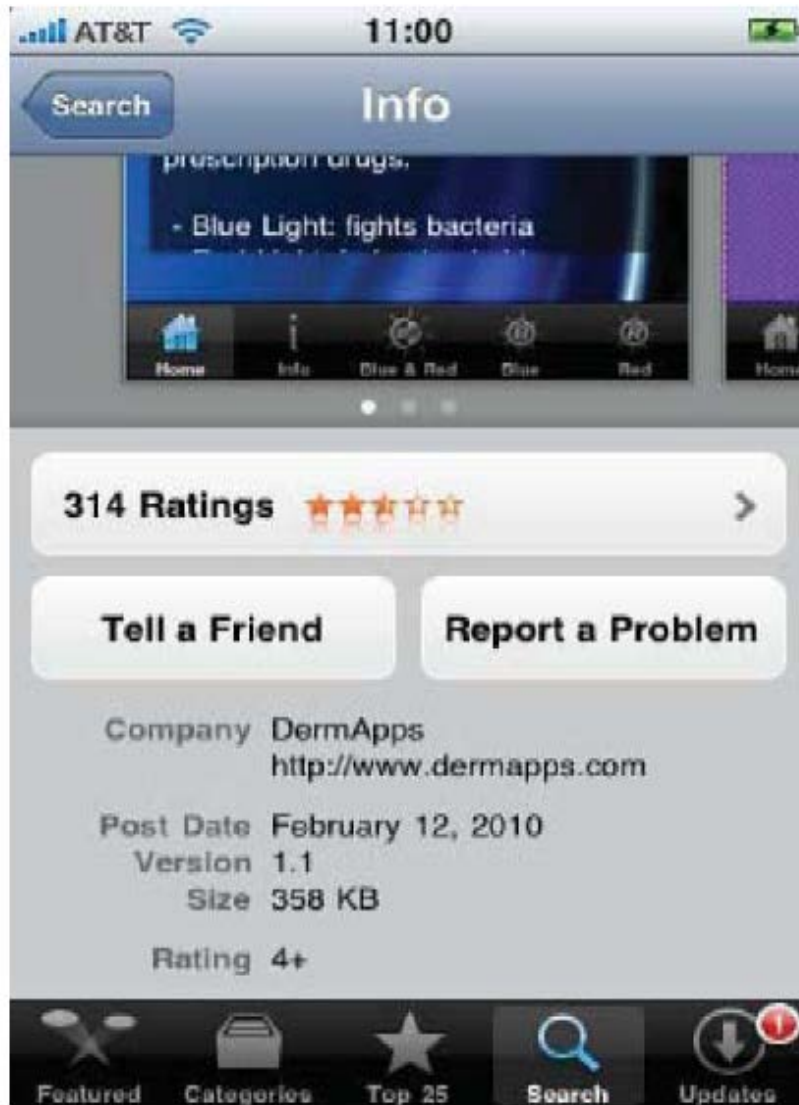
Complaint



Complaint



Complaint



Decision and Order

DECISION AND ORDER

The Federal Trade Commission (“Commission”) having initiated an investigation of certain acts and practices of the respondents named in the caption hereof, and the respondents having been furnished thereafter with a copy of a draft complaint that the Bureau of Consumer Protection proposed to present to the Commission for its consideration and which, if issued by the Commission, would charge the respondents with violation of the Federal Trade Commission Act, 15 U.S.C § 45 *et seq.*; and

Respondent, Gregory W. Pearson, and his attorney, respondent Koby Brown, who elected to proceed without counsel, and counsel for the Commission, having thereafter executed an agreement containing a consent order (“consent agreement”), an admission by the respondents of all the jurisdictional facts set forth in the aforesaid draft complaint, a statement that the signing of said consent agreement is for settlement purposes only and does not constitute an admission by the respondents that the law has been violated as alleged in the complaint, or that the facts as alleged in such complaint, other than jurisdictional facts, are true, and waivers and other provisions as required by the Commission’s Rules; and

The Commission having thereafter considered the matter and having determined that it has reason to believe that the respondents have violated the Federal Trade Commission Act, and that a complaint should issue stating its charges in that respect, and having thereupon accepted the executed consent agreement and placed such consent agreement on the public record for a period of thirty (30) days for the receipt and consideration of public comments, now in further conformity with the procedure prescribed in Section 2.34 of its Rules, the Commission hereby issues its complaint, makes the following jurisdictional findings and enters the following order:

1. Respondent Koby Brown is the developer, and a seller or marketer, of a mobile software application called “AcneApp” sold under the registered business name DERMAPPS. His principal office or place of business is located in Houston, Texas.

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2. Respondent Gregory W. Pearson is a licensed and board-certified dermatologist. He has also done business under the registered business name DERMAPPS. His principal office or place of business is located in Houston, Texas.
3. The Federal Trade Commission has jurisdiction of the subject matter of this proceeding and of the respondents, and the proceeding is in the public interest.

ORDER**DEFINITIONS**

For purposes of this order, the following definitions shall apply:

1. Unless otherwise specified, “respondents” shall mean Koby Brown and Gregory W. Pearson.
2. “Commerce” shall mean as defined in Section 4 of the Federal Trade Commission Act, 15 U.S.C. § 44.
3. The term “including” in this order shall mean “without limitation.”
4. The terms “and” and “or” in this order shall be construed conjunctively or disjunctively as necessary, to make the applicable phrase or sentence inclusive rather than exclusive.
5. The term “device” in this order shall be construed as a “device” within the meaning of Sections 12 and 15 of the Federal Trade Commission Act.

I.

IT IS ORDERED that respondents, directly or through any corporation, partnership, subsidiary, division, trade name, or other

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means, in connection with the manufacturing, labeling, advertising, promotion, offering for sale, sale, or distribution of any device, in or affecting commerce, shall not represent, in any manner, expressly or by implication, including through the use of a product name, endorsement, depiction, or illustration, that AcneApp or any other device provides effective treatment for acne, unless the representation is non-misleading and, at the time of making such representation, respondents possess and rely upon competent and reliable scientific evidence that substantiates that the representation is true. For purposes of this Part I, competent and reliable scientific evidence shall consist of at least two adequate and well- controlled human clinical studies of the device, conducted by different researchers, independently of each other, that conform to acceptable designs and protocols and whose results, when considered in light of the entire body of relevant and reliable scientific evidence, are sufficient to substantiate that the representation is true.

II.

IT IS FURTHER ORDERED that respondents, directly or through any corporation, partnership, subsidiary, division, trade name, or other means, in connection with the manufacturing, labeling, advertising, promotion, offering for sale, sale, or distribution of any device, in or affecting commerce, shall not make any representation, in any manner, expressly or by implication, including through the use of a product name, endorsement, depiction, or illustration, about the safety, benefits, performance, or efficacy of any device, unless the representation is non-misleading, and, at the time of making such representation, respondents possess and rely upon competent and reliable scientific evidence that is sufficient in quality and quantity based on standards generally accepted in the relevant scientific fields, when considered in light of the entire body of relevant and reliable scientific evidence, to substantiate that the representation is true. For purposes of this Part II, competent and reliable scientific evidence means tests, analyses, research, or studies that have been conducted and evaluated in an objective manner by qualified persons and are generally accepted in the profession to yield accurate and reliable results.

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III.

IT IS FURTHER ORDERED that respondents, directly or through any corporation, partnership, subsidiary, division, trade name, or other means, in connection with the manufacturing, advertising, labeling, promotion, offering for sale, sale, or distribution of any product or service, in or affecting commerce, shall not misrepresent, in any manner, expressly or by implication, including through the use of a product name, endorsement, depiction, or illustration, the existence, contents, validity, results, conclusions, or interpretations of any test, study, survey, or research.

IV.

IT IS FURTHER ORDERED that respondents shall pay to the Federal Trade Commission the sum of \$14,294. This payment shall be made in the following manner:

- A. The payment shall be made by wire transfer made payable to the Federal Trade Commission, the payment to be made no later than fifteen (15) days after the date that this order becomes final; provided that all respondents are primarily liable, jointly and severally, for the payment amount, including any default payment amount if the payment is in default, unless and until payment is made in full.
- B. In the event of any default in payment, which default continues for ten (10) days beyond the due date of payment, the amount due, together with interest, as computed pursuant to 28 U.S.C. § 1961(a), from the date of default to the date of payment, shall immediately become due and payable to the Commission. Respondents agree that, in such event, the facts as alleged in the complaint shall be taken as true in any subsequent litigation filed by the Commission to enforce its rights pursuant to this order, including, but not limited to, a nondischargeability complaint in any subsequent bankruptcy proceeding.

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- C. All funds paid pursuant to this Part, together with any accrued interest, shall be used by the Commission in its sole discretion to provide such relief as it determines to be reasonably related to respondents' practices alleged in the complaint, and to pay any attendant costs of administration. Such relief may include, but shall not be limited to, the rescission of contracts, payment of damages, and/or public notification respecting such unfair or deceptive acts or practices as alleged in the complaint. If the Commission determines, in its sole discretion, that such relief is wholly or partially impracticable, any funds not so used shall be paid to the United States Treasury. Respondents shall be notified as to how the funds are distributed, but shall have no right to contest the manner of distribution chosen by the Commission. No portion of the payment as herein provided shall be deemed a payment of any fine, penalty, or punitive assessment.
- D. Respondents shall make no claim to or demand for the return of the funds, directly or indirectly, through counsel or otherwise; and in the event of bankruptcy of any respondent, respondents acknowledge that the funds are not part of the debtor's estate, nor does the estate have any claim or interest therein.

V.

IT IS FURTHER ORDERED that respondents shall each, for five (5) years after the last date of dissemination of any representation covered by this order, maintain and, upon reasonable notice, make available to the Federal Trade Commission for inspection and copying:

- A. All advertisements and promotional materials containing the representation;
- B. All materials that were relied upon in disseminating the representation;

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- C. All tests, reports, studies, surveys, demonstrations, or other evidence in respondents' possession or control that contradict, qualify, or call into question the representation, or the basis relied upon for the representation, including complaints and other communications with consumers or with governmental or consumer protection organizations; and
- D. All acknowledgments of receipt of this order obtained pursuant to Part VI.

VI.

IT IS FURTHER ORDERED that respondents shall deliver a copy of this order to all current and future employees, agents, and representatives having responsibilities with respect to the subject matter of this order, and shall secure from each person a signed and dated statement acknowledging receipt of this order. For current personnel, delivery shall be within five (5) days of the date of service of this order. For new personnel, delivery shall occur prior to their first assuming their responsibilities.

VII.

IT IS FURTHER ORDERED that respondents shall each notify the Commission at least thirty (30) days prior to creating, or assuming any ownership interest in, any corporation that may affect compliance obligations arising under this order. *Provided, further,* that respondents shall each notify the Commission at least thirty (30) days prior to the dissolution, assignment, sale, merger, or other action involving such corporation that would result in the emergence of a successor corporation; the creation or dissolution of a subsidiary, parent, or affiliate that engages in any acts or practices subject to this order; the proposed filing of a bankruptcy petition; or a change in the name or address of such corporation. *Provided, however,* that, with respect to any proposed change in the corporation about which respondents learn less than thirty (30) days prior to the date such action is to take place, respondents shall notify the Commission as soon as is practicable after obtaining such knowledge. Unless otherwise directed by a representative of the Commission, all notices required by this Part

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shall be sent by overnight courier (not the U.S. Postal Service) to the Associate Director for Enforcement, Bureau of Consumer Protection, Federal Trade Commission, 600 Pennsylvania Avenue NW, Washington, DC 20580, with the subject line *In the Matter of Koby Brown and Gregory W. Pearson, dba DERMAPPS*. *Provided, however*, that, in lieu of overnight courier, notices may be sent by first-class mail, but only if an electronic version of such notices is contemporaneously sent to the Commission at Debrief@ftc.gov.

VIII.

IT IS FURTHER ORDERED that respondents, for a period of five (5) years after the date of issuance of this order, shall each notify the Commission of the discontinuance of their current business or employment, or of their affiliation with any new business or employment. The notice shall include the new business address and telephone number and a description of the nature of the business or employment, and their duties and responsibilities. Unless otherwise directed by a representative of the Commission, all notices required by this Part shall be sent by overnight courier (not the U.S. Postal Service) to the Associate Director for Enforcement, Bureau of Consumer Protection, Federal Trade Commission, 600 Pennsylvania Avenue NW, Washington, DC 20580, with the subject line *In the Matter of Koby Brown and Gregory W. Pearson, dba DERMAPPS*. *Provided, however*, that, in lieu of overnight courier, notices may be sent by first-class mail, but only if an electronic version of such notices is contemporaneously sent to the Commission at Debrief@ftc.gov.

IX.

IT IS FURTHER ORDERED that each respondent, within sixty (60) days after the date of service of this order, shall file with the Commission a true and accurate report, in writing, setting forth in detail the manner and form in which they have complied with this order. Within ten (10) days of receipt of written notice from a representative of the Commission, they shall submit additional true and accurate written reports.

Decision and Order

X.

This order will terminate on October 13, 2031, or twenty (20) years from the most recent date that the United States or the Federal Trade Commission files a complaint (with or without an accompanying consent decree) in federal court alleging any violation of this order, whichever comes later; *provided, however*, that the filing of such a complaint will not affect the duration of:

- A. Any Part in this order that terminates in less than twenty (20) years;
- B. This order's application to any respondent that is not named as a defendant in such complaint; and
- C. This order, if such complaint is filed after the order has terminated pursuant to this Part.

Provided, further, that if such complaint is dismissed or a federal court rules that respondents did not violate any provision of the order, and the dismissal or ruling is either not appealed or upheld on appeal, then the order will terminate according to this Part as though the complaint had never been filed, except that the order will not terminate between the date such complaint is filed and the later of the deadline for appealing such dismissal or ruling, and the date such dismissal or ruling is upheld on appeal.

By the Commission.

Analysis to Aid Public Comment

**ANALYSIS OF CONSENT ORDER TO
AID PUBLIC COMMENT**

The Federal Trade Commission (“FTC” or “Commission”) has accepted, subject to final approval, an agreement containing a consent order from Koby Brown and Gregory W. Pearson, dba DERMAPPS (“respondents”).

The proposed consent order (“proposed order”) has been placed on the public record for thirty (30) days for receipt of comments by interested persons. Comments received during this period will become part of the public record. After thirty (30) days, the Commission will again review the agreement and the comments received, and will decide whether it should withdraw from the agreement and take appropriate action or make final the agreement’s proposed order.

This matter involves the advertising of a mobile software application (“app”) called AcneApp which respondents developed and sold in Apple’s iTunes Store. Respondents claimed that AcneApp effectively treats acne. The instructions for this app directed consumers to hold the light-emitting display screen next to the area of skin to be treated for several minutes each day.

The Commission’s complaint alleges that respondents violated Sections 5 and 12 of the FTC Act by claiming, without substantiation, that the app provided an effective treatment for acne. The complaint also alleges that the respondents falsely represented that a study published in the British Journal of Dermatology proves that blue and red light therapy, such as that provided by AcneApp, is an effective treatment for acne.

The proposed consent order contains provisions designed to prevent respondents from engaging in similar practices in the future. Part I of the order prohibits respondents from making any representation that AcneApp, or any other device, as defined by Section 15 of the FTC Act, provides effective treatment for acne, unless respondents have competent and reliable scientific evidence to substantiate that claim.

Part II of the order requires respondents to have competent

Analysis to Aid Public Comment

and reliable scientific evidence before making any safety, performance, benefits, or efficacy claim about any device.

Part III of the order is a standard order provision relating to establishment claims, prohibiting the misrepresentation of any research, tests, or studies.

Part IV of the order requires respondents, within 15 days of the order, to pay the Commission \$14,294.

The remaining parts of the proposed order are standard provisions regarding record-keeping, dissemination of the order to officers and employees, prior notification to the Commission of corporate changes, notification of new employment, filing compliance of reports, and sunseting of the order.

The purpose of this analysis is to facilitate public comment on the proposed order, and it is not intended to constitute an official interpretation of the agreement and proposed order or to modify in any way their terms.

Complaint

IN THE MATTER OF

ANDREW N. FINKELCONSENT ORDER, ETC. IN REGARD TO ALLEGED VIOLATIONS OF
SECS. 5(A) AND 12 OF THE FEDERAL TRADE COMMISSION ACT*Docket No. C-4338; File No. 102 3206**Filed, October 13, 2011 — Decision, October 13, 2011*

Respondent Andrew Finkel developed and sold a mobile software application (“app”) called Acne Pwner in Google’s Android Marketplace. The Acne Pwner app directed consumers to hold a light-emitting display screen next to the area of skin to be treated for a few minutes each day. The complaint alleges that Respondent violated the FTC Act by claiming, without substantiation, that the Acne Pwner app effectively treated acne. The order prohibits Respondent from making any representations that Acne Pwner or any other device provides an effective treatment for acne, unless Respondent has competent and reliable scientific evidence to substantiate the claim. The order further requires Respondent to have competent and reliable scientific evidence before making any safety, performance, benefits, or efficacy claim about any device. Further, the order requires respondent to pay \$1,700 in consumer redress.

Participants

For the *Commission*: *Stacey Ferguson and James A. Prunty.*

For the *Respondent*: *Robert J. Lunn, Trevett Cristo Salzer & Andolina, P.C.*

COMPLAINT

The Federal Trade Commission, having reason to believe that Andrew N. Finkel (“respondent”) has violated the provisions of the Federal Trade Commission Act, and it appearing to the Commission that this proceeding is in the public interest, alleges:

1. Respondent Andrew N. Finkel (“Finkel”) is the developer, marketer, or seller of a mobile software application called “Acne Pwner.” At all times relevant to this complaint, Finkel, individually or in concert with others, formulated, directed, controlled, or participated in the acts or practices alleged in this

Complaint

complaint. His principal office or place of business is located in Rochester, New York.

2. Finkel has developed, labeled, advertised, promoted, offered for sale, sold, and distributed Acne Pwner to consumers, including teens, through the Android Marketplace, an electronic retail platform operated by Google, Inc., from at least February 1, 2010 and continuing thereafter. From February 1, 2010 through October 8, 2010, there were approximately 3,300 downloads of Acne Pwner.

3. Acne Pwner is a “device” within the meaning of Sections 12 and 15 of the Federal Trade Commission Act.

4. The acts and practices of respondent, as alleged herein, have been in or affecting commerce, as “commerce” is defined in Section 4 of the Federal Trade Commission Act.

5. Respondent has disseminated or caused to be disseminated advertisements for Acne Pwner through the Android Marketplace, including, but not limited to, the advertisement in the attached Exhibit A. This advertisement contains the following statements and depictions:

Pre-Download Advertisement: (Exhibit A - website print screen capture)

Kill ACNE with this simple, yet powerful tool!

“Light exposure has long been used as a short term treatment for acne. Recently, visible light has been successfully employed to treat mild to moderate acne.”

Blue frequency (Bacteria)
Red frequency (Healing)
Amber frequency (Repair) !NEW!

Keys: ZIT SKIN HEALTH SEX EASY FUN

{REVIEWS}

Complaint

* * *

6. Through the means described in Paragraph 5, respondent has represented, expressly or by implication, that Acne Pwner is an effective treatment for acne.

7. Through the means described in Paragraph 5, respondent has represented, expressly or by implication, that he possessed and relied upon a reasonable basis that substantiated the representation set forth in Paragraph 6, at the time the representation was made.

8. In truth and in fact, respondent did not possess and rely upon a reasonable basis that substantiated the representation set forth in Paragraph 6, at the time the representation was made. Therefore, the representation set forth in Paragraph 7 was, and is, false or misleading.

9. The acts and practices of respondent as alleged in this complaint constitute unfair or deceptive acts or practices, and the making of false advertisements, in or affecting commerce, in violation of Sections 5(a) and 12 of the Federal Trade Commission Act, 15 U.S.C. §§ 45(a) and 52.

THEREFORE, the Federal Trade Commission, this thirteenth day of October, 2011, has issued this complaint against respondent.

By the Commission.

Complaint

EXHIBIT A

The screenshot shows the top of an iPhone screen with various status icons (signal, Wi-Fi, battery, time 2:02 PM) and a dock with icons for Safari, App Store, iTunes, and Messages. Below the dock is the app listing for 'Acne Pwner' by Andrew Finkel. The app is priced at US\$0.99 and has a 4.5-star rating. The listing includes 'About' and 'Comments' buttons. A green bar highlights the 'Description' section, which contains the following text:

Kill ACNE with this simple, yet powerful tool!

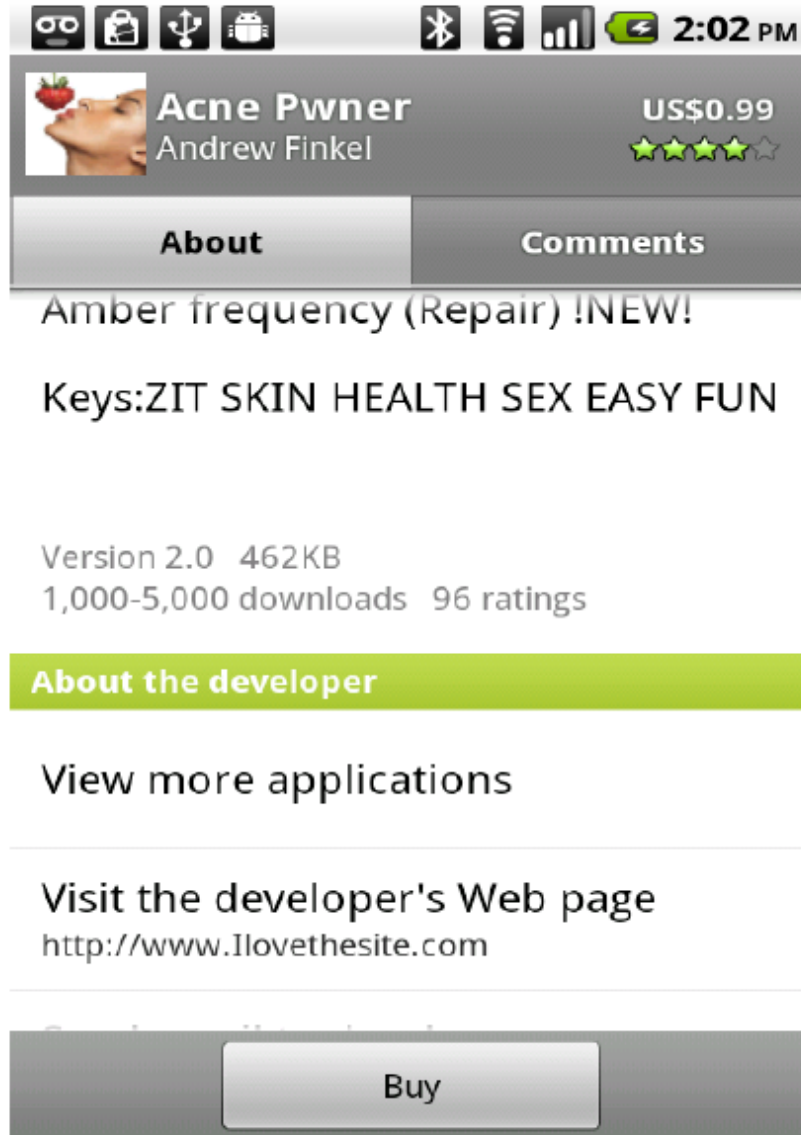
"Light exposure has long been used as a short term treatment for acne. Recently, visible light has been successfully employed to treat mild to moderate acne."

Blue frequency (Bacteria)
Red frequency (Healing)
Amber frequency (Repair) !NEW!

Keys:ZIT SKIN HEALTH SEX EASY FUN

At the bottom of the app listing is a large grey button labeled 'Buy'.

Complaint

EXHIBIT A

The screenshot shows the top portion of an Android application listing. At the top is a status bar with icons for camera, gallery, USB, Android, Bluetooth, Wi-Fi, signal strength, battery, and the time 2:02 PM. Below the status bar is the app header, which includes a profile picture of a woman with a strawberry on her lip, the app name "Acne Pwner", the developer name "Andrew Finkel", the price "US\$0.99", and a 4.5-star rating. Two buttons, "About" and "Comments", are positioned below the header. The main text of the listing reads "Amber frequency (Repair) !NEW!" followed by "Keys:ZIT SKIN HEALTH SEX EASY FUN". Below this, the app's version "Version 2.0", size "462KB", download count "1,000-5,000 downloads", and "96 ratings" are listed. A green bar highlights the "About the developer" section, which contains the text "View more applications". Below this is a link to "Visit the developer's Web page" with the URL "http://www.Ilovethesite.com". At the bottom of the listing is a large "Buy" button.

Acne Pwner
Andrew Finkel
US\$0.99
★★★★☆

About Comments

Amber frequency (Repair) !NEW!

Keys:ZIT SKIN HEALTH SEX EASY FUN

Version 2.0 462KB
1,000-5,000 downloads 96 ratings

About the developer

View more applications

Visit the developer's Web page
<http://www.Ilovethesite.com>

Buy

Complaint

EXHIBIT A

The screenshot shows the top status bar with icons for Google, a lock, USB, Android, Bluetooth, Wi-Fi, signal strength, battery, and the time 2:02 PM. Below the status bar is the app header for 'Acne Pwner' by Andrew Finkel, priced at US\$0.99 with a 4.5-star rating. Two buttons, 'About' and 'Comments', are visible. A green bar highlights the 'About the developer' section, which includes a link to 'View more applications', a link to 'Visit the developer's Web page' (http://www.Ilovethesite.com), and an option to 'Send email to developer' (afinke98@gmail.com). Another green bar highlights the 'Market content' section, which includes a 'Flag as inappropriate' option. At the bottom, a large grey button labeled 'Buy' is centered.

Complaint

EXHIBIT A



Complaint

EXHIBIT A

The screenshot shows an Android application interface. At the top, there is a status bar with various icons (Bluetooth, Wi-Fi, signal strength, battery) and the time 2:02 PM. Below the status bar is a header section for the product 'Acne Pwner' by Andrew Finkel. The header includes a small profile picture of a woman, the product name, the price 'US\$0.99', and a star rating of 4.5 out of 5. Below the header are two tabs: 'About' and 'Comments'. The 'Comments' tab is selected, showing a list of user reviews. Each review includes the user's name, the date, the rating, the text of the comment, and a thumbs up/down icon.

User	Date	Rating	Comment
grant	11/27/2010	2.5	Haha Crap
Raul	11/21/2010	5.0	So you mean is safe to use? how long do you think would be the reccomended time usage?
Anonymous	11/21/2010	5.0	@Raul It's not harmful, its the visual light spectrum. And its based on how frequency affects the body. People mostly use music for this kind of stuff
Puzzlespider	11/06/2010	4.0	Works for me, but better instructions wouldn't hurt
Kyle	11/04/2010	4.0	Didn't work for me at all

Complaint

EXHIBIT A

Acne Pwner US\$0.99
 Andrew Finkel

About **Comments**

Kyle 11/04/2010
 Didn't work for me at all

nontoxicpuppydog 11/02/2010
 I would like to have some suggestions/
 instructions on the best way to use this
 app. And, the amber color doesn't ever
 work.

Jose 10/25/2010
 Crappers, it works. Smoother skin n its
 clearing up.

cody 10/25/2010
 Helped greatly! I was skeptical at 1st but I
 definitely believe in it now.

kate 10/23/2010
 Awsome idea, just didnt work for me.
 Hope it does for others

Decision and Order

DECISION AND ORDER

The Federal Trade Commission (“Commission”) having initiated an investigation of certain acts and practices of the respondent named in the caption hereof, and the respondent having been furnished thereafter with a copy of a draft complaint that the Bureau of Consumer Protection proposed to present to the Commission for its consideration and which, if issued by the Commission, would charge the respondent with violation of the Federal Trade Commission Act, 15 U.S.C § 45 *et seq.*; and

The respondent, his attorney, and counsel for the Commission having thereafter executed an agreement containing a consent order (“consent agreement”), an admission by the respondent of all the jurisdictional facts set forth in the aforesaid draft complaint, a statement that the signing of said consent agreement is for settlement purposes only and does not constitute an admission by the respondent that the law has been violated as alleged in the complaint, or that the facts as alleged in such complaint, other than jurisdictional facts, are true, and waivers and other provisions as required by the Commission’s Rules; and

The Commission having thereafter considered the matter and having determined that it has reason to believe that the respondent has violated the Federal Trade Commission Act, and that a complaint should issue stating its charges in that respect, and having thereupon accepted the executed consent agreement and placed such consent agreement on the public record for a period of thirty (30) days for the receipt and consideration of public comments, now in further conformity with the procedure prescribed in Section 2.34 of its Rules, the Commission hereby issues its complaint, makes the following jurisdictional findings and enters the following order:

1. Respondent Andrew N. Finkel (“Finkel”) is a software developer. His current principal office or place of business is located in Rochester, New York.
2. The Federal Trade Commission has jurisdiction of the subject matter of this proceeding and of the respondent, and the proceeding is in the public interest.

Decision and Order

ORDER**DEFINITIONS**

For purposes of this order, the following definitions shall apply:

1. Unless otherwise specified, “respondent” shall mean Andrew N. Finkel.
2. “Commerce” shall mean as defined in Section 4 of the Federal Trade Commission Act, 15 U.S.C. § 44.
3. The term “including” in this order shall mean “without limitation.”
4. The terms “and” and “or” in this order shall be construed conjunctively or disjunctively as necessary, to make the applicable phrase or sentence inclusive rather than exclusive.
5. The term “device” in this order shall be construed as a “device” within the meaning of Sections 12 and 15 of the Federal Trade Commission Act.

I.

IT IS ORDERED that respondent, directly or through any corporation, partnership, subsidiary, division, trade name, or other means, in connection with the manufacturing, labeling, advertising, promotion, offering for sale, sale, or distribution of any device, in or affecting commerce, shall not represent, in any manner, expressly or by implication, including through the use of a product name, endorsement, depiction, or illustration, that Acne Pwner or any other device provides effective treatment for acne, unless the representation is non-misleading and, at the time of making such representation, respondent possesses and relies upon competent and reliable scientific evidence that substantiates that the representation is true. For purposes of this Part I, competent and reliable scientific evidence shall consist of at least two

Decision and Order

adequate and well- controlled human clinical studies of the device, conducted by different researchers, independently of each other, that conform to acceptable designs and protocols and whose results, when considered in light of the entire body of relevant and reliable scientific evidence, are sufficient to substantiate that the representation is true.

II.

IT IS FURTHER ORDERED that respondent, directly or through any corporation, partnership, subsidiary, division, trade name, or other means, in connection with the manufacturing, labeling, advertising, promotion, offering for sale, sale, or distribution of any device, in or affecting commerce, shall not make any representation, in any manner, expressly or by implication, including through the use of a product name, endorsement, depiction, or illustration, about the safety, benefits, performance, or efficacy of any device, unless the representation is non-misleading, and, at the time of making such representation, respondent possesses and relies upon competent and reliable scientific evidence that is sufficient in quality and quantity based on standards generally accepted in the relevant scientific fields, when considered in light of the entire body of relevant and reliable scientific evidence, to substantiate that the representation is true. For purposes of this Part II, competent and reliable scientific evidence means tests, analyses, research, or studies that have been conducted and evaluated in an objective manner by qualified persons and are generally accepted in the profession to yield accurate and reliable results.

III.

IT IS FURTHER ORDERED that respondent shall pay to the Federal Trade Commission the sum of \$1,700. This payment shall be made in the following manner:

- A. The payment shall be made by wire transfer made payable to the Federal Trade Commission, the payment to be made no later than fifteen (15) days after the date that this order becomes final; provided that respondent is liable for the payment amount,

Decision and Order

including any default payment amount if the payment is in default, unless and until payment is made in full.

- B. In the event of any default in payment, which default continues for ten (10) days beyond the due date of payment, the amount due, together with interest, as computed pursuant to 28 U.S.C. § 1961(a), from the date of default to the date of payment, shall immediately become due and payable to the Commission. Respondent agrees that, in such event, the facts as alleged in the complaint shall be taken as true in any subsequent litigation filed by the Commission to enforce its rights pursuant to this order, including, but not limited to, a nondischargeability complaint in any subsequent bankruptcy proceeding.
- C. All funds paid pursuant to this Part, together with any accrued interest, shall be used by the Commission in its sole discretion to provide such relief as it determines to be reasonably related to respondent's practices alleged in the complaint, and to pay any attendant costs of administration. Such relief may include, but shall not be limited to, the rescission of contracts, payment of damages, and/or public notification respecting such unfair or deceptive acts or practices as alleged in the complaint. If the Commission determines, in its sole discretion, that such relief is wholly or partially impracticable, any funds not so used shall be paid to the United States Treasury. Respondent shall be notified as to how the funds are distributed, but shall have no right to contest the manner of distribution chosen by the Commission. No portion of the payment as herein provided shall be deemed a payment of any fine, penalty, or punitive assessment.
- D. Respondent shall make no claim to or demand for the return of the funds, directly or indirectly, through counsel or otherwise; and in the event of bankruptcy, respondent acknowledges that the funds are not part of

Decision and Order

the debtor's estate, nor does the estate have any claim or interest therein.

IV.

IT IS FURTHER ORDERED that respondent shall, for five (5) years after the last date of dissemination of any representation covered by this order, maintain and, upon reasonable notice, make available to the Federal Trade Commission for inspection and copying:

- A. All advertisements and promotional materials containing the representation;
- B. All materials that were relied upon in disseminating the representation;
- C. All tests, reports, studies, surveys, demonstrations, or other evidence in his possession or control that contradict, qualify, or call into question the representation, or the basis relied upon for the representation, including complaints and other communications with consumers or with governmental or consumer protection organizations; and
- D. All acknowledgments of receipt of this order obtained pursuant to Part V.

V.

IT IS FURTHER ORDERED that respondent shall deliver a copy of this order to all current and future employees, agents, and representatives having responsibilities with respect to the subject matter of this order, and shall secure from each person a signed and dated statement acknowledging receipt of this order. For current personnel, delivery shall be within five (5) days of the date of service of this order. For new personnel, delivery shall occur prior to their first assuming their responsibilities.

Decision and Order

VI.

IT IS FURTHER ORDERED that respondent shall notify the Commission at least thirty (30) days prior to creating, or assuming any ownership interest in, any corporation that may affect compliance obligations arising under this order. *Provided, further,* that respondent shall notify the Commission at least thirty (30) days prior to the dissolution, assignment, sale, merger, or other action involving such corporation that would result in the emergence of a successor corporation; the creation or dissolution of a subsidiary, parent, or affiliate that engages in any acts or practices subject to this order; the proposed filing of a bankruptcy petition; or a change in the name or address of such corporation. *Provided, however,* that, with respect to any proposed change in the corporation about which respondent learns less than thirty (30) days prior to the date such action is to take place, the respondent shall notify the Commission as soon as is practicable after obtaining such knowledge. Unless otherwise directed by a representative of the Commission, all notices required by this Part shall be sent by overnight courier (not the U.S. Postal Service) to the Associate Director for Enforcement, Bureau of Consumer Protection, Federal Trade Commission, 600 Pennsylvania Avenue NW, Washington, DC 20580, with the subject line *In the Matter of Andrew N. Finkel*. *Provided, however,* that, in lieu of overnight courier, notices may be sent by first-class mail, but only if an electronic version of such notices is contemporaneously sent to the Commission at DEbrief@ftc.gov.

VII.

IT IS FURTHER ORDERED that respondent, for a period of five (5) years after the date of issuance of this order, shall notify the Commission of the discontinuance of his current business or employment, or of his affiliation with any new business or employment. The notice shall include the new business address and telephone number, his current residential address, and a description of the nature of his business or employment, and his duties and responsibilities. Unless otherwise directed by a representative of the Commission, all notices required by this Part shall be sent by overnight courier (not the U.S. Postal Service) to the Associate Director for Enforcement,

Decision and Order

Bureau of Consumer Protection, Federal Trade Commission, 600 Pennsylvania Avenue NW, Washington, DC 20580, with the subject line *In the Matter of Andrew N. Finkel*. *Provided, however*, that, in lieu of overnight courier, notices may be sent by first-class mail, but only if an electronic version of such notices is contemporaneously sent to the Commission at Debrief@ftc.gov.

VIII.

IT IS FURTHER ORDERED that respondent, within sixty (60) days after the date of service of this order, shall file with the Commission a true and accurate report, in writing, setting forth in detail the manner and form in which he has complied with this order. Within ten (10) days of receipt of written notice from a representative of the Commission, he shall submit additional true and accurate written reports.

IX.

This order will terminate on October 13, 2031, or twenty (20) years from the most recent date that the United States or the Federal Trade Commission files a complaint (with or without an accompanying consent decree) in federal court alleging any violation of this order, whichever comes later; *provided, however*, that the filing of such a complaint will not affect the duration of:

- A. Any Part in this order that terminates in less than twenty (20) years; and
- B. This order, if such complaint is filed after the order has terminated pursuant to this Part.

Provided, further, that if such complaint is dismissed or a federal court rules that respondent did not violate any provision of the order, and the dismissal or ruling is either not appealed or upheld on appeal, then the order will terminate according to this Part as though the complaint had never been filed, except that the order will not terminate between the date such complaint is filed

Analysis to Aid Public Comment

and the later of the deadline for appealing such dismissal or ruling, and the date such dismissal or ruling is upheld on appeal.

By the Commission.

ANALYSIS OF CONSENT ORDER TO AID PUBLIC COMMENT

The Federal Trade Commission (“FTC” or “Commission”) has accepted, subject to final approval, an agreement containing a consent order from Andrew N. Finkel (“respondent”).

The proposed consent order (“proposed order”) has been placed on the public record for thirty (30) days for receipt of comments by interested persons. Comments received during this period will become part of the public record. After thirty (30) days, the Commission will again review the agreement and the comments received, and will decide whether it should withdraw from the agreement and take appropriate action or make final the agreement’s proposed order.

This matter involves the advertising of a mobile software application (“app”) called Acne Pwner which respondent developed and sold in Google’s Android Marketplace. Respondent claimed that Acne Pwner effectively treats acne. The instructions for this app directed consumers to hold the light-emitting display screen next to the area of skin to be treated for a few minutes each day.

The Commission’s complaint alleges that respondent violated Sections 5 and 12 of the FTC Act by claiming, without substantiation, that the app provided an effective treatment for acne.

The proposed consent order contains provisions designed to prevent respondent from engaging in similar practices in the

Analysis to Aid Public Comment

future. Part I of the order prohibits respondent from making any representation that Acne Pwner, or any other device as defined by Section 15 of the FTC Act, provides effective treatment for acne, unless respondent has competent and reliable scientific evidence to substantiate that claim.

Part II of the order requires respondent to have competent and reliable scientific evidence before making any safety, performance, benefits, or efficacy claim about any device.

Part III of the order requires respondent, within 15 days of the date the order becomes final, to pay the Commission \$1,700.

The remaining parts of the proposed order are standard provisions regarding record-keeping, dissemination of the order to officers and employees, prior notification to the Commission of corporate changes, notification of new employment, filing of compliance reports, and sunseting of the order.

The purpose of this analysis is to facilitate public comment on the proposed order, and it is not intended to constitute an official interpretation of the agreement and proposed order or to modify in any way their terms.

Complaint

IN THE MATTER OF
CARDINAL HEALTH, INC.CONSENT ORDER, ETC. IN REGARD TO ALLEGED VIOLATIONS OF
SEC. 5 OF THE FEDERAL TRADE COMMISSION ACT AND SEC. 7 OF
THE CLAYTON ACT*Docket No. C-4339; File No. 091 0136*
Filed, October 18, 2011 — Decision, October 18, 2011

This consent order addresses the acquisition by Cardinal Health of nuclear pharmacies from Biotech Pharmacy, Inc., (“Biotech”) in the southwestern United States. anticompetitive effects. Nuclear pharmacies produce, distribute, and sell single photon emission computed tomography radiopharmaceuticals to hospitals and cardiology clinics, who use the products to diagnose and treat various diseases. The complaint alleges that Cardinal Health operates the nation’s largest network of nuclear pharmacies, and the acquisition would substantially lessen competition in the nuclear pharmacy markets in Las Vegas, Nevada; Albuquerque, New Mexico; and El Paso, Texas and enable Cardinal Health to increase prices for its nuclear pharmacy products. The order requires Cardinal Health to restore three nuclear pharmacies that it closed post-acquisition. The order further requires Cardinal Health to divest all intellectual property necessary for the acquirer to compete successfully in the nuclear pharmacy market. The order also requires Cardinal Health to grant each of its customers within the relevant geographic markets to terminate their existing contracts without penalty.

Participants

For the *Commission*: *William H. Efron* and *Jonathan W. Platt*.

For the *Respondent*: *Geoffrey Oliver*, *Joe Sims*, and *David Wales, Jones Day*.

COMPLAINT

Pursuant to the provisions of the Federal Trade Commission Act and the Clayton Act, and by virtue of the authority vested in it by said Acts, the Federal Trade Commission, having reason to believe that Respondent Cardinal Health, Inc.’s (“Cardinal Health”) acquisition of certain assets of Biotech, violated Section 5 of the Federal Trade Commission Act, as amended, 15 U.S.C. §

Complaint

45, and Section 7 of the Clayton Act, as amended, 15 U.S.C. § 18, and it appearing to the Commission that a proceeding in respect thereof would be in the public interest, hereby issues its Complaint, stating its charges as follows:

I. SUMMARY

1. Nuclear pharmacies provide radiopharmaceuticals to local hospitals and cardiology clinics, which use the products to diagnose and treat various diseases. Radiopharmaceuticals are drugs containing a radioactive isotope combined with a chemical compound. Due to the fact that the radioactive isotopes in radiopharmaceuticals have short half-lives and decay rapidly, a nuclear pharmacy for all practical purposes can only serve its local area. Accordingly, competition between nuclear pharmacies occurs at the local level.

2. Cardinal Health owns and operates the largest network of nuclear pharmacies in the United States. In July of 2009, Cardinal Health acquired nuclear pharmacies owned by Biotech in Las Vegas, Nevada, Albuquerque, New Mexico, and El Paso, Texas. As a result of the acquisition, Cardinal Health now holds a monopoly in Albuquerque and has obtained large market shares in Las Vegas and El Paso. If allowed to remain, the transaction would likely allow Cardinal Health to increase prices and reduce service to radiopharmaceutical customers in these three cities and surrounding local areas.

II. RESPONDENT CARDINAL HEALTH

3. Respondent Cardinal Health is a corporation organized, existing and doing business under and by virtue of the laws of the State of Ohio, with its principal executive offices at 7000 Cardinal Place, Dublin, Ohio 43017.

4. Cardinal Health is a \$99 billion health care services company. Cardinal Health is one of the leading suppliers of pharmaceuticals and medical products in the world. Cardinal Health is also a leading manufacturer of medical and surgical products, including gloves, surgical apparel, and fluid

Complaint

management products. In addition, Cardinal Health operates the nation's largest network of nuclear pharmacies.

III. THE ACQUISITION

5. On or about July 31, 2009, Cardinal Health 414, LLC, a wholly owned subsidiary of Cardinal Health, entered into an Asset Purchase Agreement (the "Agreement") with Biotech Pharmacy, Inc., Biotech Pharmacy of Northern Arizona, LLC, Biotech Nuclear, LLC, Biotech Cyclotron, LLC, Southwest Cyclotron, LLC, Biotech Cyclotron of New Mexico, LLC, Biotech Cyclotron of Arizona, LLC, Biotech Cyclotron of Texas, LLC, Leroy Candelaria, Scott Nelson, Mark Friedlander and Dennis Eshima (collectively "Biotech").

6. Pursuant to the Agreement, Cardinal Health acquired certain assets of Biotech, including nuclear pharmacies owned by Biotech in Las Vegas, Nevada, Albuquerque, New Mexico, and El Paso, Texas (the "Acquisition").

IV. JURISDICTION

7. At all times relevant herein, Cardinal Health is, and has been, engaged in "commerce" as defined in Section 1 of the Clayton Act, as amended, 15 U.S.C. § 12, and is, and has been, a "corporation" whose business is in or affects "commerce" as defined in Section 4 of the Federal Trade Commission Act, as amended, 15 U.S.C. § 44.

V. RELEVANT PRODUCT MARKET

8. The relevant product market in which to analyze the effects of the Acquisition is the production, sale, and distribution of single photon emission computed tomography ("SPECT") radiopharmaceuticals (also referred to as "low energy radiopharmaceuticals").

VI. RELEVANT GEOGRAPHIC MARKET

9. The relevant geographic markets in which to analyze the effects of the Acquisition are (i) Albuquerque, New Mexico and

Complaint

surrounding areas (the “Albuquerque market”); (ii) El Paso, Texas and surrounding areas (the “El Paso market”); and (iii) Las Vegas, Nevada and surrounding areas (the “Las Vegas market”).

VII. STRUCTURE OF THE MARKETS

10. Prior to the Acquisition, Cardinal Health and Biotech were the only two providers of low energy radiopharmaceuticals in the Albuquerque market. As a result of the Acquisition, Cardinal Health holds a monopoly in the Albuquerque market.

11. Prior to the Acquisition, Cardinal Health and Biotech were the only two providers of low energy radiopharmaceuticals in the El Paso market. As a result of the Acquisition, Cardinal held a monopoly in the El Paso market, until approximately November of 2010, when Rio Grande Nuclear Pharmacy, LLC, opened in El Paso. Currently, Cardinal Health holds a large market share in the El Paso market.

12. Prior to the Acquisition, there were three providers of low energy radiopharmaceuticals in the Las Vegas market. Cardinal Health and Biotech were the two leading providers, followed by Advanced Isotopes of Las Vegas. As a result of the Acquisition, Cardinal Health obtained and has since held a large market share in the Las Vegas market.

VIII. COMPETITIVE EFFECTS

13. The Acquisition may substantially lessen competition in the relevant markets by, among other things:

- a. Eliminating actual, direct, and substantial competition between Cardinal Health and Biotech;
- b. Reducing the number of significant competitors in each relevant market giving Cardinal Health substantial market power;
- c. Facilitating the ability of Cardinal Health to exercise unilateral market power;

Complaint

- d. Reducing Cardinal Health's incentives to improve service or product quality or to pursue further innovation;
- e. Increasing the likelihood of coordinated interaction among the remaining competitors; and
- f. Allowing Cardinal Health, unconstrained by effective competition, to increase prices.

IX. ENTRY CONDITIONS

14. Entry into the relevant markets would not be timely, likely, or sufficient to prevent or deter the likely anticompetitive effects of the Acquisition. Entrants face significant barriers in capturing sufficient business to replicate the scale and strength of either Cardinal or Biotech prior to the Acquisition.

X. VIOLATIONS CHARGED

15. The Agreement constitutes a violation of Section 5 of the Federal Trade Commission Act, as amended, 15 U.S.C. § 45.

16. The Acquisition may substantially lessen competition or tend to create a monopoly in violation of Section 7 of the Clayton Act, as amended, 15 U.S.C. § 18, and Section 5 of the Federal Trade Commission Act, as amended, 15 U.S.C. § 45.

WHEREFORE, THE PREMISES CONSIDERED, the Federal Trade Commission on this eighteenth day of October, 2011, issues its Complaint against said Respondent.

By the Commission.

Decision and Order

DECISION AND ORDER

The Federal Trade Commission (“Commission”), having initiated an investigation of the acquisition of certain assets of Biotech by Cardinal Health, Inc. (“Cardinal Health”), and Cardinal Health having been furnished thereafter with a copy of a draft Complaint that the Bureau of Competition proposed to present to the Commission for its consideration and which, if issued by the Commission, would charge Cardinal Health with violations of Section 7 of the Clayton Act, as amended, 15 U.S.C. § 18, and Section 5 of the Federal Trade Commission Act, as amended, 15 U.S.C. § 45; and

Cardinal Health, its attorneys, and counsel for the Commission having thereafter executed an Agreement Containing Consent Order (“Consent Agreement”), containing an admission by Cardinal Health of all the jurisdictional facts set forth in the aforesaid draft Complaint, a statement that the signing of said Consent Agreement is for settlement purposes only and does not constitute an admission by Cardinal Health that the law has been violated as alleged in such Complaint, or that the facts as alleged in such Complaint, other than jurisdictional facts, are true, and waivers and other provisions as required by the Commission’s Rules; and

The Commission having thereafter considered the matter and having determined that it had reason to believe that Cardinal Health has violated the said Acts, and that a Complaint should issue stating its charges in that respect, and having accepted the executed Consent Agreement and placed such Consent Agreement on the public record for a period of thirty (30) days for the receipt and consideration of public comments, and having duly considered the comments received from an interested person pursuant to Section 2.34 of its Rules, now in further conformity with the procedure described in Commission Rule 2.34, 16 C.F.R. § 2.34, the Commission hereby issues its Complaint, makes the following jurisdictional findings and issues the following Decision and Order (“Order”):

1. Cardinal Health is a corporation organized, existing and doing business under and by virtue of the laws of

Decision and Order

Ohio with its office and principal place of business located at 7000 Cardinal Health Place, Dublin, OH 43017.

2. The Federal Trade Commission has jurisdiction of the subject matter of this proceeding and of Respondent, and the proceeding is in the public interest.

ORDER**I.**

IT IS ORDERED that, as used in this Order, the following definitions shall apply:

- A. “Cardinal Health” means Cardinal Health, Inc., its directors, officers, employees, agents, representatives, successors, and assigns; and its joint ventures, subsidiaries, divisions, groups, and affiliates controlled by Cardinal Health, Inc., and the respective directors, officers, employees, agents, representatives, successors, and assigns of each.
- B. “Biotech” means the following entities collectively and individually: Biotech Pharmacy, Inc., a New Mexico corporation, Biotech Pharmacy of Northern Arizona, LLC, an Arizona limited liability company; Biotech Nuclear, LLC, a Nevada limited liability company, Biotech Cyclotron LLC, a Nevada limited liability company, Southwest Cyclotron, LLC, a Nevada limited liability company, Biotech Cyclotron of New Mexico, LLC, a New Mexico limited liability company, Biotech Cyclotron of Arizona, LLC, an Arizona limited liability company, and Biotech Cyclotron of Texas, LLC, a Texas limited liability company, and their respective directors, officers, employees, agents, representatives, successors, and assigns; and their respective joint ventures, subsidiaries, divisions, groups, and affiliates.
- C. “Commission” means the Federal Trade Commission.

Decision and Order

- D. “Acquirer” or “Acquirers” means any entity or entities approved by the Commission to acquire one or more of the Reconstituted Pharmacies pursuant to this Order.
- E. “Acquisition” means Cardinal Health’s acquisition of certain Biotech assets relating to Biotech’s Nuclear Pharmacy business, which was consummated on July 31, 2009.
- F. “Biotech Intellectual Property” means the intellectual property related to the Nuclear Pharmacies owned by Biotech prior to the Acquisition and acquired by Cardinal Health pursuant to the Acquisition, including, but not limited to:
1. copyrights, patents, software; trademarks, trade dress, trade secrets, drawings, utility models, designs, design rights, techniques, inventions, practices, recipes, raw material specifications, process descriptions, quality control methods in process, methods and other confidential or proprietary technical, business, development and other information, and all rights in any jurisdiction to limit the use or disclosure thereof;
 2. rights to obtain and file for patents and copyrights and registrations thereof;
 3. rights to sue and recover damages or obtain injunctive relief for infringement, dilution, misappropriation, violation or breach of any of the foregoing; and
 4. the exclusive right to all intellectual property acquired by Cardinal Health from Biotech pursuant to the Acquisition and used by Biotech in the Nuclear Pharmacy business prior to the Acquisition, including, but not limited to, patents, licenses, risk analysis, certificates of analysis, goodwill, trade secrets, marketing information,

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trademarks, trade names, service marks, logos, and the modifications or improvements to such intellectual property.

Provided, however, that Intellectual Property shall not include intellectual property relating solely to the Cyclotron Assets.

- G. “Common Intellectual Property” means the intellectual property related to the Nuclear Pharmacies owned by Biotech prior to the Acquisition and acquired by Cardinal Health pursuant to the Acquisition, including but not limited to know-how, technology, data, technical information, protocols (including, but not limited to, operational manuals and standard operating procedures), and quality control information.
- H. “Biotech Nuclear Pharmacy” means any and all of the Nuclear Pharmacies owned and operated by Biotech as of July 30, 2009, and located at:
- 3940 S. Eastern Avenue, Las Vegas, Nevada 89119
4030 Stockton Hill Road, Suite 8, Kingman, Arizona 86409
116 W. Castellano, El Paso, Texas 79912
4376 Alexander Boulevard, NE, Suite B, Albuquerque, New Mexico 87107
- I. “Branded Heart Perfusion Agent” means Cardiolite or Myoview.
- J. “Closing Date” means the Albuquerque Closing Date, the El Paso Closing Date, or the Las Vegas Closing Date.
- K. “Albuquerque Closing Date” means the date on which Cardinal Health (or a Divestiture Trustee) consummates a transaction to assign, grant, license, divest, transfer, deliver, or otherwise convey a Reconstituted Pharmacy located in Albuquerque, New Mexico to an Acquirer pursuant to this Order.

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- L. “El Paso Closing Date” means the date on which Cardinal Health (or a Divestiture Trustee) consummates a transaction to assign, grant, license, divest, transfer, deliver, or otherwise convey a Reconstituted Pharmacy located in El Paso, Texas to an Acquirer pursuant to this Order.
- M. “Las Vegas Closing Date” means the date on which Cardinal Health (or a Divestiture Trustee) consummates a transaction to assign, grant, license, divest, transfer, deliver, or otherwise convey a Reconstituted Pharmacy located in Las Vegas, Nevada, to an Acquirer pursuant to this Order.
- N. “Customer” means any third party that, at any time between July 1, 2009 and the relevant Closing Date, purchased Radiopharmaceuticals from any of the Former Cardinal Nuclear Pharmacies or the Biotech Nuclear Pharmacies located in Las Vegas, Nevada, El Paso, Texas, and Albuquerque, New Mexico acquired by Cardinal Health in the Acquisition.
- O. “Customer Contract” means any contract between Cardinal Health and any Customer for the preparation, dispensing and distribution of Radiopharmaceuticals, including, but not limited to, contracts with the Customers identified in Confidential Exhibit A to this Order.
- Provided, however,* Customer Contract shall not include any contract solely for the preparation, dispensing and distribution of High-energy Radiopharmaceuticals or where the Customer has committed to purchase only High-energy Radiopharmaceuticals.
- P. “Existing Customer Contract” means the Customer Contract in effect on the date that Cardinal Health notifies the relevant Customer of its contract

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termination rights pursuant to Paragraph IV of this Order.

- Q. “Cyclotron Assets” means the equipment and other assets associated with the manufacture of High-energy Radiopharmaceuticals.
- R. “Designated Employee” means the employee or person employed by Biotech at any Biotech Nuclear Pharmacy or by Cardinal at any of the Former Cardinal Health Nuclear Pharmacies at the time of the Acquisition.
- Provided, however,* “Designated Employee” does not include the persons identified in Confidential Exhibit B.
- S. “Albuquerque Divestiture Agreement” means the agreement between Cardinal Health and the Acquirer of the Reconstituted Nuclear Pharmacy located in Albuquerque, New Mexico.
- T. “El Paso Divestiture Agreement” means the agreement between Cardinal Health and the Acquirer of the Reconstituted Nuclear Pharmacy located in El Paso, Texas.
- U. “Las Vegas Divestiture Agreement” means the agreement between Cardinal Health and the Acquirer of the Reconstituted Nuclear Pharmacy located in Las Vegas, Nevada.
- V. “Divestiture Trustee(s)” means any person or entity appointed pursuant to Paragraph VIII of this Order to act as a trustee in this matter.
- W. “Former Cardinal Health Nuclear Pharmacies” means the Nuclear Pharmacies owned and operated by Cardinal Health as of July 30, 2009, at the following locations:

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61 Spectrum Boulevard, Las Vegas, Nevada 89119;
1020 Tijeras N.E., Suite 1, Albuquerque, New Mexico
87107;
1810 Murchison Road, #205, El Paso, Texas 79902.

- X. “Generic Heart Perfusion Agent” means Sestamibi.
- Y. “High-energy Radiopharmaceuticals” means any positron emission tomography (PET) Radiopharmaceutical.
- Z. “Low-energy Radiopharmaceuticals” means any non-PET Radiopharmaceutical, which is or can be used in diagnostic nuclear medicine studies, diagnostic nuclear medicine imaging or therapeutic nuclear medicine treatments.
- AA. “Monitor” means the person appointed pursuant to Paragraph VII of this Order.
- BB. “Nuclear Pharmacy” means a pharmacy dedicated to the preparation, dispensing, and distribution of Radiopharmaceuticals. *Provided, however*, “Nuclear Pharmacy” shall not include Cyclotron Assets.
- CC. “Person” means any individual, partnership, joint venture, firm, corporation, association, trust, unincorporated organization, joint venture, or other business or governmental entity, and any subsidiaries, divisions, groups or affiliates thereof.
- DD. “Radiopharmaceutical” means a drug containing a radioactive isotope which can be used in diagnostic nuclear medicine studies, diagnostic nuclear medicine imaging, therapeutic nuclear medicine treatments, or diagnostic molecular imaging.
- EE. “Reconstituted Pharmacies” means the Former Cardinal Health Nuclear Pharmacies as reconstituted pursuant to Paragraph II.A.1. of this Order.

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- FF. “Relevant Areas” means the area within a 200 mile radius of each of the Biotech Nuclear Pharmacies.
- GG. “Tech-99” means technetium-99m.
- HH. “Third Party Consents” means all consents from any person other than Cardinal Health, including all landlords, that are necessary to effect the complete transfer of the Reconstituted Pharmacies to an Acquirer.

II.**IT IS FURTHER ORDERED** that:

- A. Within six (6) months of the date on which this Order is accepted for public comment, Cardinal Health shall:
1. Reconstitute, in conjunction with each proposed Acquirer, each of the Former Cardinal Health Nuclear Pharmacies. Such reconstitution shall result in the creation of separate, stand-alone Nuclear Pharmacies, similar to the Former Cardinal Health Nuclear Pharmacies before the Acquisition, and each fully engaged in all aspects of the Nuclear Pharmacy business and compliant with USP 797 regulation developed by U.S. Pharmacopeia. Such reconstitution may include, but is not limited to, returning or replacing all equipment, supplies, fixtures, and furnishings.
 2. Divest the Reconstituted Pharmacies and the Biotech Intellectual Property, absolutely and in good faith, at no minimum price, to an Acquirer or Acquirers each of whom receives the prior approval of the Commission and in a manner that receives the prior approval of the Commission.

Provided, however, that Cardinal Health may retain a fully paid-up, irrevocable, royalty-free license to the Common Intellectual Property;

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Provided further, however, that Cardinal shall demonstrate that the Acquirer of each Reconstituted Pharmacy shall have a contract for the supply of Tech-99, independent of Cardinal Health, with a capability to obtain a volume of Tech-99 similar to the volume of Tech-99 previously provided to the Biotech Nuclear Pharmacies before the Acquisition;

Provided further, however, that Cardinal shall demonstrate that the Acquirer of each Reconstituted Pharmacy shall have distribution rights with respect to both a Branded Heart Perfusion Agent and a Generic Heart Perfusion Agent, for, at a minimum, the area previously serviced by the corresponding Biotech Nuclear Pharmacy before the Acquisition.

- B. Cardinal Health shall not prevent, restrict, limit, or interfere in any way with the ability of an Acquirer to procure or distribute any Radiopharmaceutical product or Radiopharmaceutical input, including, but not limited to, Branded Heart Perfusion Agents and Generic Heart Perfusion Agents.
- C. Before the Closing Date for each Reconstituted Pharmacy, Cardinal Health shall:
 - 1. obtain or maintain all regulatory approvals, licenses, qualifications, permits or clearances that are capable of being transferred to the Acquirer and necessary for any aspect of the operations of such Reconstituted Pharmacy, to the extent allowed by law; and
 - 2. transfer such approvals, licenses, permits or clearances to each Acquirer, to the extent they can be transferred.
- D. The purposes of this Paragraph II of the Order are:

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1. to ensure that Cardinal Health, in conjunction with the proposed Acquirer or Acquirers, reconstitutes the Former Cardinal Health Nuclear Pharmacies in Las Vegas, Nevada; Albuquerque, New Mexico; and El Paso, Texas resulting in the creation of separate, stand-alone Nuclear Pharmacies, and each fully engaged in all aspects of the Nuclear Pharmacy business;
2. to ensure that each Acquirer of the Reconstituted Pharmacies has the intention and ability to prepare and distribute Radiopharmaceuticals for use in nuclear medicine procedures, at facilities independent of Cardinal Health, similar to Cardinal Health's independent preparation and distribution of Radiopharmaceuticals prior to Cardinal Health's acquisition of Biotech, including having a Tech-99 supply agreement and distribution agreements with respect to a Branded Heart Perfusion Agent and a Generic Heart Perfusion Agent that could be used to supply customers of the Reconstituted Pharmacy;
3. to allow each Acquirer to operate the Reconstituted Pharmacies with the certifications and approvals necessary for the preparation, distribution, and pharmacology of Radiopharmaceuticals; and
4. to remedy the lessening of competition resulting from the Acquisition as alleged in the Commission's Complaint.

III.**IT IS FURTHER ORDERED** that:

- A. Cardinal Health shall take no action to prevent, restrict, limit, or interfere in any way with the ability of each Acquirer to contract with any group purchasing organization.

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Provided, however, Cardinal Health shall not be required to terminate, amend or waive any contracts entered into with group purchasing organizations unless Cardinal Health is otherwise required to terminate, amend, or waive such contracts, or portions thereof, pursuant to Paragraph IV of this Order.

- B. Cardinal Health shall, as part of the Divestiture Agreement for the Reconstituted Pharmacies in Las Vegas, NV and Albuquerque, NM, and at the Acquirer's option for those Reconstituted Pharmacies, enter into an agreement to supply F-18 fluorodeoxyglucose and other cyclotron-produced radioisotopes from Cardinal Health to the Acquirer for a period of one (1) year after the Closing Date on price terms similar to those in the contracts through which Biotech agreed to provide such radioisotopes to Cardinal Health prior to the Acquisition.

IV.**IT IS FURTHER ORDERED** that:

- A. Cardinal Health shall, within five (5) days after each Closing Date, notify each relevant Customer of its right to terminate its Existing Customer Contract with Cardinal Health.
- B. Cardinal Health shall terminate the Existing Customer Contract within thirty (30) days of receiving a Customer's request to terminate. The Customer's right to terminate such Existing Customer Contract shall be without penalty or charge, and immediately upon request of the Customer, and shall continue for twenty-four (24) months from the relevant Closing Date. Such notification shall include notification of the existence of the relevant Reconstituted Pharmacy and be in the form of the notification attached as Exhibit C to this Order.

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Provided, however, that, if after receiving such notification, the Existing Customer Contract is extended, renewed, or materially modified by mutual agreement between Cardinal Health and the Customer, including, but not limited to, modifications regarding the price or duration terms of such Existing Customer Contract, Cardinal Health shall not be required to terminate the Existing Customer Contract pursuant to this Paragraph;

Provided further however, that Cardinal Health shall include in any such extension, renewal, or material modification to such Existing Customer Contract a specific and prominent acknowledgment that if the Customer executes the extension, renewal, or material modification, Cardinal Health will not be required to terminate the Existing Customer Contract pursuant to this Paragraph.

V.

IT IS FURTHER ORDERED that:

- A. Each Divestiture Agreement, if approved by the Commission, shall be incorporated by reference into this Order and made a part hereof. Further, nothing in any Divestiture Agreement shall limit or contradict, or be construed to limit or contradict, the terms of this Order, it being understood that nothing in this Order shall be construed to reduce any rights or benefits of an Acquirer or to reduce any obligations of Cardinal Health under a Divestiture Agreement. Cardinal Health shall comply with the terms of each Divestiture Agreement, and a breach by Cardinal Health of any term of a Divestiture Agreement shall constitute a violation of this Order. To the extent that any term of a Divestiture Agreement conflicts with a term of this Order such that Cardinal Health cannot fully comply with both, Cardinal Health shall comply with the term of this Order; and
- B. Cardinal Health shall include in each Divestiture Agreement a specific reference to this Order, the

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remedial purposes thereof, and provisions to reflect the full scope and breadth of Cardinal Health's obligations to the Acquirer pursuant to this Order.

VI.**IT IS FURTHER ORDERED** that:

- A. Beginning from the Closing Date for each Reconstituted Pharmacy until ninety (90) days after such Closing Date, Cardinal Health shall:
1. facilitate employment interviews between each Designated Employee and the Acquirer of each Reconstituted Pharmacy, including providing the names and contact information for such employees and allowing such employees reasonable opportunity to interview with the relevant Acquirer, and shall not discourage such employee from participating in such interviews;
 2. not interfere in employment negotiations between each Designated Employee and the relevant Acquirer;
 3. with respect to each Designated Employee who receives an offer of employment from the relevant Acquirer:
 - a. not prevent, prohibit, or restrict, or threaten to prevent, prohibit, or restrict the Designated Employee from being employed by the relevant Acquirer, and shall not offer any incentive to the Designated Employee to decline employment with the relevant Acquirer;
 - b. cooperate with the relevant Acquirer in effecting transfer of the Designated Employee to the employ of the relevant Acquirer, if the Designated Employee accepts an offer of employment from the relevant Acquirer;

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- c. eliminate any contractual provisions or other restrictions entered into or imposed by Cardinal Health (such as noncompetition agreements) that would otherwise prevent the Designated Employee from being employed by the relevant Acquirer;
 - d. eliminate any confidentiality restrictions that would prevent the Designated Employee who accepts employment with the Acquirer from using or transferring to the relevant Acquirer any information relating to the operation of the relevant Reconstituted Pharmacy; and
 - e. unless alternative arrangements are agreed upon with the relevant Acquirer, retain the obligation for the benefit of any Designated Employee who accepts employment with the relevant Acquirer, to pay all vested bonuses, vested pensions, and other vested benefits.
- B. Cardinal Health shall not, for a period of two (2) years following each relevant Closing Date, directly or indirectly, solicit, induce, or attempt to solicit or induce any Person employed by the relevant Acquirer at the relevant Reconstituted Pharmacy to terminate his or her employment relationship with such Acquirer, unless that employment relationship has already been terminated by such Acquirer;

Provided, however, that Cardinal Health may make general advertisements for employees including, but not limited to, in newspapers, trade publications, websites, or other media not targeted specifically at the relevant Acquirer's employees;

Provided further, however, Cardinal Health may hire Designated Employees who apply for employment with Cardinal Health as long as such employees were not solicited by Cardinal Health in violation of this Paragraph.

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VII.**IT IS FURTHER ORDERED** that:

- A. Katherine L. Seifert of Seifert and Associates, Inc. shall serve as the Monitor pursuant to the agreement executed by the Monitor and Cardinal Health and attached as Exhibits D (“Monitor Agreement”) and Confidential Exhibit D-1 (Monitor compensation). The Monitor is appointed to assure that Cardinal Health expeditiously complies with all of its obligations and performs all of its responsibilities as required by this Order.
- B. The Monitor Agreement shall require that, no later than one (1) day after this Order is accepted for public comment, Cardinal Health transfers to the Monitor all rights, powers, and authorities necessary to permit the Monitor to perform her duties and responsibilities, pursuant to and consistent with, the purposes of the Order.
- C. No later than one (1) day after this Order is accepted for public comment, Cardinal Health shall, pursuant to the Monitor Agreement, transfer to the Monitor all rights, powers, and authorities necessary to permit the Monitor to perform her duties and responsibilities, pursuant to and consistent with, the purposes of the Order.
- D. Cardinal Health shall consent to the following terms and conditions regarding the powers, duties, authorities, and responsibilities of the Monitor:
 - 1. The Monitor shall have the power and authority to monitor Cardinal Health’s compliance with the terms of the Order, and shall exercise such power and authority and carry out the duties and responsibilities of the Monitor in a manner consistent with the purposes of the Order and in

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consultation with the Commission including, but not limited to:

- a. Assuring that Cardinal Health expeditiously complies with all of its obligations and performs all of its responsibilities as required by this Order; and
 - b. Monitoring any agreements between Cardinal Health and the Acquirer.
2. The Monitor shall act in a fiduciary capacity for the benefit of the Commission.
 3. Subject to any demonstrated legally recognized privilege, the Monitor shall have full and complete access to Cardinal Health's personnel, books, documents, records kept in the normal course of business, facilities and technical information, and such other relevant information as the Monitor may reasonably request, related to Cardinal Health's compliance with its obligations under the Order. Cardinal Health shall cooperate with any reasonable request of the Monitor and shall take no action to interfere with or impede the Monitor's ability to monitor Cardinal Health's compliance with the Order.
 4. The Monitor shall serve, without bond or other security, at the expense of Cardinal Health on such reasonable and customary terms and conditions as the Commission may set. The Monitor shall have authority to employ, at the expense of Cardinal Health, such consultants, accountants, attorneys and other representatives and assistants as are reasonably necessary to carry out the Monitor's duties and responsibilities. The Monitor shall account for all expenses incurred, including fees for services rendered, subject to the approval of the Commission.

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5. Cardinal Health shall indemnify the Monitor and hold the Monitor harmless against any losses, claims, damages, liabilities, or expenses arising out of, or in connection with, the performance of the Monitor's duties, including all reasonable fees of counsel and other reasonable expenses incurred in connection with the preparations for, or defense of, any claim, whether or not resulting in any liability, except to the extent that such losses, claims, damages, liabilities, or expenses result from gross negligence, malfeasance, willful or wanton acts, or bad faith by the Monitor.
 6. The Monitor Agreement shall provide that within one (1) month from the date the Monitor is appointed pursuant to this paragraph, and every sixty (60) days thereafter, the Monitor shall report in writing to the Commission concerning performance by Cardinal Health of its obligations under the Order.
 7. Cardinal Health may require the Monitor and each of the Monitor's consultants, accountants, attorneys, and other representatives and assistants to sign a customary confidentiality agreement; *provided, however*, such agreement shall not restrict the Monitor from providing any information to the Commission.
- E. The Commission may, among other things, require the Monitor and each of the Monitor's consultants, accountants, attorneys, and other representatives and assistants to sign an appropriate confidentiality agreement relating to Commission materials and information received in connection with the performance of the Monitor's duties.
- F. If the Commission determines that the Monitor has ceased to act or failed to act diligently, the Commission may appoint a substitute Monitor:

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1. The Commission shall select the substitute Monitor, subject to the consent of Cardinal Health, which consent shall not be unreasonably withheld. If Cardinal Health has not opposed, in writing, including the reasons for opposing, the selection of a proposed Monitor within ten (10) days after notice by the staff of the Commission to Cardinal Health of the identity of any proposed Monitor, Cardinal Health shall be deemed to have consented to the selection of the proposed Monitor.
 2. Not later than ten (10) days after appointment of the substitute Monitor, Cardinal Health shall execute an agreement that, subject to the prior approval of the Commission, confers on the Monitor all the rights and powers necessary to permit the Monitor to monitor Cardinal Health's compliance with the relevant terms of the Order in a manner consistent with the purposes of the Order.
- G. The Commission may on its own initiative, or at the request of the Monitor, issue such additional orders or directions as may be necessary or appropriate to assure compliance with the requirements of the Order.
- H. A Monitor appointed pursuant to this Order may be the same person appointed as the Divestiture Trustee pursuant to the relevant provisions of this Order.

VIII.**IT IS FURTHER ORDERED** that:

- A. If Cardinal Health has not fully complied with the obligations as required by Paragraphs II.A, II.B and II.C of this Order, the Commission may appoint a Divestiture Trustee to reconstitute the Former Cardinal Health Nuclear Pharmacies and divest the Reconstituted Pharmacies and enter into other agreements, assignments, and licenses, in a manner that satisfies the requirements of this Order.

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- B. In the event that the Commission or the Attorney General brings an action pursuant to § 5(l) of the Federal Trade Commission Act, 15 U.S.C. § 45(l), or any other statute enforced by the Commission, Cardinal Health shall consent to the appointment of a Divestiture Trustee in such action to effectuate the divestitures and other obligations as described in Paragraphs II.A, II.B and II.C. Neither the appointment of a Divestiture Trustee nor a decision not to appoint a Divestiture Trustee under this Paragraph VIII shall preclude the Commission or the Attorney General from seeking civil penalties or any other relief available to it, including a court-appointed Divestiture Trustee, pursuant to § 5(l) of the Federal Trade Commission Act, or any other statute enforced by the Commission, for any failure by Cardinal Health to comply with this Order.
- C. The Commission shall select the Divestiture Trustee, subject to the consent of Cardinal Health, which consent shall not be unreasonably withheld. The Divestiture Trustee shall be a person with experience and expertise in acquisitions and divestitures. If Cardinal Health has not opposed, in writing, including the reasons for opposing, the selection of any proposed Divestiture Trustee within ten (10) days after notice by the staff of the Commission to Cardinal Health of the identity of any proposed Divestiture Trustee, Cardinal Health shall be deemed to have consented to the selection of the proposed Divestiture Trustee.
- D. Not later than ten (10) days after the appointment of a Divestiture Trustee, Cardinal Health shall execute a trust agreement that, subject to the prior approval of the Commission, transfers to the Divestiture Trustee all rights and powers necessary to permit the Divestiture Trustee to effect the divestitures required by this Order.

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- E. If a Divestiture Trustee is appointed by the Commission or a court pursuant to this Paragraph VIII, Cardinal Health shall consent to the following terms and conditions regarding the Divestiture Trustee's powers, duties, authority, and responsibilities:
1. Subject to the prior approval of the Commission, the Divestiture Trustee shall have the exclusive power and authority to reconstitute the Former Cardinal Health Nuclear Pharmacies and divest the Reconstituted Pharmacies and enter into all agreements, licenses and assignments as described in Paragraphs II, III, and VI of this Order.
 2. The Divestiture Trustee shall have one (1) year after the date the Commission approves the trust agreement described herein to reconstitute the Former Cardinal Health Nuclear Pharmacies, and to divest the Reconstituted Pharmacies and enter into all agreements, licenses and assignments as described in Paragraphs II, III, and VI of this Order, absolutely and in good faith, at no minimum price, to one or more acquirers that receives the prior approval of the Commission and in a manner that receives the prior approval of the Commission.
If, however, at the end of the one (1) year period, the Divestiture Trustee has submitted a plan of divestiture or believes that the divestiture can be achieved within a reasonable time, the divestiture period or periods may be extended by the Commission; *provided, however*, the Commission may extend the divestiture period only two (2) times.
 3. Subject to any demonstrated legally recognized privilege, the Divestiture Trustee shall have full and complete access to the personnel, books, records and facilities related to the relevant assets that are required to be divested by this Order and to any other relevant information, as the Divestiture Trustee may request. Cardinal Health shall

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develop such financial or other information as the Divestiture Trustee may request and shall cooperate with the Divestiture Trustee. Cardinal Health shall take no action to interfere with or impede the Divestiture Trustee's accomplishment of the divestiture. Any delays in divestiture caused by Cardinal Health shall extend the time for divestiture under this Paragraph VIII in an amount equal to the delay, as determined by the Commission.

4. The Divestiture Trustee shall use best efforts to negotiate the most favorable price and terms available in each contract that is submitted to the Commission, subject to Cardinal Health's absolute and unconditional obligation to divest expeditiously and at no minimum price. The divestiture shall be made in the manner and to an acquirer as required by this Order;

Provided, however, if the Divestiture Trustee receives bona fide offers from more than one acquiring entity for assets and businesses to be divested pursuant to Paragraph II, and if the Commission determines to approve more than one such acquiring entity, the Divestiture Trustee shall divest to the acquiring entity selected by Cardinal Health from among those approved by the Commission;

Provided further, however, that Cardinal Health shall select such entity within five (5) days after receiving notification of the Commission's approval.

5. The Divestiture Trustee shall serve, without bond or other security, at the cost and expense of Cardinal Health, on such reasonable and customary terms and conditions as the Commission or a court may set. The Divestiture Trustee shall have the authority to employ, at the cost and expense of

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Cardinal Health, such consultants, accountants, attorneys, investment bankers, business brokers, appraisers, and other representatives and assistants as are necessary to carry out the Divestiture Trustee's duties and responsibilities. The Divestiture Trustee shall account for all monies derived from the divestiture and all expenses incurred. After approval by the Commission of the account of the Divestiture Trustee, including fees for the Divestiture Trustee's services, all remaining monies shall be paid at the direction of the Cardinal Health, and the Divestiture Trustee's power shall be terminated. The compensation of the Divestiture Trustee shall be based at least in significant part on a commission arrangement contingent on the divestiture of all of the relevant assets that are required to be divested by this Order.

6. Cardinal Health shall indemnify the Divestiture Trustee and hold the Divestiture Trustee harmless against any losses, claims, damages, liabilities, or expenses arising out of, or in connection with, the performance of the Divestiture Trustee's duties, including all reasonable fees of counsel and other expenses incurred in connection with the preparation for, or defense of, any claim, whether or not resulting in any liability, except to the extent that such losses, claims, damages, liabilities, or expenses result from gross negligence, malfeasance, willful or wanton acts, or bad faith by the Divestiture Trustee.
7. The Divestiture Trustee shall have no obligation or authority to operate or maintain the relevant assets required to be divested by this Order.
8. The Divestiture Trustee shall act in a fiduciary capacity for the benefit of the Commission.

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9. The Divestiture Trustee shall report in writing to Cardinal Health and to the Commission every sixty (60) days concerning the Divestiture Trustee's efforts to accomplish the divestiture.
 10. Cardinal Health may require the Divestiture Trustee and each of the Divestiture Trustee's consultants, accountants, attorneys and other representatives and assistants to sign a customary confidentiality agreement; *provided, however*, such agreement shall not restrict the Divestiture Trustee from providing any information to the Commission.
 11. The Commission may, among other things, require the Divestiture Trustee and each of the Divestiture Trustee's consultants, accountants, attorneys, and other representatives and assistants to sign an appropriate confidentiality agreement relating to Commission materials and information received in connection with the performance of the Divestiture Trustee's duties.
- F. If the Commission determines that a Divestiture Trustee has ceased to act or failed to act diligently, the Commission may appoint a substitute Divestiture Trustee in the same manner as provided in this Paragraph VIII.
- G. The Commission or, in the case of a court-appointed Divestiture Trustee, the court, may on its own initiative or at the request of the Divestiture Trustee issue such additional orders or directions as may be necessary or appropriate to accomplish the obligations under Paragraphs II, III, IV, and VI of this Order.
- H. The Divestiture Trustee(s) appointed pursuant to Paragraph VIII of this Order may be the same Person appointed as the Monitor pursuant to Paragraph VII of this Order.

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IX.

IT IS FURTHER ORDERED that for a period of ten (10) years from the date this Order becomes final:

- A. Cardinal Health shall not, without providing advance written notice to the Commission, acquire, directly or indirectly, any assets divested pursuant to this Order. Said notification shall be given to the Secretary of the Federal Trade Commission.

- B. Cardinal Health shall not, without providing advance written notification to the Commission in the manner described in this Paragraph IX directly or indirectly, acquire:
 - 1. any stock, share capital, equity, or other interest in any Person, corporate or non corporate, that owns, operates, manages, or owns an interest in Nuclear Pharmacies in the Relevant Areas; or
 - 2. any assets used, at the time of the Acquisition, in the operation or business of Nuclear Pharmacies in the Relevant Areas.

Said notification shall be given to the Secretary of the Federal Trade Commission and shall include, at a minimum, the following information: (i) the name and address of the acquired entity or, in the case of an asset acquisition the name and address of the entity from which assets are being acquired; (ii) a description of the transaction, including the purchase price; and (iii) identification of the assets being acquired, including their physical location.

Provided, however, that prior notification shall not be required by this paragraph for a transaction for which Notification is required to be made, and has been made, pursuant to Section 7A of the Clayton Act, 15 U.S.C. § 18a.

Provided, further, however, that prior notification shall not be required by this Paragraph IX for an acquisition, if Cardinal Health acquires not more than one percent of the outstanding

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securities or other equity interest in an entity described in this Paragraph IX.

X.**IT IS FURTHER ORDERED** that:

- A. Within thirty (30) days after the date this Order is accepted for public comment, and every sixty (60) days thereafter until Cardinal Health has fully complied with Paragraphs II.A, II.B, II.C, IV.A and VI.A of this Order, Cardinal Health shall submit to the Commission a verified written report setting forth in detail the manner and form in which it intends to comply, is complying, and has complied with this Order. Cardinal Health shall submit at the same time a copy of its report concerning compliance with this Order to the Monitor or Divestiture Trustee, if any Divestiture Trustee has been appointed pursuant to this Order. Cardinal Health shall include in its report, among other things that are required from time to time, a full description of the efforts being made to comply with the relevant Paragraphs of the Order, including a description of all substantive contacts or negotiations related to the divestiture of the relevant assets and the identity of all parties contacted. Cardinal Health shall include in its report copies of all written communications to and from such parties, all internal memoranda, and all reports and recommendations concerning completing the obligations.

- B. Beginning twelve (12) months after the date this Order becomes final, and annually thereafter on the anniversary of the date this Order becomes final, for the next nine (9) years, Cardinal Health shall submit to the Commission a verified written report setting forth in detail the manner and form in which it has complied, is complying, and will comply with this Order. Cardinal Health shall include in its compliance reports, among other things that are required from time to time, a full description of the

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efforts being made to comply with the Order and copies of all written communications to and from all persons relating to this Order. Additionally, Cardinal Health shall include in its compliance report whether or not it made any notifiable acquisitions pursuant to Paragraph IX. Cardinal Health shall include a description of such acquisitions including, but not limited to, the identity of the Person or assets acquired, the location of the Person or assets, and a detailed description of the assets or Person and its Nuclear Pharmacy operations.

XI.

IT IS FURTHER ORDERED that Cardinal Health shall notify the Commission at least thirty (30) days prior to any proposed:

- A. dissolution of Cardinal Health;
- B. acquisition, merger or consolidation of Cardinal Health; or
- C. other change in Cardinal Health, including, but not limited to, assignment and the creation or dissolution of subsidiaries, if such change might affect compliance obligations arising out of this Order.

XII.

IT IS FURTHER ORDERED that, for purposes of determining or securing compliance with this Order, and subject to any legally recognized privilege, and upon written request and upon five (5) days notice to Cardinal Health, Cardinal Health shall, without restraint or interference, permit any duly authorized representative(s) of the Commission:

- A. access, during business office hours of Cardinal Health and in the presence of counsel, to all facilities and access to inspect and copy all books, ledgers, accounts, correspondence, memoranda and all other records and

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documents in the possession or under the control of Cardinal Health related to compliance with this Order, which copying services shall be provided by Cardinal Health at its expense; and

- B. to interview officers, directors, or employees of Cardinal Health, who may have counsel present, regarding such matters.

XIII.

IT IS FURTHER ORDERED that this Order shall terminate on October 18, 2021.

By the Commission.

CONFIDENTIAL EXHIBIT A

**[Incorporated By Reference, But Redacted From the Public
Record Version]**

Decision and Order

CONFIDENTIAL EXHIBIT B

**[Incorporated By Reference, But Redacted From the Public
Record Version]**

Analysis to Aid Public Comment

**ANALYSIS OF CONSENT ORDER TO AID PUBLIC
COMMENT****I. Introduction**

The Federal Trade Commission (“Commission”) has accepted, subject to final approval, an Agreement Containing Consent Order (“Consent Agreement”) from Cardinal Health, Inc. (“Cardinal”) to remedy the anticompetitive effects stemming from Cardinal’s acquisition of Biotech’s nuclear pharmacies in the Southwestern United States. Under the terms of the Consent Agreement, Cardinal is required to reconstitute and divest to one or more Commission-approved acquirers, Cardinal’s former nuclear pharmacies in Las Vegas, Nevada, Albuquerque, New Mexico, and El Paso, Texas, and to take certain additional measures to restore competition in nuclear pharmacy markets in Las Vegas, Albuquerque, and El Paso.

On July 31, 2009, Cardinal acquired Biotech’s nuclear pharmacies in Las Vegas, Albuquerque, and El Paso (the “Acquisition”) pursuant to an Asset Purchase Agreement (“Agreement”). Prior to the Acquisition, both Cardinal and Biotech operated nuclear pharmacies in these cities. These nuclear pharmacies produced, distributed, and sold single photon emission computed tomography (“SPECT”) radiopharmaceuticals (also referred to as “low energy radiopharmaceuticals”) to hospitals and cardiology clinics. The Commission’s complaint alleges that the Acquisition and the Agreement violated Section 7 of the Clayton Act, as amended, 15 U.S.C. § 18, and Section 5 of the Federal Trade Commission Act, as amended, 15 U.S.C. § 45, because the Acquisition and Agreement may substantially lessen competition or tend to create a monopoly in the production, sale, and distribution of low energy radiopharmaceuticals in Las Vegas, Albuquerque, and El Paso and surrounding local areas.

The Consent Agreement has been placed on the public record for 30 days for receipt of comments by interested persons. Comments received during this period will become part of the public record. After 30 days, the Commission will review the Consent Agreement and comments received and decide whether to withdraw the proposed Consent Agreement, modify it, or make

Analysis to Aid Public Comment

final the Consent Agreement's proposed Decision and Order ("Order").

II. Respondent Cardinal Health, Inc.

Cardinal is a corporation organized, existing, and doing business under and by virtue of the laws of the State of Ohio, with its principal executive offices at 7000 Cardinal Place, Dublin, Ohio 43017. Cardinal, a \$99 billion health care services company, is one of the leading suppliers of pharmaceuticals and medical products in the world. Cardinal is also a leading manufacturer of medical and surgical products, including gloves, surgical apparel, and fluid management products. In addition, Cardinal operates the nation's largest network of nuclear pharmacies.

III. The Products and Structure of the Markets

Nuclear pharmacies provide radiopharmaceuticals to local hospitals and cardiology clinics, which use the products to diagnose and treat various diseases. Radiopharmaceuticals are drugs containing a radioactive isotope combined with a chemical compound. Due to the fact that the radioactive isotopes have short half-lives and decay rapidly, a nuclear pharmacy can only serve its local area. Accordingly, competition between nuclear pharmacies occurs at the local level.

The Commission's complaint alleges that the relevant product market in which to assess the effects of the Acquisition is the production, sale, and distribution of SPECT radiopharmaceuticals or low energy radiopharmaceuticals. The Commission's complaint further alleges that the relevant geographic markets in which to analyze the effects of the Acquisition are (i) Albuquerque, New Mexico and surrounding areas (the "Albuquerque market"); (ii) El Paso, Texas and surrounding areas (the "El Paso market"); and (iii) Las Vegas, Nevada and surrounding areas (the "Las Vegas market").

The Commission's complaint alleges that Cardinal and Biotech were the only two providers of low energy radiopharmaceuticals prior to the Acquisition in the Albuquerque

Analysis to Aid Public Comment

market. As a result of the Acquisition, Cardinal holds a monopoly in the Albuquerque market. With respect to the El Paso market, the Commission's complaint alleges that Cardinal and Biotech were the only two providers of low energy pharmaceuticals prior to the Acquisition. As a result of the Acquisition, Cardinal held a monopoly in the El Paso market, until approximately November of 2010, when Rio Grande Nuclear Pharmacy, LLC opened in El Paso. Currently, Cardinal holds a large market share in the El Paso market. Finally, regarding the Las Vegas market, the Complaint alleges that prior to the Acquisition, there were three providers of low energy radiopharmaceuticals in the market. Cardinal and Biotech were the two leading providers, followed by Advanced Isotopes of Las Vegas. As a result of the Acquisition, Cardinal obtained and has since held a large market share in the Las Vegas market.

IV. Effects of the Acquisition

The Commission's complaint charges that the Acquisition may substantially lessen competition in the Las Vegas, Albuquerque, and El Paso markets for the production, sale, and distribution of low energy radiopharmaceuticals, by, among other things, (i) eliminating the direct and substantial competition between Cardinal and Biotech; (ii) reducing the number of significant competitors in each relevant market giving Cardinal substantial market power; (iii) facilitating the ability of Cardinal to unilaterally exercise market power; (iv) reducing Cardinal's incentives to improve service or product quality or pursue further innovation; (v) increasing the likelihood of coordinated interaction among the remaining competitors; and (vi) allowing Cardinal, unconstrained by effective competition, to increase prices.

Analysis to Aid Public Comment

V. Entry

The Commission's complaint alleges that entry into the relevant markets would not be timely, likely, or sufficient to prevent or deter the likely anticompetitive effects of the Acquisition. The Commission's complaint further alleges that entrants face significant barriers in capturing sufficient business to replicate the scale and strength of either Cardinal or Biotech prior to the Acquisition.

VI. Terms of the Order

The Consent Agreement is designed to remedy the likely anticompetitive effects of the Acquisition by restoring, to the extent possible, the lost competition between Cardinal and Biotech in Las Vegas, Albuquerque, and El Paso. Specific terms of the Order are discussed further below.

A. Reconstitution and Divestiture of the Former Cardinal Nuclear Pharmacies to One or More Commission-Approved Acquirers

Prior to the Acquisition, both Cardinal and Biotech operated nuclear pharmacies in Las Vegas, El Paso, and Albuquerque. After the Acquisition, Cardinal relocated its nuclear pharmacy business in these cities to the former Biotech nuclear pharmacy locations and closed its Cardinal facilities. The Order requires that within six months of the date on which the Order is accepted for public comment, Cardinal must reconstitute each of the three former Cardinal nuclear pharmacies and divest each of the pharmacies to a Commission-approved acquirer.

In connection with the divestiture of the three nuclear pharmacies, Cardinal is also required to divest to each acquirer the intellectual property related to the nuclear pharmacies owned by Biotech prior to the Acquisition. Cardinal must also obtain, maintain, and transfer to the acquirer(s) all regulatory approvals, licenses, qualifications, permits, or clearances that are necessary to operate a nuclear pharmacy. Finally, although, as stated above, the Commission must approve each acquirer, the Order specifically requires that Cardinal demonstrate that each acquirer

Analysis to Aid Public Comment

has a supply of the two vital low energy radiopharmaceutical inputs, the radioisotope technetium 99 and a heart perfusion agent.

B. Customer Rights to Terminate Contracts with Cardinal

To ensure that the acquirer(s) have the opportunity to compete for sufficient business to obtain viable scale and restore competition, the Order requires that Cardinal grant each of its customers in Las Vegas, Albuquerque, and El Paso the right to terminate, without penalty or charge, its existing contract with Cardinal for the purchase of radiopharmaceuticals. Specifically, any customer that purchased radiopharmaceuticals from either Cardinal's or Biotech's nuclear pharmacy in Las Vegas, Albuquerque, or El Paso, at any time between July 1, 2009 (30 days prior to the Acquisition) and the relevant closing date (*i.e.*, the day on which Cardinal divests the reconstituted pharmacy in the customer's market), has the right to terminate its existing contract for radiopharmaceuticals with Cardinal. However, the Order does not grant customers the right to terminate radiopharmaceutical contracts with Cardinal that relate solely to the purchase of Positron Emission Tomography radiopharmaceuticals (also referred to as high energy radiopharmaceuticals).

Pursuant to the Order, Cardinal is required to notify each relevant customer within five days after the relevant closing date of the customer's right to terminate its existing contract. The Order further requires that Cardinal will terminate any relevant customer's existing contract within 30 days upon receiving that customer's request to terminate. Relevant customers will have the option to terminate their existing contract with Cardinal for a period of 24 months from the relevant closing date.

C. Facilitating the Acquirer's Employment of Certain Cardinal and Former Biotech Employees

To provide the acquirer(s) with access to any necessary employees, the Order requires Cardinal to facilitate and not interfere with the recruitment of certain former Biotech employees and current Cardinal nuclear pharmacy employees in Las Vegas, Albuquerque, and El Paso. Such employees also are

Analysis to Aid Public Comment

released from any restrictions on their ability to work for the acquirer(s).

D. A Monitor Will Help Ensure Compliance

The Order provides for the appointment by the Commission of an independent monitor with fiduciary responsibilities to the Commission, to help ensure that Cardinal carries out all of its responsibilities and obligations under the Order. The Order provides that Katherine L. Seifert, a person with significant experience in the radiopharmaceutical industry, shall serve as monitor. Ms. Seifert, currently of Seifert and Associates, Inc., provides consulting services for various clients in the radiopharmaceutical industry. In the event Cardinal fails to comply with its divestiture obligations, the Order also provides that the Commission may appoint a divestiture trustee to fulfill those requirements.

VII. Purpose of the Analysis to Aid Public Comment

The purpose of this analysis is to facilitate public comment on the proposed Decision and Order. This analysis is not intended to constitute an official interpretation of the Consent Agreement and Order.

Complaint

IN THE MATTER OF**DAVITA, INC.****CONSENT ORDER, ETC. IN REGARD TO ALLEGED VIOLATIONS OF
SEC. 5 OF THE FEDERAL TRADE COMMISSION ACT AND SEC. 7 OF
THE CLAYTON ACT**

Docket No. C-4334; File No. 111 0103
Filed, September 2, 2011 — Decision, October 20, 2011

This consent order addresses the acquisition by DaVita Inc. (“DaVita”) of CDSI Holding Company, Inc. (“CDSI”). DaVita is the second largest provider of outpatient dialysis services in the United States. CDSI is the fifth largest provider of outpatient dialysis services in the United States. The complaint alleges that the acquisition of CDSI by DaVita would substantially lessen competition, result in higher prices, and diminish service and quality for outpatient dialysis services in several geographic markets throughout the United States. The order requires DaVita to divest 29 outpatient dialysis clinics and to implement certain measures to ensure the divestitures is successful.

Participants

For the *Commission*: *Lisa D. DeMarchi Sleigh, Amy S. Posner, and Kari A. Wallace.*

For the *Respondent*: *Joel R. Grosberg and Gregory Heltzer, McDemott Will & Emery LLP.*

COMPLAINT

Pursuant to the Clayton Act and the Federal Trade Commission Act, and its authority thereunder, the Federal Trade Commission (“Commission”), having reason to believe that the Respondent DaVita Inc. (“DaVita”), a company subject to the jurisdiction of the Commission, has entered into an agreement to acquire CDSI I Holding Company, Inc. (“DSI”), a company subject to the jurisdiction of the Commission, in violation of Section 5 of the Federal Trade Commission Act (“FTC Act”), as amended, 15 U.S.C. § 45, that such acquisition, if consummated, would violate Section 7 of the of the Clayton Act, as amended, 15 U.S.C. § 18, and Section 5 of the FTC Act, as amended, 15 U.S.C. § 45, and it appearing to the Commission that a proceeding in

Complaint

respect thereof would be in the public interest, hereby issues its Complaint, stating its charges as follows:

I. DEFINITIONS

1. “Dialysis” means filtering a person’s blood, inside or outside of the body, to replicate the functions of the kidney.
2. “ESRD” means end stage renal disease, a chronic disease characterized by a near total loss of function of the kidneys, which in healthy people remove toxins and excess fluid from the blood.
3. “Outpatient dialysis services” means all procedures and services related to administering chronic dialysis treatment.

II. RESPONDENT

4. Respondent DaVita is a corporation organized, existing, and doing business under and by virtue of the laws of the State of Delaware, with its office and principal place of business located at 1551 Wewatta St. Denver, Colorado 80202. Respondent DaVita, among other things, is engaged in the provision and sale of outpatient dialysis services.

5. Respondent DaVita is, and at all times herein has been, engaged in commerce, as “commerce” is defined in Section 1 of the Clayton Act, as amended, 15 U.S.C. § 12, and is a corporation whose business is in or affects commerce, as “commerce” is defined in Section 4 of the Federal Trade Commission Act, as amended, 15 U.S.C. § 44.

III. THE ACQUIRED COMPANY

6. DSI is a is a corporation organized, existing, and doing business under and by virtue of the laws of the State of Delaware, with its office and principal place of business located at 424 Church Street, Suite 1900, Nashville, TN 37219. DSI, among other things, is engaged in the provision and sale of outpatient dialysis services.

Complaint

7. DSI is, and at all times herein has been, engaged in commerce, as “commerce” is defined in Section 1 of the Clayton Act as amended, 15 U.S.C. §12, and is a corporation whose business is in or affects commerce, as “commerce” is defined in Section 4 of the Federal Trade Commission Act, as amended, 15 U.S.C. § 44.

IV. THE PROPOSED ACQUISITION

8. On February 4, 2011, DaVita entered into an agreement (“Purchase Agreement”) to acquire DSI for approximately \$689 million in cash (the “Acquisition”).

V. THE RELEVANT MARKET

9. For the purposes of this Complaint, the relevant line of commerce in which to analyze the effects of the Acquisition is the provision of outpatient dialysis services. Most ESRD patients receive dialysis treatments three times per week in sessions lasting between three and five hours. The only alternative to outpatient dialysis treatments for patients suffering from ESRD is a kidney transplant. However, the wait-time for donor kidneys – during which ESRD patients must receive dialysis treatments – can exceed five years. Additionally, many ESRD patients are not viable transplant candidates. As a result, many ESRD patients have no alternative to ongoing dialysis treatments.

10. The relevant geographic market for the provision of dialysis services is defined by the distance ESRD patients are willing and/or able to travel to receive dialysis treatments, and is thus local in nature. Because ESRD patients often suffer from multiple health problems and may require assistance traveling to and from the dialysis clinic, these patients are unwilling and/or unable to travel long distances to receive dialysis treatment. As a general rule, ESRD patients do not travel more than 30 miles or 30 minutes to receive dialysis treatment, although travel times and distances vary depending on geographic barriers, travel patterns, and whether an area is urban, suburban, or rural.

11. For the purposes of this Complaint, the 22 geographic markets within which to assess the competitive effects of the

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proposed merger are the following 14 metropolitan statistical areas (“MSAs”) and micropolitan statistical areas (“μSAs”) other areas, or particular geographic areas contained therein: (1) Birmingham-Hoover, AL MSA; (2) Blytheville, AR μSA; (3) Phoenix-Mesa-Glendale, AZ MSA; (4) Tampa-St. Petersburg-Clearwater, FL MSA; (5) Atlanta-Sandy Springs-Marietta, GA MSA; (6) Chicago-Joliet-Naperville, IL-IN-WI MSA; (7) Indianapolis-Carmel, IN MSA; (8) Louisville/Jefferson County, KY-IN MSA; (9) Baton Rouge, LA MSA; (10) Greenville-Mauldin-Easley, SC MSA; (11) Memphis, TN-MS-AR MSA; (12) Beeville, TX μSA; (13) Corpus Christi, TX MSA; and (14) El Paso, TX MSA.

VI. THE STRUCTURE OF THE MARKET

12. The market for the provision of outpatient dialysis services is highly concentrated in each of the local areas identified in Paragraph 11, as measured by the Herfindahl-Hirschman Index (“HHI”) concentration ratios. The proposed acquisition represents a merger to monopoly in 1 market and would cause the number of providers to drop from three to two in fifteen other markets. Additionally, concentration increases significantly in the remaining six markets.

13. DaVita and DSI are actual and substantial competitors in each of the relevant markets.

VII. ENTRY CONDITIONS

14. The most significant barrier to entry into the relevant markets is locating a nephrologist with an established referral base to serve as the clinic’s medical director. By law, each dialysis clinic must have a nephrologist medical director. The medical director is essential to the competitiveness of the clinic because he or she is the clinic’s primary source of referrals. The lack of available nephrologists with an established referral stream is a significant barrier to entry into each of the relevant geographic markets identified in Paragraph 11. Additionally, an area must have certain attributes (such as a rapidly growing ESRD population, a favorable regulatory environment, average or below nursing and labor costs, and a relatively low penetration of

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managed care) to attract entry. The absence of these attributes is an additional barrier to entry into many of the relevant geographic markets.

15. New entry into the relevant markets sufficient to deter or counteract the anticompetitive effects described in Paragraph 16 is unlikely to occur, and would not occur in a timely manner because it would take over two years to enter and achieve significant market impact.

VIII. EFFECTS OF THE ACQUISITION

16. The effects of the Acquisition, if consummated, may be substantially to lessen competition and to tend to create a monopoly in the relevant markets in violation of Section 7 of the Clayton Act, as amended, 15 U.S.C. § 18, and Section 5 of the FTC Act, as amended, 15 U.S.C. § 45, in the following ways, among others:

- a. eliminating actual, direct, and substantial competition between DaVita and DSI in the market for the provision of outpatient dialysis services;
- b. increasing the ability of the merged entity unilaterally to raise prices of outpatient dialysis services; and
- c. reducing incentives to improve service or product quality in the relevant markets.

IX. VIOLATIONS CHARGED

17. The Purchase Agreement described in Paragraph 8 constitutes a violation of Section 5 of the FTC Act, as amended, 15 U.S.C. § 45.

18. The Acquisition described in Paragraph 8, if consummated, would constitute a violation of Section 7 of the Clayton Act, as amended, 15 U.S.C. § 18, and Section 5 of the FTC Act, as amended, 15 U.S.C. § 45.

Decision and Order

WHEREFORE, THE PREMISES CONSIDERED, the Federal Trade Commission on this second day of September, 2011, issues its Complaint against said Respondent.

By the Commission.

DECISION AND ORDER

The Federal Trade Commission (“Commission”), having initiated an investigation of the proposed acquisition by DaVita Inc. of CDSI I Holding Company, Inc. (“DSI”), and DaVita Inc. (hereafter referred to as “Respondent DaVita”) having been furnished thereafter with a copy of a draft of Complaint that the Bureau of Competition proposed to present to the Commission for its consideration and which, if issued by the Commission, would charge Respondent DaVita with violations of Section 7 of the Clayton Act, as amended, 15 U.S.C. § 18, and Section 5 of the Federal Trade Commission Act, as amended, 15 U.S.C. § 45; and

Respondent DaVita, its attorneys, and counsel for the Commission having thereafter executed an Agreement Containing Consent Orders (“Consent Agreement”), containing an admission by Respondent DaVita of all the jurisdictional facts set forth in the aforesaid draft of Complaint, a statement that the signing of said Consent Agreement is for settlement purposes only and does not constitute an admission by Respondent DaVita that the law has been violated as alleged in such Complaint, or that the facts as alleged in such Complaint, other than jurisdictional facts, are true, and waivers and other provisions as required by the Commission’s Rules; and

The Commission having thereafter considered the matter and having determined that it had reason to believe that Respondent DaVita has violated the said Acts, and that a Complaint should issue stating its charges in that respect, and having thereupon

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issued its Complaint and an Order to Hold Separate and Maintain Assets (“Hold Separate Order”), and having accepted the executed Consent Agreement and placed such Consent Agreement on the public record for a period of thirty (30) days for the receipt and consideration of public comments, now in further conformity with the procedure described in Commission Rule 2.34, 16 C.F.R. § 2.34, the Commission hereby makes the following jurisdictional findings and issues the following Decision and Order (“Order”):

1. Respondent DaVita Inc. is a corporation organized, existing and doing business under and by virtue of the laws of the State of Delaware with its office and principal place of business located at 1551 Wewatta St. Denver, Colorado 80202.
2. The Federal Trade Commission has jurisdiction of the subject matter of this proceeding and of Respondent DaVita, and the proceeding is in the public interest.

ORDER**I.**

IT IS ORDERED that, as used in this Order, the following definitions shall apply:

- A. “DaVita” means DaVita Inc., its directors, officers, employees, agents, representatives, successors, and assigns; and its joint ventures, subsidiaries, divisions, groups and affiliates controlled by DaVita Inc. (including, after the Effective Date, CDSI I Holding Company, Inc.), and the respective directors, officers, employees, agents, representatives, successors, and assigns of each.
- B. “DSI” means CDSI I Holding Company, Inc., its directors, officers, employees, agents, representatives, successors, and assigns; and its joint ventures, subsidiaries, divisions, groups and affiliates controlled by CDSI I Holding Company, Inc., and the respective

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directors, officers, employees, agents, representatives, successors, and assigns of each.

- C. “Commission” means the Federal Trade Commission.
- D. “Acquirer” and “Acquirers” means Frazier/NEA, and each Person that receives the prior approval of the Commission to acquire any of the Appendix A Clinic Assets pursuant to Paragraphs II or V of this Order.
- E. “Alabama Governmental Approvals For Divestiture” means any Governmental Approvals For Divestiture issued by the State of Alabama.
- F. “Alabama Clinic Assets” means the DSI Norwood Clinic, located at 1424 North Carraway Boulevard, Birmingham, AL 35234, and all Assets Associated with that Clinic.
- G. “Appendix A Clinics” means Clinics listed in Appendix A to this Order.
- H. “Appendix A Clinic Assets” means the Appendix A Clinics, the Appendix A Joint Venture Equity Interests, and all Assets Associated with each of the Appendix A Clinics, except for the Owned Real Property.
- I. “Appendix A Joint Venture Equity Interests” means the joint venture equity interest owned by DSI in each of the following joint ventures: (1) Renal Care Group South Tampa, LLC; (2) DSI El Paso, LLC (3) Renal Care Group Galleria, LLC; and (4) DSI Greenville, LLC. The joint ventures are more fully described in Appendix A-2.
- J. “Appendix F Clinics” means the clinics identified in Non-Public Appendix F that are owned by DaVita in locations proximate to the DSI Clinics listed in Appendix A. In any given location, there may be a greater, smaller, or equal number of DaVita Clinics in

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Non-Public Appendix F that correspond to DSI Clinics in any given location.

- K. “Appendix F Clinic Assets” means the Appendix F Clinics, the Appendix F Joint Venture Equity Interests and all Assets Associated with each of the Appendix F Clinics, except for the Owned Real Property.
- L. “Appendix F Joint Venture Equity Interests” means the joint venture equity interest owned by DSI described in Appendix F-2.
- M. “Assets Associated” means the following assets Relating To the Operation Of A Clinic:
1. all rights under the Clinic’s Physician Contracts;
 2. leases for the Real Property of the Clinic;
 3. consumable or disposable inventory, including, but not limited to, janitorial, office, and medical supplies, and at least ten (10) treatment days of dialysis supplies and pharmaceuticals, including, but not limited to, erythropoietin;
 4. all rights, title and interest of Respondent DaVita or DSI in any tangible property (except for consumable or disposable inventory) that has been on the premises of the Clinic at any time since January 1, 2011, including, but not limited to, all equipment, furnishings, fixtures, improvements, and appurtenances;
 5. books, records, files, correspondence, manuals, computer printouts, databases, and other documents Relating To the Operation Of The Clinic located on the premises of the Clinic or in the possession of the Regional Manager responsible for such Clinic (or copies thereof where Respondent DaVita or DSI has a legal

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obligation to maintain the original document), including, but not limited to:

- a. documents containing information Relating To patients (to the extent transferable under applicable law), including, but not limited to, medical records,
- b. financial records,
- c. personnel files,
- d. Physician lists and other records of the Clinic's dealings with Physicians,
- e. maintenance records,
- f. documents Relating To policies and procedures,
- g. documents Relating To quality control,
- h. documents Relating To Payors,
- i. documents Relating To Suppliers,
- j. documents Relating To Clinics other than the Clinic To Be Divested, *provided, however*, if such documents are located other than on the premises of the Clinic To Be Divested, Respondent DaVita may submit a copy of the document with the portions not Relating To the Clinic To Be Divested redacted, and
- k. copies of contracts with Payors and Suppliers, unless such contracts cannot, according to their terms, be disclosed to third parties even with the permission of Respondent DaVita to make such disclosure;

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6. Respondent DaVita's and DSI's Medicare and Medicaid provider numbers, to the extent transferable;
7. all permits and licenses, to the extent transferable;
8. Intangible Property relating exclusively to the Operation Of The Clinic; and a royalty-free perpetual worldwide license for the use, without any limitation, of all other Intangible Property Relating To the Operation Of The Clinic (including the right to transfer or sublicense such Intangible Property, exclusively or nonexclusively, to others by any means); and
9. assets that are used in, or necessary for, the Operation Of The Clinic.

Provided, however, that "Assets Associated" does not include Excluded Assets.

- N. "Assets To Be Divested" means the Appendix A Clinic Assets and any Appendix F Clinic Assets divested pursuant to Paragraph V.A. of the Order.
- O. "Clinic" means a facility that provides hemodialysis or peritoneal dialysis services to patients suffering from kidney disease.
- P. "Clinic's Physician Contracts" means all agreements to provide the services of a Physician to a Clinic, regardless of whether any of the agreements are with a Physician or with a medical group, including, but not limited to, agreements for the services of a medical director for the Clinic and "joinder" agreements with Physicians in the same medical practice as a medical director of the Clinic.
- Q. "Clinic To Be Divested" and "Clinics To Be Divested" means the Appendix A Clinics, the Appendix A Joint Venture Equity Interests and any Appendix F Clinics

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or Appendix F Joint Venture Equity Interests divested pursuant Paragraph V.A. of the Order.

- R. “Confidential Business Information” means competitively sensitive, proprietary, and all other information that is not in the public domain owned by or pertaining to a Person or a Person’s business, and includes, but is not limited to, all customer lists, price lists, contracts, cost information, marketing methods, patents, technologies, processes, or other trade secrets.
- S. “Contract Services” means services performed pursuant to any Clinic’s Physician Contract.
- T. “DaVita Employee Of A Clinic To Be Divested” and “DaVita Employee Of The Clinic To Be Divested” means an Employee Of A Clinic To Be Divested who is employed by Respondent DaVita or, before the acquisition by Respondent DaVita, by DSI.
- U. “DaVita’s Medical Protocols” means medical protocols promulgated by Respondent DaVita, whether in hard copy or embedded in software, that have been in effect at any time since July 1, 2010. *Provided, however,* “DaVita’s Medical Protocols” does not mean medical protocols adopted or promulgated, at any time, by any Physician or by any Acquirer, even if such medical protocols are identical, in whole or in part, to medical protocols promulgated by Respondent DaVita.
- V. “Designated DaVita Employee” means (1) a DaVita Employee Of A Clinic To Be Divested, and (2) any of the additional DaVita and DSI employees listed in Non-Public Appendix G to this Order.
- W. “Divestiture Agreement” and “Divestiture Agreements” mean any agreement pursuant to which Respondent DaVita or a Divestiture Trustee divests any Appendix A Clinic Assets or Appendix F Clinic

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Assets pursuant to this Order and with the prior approval of the Commission.

- X. “Divestiture Trustee” means the person appointed to act as trustee by the Commission pursuant to Paragraph II.A or V of this Order.
- Y. “DSI’s Medical Protocols” means medical protocols promulgated by DSI, whether in hard copy or embedded in software, that have been in effect at any time since July 1, 2010. *Provided, however,* “DSI’s Medical Protocols” does not mean medical protocols adopted or promulgated, at any time, by any Physician or by any Acquirer, even if such medical protocols are identical, in whole or in part, to medical protocols promulgated by DSI.
- Z. “Effective Date” means the date on which Respondent DaVita acquires DSI.
- AA. “Employee Of A Clinic To Be Divested” and “Employee Of The Clinic To Be Divested” mean any individual (including, but not limited to, a clinic director, manager, nurse, technician, clerk, or social worker) who is not a Regional Manager, who is employed by Respondent DaVita, or before the Acquisition, by DSI, by an Acquirer, or by another manager or owner of such Clinic To Be Divested, and who has worked part time or full-time on the premises of such Clinic To Be Divested at any time since January 1, 2011, regardless of whether the individual has also worked on the premises of any other Clinic.
- BB. “Excluded Assets” means:
1. all cash, cash equivalents, and short term investments of cash;
 2. accounts receivable;

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3. income tax refunds and tax deposits due Respondent DaVita or DSI;
4. unbilled costs and fees, and Medicare bad debt recovery claims, arising before a Clinic is divested to an Acquirer;
5. rights to the names “DaVita” and any variation of that name, and any names, phrases, marks, trade names, and trademarks to the extent they include the marks and designs in Exhibit D to this Order;
6. insurance policies and all claims thereunder;
7. prepaid items or rebates;
8. minute books (other than governing body minute books of the Clinic To Be Divested), tax returns, and other corporate books and records;
9. any inter-company balances due to or from Respondent DaVita and DSI or their affiliates;
10. all benefits plans;
11. all writings and other items that are protected by the attorney-client privilege, the attorney work product doctrine or any other cognizable privilege or protection, except to the extent such information is necessary to the Operation Of A Clinic that is divested;
12. telecommunication systems equipment and applications, and information systems equipment including, but not limited to computer hardware, not physically located at a Clinic To Be Divested but shared with the Clinic To Be Divested through local and/or wide area networking systems;
13. e-mail addresses and telephone numbers of Respondent DaVita’s and DSI’s employees;

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14. Software;
 15. computer hardware used in the Operation Of The Clinic that is (a) not located at the Clinic, and (b) not otherwise to be divested pursuant to a Divestiture Agreement;
 16. all Supplier or provider numbers issued to Respondent DaVita or DSI by a Supplier or Payor with respect to any Clinic To Be Divested, except for Respondent DaVita's or DSI's Medicare and Medicaid provider numbers for each Clinic To Be Divested;
 17. rights under agreements with Payors and Suppliers that are not assignable even if Respondent DaVita and DSI approve such assignment;
 18. office equipment and furniture that (a) is not, in the Ordinary Course Of Business, physically located at the Clinic To Be Divested, (b) is shared with Clinics other than the Clinic To Be Divested, and (c) is not necessary to the Operation Of The Clinic To Be Divested.
 19. Licensed Intangible Property; and
 20. strategic planning documents that
 - a. relate to the Operation Of The Clinic other than the Clinic To Be Divested, and
 - b. are not located on the premises of the Clinic To Be Divested.
- CC. "Frazier" means Frazier Healthcare, a growth equity and venture capital partnership organized, existing and doing business under and by virtue of the laws of the State of Delaware with its office and principal place of

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business located at 601 Union Street, Suite 3200, Seattle, WA 98101.

DD. “Frazier/NEA Divestiture Agreements” means the following agreements:

1. the Amended and Restated Asset Purchase Agreement dated August 26, 2011, by and among Dialysis Newco, Inc., CDSI I Holding Company, Inc., and DaVita Inc., and all attachments and exhibits, thereto, and
2. the Transition Services Agreement dated August 26, 2011, between Dialysis Newco, Inc. and DaVita Inc., and all attachments and exhibits, thereto.

(The Frazier/NEA Divestiture Agreements are attached as Non-Public Appendix E to this Order.)

EE. “Governmental Approvals” means any permissions or sanctions issued by any government or governmental organization, including, but not limited to, licenses, permits, accreditations, authorizations, registrations, certifications, certificates of occupancy, and certificates of need.

FF. “Government Approvals For Continued Operation” means any Governmental Approvals, other than Government Approvals For Divestiture, that an Acquirer must have to continue to operate a Clinic To Be Divested.

GG. “Governmental Approvals For Divestiture” means any Governmental Approvals that an Acquirer must have to own, and to initially operate, a Clinic To Be Divested, including, but not limited to, state-issued licenses and state-issued certificates of need.

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- HH. “Illinois Governmental Approvals For Divestiture” means any Governmental Approvals For Divestiture issued by the State of Illinois.
- II. “Illinois Clinic Assets” means the DSI Scottsdale Clinic located at 4651 West 79th Street, Unit 100 Chicago, IL 60652, and all Assets Associated with that Clinic.
- JJ. “Intangible Property” means intangible property Relating To the Operation Of A Clinic To Be Divested including, but not limited to, intellectual property, software, computer programs, patents, know-how, goodwill, technology, trade secrets, technical information, marketing information, protocols, quality control information, trademarks, trade names, service marks, logos, and the modifications or improvements to such intangible property.
- KK. “Licensed Intangible Property” means intangible property licensed to Respondent DaVita from a third party Relating To the Operation Of A Clinic To Be Divested including, but not limited to, intellectual property, software, computer programs, patents, know-how, goodwill, technology, trade secrets, technical information, marketing information, protocols, quality control information, trademarks, trade names, service marks, logos, and the modifications or improvements to such intangible property that are licensed to Respondent DaVita. (“Licensed Intangible Property” does not mean modifications and improvements to intangible property that are not licensed to Respondent DaVita.)
- LL. “Monitor Agreement” means the Monitor Agreement dated August 11, 2011, between DaVita Inc., and Richard Shermer, of R. Shermer & Co. (The Monitor Agreement is attached as Appendix C to this Order. The Monitor Agreement Compensation is attached as Confidential Appendix C-1 to this Order.)

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- MM. “NEA” means New Enterprise Associates, a venture capital firm organized, existing and doing business under and by virtue of the laws of the Cayman Islands with its office and principal place of business located at 2855 Sand Hill Road, Menlo Park, CA 94025.
- NN. “Operation Of A Clinic” and “Operation Of The Clinic” mean all activities Relating To the business of a Clinic, including, but not limited to:
1. attracting patients to the Clinic for dialysis services, providing dialysis services to patients of the Clinic, and dealing with their Physicians, including, but not limited to, services Relating To hemodialysis and peritoneal dialysis;
 2. providing medical products to patients of the Clinic;
 3. maintaining the equipment on the premises of the Clinic, including, but not limited to, the equipment used in providing dialysis services to patients;
 4. purchasing supplies and equipment for the Clinic;
 5. negotiating leases for the premises of the Clinic;
 6. providing counseling and support services to patients receiving products or services from the Clinic;
 7. contracting for the services of medical directors for the Clinic;
 8. dealing with Payors that pay for products or services offered by the Clinic, including but not limited to, negotiating contracts with such Payors and submitting claims to such Payors; and
 9. dealing with Governmental Approvals Relating To the Clinic or that otherwise regulate the Clinic.

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- OO. “Ordinary Course Of Business” means actions taken by any Person in the ordinary course of the normal day-to-day Operation Of The Clinic that is consistent with past practices of such Person in the Operation Of The Clinic, including, but not limited to past practice with respect to amount, timing, and frequency.
- PP. “Osceola Non-Compete” means the non-compete agreement between Respondent DaVita and Dr. Nawar Mansour, who was proposed as a Medical Director for a clinic that Respondent DaVita never opened in Osceola, Arkansas.
- QQ. “Other Contracts Of Each Clinic To Be Divested” means all contracts Relating To the Operation Of A Clinic, where such Clinic is a Clinic To Be Divested – including, but not limited to, contracts for goods and services provided to the Clinic and contracts with Payors – but does not mean the Clinic’s Physician Contracts and the leases for the Real Property Of The Clinic.
- RR. “Payor” means any Person that purchases, reimburses for, or otherwise pays for medical goods or services for themselves or for any other person, including, but not limited to: health insurance companies; preferred provider organizations; point of service organizations; prepaid hospital, medical, or other health service plans; health maintenance organizations; government health benefits programs; employers or other persons providing or administering self insured health benefits programs; and patients who purchase medical goods or services for themselves.
- SS. “Person” means any natural person, partnership, corporation, association, trust, joint venture, government, government agency, or other business or legal entity.

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- TT. “Physician” means a doctor of allopathic medicine (“M.D.”) or a doctor of osteopathic medicine (“D.O.”).
- UU. “Real Property Of The Clinic” means real property on which, or in which, the Clinic is located, including real property used for parking and for other functions Relating To the Operation Of The Clinic.
- VV. “Relating To” means pertaining in any way to, and is not limited to that which pertains exclusively to or primarily to.
- WW. “Regional Manager” means any individual who has been employed by Respondent DaVita or DSI with supervisory responsibility for three or more Clinics.
- XX. “Regional Manager Of A Clinic To Be Divested” and “Regional Manager Of The Clinic To Be Divested” mean a Regional Manager who has had direct supervisory responsibility for a Clinic To Be Divested at any time since January 1, 2011.
- YY. “Software” means executable computer code and the documentation for such computer code, but does not mean data processed by such computer code.
- ZZ. “Supplier” means any Person that has sold to Respondent DaVita or DSI any goods or services, other than Physician services, for use in a Clinic To Be Divested. *Provided, however,* “Supplier” does not mean an employee of Respondent DaVita or DSI.
- AAA. “Time Of Divestiture” means the date upon which an Appendix A Clinic or an Appendix F Clinic is divested to an Acquirer pursuant to this Order.

II.**IT IS FURTHER ORDERED** that:

- A. Respondent DaVita shall:

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1. within thirty (30) days after the Effective Date, divest to Frazier/NEA, absolutely, and in good faith, pursuant to and in accordance with the Frazier/NEA Divestiture Agreements all the Appendix A Clinic Assets, except for the Alabama Clinic Assets and the Illinois Clinic Assets, as on-going businesses, and grant to the Acquirer a royalty-free, worldwide exclusive license for the use, without any limitation, of the DSI Medical Protocols (including the right to transfer or sublicense such protocols, exclusively or nonexclusively, to others by any means); *provided, however,* that Respondent DaVita may receive, as a part of the Frazier/NEA Divestiture Agreements and for a reasonable amount of time during a transition period, a royalty-free perpetual worldwide license for the use of DSI's Medical Protocols (not including the right to transfer or sublicense such protocols, exclusively or nonexclusively, to others by any means).
2. within ninety (90) days after the Effective Date, divest to Frazier/NEA, absolutely, and in good faith, pursuant to and in accordance with the Frazier/NEA Divestiture Agreements, the Alabama Clinic Assets, as an on-going business.
3. within ninety (90) days after the Effective Date, divest to Frazier/NEA, absolutely, and in good faith, pursuant to and in accordance with the Frazier/NEA Divestiture Agreements, the Illinois Clinic Assets, as an ongoing business.

Provided, however, if, at the time the Commission determines to make this Order final, the Commission notifies Respondent DaVita that Frazier/NEA is not an acceptable Acquirer then, after receipt of such written notification: (1) Respondent DaVita shall immediately notify Frazier/NEA of the notice received from the Commission and shall as soon as practicable, but no

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later than within five (5) business days, effect the rescission of the Divestiture Agreement; and (2) Respondent DaVita shall: (a) within six (6) months of the date DaVita receives notice of such determination from the Commission, divest the Appendix A Clinic Assets, except for the Alabama Clinic Assets and the Illinois Clinic Assets, absolutely and in good faith, at no minimum price, as ongoing businesses to an Acquirer or Acquirers that receive the prior approval of the Commission and only in a manner that receives the prior approval of the Commission; and (b) within eight (8) months of the date DaVita receives notice of such determination from the Commission, divest the Alabama Clinic Assets and the Illinois Clinic Assets absolutely and in good faith, at no minimum price, as ongoing businesses, to an Acquirer or Acquirers that receive the prior approval of the Commission and only in a manner that receives the prior approval of the Commission.

Provided further, however, that if Respondent DaVita has complied with the terms of this Paragraph before the date on which this Order becomes final, and if, at the time the Commission determines to make this Order final, the Commission notifies Respondent DaVita that the manner in which the divestiture was accomplished is not acceptable, the Commission may direct Respondent DaVita or appoint the Divestiture Trustee, to effect such modifications to the manner of divestiture including, but not limited to, entering into additional agreements or arrangements, as the Commission may determine are necessary to satisfy the requirements of this Order.

- B. The Frazier/NEA Divestiture Agreements are incorporated by reference into this Order and made a part hereof as Confidential Appendix E. Any failure by Respondent DaVita to comply with the Frazier/NEA Divestiture Agreements shall constitute a failure to comply with the Order. The Frazier/NEA Divestiture Agreements shall not vary or contradict, or

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be construed to vary or contradict, the terms of this Order. Nothing in this Order shall reduce, or be construed to reduce, any rights or benefits of Frazier/NEA, or any obligations of Respondent DaVita, under the Frazier/NEA Divestiture Agreements.

- C. Respondent DaVita shall:
1. place no restrictions on the use by any Acquirer of any of the Assets To Be Divested or any of the Clinics To Be Divested.
 2. cooperate with the Acquirer and assist the Acquirer, at no cost to the Acquirer, at the Time Of Divestiture of each Clinic To Be Divested, in obtaining all Government Approvals For Divestiture, and all Government Approvals For Continued Operation, for each Clinic To Be Divested;
 3. at the Time Of Divestiture of each Clinic To Be Divested:
 - a. assign to the Acquirer all rights, title, and interest to leases for the Real Property Of The Clinic, and shall obtain all approvals necessary for such assignments; *provided, however*, that (1) if the Acquirer obtains all rights, title, and interest to a lease for Real Property Of A Clinic To Be Divested before the Assets To Be Divested are divested pursuant to Paragraph II.A. of this Order, and (2) the Acquirer certifies its receipt of such lease and attaches it as part of the Divestiture Agreement, then Respondent DaVita shall not be required to make the assignments for such Clinic To Be Divested as required by this Paragraph; and
 - b. assign to the Acquirer all of the Clinic's Physician Contracts, and shall obtain all

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approvals necessary for such assignment; *provided, however*, that (1) if the Acquirer enters into a Clinic's Physician Contract for a Clinic To Be Divested before the Assets To Be Divested are divested pursuant to Paragraph II.A. of this Order, and (2) the Acquirer certifies its receipt of such contract and attaches it as part of the Divestiture Agreement, then Respondent DaVita shall not be required to make the assignment for such Clinic To Be Divested as required by this Paragraph.

4. With respect to all Other Contracts Of Each Clinic To Be Divested, at the Acquirer's option and at the Time Of Divestiture of each Clinic To Be Divested:
 - a. if such contract can be assigned without third party approval, assign its rights under the contract to the Acquirer; and
 - b. if such contract can be assigned to the Acquirer only with third party approval, assist and cooperate with the Acquirer in obtaining:
 - (1) such third party approval and in assigning the contract to the Acquirer; or
 - (2) a new contract.

D. Respondent DaVita shall:

1. at the Time Of Divestiture of each Clinic To Be Divested, provide to the Acquirer of such Clinic contact information about Payors and Suppliers for the Clinic, and
2. not object to the sharing of Payor and Supplier contract terms Relating To the Clinics To Be Divested: (i) if the Payor or Supplier consents in

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writing to such disclosure upon a request by the Acquirer, and (ii) if the Acquirer enters into a confidentiality agreement with Respondent DaVita not to disclose the information to any third party.

- E. From the time Respondent DaVita signs the Agreement Containing Consent Order until sixty (60) days after the Time Of Divestiture of each Clinic To Be Divested or until January 3, 2012, whichever is later:
1. Respondent DaVita shall, if requested by the Acquirer, facilitate interviews between each Designated DaVita Employee and the Acquirer, and shall not discourage such employee from participating in such interviews;
 2. Respondent DaVita shall not interfere in employment negotiations between each Designated DaVita Employee and the Acquirer;
 3. Respondent DaVita shall not prevent, prohibit or restrict or threaten to prevent, prohibit or restrict the Designated DaVita Employee from being employed by the Acquirer, and shall not offer any incentive to the Designated DaVita Employee to decline employment with the Acquirer;
 4. Respondent DaVita shall cooperate with the Acquirer of the Clinic in effecting transfer of the Designated DaVita Employee to the employ of the Acquirer, if the Designated DaVita Employee accepts such offer of employment from the Acquirer;
 5. Respondent DaVita shall eliminate any contractual provisions or other restrictions that would otherwise prevent the Designated DaVita Employee from being employed by the Acquirer;

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6. Respondent DaVita shall eliminate any confidentiality restrictions that would prevent the Designated DaVita Employee who accepts employment with the Acquirer from using or transferring to the Acquirer any information Relating To the Operation Of The Clinic; and
7. Respondent DaVita shall pay, for the benefit of any Designated DaVita Employee who accepts employment with the Acquirer, all accrued bonuses, vested pensions and other accrued benefits.

Provided, however, that if, at any time after the Time of Divestiture, the Acquirer gives Respondent DaVita an unsolicited list of employees from the Non-Public Appendix G to whom the Acquirer does not intend to offer employment, then such employees may be hired by Respondent DaVita as full time employees without violating this Paragraph II.E. *provided, further, however,* that no earlier than fifteen (15) days after the Time of Divestiture, Respondent DaVita may submit a written request to the Acquirer identifying those persons from the Non-Public Appendix G to whom Respondent DaVita wishes to offer full time employment; and if the Acquirer within fifteen (15) days of receipt of such request grants, in writing, such request, then Respondent DaVita may offer employment to such employees; but if the Acquirer within fifteen (15) days of receipt of such request either: (i) chooses to hire such employees, or (ii) chooses to defer a hiring decision and keep the requested employees on the Non-Public Appendix G, then Respondent DaVita shall continue to comply with the terms of this Paragraph II.E. with regard to such employees.

- F. For a period of two (2) years following the Time Of Divestiture of each Clinic To Be Divested, Respondent DaVita shall not, directly or indirectly, solicit, induce, or attempt to solicit or induce any

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Designated DaVita Employee who is employed by the Acquirer to terminate his or her employment relationship with the Acquirer, unless that employment relationship has already been terminated by the Acquirer; *provided, however*, Respondent DaVita may make general advertisements for employees including, but not limited to, in newspapers, trade publications, websites, or other media not targeted specifically at Acquirer's employees; *provided, further, however*, Respondent DaVita may hire employees who apply for employment with Respondent DaVita, as long as such employees were not solicited by Respondent DaVita in violation of this Paragraph; *provided, further, however*, Respondent DaVita may offer employment to an Designated DaVita Employee who is employed by the Acquirer in only a part-time capacity, if the employment offered by Respondent DaVita would not, in any way, interfere with the employee's ability to fulfill his or her employment responsibilities to the Acquirer.

- G. With respect to each Physician who has provided services to a Clinic To Be Divested pursuant to any of the Clinic's Physician Contracts in effect at any time during the four (4) months preceding the Time Of Divestiture of the Clinic ("Contract Physician"):
1. Respondent DaVita shall not offer any incentive to the Contract Physician, the Contract Physician's practice group, or other members of the Contract Physician's practice group to decline to provide services to the Clinic To Be Divested, and shall eliminate any confidentiality restrictions that would prevent the Contract Physician, the Contract Physician's practice group, or other members of the Contract Physician's practice group from using or transferring to the Acquirer of the Clinic To Be Divested any information Relating To the Operation Of The Clinic; and
 2. For a period of three (3) years following the Time Of Divestiture of each Clinic To Be Divested, Respondent

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DaVita shall not contract for the services of the Contract Physician, the Contract Physician's practice group, or other members of the Contract Physician's practice group for the provision of Contract Services to be performed in any of the areas listed in Appendix B of this Order that correspond to such Clinic. *Provided, however,* if the Contract Physician, or the Contract Physician's practice group, or other members of the Contract Physician's practice group were providing services to a Clinic pursuant to a contract with Respondent DaVita or DSI in effect as of January 1, 2011, then Respondent DaVita may contract with such Contract Physicians, or the Contract Physician's practice group, or other members of the Contract Physician's practice group for services to be provided to that particular Clinic.

- H. Respondent DaVita shall:
1. not disclose Confidential Business Information relating exclusively to any of the Clinics To Be Divested to any Person other than the Acquirer of such Clinic;
 2. after the Time Of Divestiture of such Clinic:
 - a. Respondent DaVita shall not use Confidential Business Information relating exclusively to any of the Clinics To Be Divested for any purpose other than complying with the terms of this Order or with any law; and
 - b. Respondent DaVita shall destroy all records of Confidential Business Information relating exclusively to any of the Clinics To Be Divested , except to the extent that: (1) Respondent DaVita is required by law to retain such information, and (2) Respondent DaVita's inside or outside attorneys may keep one copy solely for archival purposes, but may not

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disclose such copy to the rest of Respondent DaVita.

- I. At the Time Of Divestiture of each Clinic To Be Divested, Respondent DaVita shall provide the Acquirer of the Clinic with manuals, instructions, and specifications sufficient for the Acquirer to access and use any information
 1. divested to the Acquirer pursuant to this Order, or
 2. in the possession of the Acquirer, and previously used by Respondent DaVita or DSI in the Operation Of The Clinic.
- J. For two (2) years following the Time Of Divestiture of each Clinic To Be Divested, Respondent DaVita shall not solicit the business of any patients that received any goods or services from such Clinic between July 1, 2010, and the date of such divestiture, *provided, however*, Respondent DaVita may (i) make general advertisements for the business of such patients including, but not limited to, in newspapers, trade publications, websites, or other media not targeted specifically at such patients, and (ii) provide advertising and promotions directly to any patient that initiates discussions with, or makes a request to, any Respondent DaVita employee.
- K. Respondent DaVita shall convey to each Acquirer of a Clinic To Be Divested the right to use any Licensed Intangible Property (to the extent permitted by the third-party licensor), if such right is needed for the Operation Of The Clinic by the Acquirer and if the Acquirer is unable, using commercially reasonable efforts, to obtain equivalent rights from other third parties on commercially reasonable terms and conditions.
- L. Respondent DaVita shall do nothing to prevent or discourage Suppliers that, prior to the Time Of

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Divestiture of any Clinic To Be Divested, supplied goods and services for use in any Clinic To Be Divested from continuing to supply goods and services for use in such Clinic.

- M. Respondent DaVita shall not acquire DSI until it has obtained for all the Appendix A Clinics:
1. all approvals for the assignment of the Clinic's Physician Contracts, as required by Paragraph II.C.3.b. of this Order;
 2. all approvals by joint venture partners necessary for the Acquirer to acquire the Appendix A Clinics that are owned by a joint venture, and shall assign all such approvals to the Acquirer; and
 3. all approvals by joint venture partners necessary for the Acquirer of Appendix A Joint Venture Equity Interests to jointly own and operate the Appendix A Clinics that are owned by the joint venture, and shall assign all such approvals to the Acquirer.

Copies of all such approvals shall be incorporated into the Divestiture Agreements as appendices.

- N. Respondent DaVita shall not acquire DSI until it has:
1. included, as part of the Divestiture Agreements, a letter stating that the Osceola Non-Compete is rescinded and that it will not be re-entered or re-negotiated for five (5) years following the Time of Divestiture; and
 2. provided notice to all parties involved in the Osceola Non-Compete that the Osceola Non-Compete has been rescinded.
- O. With respect to Respondent DaVita's Medical Protocols:

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1. Respondent DaVita shall retain a copy of DaVita's Medical Protocols until six (6) months after all of the Assets To Be Divested have been divested, pursuant to this Order;
2. If any Acquirer of a Clinic To Be Divested requests in writing to Respondent DaVita:
 - a. within six (6) months of the Time Of Divestiture of that Clinic to that Acquirer, that DaVita license a copy of DaVita's Medical Protocols to that Acquirer, DaVita shall within five (5) business days of such request, grant to that Acquirer a royalty-free perpetual worldwide license for the use, without any limitation, of DaVita's Medical Protocols (including the right to transfer or sublicense such protocols, exclusively or nonexclusively, to others by any means); or
 - b. before the Time of Divestiture, that DaVita license a copy of DaVita's Medical Protocols to that Acquirer, DaVita shall grant, as part of the Divestiture Agreements, to that Acquirer for a reasonable amount of time during a transition period, a royalty-free perpetual worldwide license for the use of DaVita's Medical Protocols (not including the right to transfer or sublicense such protocols, exclusively or nonexclusively, to others by any means); and
3. DaVita shall create no disincentive for any Acquirer of a Clinic To Be Divested to make such a request for a license for DaVita's Medical Protocols, and shall not enter into any agreement or understanding with any Acquirer that the Acquirer not make such a request.

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- P. Respondent DaVita shall not terminate any transition services agreement that is a part of the Frazier/NEA Divestiture Agreements before the end of the term approved by the Commission without:
1. the written agreement of the Acquirer and thirty (30) days prior notice to the Commission; or,
 2. in the case of a proposed unilateral termination by Respondent DaVita due to an alleged breach of an agreement by the Acquirer, sixty (60) days notice of such termination. *Provided, however,* such sixty (60) days notice shall be given only after the parties have:
 - a. attempted to settle the dispute between themselves, and
 - b. engaged in arbitration and received an arbitrator's decision, or
 - c. received a final court decision after all appeals.
- Q. The purpose of Paragraph II of this Order is to ensure the continuation of the Clinics To Be Divested as, or as part of, ongoing viable enterprises engaged in the same business in which such assets were engaged at the time of the announcement of the acquisition by Respondent DaVita Inc. of DSI, to ensure that the Clinics To Be Divested are operated independently of, and in competition with, Respondent DaVita, and to remedy the lessening of competition alleged in the Commission's Complaint.

III.

IT IS FURTHER ORDERED that for a period of five (5) years from the date this Order is issued, Respondent DaVita shall not, without providing advance written notification to the Commission in the manner described in this paragraph, directly or indirectly:

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- A. acquire any assets of or financial interest in any Clinic located in any of the areas listed in Appendix B of this Order; or
- B. enter into any contract to participate in the management or Operation Of A Clinic located in any of the areas listed in Appendix B of this Order, except to the extent that the contract relates exclusively to:
 - 1. off-site lab services or social worker support materials; or
 - 2. billing services, collection services, bookkeeping services, accounting services, supply purchasing and logistics services, or the preparation of financial reports and accounts receivable reports (collectively “Such Services”), where appropriate firewalls and confidentiality agreements are implemented to prevent Confidential Business Information of the Clinic from being disclosed to anyone participating in any way in the operation or management of any Clinic owned by Respondent DaVita or any Clinic other than the Clinic to which Such Services are being provided.

Said advance written notification shall contain (i) either a detailed term sheet for the proposed acquisition or the proposed agreement with all attachments, and (ii) documents that would be responsive to Item 4(c) of the Premerger Notification and Report Form under the Hart-Scott-Rodino Premerger Notification Act, Section 7A of the Clayton Act, 15 U.S.C. § 18a, and Rules, 16 C.F.R. § 801-803, Relating To the proposed transaction (hereinafter referred to as “the Notification), *provided, however*, (i) no filing fee will be required for the Notification, (ii) an original and one copy of the Notification shall be filed only with the Secretary of the Commission and need not be submitted to the United States Department of Justice, and (iii) the Notification is required from Respondent DaVita and not from any other party to the transaction. Respondent DaVita shall provide the Notification to the Commission at least thirty (30) days prior to consummating

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the transaction (hereinafter referred to as the “first waiting period”). If, within the first waiting period, representatives of the Commission make a written request for additional information or documentary material (within the meaning of 16 C.F.R. § 803.20), Respondent DaVita shall not consummate the transaction until thirty days after submitting such additional information or documentary material. Early termination of the waiting periods in this paragraph may be requested and, where appropriate, granted by letter from the Bureau of Competition.

Provided, however, that prior notification shall not be required by this paragraph for a transaction for which Notification is required to be made, and has been made, pursuant to Section 7A of the Clayton Act, 15 U.S.C. § 18a.

IV.**IT IS FURTHER ORDERED** that:

- A. Richard Shermer of R. Shermer & Co., shall be appointed Monitor to assure that Respondent DaVita expeditiously complies with all of its obligations and performs all of its responsibilities as required by this Order.
- B. No later than one (1) day after the Effective Date, Respondent DaVita shall, pursuant to the Monitor Agreement and to this Order, transfer to the Monitor all the rights, powers, and authorities necessary to permit the Monitor to perform their duties and responsibilities in a manner consistent with the purposes of this Order.
- C. In the event a substitute Monitor is required, the Commission shall select the Monitor, subject to the consent of Respondent DaVita, which consent shall not be unreasonably withheld. If Respondent DaVita has not opposed, in writing, including the reasons for opposing, the selection of a proposed Monitor within ten (10) days after notice by the staff of the Commission to Respondent DaVita of the identity of

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any proposed Monitor, Respondent DaVita shall be deemed to have consented to the selection of the proposed Monitor. Not later than ten (10) days after appointment of a substitute Monitor, Respondent DaVita shall execute an agreement that, subject to the prior approval of the Commission, confers on the Monitor all the rights and powers necessary to permit the Monitor to monitor Respondent DaVita's compliance with the terms of this Order, the Order to Maintain Assets, and the Divestiture Agreements in a manner consistent with the purposes of this Order.

- D. Respondent DaVita shall consent to the following terms and conditions regarding the powers, duties, authorities, and responsibilities of the Monitor:
1. The Monitor shall have the power and authority to monitor Respondent DaVita's compliance with the terms of this Order, the Order to Maintain Assets, and the Divestiture Agreements, and shall exercise such power and authority and carry out the duties and responsibilities of the Monitor in a manner consistent with the purposes of this Order and in consultation with the Commission, including, but not limited to:
 - a. Assuring that Respondent DaVita expeditiously complies with all of its obligations and perform all of its responsibilities as required by the this Order, the Order to Maintain Assets, and the Divestiture Agreements;
 - b. Monitoring any transition services agreements;
 - c. Assuring that Confidential Business Information is not received or used by Respondent DaVita or the Acquirers, except as allowed in this Order and in the Order to Maintain Assets, in this matter.

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2. The Monitor shall act in a fiduciary capacity for the benefit of the Commission.
3. The Monitor shall serve for such time as is necessary to monitor Respondent DaVita's compliance with the provisions of this Order, the Order to Maintain Assets, and the Divestiture Agreements.
4. Subject to any demonstrated legally recognized privilege, the Monitor shall have full and complete access to Respondent DaVita's personnel, books, documents, records kept in the Ordinary Course Of Business, facilities and technical information, and such other relevant information as the Monitor may reasonably request, related to Respondent DaVita's compliance with its obligations under this Order, the Order to Maintain Assets, and the Divestiture Agreements. Respondent DaVita shall cooperate with any reasonable request of the Monitor and shall take no action to interfere with or impede the Monitor's ability to monitor Respondent DaVita's compliance with this Order, the Order to Maintain Assets, and the Divestiture Agreements.
5. The Monitor shall serve, without bond or other security, at the expense of Respondent DaVita on such reasonable and customary terms and conditions as the Commission may set. The Monitor shall have authority to employ, at the expense of Respondent DaVita, such consultants, accountants, attorneys and other representatives and assistants as are reasonably necessary to carry out the Monitor's duties and responsibilities. The Monitor shall account for all expenses incurred, including fees for services rendered, subject to the approval of the Commission.
6. Respondent DaVita shall indemnify the Monitor and hold the Monitor harmless against any losses, claims, damages, liabilities, or expenses arising out

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of, or in connection with, the performance of the Monitor's duties, including all reasonable fees of counsel and other reasonable expenses incurred in connection with the preparations for, or defense of, any claim, whether or not resulting in any liability, except to the extent that such losses, claims, damages, liabilities, or expenses result from misfeasance, gross negligence, willful or wanton acts, or bad faith by the Monitor.

7. Respondent DaVita shall report to the Monitor in accordance with the requirements of this Order and/or as otherwise provided in any agreement approved by the Commission. The Monitor shall evaluate the reports submitted to the Monitor by Respondent DaVita, and any reports submitted by the Acquirer with respect to the performance of Respondent DaVita's obligations under this Order, the Order to Maintain Assets, and the Divestiture Agreements.
 8. Within one (1) month from the date the Monitor is appointed pursuant to this paragraph, every sixty (60) days thereafter, and otherwise as requested by the Commission, the Monitor shall report in writing to the Commission concerning performance by Respondent DaVita of its obligations under this Order, the Order to Maintain Assets, and the Divestiture Agreements.
 9. Respondent DaVita may require the Monitor and each of the Monitor's consultants, accountants, attorneys, and other representatives and assistants to sign a customary confidentiality agreement; *provided, however*, such agreement shall not restrict the Monitor from providing any information to the Commission.
- E. The Commission may, among other things, require the Monitor and each of the Monitor's consultants, accountants, attorneys, and other representatives and

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assistants to sign an appropriate confidentiality agreement Relating To Commission materials and information received in connection with the performance of the Monitor's duties.

- F. If the Commission determines that the Monitor has ceased to act or failed to act diligently, the Commission may appoint a substitute Monitor in the same manner as provided in this Paragraph IV.
- G. The Commission may on its own initiative, or at the request of the Monitor, issue such additional orders or directions as may be necessary or appropriate to assure compliance with the requirements of this Order, the Order to Maintain Assets, and the Divestiture Agreements.
- H. A Monitor appointed pursuant to this Order may be the same Person appointed as a trustee pursuant to Paragraph V of this Order and may be the same Person appointed as Monitor under the Order to Maintain Assets.

V.**IT IS FURTHER ORDERED** that:

- A. If Respondent DaVita has not divested, absolutely and in good faith and with the Commission's prior approval, all of the Appendix A Assets pursuant to Paragraph II of this Order, the Commission may appoint a trustee to (1) divest any of the Appendix A Assets that have not been divested pursuant to Paragraph II of this Order in a manner that satisfies the requirements of Paragraph II of this Order, which may include negotiations with landlords holding leases to the Assets to be Divested; or, in the event the Appendix A Clinics cannot be divested for whatever reason, (2) divest selected Appendix F Clinic Assets at the option of the Divestiture Trustee and the Commission. In the event that the Commission or the

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Attorney General brings an action pursuant to Section 5(l) of the Federal Trade Commission Act, 15 U.S.C. § 45(l), or any other statute enforced by the Commission, Respondent DaVita shall consent to the appointment of a trustee in such action to divest the relevant assets in accordance with the terms of this Order. Neither the appointment of a trustee nor a decision not to appoint a trustee under this Paragraph shall preclude the Commission or the Attorney General from seeking civil penalties or any other relief available to it, including a court appointed trustee, pursuant to § 5(l) of the Federal Trade Commission Act, or any other statute enforced by the Commission, for any failure by Respondent DaVita to comply with this Order.

- B. The Commission shall select the trustee, subject to the consent of Respondent DaVita, which consent shall not be unreasonably withheld. The trustee shall be a Person with experience and expertise in acquisitions and divestitures. If Respondent DaVita has not opposed, in writing, including the reasons for opposing, the selection of any proposed trustee within ten (10) days after receipt of notice by the staff of the Commission to Respondent DaVita of the identity of any proposed trustee, Respondent DaVita shall be deemed to have consented to the selection of the proposed trustee.
- C. Within ten (10) days after appointment of a trustee, Respondent DaVita shall execute a trust agreement that, subject to the prior approval of the Commission, transfers to the trustee all rights and powers necessary to permit the trustee to effect the divestitures required by this Order.
- D. If a trustee is appointed by the Commission or a court pursuant to this Order, Respondent DaVita shall consent to the following terms and conditions regarding the trustee's powers, duties, authority, and responsibilities:

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1. Subject to the prior approval of the Commission, the trustee shall have the exclusive power and authority to divest any of the Appendix A Assets that have not been divested pursuant to Paragraph II of this Order and, subject to the provisions of Paragraph V.A. of the Order, divest Appendix F Clinic Assets.
2. The trustee shall have twelve (12) months from the date the Commission approves the trust agreement described herein to accomplish the divestiture, which shall be subject to the prior approval of the Commission. If, however, at the end of the twelve (12) month period, the trustee has submitted a divestiture plan or the Commission believes that the divestiture can be achieved within a reasonable time, the divestiture period may be extended by the Commission; *provided, however*, the Commission may extend the divestiture period only two (2) times.
3. Subject to any demonstrated legally recognized privilege, the trustee shall have full and complete access to the personnel, books, records, and facilities related to the relevant assets that are required to be divested by this Order and to any other relevant information, as the trustee may request. Respondent DaVita shall develop such financial or other information as the trustee may request and shall cooperate with the trustee. Respondent DaVita shall take no action to interfere with or impede the trustee's accomplishment of the divestiture. Any delays in divestiture caused by Respondent DaVita shall extend the time for divestiture under this Paragraph V in an amount equal to the delay, as determined by the Commission or, for a court appointed trustee, by the court.

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4. The trustee shall use commercially reasonable best efforts to negotiate the most favorable price and terms available in each contract that is submitted to the Commission, subject to Respondent DaVita's absolute and unconditional obligation to divest expeditiously and at no minimum price. The divestiture shall be made in the manner and to an Acquirer or Acquirers that receives the prior approval of the Commission, as required by this Order; *provided, however*, if the trustee receives bona fide offers for particular assets from more than one acquiring entity, and if the Commission determines to approve more than one such acquiring entity for such assets, the trustee shall divest the assets to the acquiring entity selected by Respondent DaVita from among those approved by the Commission; *provided, further, however*, that Respondent DaVita shall select such entity within five (5) days of receiving notification of the Commission's approval.

5. The trustee shall serve, without bond or other security, at the cost and expense of Respondent DaVita, on such reasonable and customary terms and conditions as the Commission or a court may set. The trustee shall have the authority to employ, at the cost and expense of Respondent DaVita, such consultants, accountants, attorneys, investment bankers, business brokers, appraisers, and other representatives and assistants as are necessary to carry out the trustee's duties and responsibilities. The trustee shall account for all monies derived from the divestiture and all expenses incurred. After approval by the Commission and, in the case of a court appointed trustee, by the court, of the account of the trustee, including fees for the trustee's services, all remaining monies shall be paid at the direction of Respondent DaVita, and the trustee's power shall be terminated. The compensation of the trustee shall be based at least in significant part on a

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commission arrangement contingent on the divestiture of all of the relevant assets that are required to be divested by this Order.

6. Respondent DaVita shall indemnify the trustee and hold the trustee harmless against any losses, claims, damages, liabilities, or expenses arising out of, or in connection with, the performance of the trustee's duties, including all reasonable fees of counsel and other expenses incurred in connection with the preparation for, or defense of, any claim, whether or not resulting in any liability, except to the extent that such losses, claims, damages, liabilities, or expenses result from misfeasance, gross negligence, willful or wanton acts, or bad faith by the trustee.
 7. The trustee shall have no obligation or authority to operate or maintain the relevant assets required to be divested by this Order.
 8. The trustee shall report in writing to Respondent DaVita and to the Commission every sixty (60) days concerning the trustee's efforts to accomplish the divestiture.
 9. Respondent DaVita may require the trustee and each of the trustee's consultants, accountants, attorneys, and other representatives and assistants to sign a customary confidentiality agreement; *provided, however*, such agreement shall not restrict the trustee from providing any information to the Commission.
- E. If the Commission determines that a trustee has ceased to act or failed to act diligently, the Commission may appoint a substitute trustee in the same manner as provided in this Paragraph V.
- F. The Commission or, in the case of a court appointed trustee, the court, may on its own initiative or at the

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request of the trustee issue such additional orders or directions as may be necessary or appropriate to accomplish the divestiture required by this Order.

- G. The trustee appointed pursuant to this Paragraph may be the same Person appointed as the Monitor pursuant to the relevant provisions of this Order or the Order to Maintain Assets.

VI.**IT IS FURTHER ORDERED** that:

- A. Beginning thirty (30) days after the date this Order becomes final, and every thirty (30) days thereafter until Respondent DaVita has fully complied with Paragraphs II.A., II.B., II.C., II.D., II.E., II.G.1, II.I, II.K., II.L., II.M., II.N., and II.O. of this Order, Respondent DaVita shall submit to the Commission a verified written report setting forth in detail the manner and form in which it intends to comply, is complying, and has complied with the terms of this Order, the Order to Maintain Assets, and the Divestiture Agreements. Respondent DaVita shall submit at the same time a copy of these reports to the Monitor.
- B. Beginning twelve (12) months after the date this Order becomes final, and annually thereafter on the anniversary of the date this Order becomes final, for the next four (4) years, Respondent DaVita shall submit to the Commission verified written reports setting forth in detail the manner and form in which it is complying and has complied with this Order, the Order to Maintain Assets, and the Divestiture Agreements. Respondent DaVita shall submit at the same time a copy of these reports to the Monitor.

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VII.

IT IS FURTHER ORDERED that Respondent DaVita shall notify the Commission at least thirty (30) days prior to:

- A. Any proposed dissolution of DaVita,
- B. Any proposed acquisition, merger or consolidation of DaVita, or
- C. Any other change in DaVita that may affect compliance obligations arising out of this Order, including but not limited to assignment, the creation or dissolution of subsidiaries, or any other change in DaVita.

VIII.

IT IS FURTHER ORDERED that, for the purpose of determining or securing compliance with this Order, and subject to any legally recognized privilege, and upon written request with reasonable notice to Respondent DaVita, Respondent DaVita shall permit any duly authorized representative of the Commission:

- A. Access, during office hours of DaVita and in the presence of counsel, to all facilities and access to inspect and copy all books, ledgers, accounts, correspondence, memoranda, and all other records and documents in the possession or under the control of DaVita related to compliance with this Order; and
- B. Upon five (5) days' notice to DaVita and without restraint or interference from DaVita, to interview officers, directors, or employees of DaVita, who may have counsel present, regarding such matters.

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IX.

IT IS FURTHER ORDERED that this Order shall terminate on October 21, 2021.

By the Commission.

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APPENDIX A-1**CLINICS**

	Clinic Name	Clinic Address
1	DSI Norwood	1424 North Carraway Boulevard Birmingham, AL 35234
2	DSI Avondale	13055 West McDowell Road Avondale, AZ 85323
3	DSI Mesa	1337 South Gilbert Road, #109 Mesa, AZ 85204
4	DSI Northeast Phoenix	3305 East Greenway Road Phoenix, AZ 85032
5	DSI Phoenix South	4621 South Central Avenue Phoenix, AZ 85040
6	DSI Southwest Mesa	1457 West Southern Avenue, Ste. D19 Mesa, AZ 85202
7	DSI Tempe	8820 South Kyrene Road Tempe, AZ 85284
8	DSI South Tampa	731 West Lumsden Brandon, FL 33511
9	DSI Tampa Central	4705 N. Armenia Avenue Tampa, FL 33603
10	DaVita Woodstock	2001 Professional Pkwy, Ste. 100 Woodstock, GA 30188
11	DSI Covington	4179 Baker Street NE Covington, GA 30014
12	DSI Cobb County	506 Roswell Street, Bldg. 100 Marietta, GA 30060
13	DSI Scottsdale	4651 West 79 th Street, Unit 100 Chicago, IL 60652
14	DSI Greenwood	125 Airport Parkway, Suite 140 Greenwood, IN 46143

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	Clinic Name	Clinic Address
15	DSI Northwest Indianapolis	6488 Corporate Drive Indianapolis, IN 46278
16	DSI Louisville	635 S. 3 rd Street Louisville, KY 40202
17	DaVita Baton Rouge	3888 North Blvd. Baton Rouge, LA 70806
18	DaVita Denham Springs	26737 Highway 1032 Denham Springs, LA 70726
19	DSI Pleasantburg	110 Chalmers Road Greenville, SC 29605
20	DSI Easley	125 Whitmire Road Easley, SC 29640
21	DSI Greenville	3 Butternut Drive, Ste. A Greenville, SC 29605
22	DSI Powderhorn	16 Powderhorn Road Simpsonville, SC 29681
23	DSI Galleria	8592 Ricky Bell Cove Memphis, TN 38133
24	DSI Memphis South	3960 Knight Arnold Road, Ste. 107 Memphis, TN 38118
25	DaVita Beeville	100 W. Huntington Street Beeville, TX 78102
26	DSI El Paso East	10737 Gateway West, Ste. 100-101 El Paso, TX 79935
27	DSI El Paso West	3100 North Stanton El Paso, TX 79902
28	DSI El Paso South (<i>de novo</i>)	10651N. Loop Rd. El Paso, TX 79927
29	DaVita Oso Bay	7502 South Padre Island Dr. Corpus Christi, TX 78412

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APPENDIX A-2**JOINT VENTURES**

(Joint Ventures From Which DaVita Will Divest Its Joint Venture
Equity Interests and Clinics Owned by Joint Ventures)

	Joint Venture Name	Clinic Name (Medicare Provider Number)	Clinic Address
1	Renal Care Group South Tampa, LLC	South Tampa (102824)	731 W Lumsden Road, Brandon, FL 33511
2	DSI El Paso, LLC	El Paso Kidney Center East (452749)	10737 Gateway West, Suite 100, El Paso, TX 79935
3	Renal Care Group Galleria, LLC	Galleria Renal Center (442660)	8592 Ricky Bell Cove, Memphis, TN 38113
4	DSI Greenville, LLC	Twin Oaks Dialysis - Greenville (422503)	3 Butternut Drive, Greenville, SC 29605

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APPENDIX B**AREA DEFINITIONS TO APPENDIX A****AREA DEFINITIONS**

- Five digit numbers refer to zip codes.
- Geographic areas bounded by roads include all properties abutting the referenced road (*i.e.*, properties on both sides of the road).
- Zip codes or other areas fully surrounded by areas included in the area definition shall be considered part of the area definition.
- Area definitions are based on maps submitted to the Commission staff by DaVita.

	Divested Clinics (Medicare Provider Numbers)	Corresponding Area Definition
1	DSI Norwood	The area in and/or near Birmingham, Alabama, consisting of: 35203, 35204, 35205, 35206, 35207, 35208, 35211, 35212, 35213, 35214, 35215, 35217, 35218, 35222, 35233, 35234, 35254, and the portion of 35224 that lies east of County Road 65, southeast of Lexington Street, southeast of 8 th Avenue, southeast of Richmond Street, southeast of 10 th Avenue, east of 57 th Street, and north of Ens-Pleasant Grove Road.
2	DVA Osceola	The area in and/or near Osceola, Arkansas, consisting of Mississippi County (Arkansas).
3	DSI Avondale	The area in and/or near Avondale, Arizona, consisting of: 85031, 85033, 85035, 85037, 85043, 85323, 85353, 85392, 85395, the portion of 85326 that lies east of North 195 th Avenue, east of South 195 th Avenue, and north of the Gila River, the portion of 85338 that lies north of the Gila River, the portion of 85340 that lies south of West Camelback Road and east of North 195 th Avenue, and the portion of 85396 that lies east of North 195 th Avenue.
4	DSI NE Phoenix	The area in and/or near Phoenix, Arizona, consisting of:

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		85012, 85013, 85014, 85015, 85017, 85020, 85021, 85022, 85023, 85024, 85028, 85029, 85032, 85050, 85051, 85254, the portions of 85007, 85003, and 85004 that lie north of Interstate 10, the portion of 85006 that lies north of Interstate 10 and west of Highway 51, the portion of 85009 that lies north of Interstate 10 and east of Interstate 17 and the portion of 85027 that lies east of Interstate 17.
5	DSI South Phoenix	The area in and/or near Phoenix, Arizona, consisting of: 85003, 85004, 85006, 85007, 85008, 85009, 85012, 85013, 85014, 85015, 85016, 85018, 85034, 85035, 85040, 85041, 85042, 85043; and the portion of 85339 that lies east of S 79 th Avenue, north of Dobbins Road, east of W. Carver Road, and east of S 51 st Avenue.
6	DSI Mesa, Southwest Mesa, Tempe	The area in and/or near Mesa, Arizona consisting of: 85040, 85042, 85044, 85201, 85202, 85203, 85204, 85205, 85206, 85210, 85213, 85224, 85225, 85233, 85234, 85236, 85248, 85249, 85281, 85282, 85283, 85284, 85286, 85287, 85295, 85296, and the portion of 85226 that lies east of Interstate 10.
7	DSI South Tampa	The area in and/or near Brandon, Florida, consisting of: 33510, 33511, 33527, 33534, 33569, 33578, 33584, 33594, 33596, 33610, and 33619.
8	DSI Tampa	The area in and/or near Tampa, Florida, consisting of: 33602, 33603, 33604, 33605, 33606, 33607, 33609, 33610, 33611, 33612, 33613, 33614, 33615, 33616, 33617, 33619, 33624, 33625, 33626, 33629, 33634, and 33635.
9	DSI Cobb County	The area in and/or near Marietta, Georgia consisting of: 30008, 30060, 30062, 30064, 30066, 30067, 30101, 30102, 30144, 30152, and the portion of 30080 that lies north of Windy Hill Road SE.
10	DVA Woodstock	The area in and/or near Woodstock, Georgia consisting of: 30066, 30101, 30102, 30107, 30114, 30115, 30152, 30188, and 30189.
11	DSI Covington	The area in and/or near Covington, Georgia consisting of: 30012, 30013, 30014, 30016, 30025, 30054, and 30094.
12	DSI Scottsdale	The area in and/or near Chicago, Illinois consisting of: 60453, 60455, 60456, 60457, 60458, 60459, 60609, 60617, 60619, 60620, 60621, 60628, 60629, 60632, 60636, 60638, 60643, 60652, 60655, and 60805.
	DSI Greenwood	The area in and/or near Indianapolis, Indiana consisting of:

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13		46142, 46143, 46131, 46184, and the portions of 46217, 46221, 46227, 46237, 46239, and 46259 that lie to the south of Interstate 74.
14	DSI Northwest Indianapolis	The area in and/or near Indianapolis, Indiana consisting of 46214, 46222, 46224, 46228, the portion of 46278 that lies to the east of Interstate 65; the portions 46268, and 46260 that lie to the south of Interstate 865/465, and the portion of 46077 that lies to the south of Interstate 865/465 and east of Interstate 65.
15	DSI Louisville	The area in and/or near Louisville, Kentucky consisting of: 40202, 40203, 40204, 40205, 40206, 40209, 40209, 40210, 40211, 40212, 40215, 40214, 40216, 40258, 40292, and the portion of 40231 that lies to the north of Interstate 264.
16	DVA Baton Rouge 2230	The area in and/or near Baton Rouge, Louisiana consisting of: 70706, 70726, 70739, 70767, 70785, 70801, 70802, 70803, 70805, 70806, 70807, 70808, 70806, 70809, 70812, 70815, 70816, and 70817.
17	DSI Easley, Greenville, Pleasantburg, Powderhorn	The area in and/or near Greenville, South Carolina consisting of: 29625, 29660, 29601, 29605, 29607, 29609, 29611, 29613, 29615, 29617, 29630, 29640, 29642, 29644, 29645, 29657, 29661, 29662, 29669, 29671, 29673, 29680, 29681, and the portion of 29687 that lies south of State Highway 290 and S-23-415.
18	DSI Galleria	The area in and/or near Memphis, Tennessee consisting of: 38002, 38016, 38018, 38068, 38120, 38125, 38127, 38128, 38133, 38134, and 38135.
19	DSI Memphis South:	The are in and/or near Memphis, Tennessee, consisting of: 38111, 38114, 38115, 38117, 38118, 38141, and 38152.
20	DVA Beeville 2245	The area in and/or near Beeville, Texas consisting of: 78102, 78389, 78391. the portion of 77963 that lies south of State Highway 239 and west of US-77, the portion of 78022 that lies east of I-37, the portion of 78071 that lies east of I-37 and State Highway 72, the portion of 78119 that lies south of State Highway 72 and State Highway 239, the portion of 78368 that lies east of I-37, and the portions of 78377, 78378 and 78391 that lie west of US-77.
21	DVA Oso Bay 2219	The area in and/or near Corpus Christi, Texas consisting of: 78401, 78402, 78404, 78405, 78407, 78411, 78413, 78414, 78415, 78416, 78417, 78418, and 78419.

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22	DSI El Paso W and El Paso E	The area in and/or near El Paso, Texas consisting of: 88063, 79836, 79838, 79853, 79901, 79902, 79903, 79905, 79907, 79912, 79922, 79927, 79930, 79932, 79968, and the portions of 79821 and 79835 that lie to the west of E.P.N.G. Pipeline Rd., the portions of 79904 and 79924 that lie to the east of US-54, the portions of 79925, 79935 and 79936 that lie to the south of US-62, and the portions of 79928 and 79938 that are within El Paso County (Texas), Texas.
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CONFIDENTIAL APPENDIX C

**[Redacted From the Public Record Version, But Incorporated
By Reference]**

Decision and Order

CONFIDENTIAL APPENDIX D

**[Redacted From the Public Record Version, But Incorporated
By Reference]**

CONFIDENTIAL APPENDIX E

**[Redacted From the Public Record Version, But Incorporated
By Reference]**

Decision and Order

CONFIDENTIAL APPENDIX F

**[Redacted From the Public Record Version, But Incorporated
By Reference]**

CONFIDENTIAL APPENDIX F-2

**[Redacted From the Public Record Version, But Incorporated
By Reference]**

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CONFIDENTIAL APPENDIX G

**[Redacted From the Public Record Version, But Incorporated
By Reference]**

Order to Maintain Assets

ORDER TO HOLD SEPARATE AND MAINTAIN ASSETS

The Federal Trade Commission (“Commission”), having initiated an investigation of the proposed acquisition by DaVita Inc. of CDSI I Holding Company, Inc. (“DSI”), and DaVita Inc. (hereafter referred to as “Respondent DaVita”) having been furnished thereafter with a copy of a draft of Complaint that the Bureau of Competition proposed to present to the Commission for its consideration and which, if issued by the Commission, would charge Respondent DaVita with violations of Section 7 of the Clayton Act, as amended, 15 U.S.C. § 18, and Section 5 of the Federal Trade Commission Act, as amended, 15 U.S.C. § 45; and

Respondent DaVita, its attorneys, and counsel for the Commission having thereafter executed an Agreement Containing Consent Orders (“Consent Agreement”), containing an admission by Respondent DaVita of all the jurisdictional facts set forth in the aforesaid draft of Complaint, a statement that the signing of said Consent Agreement is for settlement purposes only and does not constitute an admission by Respondent DaVita that the law has been violated as alleged in such Complaint, or that the facts as alleged in such Complaint, other than jurisdictional facts, are true, and waivers and other provisions as required by the Commission’s Rules; and

The Commission, having thereafter considered the matter and having determined that it had reason to believe that Respondent has violated the said Acts, and that a Complaint should issue stating its charges in that respect, and having accepted the executed Consent Agreement and placed such Consent Agreement on the public record for a period of thirty (30) days for the receipt and consideration of public comments, now in further conformity with the procedure described in Commission Rule 2.34, 16 C.F.R. § 2.34, the Commission hereby issues its Complaint, makes the following jurisdictional findings, and issues the following Order to Hold Separate and Maintain Assets (“Hold Separate Order”):

1. Respondent DaVita Inc. is a corporation organized, existing and doing business under and by virtue of the laws of the State of Delaware with its office and

Order to Maintain Assets

principal place of business located at 1551 Wewatta St. Denver, Colorado 80202.

2. The Federal Trade Commission has jurisdiction of the subject matter of this proceeding and of Respondent DaVita, and the proceeding is in the public interest.

ORDER**I.**

IT IS ORDERED that all capitalized terms used in this Hold Separate Order, but not defined herein, shall have the meanings attributed to such terms in the Decision and Order contained in the Consent Agreement. In addition to the definitions in Paragraph I of the Decision and Order attached to the Agreement Containing Consent Orders, the following definitions shall apply:

- A. “DaVita Clinics” means the DaVita-owned Clinics listed in Appendix A to the Decision and Order and the DaVita Clinics in Non-Public Appendix F to the Decision and Order.
- B. “Decision and Order” means:
 1. the Proposed Decision and Order contained in the Consent Agreement in this matter until the issuance of a final Decision and Order by the Commission; and
 2. the Final Decision and Order issued and served by the Commission.
- C. “Divestiture Date” means the earliest date on which all of the of the divestitures required by the Decision and Order have been completed.
- D. “Hold Separate Period” means the time from the Effective Date until one day after the Divestiture Date.

Order to Maintain Assets

- E. “Hold Separate Trustee” means the person appointed pursuant to Paragraph III of this Hold Separate Order.
- F. “Monitor” means any monitor appointed pursuant to Paragraph VII of this Hold Separate Order.
- G. “Orders” means the Decision and Order and this Order to Hold Separate and Maintain Assets.

II. (Asset Maintenance)**IT IS FURTHER ORDERED** that:

- A. From the date Respondent DaVita signs the Consent Agreement until the Divestiture Date, Respondent DaVita shall:
 - 1. Maintain each of the DaVita Clinics and all Assets Associated with such Clinics in substantially the same condition (except for normal wear and tear) existing at the time Respondent DaVita signs the Consent Agreement;
 - 2. Take such actions that are consistent with the past practices of Respondent DaVita in connection with each of the DaVita Clinics and the Assets Associated with each and that are taken in the Ordinary Course Of Business and in the normal day today operations of Respondent DaVita;
 - 3. Keep available the services of the current officers, employees, and agents of Respondent DaVita; and maintain the relations and good will with Suppliers, Payors, Physicians, landlords, patients, employees, agents, and others having business relations with the DaVita Clinics and the Assets Associated with them in the Ordinary Course Of Business;
 - 4. Preserve the DaVita Clinics and all Assets Associated with them as an ongoing businesses and

Order to Maintain Assets

not take any affirmative action, or fail to take any action within Respondent DaVita's control, as a result of which the viability, competitiveness, and marketability of the DaVita's Clinics or the Assets Associated with them would be diminished;

- B. From the date Respondent DaVita signs the Consent Agreement until the Divestiture Date, Respondent DaVita shall:
1. Not object to the sharing with the Acquirer the Payor and Supplier contract terms Relating To the Clinics To Be Divested: (i) if the Payor or Supplier consents in writing to such disclosure upon a request by the Acquirer, and (ii) if the Acquirer enters into a confidentiality agreement with Respondent DaVita not to disclose the information to any third party; and
 2. Cooperate with the Acquirer and assist the Acquirer, at no cost to the Acquirer, in obtaining all Third Party Approvals and Government Approvals For Divestiture, and all Government Approvals For Continued Operation, for each Clinic To Be Divested.
- C. The purposes of this Paragraph II are to: (1) preserve the DaVita Clinics as viable, competitive, and ongoing businesses until the divestitures required by the Decision and Order are achieved; (2) prevent interim harm to competition pending the relevant divestitures and other relief; and (3) help remedy any anticompetitive effects of the proposed DaVita-DSI Acquisition as alleged in the Commission's Complaint.

III. (DSI Hold Separate)

IT IS FURTHER ORDERED that:

- A. From the Effective Date until the until the Divestiture Date, Respondent DaVita shall hold the entirety of DSI

Order to Maintain Assets

separate, apart, and independent of Respondent DaVita. To hold DSI separate, Respondent DaVita shall, among other things:

1. Not offer DSI employees positions with Respondent DaVita, other than continuing the positions they have within DSI; and
2. Do nothing to prevent or discourage suppliers that, prior to the Effective Date, supplied goods and services to DSI from continuing to supply goods and services to DSI.

Provided, however, that Respondent DaVita may divest any of the Appendix A Clinics to the Acquirer during the Hold Separate Period once all the approvals for divestiture pursuant to the Consent Agreement have been satisfied.

- B. At any time after the Effective Date, the Commission may appoint a Hold Separate Trustee to assure that DSI is held separate from Respondent DaVita.
1. The Commission shall select the Hold Separate Trustee, subject to the consent of Respondent DaVita which consent shall not be unreasonably withheld. If Respondent DaVita has not opposed, in writing, including the reasons for opposing, the selection of a proposed Hold Separate Trustee within five (5) business days after notice by the staff of the Commission to Respondent DaVita of the identity of any proposed Hold Separate Trustee, Respondent DaVita shall be deemed to have consented to the selection of the proposed Hold Separate Trustee.
 2. Not later than five (5) business days after appointment of the Hold Separate Trustee, Respondent DaVita shall execute an agreement that, subject to the prior approval of the Commission, confers on the Hold Separate Trustee

Order to Maintain Assets

all the rights and powers necessary to permit the Hold Separate Trustee to perform his duties and responsibilities, pursuant to this Hold Separate Order and consistent with the purposes of this Hold Separate Order.

3. Not later than ten (10) business days after appointment of the Hold Separate Trustee, Respondent DaVita shall, pursuant to the Hold Separate Trustee Agreement, transfer to the Hold Separate Trustee all rights, powers, and authorities necessary to permit the Hold Separate Trustee to perform his/her duties and responsibilities, pursuant to this Hold Separate Order and consistent with the purposes of the Decision and Order.
4. Respondent DaVita shall consent to the following terms and conditions regarding the powers, duties, authorities, and responsibilities of the Hold Separate Trustee:
 - a. The Hold Separate Trustee shall have the responsibility, consistent with the terms of this Hold Separate Order and the Decision and Order, for monitoring the organization of DSI, for managing DSI through the Manager; for maintaining the independence of DSI; and for monitoring Respondent DaVita's compliance with its obligations pursuant to the Orders.
 - b. Subject to all applicable laws and regulations, the Hold Separate Trustee shall have full and complete access to all personnel, books, records, documents and facilities of DSI or to any other relevant information as the Hold Separate Trustee may reasonably request including, but not limited to, all documents and records kept by Respondent DaVita in the ordinary course of business that relate to DSI. Respondent DaVita shall develop such financial or other information as the Hold

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Separate Trustee may request and shall cooperate with the Hold Separate Trustee. Respondent DaVita shall take no action to interfere with or impede the Hold Separate Trustee's ability to monitor Respondent DaVita's compliance with the Orders or otherwise to perform his/her duties and responsibilities consistent with the terms of this Hold Separate Order.

- c. The Hold Separate Trustee shall have the authority to employ, at the cost and expense of Respondent DaVita, such consultants, accountants, attorneys, and other representatives and assistants as are reasonably necessary to carry out the Hold Separate Trustee's duties and responsibilities.
- d. The Commission may require the Hold Separate Trustee, and Persons hired by the Hold Separate Trustee, to sign an appropriate confidentiality agreement relating to Commission materials and information received in connection with performance of the Hold Separate Trustee's duties.
- e. Respondent DaVita may require the Hold Separate Trustee, and Persons hired by the Hold Separate Trustee, to sign a confidentiality agreement prohibiting the disclosure of any Confidential Business Information gained as a result of his or her role as Hold Separate Trustee to anyone other than the Commission.
- f. Thirty (30) days after the appointment of the Hold Separate Trustee pursuant to this Paragraph III.B., and every thirty (30) days thereafter until the Hold Separate Order terminates, the Hold Separate Trustee shall report in writing to the Commission concerning the efforts to accomplish the purposes of this

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Hold Separate Order. Included within that report shall be the Hold Separate Trustee's assessment of the extent to which the businesses comprising DSI are meeting (or exceeding) their projected goals as are reflected in operating plans, budgets, projections or any other regularly prepared financial statements.

- g. If the Hold Separate Trustee ceases to act or fails to act diligently and consistent with the purposes of this Hold Separate Order, the Commission may appoint a substitute Hold Separate Trustee consistent with the terms of this paragraph, subject to the consent of Respondent DaVita, which consent shall not be unreasonably withheld. If Respondent DaVita has not opposed, in writing, including the reasons for opposing, the selection of the substitute Hold Separate Trustee within five (5) business days after notice by the staff of the Commission to Respondent DaVita of the identity of any substitute Hold Separate Trustee, Respondent DaVita shall be deemed to have consented to the selection of the proposed substitute trustee. Respondent DaVita and the substitute Hold Separate Trustee shall execute a new Hold Separate Trustee Agreement, subject to the approval of the Commission, consistent with this Paragraph III.B.
- C. Before the Agreement Containing Consent is signed by Respondent DaVita, Respondent DaVita shall designate Leif Murphy to be Manager of DSI for the duration of the Hold Separate Period.
1. Respondent DaVita shall transfer all rights, powers, and authorities necessary to manage and maintain DSI, to the Manager.
 2. The Manager shall report directly and exclusively to the Hold Separate Trustee, if one is appointed,

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or otherwise to Commission staff, and shall manage DSI independently of the management of Respondent DaVita. The Manager shall not be involved, in any way, in the operations of the other businesses of Respondent DaVita during the term of this Hold Separate Order.

3. The Monitor will monitor the activities of the Manager and the operations of DSI during the Hold Separate Period.
4. The Manager shall have no financial interests (other than existing options and interests in securities of Respondent DaVita) affected by Respondent DaVita's revenues, profits or profit margins, except that the compensation of the Manager for managing DSI may include economic incentives dependent on the financial performance of DSI if there are also sufficient incentives for the Manager to operate DSI at no less than current rates of operation (including, but not limited to, current rates of production and sales) and to achieve the objectives of this Hold Separate Order.
5. The Manager shall make no material changes in the present operation of DSI except with the approval of the Hold Separate Trustee, in consultation with the Commission staff, or Commission staff.
6. The Manager shall have the authority, with the approval of the Hold Separate Trustee or Commission staff, to remove employees and replace them with others of similar experience or skills. If any person ceases to act or fails to act diligently and consistent with the purposes of this Hold Separate Order, the Manager, in consultation with the Hold Separate Trustee or Commission staff, may request Respondent DaVita to, and Respondent DaVita shall, appoint a substitute

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person, which person the Manager shall have the right to approve.

7. In addition to those employees within DSI, the Manager may employ such Persons as are reasonably necessary to assist the Manager in managing DSI.
 8. The Commission staff or the Hold Separate Trustee, in consultation with the Commission staff, shall be permitted, to remove the Manager for cause. Within fifteen (15) days after such removal of the Manager, Respondent DaVita shall appoint a replacement Manager, subject to the approval of the Commission, on the same terms and conditions as provided in Paragraph III.C. of this Hold Separate Order.
 9. In the event that the Manager ceases to act as Manager, then Respondent DaVita shall select substitute Manager(s), subject to the approval of the Hold Separate Trustee, if appointed, and Commission staff, and transfer to the substitute Manager(s) all rights, powers and authorities necessary to permit the substitute Manager(s) to perform his/her/their duties and responsibilities, pursuant to this Hold Separate Order.
- D. No later than five (5) days after this Hold Separate Order becomes final, Respondent DaVita shall circulate to the DSI management and regional managers a copy of this Hold Separate Order and the Consent Agreement with the Commission's press release and analysis to aid public comment.
- E. The purposes of this Paragraph III are to: (1) preserve DSI as a viable, competitive, and ongoing business independent of Respondent DaVita until the divestitures required by the Decision and Order is achieved; (2) assure that no Confidential Business Information is exchanged between Respondent DaVita

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and DSI, except in accordance with the provisions of this Hold Separate Order; (3) prevent interim harm to competition pending the relevant divestitures and other relief; and (4) help remedy any anticompetitive effects of the proposed DaVita-DSI Acquisition as alleged in the Commission's Complaint.

IV. (Acquisition Requirements)**IT IS FURTHER ORDERED** that:

- A. Respondent DaVita shall not acquire DSI until it has obtained for all the Appendix A Clinics:
1. all approvals for the assignment of the Clinic's Physician Contracts, as required by Paragraph II.C.3.b. of the Decision and Order;
 2. all approvals by joint venture partners necessary for the Acquirer to acquire the Appendix A Clinics that are owned by a joint venture, and shall assign all such approvals to the Acquirer; and
 3. all approvals by joint venture partners necessary for the Acquirer of Appendix A Joint Venture Equity Interests to jointly own and operate the Appendix A Clinics that are owned by the joint venture, and shall assign all such approvals to the Acquirer.

Copies of all such approvals shall be incorporated into the Divestiture Agreements as appendices.

- B. Respondent DaVita shall not acquire DSI until it has:
1. included, as part of the Divestiture Agreements, a letter stating that the Osceola Non-Compete is rescinded and that it will not be re-entered or re-negotiated for five (5) years following the Time of Divestiture; and

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2. provided notice to all parties involved in the Osceola Non-Compete that the Osceola Non-Compete has been rescinded.

V. (Divestiture Requirements)

IT IS FURTHER ORDERED that at the Time Of Divestiture of each Clinic To Be Divested Respondent shall:

- A. assign to the Acquirer all rights, title, and interest to leases for the Real Property Of The Clinic, and shall obtain all approvals necessary for such assignments; *provided, however*, that (1) if the Acquirer obtains all rights, title, and interest to a lease for Real Property Of A Clinic To Be Divested before the Assets To Be Divested are divested pursuant to Paragraph II.A. of the Decision and Order, and (2) the Acquirer certifies its receipt of such lease and attaches it as part of the Divestiture Agreement, then DaVita shall not be required to make the assignments for such Clinic To Be Divested as required by this Paragraph; and
- B. assign to the Acquirer all of the Clinic's Physician Contracts, and shall obtain all approvals necessary for such assignment; *provided, however*, that (1) if the Acquirer enters into a Clinic's Physician Contract for a Clinic To Be Divested before the Assets To Be Divested are divested pursuant to Paragraph II.A. of the Decision and Order, and (2) the Acquirer certifies its receipt of such contract and attaches it as part of the Divestiture Agreement, then Respondent DaVita shall not be required to make the assignment for such Clinic To Be Divested as required by this Paragraph.

VI. (Facilitate Hiring)

IT IS FURTHER ORDERED that from the time Respondent DaVita signs the Agreement Containing Consent Order until sixty (60) days after the Time Of Divestiture of each Clinic To Be Divested or until January 3, 2012, whichever is later,:

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- A. Respondent DaVita (which includes the Hold Separate Manager where applicable during the Hold Separate Period) shall:
1. if requested by the Acquirer, facilitate interviews between each Designated DaVita Employee and the Acquirer, and shall not discourage such employee from participating in such interviews;
 2. not interfere in employment negotiations between each Designated DaVita Employee and the Acquirer;
 3. not prevent, prohibit or restrict or threaten to prevent, prohibit or restrict the Designated DaVita Employee from being employed by the Acquirer, and shall not offer any incentive to the Designated DaVita Employee to decline employment with the Acquirer;
 4. cooperate with the Acquirer of the Clinic in effecting transfer of the Designated DaVita Employee to the employ of the Acquirer, if the Designated DaVita Employee accepts such offer of employment from the Acquirer;
 5. eliminate any contractual provisions or other restrictions that would otherwise prevent the Designated DaVita Employee from being employed by the Acquirer;
 6. eliminate any confidentiality restrictions that would prevent the Designated DaVita Employee who accepts employment with the Acquirer from using or transferring to the Acquirer any information Relating To the Operation Of The Clinic; and
 7. pay, for the benefit of any Designated DaVita Employee who accepts employment with the

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Acquirer, all accrued bonuses, vested pensions and other accrued benefits.

Provided, however, that if, at any time after the Time of Divestiture, the Acquirer gives Respondent DaVita an unsolicited list of employees from the Non Public Appendix G of the Decision and Order to whom the Acquirer does not intend to offer employment, then such employees may be hired by Respondent DaVita as full time employees without violating this Paragraph VI. *Provided, further, however,* that no earlier than fifteen (15) days after the Time of Divestiture, Respondent DaVita may submit a written request to the Acquirer identifying those persons from the Non Public Appendix G of the Decision and Order to whom Respondent DaVita wishes to offer full time employment; and if the Acquirer within fifteen (15) days of receipt of such request grants, in writing, such request, then Respondent DaVita may offer employment to such employees; but if the Acquirer within fifteen (15) days of receipt of such request either: (i) chooses to hire such employees, or (ii) chooses to defer a hiring decision and keep the requested employees on the Non Public Appendix G, then Respondent DaVita shall continue to comply with the terms of this Paragraph VI. with regard to such employees..

- B. With respect to each Physician who has provided services to a Clinic To Be Divested pursuant to any of the Clinic's Physician Contracts in effect at any time during the four (4) months preceding the Time Of Divestiture of the Clinic ("Contract Physician"), DaVita shall not offer any incentive to the Contract Physician, the Contract Physician's practice group, or other members of the Contract Physician's practice group to decline to provide services to the Clinic To Be Divested, and shall eliminate any confidentiality restrictions that would prevent the Contract Physician, the Contract Physician's practice group, or other members of the Contract Physician's practice group

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from using or transferring to the Acquirer of the Clinic To Be Divested any information Relating To the Operation Of The Clinic.

VII. (Confidentiality)

IT IS FURTHER ORDERED that:

- A. From the Effective Date until the Divestiture Date:
1. Respondent DaVita shall not permit any of its employees, officers, or directors to be involved in the operations of DSI, unless otherwise authorized by this Hold Separate Order.
 2. Respondent DaVita, and Respondent DaVita's or DSI's personnel operating DSI, shall retain and maintain all Confidential Business Information of DSI on a confidential basis, separate and apart from Respondent DaVita and, except as is requested by Respondent DaVita for purposes of the divestiture of the Appendix A Clinics as required by the Decision and Order, in this matter, such persons shall be prohibited from providing, discussing, exchanging, circulating, or otherwise furnishing any such information to Respondent DaVita or with Respondent DaVita's personnel.
 3. Respondent DaVita shall not, directly or indirectly, receive, disclose, or use any Confidential Business Information Related To DSI to any Person except the Appendix A Clinics Acquirer or other persons specifically authorized by the Appendix A Clinics Acquirer to receive such information, or than as necessary to comply with the following:
 - a. the requirements of the Orders
 - b. applicable laws and regulations.

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4. Respondent DaVita shall not provide, disclose or otherwise make available, directly or indirectly, any such Confidential Business Information related to the operation of DSI to Respondent DaVita's employees, other than those employees operating DSI pursuant to this Hold Separate Order.
 5. Respondent DaVita shall institute procedures and requirements to ensure that:
 - a. Confidential Business Information Related to DSI is not provided to, or obtained by, Respondent DaVita's employees, other than those employees operating DSI pursuant to this Hold Separate Order;
 - b. Respondent DaVita employees with access to Confidential Business Information Relating To DSI do not provide, disclose or otherwise make available, directly or indirectly, any Confidential Business Information in contravention of this Hold Separate Order; and
 - c. Respondent DaVita's employees, other than those employees operating DSI pursuant to this Hold Separate Order, do not solicit, access or use any Confidential Business Information that they are prohibited under this Hold Separate Order from receiving for any reason or purpose.
- B. From the Effective Date until the Divestiture Date, Respondent DaVita shall require any Persons with access to Confidential Business Information Relating To the DSI to not to disclose any Confidential Business Information Relating To DSI to Respondent DaVita or to any third party except as otherwise permitted by this Hold Separate Order.
- C. DaVita shall:

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1. not disclose Confidential Business Information relating exclusively to any of the Clinics To Be Divested to any Person other than the Acquirer of such Clinic;
 2. after the Time Of Divestiture of such Clinic:
 - a. DaVita shall not use Confidential Business Information relating exclusively to any of the Clinics To Be Divested for any purpose other than complying with the terms of this Order or with any law; and
 - b. DaVita shall destroy all records of Confidential Business Information relating exclusively to any of the Clinics To Be Divested , except to the extent that: (1) DaVita is required by law to retain such information, and (2) DaVita's inside or outside attorneys may keep one copy solely for archival purposes, but may not disclose such copy to the rest of DaVita.
- D. The purposes of this Paragraph IV are to: (1) preserve DSI as a viable, competitive, and ongoing business independent of Respondent DaVita until the divestitures required by the Decision and Order are achieved; (2) assure that no Confidential Business Information is exchanged between Respondent DaVita and DSI, except in accordance with the provisions of this Hold Separate Order; (3) prevent interim harm to competition pending the relevant divestitures and other relief; and (4) help remedy any anticompetitive effects of the proposed DaVita-DSI Acquisition as alleged in the Commission's Complaint.

VIII. (Monitor)**IT IS FURTHER ORDERED** that:

- A. Richard Shermer of R. Shermer & Co. shall be appointed Monitor to assure that Respondent DaVita

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expeditiously complies with all of its obligations and performs all of its responsibilities as required by this Hold Separate Order and the Decision and Order.

- B. No later than one (1) day after the Effective Date, Respondent DaVita shall, pursuant to the Monitor Agreement, attached as Appendix A and Confidential Appendix A-1, and to this Hold Separate Order, transfer to the Monitor all the rights, powers, and authorities necessary to permit the Monitor to perform their duties and responsibilities in a manner consistent with the purposes of this Hold Separate Order.
- C. In the event a substitute Monitor is required, the Commission shall select the Monitor, subject to the consent of Respondent DaVita, which consent shall not be unreasonably withheld. If Respondent DaVita has not opposed, in writing, including the reasons for opposing, the selection of a proposed Monitor within ten (10) days after notice by the staff of the Commission to Respondent DaVita of the identity of any proposed Monitor, Respondent DaVita shall be deemed to have consented to the selection of the proposed Monitor. Not later than ten (10) days after appointment of a substitute Monitor, Respondent DaVita shall execute an agreement that, subject to the prior approval of the Commission, confers on the Monitor all the rights and powers necessary to permit the Monitor to monitor Respondent DaVita's compliance with the terms of this Hold Separate Order, the Decision and Order, and the Divestiture Agreements in a manner consistent with the purposes of this Order.
- D. Respondent DaVita shall consent to the following terms and conditions regarding the powers, duties, authorities, and responsibilities of the Monitor:
 - 1. The Monitor shall have the power and authority to monitor Respondent DaVita's compliance with the terms of this Hold Separate Order, the Decision

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and Order, and the Divestiture Agreements, and shall exercise such power and authority and carry out the duties and responsibilities of the Monitor in a manner consistent with the purposes of this Order and in consultation with the Commission, including, but not limited to:

- a. Assuring that Respondent DaVita expeditiously complies with all of its obligations and perform all of its responsibilities as required by the this Hold Separate Order, the Decision and Order, and the Divestiture Agreements;
 - b. Monitoring any transition services agreements;
 - c. Assuring that Confidential Business Information is not received or used by Respondent DaVita or the Acquirer, except as allowed in this Hold Separate Order and in the Decision and Order, in this matter.
2. The Monitor shall act in a fiduciary capacity for the benefit of the Commission.
 3. The Monitor shall serve for such time as is necessary to monitor Respondent DaVita's compliance with the provisions of this Hold Separate Order, the Decision and Order, and the Divestiture Agreements.
 4. Subject to any demonstrated legally recognized privilege, the Monitor shall have full and complete access to Respondent DaVita's personnel, books, documents, records kept in the Ordinary Course Of Business, facilities and technical information, and such other relevant information as the Monitor may reasonably request, related to Respondent DaVita's compliance with its obligations under this Hold Separate Order, the Decision and Order, and the Divestiture Agreements. Respondent DaVita shall cooperate with any reasonable request of the

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Monitor and shall take no action to interfere with or impede the Monitor's ability to monitor Respondent DaVita's compliance with this Hold Separate Order, the Decision and Order, and the Divestiture Agreements.

5. The Monitor shall serve, without bond or other security, at the expense of Respondent DaVita on such reasonable and customary terms and conditions as the Commission may set. The Monitor shall have authority to employ, at the expense of Respondent DaVita, such consultants, accountants, attorneys and other representatives and assistants as are reasonably necessary to carry out the Monitor's duties and responsibilities. The Monitor shall account for all expenses incurred, including fees for services rendered, subject to the approval of the Commission.
6. Respondent DaVita shall indemnify the Monitor and hold the Monitor harmless against any losses, claims, damages, liabilities, or expenses arising out of, or in connection with, the performance of the Monitor's duties, including all reasonable fees of counsel and other reasonable expenses incurred in connection with the preparations for, or defense of, any claim, whether or not resulting in any liability, except to the extent that such losses, claims, damages, liabilities, or expenses result from misfeasance, gross negligence, willful or wanton acts, or bad faith by the Monitor.
7. Respondent DaVita shall report to the Monitor in accordance with the requirements of this Hold Separate Order and/or as otherwise provided in any agreement approved by the Commission. The Monitor shall evaluate the reports submitted to the Monitor by Respondent DaVita, and any reports submitted by the Acquirer with respect to the performance of Respondent DaVita's obligations

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under this Hold Separate Order, the Decision and Order, and the Divestiture Agreements.

8. Within one (1) month from the date the Monitor is appointed pursuant to this paragraph, every sixty (60) days thereafter, and otherwise as requested by the Commission, the Monitor shall report in writing to the Commission concerning performance by Respondent DaVita of its obligations under this Hold Separate Order, the Decision and Order, and the Divestiture Agreements.
 9. Respondent DaVita may require the Monitor and each of the Monitor's consultants, accountants, attorneys, and other representatives and assistants to sign a customary confidentiality agreement; *provided, however*, such agreement shall not restrict the Monitor from providing any information to the Commission.
- E. The Commission may, among other things, require the Monitor and each of the Monitor's consultants, accountants, attorneys, and other representatives and assistants to sign an appropriate confidentiality agreement Relating To Commission materials and information received in connection with the performance of the Monitor's duties.
- F. If the Commission determines that the Monitor has ceased to act or failed to act diligently, the Commission may appoint a substitute Monitor in the same manner as provided in this Paragraph VIII.
- G. The Commission may on its own initiative, or at the request of the Monitor, issue such additional orders or directions as may be necessary or appropriate to assure compliance with the requirements of this Hold Separate Order, the Decision and Order, and the Divestiture Agreements.

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- H. The Monitor appointed pursuant to this Order may be the same Person appointed as a Hold Separate Trustee pursuant to Paragraph IV of this Order and may be the same Person appointed as Monitor or Divestiture Trustee under the Decision and Order.

IX. (Compliance Reports)

IT IS FURTHER ORDERED that within thirty (30) days after the date this Hold Separate Order becomes final, and every sixty (60) days thereafter until the Hold Separate Order terminates, Respondent DaVita shall submit to the Commission a verified written report setting forth in detail the manner and form in which it intends to comply, is complying, and has complied with this Hold Separate Order and the related Decision and Order; *provided, however,* that, after the Decision and Order in this matter becomes final, the reports due under this Hold Separate Order shall be consolidated with, and submitted to the Commission at the same time as, the reports required to be submitted by Respondent DaVita pursuant to the Decision and Order.

X. (Change in DaVita)

IT IS FURTHER ORDERED that Respondent DaVita shall notify the Commission at least thirty (30) days prior to:

- A. Any proposed dissolution of DaVita,
- B. Any proposed acquisition, merger or consolidation of DaVita, or
- C. Any other change in DaVita that may affect compliance obligations arising out of this Order, including but not limited to assignment, the creation or dissolution of subsidiaries, or any other change in DaVita.

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XI. (Access)

IT IS FURTHER ORDERED that, for the purpose of determining or securing compliance with this Order, and subject to any legally recognized privilege, and upon written request with reasonable notice to Respondent DaVita, DaVita shall permit any duly authorized representative of the Commission:

- A. Access, during office hours of DaVita and in the presence of counsel, to all facilities and access to inspect and copy all books, ledgers, accounts, correspondence, memoranda, and all other records and documents in the possession or under the control of DaVita related to compliance with this Order; and
- B. Upon five (5) days' notice to DaVita and without restraint or interference from DaVita, to interview officers, directors, or employees of DaVita, who may have counsel present, regarding such matters.

XII. (Termination)

IT IS FURTHER ORDERED that this Hold Separate Order shall terminate on the earlier of:

- A. Three (3) days after the Commission withdraws its acceptance of the Consent Agreement pursuant to the provisions of Commission Rule 2.34, 16 C.F.R. § 2.34; or
- B. The latter of:
 - 1. the day after the divestitures pursuant to Paragraph II of the Decision and Order are accomplished, or
 - 2. the day after the Commission otherwise directs that this Hold Separate Order is terminated.

By the Commission.

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APPENDIX A

MONITOR AGREEMENT

MONITOR AGREEMENT

MONITOR AGREEMENT (the "Agreement"), dated as of August 11, 2011, between DaVita Inc ("Respondent") and Richard A. Shermier of R. Shermier & Company ("Monitors").

PRELIMINARY STATEMENT

WHEREAS the Federal Trade Commission (the "Commission") is considering for public comment an Agreement Containing Consent Orders with Respondent, which provides, among other things, that Respondent divest a number of dialysis clinics and assets associated with those clinics, enter into agreements – if necessary – providing the acquirers of the dialysis clinics with transition services, and engage a monitor to monitor Respondent's compliance with its obligations under the Decision and Order and Asset Maintenance Order ("Orders");

WHEREAS, the Commission is expected to issue the Agreement Containing Consent Orders and appoint the Monitors pursuant to the Orders to monitor Respondent's compliance with the terms of the Orders, and the Monitors have consented to such appointment;

WHEREAS, the Orders further provide that Respondent shall execute an agreement, subject to prior approval of the Commission, conferring all the rights and powers necessary to permit the Monitors to carry out their duties and responsibilities pursuant to the Orders;

WHEREAS, this Monitor Agreement, although executed by the Monitors and Respondent, is not effective for any purpose, including but not limited to imposing rights and responsibilities on Respondent or the Monitors under the Orders, until the Asset Maintenance Order has been issued and the Monitor Agreement has been approved by the Commission;

WHEREAS, the parties to this Agreement intend to be legally bound, subject only to the Commission's approval of this Agreement.

DEFINITIONS

1. "Respondent "DaVita" means DaVita Inc., a corporation organized, existing and doing business under and by virtue of the laws of the State of Delaware, with its office and principal place of business located at El Segundo, CA, its directors, officers, employees, agents, attorneys, representatives, predecessors, successors, and assigns; its joint ventures, divisions, groups and affiliates controlled by DaVita, and the respective directors, officers, employees, agents, attorneys, representatives, predecessors, successors, and assigns of each.
2. "Other Parties" means any Person that receives approval of the Commission to acquire any of the Assets To Be Divested or is a party to the Relevant Agreements pursuant to Paragraph II and V of the Decision and Order.
3. "Relevant Agreements" means: all the divestiture agreements and transition services agreements entered into pursuant to Paragraphs II and V of the Decision and Order, and the

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Transition Services Agreement between Frazier Healthcare, New Enterprise Associates, and DaVita.

4. All other capitalized words or phrases appearing in this Agreement that are not otherwise defined herein are deemed to have the defined meanings assigned to them in the Orders.

ARTICLE I

Powers of the Monitors. The Monitors shall have the rights, duties, powers and authority conferred upon the Monitor by the Orders that are necessary for the Monitors to monitor Respondent's compliance with the Orders. No later than one day after the Effective Date, Respondent hereby transfers to the Monitors all rights, powers, and authorities necessary to permit the Monitor to perform his duties and responsibilities pursuant to the Asset Maintenance Order and consistent with the purposes of the Decision and Order. Any descriptions thereof contained in this Agreement in no way modify the Monitors' powers and authority or Respondent's obligations under the Orders.

Monitor's Duties. The Monitors shall monitor Respondent's compliance with the Orders, including but not limited to:

- a. Assuring that Respondent expeditiously comply with all of their obligations and perform all of their responsibilities as required by the Orders in this matter;
- b. Monitoring Relevant Agreements;
- c. Assuring that Confidential Business Information is not received or used by Respondent or Other Parties, except as allowed in the Orders in this matter.

Duration of Monitor's Authority. The Monitors shall have all powers and duties described above and consistent with the Orders for the term set forth in the Orders.

Confidential and Proprietary Information. The Monitors shall enter into a confidentiality agreement, attached hereto as Confidential Exhibit A, agreeing to be bound by the terms and conditions of the Orders. The Monitors must retain and maintain all Material Confidential Information it receives from either Respondent or Relevant Parties on a confidential basis except as is permitted by the Orders. The Monitors may disclose confidential information only to persons employed by or working with the Monitors under this Agreement, to persons employed at the Commission, and as permitted by Respondent or Relevant Parties with respect to information they provided the Monitor. The Monitors shall require any person retained by the Monitor to assist in carrying out the duties and responsibilities of the Monitors to execute a confidentiality agreement that requires the same standard of care and obligations of confidentiality to which the Monitors must adhere under this Agreement. The Monitors shall maintain the confidentiality, for a period of five (5) years after the termination of this Agreement, of all other aspects of the performance of his duties under this Agreement and shall not disclose any confidential information relating thereto.

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Restrictions. The Monitors shall not be involved in any way in the management, production, supply and trading, sales marketing, and financial operations of the competing products of the Respondent.

Reports. Monitors shall report to the Commission pursuant to the terms of the Orders and as otherwise requested by the Commission staff.

Access to records, documents and facilities. Subject to any demonstrated legally recognized privilege, the Monitor shall have full and complete access to Respondent' personnel, to include those employees designated to be transferred to an acquirer, books, documents, records kept in the normal course of business, facilities and technical information, and such other relevant information as the Monitors may reasonably request, related to Respondent' compliance with their obligations under the Orders in this matter. Documents, records and other relevant information are to be provided in an electronic format if they exist in that form. Respondent shall cooperate with any reasonable request of the Monitors and shall take no action to interfere with or impede the Monitor's ability to monitor Respondent' compliance with the Orders.

ARTICLE II

Retention and payment of Counsel, Consultants, and other Assistants. The Monitors shall have the authority to employ, at the cost and expense of the Respondent, such attorneys, consultants, accountants, and other representatives and assistants as are necessary to carry out the Monitors' duties and responsibilities as allowed pursuant to the Orders.

1.1 Compensation. The Monitors shall be compensated by Respondent for his services under this Agreement, including all work in connection with the negotiation and preparation of this Monitor Agreement, pursuant to the fee schedule attached as Confidential Exhibit B for time spent in connection with the discharge of his duties under this Agreement and the Orders. In addition, Respondent will pay: (a) out-of-pocket expenses reasonably incurred by the Monitors in the performance of his duties under the Mandate; and (b) fees and disbursements reasonably incurred by any advisor appointed by the Monitors pursuant to the first paragraph in Article II. At its own expense, Respondent may retain an independent auditor to verify such invoices. The Monitors shall provide Respondent with monthly invoices for time and expenses that include details and an explanation of all matters for which the Monitors submit an invoice to Respondent. Respondent shall pay such invoices within thirty (30) days of receipt. The Monitor and Respondent shall submit any disputes about invoices to a mutually agreed upon third party for assistance in resolving such disputes.

1.2 To the extent available, Respondent will provide the Monitor with temporary workspace and access to office equipment owned or used by Respondent at sites the Monitor is required to visit in order to fulfill its obligations under this Agreement. Monitor agrees to comply with all of Respondents' safety and security regulations, instructions and procedures while at Respondents' sites.

ARTICLE III

1.1 Monitor's liabilities and indemnification. Respondent shall indemnify the Monitors and hold the Monitors harmless against any losses, claims, damages, liabilities, or

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expenses arising out of, or in connection with, the performance of the Monitors' duties, including all reasonable fees of counsel and other expenses incurred in connection with the preparation for, or defense of any claim, whether or not resulting in any liability, except to the extent that such losses, claims, damages, liabilities, or expenses result from gross negligence, willful or wanton acts, or bad faith by the Monitors. The Monitor's maximum liability to Respondents relating to services rendered in accordance with this Agreement (regardless of form of action, whether in contract, statutory law, or tort) shall be limited to an amount equal to the total sum of the fees paid to the Monitor by the Respondent. Any claim arising from this Agreement that Respondents may have against the Monitor must be brought no later than one (1) year following the termination or expiration of this Agreement. In the performance of its duties under this Agreement, the Monitor shall exercise the standard of care and diligence that would be expected of a reasonable person in the conduct of his own business affairs. The Monitor shall not be liable for any delays or other failures to perform resulting from circumstances or causes beyond its reasonable control, including, without limitation, fire or other casualty, act of God, strike or labor dispute, war or other violence, or any law, order or requirement of any governmental agency or authority. The Monitor warrants that it will perform its obligations hereunder in good faith. R. Shermer & Company disclaims other warranties, expressed or implied, other than those expressly agreed to in writing between the Parties.

Monitor's removal. If the Commission determines that Monitors cease to act or fail to act diligently and consistent with the purpose of the Orders, Respondent shall terminate this Agreement and appoint a substitute Monitor, subject to Commission approval and consistent with the Orders.

Approval by the Commission. This Agreement shall have no force or effect until approved by the Commission, other than Respondent obligations under Exhibit A and the confidentiality provisions herein.

Termination: This Agreement shall terminate the earlier of: (a) the date set forth in the Order, unless the Commission requires a final report or meeting with the Monitor, in which case, the Order will terminate thirty (30) days following the date set forth in the Order; (b) Respondent's receipt of written notice from the Commission that the Commission has determined that Richard Shermer has ceased to act or failed to act diligently, or are unwilling or unable to continue to serve as Monitor; (c) with at least thirty (30) days advance notice to be provided by the Monitor to Respondent and to the Commission, upon resignation of the Monitors; or (d) when DaVita's last obligation under the Orders and the Relevant Agreements that pertains to the Monitors' service has been fully performed, provided, however, that the Commission may require that DaVita extend this Monitor Agreement or enter into an additional agreement with the Monitors as may be necessary or appropriate to accomplish the purposes of the Orders. If this Monitor Agreement is terminated for any reason, the confidentiality obligations set forth in this Agreement will remain in force.

Conflicts of Interest: If the Monitors become aware during the term of this Agreement that he has or may have a conflict of interest that may affect or could have the appearance of affecting performance by the Monitor of any of his duties under this Agreement, the Monitors shall promptly inform Respondent and the Commission of any such conflict.

Order to Maintain Assets

APPENDIX A

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IN WITNESS WHEREOF, the parties hereto have caused this Agreement to be executed
as of the date first above written.

MONITORS

BY:

NAME: RICHARD A. SHERMER
R. Shermer & Company

RESPONDENT

BY:

NAME: David R. Finn
TITLE: Vice President

Order to Maintain Assets

CONFIDENTIAL APPENDIX A-1

**[Redacted From the Public Record Version, But Incorporated
By Reference]**

Analysis to Aid Public Comment

ANALYSIS OF CONSENT ORDER TO AID PUBLIC COMMENT

The Federal Trade Commission (“Commission”) has accepted, subject to final approval, an Agreement Containing Consent Orders (“Consent Agreement”) from DaVita Inc. (“DaVita”). The purpose of the Consent Agreement is to remedy the anticompetitive effects resulting from DaVita’s purchase of CDSI I Holding Company, Inc. (“DSI”). Under the terms of the Consent Agreement, DaVita is required to divest 28 dialysis clinics and terminate one management contract in 22 markets across the United States.

The Consent Agreement has been placed on the public record for 30 days to solicit comments from interested persons. Comments received during this period will become part of the public record. After 30 days, the Commission will again review the Consent Agreement and the comments received, and will decide whether it should withdraw from the Consent Agreement or make it final.

Pursuant to an agreement dated February 4, 2011, DaVita proposes to acquire DSI for approximately \$689 million. The Commission’s complaint alleges that the proposed acquisition, if consummated, would violate Section 7 of the Clayton Act, as amended, 15 U.S.C.

Commission Act, as amended, 15 U.S.C.

competition for the provision of outpatient dialysis services in 22 markets.

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The Parties

Headquartered in Denver, Colorado, DaVita is the second largest provider of outpatient dialysis services in the United States. DaVita operates 1,612 outpatient dialysis clinics in 42 states and the District of Columbia at which approximately 125,000 end stage renal disease (“ESRD”) patients receive treatment. In 2010 DaVita’s revenues were approximately \$7.63 billion.

Analysis to Aid Public Comment

DSI, headquartered in Nashville, Tennessee, is a privately held company and the fifth largest provider of outpatient dialysis services in the United States. DSI operates 106 dialysis centers, providing dialysis services to approximately 8,000 patients in 23 states.

Outpatient Dialysis Services

Outpatient dialysis services is the appropriate relevant product market in which to assess the effects of the proposed transaction. For patients suffering from ESRD, dialysis treatments are a life-sustaining therapy that replaces the function of the kidneys by removing toxins and excess fluid from the blood. Most ESRD patients receive dialysis treatments three times per week in sessions lasting between three and five hours. Kidney transplantation is the only alternative to dialysis for ESRD patients. However, the wait-time for donor kidneys – during which ESRD patients must receive dialysis treatments – can exceed five years. Additionally, many ESRD patients are not viable transplant candidates. As a result, many ESRD patients have no alternative to ongoing dialysis treatments.

The relevant geographic markets for the provision of dialysis services are local in nature. They are limited by the distance ESRD patients are willing and/or able to travel to receive dialysis treatments. Most ESRD patients are quite ill and suffer from multiple health problems. As such, it is difficult for ESRD patients to travel long distances for dialysis treatment. Generally, ESRD patients are unwilling and/or unable to travel further than 30 miles or 30 minutes to receive dialysis treatments, depending on traffic patterns, local geography, and the patient's proximity to the nearest center. As a result, competition among dialysis clinics occurs at a local level, corresponding to metropolitan areas or subsets thereof.

Entry into the outpatient dialysis services markets addressed by the Consent Agreement on a level sufficient to deter or counteract the likely anticompetitive effects of the proposed transaction is not likely to occur in a timely manner. The primary barrier to entry is the difficulty associated with locating nephrologists with established patient pools to serve as medical

Analysis to Aid Public Comment

directors. By law, each dialysis clinic must have a nephrologist medical director. As a practical matter, medical directors are essential to the success of a clinic because they are the primary source of referrals. The lack of available nephrologists with an established referral stream is a significant barrier to entry into each of the relevant markets. Beyond that, entry is also inhibited where certain attributes (such as a rapidly growing ESRD population, a favorable regulatory environment, average or below nursing and labor costs, and a low penetration of managed care) are not present, as is the case in many of the geographic markets identified in the Commission's complaint.

Each of the geographic markets addressed by the Consent Agreement is highly concentrated. The proposed acquisition represents a merger to monopoly in one market and would cause the number of providers to drop from three to two in fifteen other markets. Additionally, concentration increases significantly in the remaining six markets addressed by the Consent Agreement. In each of these markets, the post-acquisition HHI level exceeds 3,500, and the change in HHI is more than 170. The high post-acquisition concentration levels, along with the elimination of DaVita and DSI's head-to-head competition in these markets, indicates that the combined firm would be able to exercise unilateral market power. The evidence shows that health insurance companies and other private payors who pay for dialysis services used by their members benefit from direct competition between DaVita and DSI when negotiating rates charged by dialysis providers. As a result, the proposed combination likely would result in higher prices and diminished service and quality for outpatient dialysis services in many geographic markets.

The Consent Agreement

The Consent Agreement effectively remedies the proposed acquisition's anticompetitive effects in 22 markets where both DaVita and DSI operate dialysis clinics by requiring DaVita to divest -- prior to acquiring DSI -- 29 outpatient dialysis clinics to Dialysis Newco, Inc., a corporation formed by Frazier Healthcare and New Enterprise Associates ("Frazier/NEA").

Analysis to Aid Public Comment

As part of these divestitures, DaVita is required to obtain the agreement of the medical directors affiliated with the divested clinics to continue providing physician services after the transfer of ownership to Frazier/NEA. Similarly, the Consent Agreement requires DaVita to obtain the consent of all lessors necessary to assign the leases for the real property associated with the divested clinics to Frazier/NEA. These provisions ensure that Frazier/NEA will have the assets necessary to operate the divested clinics in a competitive manner.

The Consent Agreement contains several additional provisions designed to ensure that the divestitures are successful. First, the Consent Agreement provides Frazier/NEA with the opportunity to interview and hire employees affiliated with the divested clinics and prevents DaVita from offering these employees incentives to decline Frazier/NEA's offer of employment. This will ensure that Frazier/NEA has access to patient care and supervisory staff who are familiar with the clinics' patients and the local physicians. Second, the Consent Agreement prevents DaVita from contracting with the medical directors (or their practice groups) affiliated with the divested clinics for three years. This provides Frazier/NEA with sufficient time to build goodwill and a working relationship with its medical directors before DaVita can attempt to capitalize on its prior relationships in soliciting their services. Third, to ensure continuity of patient care and records as Frazier/NEA implements its quality care, billing, and supply systems, the Consent Agreement allows DaVita to provide transition services for a period of 12 months. Firewalls and confidentiality agreements have been established to ensure that competitively sensitive information is not exchanged. Fourth, the Consent Agreement requires DaVita to provide Frazier/NEA with a license to use DSI's policies, procedures, and medical protocols, as well as the option to obtain DaVita's medical protocols, which will further enhance Frazier/NEA's ability to provide continuity of care to patients. Finally, the Consent Agreement requires DaVita to provide prior notice to the Commission of its planned acquisitions of dialysis clinics located in the 22 markets addressed by the Consent Agreement. This provision ensures that subsequent acquisitions do not adversely impact competition in the markets at issue and undermine the remedial goals of the proposed order.

Analysis to Aid Public Comment

The Commission is satisfied that Frazier/NEA is a qualified acquirer of the divested assets. Dialysis Newco, Inc. is a newly-formed company whose management has experience operating, acquiring, integrating, and developing outpatient dialysis clinics. The company has received a substantial equity investment from Frazier, a firm with a dedicated focus on healthcare, and NEA, the world's largest venture capital firm with over \$10.5 billion under management.

The Commission has appointed Richard Shermer of R. Shermer & Co. as an Interim Monitor to oversee the transition service agreements, and the implementation of, and compliance with, the Consent Agreement. Mr. Shermer assists client companies undergoing regulator-mandated ownership transitions, including experience with transitions of outpatient dialysis clinics.

The purpose of this analysis is to facilitate public comment on the Consent Agreement, and it is not intended to constitute an official interpretation of the proposed Decision and Order or the Order to Maintain Assets, or to modify their terms in any way.

Opinion of the Commission

IN THE MATTER OF**THE NORTH CAROLINA BOARD OF DENTAL
EXAMINERS**

FINAL COMMISSION OPINION AND ORDER

Docket No. D-9343; File No. 111 0103
Filed, September 2, 2011 — Decision, December 2, 2011

On July 17, 2010, the Commission issued an administrative complaint alleging that the North Carolina Board of Dental Examiners (“Board”) harmed competition by ordering non-dentists to stop providing teeth-whitening services in the state. As a result, which has madeThe complaint alleged teeth-whitening services performed by non-dentists are significantly less expensive than when performed by dentists. As a result of the Board’s actions, it became more difficult and more expensive for North Carolina consumers to obtain teeth-whitening services. In an Initial Decision issued July 14, 2011, Administrative Law Judge Chappell (“ALJ”) held that non-dentists compete with dentists to provide teeth whitening services in North Carolina and that the Board’s concerted action to exclude non-dentist-provided teeth whitening services from the market had a tendency to harm competition. The ALJ further held that the Dental Board’s action had no valid pro-competitive justification and constituted an unreasonable restraint of trade and an unfair method of competition. Accordingly, the ALJ issued an order requiring the Board to stop the challenged conduct. The Board appealed the Initial Decision to the Commission for *de novo* review. In its Final Opinion, the Commission unanimously affirmed the ALJ’s Initial Decision, holding that the Board excluded non-dentists from the market for teeth-whitening services, in violation of Section 5 of the FTC Act. The Commission found that the Board’s conduct constituted concerted action and that this concerted action resulted in higher prices and reduced choices for consumer. The Commission further held the Board had failed to advance a legitimate procompetitive justification for its conduct. In examining the Board’s conduct, the Commission applied both a full “rule of reason” analysis, as well as an abbreviated “quick look” approach. reasons The Final Order of the Commission bars the Board from ordering non-dentists to stop providing teeth-whitening products or services and from informing teeth whitening providers that it is illegal for non-dentists to provide teeth whitening products or services.

Participants

For the *Commission*: *Michael Bergman, Michael J. Bloom, Richard B. Dagen, William L. Lanning, Steve J. Osnowitz,*

Opinion of the Commission

Tejasvi Srimashnam, Michael Turner, and Melissa Westman-Cherry.

For the Respondent: Brenner A. Allen, Noel Allen, Carolin Bakewell, Catherine E. Lee, Jackson S. Nichols, and M. Jackson Nichols, Allen Pinnix & Nichols, P.A.

OPINION OF THE COMMISSION

By ROSCH, Commissioner, For A Unanimous Commission:¹

I. INTRODUCTION²

This case involves the efforts of the North Carolina State Board of Dental Examiners (“Respondent” or the “Board”) to prevent non-dentists from providing teeth whitening services in North Carolina. The Board is an agency of the State of North Carolina and is charged with regulating the practice of dentistry in the state. By law, six of the eight members of the Board must be practicing dentists.

In the early 1990s, dentists in North Carolina and elsewhere began offering teeth whitening services through the use of various forms of peroxide. Since then, teeth whitening has become one of the most popular cosmetic dentistry procedures and is now offered by most dentists either as an in-office procedure or as a custom-made take-home kit.

In response to the popularity of teeth whitening, non-dentists began offering teeth whitening services at locations such as mall

¹ Commissioner Julie Brill has not participated in this matter.

² This opinion uses the following abbreviations for citations to the record:

Initial Decision	ID
ALJ Findings of Fact	IDF
Respondent’s Appeal Brief	RAB
Complaint Counsel’s Answering Brief on Appeal	CCAB
Respondent’s Reply Brief on Appeal	RRB
Complaint Counsel’s Exhibit	CX
Respondent’s Exhibit	RX
Trial Transcript	Tr.

Opinion of the Commission

kiosks, spas, retail stores, and salons in North Carolina in approximately 2003. These providers use techniques similar to those used by dentists to whiten teeth and, like dentists, can whiten teeth in a single session. However, non-dentist providers charge significantly less than dentists for the procedure and often offer greater convenience.

Dentists who performed teeth whitening services soon began complaining to the Board about the provision of teeth whitening services by non-dentists. These complaints often noted that these new providers charged less than dentists but rarely mentioned any public health or safety concerns. In response to these complaints, the Board issued dozens of cease and desist letters to non-dentist teeth whitening service providers and distributors of teeth whitening products and equipment. In addition, the Board sent letters to mall owners and operators urging them not to lease space to non-dentist teeth whitening providers. The Board had no authority to issue cease and desist orders under its enabling statute.

As a result of the Board's actions, many non-dentists stopped providing teeth whitening services and several marketers of teeth whitening systems stopped selling their products and equipment in North Carolina. In addition, several mall operators refused to lease space to, or cancelled existing leases with, non-dentist teeth whitening providers.

Based on our *de novo* review of the facts and law in this matter, we conclude that the Board sought to, and did, exclude non-dentist providers from the market for teeth whitening services in violation of Section 5 of the Federal Trade Commission Act, 15 U.S.C. § 45. We agree with Chief Administrative Law Judge D. Michael Chappell (the "ALJ") that Respondent's conduct constituted concerted action, that Respondent's conduct had a tendency to harm competition and in fact did harm competition, and that Respondent has failed to advance a legitimate procompetitive justification. We find liability under an abbreviated, or quick look, approach as well as under a full rule of reason analysis. We agree with the ALJ that the appropriate remedy is to prohibit the Board from directing non-dentist teeth whitening providers to cease providing their teeth whitening

Opinion of the Commission

products or services, and we adopt (with minor changes) the Order entered below.

II. FACTUAL BACKGROUND

The following is a summary of the findings of fact of the ALJ. Except as noted, Respondent does not challenge the ALJ's findings. We adopt the ALJ's findings of fact to the extent that they are not inconsistent with this opinion.

The Board

The North Carolina State Board of Dental Examiners is an agency of the State of North Carolina and is charged with regulating the practice of dentistry in the interest of public health, safety, and welfare of the citizens of North Carolina. (IDF 1, 33, 87.) The Board has the authority to issue and renew licenses and to take disciplinary action against dentists practicing in North Carolina. (IDF 35.) The Board is funded by dues and fees paid by licensed dentists and dental hygienists in North Carolina. (IDF 13-14.)

The Board consists of eight members: six licensed dentists, one licensed dental hygienist, and one consumer member, who is neither a dentist nor a dental hygienist. (IDF 2.) Each dentist elected to the Board must be licensed and actively engaged in the practice of dentistry while serving on the Board. (IDF 6-8.) The six dentist members of the Board are elected to the Board by other licensed dentists in North Carolina and, if an election is contested, a candidate may describe his or her positions on issues that may come before the Board. (IDF 15-23.) Many Board members have provided teeth whitening services through their private practices and derived income from those services while serving on the Board. (IDF 9-12.)

The Dental Practice Act provides that it is unlawful for an individual to practice dentistry in North Carolina without a license from the Board. *See* N.C. General Statutes § 90-29(a); IDF 41. Under the Dental Practice Act, a person "shall be deemed to be practicing dentistry" if that person "[r]emoves stains, accretions or deposits from the human teeth." N.C. General Statutes § 90-29(b)(2); IDF 42. In the event of a suspected unlicensed

Opinion of the Commission

practice of dentistry, the Board may bring an action to enjoin the practice in North Carolina Superior Court or may refer the matter to the District Attorney for criminal prosecution. *See* N.C. General Statutes § 90-40.1; IDF 43, 44, 190; Response to Complaint ¶ 19; RAB at 2-3; RRB at 5. The Board does not have the authority to discipline unlicensed individuals or to order non-dentists to stop violating the Dental Practice Act. *See* N.C. General Statutes §§ 90-27, -29, -40, -40.1; IDF 45-49.

Teeth Whitening Services

There are four categories of teeth whitening products or services available in North Carolina: dentist in-office services, dentist-provided take-home kits, services provided by a non-dentist, and over-the-counter (OTC) products.³ (IDF 105.) All four methods involve the application of some form of peroxide to the teeth using a gel or strip. (IDF 106, 151.) All four methods trigger a chemical reaction that results in whiter teeth. (IDF 106.)

Despite their similar characteristics, the four techniques vary in terms of immediacy of results, ease of use, provider support, and price. (IDF 107.) Dentist in-office services are quick, effective, and provided by a professional, but are costly compared to the other methods and require making an appointment. (IDF 108-20.) Take-home kits provided by dentists are effective and somewhat less expensive than in-office services but require the user to apply the product at home a number of times and usually require at least two trips to the dentist. (IDF 121-28.) Non-dentist services (like dentist in-office services) are quick and effective but are typically priced below dentist services and may

³ At pages 16 and 17 of Respondent's appeal brief, Respondent objects to Finding 100, which identifies various techniques to whiten teeth, because the ALJ's use of the phrase "through dental stain removal" could be interpreted—despite the ALJ's statements to the contrary (*see, e.g.*, ID at 82, 109)—as a reference to the Dental Practice Act's definition of the practice of dentistry as a person that "removes stains." N.C. General Statutes § 90-29(b)(2). Respondent's interpretation of Finding 100 is questionable, but, for clarity, we strike the phrase "through dental stain removal" from Finding 100 and otherwise affirm that finding.

Opinion of the Commission

not require an appointment.⁴ (IDF 137-50.) OTC products are low cost and convenient but require diligent and repeated application by the consumer. (IDF 129-36.) Consumers' preferences with respect to efficacy, cost, and convenience vary (IDF 169, 172, 174), and there is competition among providers offering the different methods of teeth whitening (IDF 157, 158), including through the use of comparative advertising (IDF 163-68).

The Board's Cease and Desist Letters

The Board conducts investigations of allegations that persons are engaged in the unauthorized practice of dentistry. (IDF 175.) Complaints to the Board regarding the unauthorized practice of dentistry are handled by an investigative panel consisting of a case officer, the Deputy Operations Officer, an Investigator, and sometimes the Board's legal counsel. (IDF 181-83.) The case officer, who must be one of the dentists serving on the Board, directs the investigation and is authorized by the Board to make enforcement decisions. (IDF 184-91.) The consumer member of the Board and the hygienist member of the Board did not participate in teeth whitening investigations, notwithstanding their authority to do so under the Dental Practice Act. (IDF 38-40, 59-60, 184, 192-93.)

Starting in or around 2003, the Board began receiving complaints from dentists about non-dentist providers of teeth whitening services. (IDF 194-95.) Almost all of these complaints came from licensed dentists (IDF 227, 229-30), many

⁴ Respondent argues that Findings 140 and 141 are flawed because Complaint Counsel's expert, Dr. Martin Giniger, lacked foundation for his testimony concerning the bleaching process used by non-dentist teeth whitening systems. (RAB at 17.) These findings are not material to the Commission's resolution of this matter and, in any event, Dr. Giniger had an adequate foundation for this testimony. Dr. Giniger has published numerous articles in peer-reviewed publications on teeth whitening (Giniger, Tr. 88-91; CX653 at 56-59), has taught dental students about teeth whitening (Giniger, Tr. 93-94), holds nine patents related to teeth whitening (Giniger, Tr. 95; CX653 at 55), has provided consulting services to several companies making teeth whitening products including those marketed to non-dentist providers (Giniger, Tr. 98; CX653 at 2; IDF 81), and reviewed the manuals for two companies offering non-dentist teeth whitening systems (CX653 at 22).

Opinion of the Commission

of whom derived income from teeth whitening services (IDF 233). Many of these complaints noted that these non-dentist providers offered low prices (IDF 196, 232); only on rare occasion did they indicate possible consumer harm (IDF 228, 231).

The Board discussed the increasing number of complaints regarding non-dentist teeth whitening services in its meetings. (IDF 198, 206.) On several occasions, Board members informed practicing dentists that the Board was investigating complaints about non-dentist teeth whiteners and was attempting to shut down these providers.⁵ (IDF 201, 205.)

Since 2006, the Board has sent at least 47 cease and desist letters to 29 non-dentist teeth whitening manufacturers and providers. (IDF 208-09, 216-18, 230, 262-83.) Starting in 2007 and at the direction of the Board's President, the Board began issuing cease and desist letters on the basis of a complaint, without any investigation. (IDF 210-15.) These letters were sent on the official letterhead of the Board and stated in capitalized lettering at the top: "NOTICE AND ORDER TO CEASE AND DESIST," "NOTICE TO CEASE AND DESIST," "CEASE AND DESIST NOTICE," or "NOTICE OF APPARENT VIOLATION AND DEMAND TO CEASE AND DESIST." (IDF 219, 220, 222, 223.) The letters go on to order the provider to cease and desist from "all activity constituting the practice of dentistry." (IDF 221-23.) Some of the letters stated that the sale or use of non-dentist teeth whitening products constituted a misdemeanor. (IDF 265-66, 280.) The Board's goal in sending these letters was to stop non-dentists from providing teeth whitening services. (IDF 234-45, 286-87.)

The Board's cease and desist letters were effective in causing non-dentists to stop providing teeth whitening services in North

⁵ Respondent disputes Finding 205, which states that members of the Board told dentists attending a conference that the Board was investigating complaints about non-dentist teeth whiteners. (RAB at 18.) Respondent is correct that there was conflicting testimony on this point, but the weight of evidence—including the testimony of the Board's President and official Board meeting minutes—supports this finding. (CX565 at 67 (Hardesty Dep. at 259-61); CX109 at 3.)

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Carolina. (IDF 247-56.) This was due in part to the perception of some recipients that the letters carried the force of law. (IDF 246.) The Board's letters were also effective in causing manufacturers and distributors of teeth whitening products used by non-dentist providers to exit or delay entering the North Carolina market.⁶ (IDF 70-72, 267-70, 272, 277-79, 281-83.)

The Board's Letters to Mall Operators and the Cosmetology Board

In November 2007, the Board sent eleven letters to mall operators warning them that kiosk teeth whiteners were violating the Dental Practice Act and requesting that they not lease space to these operators. (IDF 97, 288-93.) As a result, some mall operators refused to lease space to non-dentist teeth whiteners or cancelled existing leases. (IDF 98, 294-313.)

Based on its understanding that many of the non-dentist teeth whitening providers were salons and spas regulated by the North Carolina Board of Cosmetic Art Examiners ("cosmetology board"), the Board sought to enlist the aid of the cosmetology board in discouraging its licensees from providing teeth whitening services. (IDF 314-23.) In February 2007, the cosmetology board posted a notice on its website that was prepared by the Board suggesting that teeth whitening "constitutes the practice of dentistry" and that the "unlicensed practice of dentistry in our state is a misdemeanor." (IDF 320, 322.) As a result of the cosmetology board's posting, some cosmetologists stopped providing teeth whitening services. (IDF 324-27.)

III. PROCEDURAL HISTORY

⁶ Respondent asserts that Finding 268, which states that WhiteScience lost all of its sales in North Carolina as a result of the Board's actions, is inconsistent with testimony of the President of WhiteScience that his company continued to do business in North Carolina. (RAB at 17-18.) In fact, WhiteScience's President testified that the company did lose all of its sales in the state in response to the Board's actions but later reentered the state after learning that the Board would handle allegations of unauthorized practice of dentistry on a case-by-case basis. (Nelson, Tr. 735-36, 785-89, 800-01, 809-11; *see also* IDF 263-70, 278.)

Opinion of the Commission

A. Pleadings And Pre-Trial Motions

On June 17, 2010, the Commission issued a single-count Complaint in this matter against the Board. The Complaint alleged that the Board classified teeth whitening as the practice of dentistry and violated Section 5 of the FTC Act by enforcing this determination through cease and desist orders that were neither authorized nor supervised by the State, and that were designed to, and did, drive non-dentist teeth whiteners out of North Carolina.

The Complaint alleged that the Board, reacting to the competitive threat posed by non-dentist providers, sought to exclude, and did exclude, non-dentists from the market for teeth whitening services in North Carolina. (Compl. ¶¶ 13-23.) According to the Complaint, the Board sent dozens of cease and desist letters to non-dentist teeth whitening providers and distributors, discouraged prospective non-dentist providers from opening teeth whitening businesses, and sent letters to owners and operators of shopping malls to discourage their leasing space to non-dentist teeth whitening businesses. (*Id.* ¶¶ 20-22.) These actions were allegedly not authorized by statute and did not involve any oversight by the State. (*Id.* ¶ 19.) The Complaint did not challenge any attempts by the Board to commence civil or criminal proceedings against alleged violators of the North Carolina Dental Practice Act, N.C. General Statutes § 90-22 *et seq.*

The Complaint alleged that the Board's actions have had the effect of restraining competition unreasonably and injuring consumers in North Carolina by preventing and deterring non-dentists from providing teeth whitening services; depriving consumers of the benefits of price competition; and reducing consumer choice for the provision of teeth whitening services. (*Id.* ¶¶ 24-25.) The Complaint further alleged that the Board's actions do not qualify for the state action defense and are not reasonably related to any efficiencies or other benefits sufficient to justify their harmful effect on competition. (*Id.* ¶ 23.) The Notice of Contemplated Relief attached to the Complaint seeks an order that would require Respondent to discontinue the challenged conduct.

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The Board filed a Response to Complaint dated July 6, 2010. The Response admitted that the Board had sent letters to non-dentists offering teeth whitening services with the caption: “Notice and Order to Cease and Desist.” (Response ¶ 20; *see also id.* ¶ 19 (acknowledging that the Board had sent “cease and desist letters”).) The letters “inform[ed] the recipient of the investigation, quote[d] the applicable statute, and demand[ed] that the recipient stop violating that statute.” (*Id.* ¶ 20.) The Response further admitted that the Board’s staff had sent letters to mall owners and property management companies requesting their “assistance in preventing *unlawful* activity on their premises,” namely, “teeth whitening services by non-dentists.” (*Id.* ¶ 22 (emphasis in original).) Respondent also admitted that Board staff had informed non-dentists who were considering opening teeth whitening businesses that such services could be performed only by a licensed dentist. (*Id.* ¶ 21.)

The Board’s Response further admitted that “[a]ny enforcement actions by the Board against non-licensees who are providing teeth whitening services, whether civil or criminal, may only be pursued in the state’s courts.” (*Id.* ¶ 19; *see also id.* (“[N]o kiosk, spa or other provider of teeth whitening services by a non-dentist could actually be forced to stop operations unless the Board obtained either a court order or the cooperation of a district attorney in a criminal conviction and a court judgment.”)) The Response otherwise denied the allegations of the Complaint, including the alleged product market, that concerted activity had occurred, that the cease and desist letters were orders, and that the Board’s actions had caused anticompetitive effects in the purported relevant market.

As affirmative defenses, the Response asserted, among other things, that the Board is immune from suit under the state action doctrine, possesses sovereign immunity under the Eleventh Amendment, and is protected by the Tenth Amendment; that the Commission lacks subject matter jurisdiction; that the Board’s actions had no substantial effect on U.S. commerce; and that the requested relief was not in the public interest. (*Id.* at 20-21.)

Prior to the start of the trial before the ALJ, Complaint Counsel and Respondent filed cross motions on the issue of the applicability of the state action doctrine to the Board’s conduct.

Opinion of the Commission

In an Opinion and Order dated February 3, 2011, the Commission rejected the Board's invocation of the state action doctrine as a basis for exempting its challenged conduct from the FTC Act. *See North Carolina Board of Dental Examiners*, 151 F.T.C. 607, 615-33 (2011). The Commission explained that because the Board is controlled by practicing dentists, the Board's challenged conduct must be actively supervised by the State for it to claim state action exemption from the antitrust laws. *Id.* at 617-28. Because the undisputed facts showed that there was no such supervision, the antitrust laws applied to the Board's conduct. *Id.* at 628-33. The Commission also concluded that it has jurisdiction over the Board because states and their regulatory bodies constitute "persons" under the FTC Act. *Id.* at 614-15.

On January 14, 2011, Respondent filed a motion to disqualify the Commission, asserting that the Commission lacks the constitutional authority to decide whether it has jurisdiction over the Board and had prejudged the issues in the proceeding. In a February 16, 2011 Opinion, the Commission denied Respondent's motion. *See North Carolina Board of Dental Examiners*, 151 F.T.C. 644 (2011). The Opinion concluded that the Commission has jurisdiction to decide whether the Board can avail itself of the state action exemption and that the Board had presented no evidence of prejudgment.

On February 1, 2011, Respondent filed a complaint for declaratory judgment and injunctive relief in the United States District Court for the Eastern District of North Carolina. The complaint alleged that the FTC lacked jurisdiction over the Board and that these proceedings violated various constitutional rights of the Board. On May 3, 2011, the District Court dismissed the action for lack of subject matter jurisdiction, explaining that "the appropriate forum for plaintiff's arguments is in the administrative proceedings, followed by a potential appeal to the Fourth Circuit Court of Appeals." *North Carolina State Board of Dental Examiners v. FTC*, 768 F. Supp. 2d 818, 822 (E.D.N.C. 2011). Appeal of the dismissal is pending before the Fourth Circuit.

During the trial, which began on February 17, 2011 and concluded on March 16, 2011, the ALJ heard testimony from twelve fact and four expert witnesses and admitted more than

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eight hundred exhibits into evidence. The ALJ closed the hearing record on March 30, 2011. Complaint Counsel and the Board filed concurrent post-trial briefs and proposed findings on April 25, 2011 and filed replies on May 5, 2011. The ALJ heard closing arguments on May 11, 2011.

B. Initial Decision

The ALJ issued an Initial Decision (“ID”) on July 14, 2011, finding that the Board’s concerted action to exclude non-dentists from the market for teeth whitening services in North Carolina constituted an unreasonable restraint of trade and an unfair method of competition in violation of Section 5 of the FTC Act. In particular, the ALJ found that dentist members of the Board had a common scheme or design, and hence an agreement, to exclude non-dentists from the market for teeth whitening services and to deter potential providers of teeth whitening services from entering the market. To achieve this objective, dentist members of the Board caused the Board to (a) send letters to non-dentist teeth whitening providers ordering them to cease and desist from offering these services, (b) send letters to manufacturers of equipment used by non-dentist providers ordering them to cease and desist from assisting clients offering teeth whitening services, (c) send letters to dissuade persons considering opening non-dentist teeth whitening businesses, (d) send letters to owners or operators of malls to dissuade them from leasing space to non-dentist providers of teeth whitening services, and (e) elicit the help of the cosmetology board to dissuade its licensees from providing teeth whitening services. The ALJ concluded that these actions, by their nature, had the tendency to harm competition.

The ALJ found that the relevant market consists of teeth whitening services provided by dentists and non-dentists, but determined that the relevant market did not include self-administered teeth whitening products. The ALJ concluded that the Board had market power in the relevant market, as demonstrated by its ability to exclude non-dentist providers from the relevant market.

The ALJ found that the Board’s concerted actions were effective in causing non-dentist teeth whitening providers to exit

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the relevant market, manufacturers to reduce the availability of their teeth whitening products to non-dentist providers, and mall owners and operators to stop leasing space to non-dentist providers.

The ALJ rejected the Board's proffered procompetitive justifications. The ALJ concluded that the antitrust laws do not permit a defense based on social welfare or public safety concerns, as asserted by the Board. In addition, the ALJ rejected Respondent's argument that teeth whitening services should be offered at a cost that reflects the skills of dentists as inimical to the basic policy of the antitrust laws. The ALJ also rejected Respondent's proffered justification that the Board's actions had the benefit of promoting legal competition. Finally, the ALJ observed that the Board's remaining justifications were essentially a reiteration of its state action argument, which had been rejected by the Commission.

As a remedy, the ALJ ordered the Board to cease and desist from directing a non-dentist to stop providing teeth whitening services or products, as well as from prohibiting or discouraging the provision of these goods and services. The ALJ's Order also requires the Board to cease and desist from communicating to certain third parties that non-dentist teeth whitening goods or services violate the Dental Practice Act. The ALJ's Order does not prohibit the Board from investigating, filing a court or administrative action, or communicating notice of its intent to file a court or administrative action against a non-dentist provider for an alleged violation of the Dental Practice Act.

C. Appeal

Respondent timely filed a Notice of Appeal on July 28, 2011. Complaint Counsel did not file an appeal from the Initial Decision. The Commission heard oral argument on October 28, 2011.⁷

⁷ Complaint Counsel submitted a packet of materials to the Commission a few hours before oral argument. (Oral Argument Tr. 4-5, 37-38.) In light of Respondent's inability to meaningfully review or object to these materials in advance of oral argument, the Commission has given no consideration to the packet in reaching its decision.

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Respondent makes three principal claims on appeal. Respondent first argues that no contract, combination, or conspiracy to restrain trade existed. In particular, Respondent asserts that the Board is not capable of engaging in concerted action because it does not consist of independent economic actors with distinct economic interests. (RAB at 11-15, 25-26.) In addition, Respondent argues that even if the members of the Board were capable of concerted action, there was no evidence to support a finding that they did so in this case.

Respondent's second principal claim on appeal is that several procompetitive justifications outweigh any harm to competition. (RAB at 7-10, 29-34.) Respondent asserts that the ALJ failed to consider that the Board's actions were those of a state agency that intended to and did promote the public welfare and thus enhanced legal competition.

Respondent's third principal claim on appeal is that the ALJ's proposed remedy is overbroad and will prevent the Board from investigating or challenging violations of the North Carolina Dental Practice Act. (RAB at 37.) Respondent also asserts that the proposed remedy violates the Commerce Clause of and Tenth Amendment to the United States Constitution. (RAB at 39-46.)

In addition, Respondent seeks to relitigate two issues resolved in the Commission's February 3, 2011 Opinion and Order, namely the Commission's jurisdiction to hear this case and the applicability of the state action defense. (RAB at 22-24, 29-31.) We note, as an initial matter, that an appeal from an ALJ's Initial Decision is not the proper means by which to seek reconsideration of a Commission decision. In any event, Respondent has failed to identify any change in controlling law, new evidence, or a need to correct a clear error or manifest injustice that would warrant reconsidering our prior decision on either of these issues.⁸

IV. STANDARD OF REVIEW

The Commission reviews the ALJ's findings of facts and conclusions of law *de novo*, considering "such parts of the record

⁸ See also note 20, *infra* (addressing whether the Board is a "person" under the FTC Act).

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as are cited or as may be necessary to resolve the issues presented.” The Commission may “exercise all the powers which it could have exercised if it had made the initial decision.”⁹ Commission Rule 3.54, 16 C.F.R. § 3.54.

V. LEGAL FRAMEWORK

Although the reach of Section 5 of the FTC Act extends beyond that of Section 1 of the Sherman Act, *see FTC v. Sperry & Hutchinson Co.*, 405 U.S. 233, 239 (1972), in this case we follow the standards of Section 1 to assess whether the challenged actions of the Board violate Section 5. *See California Dental Ass’n v. FTC*, 526 U.S. 756, 762 & n.3 (1999); *FTC v. Indiana Federation of Dentists*, 476 U.S. 447, 451-55 (1986); *FTC v. Cement Institute*, 333 U.S. 683, 694 (1948); *Fashion Originators’ Guild of America, Inc. v. FTC*, 312 U.S. 457, 463-64 & n.4 (1941); *Realcomp II, Ltd. v. FTC*, 635 F.3d 815, 824 (6th Cir. 2011); *Polygram Holding, Inc. v. FTC*, 416 F.3d 29, 32 (D.C. Cir. 2005).

Section 1 of the Sherman Act prohibits “[e]very contract, combination . . . or conspiracy, in restraint of trade or commerce among the several States.” 15 U.S.C. § 1. Despite its broad language, the ban on contracts in restraint of trade extends only to unreasonable restraints of trade, *i.e.*, restraints that impair competition. *State Oil Co. v. Khan*, 522 U.S. 3, 10 (1997). Thus, a violation of Section 1 requires proof of two elements: “(1) a contract, combination, or conspiracy; (2) that imposed an unreasonable restraint of trade.” *Valuepest.com of Charlotte, Inc. v. Bayer Corp.*, 561 F.3d 282, 286 (4th Cir. 2009) (quoting *Dickson v. Microsoft Corp.*, 309 F.3d 193, 202 (4th Cir. 2002)).

The first element requires proof of some kind of agreement because “[i]ndependent action is not proscribed.” *Monsanto Co. v. Spray-Rite Service Corp.*, 465 U.S. 752, 761 (1984). To demonstrate an agreement, a plaintiff must show that the parties

⁹ The *de novo* standard of review is required by the Administrative Procedure Act, 5 U.S.C. § 557(b), and the FTC Act, 15 U.S.C. § 45(b), (c), and applies to both findings of fact and inferences drawn from those facts. *See Realcomp II, Ltd.*, No. 9320, 2009 FTC LEXIS 250, *37 n.11 (2009), *aff’d*, *Realcomp II, Ltd. v. FTC*, 635 F.3d 815 (6th Cir. 2011).

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“had a conscious commitment to a common scheme designed to achieve an unlawful objective.” *Id.* at 768. This may be proved through “direct or circumstantial evidence.” *Id.* In addition, the agreement must “deprive[] the marketplace of independent centers of decisionmaking” in order to raise Section 1 concerns. *American Needle, Inc. v. NFL*, 130 S. Ct. 2201, 2212 (2010) (quoting *Copperweld Corp v. Independence Tube Corp.*, 467 U.S. 752, 769 (1984)).

With respect to the second element, the Supreme Court has explained that “a restraint may be adjudged unreasonable either because it fits within a class of restraints that has been held to be ‘per se’ unreasonable, or because it violates what has come to be known as the ‘Rule of Reason.’” *Indiana Federation of Dentists*, 476 U.S. at 457-58. Under per se analysis, “certain agreements or practices are so ‘plainly anticompetitive,’ . . . and so often ‘lack . . . any redeeming virtue,’ . . . that they are conclusively presumed illegal without further examination.” *Broadcast Music, Inc. v. Columbia Broadcasting System, Inc.*, 441 U.S. 1, 8 (1979) (citations omitted). “A court need not then inquire whether the restraint’s authors actually possess the power to inflict public injury . . ., nor will the court accept argument that the restraint in the circumstances is justified by any procompetitive purpose or effect.” *United States v. Realty Multi-List, Inc.*, 629 F.2d 1351, 1362 (5th Cir. 1980) (citations omitted).

Complaint Counsel does not contend that the challenged conduct of the Board is unreasonable per se and instead challenges the Board’s conduct under the rule of reason. When evaluating conduct under the rule of reason, the Supreme Court has called for “an enquiry meet for the case, looking to the circumstances, details, and logic of a restraint,” with the aim of reaching “a confident conclusion about the principal tendency of a restriction.” *California Dental*, 526 U.S. at 781.

In *Indiana Federation of Dentists*, the Court outlined three alternative modes of analysis under the rule of reason. That case concerned a group of dentists who agreed to withhold x-rays from dental insurance companies that requested their use in benefits determination. The Court applied a rule of reason analysis and affirmed the Commission’s finding that the practice violated Section 1 of the Sherman Act. In applying the rule of reason, the

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Court condemned the practice on two alternative grounds and endorsed the existence of a third possible route to condemnation under the rule of reason (albeit one not applicable to the facts it confronted).

First, the Court held that it was faced with a type of restraint that, by its very nature, required justification even in the absence of a showing of market power. 476 U.S. at 459-60. According to the Court, because the practice was “a horizontal agreement among the participating dentists to withhold from their customers a particular service that they desire,” then “no elaborate industry analysis is required to demonstrate the anticompetitive character of such an agreement.” *Id.* at 459 (quoting *National Society of Professional Engineers v. United States*, 435 U.S. 679, 692 (1978)). Accordingly, the practice “require[d] some competitive justification even in the absence of a detailed market analysis.” *Id.* at 460 (quoting *NCAA v. Board of Regents*, 468 U.S. 85, 109-10 (1984)). We have previously condemned several types of restraints under this “inherently suspect” form of analysis.¹⁰ *See, e.g., Realcomp II, Ltd.*, No. 9320, 2009 FTC LEXIS 250 (2009), *aff’d on other grounds, Realcomp II, Ltd. v. FTC*, 635 F.3d 815 (6th Cir. 2011); *North Texas Specialty Physicians*, 140 F.T.C. 715 (2005), *aff’d, North Texas Specialty Physicians v. FTC*, 528 F.3d 346 (5th Cir. 2008); *Polygram Holding, Inc.*, 136 F.T.C. 310 (2003), *aff’d, Polygram Holding, Inc. v. FTC*, 416 F.3d 29, 32 (D.C. Cir. 2005).

Second, the Court held that even if the restriction in question was “not sufficiently ‘naked’ to call this principle into play, the Commission’s failure to engage in detailed market analysis [was] not fatal to its finding of a violation of the Rule of Reason,” because the record contained direct evidence of anticompetitive effects. 476 U.S. at 460. The Court reasoned that “[s]ince the purpose of the inquiries into market definition and market power is to determine whether an arrangement has the potential for genuine adverse effects on competition, ‘proof of actual detrimental effects, such as a reduction of output,’ can obviate the

¹⁰ Antitrust tribunals have used a variety of terms to address this approach, including “abbreviated,” “truncated,” or “quick look” analysis. *See California Dental*, 526 U.S. at 770-71 (collecting cases). For simplicity, we adhere to the “inherently suspect” terminology we used in *Polygram*.

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need for an inquiry into market power, which is but a ‘surrogate for detrimental effects.’” *Id.* at 460-61 (quoting 7 Areeda, *Antitrust Law* ¶ 1511, at 429 (1986)); *see also Realcomp*, 635 F.3d at 827 (“If adverse effects are clear, inquiry into market power is unnecessary.”).

Third, the Court’s discussion of the “proof of actual detrimental effects” prong of the analysis made clear that the traditional mode of analysis—inquiring into market definition and market power—was still available, although not applicable to the case before it because the Commission had not attempted to prove market power. Although the Court did not explore this mode of analysis in detail, it observed that “the purpose of the inquiries into market definition and market power is to determine whether an arrangement *has the potential* for genuine adverse effects on competition.” *Id.* at 460 (emphasis added). Numerous lower courts have confirmed that the Court’s conclusion in *Indiana Federation of Dentists* that market power is “a surrogate for detrimental effects” logically compels the result that, if the tribunal finds that the defendants had market power and that their conduct tended to reduce competition, it is unnecessary to demonstrate directly that their practices had adverse effects on competition. *See, e.g., Realcomp*, 635 F.3d at 827-31; *United States v. Brown University*, 5 F.3d 658, 668-69 (3d Cir. 1993); *Flegel v. Christian Hospital*, 4 F.3d 682, 688 (8th Cir. 1993); *Gordon v. Lewistown Hospital*, 423 F.3d 184, 210 (3d Cir. 2005); *Law v. NCAA*, 134 F.3d 1010, 1019 (10th Cir. 1998); *Toys “R” Us, Inc. v. FTC*, 221 F.3d 928, 937 (7th Cir. 2000).

The Supreme Court addressed the role of abbreviated rule of reason analysis again in *California Dental*. That case concerned a professional association’s ethical canon that effectively prohibited members from advertising price discounts in most cases and entirely precluded advertising regarding the quality of services. The FTC and the Ninth Circuit had concluded that the restrictions resulting from this rule were tantamount to naked restrictions on price competition and output, 526 U.S. at 762-64, and therefore applied an “abbreviated, or ‘quick look,’ rule of reason analysis,” and found them unlawful without a “full-blown rule of reason inquiry” or an “elaborate industry analysis.” *Id.* at 763 (citing *NCAA*, 468 U.S. at 109-10 & n.39).

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The Supreme Court agreed that restrictions with obvious anticompetitive effects, such as those in *Professional Engineers, NCAA*, and *Indiana Federation of Dentists*, do not require a “detailed market analysis” and may be held unlawful under a rule of reason framework unless the defendants proffer some acceptable “competitive justification” for the practice. Such analysis is appropriate if “an observer with even a rudimentary understanding of economics could conclude that the arrangements in question would have an anticompetitive effect on customers and markets.” *California Dental*, 526 U.S. at 769, 770. The Court found, however, that the particular advertising rules under review in that case might plausibly “have a procompetitive effect by preventing misleading or false claims that distort the market,” particularly given the “disparities between the information available to the professional and the patient” and the “inherent asymmetry of knowledge” about the service. *Id.* at 771-72, 778 (quotation omitted). Thus, while “it is also . . . possible that the restrictions might in the final analysis be anticompetitive[,] . . . [t]he obvious anticompetitive effect that triggers abbreviated analysis has not been shown.” *Id.* at 778.

While the Court accordingly called, in that case, for a “more sedulous” market analysis, *id.* at 781, it took pains to add that its ruling did “not, of course, necessarily . . . call for the fullest market analysis. . . . [I]t does not follow that every case attacking a less obviously anticompetitive restraint (like this one) is a candidate for plenary market examination.” *Id.* at 779. Rather, the Court stated, “[w]hat is required . . . is an enquiry meet for the case, looking to the circumstances, details, and logic of a restraint.” *Id.* at 781.

In this Opinion, we analyze Respondent’s conduct under the three modes of analysis endorsed in *Indiana Federation of Dentists*. It is important to note, however, that we could have selected just one of these modes of analysis and, if this approach had supported a finding that the Board’s conduct is unlawful, it would have been unnecessary to engage in any further analysis. The fact that all three modes of inquiry under *Indiana Federation of Dentists* lead to the same result reinforces our conclusion that the conduct at issue is anticompetitive.

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VI. ANALYSIS**A. Concerted Action**

The ALJ concluded that “the Board had a common scheme or design, and therefore an agreement, to prevent or eliminate non-dentist teeth whitening services in North Carolina.” (ID at 77-79.) The ALJ concluded that this agreement could be inferred from the Board’s course of conduct in issuing cease and desist letters and other communications designed to discourage non-dentist teeth whitening. (ID at 78-79.) In addition, the ALJ concluded that even though the Board was a single legal entity, it was legally capable of concerted action because it was controlled by dentists with competing economic interests. (ID at 71-76.)

Respondent argues that the concerted action required by Section 1 of the Sherman Act has not been shown because the Board’s members are not separate economic actors capable of a conspiracy. Respondent further argues that there is no evidence that members of the Board in fact engaged in concerted action. We find both of these arguments to be without merit.

Section 1 of the Sherman Act requires a “contract, combination . . . or conspiracy” that unreasonably restrains trade. 15 U.S.C. § 1. “Independent action is not proscribed.” *Monsanto Co. v. Spray-Rite Service Co.*, 465 U.S. 752, 761 (1984); *see also Copperweld*, 467 U.S. at 767-68 (“Section 1 . . . does not reach conduct that is wholly unilateral” (quotation omitted)); *Virginia Vermiculite, Ltd. v. Historic Green Springs, Inc.*, 307 F.3d 277, 280 (4th Cir. 2002) (“It is incontestable that ‘concerted action’ in restraint of trade lies at the heart of a Sherman Act section 1 violation.”).

In its recent *American Needle* decision, the Supreme Court explained that “concerted action under § 1 does not turn simply on whether the parties involved are legally distinct entities.” *American Needle, Inc. v. NFL*, 130 S. Ct. 2201, 2209 (2010); *see also id.* at 2211 (“the question is not whether the defendant is a legally single entity or has a single name”). Instead, the “relevant inquiry . . . is whether there is a ‘contract, combination . . . or conspiracy’ amongst separate economic actors pursuing separate economic interests, such that the agreement deprives the

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marketplace of independent centers of decisionmaking, and therefore of diversity of entrepreneurial interests, and thus of actual or potential competition.” *Id.* at 2212 (quotations and citations omitted).

For example, a parent corporation and its wholly-owned subsidiary “are incapable of conspiring with each other for purposes of § 1 of the Sherman Act.” *Copperweld*, 467 U.S. at 777. Although a parent corporation and its wholly-owned subsidiary are legally separate entities, they lack “independent centers of decisionmaking” necessary to raise Section 1 concerns. *Id.* at 769. Likewise, “an internal agreement to implement a single, unitary firm’s policies does not raise the antitrust dangers that § 1 was designed to police.” *Id.* Nevertheless, the Court has “repeatedly found instances in which members of a legally single entity violated § 1 when the entity was controlled by a group of competitors and served, in essence, as a vehicle for ongoing concerted activity.” *American Needle*, 130 S. Ct. at 2209 (listing cases).

The Fourth Circuit has similarly recognized that corporate agents are capable of a Section 1 conspiracy when they have independent personal stakes in the object of the conspiracy. *See American Chiropractic v. Trigon Healthcare*, 367 F.3d 212, 224 (4th Cir. 2004) (“We have continued to recognize . . . the independent personal stake exception.”); *Greenville Publishing Co. v. Daily Reflector, Inc.*, 496 F.2d 391, 399-400 (4th Cir. 1974) (corporation found capable of conspiring with president of corporation because the officer had “an independent personal stake in achieving the corporation’s illegal objective”). The “personal stake” principle is relevant only where the officers with the independent interests exercise some degree of control over the firm’s decisionmaking process. *See Oksanen v. Page Memorial Hospital*, 945 F.2d 696, 705 (4th Cir. 1991) (en banc) (“If the officer cannot cause a restraint to be imposed and his firm would have taken the action anyway, then any independent interest is largely irrelevant to antitrust analysis.”).

In the instant case, the ALJ correctly found that Board members were capable of conspiring because they are actual or potential competitors. As required by Section 90-22(b) of the Dental Practice Act, dentist Board members continued to operate

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separate dental practices while serving on the Board (IDF 6-8), giving them distinct and potentially competing economic interests. *Cf. American Needle*, 130 S. Ct. at 2213 (NFL teams are “potentially competing suppliers”). At oral argument, Respondent appeared to acknowledge that members of the Board are potential competitors. (Oral Argument Tr. 9-10 (“they are potential competitors”).)

In addition, Board members had a personal financial interest in excluding non-dentist teeth whitening services. *Id.* at 2215 (“Agreements made within a firm can constitute concerted action covered by § 1 when the parties to the agreement act on interests separate from those of the firm itself . . .”). At least eight of the ten dentist Board members serving from 2005 to 2010 (Drs. Allen, Burnham, Feingold, Hardesty, Holland, Morgan, Owens, and Wester) provided teeth whitening services in their private practices. (IDF at 6-9; *see also* IDF 32 (identifying Board members).) For example, during their tenures on the Board, one Board member earned over \$75,000 from teeth whitening services, while another earned over \$40,000.¹¹ (IDF 10-11, 32.) The dentist members of the Board therefore stood to benefit financially from the challenged restrictions. (Baumer, Tr. 1856; *see also* IDF 102 (noting growth in dentist-provided teeth whitening).) In addition, all dentist Board members were elected to the Board by other licensed dentists, many of whom also have a financial interest in limiting the practice of teeth whitening to dentists. (IDF 15-23.) Thus, as the ALJ concluded, “Board members have a significant, nontrivial financial interest in the business of their profession, including teeth whitening.” (IDF 12.)

¹¹ Respondent asserts that Findings 9, 10, 11, 104, and 233 exaggerate the financial interest of the Board and other dentists in teeth whitening by including income from forms of teeth whitening services outside the ALJ’s relevant market. (RAB at 11-15.) In light of our conclusion that the relevant market is broader than that found by the ALJ (*see* Section VI.B.2.a, *infra*), Respondent’s objections to these findings are moot. Respondent also objects to a citation to Dr. Baumer’s testimony in Finding 12 but not the finding itself. (RAB at 15-16.) Even without the disputed citation, we would affirm Finding 12 based on the other evidence cited by the ALJ.

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Respondent's economic expert acknowledged that Board members have a financial interest in the challenged restrictions.¹² Respondent's economist testified that state regulatory boards can be, and have been, used to exclude competition and augment the income of licensed practitioners. (Baumer, Tr. 1763 (referring to CX822 at 19), 1848-50, 1855-56, 1884, 1896-98, 1901-03, 1911-13, 1915; RX078 at 8.) He also acknowledged that the Board's decision to ban non-dentist teeth whitening may have been "influenced by the impact on the bottom line." (Baumer, Tr. 1859-62; *see also* Baumer, Tr. 1781 (similar).)

Our finding that Board members have a capacity to conspire is buttressed by the significant degree of control exercised by dentist members of the Board with respect to the challenged restraints. A majority of the members of the Board had a personal financial interest in excluding non-dentist teeth whitening. (IDF 2, 6-11.) Furthermore, all of the key decisionmakers in teeth whitening matters had a personal stake in the conspiracy because dentists were the only Board members involved in teeth whitening investigations (the consumer and dental hygienist Board members were excluded). (IDF 40, 59-60, 184, 192-93.)

Respondent nevertheless argues that dentist board members lack a financial interest in the challenged restraints because there is not a "significant degree" of competition between dentist-provided teeth whitening and non-dentist provided teeth whitening. (RRB at 3-4.) This assertion is contradicted not only by the testimony of Respondent's own economic expert, who stated that there is a high cross-elasticity between these two forms

¹² The following exchange with Respondent's economist, Dr. Baumer, occurred at page 1856 of the trial transcript:

Q. Now . . . you believe that the board, the North Carolina State Board of Dental Examiners, is concerned about the financial interest of dentists in North Carolina; correct?

A. Yes. I think they are.

Q. And you believe that dentists in North Carolina do have a financial interest in excluding non-dentist teeth whitening; correct?

A. There is a financial aspect to that. Correct.

Q. And that they have a financial interest in excluding the non-dentist teeth whiteners; correct?

A. Yes.

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of teeth whitening (Baumer, Tr. 1842-45), but also by Respondent's acknowledgement that these two services are in the same relevant market (RAB at 10-11, 27; *see also* Baumer, Tr. 1711; *cf.* Kwoka, Tr. 994-1002 (testimony of Complaint Counsel's expert)).

Thus, despite the general principle that joint action by corporate officers is usually "not the sort of 'combination' that § 1 is intended to cover," *American Needle*, 130 S. Ct. at 2212, here the evidence shows that the dentist members of the Board were separate economic actors pursuing separate economic interests whose joint decisions could deprive the marketplace of actual or potential competition. Because their agreement joined together "independent centers of decisionmaking" *id.* at 2209, 2211, 2212, 2213, 2214 (quoting *Copperweld*, 467 U.S. at 769), the Board members were capable of conspiring under Section 1.

In a similar case, the board of directors of a nationwide moving company adopted a policy restricting its local affiliates' ability to offer interstate carriage. The Court of Appeals for the D.C. Circuit concluded that the directors had formed a Section 1 conspiracy because nine of the eleven board members were "actual or potential competitors" and stood to personally benefit from the challenged restriction. *Rothery Storage & Van Co. v. Atlas Van Lines, Inc.*, 792 F.2d 210, 215 (D.C. Cir. 1986).

Our conclusion is also consistent with our disposition of the *Massachusetts Board* case. That matter involved a challenge to a state agency's restrictions on the use of truthful advertising by its optometrist licensees. We concluded that the members of the optometry board were separate legal entities capable of conspiring in restraint of trade because each optometrist on the board was engaged in the private practice of optometry and stood to benefit from the restraints in question. *See Massachusetts Board of Registration in Optometry*, 110 F.T.C. 549, 610-11 (1988).

We turn next to the issue of whether the element of concerted action has been satisfied. *See Oksanen*, 945 F.2d at 706 (even if there is a "capacity to conspire," a court must determine whether a conspiracy actually exists).

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A plaintiff alleging conspiracy must demonstrate that the parties “had a conscious commitment to a common scheme designed to achieve an unlawful objective.” *Monsanto*, 465 U.S. at 768; *Thompson Everett, Inc. v. National Cable Advertising, L.P.*, 57 F.3d 1317, 1324 (4th Cir. 1995) (same). *Monsanto* requires “something more” than independent action, and must rise to the level of “a unity of purpose or a common design and understanding, or a meeting of minds.” *Parkway Gallery Furniture, Inc. v. Kittinger/Pennsylvania House Group, Inc.*, 878 F.2d 801, 805 (4th Cir. 1989).

A plaintiff may demonstrate an agreement by “direct or circumstantial evidence.” *Monsanto*, 465 U.S. at 768; *see also American Chiropractic*, 367 F.3d at 225-26 (“A plaintiff can offer direct or circumstantial evidence to prove concerted action.”); *Laurel Sand & Gravel, Inc. v. CSX Transp., Inc.*, 924 F.2d 539, 542 (4th Cir. 1991) (“An agreement to restrain trade may be inferred from other conduct.”). But care must be taken with respect to inferences drawn from circumstantial evidence because “conduct as consistent with permissible competition as with illegal conspiracy does not, standing alone, support an inference of antitrust conspiracy.” *Matsushita Electric Industrial Co. v. Zenith Radio Corp.*, 475 U.S. 574, 588 (1986). For example, “mere contacts and communications, or the mere opportunity to conspire . . . is insufficient evidence from which to infer an antitrust conspiracy.” *Oksanen*, 945 F.2d at 706 (quoting *Cooper v. Forsyth County Hospital Authority*, 789 F.2d 278, 281 (4th Cir. 1986)).

The concerted action requirement can be satisfied even where one or more of the co-conspirators had differing motives or goals or “acted unwillingly, reluctantly, or only in response to coercion”; it is sufficient to show that the co-conspirators “acquiesced in an illegal scheme.” *Dickson*, 309 F.3d at 205 (quotation and citation omitted); *see also Virginia Vermiculite*, 156 F.3d at 541 (“[I]t is not necessary that HGSI have shared Grace’s alleged anticompetitive motive in entering into a proscribed restraint; it is sufficient that HGSI, regardless of its own motive, merely acquiesced in the restraint with the knowledge that it would have anticompetitive effects.”); *Duplan Corp. v. Deering Milliken Inc.*, 594 F.2d 979, 982 (4th Cir. 1979)

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(“Where, as here, the [defendants] were knowing participants in a scheme whose effect was to restrain trade, the fact that their motives were different from or even in conflict with those of the other conspirators is immaterial.”).

Here, there is direct evidence demonstrating that the dentist members of the Board had a common plan to exclude non-dentist teeth whitening providers from the market. On several occasions, the Board discussed teeth whitening services provided by non-dentists and then voted to take action to restrict these services. (IDF 264, 276, 289, 317, 318, 321.) For example:

- At the Board’s February 2007 meeting, the Board discussed the increase in complaints involving spas offering teeth whitening procedures and voted to send a letter to the cosmetology board with the goal of discouraging this practice. (IDF 317-18, 321, 323.) The Board’s then-Secretary and Treasurer testified that there was “consensus” on the Board to send the letter and that “nobody had any objections.” (CX565 at 62 (Hardesty Dep. at 240).)
- At its August 2007 Board meeting, the Board directed its staff to send letters to two teeth whitening manufacturers with the intention of discouraging or preventing the companies from providing products and equipment to non-dentist teeth whitening service providers in North Carolina. (IDF 264, 276, 286.)
- In late 2007 the Board unanimously voted to send letters to mall operators to dissuade them from leasing space to non-dentist teeth whiteners. (IDF 289, 292.)

There is also a wealth of circumstantial evidence tending to show that the members of the Board had a common scheme to exclude non-dentist teeth whiteners. In particular, members of the Board engaged in a consistent practice of discouraging non-dentist teeth whitening services by sending dozens of cease and desist letters and other communications to providers of these services (IDF 207-45), manufacturers and distributors (IDF 261-80), mall owners and operators (IDF 288-93), the cosmetology board (IDF 317-22), and potential entrants (IDF

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284). These communications were similar, regardless of the recipient (IDF 208-26, 262, 288, 320), and they had a common objective of discouraging non-dentist teeth whitening (IDF 234-45, 286-87, 293, 323). These cease and desist letters were on Board letterhead, indicated that the directives came from the Board, and stated that responses should be directed to the Board. (IDF 219 (listing exhibits).) Respondent acknowledged that the Board's case officers, all of whom were dentist Board members (IDF 184), were acting within their delegated authority when they sent the cease and desist letters. (Oral Argument Tr. 11-12.) The Board never took any steps to repudiate the actions of its case officers.

We agree with the ALJ that the consistency and frequency of the Board's message regarding non-dentist teeth whitening, over the course of several years and across the tenures of varying Board members (IDF 32), constitute probative circumstantial evidence of an agreement among Board members. (ID at 78.) We also find significant that on at least three occasions, members of the Board or Board counsel informed third parties that the Board was taking action against non-dentist teeth whitening kiosks. (IDF 201, 205; CX254 at 1; *see also* CX369 (noting that the Board had a "strategy" for addressing teeth whitening kiosks).) For example, after receiving an inquiry from a dentist about a teeth whitening kiosk in 2008, the Board's Chief Operations Officer responded that "we are currently going forth to do battle" with "bleaching kiosks" and that "[w]e've sent out numerous cease and desist orders throughout the state." (IDF 201; CX404 at 1-2.)

Respondent argues that the Board's use of multiple case officers and case-specific recommendations when investigating teeth whitening complaints demonstrates that Board members were acting independently when they sent the cease and desist letters. (RAB at 26.) To the contrary, the fact that multiple agents of the Board delivered a consistent message over a period of several years to numerous and various types of third parties with no repudiation by the Board tends to negate the possibility that they were acting independently and reinforces our conclusion that the Board's representatives were acting pursuant to the

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Board's agreement and plan to exclude non-dentist teeth whiteners.

B. Restraint Of Trade

In this Section, we review the challenged conduct of the Board under the rule of reason using the three alternative modes of analysis described in *Indiana Federation of Dentists*. We find that the inherently suspect nature of the conduct, the indirect evidence, and the direct evidence all indicate that the Board's concerted action is anticompetitive. We also find that Respondent has failed to advance a legitimate procompetitive justification for its conduct.

1. The Board's Conduct under *Polygram's* "Inherently Suspect" Framework

As discussed in Section V above, "not all trade restraints require the same degree of fact-gathering and analysis." *Polygram*, 136 F.T.C. at 327 (citing *Standard Oil Co. v. United States*, 221 U.S. 1, 65 (1911)); *see also California Dental*, 526 U.S. at 781 ("What is required . . . is an enquiry meet for the case, looking to the circumstances, details, and logic of a restraint"). Thus, in *Polygram*, we held that in a limited category of cases—when "the conduct at issue is inherently suspect owing to its likely tendency to suppress competition"—our "scrutiny of the restraint itself . . . without consideration of market power" is sufficient to condemn the restraint, unless the defendant can articulate a legitimate justification for that restraint. 136 F.T.C. at 344; *see also Oksanen*, 945 F.2d at 709 ("a detailed inquiry into a firm's market power is not essential when the anticompetitive effects of its practices are obvious"); *North Texas Specialty Physicians*, 528 F.3d at 362 (physicians group's collective negotiations of fee-for-service contracts "bear a very close resemblance to horizontal price fixing" such that inherently suspect analysis was appropriate); *Realcomp*, 2009 FTC LEXIS 250, at *55-73 (finding that restrictions imposed by real estate multiple listings service were inherently suspect because they "were, in essence, an agreement among horizontal competitors to restrict the availability of information" to consumers and that restricted "the ability of low-cost, limited service" rivals to compete).

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a. The Board's Conduct is Inherently Suspect

Applying *Polygram's* “inherently suspect” framework, we conclude that the challenged conduct of the Board can reasonably be characterized as “giv[ing] rise to an intuitively obvious inference of anticompetitive effect.” *California Dental*, 526 U.S. at 781; *see also Continental Airlines, Inc. v. United Airlines, Inc.*, 277 F.3d 499, 509 (4th Cir. 2002) (“the anticompetitive impact . . . is clear from a quick look”). Both accepted economic theory and past judicial experience with analogous conduct support our finding that “the experience of the market has been so clear . . . about the principal tendency” of this conduct so as to enable us to draw “a confident conclusion” that—absent any legitimate justification advanced by Respondent—competition and consumers are harmed by the Board’s challenged practices. *California Dental*, 526 U.S. at 781.

The challenged conduct is, at its core, concerted action excluding a lower-cost and popular group of competitors. The Board not only foreclosed non-dentist providers from access to equipment suppliers and customers, but also directly excluded these providers from the market by sending them cease and desist letters.

Teeth whitening is one of the most popular cosmetic dentistry procedures, resulting in significant income to North Carolina dentists, including those on the Board. (IDF 9-12, 104, 233.) In response to the popularity of teeth whitening, non-dentists began offering teeth whitening services in North Carolina at mall kiosks and other locations. (IDF 137-38.) These providers charged significantly less than dentists despite achieving similar results. (IDF 117, 147, 150)

Dentists soon began complaining to the Board about the lower prices offered by non-dentists for teeth whitening services. (IDF 194-96, 232.) Members of the Board likewise recognized that proliferation of non-dentist teeth whitening operations would adversely affect the income of dentists. (IDF 159-61.)

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In response to the complaints, the Board issued dozens of cease and desist letters to non-dentist teeth whitening service providers and distributors of teeth whitening equipment. (IDF 208-09, 216-18, 230, 262-83.) Some of the letters stated that the sale or use of non-dentist teeth whitening products constituted a misdemeanor. (IDF 265-66, 280.) The Board viewed these letters as having the force of law and recipients of these communications had a similar understanding. (IDF 240-46.) In addition, the Board warned potential entrants not to offer teeth whitening services unless supervised by a dentist (IDF 284-85), sent letters to mall owners and operators urging them not to lease space to non-dentist teeth whitening providers (IDF 97, 288-93), and enlisted the assistance of the cosmetology board to warn its licensees that providing teeth whitening services could be a misdemeanor. (IDF 314-23.) The goal and effect of sending these letters and other communications was to stop non-dentists from providing teeth whitening services. (IDF 234-57, 286-87.)

No advanced degree in economics is needed to recognize that exclusion of products from the marketplace that are desired by consumers is likely to harm competition and consumers, absent a compelling justification. Users of the excluded product are made worse off because they must either shift to other, less desirable types of products, or forgo making a purchase entirely. (Kwoka, Tr. 1008-13, 1016; Baumer, Tr. 1720-21, 1724; CX822 at 10.) Consumers of similar non-excluded products are also likely to be harmed because suppliers of those products will face less competition and therefore have a greater ability to raise prices or reduce service. (Kwoka, Tr. 1013-17; Baumer, Tr. 1700, 1763, 1781; CX822 at 10-11.) Excluding a rival product from the marketplace not only eliminates current competition from those providers, but also eliminates prospective competition from future entrants. (Kwoka, Tr. 1017-18; CX822 at 12.) These future competitors could offer additional sources of supply for the product, as well as new product innovations. (Kwoka, Tr. 1011, 1017-18.)

Respondent's economic expert acknowledged that the challenged conduct would tend to restrict supply and cause higher prices. (Baumer, Tr. 1700, 1719-21, 1724, 1726-27 (referring to CX822 at 13), 1763, 1781, 1839-41.) He testified on several

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occasions that this conclusion was a matter of “Econ 101,” meaning that it required no more than a rudimentary level of economic analysis. (Baumer, Tr. 1721, 1724, 1763, 1781, 1840.)

He explained that product exclusion would harm competition and consumers in terms of both price and choice.¹³ (Baumer, Tr. 1841.)

Agreements to exclude an entire class of competitors from the marketplace by foreclosing access to suppliers, customers, or the market itself have long been treated as per se illegal or presumptively illegal under the antitrust laws. In these cases, the methods of exclusion have varied but the holdings are consistent in condemning such conduct with little, if any, consideration of any purported defenses.

In *Fashion Originators’ Guild of America, Inc. v. FTC*, 312 U.S. 457 (1941), manufacturers of women’s garments, working through an industry association, boycotted retailers that sold copies of their original designs. The Supreme Court affirmed the FTC’s conclusion that this scheme was an unfair method of competition, notwithstanding the organization’s claim that the copying of garment designs was a tortious act. The Court explained that the association’s policy “has both as its necessary tendency and as its purpose and effect the direct suppression of competition.” *Id.* at 465. The Court was particularly concerned that the scheme, if successful, would have eliminated an entire class of competitors—as the Court called it, a “rival method of competition”—from the marketplace. *Id.* at 467. The Court concluded that the manufacturers’ prevention-of-torts defense was not cognizable under the antitrust laws: “even if copying were an acknowledged tort under the law of every state, that situation would not justify petitioners in combining together to regulate and

¹³ Dr. Baumer qualified this testimony by noting that consumers might not be harmed by higher prices and fewer competitive options if they “felt like the market was safer” and, as a result, increased their consumption of the remaining products in the market. (Baumer, Tr. 1724; *see also id.* at 1727.) However, Dr. Baumer did not offer an opinion, and Respondent has not identified any evidence, that (a) safety concerns currently inhibit some consumers from whitening their teeth or (b) that prohibiting non-dentist teeth whitening would lead to the perception that teeth whitening is a safer practice, thereby increasing overall demand for teeth whitening products.

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restrain interstate commerce in violation of federal law.” *Id.* at 468.

The Supreme Court addressed exclusion of a class of competitors again in *United States v. General Motors Corp.*, 384 U.S. 127 (1966). In that case, a group of Chevrolet automobile dealers successfully pressured General Motors not to sell to dealers that resold their inventory through discounters. The conspiring dealers then established a monitoring venture to ensure compliance. The Court found that the “[e]xclusion of traders from the market by means of combination or conspiracy is . . . inconsistent with the free-market principles embodied in the Sherman Act” and per se illegal. *Id.* at 146. The Court was especially troubled that one of the purposes of the concerted effort “was to protect franchised dealers from real or apparent price competition.” *Id.* at 147. Consistent with the *Fashion Originators’ Guild* case, the Court declined to consider the parties’ asserted justification—in this case, that sales to discounters violated the dealers’ franchise agreements. *Id.* at 139-40.

The Supreme Court has likewise held that agreements to exclude a single competitor are per se illegal or presumptively illegal. For example, in *Radiant Burners, Inc. v. Peoples Gas Light & Coke Co.*, 364 U.S. 656 (1961), a manufacturer alleged that an industry association refused to grant a “seal of approval” to its ceramic gas burner because of the influence of competitors in the association. As a result of the association’s action, the manufacturer’s burner was “effectively excluded from the market.” *Id.* at 658. The Court held that the plaintiff had alleged a per se illegal boycott because of its “monopolistic tendency,” notwithstanding that the victim was limited to a single manufacturer. *Id.* at 660 (quoting *Klor’s, Inc. v. Broadway-Hale Stores*, 359 U.S. 207, 213 (1959)).

Similarly, in *American Society of Mechanical Engineers, Inc. v. Hydrolevel Corp.*, 456 U.S. 556 (1982), the dominant fuel cutoff manufacturer used its influence in ASME, a standards organization, to prevent the organization from approving a rival’s alternative design. ASME’s standards were so influential that, according to the Court, it was “in reality an extra-governmental agency, which prescribes rules for the regulation and restraint of

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interstate commerce.” *Id.* at 570 (quoting *Fashion Originators’ Guild*, 312 U.S. at 465). The jury found ASME liable under Section 1, and the Court affirmed. While the issue before the Court was whether a standards organization could be liable for the acts of its agents, the Court nevertheless commented that the “anticompetitive practices of ASME’s agents are repugnant to the antitrust laws.” *Id.* at 574. Participants in standards organizations have “the power to frustrate competition in the marketplace . . . [and] to harm their employers’ competitors through manipulation of [the standards organization’s] codes.” *Id.* at 571.

In its most recent decision addressing competitor exclusion, the Court, citing to *Fashion Originators’ Guild*, *General Motors*, and *Radiant Burners*, held that certain concerted refusals to deal or group boycotts remain per se violations of the Sherman Act. See *Northwest Wholesale Stationers v. Pacific Stationary & Printing Co.*, 472 U.S. 284, 290 (1985); see also *Oksanen*, 945 F.2d at 708 (“Certain forms of agreements, such as varieties of group boycotts, have been classified as per se violations.”). Where competitors “cut off access to a supply, facility, or market necessary to enable the boycotted firm to compete,” *Northwest Wholesale Stationers*, 472 U.S. at 294, the conduct may be conclusively presumed to be anticompetitive, at least when it does not “enhance overall efficiency and make markets more competitive.” *Id.* In contrast, courts apply the rule of reason to competitor exclusions if the restraints are imposed by a joint venture that lacks market power or exclusive access to an element essential to effective competition. See *id.* at 295-96.

Here, the challenged conduct consists of concerted action denying non-dentist teeth whiteners access to both suppliers and customers (by foreclosing access to retail space), as well as to the market itself. As such, the Board’s conduct bears a close resemblance to conduct that the Supreme Court has condemned as per se illegal and that the Court continues to treat as conclusively anticompetitive under *Northwest Wholesale Stationers*. Cf. *North Texas Specialty Physicians*, 528 F.3d at 362 (inherently suspect analysis appropriate where restraints “bear a very close resemblance to horizontal price fixing”). Furthermore, as discussed below, this is not a case involving conduct plausibly

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designed to enhance competition for teeth whitening products or services.

Respondent contends that *Fashion Originators' Guild*, *General Motors*, *Radiant Burners*, *Hydrolevel*, and *Northwest Wholesale Stationers* are inapposite because they involved private organizations, such as professional associations, rather than state licensing boards. (RRB at 16-17.) We disagree. The competitive concern in both of these contexts is that an organization with the power to exclude is used to facilitate or enforce an anticompetitive agreement among private parties. If anything, state agencies, such as the Board, are likely to have greater ability to enforce restrictions than private organizations. The Court has noted the significant potential for competitive injury stemming from concerted conduct among private parties enforced by state agencies. *See, e.g., Hydrolevel*, 456 U.S. at 570-74 (condemning an agreement among private actors that was enforced by state agencies); *Allied Tube & Conduit Corp. v. Indian Head*, 486 U.S. 492, 500 (1988) (an agreement to manipulate a vote of a standard setting organization whose codes were routinely adopted by state and local governments raises a “serious potential for anticompetitive harm”).

Furthermore, as conceded by Respondent’s economic expert, state licensing boards, including dental boards, have a history of enforcing restrictions designed to enhance the income of their licensees at the expense of consumers, even though members of these organizations had taken oaths to protect the public health.¹⁴ (Baumer, Tr. 1847-54, 1855 (“self-interest definitely had an impact”), 1884, 1896-1901, 1912-17; CX826 at 11 (“The public lost at the expense of the professional.”) (Baumer, Dep. at 36-37)). Some medical boards and other professional healthcare boards continue to engage in these anticompetitive practices. (Baumer, Tr. 1898, 1901-04, 1911-12; CX826 at 12, 36 (Baumer Dep. at 39, 136).) As a result, “when there’s licensing taking place, my ears go up, . . . [and] we look very carefully for

¹⁴ Respondent’s expert acknowledged that some of these concerns are presented by this case. In particular, Dr. Baumer observed that the Board is concerned about the financial interests of North Carolina dentists and that those interests could have affected the Board’s decision to exclude non-dentist teeth whitening providers. (Baumer, Tr. 1856-62.)

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evidence of anticompetitive behavior.” (Baumer, Tr. 1897.) This testimony reinforces our conclusion that a more deferential standard should not be applied to concerted activity enforced through a state agency controlled by financially interested actors than through a private body.

In sum, the challenged conduct—an agreement among competitors to exclude other competitors from the market by preventing their access to suppliers, customers, and the market itself—bears a close resemblance to conduct condemned by the Supreme Court as *per se* illegal. As conceded by Respondent’s economic expert, such conduct has an obvious tendency to suppress competition, increase prices, and harm consumers of teeth whitening products and services. In particular, the restraints alleviate downward price pressure on dentists and eliminate an entire class of product desired by some consumers. We therefore conclude that the challenged conduct is inherently suspect under *Polygram* and thus presumptively unreasonable unless Respondent can produce a legitimate justification.

b. The Board’s Proffered Justifications

Although the Board’s actions had a clear tendency to suppress competition and harm consumers, the *Polygram* framework requires consideration of whether Respondent can overcome this presumption of unreasonableness by showing that the practice has “some countervailing procompetitive virtue.” *Indiana Federation of Dentists*, 476 U.S. at 459; *see also Northwest Wholesale Stationers*, 472 U.S. at 294 (practices can be “justified by plausible arguments that they were intended to enhance overall efficiency and make markets more competitive”); *Continental Airlines*, 277 F.3d at 510 (“even when a court eschews a full rule-of-reason analysis and so forgoes detailed examination of the relevant market, it must carefully consider a challenged restriction’s possible procompetitive justifications”).

A cognizable justification is ordinarily one that stems from measures that increase output or improve product quality, service, or innovation. *See Indiana Federation of Dentists*, 476 U.S. at 459 (procompetitive justifications include “creation of efficiencies in the operation of a market or the provision of goods and services”); *Broadcast Music*, 441 U.S. at 19-20 (courts should

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examine whether the practice will “increase economic efficiency and render markets more, rather than less, competitive” (quotation and citation omitted)); *Paladin Associates v. Montana Power Co.*, 328 F.3d 1145, 1157 (3d Cir. 2003) (“improving customer choice” and reducing costs are procompetitive justifications); *Polygram*, 136 F.T.C. at 345-46.

A plausible justification is one that “cannot be rejected without extensive factual inquiry.” *Polygram*, 136 F.T.C. at 347. “The defendant, however, must do more than merely assert that its purported justification benefits consumers . . . [rather,] it must articulate the specific link between the challenged restraint and the purported justification.” *Id.*; see also *North Texas Specialty Physicians*, 528 F.3d at 368 (“some facial plausibility” of purported justification insufficient to rebut liability under abbreviated rule of reason analysis).

If a justification is not only cognizable but also plausible, then further examination of the restraint’s effect on competition is warranted. Otherwise, “the case is at an end and the practices are condemned.” *Polygram*, 136 F.T.C. at 345.

Respondent offers three justifications for its conduct, all of which were rejected by the ALJ.¹⁵ Respondent’s first asserted defense is that its actions were intended to promote public health and welfare. Respondent asserts that there are health and safety risks when teeth whitening is performed by a non-dentist and that the ALJ erred by not making any findings as to the safety of non-dentist teeth whitening. (RAB at 7-10, 39.) Similarly, Respondent urges that we recognize a defense, separate and apart from the state action defense, based on a state agency’s enforcement of a state statute. (RAB at 29-34, 39.)

¹⁵ Respondent also asserts as a justification that its conduct constituted state action, an argument that the Commission rejected in its February 3, 2011 decision. See *North Carolina Dental*, 151 F.T.C. at 615-33. In the proceedings below, Respondent asserted that permitting non-dentists to perform teeth whitening could result in the production of an inferior service. The ALJ rejected that argument, explaining that such a claim was tantamount to an assertion that competition itself is harmful (ID at 108-09), and Respondent does not contest the ALJ’s resolution of that issue here.

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Courts have rejected social welfare and public safety concerns as cognizable justifications for restraints on competition. In *Professional Engineers*, the Supreme Court reviewed a trade association ethics rule that effectively prohibited engineers from engaging in competitive bidding. The association asserted as a defense that “awarding engineering contracts to the lowest bidder, regardless of quality, would be dangerous to public health, safety, and welfare.” *Professional Engineers*, 435 U.S. at 685. The Court held that such a defense was not cognizable under the Sherman Act:

The Sherman Act reflects a legislative judgment that ultimately competition will produce not only lower prices, but also better goods and services. . . . The assumption that competition is the best method of allocating resources in a free market recognizes that all elements of a bargain—quality, service, safety, and durability—and not just the immediate cost, are favorably affected by the free opportunity to select among alternative offers. . . . The fact that engineers are often involved in large-scale projects significantly affecting the public safety does not alter our analysis. Exceptions to the Sherman Act for potentially dangerous goods and services would be tantamount to a repeal of the statute. In our complex economy, the number of items that may cause serious harm is almost endless

Id. at 695. The association’s defense that competition would lead consumers to choose dangerous and inferior quality services was therefore rejected as a matter of law.

Similarly, in *Indiana Federation of Dentists*, the Court held that a health and safety defense was not available for an alleged Sherman Act violation in the dental field. In that case, a group of dentists agreed not to submit x-rays to insurers, asserting that “the provision of x-rays might lead the insurers to make inaccurate determinations of the proper level of care and thus injure the health of the insured patients.” 476 U.S. at 452. Accepting this argument, according to the Court, would have been “nothing less than a frontal assault on the basic policy of the Sherman Act.” *Id.* at 463 (quoting *Professional Engineers*, 435 U.S. at 695). The Court explained that prevention of “unwise and even

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dangerous choices” was not a cognizable justification for collusion. *Id.* at 463.

In *Virginia Academy of Clinical Psychologists v. Blue Shield of Virginia*, 624 F.2d 476 (4th Cir. 1980), two health plans controlled by physicians agreed not to pay for services rendered by clinical psychologists unless those services were billed through a physician. The Fourth Circuit, reversing the district court, found that the policy would reduce “consumer and provider alternatives” and increase costs. *Id.* at 486. The court rejected the health plan’s argument that physician supervision of psychologists was necessary for optimum health outcomes, explaining that “we are not inclined to condone anticompetitive conduct upon an incantation of ‘good medical practice.’” *Id.* at 485; *see also Wilk v. AMA*, 719 F.2d 207, 228 (7th Cir. 1983) (“[A] generalized concern for the health, safety and welfare of members of the public . . ., however genuine and well-informed such a concern may be, affords no legal justification for economic measures to diminish competition with [chiropractors] by [some medical doctors].”)

Respondent contends that the preceding line of cases is distinguishable because the cases do not involve a state agency acting pursuant to a state statute. Respondent asserts that a valid defense to a Sherman Act claim exists where a state agency is “promoting the public health and enforcing state law,” even where the requirements of the state action doctrine are not satisfied. (RAB at 32.) Although Respondent asserts that such a defense is consistent with a line of lower court cases allegedly justifying conduct based on “public service or ethical norms” (RAB at 31-32), Respondent does not cite to any cases on point and we are aware of no authority for such a defense.

To the extent that Respondent’s claims are premised on principles of federalism and a concern with state prerogatives, the Supreme Court has already defined the contours for such a defense. *See Parker v. Brown*, 317 U.S. 341 (1943). Almost 70 years ago, the Supreme Court created the state action defense for state or private actors acting pursuant to a state regulatory program. As we concluded in our February 3, 2011 decision, that defense requires a showing of both “clear articulation” and “active

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supervision” for state boards controlled by financially interested members, such as Respondent. *See North Carolina Dental*, 151 F.T.C. at 617-28. Respondent’s proposal would substantially weaken these requirements. As we understand Respondent’s position, it would only have to show “articulation” to make out a defense, rather than both “clear articulation” and “active supervision.” Given that the Supreme Court has already established a defense for Sherman Act claims based on the actions of state officials and that Respondent’s proposed “enforcement of state law” defense has the potential to seriously undermine the state action doctrine, we see no reason to recognize Respondent’s proposed new defense.

To the extent that Respondent’s defense is meant to invoke a competitive analysis, Respondent has failed to explain why the Board’s status as a state agency changes the likely competitive impact of its conduct and therefore renders the relevant case law rejecting health and safety defenses inapplicable. There is nothing in those decisions to suggest that they turned on this distinction. To the contrary, the Court rejected the notion of a health or safety defense because it was extraneous to an analysis of competitive effects, not because of the private nature of the actors. *See Professional Engineers*, 435 U.S. at 695; *Indiana Federation of Dentists*, 476 U.S. at 463.

Respondent’s public safety defense fails for another reason: the challenged actions of the Board are not consistent with its enforcement mandates under the Dental Practice Act. The Complaint does not challenge the Board’s enforcement of the Dental Practice Act against non-dentist teeth whiteners in the state courts, which is the only way the Board is authorized to enforce the Act (other than referring a case to a state prosecutor). *See* N.C. General Statutes § 90-40.1; IDF 43, 44, 190; Response to Complaint ¶ 19; RAB at 2-3; RRB at 5. Rather, this proceeding challenges actions, including sending cease and desist letters to non-dentists, that were not authorized by the Dental Practice Act. *See* N.C. General Statutes §§ 90-27, -29, -40, -40.1; IDF 45-49, 190.

Finally, even if a public safety defense were cognizable under the antitrust laws, we would find that Respondent had failed to

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introduce sufficient evidence to establish such a justification.¹⁶ Although several Board members identified a number of theoretical risks from non-dentist teeth whitening, none was able to cite to any clinical or empirical evidence validating any of these concerns. (Response to RFA 21, 38, 39; *see also* Hardesty, Tr. 2818, 2829; CX565 at 38 (Hardesty Dep. at 145); CX554 at 26 (Allen Dep. at 95-96); CX555 at 16, 26 (Brown Dep. at 55-56, 97); Wester, Tr. 1313-15, 1402, 1405-06; CX560 at 65-66 (Feingold Dep. at 252-54); CX567 at 37 (Holland Dep. at 138-40); CX564 at 16 (Hall Dep. at 55-56); Owens, Tr. 1664.) Likewise, Respondent's expert witness, Dr. Haywood, testified that he was unaware of any scientific evidence demonstrating any consumer injury from non-dentist teeth whitening.¹⁷ (Haywood, Tr. 2696, 2713-14, 2729; CX402 at 5 ("The effects on pulp have . . . no clinical consequence other than immediate but transient sensitivity."))

Respondent points to four alleged instances of possible consumer injury caused by non-dentist teeth whitening that were brought to the Board's attention. (RAB at 10.) However, we question whether four anecdotal reports of harm over a multi-year period based on products considered safe by the FDA (Giniger, Tr. 155, 250, 256) and used over a million times over the last twenty years (Giniger, Tr. 122, 257) could constitute adequate evidence of a potential health or safety risk. (Kwoka, Tr. 1078.)

¹⁶ Respondent asserts that because Complaint Counsel did not file an appeal from the ALJ's Initial Decision, under FTC Rule of Practice 3.52(b), 16 C.F.R. § 3.52(b), the Commission may not make any new factual findings or legal conclusions requested by Complaint Counsel. (RRB at 1, 9.) Rule 3.52(b) contains no such limitation; furthermore, under Rule 3.54, 16 C.F.R. § 3.54, the Commission can conduct a *de novo* review of the entire record and make factual findings and conclusions of law to the same extent as the ALJ.

¹⁷ Dr. Haywood's principal concern with non-dentist teeth whitening is that it may mask a pathology. (Haywood, Tr. 2950; CX823 at 20 (Haywood Dep. at 70)). However, as Dr. Giniger testified, it is highly unlikely that non-dental teeth bleaching would make a tooth so white as to make a pathology undetectable by a dentist or for a pathology not to present other symptoms such as swelling, purulence, pain, or redness. (Giniger, Tr. 301-20, 356, 437-38). Furthermore, there are no studies or case reports identifying an incident of masked pathology from any form of teeth bleaching (Giniger, Tr. 301-02, 319-20; Haywood, Tr. 2734-35, 2928-32), despite the tens of millions of instances of over-the-counter teeth whitening (CX585 at 9).

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Compounding this concern is the lack of any investigation or medical documentation with respect to two of the four reports of injury. (RX17 at 1, 2.) In the third case, a dentist's examination revealed that the patient suffered from bone loss and infection unrelated to the teeth whitening procedure and that any discomfort from the teeth whitening procedure would be temporary and treatable. (CX575 at 15-24 (Hasson Dep. at 53-89).) The fourth reported case of harm is somewhat more compelling, but even in this case, the reported injuries do not appear to have been permanent and may have been caused by a preexisting pathology. (Runsick, Tr. 2136; Giniger, Tr. 274-77.)

The lack of contemporaneous evidence that the challenged conduct was motivated by health or safety concerns reinforces our rejection of Respondent's public safety defense on the merits. Respondent has not identified any evidence that the Board concluded prior to embarking on the challenged conduct that non-dentist teeth whitening was an unsafe practice. Indeed, Respondent was unable to point us to any such evidence at oral argument. (Oral Argument Tr. 17-19, 21-22, 33-34.) Moreover, the Board began issuing cease and desist letters two years before it received any reports of consumer injury. (*Compare* CX38 at 1 (first cease and desist letter, dated January 11, 2006), *with* CX476 at 1 (first complaint claiming injury, dated February 20, 2008); *see also* Respondent's Proposed Finding of Fact 459 (acknowledging that the Board received the first complaint of injury "in or about 2008").) Indeed, with just two possible exceptions—the cease and desist letters to Port City Tanning and Lite Bright—none of the challenged conduct of the Board appears to have been motivated by even the pretext of specific health or safety concerns. (CX59 (cease and desist letter to Port City Tanning); RX21 at 3-7 (complaint of injury regarding Port City Tanning); CX388 (cease and desist letter to Lite Bright); RX17 at 1, 2 (complaints of injury regarding Lite Bright)).

In contrast, there was a wealth of evidence presented at trial suggesting that non-dentist provided teeth whitening is a safe cosmetic procedure. (Giniger, Tr. 121-24, 134-35, 145-47, 155-57, 212-30, 239-65, 354-56, 445-47, 453-55; Nelson, Tr. 771; Osborn, Tr. 664-65; Valentine, Tr. 547.) Despite the millions of teeth whitening procedures performed by non-dentists,

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Respondent points to no studies suggesting any health risks (other than transient sensitivity) from the procedure. (*Cf.* Giniger, Tr. 121-23, 147, 217-19, 257-58, 355-56, 453-55 (asserting that there are no studies indicating a health risk from non-dental teeth whitening).) Consequently, the record as a whole fails to substantiate Respondent's public safety claims.

Respondent's second defense is that its actions were intended to promote "legal competition." (RAB at 20, 31.) As an initial matter, however, North Carolina courts have never concluded that teeth whitening services provided by non-dentists are unlawful. (ID at 8, 109; Oral Argument Tr. 49.) More significantly, the Supreme Court has repeatedly rejected this argument as a matter of antitrust doctrine. In *Indiana Federation of Dentists*, a group of dentists attempted to justify their withholding of x-rays from insurance companies by arguing that an insurance company's review of dental x-rays would constitute the unauthorized practice of dentistry under state law. The Court dismissed this argument: "That a particular practice may be unlawful is not, in itself, a sufficient justification for collusion among competitors to prevent it." 476 U.S. at 465. Likewise, in *Fashion Originators' Guild*, the Court held that even if the sale of the excluded products was tortious, "that situation would not justify petitioners in combining together to regulate and restrain interstate commerce in violation of federal law." 312 U.S. at 468. In both of these cases, the Court found it unnecessary to decide whether the excluded product or practice actually violated state law. Accordingly, we do not credit this defense.

Respondent's third defense is that it acted "in good faith." (RAB at 32.) This is not a valid defense under the antitrust laws. The Supreme Court has held that "good motives will not validate an otherwise anticompetitive practice." *NCAA*, 468 U.S. at 101 n.23; *see also United States v. Griffith*, 334 U.S. 100, 105-06 (1948) (practice may be condemned even if respondent "had no intent or purpose unreasonably to restrain trade"); *Associated Press v. United States*, 326 U.S. 1, 16 n.15 (1945) ("the Sherman Act cannot 'be evaded by good motives. The law . . . cannot be set up against it in a supposed accommodation of its policy with the good intention of parties'" (quoting *Standard Sanitary Manufacturing Co. v. United States*, 226 U.S. 20, 49 (1912)));

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Chicago Board of Trade v. United States, 246 U.S. 231, 238 (1918) (rejecting notion that “a good intention will save an otherwise objectionable regulation”).

Accordingly, under *Polygram’s* “inherently suspect” framework, we conclude that the Board’s conduct is unreasonable and violates both Section 1 of the Sherman Act and Section 5 of the FTC Act. We next consider whether a more elaborate rule of reason analysis, encompassing considerations of market power and effects, provides an alternative basis for our conclusion that the Board’s conduct is anticompetitive.

2. The Board’s Conduct under the Full Rule of Reason

In this section, we evaluate the Board’s conduct under a more fulsome rule of reason analysis and again conclude that the Board’s conduct violates the antitrust laws. As indicated in Section V, *supra*, a plaintiff can establish an affirmative case in either of two ways. It can do so indirectly by demonstrating the defendant’s market power, which, when combined with the anticompetitive nature of the restraints, provides the necessary confidence to predict the likelihood of anticompetitive effects. Or, the plaintiff can provide direct evidence of “actual, sustained adverse effects on competition” in the relevant markets, which would be “legally sufficient to support a finding that the challenged restraint was unreasonable”—whether or not the plaintiff has made any showing regarding market power. *Indiana Federation of Dentists*, 476 U.S. at 461; *see also Realcomp*, 635 F.3d at 825 (“If [Respondent’s] challenged policies are shown to have anticompetitive effect, or if [Respondent] is shown to have market power and to have adopted policies *likely* to have an anticompetitive effect, then the burden shifts to [Respondent] to provide procompetitive justifications for the policies.”); *Tops Markets, Inc. v. Quality Markets, Inc.*, 142 F.3d 90, 96 (2d Cir. 1998) (plaintiff has “two independent means by which to satisfy the adverse-effect requirement”—direct proof of “actual adverse effect on competition” or “indirectly by establishing . . . sufficient market power to cause an adverse effect on competition”); *Law*, 134 F.3d at 1019 (“plaintiff may establish anticompetitive effect indirectly by proving that the defendant possessed the requisite market power within a defined market or directly by showing

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actual anticompetitive effects”); *Brown University*, 5 F.3d at 668 (similar).

Under this full rule of reason analysis, we find support in the record for a conclusion that the Board’s agreement is anticompetitive, which shifts the burden to Respondent to produce a legitimate countervailing justification in order to avoid condemnation. Since Respondent has failed to assert a legitimate, procompetitive justification, we conclude that the Board’s concerted action violates Section 1 of the Sherman Act and Section 5 of the FTC Act.

a. The Board Possesses Market Power in the Market for Teeth Whitening Products and Services

At this stage of the proceeding, the parties do not dispute that the relevant market consists of four types of teeth whitening: dentist in-office services, dentist take-home kits, non-dentist service providers, and over-the-counter products.¹⁸ (RAB at 10-11, 27; CCAB at 32.) All four of these products perform the same function (teeth whitening) using a similar technique (application of a form of peroxide to the teeth). (IDF 106-50.) See *Brown Shoe Co. v. United States*, 370 U.S. 294, 325 (1962) (the “boundaries of a product market are determined by the reasonable interchangeability of use or the cross-elasticity of demand between the product itself and substitutes for it”); *United States v. E. I. du Pont de Nemours & Co.*, 351 U.S. 377, 395 (1956); *Greenville Publishing Co. v. Daily Reflector, Inc.*, 496 F.2d 391, 399 (4th Cir. 1974) (a relevant market is defined by the scope of “reasonable interchangeability”).

The record shows that market participants view themselves as offering comparable services, recognize that substantial price and non-price competition exists between them, and target their advertising toward consumers who may be considering using a different type of teeth whitening service. (IDF 157-69.) Respondent’s economic expert testified that the four types of teeth

¹⁸ In light of the parties’ agreement on the relevant market, we have no need to consider whether same-day teeth whitening services (dentist in-office services and non-dentist providers) constitute an additional relevant market, as found by the ALJ. (ID at 63-71.)

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whitening are differentiated products within an overall teeth whitening market. (Baumer, Tr. 1711.) He also testified that there is a high cross-elasticity among the four types of teeth whitening products. (Baumer, Tr. 1842-45.) Complaint Counsel's economic expert, while disclaiming an opinion on the relevant market, did not dispute Respondent's expert in this respect and further testified that "these alternative methods are in fact very much in competition with one another." (Kwoka, Tr. 997-1000.) The parties also agree that the relevant geographic market is North Carolina. (ID at 64.)

The ALJ concluded, and Respondent does not dispute,¹⁹ that the Board has market power based on the Board's power to exclude competition. *See du Pont*, 351 U.S. at 391 ("Monopoly power is the power to control prices or exclude competition."); *Hydrolevel*, 456 U.S. at 570-71 (finding that standard setting organization had market power based on power to exclude). We agree.

The Board, as the agency with power to enforce the Dental Practice Act, has the authority to regulate and discipline dentists in North Carolina. *See* N.C. General Statutes §§ 90-30, -31, -34, -40, -40.1, -41, -42; *cf. Massachusetts Board of Optometry*, 110 F.T.C. at 588 (state optometry board possessed market power on account of its ability to regulate the business of optometry and "to impose sanctions on any optometrist who fails to obey its rules and regulations"). In addition, the Board was able to use its perceived authority to exclude non-dentists from providing teeth whitening services in North Carolina. (IDF 240-56, 324-27). Respondent's expert agreed, noting that the Board has "the power to exclude competition" (CX826 at 36 (Baumer Dep. at 136-37); *see also* Baumer, Tr. 1722 ("The board has the power to exclude.")) and the power to impose entry barriers (Baumer, Tr. 1840).

¹⁹ Respondent briefly contests the ALJ's finding of market power in its reply brief (RRB at 15) but failed to address this issue in its opening brief, thereby waiving the argument. Rule 3.52, 16 C.F.R. § 3.52 ("The Commission will not consider new arguments or matters raised in reply briefs that could have been raised earlier in the principal briefs."). As noted in the text, even absent a waiver, we would find that the Board had market power.

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b. Indirect Evidence of Anticompetitive Effects

The ALJ's uncontested finding of market power, coupled with our earlier determination that the challenged conduct would tend to suppress competition, provides "indirect" evidence that those policies have or likely will have anticompetitive effects. *See Craftsmen Limousine, Inc. v. Ford Motor Co.*, 491 F.3d 380, 388 (8th Cir. 2007); *Law*, 134 F.3d at 1019; *Tops Markets*, 142 F.3d at 96; *Levine v. Central Florida Medical Affiliates, Inc.*, 72 F.3d 1538, 1551 (11th Cir. 1996); *Brown University*, 5 F.3d at 669; *Realcomp*, 2009 FTC LEXIS 250, at *95. As the Sixth Circuit recently explained, "[m]arket power and the anticompetitive nature of the restraint are sufficient to show the potential for anticompetitive effects under a rule-of-reason analysis, and once this showing has been made, [Respondent] must offer procompetitive justifications." *Realcomp*, 635 F.3d at 827; *see also id.* at 827 n.6 (observing that "[o]ther circuits have permitted an inference of adverse effects based on a showing of market power and anticompetitive tendencies.").

In light of the Board's market power and the facially restrictive nature of the policies at issue, no additional analysis is required under the rule of reason to support our conclusion that the Board's restraints are unreasonable because they will predictably result in harm to competition.

c. Direct Evidence of Anticompetitive Effects

The ALJ found, and we agree, that the Board's concerted action resulted in the exclusion of non-dentist providers from the market and the prevention of new entry by potential suppliers, both of which injured competition and consumers. (ID at 97-104.) This finding of actual anticompetitive effects—which Respondent does not dispute in its appeal to the Commission—is by itself sufficient to shift the burden to Respondent to produce a procompetitive justification. *See Realcomp*, 635 F.3d at 827 ("If adverse effects are clear, inquiry into market power is unnecessary."); *Law*, 134 F.3d at 1019 ("showing actual anticompetitive effects" satisfies plaintiff's initial burden); *Brown University*, 5 F.3d at 668 (plaintiff can meet its initial burden under the rule of reason "by proving the existence of actual anticompetitive effects, such as reduction of output, increase in

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price, or deterioration in quality of goods or services” (citation omitted)).

The undisputed evidence shows that, as a result of the Board’s actions—including sending cease and desist letters to providers and manufacturers, sending letters to mall operators, and posting a warning on the cosmetology board’s website—numerous non-dentist teeth whitening providers in North Carolina stopped offering teeth whitening services. (IDF 246-56, 324-27; *see also* IDF 284-85 (potential entrants discouraged from entering).) The Board’s actions also cut off access to leading suppliers of teeth whitening products and retail space used by non-dentist providers. (IDF 70-72, 98, 267-70, 272, 277-83, 294-313.) Respondent’s economic expert acknowledged that “[n]ot surprisingly, the actions of the State Board were effective and many kiosk and spa operator[s] . . . ceas[ed] their actions.” (RX78 at 8; *see also* Baumer, Tr. 1720 (“we know that post-exclusion non-dentist teeth whitening is reduced”); Kwoka, Tr. 1136 (“the letters were effective”).)

The parties’ experts agreed that the Board’s exclusion of non-dentist providers led to higher prices, although they disputed the extent of the price increase. (Kwoka, Tr. 1029-32 (there is “a substantial price effect”); Baumer, Tr. 1732 (“I can’t disagree” with the claim that “there’s a small impact” on price), 1815 (the Board’s actions caused “maybe slightly higher prices”); RX140 at 11). In reaching these conclusions neither party’s economic expert prepared a quantitative analysis of the price effects of the Board’s restraints.

In light of the restraints’ obvious disruption of the “proper functioning of the price-setting mechanism of the market,” a precise quantification of the price increase was unnecessary. *Indiana Federation of Dentists*, 476 U.S. at 461-62; *see also United States v. Microsoft Corp.*, 253 F.3d 34, 79 (D.C. Cir. 2001) (when dealing with emerging competition, no showing of actual harm is required; the proper test is whether “the exclusion of nascent threats [would be] . . . reasonably capable of contributing significantly to a defendant’s continued monopoly power.”); *Realcomp*, 2009 FTC LEXIS 250, at *46 (“elaborate econometric proof that [the restraint] resulted in higher prices” is unnecessary

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(quotation omitted)). This is particularly true in this case, given the parties' agreement that data were not available to do a study of price effects. (Kwoka, Tr. 1029-39, 1187; Baumer, Tr. 1978-79; CX822 at 15.)

In addition to increasing prices, the Board's conduct deprived consumers of choice. *Realcomp*, 2009 FTC LEXIS 250, at *111 (liability under rule of reason appropriate if respondent's practices "narrow consumer choice or hinder the competitive process"). The Board deprived consumers of the option of going to a mall, salon, or spa for teeth whitening services. In addition, consumers can no longer obtain same-day teeth whitening services (unless their local dentist provides walk-in teeth whitening service). The courts recognize that the elimination of products desired by consumers reduces consumer welfare. *Indiana Federation of Dentists*, 476 U.S. at 459 (absent a procompetitive virtue, "an agreement limiting consumer choice . . . cannot be sustained under the Rule of Reason"); *Conwood Co. v. U.S. Tobacco Co.*, 290 F.3d 768, 789 (6th Cir. 2002) (defendant's "actions caused higher prices and reduced consumer choice, both of which are harmful to competition"). Both parties' experts agree. (Kwoka, Tr. 1031-33, 1102, 1181-82; Baumer, Tr. 1776 (referring to CX822 at 29); 1974-76; CX822 at 16.)

d. Procompetitive Justifications

Notwithstanding our finding that the Board's conduct is anticompetitive under a more fulsome rule of reason analysis, Respondent may be able to defeat a finding of liability if its practices can be "justified by plausible arguments that they were intended to enhance overall efficiency and make markets more competitive." *Northwest Wholesale Stationers*, 472 U.S. at 294.

As discussed at length in Section VI.B.1.b above, however, Respondent's proffered justifications fail to satisfy those standards. Respondent asserts that its effort to exclude non-dentist providers of teeth whitening services would promote public safety and protect "legal competition" for teeth whitening services. Under Supreme Court precedent, these are not valid justifications for anticompetitive conduct. Furthermore, the asserted defenses do not appear to be plausibly related to any goal

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of the antitrust laws, such as increasing output or innovation. Accordingly, Respondent has failed to overcome the anticompetitive effects of its conduct with any legitimate, procompetitive justifications. We therefore conclude that the Board's actions also violated the antitrust laws under a full rule of reason analysis.

VII. REMEDY

To remedy Respondent's violation of Section 5, the ALJ issued an Order prohibiting the Board from directing non-dentists to cease providing teeth whitening products and services. (ID at 110-17, 123-30.) The Order also requires the Board not to communicate to any current or prospective non-dentist provider, lessor of commercial property, or actual or prospective distributor of teeth whitening products that a non-dentist's teeth whitening products or services violate the Dental Practice Act. (ID at 112, 124.) However, the ALJ's Order expressly carves out certain Board actions from these prohibitions (to which we make one addition). The Order does not prohibit the Board from investigating and prosecuting suspected violations of the Dental Practice Act. Further, the Order permits the Board to communicate its opinion that certain teeth whitening products or services may violate the Dental Practice Act, and its bona fide intention to seek court action or to seek administrative remedies for suspected violations of the Act so long as such communications include a prescribed statement notifying the recipient that the Board cannot make legal determinations or order the recipient to discontinue providing teeth whitening products or services. Finally, the ALJ ordered the Board to send notices to parties affected by the Order, as well as various ancillary relief, including reporting and record keeping requirements to enable the Commission to verify compliance with the Order. (ID at 114-15, 125-27.)

The Commission is "clothed with wide discretion" to determine the type of order necessary to remedy a violation of FTC Act. *Chicago Bridge & Iron Co. v. FTC*, 534 F.3d 410, 441 (5th Cir. 2008); *see also Jacob Siegel Co. v. FTC*, 327 U.S. 608, 611 (1946); *American Medical Association*, 94 F.T.C. 701 (1979).

The Commission has wide latitude to extend the order as needed

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to prevent future violations and remediate past harms. “Having established a violation, the Commission must ‘be allowed effectively to close all roads to the prohibited goal, so that the order may not be by-passed with impunity.’” *American Medical Association*, 94 F.T.C. at 1010-11 (citing *FTC v. Ruberoid Co.*, 343 U.S. 470, 473 (1952)). However, the Commission’s discretion is not unlimited; its remedy must be reasonably related to the violation. *Ruberoid*, 343 U.S. at 473; *Jacob Siegel*, 327 U.S. at 613.

The Commission has determined to issue a Final Order very similar to the ALJ’s proposed remedy. The Final Order is reasonably tailored to remediating the effects of the Board’s past violations and preventing future violations. Moreover, it provides an effective remedy for Respondent’s illegal conduct without impeding the Board’s ability to fulfill its statutory role in the regulation of dentists and the practice of dentistry in North Carolina.

As discussed above and in the ALJ’s opinion, the Board’s illegal activity centered on enforcing its determination that non-dentists providing any teeth whitening services violated the Dental Practice Act by sending out various communications, including cease and desist letters, that exceeded its statutory authority. Section II of the Final Order prevents the Board from continuing these unlawful practices. It prohibits the Board from directing a non-dentist provider to stop providing teeth whitening products and services (Final Order § II, ¶ A), or impeding or discouraging non-dentist providers from providing teeth whitening products and services (Final Order § II, ¶ B).

Section II of the Final Order also requires the Board to cease and desist from communicating to any non-dentist provider that it is a violation of the Dental Practice Act for a non-dentist to provide teeth whitening goods and services, or that such provider’s provision of teeth whitening products or services violates the Act. (Final Order § II, ¶ C.) The Final Order further prohibits the Board from making similar communications to third parties, including prospective providers of teeth whitening goods and services, current or prospective lessors of commercial property, and manufacturers or distributors of teeth whitening products. (Final Order § II, ¶¶ D-F.) The Final Order thus prohibits the types of communications that the Board used to

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exclude non-dentist providers from the provision of teeth whitening goods and services. Accordingly, these restrictions are reasonable and necessary to prevent future illegal activity by the Board. Further, the Board can effectively carry out its statutory responsibilities without such communications. Indeed, as the facts illustrate here, communications of the type prohibited by the Final Order may confuse recipients as to the actual role and authority of the Board. (IDF 246.)

To ensure the Board cannot indirectly accomplish what it has been barred from doing directly, Section II.G of the Final Order also prohibits the Board from inducing or assisting any other person in discouraging the provision of teeth whitening by non-dentist providers. This type of prohibition is well within the authority of the Commission. *See Ruberoid*, 343 U.S. at 473 (FTC orders need not be restricted to the “narrow lane” of the respondent’s violation, but rather may “close all roads to the prohibited goal, so that its order may not be by-passed with impunity”); *Toys “R” Us*, 221 F.3d at 940 (“[T]he FTC is not limited to restating the law in its remedial orders. Such orders can restrict the options for a company that has violated § 5, to ensure that the violation will cease and competition will be restored.”). This prohibition is substantively identical to the analogous provision in the ALJ’s Order but incorporates a clarifying edit.

The final portion of Section II of the Final Order ensures that the Board will be able to carry out its legitimate statutory duties by excluding certain acts from the scope of the prohibitions contained in the Section. Specifically, it states that nothing in the Final Order prohibits the investigation and prosecution of non-dentists for alleged violations of the Dental Practice Act. Further, it ensures that the Final Order will not be read to prevent the Board from communicating its opinion regarding whether a particular method of teeth whitening violates the Dental Practice Act or from providing notice of its bona fide intention to bring a legal proceeding against a person for violating the Dental Practice Act.

We add an additional provision to this portion of the Final Order to make it clear that the Board may also communicate

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factual information regarding changes to North Carolina statutes or future legal proceedings in North Carolina regarding teeth whitening services provided by non-dentist providers. (Final Order § II, second subsection (ii).) To ensure that these communications are not misleading as to the statutory authority and role of the Board, or otherwise violate the prohibitions contained in Section II, the Final Order requires the Board to include in the communications the disclosure set forth in Appendix A of the Final Order. We also clarify in the first subsection (iii) of Section II of the Final Order that nothing in the Final Order prohibits the use of administrative proceedings against dentists for alleged violations of the Dental Practice Act. This change is necessary because administrative remedies are only available against dentists. (IDF 46, 48.)

Section III of the Final Order requires the Board to send notices and other disclosures to parties affected by the Final Order. Such notices are within the Commission's remedial authority. *See Realcomp*, 2009 FTC LEXIS 250, at *129 (requiring respondent to provide a copy of the Commission's order to affected persons). In particular, Section III requires the Board to send copies of the Complaint and Final Order to all present and future members, employees, and agents of the Board. This will facilitate compliance with the Final Order. Section III also requires the Board to send certain disclosures to each person to whom the Board previously sent a cease and desist letter or similar communication regarding the legality of non-dentist teeth whitening. Such disclosures will help rectify the Board's prior illegal conduct by correcting the impressions created by the Board's communications. *Cf. Novartis Corp. v. FTC*, 223 F.3d 783, 786 (D.C. Cir. 2000) (upholding order requiring corrective advertising); *Southwest Sunsites, Inc. v. FTC*, 785 F.2d 1431, 1439 (9th Cir. 1986) (same).

Finally, the Final Order imposes limited requirements on the Board to facilitate the Commission's ability to monitor the Board's compliance with the terms of the Final Order. The Board is required to provide an initial compliance report, followed by annual reports thereafter, containing specified information and to provide Commission representatives with reasonable access to information and personnel as needed to verify compliance with

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the Final Order. (Final Order §§ IV-VI.) Such ancillary provisions are common in Commission orders. *See, e.g., Realcomp*, 2009 FTC LEXIS 250, at *130 (requiring compliance reports); *Advocate Health Partners*, No. C-4184, 2007 FTC LEXIS 17, at *26-28 (2007) (requiring compliance reports and reasonable inspection).

Respondent does not appeal any specific provision of the ALJ's Order but argues that the ALJ's Order, taken as a whole, would restrict the Board's ability to conduct bona fide investigations into possible violations of the North Carolina Dental Practice Act, would prevent the Board from enforcing the Act, and would violate the Commerce Clause of and Tenth Amendment to the U.S. Constitution. We find these arguments to be without merit.

Respondent argues first that the "Order clearly restricts the State Board's ability to conduct a bona fide investigation into possible violations of the North Carolina Dental Practice Act, as it renders useless the State Board's ability to prevent unlicensed teeth whitening services." (RAB at 40.) To the contrary, as discussed above, the Final Order is much more limited and specifically states that "nothing in this Order prohibits the Board from . . . investigating a Non-Dentist Provider for suspected violations of the Dental Practice Act." (Final Order § II.) The Final Order explicitly permits the Board to bring (or cause to be brought) judicial proceedings against non-dentist providers, to bring administrative proceedings against dentists, and to send bona fide litigation warning letters to targets of investigations. (*Id.*) Since the Board's authority to enforce the Dental Practice Act against non-dentists is limited to seeking recourse from the North Carolina courts or referring a matter to a District Attorney (N.C. General Statutes § 90-40.1; IDF 43, 44, 190; Response to Complaint ¶ 19; RAB at 2-3; RRB at 5), the Final Order will not prevent or impede the Board from carrying out its enforcement duties. Indeed, the Board's Chief Operating Officer testified that the Board's ability to enforce the Act would not be affected if it sent litigation warning letters instead of cease and desist letters. (IDF 258; *see also* IDF 259-60 (no cease and desist language in Board letters from 2000 to 2002).)

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Respondent also argues that the ALJ's Order would violate the Tenth Amendment to the U.S. Constitution by directing the actions of state officials. Respondent relies on *New York v. United States*, 505 U.S. 144 (1992) and *Printz v. United States*, 521 U.S. 898 (1997). In these cases, the Supreme Court held that Congress may not enact a law that would direct the functioning of the states' executives or legislatures but may enact laws of general applicability that incidentally apply to state governments. See *Printz*, 521 U.S. at 932 ("the incidental application to the States of a federal law of general applicability" is lawful); *New York*, 505 U.S. at 160 (Congress may "subject state governments to generally applicable laws"); see also *Kennedy v. Allera*, 612 F.3d 261, 269 (4th Cir. 2010) ("[T]he Tenth Amendment prohibits the federal government from commandeering state officers by compelling them to enforce a federal regulatory program."). It is undisputed that the FTC Act is a statute of general applicability and is not directed at states or state officials. Accordingly, the Court's line of cases prohibiting the commandeering of state officials is inapplicable.

Alternatively, Respondent asserts that under *California State Board of Optometry v. FTC*, 910 F.2d 976 (D.C. Cir. 1990), the Tenth Amendment prevents the FTC from imposing restrictions on a state's regulatory scheme.²⁰ Respondent overreaches by trying to stretch that case to include activity that is outside the scope of the regulatory scheme of the Dental Practice Act. In *California State Board of Optometry*, the D.C. Circuit reviewed an FTC trade regulation rule, passed pursuant to the Magnuson-Moss Amendments to the FTC Act, declaring that certain state laws restricting the practice of optometry constituted unfair acts or practices. The court held that state regulation of the practice of optometry is a quintessentially sovereign act and therefore rejected the rule as an improper attempt to regulate state

²⁰ Respondent also asserts that *California State Board of Optometry* held that a state cannot be a "person" for purposes of jurisdiction when it acts in its sovereign capacity. (RAB at 24.) That decision, even under Respondent's reading, is inapposite because the Board is not a sovereign, and the challenged practices exceeded what the North Carolina legislature authorized. In addition, the Commission's jurisdiction to hear this matter was resolved in the Commission's February 3, 2011 decision, and Respondent did not dispute that it is a "person" before the ALJ. (ID at 59.)

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action. In contrast, this case does not involve a challenge to a state law or regulation, but rather a challenge to conduct by the Board that went beyond its statutory mandate. Furthermore, the Commission has already concluded that the Board's conduct in question does not satisfy the requirements of the state action defense. *See North Carolina Dental*, 151 F.T.C. at 615-33.

Finally, Respondent argues, without citation to any case law, that the ALJ's Order would violate the Commerce Clause of the U.S. Constitution because it regulates the practice of dentistry in North Carolina. To the contrary, however, the Final Order neither regulates the practice of dentistry nor violates the Commerce Clause of the Constitution. The Constitution grants Congress the power to "regulate Commerce . . . among the several states." U.S. Constitution, art. I, § 8, cl. 3. Pursuant to this authority, Congress passed the FTC Act and gave the agency the authority to prevent, *inter alia*, "[u]nfair methods of competition in or affecting commerce." 15 U.S.C. § 45(a). The jurisdictional reach of the Commission extends as far as the Commerce Clause. (ID at 59-62.) The ALJ found, and Respondent does not dispute in this appeal, that the Board's acts have a substantial effect on interstate commerce and are therefore in or affecting commerce. (ID at 62.) Furthermore, as described above, the Final Order does not regulate the practice of dentistry in North Carolina. The Commission has declined to address whether teeth whitening constitutes stain removal under the Dental Practice Act, and the Final Order does not interfere with the ability of the Board to fulfill its statutory obligations. Rather, the Final Order is limited to ensuring that the Board does not violate the antitrust laws through anticompetitive acts and practices that are not authorized or required by the Dental Practice Act.

VIII. CONCLUSION

Based on a *de novo* review of the facts and law in this matter, the Commission concludes that the Board has violated Section 5 of the FTC Act, 15 U.S.C. § 45. The Commission has therefore issued a Final Order to remedy the Board's violations and to prevent their recurrence.

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FINAL ORDER

The Commission has heard this matter upon the appeal of Respondent from the Initial Decision, and upon briefs and oral argument in support thereof and in opposition thereto. For the reasons stated in the accompanying Opinion of the Commission, the Commission has determined to sustain the Initial Decision with certain modifications:

IT IS ORDERED that the Initial Decision of the administrative law judge be, and it hereby is, adopted as the Findings of Fact and Conclusions of Law of the Commission, to the extent not inconsistent with the findings of fact and conclusions contained in the accompanying Opinion.

Other findings of fact and conclusions of law of the Commission are contained in the accompanying Opinion.

IT IS FURTHER ORDERED that the following Order to cease and desist be, and it hereby is, entered:

ORDER**I.**

IT IS ORDERED that, as used in this Order, the following definitions shall apply:

- A. "Board" means the North Carolina State Board of Dental Examiners ("NCSBDE"), its officers, directors, members, employees, agents, attorneys, representatives, successors, and assigns; and the subsidiaries, divisions, groups, and affiliates controlled by it; and the respective officers, directors, members, employees, agents, attorneys, representatives, successors, and assigns of each.
- B. "Communicate" or "Communicating" means exchanging, transferring, or disseminating any information, without regard to the manner or means by which it is accomplished.

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- C. “Communication” means any information exchange, transfer, or dissemination, without regard to the means by which it is accomplished, including, without limitation, oral or written, in any manner, form, or transmission medium.
- D. “Dental Practice Act” means any legislation that is administered by the Board, including, North Carolina General Statutes, Chapter 90, Article 2 (Dentistry) (N.C. Gen. Stat. §§ 90-22 - 90-48.3 (2010)) and Article 16 (Dental Hygiene Act) (N.C. Gen. Stat. §§ 90-221 - 90-233.1 (2010)).
- E. “Dentist” means any individual holding a license, issued by the Board, to practice dentistry in North Carolina.
- F. “Direct” or “Directing” means to order, direct, command or instruct.
- G. “Non-Dentist Provider” means any Person other than a Dentist engaged in the provision, distribution or sale of any Teeth Whitening Goods or Teeth Whitening Services.
- H. “Person” means both natural persons and artificial persons, including, but not limited to, corporations, and unincorporated entities.
- I. “Principal Address” means either (i) primary business address, if there is a business address, or (ii) primary residential address, if there is no business address.
- J. “Teeth Whitening Goods” means any formulation containing a peroxide bleaching agent, whether or not used in conjunction with an LED light source, and any other ancillary products used in the provision of Teeth Whitening Services.
- K. “Teeth Whitening Services” means whitening teeth through the use of a formulation containing a peroxide bleaching agent, whether or not used in conjunction with an LED light source.
- L. “Third Party” means any Person other than NCSBDE.

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II.

IT IS FURTHER ORDERED that Respondent, directly or indirectly, or through any corporate or other device, in connection with the provision of Teeth Whitening Services in or affecting commerce, as “commerce” is defined in Section 4 of the Federal Trade Commission Act, 15 U.S.C. § 44, cease and desist from:

- A. Directing a Non-Dentist Provider to cease providing Teeth Whitening Goods or Teeth Whitening Services;
- B. Prohibiting, restricting, impeding, or discouraging the provision of Teeth Whitening Goods or Teeth Whitening Services by a Non-Dentist Provider;
- C. Communicating to a Non-Dentist Provider that: (i) such Non-Dentist Provider is violating, or has violated the Dental Practice Act by providing Teeth Whitening Goods or Teeth Whitening Services; or (ii) the provision of Teeth Whitening Goods or Teeth Whitening Services by a Non-Dentist Provider is a violation of the Dental Practice Act;
- D. Communicating to a prospective Non-Dentist Provider that: (i) a Non-Dentist Provider would violate the Dental Practice Act by providing Teeth Whitening Goods or Teeth Whitening Services; or (ii) the provision of Teeth Whitening Goods or Teeth Whitening Services by a Non-Dentist Provider would violate the Dental Practice Act;
- E. Communicating to a lessor of commercial property or any other Third Party that (i) the provision of Teeth Whitening Goods or Teeth Whitening Services by a Non-Dentist Provider is a violation of the Dental Practice Act, or (ii) that any Non-Dentist Provider is violating or has violated the Dental Practice Act by providing Teeth Whitening Goods or Teeth Whitening Services;
- F. Communicating to an actual or prospective

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manufacturer, distributor, or seller of Teeth Whitening Goods used by Non-Dentist Providers, or to any other Third Party that (i) the provision of Teeth Whitening Goods or Teeth Whitening Services by a Non-Dentist Provider is a violation of the Dental Practice Act, or (ii) that any Non-Dentist Provider is violating or has violated the Dental Practice Act by providing Teeth Whitening Goods or Teeth Whitening Services; and

- G. Inducing, urging, encouraging, assisting or attempting to induce, any Person to engage in any action that would violate Paragraphs II.A through II.F if such action were taken by Respondent;

Provided, however, that nothing in this Order prohibits the Board from:

- (i) investigating a Non-Dentist Provider for suspected violations of the Dental Practice Act;
- (ii) filing, or causing to be filed, a court action against a Non-Dentist Provider for an alleged violation of the Dental Practice Act pursuant to N.C. Gen. Stat. §§ 90-40, 90-40.1, or 90-233.1; or
- (iii) pursuing any administrative remedies against a Dentist pursuant to and in accordance with the North Carolina Annotated Code;

Provided further, that nothing in this Order prohibits the Board from Communicating to a Third Party:

- (i) notice of its belief or opinion regarding whether a particular method of providing Teeth Whitening Goods or Teeth Whitening Services may violate the Dental Practice Act;
- (ii) factual information regarding legislation and court proceedings concerning Teeth Whitening Goods or Teeth Whitening Services provided by Non-Dentist Providers;

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(iii)notice of its bona fide intention to file a court action against that Person for a suspected violation of the Dental Practice Act with regard to Teeth Whitening Goods or Teeth Whitening Services; or

(iii)notice of its bona fide intention to pursue administrative remedies with regard to Teeth Whitening Goods or Teeth Whitening Services,

so long as such Communication includes, with equal prominence, the paragraph included in Appendix A to this Order.

III.

IT IS FURTHER ORDERED that Respondent shall:

- A. Within thirty (30) days from the date this Order becomes final, send a copy of this Order and the Complaint by first-class mail with delivery confirmation or electronic mail with return confirmation to:
1. each Board member; and
 2. each officer, director, manager, representative, agent, attorney, and employee of the Board;
- B. Distribute by first-class mail, return receipt requested, a copy of this Order and the Complaint to each individual who becomes a Board member, or an officer, director, manager, attorney, representative, agent or employee of Board, and who did not previously receive a copy of this Order and the Complaint from Respondent, within ten (10) days of the time that he or she assumes such position;
- C. Within thirty (30) days from the date this Order becomes final, send a copy of the letter, on the Board's official letterhead, with the text included in Appendix

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B to this Order, by first-class mail with delivery confirmation or electronic mail with return confirmation to:

1. each Person, including without limitation actual or prospective Non-Dentist Providers, manufacturers of goods and services used by Non-Dentists Providers, or any other Third Party, to whom the Board Communicated a cease-and-desist order, letter, or other similar Communication;
 2. each Person, including without limitation actual or prospective lessors of commercial property or any other Third Party, to whom the Board Communicated (i) that the provision of Teeth Whitening Goods or Teeth Whitening Services by a Non-Dentist Provider is a violation of the Dental Practice Act, or (ii) that any Non-Dentist Provider is violating, has violated, or may be violating the Dental Practice Act by providing Teeth Whitening Goods or Teeth Whitening Services; and
 3. any other Third Party to whom, or with whom, the Board Communicated substantially the same information set forth in C.1 and C.2 of this Paragraph III;
- D. Within sixty (60) days from the date this Order becomes final, Respondent shall arrange with the North Carolina Board of Cosmetic Art Examiners for the notice included as Appendix C to this Order to appear on the website of that Board for a period of six (6) months;

Provided, however, should Respondent be unable within sixty (60) days to arrange with the North Carolina Board of Cosmetic Art Examiners for such notice to appear on that Board's website, Respondent shall within ninety (90) days from the date this Order becomes final: (1) obtain from the North Carolina Board of Cosmetic Art Examiners its most current list

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of licensees; and (2) send the Appendix C notification by first-class mail with delivery confirmation or electronic mail with return confirmation to each licensee on that current list;

IV.

IT IS FURTHER ORDERED that Respondent shall file verified written reports within sixty (60) days from the date this Order becomes final, annually thereafter for three (3) years on the anniversary of the date this Order becomes final, and at such other times as the Commission may by written notice require. Each report shall include, among other information that may be necessary:

- A. The identity, including address and telephone number, of each Non-Dentist Provider, and any other Third Party, that the Board Communicated with during the relevant reporting period regarding Teeth Whitening Goods or Teeth Whitening Services;
- B. Copies of all Communications with any Non-Dentist Provider, and any other Third Party regarding the provision of Teeth Whitening Goods or Teeth Whitening Services;
- C. Copies of the delivery confirmations or electronic mail with return confirmations required by Paragraph III. A and B; and
- D. A detailed description of the manner and form in which Respondent has complied, and is complying, with this Order.

V.

IT IS FURTHER ORDERED that Respondent shall notify the Commission of any change in its principal address within twenty (20) days of such change in address.

VI.

IT IS FURTHER ORDERED that, for the purpose of determining or securing compliance with this Order, and subject

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to any legally recognized privilege, and upon written request and upon five (5) days' notice to NCSBDE, that NCSBDE shall, without restraint or interference, permit any duly authorized representative of the Commission:

- A. Access, during office hours of NCSBDE and in the presence of counsel, to all facilities and access to inspect and copy all books, ledgers, accounts, correspondence, memoranda, and all other records and documents in the possession, or under the control, of NCSBDE relating to compliance with this Order, which copying services shall be provided by NCSBDE at its expense; and
- B. To interview officers, directors, or employees of NCSBDE, who may have counsel present, regarding such matters.

VII.

IT IS FURTHER ORDERED that this Order shall terminate on December 2, 2031.

Opinion of the Commission

APPENDIX A

The Federal Trade Commission issued a Final Order on December 2, 2011, which requires the Dental Board to provide you with the following Notice. The Dental Board hereby notifies you that the opinion of the Dental Board expressed in this communication is not a legal determination. The Dental Board does not have the authority to order you to discontinue providing Teeth Whitening Goods or Teeth Whitening Services. Only a court may determine that you have violated, or are violating, any law, and, if appropriate, impose a remedy or penalty for such violation.

Further, pursuant to 21 N.C.A.C. 16N .0400 and N.C. Gen. Stat. § 150B-4, you may have the right, prior to the initiation of any court action by the Dental Board, to request a declaratory ruling regarding whether your method of providing teeth whitening goods or services is lawful.

You are further notified that any right to a declaratory ruling from the Dental Board supplements any other legal rights that you may already have to establish the legality of your teeth whitening goods or services. Complete copies of the Federal Trade Commission's Complaint and Final Order are available on the Commission's website at <http://www.ftc.gov>.

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APPENDIX B

(Letterhead of NCSBDE)

(Name and Address of the Recipient)

Dear (Recipient):

As you may know, the Federal Trade Commission issued an Administrative Complaint in 2010 against the Dental Board challenging the legality of the Dental Board's attempts to restrict the provision of teeth whitening services by non-dentists in North Carolina. At the conclusion of that administrative proceeding, the Commission issued a Final Order requiring the Dental Board, among other things, to cease and desist from certain activities involving teeth whitening by non-dentists and to take certain remedial actions, of which this letter is one part. Complete copies of the Federal Trade Commission's Complaint and Final Order are available on the Commission's website at <http://www.ftc.gov>.

You are receiving this letter because you previously received from the Dental Board either: (1) a letter directing or ordering you to cease and desist the unlicensed provision of dental teeth whitening services, or selling dental teeth whitening goods or services to non-dentist teeth whiteners, in violation of the Dental Practice Act, N.C. Gen. Stat. §§ 90-29(b)(2), 90-40, and/or 90-40.1; or (2) a letter advising you (i) that a non-dentist would or might violate the Dental Practice Act by providing teeth whitening goods or services; or (ii) that the provision of teeth whitening goods or services by a non-dentist would or might violate the Dental Practice Act, N.C. Gen. Stat. §§ 90-29(b)(2), 90-40, and/or 90-40.1.

The Dental Board hereby notifies you that the prior letter you received from the Dental Board only expressed the opinion of the Dental Board, and that such opinion is not a legal determination. The Dental Board does not have the authority to order you to discontinue providing Teeth Whitening Goods or Teeth Whitening Services. Only a court may determine that you are violating, or have violated, any law and, if appropriate, impose a

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remedy or penalty for such violation. Further, you may have the right to request a declaratory ruling from the Dental Board, pursuant to 21 N.C.A.C. 16N .0400 and N.C. Gen. Stat. § 150B-4, regarding whether a particular method of providing teeth whitening goods or services is lawful. You are further notified that any right to a declaratory ruling from the Dental Board supplements any other legal rights that you may already have to establish the legality of any particular method of providing teeth whitening goods or services.

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APPENDIX C**Teeth Whitening Notice**

As you may know, the Federal Trade Commission issued an Administrative Complaint in 2010 against the Dental Board challenging the legality of the Dental Board's attempts to restrict the provision of teeth whitening services by non-dentists in North Carolina. At the conclusion of that administrative proceeding, the Commission issued a Final Order requiring the Dental Board, among other things, to cease and desist from certain activities involving teeth whitening by non-dentists and to take certain remedial actions, of which this Notice is one part. Complete copies of the Federal Trade Commission's Complaint and Final Order are available on the Commission's website at <http://www.ftc.gov>.

In 2007, the Cosmetology Board, at the request of the Dental Board, displayed a "Teeth Whitening Bulletin" on the Cosmetology Board's website advising cosmetologists and estheticians "that any process that 'removes stains, accretions or deposits from human teeth' constitutes the practice of dentistry . . . Taking impressions for bleaching trays also constitutes the practice of dentistry" That Bulletin further advised that it was a misdemeanor for anyone other than a licensed dentist to provide those services.

The Dental Board hereby notifies you that the prior Bulletin, described above, only expressed the opinion of the Dental Board, and that such opinion is not a legal determination. The Dental Board does not have the authority to order you to discontinue providing Teeth Whitening Goods or Teeth Whitening Services. Only a court may determine that you have violated, or are violating, any law and, if appropriate, to impose a remedy or penalty for such violation. Further, you may have the right to request a declaratory ruling from the Dental Board, pursuant to 21 N.C.A.C. 16N .0400 and N.C. Gen. Stat. § 150B-4, regarding whether a particular method of providing teeth whitening goods or services is lawful. You are further notified that any right to a declaratory ruling from the Dental Board supplements any other

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legal rights that you may already have to establish the legality of any particular method of providing teeth whitening goods or services.

By the Commission, Commissioner Brill recused.

Initial Decision

IN THE MATTER OF
PROMEDICA HEALTH SYSTEM, INC.

INITIAL DECISION AND ORDER

Docket No. D-9346; File No. 101 0167
Filed, January 6, 2011 — Decision, December 5, 2011

In January 2011, the Commission issued an administrative complaint challenging the consummated acquisition by ProMedica Health System, Inc. (“ProMedica”) of St. Luke’s Hospital in Lucas County, Ohio. The complaint alleged the acquisition reduced competition for general acute-care and inpatient obstetrical services and allowed ProMedica to raise prices for these services, significantly harming patients, local employers, and employees. Following an administrative hearing, Chief Administrative Law Judge D. Michael Chappell (“ALJ”) issued an Initial Decision holding that ProMedica’s acquisition of St. Luke’s Hospital eliminated competition between the two firms in the market for general acute care inpatient hospital services and reduced the number of competing hospitals in the Lucas County market from four to three. The ALJ held that the acquisition increased ProMedica’s bargaining power with commercial health plans, thereby leading to higher reimbursement rates. The ALJ further concluded that those higher rates likely would be passed on to the commercial health plans’ customers, including employers and employees, to the detriment of consumers. The ALJ ordered ProMedica to divest St. Luke’s Hospital to an Commission-approved buyer within 180 days. The order further required ProMedica to take steps to maintain the viability of St. Luke’s Hospital until it is divested and to provide transitional services to the approved acquirer.

Participants

For the *Commission*: *Richard Cunningham, Janelle Filson, Alexis Gilman, Kevin Hahm, Krisztian Katona, Jeanne Liu, Jeffrey Perry, Sara Razi, Matthew Reilly, Stephanie Reynolds, Kaj Rozga, Sarah Swain, Matthew Tabas, Nicholas Widnell, Stelios Xenakis, and Michelle Yost.*

For the *Respondent*: *Carrie G. Amezcua, Erin C. Arnold, James B. Camden, Amy Carletti, Christine G. Devlin, Amy Hancock, David Marx, Jr., Daniel Powers, Vincent C. van Panhuys, Jennifer L. Westbrook, and Stephen Y. Wu, McDermott Will & Emery LLP.*

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INITIAL DECISION

By CHAPPELL, D. MICHAEL, Chief Administrative Law Judge:

I. INTRODUCTION**A. Overview**

This is the Initial Decision on an administrative complaint, discussed in further detail below, charging that a hospital joinder (the “Joinder”) between ProMedica Health System, Inc. (“Respondent” or “ProMedica”) and St. Luke’s Hospital (“St. Luke’s”), pursuant to which St. Luke’s, a previously independent hospital, became part of ProMedica, may substantially lessen competition, in violation of Section 7 of the Clayton Act, as amended, 15 U.S.C. § 18.

As explained herein, the preponderance of the evidence presented demonstrates a reasonable probability that the Joinder of St. Luke’s with ProMedica is likely to substantially lessen competition in the market for the sale of general acute-care inpatient hospital services to commercial health plans in Lucas County, Ohio. Having determined that the Joinder violates Section 7 of the Clayton Act, an Order will issue herewith requiring, *inter alia*, that ProMedica divest itself of St. Luke’s.

B. Summary of the Complaint and Answer

The Commission issued an administrative complaint against Respondent ProMedica on January 6, 2011 (“Complaint”). The Complaint alleges that ProMedica effectively acquired and took control of its nearby competitor, St. Luke’s, upon consummation of a Joinder Agreement on August 31, 2010, and that ProMedica’s acquisition of St. Luke’s threatens to substantially lessen competition for health-care services in Lucas County, Ohio. Complaint ¶¶ 1, 2. The relevant service markets alleged in the Complaint are: (1) general acute-care (“GAC”) inpatient hospital services sold to commercial health plans; and (2) inpatient obstetrical (“OB”) services; and the alleged relevant geographic market is Lucas County, Ohio. Complaint ¶¶ 12-19.

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According to the Complaint, the Joinder is presumptively unlawful because it reduces the number of competitors from four to three in the GAC inpatient services market and from three to two in the OB services market, and results in high post-acquisition market shares and concentration. Complaint ¶¶ 20-22.

The Complaint also charges that having St. Luke's as part of the ProMedica system "vests ProMedica with an increased ability and incentive to demand supracompetitive reimbursement rates from commercial health plans and their membership." Complaint ¶ 23. The Complaint alleges that, with St. Luke's as part of its system, ProMedica becomes a "must have" system for commercial health plan networks in Lucas County, thereby providing ProMedica with significantly greater negotiating "clout" in its negotiations with commercial health plans. Complaint ¶¶ 25-27. The Complaint also alleges that increased reimbursement rates obtained by ProMedica from commercial health plans will be passed on to the plans' employer and employee customers. Complaint ¶¶ 29-30. Further, the Complaint alleges that the Joinder will reduce both the quality and the breadth of available services in Lucas County. Complaint ¶ 31.

Next, the Complaint alleges that neither hospital entry nor expansion by the remaining hospitals in Lucas County will deter or counteract the alleged likely harm to competition and that no merger-specific efficiencies justify the Joinder. Complaint ¶¶ 34-38.

Based on the foregoing, the Complaint charges one violation: the Acquisition may substantially lessen competition in the relevant markets in violation of Section 7 of the Clayton Act, as amended, 15 U.S.C. § 18. Complaint ¶ 40.

Respondent filed its Answer to the Complaint on January 25, 2011. The Answer admits that GAC inpatient hospital services sold to commercial health plans constitutes a valid service market, but denies that inpatient OB services is an appropriate relevant market. The Answer also admits that Lucas County, Ohio is the relevant geographic market in which to analyze the effects of the Joinder. Answer ¶¶ 12-19. Respondent further denies all other

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material allegations of the Complaint, including that the Joinder is presumptively unlawful; will enable, or result in, ProMedica's charging supracompetitive reimbursement rates; or reduce the quality and breadth of services available in Lucas County, Ohio. Answer ¶¶ 20-33. Respondent further denies that neither entry nor expansion will deter or counteract the Joinder's alleged likely harm to competition, and that no merger-specific efficiencies justify the Joinder. Answer ¶¶ 34-38.

C. Procedural History

In July 2010, the Federal Trade Commission ("FTC") and the state of Ohio Attorney General's staff began an investigation into the potential anticompetitive effects of ProMedica's acquisition of St. Luke's. On August 18, 2010, before the Joinder was consummated, the FTC and ProMedica entered into a limited, 60-day Hold Separate Agreement. Among other things, the Hold Separate Agreement prevented: (1) ProMedica's termination of St. Luke's health-plan contracts (while allowing health plans the option to extend their contracts with St. Luke's past the termination date, if a new agreement was not reached); (2) the elimination, transfer, or consolidation of any clinical service at St. Luke's; and (3) the termination of employees at St. Luke's without cause. (PX00069 at ¶¶ 1-5).

On January 7, 2011, the FTC and state of Ohio brought suit in the Northern District of Ohio, seeking a temporary restraining order and preliminary injunction. *FTC and State of Ohio v. ProMedica Health Sys.*, No.3:11-cv-00047-DAK (N.D. Ohio filed January 7, 2011). After hearing summaries of testimony and detailed briefing, on March 29, 2011, Judge Katz of the Northern District of Ohio entered a preliminary injunction holding the parties to the terms of their August 18, 2010 Hold Separate Agreement, pending the outcome of the present administrative proceedings. *FTC v. ProMedica Health Sys., Inc.*, 2011 U.S. Dist. LEXIS 33434 (N.D. Ohio March 29, 2011). The decision reached by the district court on the preliminary injunction hearing does not have preclusive effect on these proceedings. *In re R.R. Donnelley & Sons Co.*, No. 9243, 1995 FTC LEXIS 215, at *25 (July 21, 1995).

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The administrative hearing in the instant case began on May 31, 2011 and concluded on August 18, 2011. By Order dated August 23, 2011, the hearing record was closed. Over 2,600 exhibits were admitted, 34 witnesses testified, either live or by deposition, and there are 7,955 pages of trial transcript. The parties' proposed findings of fact, replies to proposed findings of fact, post-trial briefs, and reply briefs total 2,350 pages.

Rule 3.51(a) of the Commission's Rules of Practice states that "[t]he Administrative Law Judge shall file an initial decision within 70 days after the filing of the last filed initial or reply proposed findings of fact, conclusions of law and order . . ." 16 C.F.R. § 3.51(a). The parties filed concurrent post-trial briefs and proposed findings of fact on September 13, 2011. The parties filed replies to the other's proposed findings and briefs on September 23, 2011. Pursuant to Commission Rule 3.41(b)(6), closing arguments were held on September 29, 2011. This Initial Decision is filed in compliance with Commission Rule 3.51(a).

D. Evidence

This Initial Decision is based on a consideration of the whole record relevant to the issues, including the exhibits properly admitted into evidence, deposition transcripts, and the transcripts of testimony at trial, and addresses the material issues of fact and law. The briefs and proposed findings of fact and conclusions of law, and the replies thereto, submitted by the parties were thoroughly reviewed. Proposed findings of fact submitted by the parties, but not included in this Initial Decision were rejected, either because they were not supported by the evidence or because they were not dispositive or material to the determination of the allegations of the Complaint or the defenses thereto. The Commission has held that Administrative Law Judges are not required to discuss the testimony of each witness or all exhibits that are presented during the administrative adjudication. *In re Amrep Corp.*, No. 9018, 102 F.T.C. 1362, 1670, 1983 FTC LEXIS 17, *566-67 (Nov. 2, 1983). Further, administrative adjudicators are "not required to make subordinate findings on every collateral contention advanced, but only upon those issues of fact, law, or discretion which are 'material.'" *Minneapolis & St. Louis Ry. Co. v. United States*, 361 U.S. 173, 193-94 (1959).

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Accord Stauffer Labs., Inc. v. FTC, 343 F.2d 75, 89 (9th Cir. 1965). See also *Borek Motor Sales, Inc. v. National Labor Relations Bd.*, 425 F.2d 677, 681 (7th Cir. 1970) (holding that it is adequate for the Board to indicate that it had considered each of the company's exceptions, even if only some of the exceptions were discussed, and stating that "[m]ore than that is not demanded by the [Administrative Procedure Act] and would place a severe burden upon the agency").

Under Commission Rule 3.51(c)(1), "[a]n initial decision shall be based on a consideration of the whole record relevant to the issues decided, and shall be supported by reliable and probative evidence." 16 C.F.R. § 3.51(c)(1); see *In re Chicago Bridge & Iron Co.*, No. 9300, 138 F.T.C. 1024, 1027 n.4, 2005 FTC LEXIS 215, at *3 n.4 (Jan. 6, 2005). Under the Administrative Procedure Act ("APA"), an Administrative Law Judge may not issue an order "except on consideration of the whole record or those parts thereof cited by a party and supported by and in accordance with the reliable, probative, and substantial evidence."

5 U.S.C. § 556(d). All findings of fact in this Initial Decision are supported by reliable, probative, and substantial evidence. Citations to specific numbered findings of fact in this Initial Decision are designated by "F."¹

Pursuant to Commission Rule 3.45(b), several orders were

¹ References to the record are abbreviated as follows:

CX – Complaint Counsel's Exhibit

RX – Respondent's Exhibit

JX – Joint Exhibit

Tr. – Transcript of testimony before the Administrative Law Judge

Dep. – Transcript of Deposition

IHT – Investigational Hearing Transcript

CCB – Complaint Counsel's Post-Trial Brief

CCRB – Complaint Counsel's Post-Trial Reply Brief

CCFF – Complaint Counsel's Proposed Findings of Fact

CCRRFF – Complaint Counsel's Reply to Respondent's Proposed Findings of Fact

RB – Respondent's Post-Trial Brief

RRB – Respondent's Reply Brief

RFF – Respondent's Proposed Findings of Fact

RRCCFF – Respondent's Reply to Complaint Counsel's Proposed Findings of Fact

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issued in this case granting *in camera* treatment to material, after finding, in accordance with the Rule, that its public disclosure would likely result in a clearly defined, serious injury to the entity requesting *in camera* treatment. 16 C.F.R. § 3.45(b). In addition, when the parties sought to elicit testimony at trial that revealed information that had been granted *in camera* treatment, the hearing went into an *in camera* session.

Commission Rule 3.45(a) allows the Administrative Law Judge “to grant *in camera* treatment for information at the time it is offered into evidence subject to a later determination by the [administrative] law judge or the Commission that public disclosure is required in the interests of facilitating public understanding of their subsequent decisions.” *In re Bristol-Myers Co.*, Nos. 8917-19, 90 F.T.C. 455, 457, 1977 FTC LEXIS 25, at *6 (Nov. 11, 1977). As the Commission later reaffirmed in another leading case on *in camera* treatment, since “in some instances the ALJ or Commission cannot know that a certain piece of information may be critical to the public understanding of agency action until the Initial Decision or the Opinion of the Commission is issued, the Commission and the ALJs retain the power to reassess prior *in camera* rulings at the time of publication of decisions.” *In re General Foods Corp.*, No. 9085, 95 F.T.C. 352, 356 n.7; 1980 FTC LEXIS 99, at *12 n.7 (March 10, 1980). Thus, in instances where a document or trial testimony had been given *in camera* treatment, but the portion of the material cited to in this Initial Decision does not in fact require *in camera* treatment, such material is disclosed in the public version of this Initial Decision, pursuant to Commission Rule 3.45(a) (the ALJ “may disclose such *in camera* material to the extent necessary for the proper disposition of the proceeding”). Where *in camera* information is used in this Initial Decision, it is indicated in bold font and braces (“{ }”) in the *in camera* version and is redacted from the public version of the Initial Decision, in accordance with Commission Rule 3.45(e).

E. Summary of Initial Decision

The preponderance of the evidence in the record, viewed as a whole, demonstrates a reasonable probability that the Joinder of St. Luke’s and ProMedica will substantially lessen competition in

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the relevant market for the sale of general acute-care (“GAC”) inpatient hospital services to commercial health plans, referred to herein as managed care organizations (“MCOs”), in Lucas County, Ohio. Complaint Counsel failed to prove a separate relevant product market for the sale of inpatient OB services to MCOs.

The statistical evidence presented demonstrates that the Joinder will significantly increase ProMedica’s market share and market concentration in the already highly-concentrated GAC inpatient hospital services market, reducing the number of competing hospital providers with which MCOs can contract from four to three. The preponderance of the evidence also demonstrates that, by eliminating MCOs’ option of contracting with St. Luke’s alone, the Joinder will significantly increase Respondent’s bargaining leverage in negotiations with MCOs and provide Respondent with sufficient market power to enable it to increase the reimbursement rates it charges MCOs for GAC inpatient hospital services. The evidence further shows that increased reimbursement rates charged to MCOs for the provision of GAC inpatient hospital services would likely be passed on to MCOs’ customers, including employers and employees, to the detriment of consumers. Thus, there is a reasonable probability that the Joinder is likely to result in anticompetitive effects in the relevant market.

Respondent’s claims, that competitor repositioning and/or steering methodologies are likely to constrain Respondent from imposing supracompetitive prices, are not sufficiently supported by the evidence, and are, therefore, rejected. The procompetitive benefits and efficiencies that Respondent asserts will result from the Joinder, while having some support in the record, are insufficient to outweigh the likely anticompetitive effects of the Joinder. Thus, Respondent’s defenses based upon procompetitive benefits and efficiencies are rejected. In addition, while the evidence is clear that St. Luke’s was in a considerably weakened financial condition in the years prior to the Joinder, applicable case law does not support allowing the Joinder with Respondent on this basis.

Accordingly, Complaint Counsel has met its burden of

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demonstrating a reasonable probability that the Joinder is likely to substantially lessen competition in the market for the sale of GAC inpatient hospital services to MCOs in Lucas County, Ohio, in violation of Section 7 of the Clayton Act. Section 11 of the Clayton Act directs the FTC to issue orders requiring a violator of Section 7 to divest itself of the acquired assets. Divestiture is the usual and proper remedy where a violation of Section 7 has been found. Respondent has failed to demonstrate that this case presents unusual circumstances sufficient to override the presumption that total divestiture is the appropriate method to restore competition. Therefore, the Order entered in this case requires total divestiture, as well as necessary ancillary relief.

II. FINDINGS OF FACT**A. The Parties****1. ProMedica Health Systems, Inc.**

1. ProMedica Health System, Inc. (“ProMedica”) is a nonprofit health-care system incorporated in the state of Ohio and headquartered at 1801 Richard Road, Toledo, Ohio, 43607. ProMedica’s health-care system serves northwestern and west-central Ohio and southeastern Michigan. (Complaint ¶ 7; Answer ¶ 7).

2. ProMedica is an integrated health-care delivery system that includes a physician component, a hospital component, and Paramount Healthcare, an insurance company. (Oostra, Tr. 5772, 5784; *see* Section II.H.4, *infra*).

3. ProMedica has a total of eleven hospitals in Ohio and Michigan. (Oostra, Tr. 5772-5773).

4. ProMedica’s Michigan hospitals are Bixby Hospital in Adrian, Michigan; Herrick Hospital in Tecumseh, Michigan; and Hillsdale Hospital, a ProMedica affiliate, located in Hillsdale, Michigan. (Oostra, Tr. 5773).

5. ProMedica’s Ohio hospitals outside of the Lucas County, Ohio area are Defiance Regional Medical Center in Defiance,

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Ohio; Fostoria Community Hospital in Fostoria, Ohio; and a joint operating company hospital in Lima, Ohio. (Oostra, Tr. 5773).

2. St. Luke's Hospital

6. St. Luke's Hospital ("St. Luke's"), located at 5901 Monclova Road, Maumee, Ohio, 43537, is a formerly independent, nonprofit general acute-care community hospital. (Complaint ¶ 9; Answer ¶ 9).

7. St. Luke's has ownership interests in two medical office buildings in Perrysburg, Wood County, Ohio. It also operates three outpatient radiology imaging centers: one is located in Sylvania, Ohio; one in Toledo, and one in Oregon, Ohio. (Wakeman, Tr. 2752-2753).

8. St. Luke's also has a 50 percent ownership in SurgiCare, an outpatient center located on St. Luke's campus. (Wakeman, Tr. 2873).

B. The Joinder Agreement

9. On May 25, 2010, the parties entered into a Joinder Agreement ("Joinder Agreement"), to which OhioCare Health System, Inc. ("OhioCare") and the St. Luke's Foundation were also parties. (PX00058 at 001; Hanley, Tr. 4627-4628, *in camera*).

10. Prior to the Joinder Agreement, St. Luke's was a wholly owned subsidiary of OhioCare, along with several other subsidiaries including St. Luke's Hospital Foundation; Care Enterprises, Inc.; Physician Advantage MSO; and OhioCare Physicians, LLC ("WellCare"). (Wakeman, Tr. 2733; RX1139 at 000008, 000032-000033; PX00058 at 001).

11. Pursuant to the Joinder Agreement, effective September 1, 2010, ProMedica became the sole corporate member or shareholder of St. Luke's and other affiliated entities. (Complaint ¶ 2, Answer ¶¶ 2, 11; PX00058 at 009-012 (Joinder Agreement § 3.1)).

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C. The Voluntary Hold Separate Agreement

12. On August 18, 2010, the FTC and ProMedica entered into a limited, 60-day Hold Separate Agreement, to allow the FTC investigation to continue. (PX00069 (Hold Separate Agreement); FTC Petition, Petition Ex. 1 at ¶ 15 (Liu, Decl.), *ProMedica Health Sys., Inc.*, No. 3:10-cv-02340-DAK).

13. The Hold Separate Agreement includes several key provisions designed to temporarily preserve St. Luke's viability, competitiveness, and marketability. The Hold Separate Agreement prevents, among other things: (1) ProMedica's termination of St. Luke's health-plan contracts (while allowing health plans the option to extend their contracts with St. Luke's past the termination date, if a new agreement is not reached); (2) the elimination, transfer, or consolidation of any clinical service at St. Luke's; and (3) the termination of employees at St. Luke's without cause. (PX00069 at 001 (¶¶ 1-5)).

D. Federal District Court Proceedings

14. On January 6, 2011, the Commission authorized FTC staff to seek preliminary relief in federal district court that would require ProMedica to preserve St. Luke's as a viable, independent competitor during the FTC's administrative proceeding and any subsequent appeals. (Complaint ¶ 18, *ProMedica Health Sys., Inc.*, No. 3:10-cv-02340-DAK).

15. On January 7, 2011, the FTC and the State of Ohio filed an action for a temporary restraining order ("TRO") and preliminary injunction ("PI"), under Sections 13(b) and 16 of the FTC Act, 15 U.S.C. §§ 53(b), 26. (Complaint, *ProMedica Health Sys., Inc.*, No. 3:10-cv-02340-DAK). Plaintiffs sought temporary and preliminary injunctive relief from the court to prevent further integration of St. Luke's until the conclusion of the full administrative proceeding on the merits. (Complaint ¶ 7, *ProMedica Health Sys., Inc.*, No. 3:10-cv-02340-DAK).

16. On January 10, 2011, ProMedica answered the complaint and filed a response in opposition to Plaintiffs' motion for a TRO. (Answer, *ProMedica Health Sys., Inc.*, No. 3:10-cv-02340-DAK;

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Def.'s Resp. in Opp. to Pltfs.' Motion for TRO, *ProMedica Health Sys., Inc.*, No. 3:10-cv-02340-DAK).

17. On February 10 and 11, 2011, the District Court held a one and a half day hearing regarding the motion for a preliminary injunction. (*FTC v. ProMedica Health Sys.*, No. 3:11 CV 47, 2011 U.S. Dist. LEXIS 33434 at *2-3, *5 (N.D. Ohio March 29, 2011)).

18. On March 29, 2011, U.S. District Court Judge David A. Katz, issued his decision. (*ProMedica*, 2011 U.S. Dist. LEXIS 33434). Judge Katz ordered that the Hold Separate Agreement was to continue until either the completion of all legal proceedings by the Commission, including all appeals, or further order of the District Court, with an update on November 30, 2011, if the FTC had not completed actions by that date. (*FTC v. ProMedica*, 2011 U.S. Dist. LEXIS 33434 at *164).

E. Hospital Services

1. Inpatient hospital services

19. Inpatient services are those services that require admission to the hospital for a period of 24 hours or more, while outpatient services either do not require admission to the hospital or require patients to stay in a hospital less than a day. (Korducki, Tr. 483-484; Radzialowski, Tr. 638).

a. Primary, secondary, tertiary, and quaternary services

20. There is a continuum of different levels of intensity of inpatient hospital services. This continuum is typically described with reference to various levels or types of services. (Radzialowski, Tr. 637).

21. Primary services are those that occur regularly in the community and are of mild to moderate severity, including routine procedures such as hernias, gallbladders, and inpatient pediatrics. (Gold, Tr. 195, Korducki, Tr. 481-482; Radzialowski, Tr. 637).

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22. Secondary services are more complex than primary services and require some specialization and greater resources, including, for example, complex orthopedic surgery and bariatric services. (Korducki, Tr. 482, 485; Radzialowski, Tr. 637).

23. Tertiary services are more complex and specialized than primary and secondary services, and are often more invasive and require different technology and resources. (Korducki, Tr. 482; Radzialowski, Tr. 637; Shook, Tr. 893). Tertiary services include complex electrophysiology, burn units, or neurological intensive care. (Gold, Tr. 194-195; Shook, Tr. 893).

24. Hospitals that provide tertiary services typically also provide less complex primary and secondary services. (Radzialowski, Tr. 737).

25. Quaternary services are the most complex and include procedures such as transplants and tend to require very specific technologies. (Shook, Tr. 921; Radzialowski, Tr. 637; Guerin-Calvert, Tr. 7185).

26. The dividing line between the various levels of service is not precisely defined and may even differ from patient to patient, depending on the patient's health and medical history. What is a primary or secondary level procedure for one person may be a tertiary level procedure for another patient. (Shook, Tr. 892-894; Korducki, 483; PX01917 at 003-004 (Radzialowski Dep. at 9-10, *in camera*)).

b. Inpatient obstetrical services

27. Some obstetrical ("OB") services (F. 312) are offered as inpatient services and others are offered as outpatient services. (Marlowe, Tr. 2432).

28. Childbirth, recovery and some postpartum services are provided on an inpatient basis at a hospital. (Marlowe, Tr. 2431-2433; Read, Tr. 5275).

29. LDRP stands for "labor, delivery, recovery, and postpartum." The term refers to a patient room that

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accommodates a woman from her admission to the hospital when she is in labor through delivery and recovery until she leaves the hospital. (Marlowe, Tr. 2407-2408).

30. In an LDR room, patients labor, deliver and recover in one room before being transferred to a postpartum room. (Marlowe, Tr. 2409; Read, Tr. 5280).

31. OB services other than actual childbirth, recovery, and immediate postpartum services are generally delivered on an outpatient basis. These services may include office visits and ultrasound or lab tests. (Marlowe, Tr. 2431-2433; Read, Tr. 5276).

2. Outpatient services

32. Outpatient services are those services that do not require an overnight stay in the hospital. (JX00002A ¶ 2).

33. Outpatient services include therapeutic services, such as physical therapy or respiratory therapy, and diagnostic services, such as lab, radiology, EKG, MRI and CT scanning. (Shook, Tr. 984-985; Beck, Tr. 429-430).

34. Outpatient services also include general medical-surgical procedures that do not require a 24-hour admission. (Shook, Tr. 892-893). Specialized services such as oncology care, wound care, and sleep studies also constitute outpatient services. (Beck, Tr. 429-430; Korducki, Tr. 516).

35. Gynecological care is an outpatient service. (Gold, Tr. 203).

36. Most hospitals treat more patients on an outpatient basis than on an inpatient basis. (Radzialowski, Tr. 738).

37. Hospitals in Toledo have seen a shift in services from the inpatient setting to the outpatient setting and recognize that an increasing percentage of services are being sought, and rendered, on an outpatient basis. (Shook, Tr. 878-879, 1022; Beck, Tr. 409; RX270 at 000004, *in camera*).

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F. Reimbursement/payment for hospital services

38. Hospitals receive reimbursement for their services from various sources. Most patients treated by hospitals fall into one of three broad payment categories: Medicare/Medicaid, self-pay/indigent, or private commercial insurance. (Oostra, Tr. 5783; Town, Tr. 3608).

39. In Lucas County, Ohio, roughly 65 percent of patients receiving inpatient care are covered by Medicare or Medicaid, roughly 29 percent are privately insured, and roughly 6 percent are self-pay. (PX02148 at 010 (¶ 14) (Town Expert Report), *in camera*).

1. Government insurance

40. Medicare is a health insurance program administered by the federal government, and Medicaid is a health insurance program administered by state governments. (Wachsman, Tr. 4847-4848).

41. To be eligible for Medicare, generally, patients must be age 65 or older. (Pugliese, Tr. 1435).

42. Hospitals are obligated to accept Medicaid admissions. (Guerin-Calvert, Tr. 7296).

43. Providers cannot negotiate Medicare and Medicaid reimbursement rates, which are established by the Centers for Medicare and Medicaid Services (“CMS”). (Wachsman, Tr. 4847-4848; McGinty, Tr. 1169).

2. Commercial health insurance

44. Privately-insured patients obtain health insurance coverage primarily through commercial health plans. (PX02148 at 010 (¶ 15) (Town Expert Report), *in camera*). These health plans typically use a variety of methods to manage the cost of the medical care provided to their members. (Town, Tr. 3616; PX02148 at 010 (¶ 15) (Town Expert Report), *in camera*).

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45. Managed Care Organizations (“MCOs”) include companies that negotiate provider networks with hospitals and offer health insurance products to employers. (Rupley, Tr. 1968; Radzialowski, Tr. 731-733; Pirc, Tr. 2175-2176, 2274-2275).

46. The health insurance products that health plans offer to employers fall into two broad categories: self-insured and fully-insured. (Town, Tr. 3612; PX02148 at 011-012 (¶ 18) (Town Expert Report), *in camera*; Pugliese, Tr. 1430-1432; Pirc, Tr. 2175; Radzialowski, Tr. 624-625; McGinty, Tr. 1226-1227; Sheridan, Tr. 6701, *in camera*; Sandusky, Tr. 1293).

47. For the typical “fully-insured” health insurance product, health plans charge a fixed premium for a set period of time, and the risk that expenses for health-care may exceed the premiums collected is typically borne by the health insurer and not the employer. (Radzialowski, Tr. 624; Sandusky, Tr. 1390; Pugliese, Tr. 1430-1431; Pirc, Tr. 2175-2176; Randolph, Tr. 6916-6917, 6920).

48. An MCO may also act as a third party administrator (“TPA”), providing claims-handling services as part of an “administrative services only” (“ASO”) contract with self-insured employers. (Neal, Tr. 2096-2097; Radzialowski, Tr. 731-733; Pirc, Tr. 2175-2176, 2273-2275).

49. For self-insured products, the employer typically funds an account that the insurer draws upon to pay health-care expenses. (Pugliese, Tr. 1431).

50. Under a self-insured plan, or ASO, plan, the employer collects premiums from its employees and bears the risk that health-care expenses paid out may exceed the premiums collected by the employer. (Radzialowski, Tr. 624-625; McGinty Tr. 1155; Sandusky, Tr. 1293-1296, 1390; Pugliese, Tr. 1430-1431; Pirc, Tr. 2175-2176; Randolph, Tr. 6917-6919).

51. Under a self-insured plan, the employer pays the MCO a fee in exchange for access to the health plan’s provider network at the rates negotiated by the health plan and, typically, for

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administration of its employees' claims. (Pirc, Tr. 2175-2176; Pugliese, Tr. 1431-1432; Radzialowski, Tr.621-622, 629-630).

3. Self-pay/indigent

52. In Lucas County, if a self-pay patient cannot afford his or her charges, hospitals provide indigent and charity care at their own expense. (Town, Tr. 3608-3609;Wachsman, Tr. 4848-4849; Gold, Tr. 268-269; PX01923 at 025-026 (Town, Dep. at 99-101)).

G. The Hospitals

1. ProMedica Hospitals

53. Not including St. Luke's, ProMedica's hospitals in Lucas County are The Toledo Hospital ("TTH"), Toledo Children's Hospital, Flower Hospital ("Flower") and Bay Park Community Hospital ("Bay Park"). (Complaint ¶ 8; Answer ¶ 8; McGinty, Tr. 1186; Oostra, Tr. 5773).

a. The Toledo Hospital

54. The Toledo Hospital ("TTH") was the first hospital to become part of what was to become ProMedica Health System. (Oostra, Tr. 5776).

55. TTH is licensed for between 700 and 800 beds (not including the Toledo Children's Hospital on its campus) of which approximately 550 are staffed beds. (Oostra, Tr. 5773; PX01904 at 017 (Steele, IHT at 58-59)).²

56. TTH offers all basic general acute-care ("GAC") services, as well as more specialized, higher-acuity tertiary services. (McGinty, Tr. 1186-1187; Pirc, Tr. 2188; Oostra, Tr. 5773-5774).

² The term "staffed beds" refers to beds that are actually set up and available for use by patients and which have nursing staff, physicians, pharmacists, and other support staff to attend to them. The term "registered beds" describes a hospital's maximum beds allowable by state statute. (Gold, Tr. 201-202; Guerin-Calvert, Tr. 7278).

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57. In addition to primary services, ranging from general medical-surgical to orthopedic care and obstetrics, TTH also houses a Level I trauma center. (Oostra, Tr. 5774).

58. TTH is one of only two Lucas County hospitals that offer Level III inpatient OB services. (Shook, Tr. 1045; Marlowe, Tr. 2436).

59. TTH draws its patients primarily from the Toledo area. (Oostra, Tr. 5776-5777).

b. Flower Hospital

60. Flower is a full-service community hospital. (McGinty, Tr. 1186; Pirc, Tr. 2188; Oostra, Tr. 5777). Flower became part of ProMedica around 1995. (Oostra, Tr. 5778).

61. Flower is licensed for approximately 300 beds and has approximately 250 staffed beds. (Oostra, Tr. 5777; PX02389 at 015, *in camera*).

62. Flower offers services including GAC, general medical-surgical, obstetrics, outpatient radiation and chemotherapy, and post-acute services, such as a rehab center and an Alzheimer's center. (Oostra, Tr. 5777).

63. As a community-style hospital, Flower does not provide tertiary care. (PX01902 at 008 (Sheridan, IHT at 23-24), *in camera*).

64. Flower offers Level I inpatient OB services. (Marlowe, Tr. 2435; Read, Tr. 5276). Flower offers inpatient OB services in an LDRP setting. (Marlowe, Tr. 2409, 2435; Read, Tr. 5276, 5281).

65. Flower is located in Sylvania, Ohio, and draws its patients primarily from Southeast Michigan and the Sylvania area. Flower draws patients from Michigan because it is located very close to the Michigan border. (Oostra, Tr. 5778).

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c. Bay Park

66. Bay Park is a full-service community hospital, offering all GAC services, including emergency, OB services, and general medical-surgical services, among other general services. (Oostra, Tr. 5778; McGinty, Tr. 1186; Pirc, Tr. 2188).

67. Bay Park opened around the year 2000. (Oostra, Tr. 5779).

68. As a community-style hospital, Bay Park does not provide tertiary care. (PX01902 at 008 (Sheridan, IHT at 23-24), *in camera*).

69. Bay Park offers Level I inpatient OB services in an LDRP setting. (Marlowe, Tr. 2435; Read, Tr. 5276, 5281).

70. Bay Park has approximately 86 staffed and registered beds. (Oostra, Tr. 5778).

71. Bay Park is located in Oregon, Ohio, approximately 40 minutes from Flower and 20 minutes from TTH. (Oostra, Tr. 5778-5779).

2. St. Luke's Hospital

72. St. Luke's is located in a suburban area southwest of the city of Toledo, in southwest Lucas County. (Wakeman, Tr. 2477). St. Luke's offers GAC inpatient services. (Joint Stipulations of Law and Fact, JX00002A ¶ 5).

73. St. Luke's is a full-service community hospital with a range of outpatient and inpatient services, including: emergency services, medical-surgical services, OB services, intensive care services, imaging services, and limited oncology, neurosurgery, and pediatric services. (Wakeman, Tr. 2753-2755).

74. Other than some tertiary cardiac services through its heart center, such as angioplasty and open heart surgery, St. Luke's performs few if any tertiary services and no quaternary services. (PX01909 at 029 (Dewey, IHT at 109); JX00002A ¶ 6).

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75. St. Luke's offers Level I inpatient OB services. (Shook, Tr. 1045; Marlowe, Tr. 2435; Read, Tr. 5276; Wakeman, Tr. 2755). St. Luke's does not offer more complex OB services. (Wakeman, Tr. 2755-2756). St. Luke's offers its inpatient OB services in an LDRP setting. (Marlowe, Tr. 2408-2409; Read, Tr. 5281).

76. St. Luke's has delivered approximately 600 babies a year over the past ten years. (Marlowe, Tr. 2443).

77. St. Luke's has 178 staffed beds. (Wakeman, Tr. 2638, *in camera* (about 175-185 staffed beds); PX01322, *in camera*).

78. St. Luke's draws most of its patients from the zip codes closest to the hospital, including what St. Luke's refers to as its "primary service area" comprising about 14 surrounding zip codes, and what St. Luke's refers to as its "core service area" comprising 7 or 8 zip codes in southwest Lucas County and north Wood County. (Wakeman, Tr. 2756-2757; PX01016 at 003, *in camera*).

3. Mercy Health Partners

79. Mercy Health Partners ("Mercy") is a not-for-profit hospital system in northwestern Ohio that is part of Catholic Health Partners ("CHP"). Mercy operates six hospitals in CHP's northern region, three of which are located in Lucas County and near Toledo. (Shook, Tr. 887, 889-890).

80. Mercy offers GAC inpatient services. (Joint Stipulations of Law and Fact, JX00002A ¶ 7).

81. Mercy's three general population hospitals in Lucas County are St. Vincent, Mercy St. Anne Hospital ("St. Anne"), and Mercy St. Charles Hospital ("St. Charles"). (Shook, Tr. 892).

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a. St. Vincent

82. St. Vincent is a large, tertiary teaching facility with eight intensive care units, a Level I trauma center, a Level III OB unit, and a large cardiology service known as the Regional Heart and Vascular Center. (Shook, Tr. 887-888, 895-896, 1045).

83. St. Vincent has 568 registered beds and 445 staffed beds. (Guerin-Calvert, Tr. 7176-7177).

84. St. Vincent is the only other Lucas County hospital besides TTH that offers Level III inpatient OB services. (Shook, Tr. 1045; Marlowe, Tr. 2436). St. Vincent offers its inpatient OB services in an LDR setting. (Read, Tr. 5281).

85. St. Vincent also has the only burn unit in Northwest Ohio. (Shook, Tr. 1029; Wakeman, Tr. 2759).

86. St. Vincent delivered 1180 babies in 2010. (Marlowe, Tr. 2444).

87. St. Vincent is located in downtown Toledo and is the largest provider to Medicaid patients in the state of Ohio. (Shook, Tr. 887-889).

88. A disproportionate share payment is a payment that a hospital receives from the state of Ohio when it treats a certain number of Medicaid patients. (Shook, Tr. 1101, *in camera*).

89. St. Vincent qualifies for disproportionate share payments due to the high level of Medicaid patients it treats. (Shook, Tr. 1101-1102, *in camera*).

90. Mercy is making extensive renovations at St. Vincent to add more private beds. (Shook, Tr. 903-904).

91. The hospital located closest to St. Vincent is ProMedica's TTH. (Shook, Tr. 899).

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b. St. Anne

92. St. Anne, which opened in 2002 and is located in west Toledo, is a general medical-surgical hospital with operating rooms and performs both inpatient and outpatient surgeries. St. Anne does not offer tertiary services, obstetrics, psychiatric services, or serious emergency services. (Shook, Tr. 899-900, 903).

93. St. Anne has 128 registered beds and 96 staffed beds. (Guerin-Calvert, Tr. 7178).

94. St. Anne offered inpatient OB services when it opened, but Mercy discontinued those services at St. Anne in early 2008, because St. Anne experienced a significant decrease in deliveries and no longer performed enough deliveries to maintain quality standards or break even financially. (Shook, Tr. 901, 958, 1047).

95. Prior to the decision to no longer offer OB services, St. Anne delivered about 400 babies a year. Mercy estimated that a hospital needed to deliver 800 or 900 babies a year in order to break even financially. (Shook, Tr. 1047).

96. It is highly unlikely that St. Anne's will reinstitute OB services. (Shook, Tr. 958-959).

97. St. Anne is the closest hospital to ProMedica's Flower Hospital. (Shook, Tr. 917; Oostra, Tr. 5802-5803).

c. St. Charles

98. St. Charles is located in Oregon, Ohio, on the east-side of the Maumee River from downtown Toledo. (Shook, Tr. 902).

99. St. Charles is a general medical-surgical hospital that also offers Level II OB services. (Shook, Tr. 902). St. Charles is the only Lucas County, Ohio hospital that offers Level II inpatient OB services. (Shook, Tr. 1045). St. Charles offers its inpatient OB services in an LDRP setting. (Read, Tr. 5281).

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100. St. Charles does not offer tertiary services. (Shook, Tr. 903).

101. St. Charles has approximately 350 registered beds and fewer than 150 staffed beds. (Shook, Tr. 903).

102. St. Charles is located less than one mile away from ProMedica's Bay Park hospital. (Shook, Tr. 917, 1035-1036).

4. UTMC

103. University of Toledo Medical Center ("UTMC") is part of the University of Toledo and is an instrumentality of the State of Ohio. (Gold, Tr. 295).

104. UTMC was formed when the University of Toledo and the Medical College of Ohio merged in 2006. (Gold, Tr. 186).

105. UTMC is considered a research and teaching hospital. (Radzialowski, Tr. 737; McGinty, Tr. 1188).

106. UTMC's mission is to support the academic needs of the University of Toledo, to deliver high-quality health-care, and to serve the tertiary and quaternary needs of the community. (Gold, Tr. 192-193, 252-253; Radzialowski, Tr. 743).

107. UTMC provides GAC inpatient hospital services. (Joint Stipulations of Law and Fact, JX00002A ¶ 7).

108. UTMC is the only hospital in Lucas County that offers quaternary services. (Radzialowski, Tr. 743)

109. UTMC focuses on providing tertiary and quaternary hospital services, as a way to fulfill its mission of educating medical students. (Gold, Tr. 192-194; Shook, Tr. 920-921).

110. UTMC does not offer inpatient OB services. (Answer ¶¶ 4, 15, 20; Oostra, Tr. 5972; Gold, Tr. 203, 220).

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UTMC does not plan to offer inpatient OB services in the future. (Gold, Tr. 220).

111. UTMC has more than 300 registered beds of which approximately 225 are staffed. (Gold, Tr. 199-201).

112. In 2008, UTMC treated 3,114 commercially insured patients. (PX02136 at 035, *in camera*).

113. UTMC's service area overlaps substantially with St. Luke's, with a high proportion of St. Luke's GAC discharges drawing from zip codes in which UTMC also draws a significant number of GAC discharges. (PX02136 at 010, *in camera*).

H. Managed Care Organizations

114. MCOs operating in Lucas County, Ohio include Medical Mutual of Ohio, Anthem Blue Cross Blue Shield, Paramount Healthcare, FrontPath Health Coalition, United Healthcare, Aetna, Inc., Humana, Inc., and some smaller companies. (Pugliese, Tr. 1574; Pirc, Tr. 2178).

1. MCO terminology

115. "MCO" refers to managed care organization. MCOs may be variously referred to as "payors," "health insurance plans," or "health insurance companies." The terms are used interchangeably. (Pirc, Tr. 2175; Town, Tr. 3610-3612).

116. "Member" or "insured" is the term used to refer to the person who is covered by a particular payor's insurance plan. (Radzialowski, Tr. 616-617).

117. "HMO" stands for Health Maintenance Organization. (Radzialowski, Tr. 609).

118. An HMO is a collaborative product where a member is supposed to work through a primary care physician ("PCP"), who is the gatekeeper for his or her care and ensures coordination among all health-care providers. (Radzialowski, Tr. 609; Randolph, Tr. 6895).

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119. HMOs traditionally required members to obtain referrals from their PCPs, before they could obtain care from specialists. (Radzialowski, Tr. 610).

120. HMOs have evolved over the years and some HMOs today have fewer restrictions than the traditional HMOs did. (Radzialowski, Tr. 610).

121. In a pure HMO product, if a member goes to a non-preferred provider, they receive no benefits or reimbursement for services. (Radzialowski, Tr. 614).

122. “PPO” stands for Preferred Provider Organization. (Radzialowski, Tr. 612).

123. In a PPO plan, members receive a list of preferred or “in-network” providers. If they obtain care from one of the listed providers, their out-of-pocket costs are lower than if they see a provider that is not on the list (e.g., an “out-of-network” provider). (Radzialowski, Tr. 612).

124. MCOs also offer point-of-service (“POS”) plans. These plans vary from MCO to MCO, but are generally less restrictive than an HMO and more restrictive than a PPO. (Radzialowski, Tr. 613).

125. In a POS plan, some out-of-network providers are available to the member, at a higher coinsurance level. (Randolph, Tr. 6895).

126. In a POS plan, a member is encouraged to have a PCP as a gatekeeper, but this is not a requirement. (Radzialowski, Tr. 614).

127. In a traditional indemnity plan, there are no restrictions on the medical care that is received. The MCO will pay whatever amount the hospital bills. (Radzialowski, Tr. 615-616).

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2. Medical Mutual of Ohio

128. Medical Mutual of Ohio (“MMO”) is an MCO that operates statewide networks in Ohio, Indiana, Georgia, and South Carolina and operates in 17 counties of Kentucky. (Pirc, Tr. 2174).

129. MMO offers health insurance plans, dental plans, and term life insurance. (Pirc, Tr. 2273).

130. The commercial health insurance products offered by MMO include PPO, HMO, and POS plans. (Pirc, Tr. 2174-2175). MMO exited the market for Medicare Advantage, a health insurance plan for Medicare recipients, beginning January 1, 2011. (Pirc, Tr. 2273).

131. MMO also provides third party administration services to employers who self-insure their employees’ health insurance. (Pirc, Tr. 2273-2274; Neal, Tr. 2096).

132. MMO provides health insurance to approximately 1.4 million individuals (“covered lives”) in Ohio, and is the largest MCO in Lucas County, with approximately 100,000 covered lives in Lucas County. (Pirc, Tr. 2177-2178, 2273).

133. MMO has a market share of approximately 25 percent in Lucas County. (Pirc, Tr. 2178).

134. Approximately 60 percent of MMO’s commercial health insurance business in Lucas County comes from administrative services it provides to self-insured employers; the remaining 40 percent is for fully-insured products. (Pirc, Tr. 2274).

135. MMO currently has all of the Lucas County hospitals in all of its networks. (Pirc, Tr. 2203).

136. ProMedica’s hospitals have participated in the MMO network since January 1, 2008. (Pirc, Tr. 2204; 2275).

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137. Mercy has participated in the MMO network for more than 10 years. (Pirc, Tr. 2275).

138. UTMC has participated in MMO's network for more than 10 years. (Pirc, Tr. 2275).

139. St. Luke's has participated in MMO's network for more than 10 years. (Pirc, Tr. 2275).

3. Anthem Blue Cross Blue Shield

140. Anthem Blue Cross Blue Shield ("Anthem") is an MCO that offers health, dental, vision, behavioral health, life and disability insurance plans. (Pugliese, Tr. 1534-1535).

141. Anthem's parent company is WellPoint. WellPoint is a publicly traded, for-profit national health insurer, offering health insurance products in Ohio and many other states. WellPoint has over 33.3 million insured members in its MCO and is the largest health benefits company in the United States in terms of medical membership. (Pugliese, Tr. 1427, 1528-1530).

142. WellPoint is an independent licensee of the Blue Cross and Blue Shield Association and markets its health insurance products under the Blue Cross Blue Shield brand. (Pugliese, Tr. 1528)

143. Blue Cross Blue Shield is the most recognized brand in the health-care industry. (Pugliese, Tr. 1528).

144. Anthem's position as the exclusive licensee of Blue Cross Blue Shield in Ohio gives it national name recognition that other health insurance providers do not have. (Pugliese, Tr. 1531).

145. Anthem affirmatively markets this national name recognition to health-care providers when trying to contract with them to become part of the Anthem provider network. (Pugliese, Tr. 1531).

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146. Anthem also affirmatively markets its national name recognition to employers and members. (Pugliese, Tr. 1531).

147. Anthem, with approximately 30,000 commercially insured members in Lucas County, is one of the top two or three MCOs in Lucas County. (Pugliese, Tr. 1436; RX204 at 000003 (Pugliese, Dep. at 9)).

148. Anthem offers a broad spectrum of managed care plans in Ohio, including PPO plans, HMO plans, POS plans and traditional indemnity plans. (Pugliese, Tr. 1531-1532).

149. In Lucas County, Anthem markets a broad access PPO network, which includes the vast majority of available providers, to commercial customers. (Pugliese, Tr. 1434-1435).³

150. Anthem also markets a Medicare Advantage HMO plan with a narrower network, mostly to individual Medicare enrollees. (Pugliese, Tr. 1434-1436).

151. Anthem primarily markets its commercial health insurance products to employers. (Pugliese, Tr. 1429-1430).

152. Anthem serves a wide variety of employers, ranging from large employers with more than 1,000 employees to small companies with less than 50 employees. (Pugliese, Tr. 1429-1430).

153. For its commercial health insurance plans, Anthem offers a fully-insured product and a self-insured product, its administrative services only product. (Pugliese, Tr. 1430).

154. Anthem's self-insured product comprises approximately 55 percent of its commercial business in Lucas County. (Pugliese, Tr. 1432).

155. Anthem's self-insured employers pay an administrative fee to Anthem for managing the benefit design and

³ With respect to provider networks, the terms "broad access" and "open provider network" are synonymous. (Pirc, Tr. 2203).

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handling claim administration. To pay for health-care expenses, Anthem draws against an employer-funded account. (Pugliese, Tr. 1431).

156. Anthem currently has all Lucas County hospitals in its commercial PPO network. (Pugliese, Tr. 1450).

157. ProMedica has participated in Anthem's network for at least 20 years. (Pugliese, Tr. 1538).

158. Mercy began participating in Anthem's commercial PPO network as of January 1, 2008. (Pugliese, Tr. 1539).

159. UTMC has participated in Anthem's network since 2003 or 2004. (Pugliese, Tr. 1476, *in camera*; Pugliese, Tr. 1538).

160. St. Luke's participated in Anthem's network prior to 2005. (Pugliese, Tr. 1538-1539).

161. Anthem terminated St. Luke's PPO contract effective January 31, 2005. (Pugliese, Tr. 1539; RX1026 at 000001).

162. St. Luke's began participating in Anthem's network again in July 2009. (Pugliese, Tr. 1477, *in camera*; Wakeman, Tr. 2530-2531).

4. Paramount Healthcare

163. Paramount Healthcare ("Paramount") is a wholly owned subsidiary of ProMedica. Paramount is one of the largest commercial MCOs in Lucas County. (Complaint ¶ 8; Answer ¶ 8; Wachsmann, Tr. 4855-4856; Hanley, Tr. 4784-4785, *in camera*; PX00270 at 024 (S&P Credit Presentation)).

164. Paramount is licensed for its Medicare, Medicaid, and commercial insurance products in Ohio, and is licensed for its commercial and Medicare products in Michigan. (Randolph, Tr. 6905).

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165. Paramount's health insurance products are marketed in Lucas County, Ohio, as well as in certain counties in the southeastern part of Michigan and northwest Ohio. (Randolph, Tr. 6895-6896).

166. Paramount's HMO product is its largest product, and is offered as either a fully-insured or self-insured product. (Randolph, Tr. 6907-6908).

167. Paramount Healthcare is the trade name for Paramount's commercial HMO product. (Randolph, Tr. 6907).

168. There are approximately 85,000 to 90,000 covered lives in Paramount's commercially insured products. (Randolph, Tr. 6906).

169. Approximately 50 percent of Paramount's commercially insured membership is fully-insured, and approximately 50 percent is self-insured. (Randolph, Tr. 6929).

170. Paramount's provider network is low cost, meaning Paramount's aggregate premium cost is low compared to its competitors in northwest Ohio. (Randolph, Tr. 6940).

171. Paramount focuses its marketing efforts to employers and providers by noting its low cost and local service. (Randolph, Tr. 6915-6916, 6942).

172. Paramount has an arrangement with ProMedica hospitals, resulting in a closed or limited network of hospitals. The Mercy hospitals do not participate in Paramount's network. (Radzialowski, Tr. 627; Pugliese Tr. 1574-1575).

173. Paramount's hospital provider network in Lucas County includes the ProMedica Hospitals (Flower, TTH, Toledo Children's Hospital, Bay Park, and, pursuant to the Joinder Agreement, St. Luke's) and UTMC. (Randolph, Tr. 6936; PX00058 at 022-023).

174. Paramount's low premium costs are attributable in part to Paramount's ability, as a part of the ProMedica Health System,

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to obtain favorable pricing from ProMedica hospitals. Paramount gets the best pricing from ProMedica compared to any other MCO. (Randolph, Tr. 7070-7071).

175. Paramount's low premium costs are attributable in part to Paramount's offering a narrow network, and providers' resulting expectation that the narrow network will result in increased patient volume. (Randolph, Tr. 6966).

176. Paramount maintains a closed or limited provider network because ProMedica believes that it can keep costs lower by keeping the provider panel limited. (Oostra, Tr. 5788-5789).

177. St. Luke's had been included in the Paramount network prior to January 1, 2001, when the contract ended and the parties did not successfully negotiate a new contract. (PX01022 at 002; Rupley, Tr. 1938-1940; Randolph, Tr. 6997-6999).

178. St. Luke's was not an in-network provider with Paramount between 2001 and August 31, 2010. (Joint Stipulations of Law and Fact, JX00002A ¶ 46).

179. St. Luke's rejoined Paramount's hospital provider network as part of the Joinder Agreement with ProMedica in September 2010. (PX00058 at 021-022; Randolph, Tr. 7004).

180. Paramount's hospital provider network is the smallest in Lucas County compared to its competitors. (Randolph, Tr. 6934).

181. For physician providers, Paramount's network is comparable to the networks of its competitors in Lucas County. (Randolph, Tr. 6934).

182. Approximately 80 percent of the physician providers in Paramount's network are independent of a hospital or health system, including physicians employed by Mercy and St. Luke's when St. Luke's was not in Paramount's provider network. (Randolph, Tr. 6933, 6938-6939).

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5. FrontPath Health Coalition

183. FrontPath Health Coalition (“FrontPath”) is a membership organization governed and managed by a coalition of 125 to 130 business “sponsors,” which include corporations, labor organizations, and public entities. (Sandusky, Tr. 1283, 1299).

184. FrontPath does business in northwest Ohio, southeast Michigan, and northeast Indiana. (Sandusky, Tr. 1298).

185. FrontPath’s sponsors include labor organizations and public entities, but are predominantly self-insured, large employers. (Sandusky, Tr. 1284-1285, 1293, 1299).

186. FrontPath has the “lion’s share” of the market for self-insured employers, and has recently begun offering a fully-insured product. (Sandusky, Tr. 1300, 1397).

187. For its self-insured employers, FrontPath does not design the employee health benefits plans or decide upon the specific elements of the plans they offer, such as deductibles, coverage breadth and limits, or out-of-pocket limits. These are determined by the employers. (Sandusky, Tr. 1390-1391, 1395).

188. FrontPath is one of the top three or four MCOs in Lucas County, with approximately 125,000 total covered lives, of which approximately 80,000 are in Lucas County. (Sandusky, Tr. 1299, 1300).

189. FrontPath’s fully-insured product has only approximately 2,000 covered lives and represents a very small portion of FrontPath’s overall preferred provider network business. (Sandusky, Tr. 1399).

190. FrontPath seeks to create provider networks that offer a full complement of services, including primary, secondary, tertiary and quaternary care services. (Sandusky, Tr. 1400-1401).

191. All Lucas County hospitals participate in the FrontPath network. (Sandusky, Tr. 1315).

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192. Not every Lucas County hospital offers all the services FrontPath seeks when building its provider network. (Sandusky, Tr. 1401).

193. In order for FrontPath to offer a full complement of health-care services, it is essential for it to include a least one hospital that offers advanced services. (Sandusky, Tr. 1401).

194. St. Luke's does not offer the high level secondary, tertiary or quaternary services FrontPath requires in its network. (Sandusky, Tr. 1401).

195. St. Luke's does not offer neonatal intensive care that FrontPath requires in its network. (Sandusky, Tr. 1402).

196. FrontPath requires other hospitals in addition to St. Luke's in order to meet all the needs of its sponsors. (Sandusky, Tr. 1402).

6. United Healthcare

197. United Healthcare ("United") is an MCO that offers various health insurance products throughout the United States. (Sheridan, Tr. 6613).

198. In Lucas County, United offers predominantly PPO plans. (Sheridan, Tr. 6613).

199. United has approximately 1 million commercial members in Ohio. (Sheridan, Tr. 6614).

200. Within Lucas County, United has approximately 15,000 commercially insured members. (Sheridan, Tr. 6615).

201. United's customers in Lucas County included the Catholic Diocese of Toledo and national accounts such as Best Buy that have a presence in Toledo; however, other than these large customers, United generally serves smaller groups in Lucas County. (Sheridan, Tr. 6615; PX01902 at 006 (Sheridan, IHT at 17, *in camera*)).

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202. When building its hospital provider network, United considers access, hospital quality, physician privileges, and the types of services offered. (Sheridan, Tr. 6622).

203. In its negotiations with hospital providers, [redacted] seeks competitive reimbursement rates that are “on par” with or “in the ballpark” with other competing MCOs. (PX01902 at 012 ([redacted], IHT at 39-40, *in camera*)).

204. All hospitals in Lucas County currently participate in United’s provider network. (Sheridan, Tr. 6620).

205. ProMedica participated with United until December 31, 2005 when it left the network. ProMedica rejoined United’s network in the fall of 2010. (Sheridan, Tr. 6620-6621; PX01902 at 014 (Sheridan, IHT at 49, *in camera*)).

206. Mercy became a participating provider with United on January 1, 2006. (Sheridan, Tr. 6620).

207. UTMC began participating with United in 2008. (PX01902 at 014 (Sheridan, IHT at 49, *in camera*)).

208. Over the past six years, United’s membership level has stayed consistent. This consistency was not affected by the loss of ProMedica from the network, or by the addition of Mercy, and later UTMC, to its network. (Sheridan, Tr. 6621-6622).

7. Aetna, Inc.

209. Aetna, Inc. (“Aetna”) is a national, for-profit, publicly traded health insurance company that operates individual subsidiaries in each state that are subsidiaries of the national company. (Radzialowski, Tr. 608, 611, 740, 827, *in camera*).

210. Aetna has millions of members nationwide. (Radzialowski, Tr. 744).

211. Aetna’s largest customers are large national corporations that have sites throughout the United States. (Radzialowski, Tr. 608).

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212. Aetna offers three types of commercial health insurance products: HMO plans (a standard HMO and a less restrictive Open Access HMO), a Managed Choice plan, and a PPO plan. Aetna's Managed Choice plan is a POS plan that is less restrictive than its HMO plans and more restrictive than its PPO plan. (Radzialowski, Tr. 601-602, 610, 612).

213. Aetna's customers in Lucas County include large employers such as the State of Ohio, IBM, and Microsoft. (Radzialowski, Tr. 620).

214. Aetna estimates that, nationally and in Lucas County, its HMO product represents 50 percent of its commercial health-care insurance business; its POS product represents 20 percent of its business; and its PPO product represents 30 percent of its business. (Radzialowski, Tr. 613, 617).

215. In Ohio, Aetna has between 750,000 and 1,000,000 commercial members. (Radzialowski, Tr. 744).

216. In Lucas County, Aetna has approximately 30,000 members for its commercial insurance products. Of its 30,000 commercially insured members, approximately 10,000 are fully-insured and 20,000 are self-insured. (Radzialowski, Tr. 618, 626).

217. For Aetna's self-insured employers, in exchange for an administrative fee paid to Aetna, Aetna designs their policy, provides identification cards for employees, provides access to the network of providers that it has created, and administers member claims. (Radzialowski, Tr. 629-630).

218. The predominant factors that Aetna looks to when building a provider network are a full complement of services, geographic locations for the provision of those services that meet the needs and desires of the people that buy the insurance, and services that meet Aetna's required quality. (Radzialowski, Tr. 655-656).

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219. Aetna considers it essential to have at least one tertiary hospital in its network, but Aetna does not require more than one Lucas County hospital that provides tertiary or higher-level services in its network. (Radzialowski, Tr. 599-600, 656-657, 743).

220. Individual providers do not need to provide the full spectrum of care as long as the whole network contains all the options needed for individual pieces of care. (Radzialowski, Tr. 656).

221. Aetna believes that it would be unable to provide an adequate network in Lucas County with St. Luke's alone if it did not also have either TTH or St. Vincent in its network. (Radzialowski, Tr. 743).

222. Aetna has contracted with all hospitals in Lucas County since 2006. (Radzialowski, Tr. 670).

223. Prior to 2006, Aetna did not contract with UTMC. (Radzialowski, Tr. 670-671).

224. Aetna did not see a dramatic increase or decrease in its business since 2004, including in the time period from 2006 to 2008 during which Aetna's network included all Toledo area hospitals in its network but the networks of MMO and Anthem did not. (Radzialowski, Tr. 741-742).

225. In contract negotiations with hospitals, Aetna seeks to leverage its national brand image. (Radzialowski, Tr. 658-659, 744).

8. Humana, Inc.

226. Humana, Inc. ("Humana") is a large, publicly-traded, national health-care company that offers a diverse range of products and services. (McGinty, Tr. 1224).

227. Humana operates in all 50 states, and has approximately 10.2 million covered lives nationally in its government and commercial insurance programs, with about 70

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percent of those covered by government products. (McGinty, Tr. 1154-1155, 1225).

228. Of the 470,000 persons covered by Humana's commercial and government products in Ohio, approximately 9,000 reside in Lucas County, with approximately 7,000 covered by government products and approximately 2,000 covered by commercial insurance. (McGinty, Tr. 1226).

229. Humana offers both a fully-insured and a self-insured product in Lucas County. The majority of Humana's commercial members are self-insured. (McGinty, Tr. 1226-1228).

230. The only MCO product that Humana offers to employers in Lucas County is its ChoiceCare PPO network. (McGinty, Tr. 1228).

231. In constructing a network, Humana evaluates price, geographic access, and quality, and also seeks to achieve a hospital configuration that offers high-end tertiary services, as well as, a robust network of community hospitals. (McGinty, Tr. 1172-1173).

232. Humana believes that the only way it will be able to sustain a statewide presence in Ohio for the commercial side of its business is to move toward narrower networks composed of high-quality, very efficient hospitals and providers. (McGinty, Tr. 1191).

233. Humana currently includes all Lucas County hospitals in its commercial PPO network. (McGinty, Tr. 1234).

I. Competitive Dynamics in MCO Contracting

1. Generally

234. MCOs contract with physicians, hospitals and ancillary providers to create a provider network. Members of MCOs who receive medical services from in-network providers pay a much lower share of the costs than members who receive medical

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services from out-of-network providers. (Radzialowski, Tr. 584; Pirc, Tr. 2176-2177).

235. A hospital becomes part of an MCO's network by entering into a provider contract with that MCO. (Town, Tr. 3621-3622; *see* Radzialowski, Tr. 658-661; Pugliese, Tr. 1454-1456; Pirc, Tr. 2205-2207).

236. The lower cost that members incur when using in-network providers provides a financial incentive to use in-network providers. (Sandusky, Tr. 1395-1397). Accordingly, a hospital's volume of patients from a specific MCO is largely determined by whether the hospital is part of the MCO's provider network. (Town, Tr. 3621-3622, 3626-3627; PX02148 at 014 (¶ 23) (Town Expert Report), *in camera*; Wachsman, Tr. 4852-4855).

237. MCOs compete with one another to be offered by employers in the menu of insurance products that employers offer to their employees. (Town, Tr. 3616-3617; PX02148 at 011 (¶ 17) (Town Expert Report), *in camera*; PX01944 at 028 (Pirc, Dep. at 106-107); *see also* Neal, Tr. 2092, 2099-2100; Caumartin, Tr. 1839; Buehrer, Tr. 3066-3067 (employers evaluate and negotiate various MCO offerings for their employees)).

238. Once included in the employer's menu of health insurance products, MCOs compete with one another to attract enrollees. (PX02148 at 011 (¶ 17) (Town Expert Report), *in camera*; PX01944 at 028 (Pirc, Dep. at 106-107); Neal, Tr. 2099-2100; Sandusky, Tr. 1302-1303).

239. Hospitals compete with one another for inclusion in MCOs' provider networks. (Town, Tr. 3626; PX02148 at 013-014 (¶¶ 20-21) (Town Expert Report), *in camera*; Sheridan, Tr. 6676; Pugliese, Tr. 1456-1457; Wachsman, Tr. 4852-4855).

240. One of the aspects upon which hospitals compete with each other is through the reimbursement rate the hospitals are willing in negotiations to offer or agree upon with payers. (Wachsman, Tr. 5115).

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241. A hospital's volume of patients from a specific MCO is largely determined by whether the hospital is part of the MCO's network. (Town, Tr. 3621-3622; 3626-3627; PX02148 at 014 (Town Expert Report), *in camera*; Wachsman, Tr. 4852-4855).

242. Once included in an MCO's network, hospitals in that network compete with one another to attract the MCO's members. (Town, Tr. 3630-3631; PX02148 at 014 (¶ 22) (Town Expert Report), *in camera*; Pugliese, Tr. 1456-1457; Sheridan, Tr. 6676).

243. Patients consider a variety of factors when choosing a hospital for inpatient services, including whether their physician has admitting privileges at a particular hospital, their doctor's preferences, and insurance coverage. (RX26 (Riordan, Dep. at 52-54, 56-57, 122); Shook, Tr. 939; Marlowe, Tr. 2444-2445; Town Tr. 3632; Read, Tr. 5283).

244. Patients also consider hospital quality and location as two of many factors when selecting a hospital. (Marlowe, Tr. 2444-2445; Read, Tr. 5283; Town, Tr. 3631).

245. In-network hospitals compete to attract patients primarily on non-price dimensions, clinical quality, amenities, cost, location, visibility, physician location, and patient experience, among others factors. (Town, Tr. 3630-3631; PX02148 at 014 (¶ 22) (Town Expert Report), *in camera*; Wachsman, Tr. 5115-5116; *see* Sandusky, Tr. 1304-1305; Wachsman, Tr. 5110-5111; Shook, Tr. 945-946; *see also* JX00002A at 002 (¶ 11) (Joint Stipulations of Law and Fact)).

246. Historically, MCOs in the Toledo area were comprised of various narrow network configurations. In recent years, employers changed their perspective on narrow networks and, as a result, MCOs, such as Medical Mutual and Anthem, were able to sell plans with broad networks. At present, with the exception of Paramount, all Lucas County MCOs offer broad, open-access networks. (McGinty, Tr. 1262-1263; *see* F. 172).

247. Generally, the lower the premium, the more attractive the MCO's product is to employers and their employees, provided the MCO's network offers the employees' preferred set of

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providers. (PX02148 at 011 (¶ 17) (Town Expert Report), *in camera*; Sandusky, Tr. 1287-1288; Lortz, Tr. 1699-1700, 1707; Caumartin, Tr. 1848-1849; *see also* Pirc, Tr. 2284; Pugliese, Tr. 1455).

2. Employers and employees

248. Employers generally do not negotiate directly with hospitals, but rather rely on MCOs to do so. (Neal, Tr. 2095, 2106; Pugliese, Tr. 1432-1433, 1547; Radzialowski, Tr. 748; PX01914 at 014 (Pirc, IHT at 49); Town, Tr. 3611; *see also* Caumartin, Tr. 1838-1839, 1873; Buehrer, Tr. 3062, 3089).

249. Employers rely on MCOs to develop the network of providers that employees/MCO members can access. (Neal, Tr. 2144-2145; Buehrer, Tr. 3066-3067; Town, Tr. 3955).

250. Commercially insured patients generally obtain health insurance through their employer. (Town, Tr. 3609-3610; PX02148 at 004-005 (¶ 4) (Town Expert Report), *in camera*).

251. Employers offer health insurance to their employees as part of their employees' total compensation package. (Town, Tr. 3610).

252. Some employers have exclusive relationships with a particular MCO, meaning that those employers agree only to use that MCO's provider network for their health services. (Sandusky, Tr. 1399-1400).

253. Employers may offer multiple MCO products to their employees, and from more than one MCO. (Radzialowski, Tr. 619-620; Sandusky, Tr. 1400).

254. When an employer offers multiple plans or networks, the employer may price the offerings at different premium levels. (Sandusky, Tr. 1400).

255. In choosing an MCO, employers consider principally the cost and the breadth of the provider networks available to their employees, in terms of geography, the types of services available,

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and choice of providers. (Neal, Tr. 2101-2104; Caumartin, Tr. 1848-1849; Buehrer, Tr. 3068, 3074-3075).

256. Employers want a health plan that offers a network with broad provider access so that employees and their family members can use their preferred physician or hospital. (Caumartin, Tr. 1861; Lortz, Tr. 1700-1704; Buehrer, Tr. 3068, 3074-3075; Neal, Tr. 2105-2107; PX02148 at 011 (¶ 17) (Town Expert Report), *in camera*).

257. Employers are generally willing to pay a higher premium for plans that have broad provider networks, than they are for plans that have narrower provider networks. However, some employers may find cost to be more important than breadth and prefer a narrower network in exchange for lower cost. (Pirc, Tr. 2282; Radzialowski, Tr. 665; McGinty, Tr. 1263; Pirc, Tr. 2214-2215; Randolph, Tr. 6943-6944).

258. Employers may use consultants to solicit and evaluate what MCOs offer, including cost, quality and access. (Neal, Tr. 2092; Caumartin, Tr. 1836, 1839, 1848-1849).

259. At the employer level, cost means the premium or the medical expenses. (Randolph, Tr. 6980-6981).

260. Employers seek to meet the health-care coverage preferences of their employees, while keeping their own costs low. (Caumartin, Tr. 1848-1849).

261. At the employee level, cost refers to the employee contribution to the premium, if any. In addition, the level of benefits, *i.e.*, the benefit design, affects employee cost by setting the level of any copays, coinsurance, deductibles, and out-of-pocket maximums. (Randolph, Tr. 6980-6981; Lortz, Tr. 1699-1700).

262. Employees want the best coverage at the lowest cost. (Lortz, Tr. 1699-1700, 1706-1707).

263. Based upon a negotiation process, employers select the combination of rates, benefit structures, and health-care provider

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networks that best meets the needs of the employer and its employees. (PX02148 at 013 (¶ 19) (Town Expert Report), *in camera*; Town, Tr. 3616-3617; Neal, Tr. 2099-2100, 2102; Caumartin, Tr. 1848-1849; Buehrer, Tr. 3066-3067, 3068, 3074-3075; Pugliese, Tr. 1432-1434; Radzialowski, Tr. 620-622).

3. Managed care organizations

264. MCOs seek to negotiate the lowest reimbursement rates that they can achieve. (Radzialowski, Tr. 750; McGinty, Tr. 1240; Pugliese, Tr. 1553; Pirc, Tr. 2211-2112).

265. In negotiating reimbursement rates with a hospital, an MCO's primary goal is to secure the lowest reimbursement rates possible, so that it can offer the lowest premium to employers relative to competing MCOs and thereby grow its business. (PX01914 at 014 (Pirc, IHT at 48-49).

266. The financial incentive for using in-network providers drives more patient volume to in-network providers, and thereby increases the MCOs' "bargaining leverage" with the providers. (Sandusky, Tr. 1395-1397).

267. "Bargaining leverage" may be defined as the advantage, or perception of advantage, of a particular entity at the bargaining table to try to make use of certain attributes in the negotiation. (Guerin-Calvert, Tr. 7440).

268. An MCO can obtain leverage against a hospital in negotiations by threatening to enter into an exclusive arrangement with a competing hospital. (Radzialowski, Tr. 659-660).

269. Narrower hospital networks, *i.e.*, networks that exclude certain hospitals, drive more volume to the hospitals remaining in-network, which increases the network's value to those remaining hospitals, and typically results in the MCO obtaining more favorable reimbursement terms from the hospitals in exchange for that increased volume. (Radzialowski, Tr. 657-658).

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270. A narrower network can be more valuable to a participating hospital than a broader network, because the hospital in the narrower network would get more patients from that MCO. (Town, Tr. 4108). As a result, a hospital and an MCO may agree to lower reimbursement rates for a narrower network than for a broader network. (Town, Tr. 4109; Radzialowski, Tr. 657-658). Conversely, if an MCO goes from a narrow network to a broad network, the network becomes less valuable to the in-network hospitals, making those in-network hospitals less willing to agree to a lower price or discount. (Town, Tr. 4111-4112).

271. The more employer groups an MCO has, the more bargaining leverage it has because the members represent the potential revenue stream to the hospital. (Radzialowski, Tr. 659-660; Pirc, Tr. 2209; Pugliese, Tr. 1459 “The amount of business that [Anthem’s] customers are currently giving [the hospital] in terms of the flow of revenue from Anthem . . . is very important and critical.”). A national brand name also enhances an MCOs bargaining leverage. (Radzialowski, Tr. 659-660)

272. The more patient volume that a hospital stands to lose if it fails to reach an agreement with the MCO, the greater the bargaining leverage the MCO will have with the hospital. (PX02148 at 016-017 (¶ 28) (Town Expert Report), *in camera*; PX02072 at 002-003 (¶ 9) (Firmstone, Decl.), *in camera*; see Radzialowski, Tr. 661-662).

273. In building a hospital network, MCOs seek to offer a full complement of GAC inpatient services, which includes access to higher level secondary, tertiary and quaternary services within the network. (Radzialowski, Tr. 655-656; Sandusky, Tr. 1400-1401).

274. MCOs require at least one hospital in the network that offers advanced services, including tertiary services, but the network need not include more than one such hospital. (Sandusky, Tr. 1401; Radzialowski, Tr. 599-600, 656-657, 743).

275. Hospital networks that include all hospitals in a given area may be more costly than narrower networks that do not

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include as many hospitals. (Radzialowski, Tr. 657-658; McGinty, Tr. 1262).

276. MCOs must balance their customers' preferences for broad networks against the associated higher reimbursement costs the MCO will have to pay the providers, and the resulting effect on their plans' competitiveness to employers. (Radzialowski, Tr. 657-658).

277. In deciding whether to add a hospital to its network, an MCO balances the value its current and prospective members place on having in-network access to the hospital – and the resulting increase in the marketability of the MCOs network – against the costs, in terms of reimbursements rates, of adding that hospital to the network. (Pirc, Tr. 2167-2169, 2208-2211; *see* Radzialowski, Tr. 655-658; *see also* PX02148 at 013 (¶ 20) (Town Expert Report), *in camera*).

278. MCOs seek to offer marketable plans to employers, in terms of cost, geographical coverage, quality, and breadth of services, while at the same time staying competitive by, among other things, obtaining low reimbursement rates. (Pirc, Tr. 2284; Pugliese, Tr. 1455; Radzialowski, Tr. 583, 588-589, 595, 600, 652-654; McGinty, Tr. 1172-1173).

279. Marketability of a hospital network refers to the attractiveness of the network to consumers and the willingness of the consumers to purchase it. (Radzialowski, Tr. 589).

280. MCOs use general market knowledge, feedback from the field, and/or claims utilization data to determine the attractiveness and marketability of their offerings. (Pirc, Tr. 2178-2180; Radzialowski, Tr. 588-590; PX01914 at 014-015 (Pirc, IHT at 49-51).

281. MCOs believe that that Lucas County employers prefer a network with access to a broad provider network. (Radzialowski, Tr. 657; Pugliese, Tr. 1449; Pirc, Tr. 2281; Sheridan, Tr. 6680-6681; Town, Tr. 3617-3618, 3628; PX02148 at 013 (¶ 20) (Town Expert Report), *in camera*).

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282. MCOs believe that patients prefer to have open access to a broad network of hospitals and physicians. (Pugliese, Tr. 1544; Pirc, Tr. 2281).

283. MCOs believe that patients generally prefer to obtain basic or routine inpatient care in a hospital that is close to them. (Randolph, Tr. 7102, *in camera*; Pugliese, Tr. 1450; Sheridan, Tr. 6680-6681; Pirc, 2297). For certain services, such as tertiary services, patients are willing to travel further. (Radzialowski, Tr. 633-634).

284. MMO has not performed any market study regarding how far its members are willing to travel for GAC inpatient services, including any study of where expectant mothers went to deliver their babies in Lucas County. (Pirc, Tr. 2297-2298).

285. Anthem has not performed any analysis in Lucas County regarding how far Anthem's insureds will travel for GAC inpatient services, and Anthem has not studied where its insureds in Lucas County obtain GAC inpatient services relative to where those persons actually live. (Pugliese, Tr. 1563).

286. MCOs believe that employers and consumers want affordable plans, broad access provider networks that include all of the major facilities, a complement of physicians, and personal benefit designs that meet their needs. (Pugliese, Tr. 1449; Sandusky, Tr. 1315-1316).

287. MCOs estimate what it would cost to have a network without a particular hospital, *i.e.*, how much business would the MCO lose. "Some customers adapt. They'll work around it, and cost is more important. But other customers would not adapt." (Radzialowski, Tr. 665-666).

288. The reimbursement rates and other terms an MCO will agree to are based primarily on whether the MCO believes it can still sell its plans without that hospital in its network, and what losses the MCO would incur if the hospital were out of network. (Pirc, Tr. 2208).

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289. The degree of harm to the marketability of an MCO's provider network from omitting a hospital will depend on whether that MCO's main competitors offer broad or narrow hospital networks. (See PX01944 at 025 (Pirc, Dep. at 94-95), *in camera*). The marketability of the MCO's product will suffer more from omitting a hospital if the MCO's competitors market broad hospital networks than if the MCO's competitors market restricted hospital networks. (See PX01944 at 025 (Pirc, Dep. at 94-95), *in camera*).

4. Hospitals

290. Hospitals in and around Lucas County seek to maximize the reimbursement they receive from MCOs. Hospitals seek to cover their total cost of patient care, which tends to increase over time, and yield an operating margin to fund capital expenditures, expansion, and maintain a strong balance sheet. (Gold, Tr. 209-210, 265-266, 268; Korducki, Tr. 539, 547-549, 554; Beck, Tr. 432, 434; Shook, Tr. 950, 1050).

291. There is no difference in the way that for-profit and nonprofit hospitals negotiate with MCOs. (Radzialowski, Tr. 670; Sandusky, Tr. 1330; McGinty, Tr. 1239; Pugliese, Tr. 1462-1463; Pirc, Tr. 2212-2213; Sheridan, Tr. 6684). Both for-profit and nonprofit hospitals have a margin of revenue that they need and aim to achieve and they attempt to maximize commercial reimbursement rates to the full extent that their bargaining leverage will allow. (Pugliese, Tr. 1462-1463; Pirc, Tr. 2212-2213; Radzialowski, Tr. 670, 740; Sandusky, Tr. 1330; McGinty Tr. 1185-1186; Sheridan, Tr. 6684-6685; PX01900 at 010-011 (Mullins, IHT at 34-35, 37), *in camera*).

292. In addition to the reimbursement goals described in F. 290, because Medicare and Medicaid reimbursements do not cover the costs of providing the hospital services to Medicare and Medicaid patients, (*see* F. 518 (89 to 90 percent); Wachsman, Tr. 4848; Guerin-Calvert, Tr. 7299; RX71(A) at 000128, 000133, *in camera*), hospitals seek to make up the shortfall from Medicare and Medicaid reimbursements with payments from MCOs. (Guerin-Calvert, Tr. 7304, 7935-7936; Wachsman, Tr. 4848).

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293. The greater a hospital's bargaining leverage, the higher, generally speaking, the reimbursement rates will be. (Pirc, Tr. 2211).

294. If an MCO's network is substantially less attractive or less marketable to employers due to the exclusion of a hospital, that hospital will be able to command higher rates for its inclusion in the MCO's network than a less-valued hospital. (PX02148 at 016 (¶ 27), (Town Expert Report), *in camera*; Town, Tr. 3640-3643, 3806, *in camera*; Pirc, Tr. 2209-2211).

295. The more valued the hospital system is by the MCO's members, the more important the system is to the MCO's ability to market its network, and the more bargaining leverage the hospital system will possess in contract negotiations with the MCO. (Sandusky, Tr. 1348-1349, *in camera*; Pirc, Tr. 2168-2169, 2210; *see also* PX02148 at 016 (¶ 27) (Town Expert Report), *in camera*; Town, Tr. 3641-3643).

296. Factors that increase a hospital's bargaining position, vis-a-vis an MCO, are member preferences, a broad geographic distribution of facilities, broad services lines, and a large number of physicians that the hospital employs and controls. (Lortz, Tr. 1700-1701, Pirc, Tr. 2189, 2210; Pugliese, Tr. 1458-1461).

297. A hospital's location in Lucas County is an important factor in contract negotiations, particularly if there are no alternatives in that location. (Radzialowski, Tr. 663 ("hospital's leverage comes from the geographic location, which is where they are situated, whether or not they have any competitors nearby"); Pirc, Tr. 2199 ("if there's no alternative, [location within the county] increases a hospital's leverage"); Pugliese, Tr. 1451-1452, 1459).

298. The more hospitals that a system controls, the more bargaining leverage it has. This is because failure to reach an agreement results in more hospitals leaving the network, which decreases the marketability of the MCOs, and results in greater potential loss of business. (Pirc, Tr. 2210; Radzialowski, Tr. 663).

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J. The Relevant Market

1. Relevant product market

a. General acute-care inpatient hospital services

299. The relevant product market is all general acute-care (“GAC”) inpatient hospital services – primary, secondary, and tertiary services – sold to commercial health plans.

F. 300-311; Joint Stipulations of Law and Fact, JX00002A ¶ 3; Response to RFA at ¶ 1; Answer ¶ 12). *See* F. 20-26 for definitions of primary, secondary, tertiary.

300. GAC inpatient services are a broad “cluster market” of inpatient surgical, medical, and supporting services provided in a hospital setting to commercially insured patients. (PX02148 at 021-023 (¶¶ 38, 40) (Town Expert Report), *in camera*); *see* Gold, Tr. 195; Korducki, Tr. 481-482).

301. All GAC inpatient services in the cluster market use the same assets, the same operating rooms, the same beds, the same wards, the same nursing staff, and all require an overnight stay. (Guerin-Calvert, Tr. 7188, 7191).

302. Individual services within the GAC cluster market are not clinical substitutes for each other. (Guerin-Calvert, Tr. 7631-7632; Town, Tr. 3665).

303. In using a cluster market approach, the demand that is analyzed is the demand for a set of services and skills. (Guerin-Calvert, Tr. 7190).

304. MCOs demand, and contract for, a broad array of inpatient services together, such as medical-surgical care. (Guerin-Calvert, Tr. 7190; Town, Tr. 3686-3687).

305. When MCOs contract with hospitals, they do not distinguish between services available to commercially insured patients and government insured patients; they look at all services available at that hospital to any patient. (Guerin-Calvert, Tr. 7202).

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306. The parties agree that the following are excluded from the relevant market: outpatient services, quaternary services, rehabilitation, skilled care, psychiatric care, detoxification services, and Major Diagnostic Category (“MDC”) Codes 2, 19, 20, and 17. (RPF 1013-1016; CCRPF 1013-1016; Guerin-Calvert, Tr. 7191-7192, 7195; Town 3686-3687).

307. The GAC market excludes outpatient services (F. 32-35) because health plans and patients could not substitute outpatient services for inpatient care in response to a price increase. Such substitution is, instead, based on clinical considerations. (Answer ¶ 13; Response to RFA at ¶ 3; Guerin-Calvert, Tr. 7637; Radzialowski, Tr. 638-639; PX01914 at 007-008 (Pirc, IHT at 21-22); Town, Tr. 3669-3671).

308. It is also appropriate to exclude outpatient services from GAC services because they have different competitive conditions than inpatient services. For example, there may be a different set or mix of market competitors, not just hospitals. (Guerin-Calvert, Tr. at 7637, 7640; *see* Town, Tr. 3672-3673).

309. The GAC inpatient hospital services market excludes quaternary services because they are often excluded in MCOs’ contracts for GAC inpatient services or contracted for separately. (Guerin-Calvert, Tr. 7191-7192; F. 306 (parties agree that quaternary services are excluded)).

310. The GAC inpatient hospital services market excludes rehabilitation, skilled care, psychiatric care, and detoxification because these services are separately contracted and negotiated for and are sometimes provided as outpatient services. (Guerin-Calvert, Tr. 7195; Town, Tr. 3686-3687; F. 306 (parties agree that these services are excluded)).

311. The GAC inpatient hospital services market excludes MDC codes 2, 19, 20, and 17 from the relevant product market because these are codes for behavioral health services and have traditionally been excluded. (Guerin-Calvert, Tr. 7197;

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Town, Tr. 4211, 4221; F. 306 (parties agree that these services are excluded)).

b. Inpatient obstetrical hospital services

312. Inpatient obstetrical services are a cluster of procedures relating to pregnancy, labor, and post-delivery care provided to patients for the labor and delivery of newborns. (Response to RFA at ¶ 4; Marlowe, Tr. 2388, 2431-2432; Read, Tr. 5275).

313. No other hospital services are reasonably interchangeable with inpatient OB services. (Guerin-Calvert, Tr. 7667-7668; PX01935 at 005 (Read, Dep. at 11); PX02148 at 023-024 (¶ 41) (Town Expert Report), *in camera*; see Response to RFA at ¶ 4).

314. ProMedica and St. Luke's track separate market shares and other data for a variety of services, including inpatient OB services, cardiac cases, orthopedics, and cancer services. (Response to RFA at ¶ 5; PX01016 at 003, *in camera*; PX01077 at 003, 005; PX00009 at 022; PX01077 at 004).

315. Negotiations between hospital providers and MCOs cover the full range of inpatient services that the MCO's members may need, including inpatient OB services. (Pugliese, Tr. 1550; McGinty, Tr. 1240; Town, Tr. 4049-4050; Guerin-Calvert, Tr. 7229-7230; Randolph, Tr. 6960).

316. Contracts with some major MCOs in Lucas County do not separately carve out obstetric rates from the GAC inpatient care rates. (Pugliese, Tr. 1622, *in camera*; RX1886, *in camera*; RX1882, *in camera*; RX1890, *in camera*; RX1045, *in camera*; PX02385, *in camera*; PX02533, *in camera*; RX305; RX306, *in camera*; RX329, *in camera*).

317. Contracts with some major MCOs in Lucas County do separately carve out obstetric rates from the GAC inpatient care rates. (Radzialowski, Tr. 808, *in camera*; 752-753; Sheridan, Tr. 6662, *in camera*, 6683-6684; see, e.g., PX00365 at

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030 (ProMedica-United Contract), *in camera*; PX00363 at 019, 022 (ProMedica-Aetna Contract)).

318. To the extent that inpatient obstetrical rates are listed separately in some contracts, it is at the request of the MCOs rather than ProMedica. (Wachsman, Tr. 5158, *in camera*).

319. Hospitals have not price-discriminated for inpatient OB services and there is no basis on which hospitals could price-discriminate for inpatient OB services. (Guerin-Calvert, Tr. 7230).

320. Inpatient OB services are provided in conjunction with other services, and the terms and conditions on which they are negotiated are very similar. (Guerin-Calvert, Tr. 7230).

2. Relevant geographic market

a. Lucas County, Ohio

321. The relevant geographic market is Lucas County, Ohio. (F. 322-330; Town, Tr. 3688; PX02148 at 025-032 (¶¶ 45-55) (Town Expert Report), *in camera*; Response to RFA at ¶ 7; *see* PX00900 (Map of Northwest Ohio)).

322. Both Complaint Counsel's and Respondent's economic experts agree that the relevant geographic market is Lucas County, Ohio. (Guerin-Calvert, Tr. 7155; Town, Tr. 3688-3689, 4068-4069).

323. No MCO has marketed a health plan to Lucas County customers without including at least one Lucas County hospital. (Randolph, Tr. 7064-7065).

324. A hypothetical monopolist controlling every hospital in Lucas County could increase the price of GAC inpatient services in Lucas County by at least 5 to 10 percent, a small but significant amount. (Guerin-Calvert, Tr. 7681; PX01954 at 042-043 (Guerin-Calvert, Dep. at 164-165), *in camera*; Town, Tr.

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3688-3690; PX02148 at 016, 025-026, 029 (¶¶ 27, 45, 51) (Town Expert Report), *in camera*).

325. When ProMedica retained Navigant Consulting to perform a clinical integration study for ProMedica's Toledo-area hospitals, (*infra* F. 1026-1027) Navigant examined the geographic area in which ProMedica competed. (Nolan, Tr. 6253, 6275-6276, *in camera*; PX01216 at 004-008 (Navigant Service Line and Clinical Integration Market Trends and Facilities Assessment Aug. 2010), *in camera*). Navigant examined only Lucas County and excluded all hospitals located outside of Lucas County from its market share analysis. (Nolan, Tr. 6326-6327, *in camera*).

326. Patients have a preference for local care and close access to health-care providers. (Pirc, Tr. 2184; Pugliese, Tr. 1450-1451 (Anthem's Lucas County members "will stay closer to home for common services, preventative care services.")); Randolph, Tr. 7102; Rupley, Tr. 1962; Sandusky, Tr. 1306; Sheridan, Tr. 6681; Shook, Tr. 942; Town, Tr. 3694, 3759, *in camera*; *see also* PX01917 at 008 (Radzialowski, Dep. at 26-27), *in camera*).

327. With extremely rare exceptions, Lucas County residents do not use more distant providers of GAC inpatient services. (Sheridan, Tr. 6680-6682; Town, Tr. 3691; PX02148 at 026, 155-159 (¶ 46, Ex. 10) (Town Expert Report), *in camera*).

328. Patient flow data reveals that nearly all Lucas County residents (97.9 percent) stay within Lucas County for GAC inpatient services. (PX02148 at 026 (¶ 46) (Town Expert Report), *in camera*). In other words, only 2.1 percent of Lucas County residents leave the county for general acute-care services. (PX02148 at 026 (¶ 46) (Town Expert Report), *in camera*; *see also* Sheridan, Tr. 6682). "[P]atients residing in Lucas County have an obvious and strong preference for hospitals located within Lucas County." (PX02148 at 026 (¶ 46) (Town Expert Report), *in camera*).

329. The average travel time from home to hospital for Lucas County GAC patients is 11.5 minutes, with 50 percent of

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patients traveling less than 8.7 minutes. (Town, Tr. 3693-3694; PX02148 at 030, 140 (¶ 52, Ex. 5) (Town Expert Report), *in camera*). *Accord* (at 000032 (¶ 52) (Guerin-Calvert Expert Report), *in camera*) (the vast majority of patients travel less than 20 minutes for health-care services).

330. While travel time is important, patients usually rank availability of a service, access to a particular physician, and alignment of a patient's insurance company ahead of the geographic location of the hospital. (Wakeman, Tr. 2510; RX71(A) at 000021, n.22, *in camera*).

b. Non-Lucas County hospitals

331. The primary reason patients who live in Lucas County do not travel outside of Lucas County is distance. (Radzialowski, Tr. 649; Sheridan, Tr. 6681; *see also* Pirc, Tr. 2184; Pugliese, Tr. 1451; Andreshak, Tr. 1768).

332. Hospitals in counties adjacent to Lucas County are not acceptable alternatives for one MCO's Lucas County members. (Pugliese, Tr. 1451).

333. Wood County Hospital, located in Bowling Green, Ohio, is approximately 25 miles and 35 minutes from downtown Toledo. (Korducki, Tr. 475, 504-505; *see* PX00900 (Map of Northwest Ohio)).

334. Wood County Hospital routinely reviews Ohio Hospital Association data to track patient flow. (Korducki, Tr. 469-470). Wood County Hospital primarily serves the area south of Route 582 in Wood County, southward to the bottom of Wood County, and westward into the eastern half of Henry County. (Korducki, Tr. 506, 508-509).

335. Eighty-one percent of Wood County Hospital's patient admissions are from ten contiguous zip codes in this area. (Korducki, Tr. 506). There are no Lucas County zip codes included in this area. (Korducki, Tr. 509).

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336. Wood County Hospital has approximately 3,600 to 3,700 patient admissions per year. (Korducki, Tr. 511). In each of the last two years, approximately 100 Lucas County residents have sought inpatient hospital services at Wood County Hospital. (Korducki, Tr. 510-511). In other words, approximately 2.7 percent of Wood County Hospital's inpatient admissions are of Lucas County residents. (See Korducki, Tr. 510-511). Some of these Lucas County residents are coming to Wood County Hospital for bariatric services, for which Wood County Hospital is the only hospital in northwest Ohio that is a Center of Excellence. (Korducki, Tr. 511-512).

337. Fulton County Health Center is approximately 30 miles and a 45 minute drive from St. Luke's. (Beck, Tr. 384-385; see PX00900 (map of northwest Ohio)).

338. Fulton County Health Center looks at data provided by the Ohio Hospital Association to track patient flow. (Beck, Tr. 386-388). Most of Fulton County Health Center's patients come from the area around the hospital in Fulton County. (Beck, Tr. 388).

339. Patients in Lucas County do not come to Fulton County Health Center for GAC inpatient services. (Beck, Tr. 389; 392-393 ("there's sufficient health care in Lucas County that there's no need to come to [Fulton County Health Center]")).

340. St. Luke's did not view Wood County Hospital or Fulton County Health Center as significant competitors. (PX01933 at 047 (Oppenlander, Dep. at 178-179), *in camera*).

341. Wood County Hospital and Fulton County Health Center do not compete with Lucas County hospitals for GAC inpatient services, including obstetrical services. (Pirc, Tr. 2191-2193; Radzialowski, Tr. 648-651; Sandusky, Tr. 1315).

K. Market Shares and Concentration

1. Framework for evaluating market shares

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a. Markets used for generating statistics

342. The expert witnesses proffered by the parties (hereafter, “experts,” (Town, for Complaint Counsel and Guerin-Calvert, for Respondent)) utilized different parameters of the product market in calculating market shares. Complaint Counsel’s expert calculated market shares based on a market of only those GAC inpatient services (identified as “diagnostic related groups” or “DRGs” that both ProMedica and St. Luke’s sold to MCOs. (PX02148 at 019-021). Respondent’s expert included all GAC inpatient services in her market share calculations. (RX71(A) at 000161; Guerin-Calvert, Tr. 7726-7727).

343. The experts treated OB services differently in calculating market shares. Complaint Counsel’s expert’s calculation of market share for GAC inpatient services excluded market shares of inpatient OB services. Instead, Complaint Counsel’s expert calculated market shares of OB services only as a separate market. (PX02150 at 001). Respondent’s expert’s calculations of market shares for GAC inpatient services included inpatient OB services. (RX71(A) at 000161-000165).

b. Methodology

344. The experts utilized different methodologies in calculating market shares. Complaint Counsel’s expert calculated market shares based on total patient days. (PX02148 at 034 n.97). Respondent’s expert calculated market shares based on billed charges and discharges. (RX71(A) at 000036-000037, 000162-000163). In addition, Respondent calculated shares based on staffed beds and registered beds. (RPFF 1051-53).

345. Market shares can be accurately based on number of discharges, billing charges, revenue, or patient days. No matter which one is selected, the calculated market shares “would be unaffected.” (Town, Tr. 3701-3702, 3709-3710).

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346. Patient days, which measure how long a patient stays in the hospital, take the acuity of the illness or procedure that a patient has into account. (Town, Tr. 3701).

347. Billed charges are the summation of the retail or list price of hospital services sold to patients. Billed charges may not give the most accurate view of the marketplace, because commercial insurers pay discounted prices for services, not the full chargemaster price. (Town, Tr. 3707-3708; Korducki, Tr. 534-535; Pugliese, Tr. 1507, *in camera*; McGinty, Tr. 1195-1196; Sandusky, Tr. 1346-1347, *in camera*). See F. 499 for definition of chargemaster.

348. Discharges measure the number of patients that were admitted and discharged. (Town, Tr. 3701).

c. HHI calculations

349. The U.S. Department of Justice and the Federal Trade Commission utilize the Herfindahl-Hirschman Index (“HHI”) to measure market concentration. (Answer ¶ 22).

350. The HHI is calculated by summing the squares of the market shares of all firms in the market. A transaction that increases concentration by 200 points or more and results in a highly-concentrated market (HHI over 2,500) is presumed likely to enhance market power. (Town, Tr. 3696-3699; Merger Guidelines § 5.3).

351. Complaint Counsel’s expert calculated HHIs for two product markets: GAC inpatient services, exclusive of OB services; and inpatient OB services. (PX02148 at 021-025; PX02150 at 001).

352. Respondent’s expert did not calculate HHIs for any of the proposed product markets in this case. (Guerin-Calvert, Tr. 7723).

353. Respondent’s expert admits that the appropriate starting point in merger analysis involves calculating market shares and HHI concentration indices and that she has calculated

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HHIs in previous merger matters where she has testified as an expert. (Guerin-Calvert, Tr. 7718-7721; PX01925 at 005 (Guerin-Calvert, Dep. at 11)).

2. Calculation of market shares

a. Beds

354. The hospitals' shares of registered beds in 2009 are as follows: ProMedica hospitals, 34.3%; St. Luke's, 9.4 %; Mercy, 32.5%; and UTMC, 9.6%. (PX02123 at 025).⁴

355. The hospitals' shares of staffed beds (less non acute-care beds) in 2009 are as follows: ProMedica hospitals, 39.4%; St. Luke's, 8.4%; Mercy, 31.7% and UTMC, 8.9%. (PX02123 at 025).

356. Before and after the Joinder, ProMedica's market share is higher than its competitors in Lucas County, whether calculated by registered beds, beds-in-use, or occupancy. (Joint Stipulations of Law and Fact, JX00002A ¶ 17).

b. Billed charges

357. Based on billed charges, Respondent's expert calculated market shares of Lucas County GAC inpatient services, inclusive of inpatient OB services in 2009 as follows: ProMedica, 46%; St. Luke's, 7%; Mercy, 35%, and UTMC, 10%. Combined, ProMedica and St. Luke's have a 53% share, which is higher than the 45% share of Mercy and UTMC combined. (RX71(A) at 000162, *in camera*; see also RPF 1056).⁵

⁴ The shares of ProMedica, St. Luke's, Mercy and UTMC set forth in F. 354-355 do not add up to 100% because Respondent's expert also included shares from Fulton County Health Center, Fremont Memorial Hospital, HB Magruder Memorial Hospital, and Wood County Hospital. See PX02123 at 025.

⁵ The shares of ProMedica, St. Luke's, Mercy and UTMC set forth in F. 357-358 do not add up to 100% because Respondent's expert also included shares from Wood, Michigan, and the Cleveland Clinic. See RX71(A) at 000162, 00165.

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358. Based on billed charges, Respondent's expert calculated market shares of Lucas County "commercial discharges" for "GAC + non-GAC + OB +non-OB" in 2009 as follows: ProMedica, 49%; St. Luke's, 5%; Mercy, 33%; and UTMC, 9%. Combined, ProMedica and St. Luke's have a 54% share, which is higher than the 42% share of Mercy and UTMC combined. (RX71(A) at 000165, *in camera*).

c. Discharges

359. Based on discharges, Respondent's expert calculated market shares of Lucas County GAC inpatient services, inclusive of inpatient OB services, in 2009 as follows: ProMedica, 42%; St. Luke's, 12%; Mercy, 32%; UTMC, 11%. Combined, ProMedica and St. Luke's have a 54% share, which is higher than the 43% share of Mercy and UTMC combined. (RX71(A) at 000162, *in camera*).

360. Based on discharges, Respondent's expert calculated market shares of Lucas County "commercial discharges" for "GAC + non-GAC + OB +non-OB" in 2009 as follows: ProMedica 48%; St. Luke's, 10%; Mercy, 29%; UTMC, 9%. Combined, ProMedica and St. Luke's have a 58% share, which is higher than the 38% share of Mercy and UTMC combined. (RX71(A) at 000165, *in camera*).

361. Internal documents prepared by St. Luke's indicate the following GAC market shares, based on discharges of ProMedica and St. Luke's combined: 67%⁶ (2008, SLH Core Service Area); 50.3%⁷ (2007, SLH Primary Service Area); 53.6% (2009, SLH 80% Primary Service Area); and 68.4% (2009, SLH Core Service Area). (PX01016 at 003, *in camera*; PX01077 at 006; PX01236 at 002; and (PX01235 at 003).

362. St. Luke's defines its core service area as the eight zip codes surrounding St. Luke's, where 55-60 percent of the

⁶ These statistics include only St. Luke's, TTH, and Flower, and do not include ProMedica's Bay Park, market shares.

⁷ *Ibid.*

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admission base comes from, and defines its primary service area as where approximately 80 percent of St. Luke's patients come from. (Rupley, Tr. 1944, 1949; PX01077 at 008; PX01418 at 005; PX01077 at 008).

363. An internal document prepared by ProMedica in its 2008 Presentation to Standard & Poor's indicates that ProMedica's market share of the Toledo Metropolitan Statistical Area, in 2006, based on discharges, was 45%, while St. Luke's was 10%. (PX00270 at 025).

d. Patient days

364. Based on patient days, Complaint Counsel's expert calculated market shares of Lucas County GAC inpatient services, exclusive of OB services pre-acquisition, as follows: ProMedica, 46.8%; St. Luke's, 11.5%; Mercy, 28.7%; UTMC, 13%. Post-acquisition, ProMedica has a 58.3% market share. (PX02148 at 143 (Town Expert Report, Ex. 6, *in camera*); see also PX02150 at 001-002 (market share chart)).

365. The market shares calculated by Complaint Counsel's expert do not change materially if tertiary and quaternary services are included. (Town, Tr. 3714-3715; Guerin-Calvert, Tr. 7694-7695).

366. The market shares calculated by Complaint Counsel's expert do not change materially if Wood County Hospital and Fulton County Health Center are included. (Town, Tr. 3711-3712).

367. Using Complaint Counsel's expert's calculations in F. 364, ProMedica's market share is 60% higher than Mercy's for GAC inpatient services. (PX02148 at 036 (¶ 66) (Town Expert Report, *in camera*)). UTMC's 13% market share is less than one-third of ProMedica's market share. (See PX02148 at 143 (Town Expert Report, Ex. 6, *in camera*); PX02150 at 001 (Market share chart)).

368. Based on the market definition and shares in F. 342-343 and 364, Complaint Counsel's expert calculated HHIs

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and concluded that the pre-acquisition HHI was 3312; the change in the HHI was 1078.2, well above the 200 point threshold of the Merger Guidelines; and the resulting post-acquisition HHI is 4391, well above the 2500 threshold to be considered “highly concentrated.” PX02148 at 034 (¶ 61), 143 (Exhibit 6) (Town Expert Report), *in camera*; PX02150 at 001; Town, Tr. 3703-3704).

3. Conclusion

369. Respondent’s expert conceded that, using her relevant market definition (F. 342-343), the pre-HHI meets the Merger Guidelines’ presumption of a highly concentrated market and that the post-HHI would be around 4000. (Guerin-Calvert, Tr. 7730).

370. Regardless of which methodology or market parameter is used, the Joinder significantly increases concentration in the already highly-concentrated Lucas County GAC inpatient services market. (Town, Tr. 3702-3705).

L. Background Facts Regarding St. Luke’s Joinder with ProMedica

371. St. Luke’s was struggling financially in the years preceding the Joinder. (Part II.N., *infra*).

372. St. Luke’s had an operating loss of [redacted] million in 2007, [redacted] million in 2008, and [redacted] million in 2009. This amounted to operating margins of [redacted] percent in 2007, [redacted] percent in 2008, and [redacted] percent in 2009. (RX56 at 000006 (Table 1), *in camera*).

373. The overall cost coverage ratio for St. Luke’s, including MCOs, government payors, and self-pay, was [redacted]. (RX56 at 000010).

374. The cost coverage ratio for St. Luke’s, including only Anthem and MMO, which combined represent approximately [redacted] percent of St. Luke’s total revenue, was [redacted]. (RX56 at 000010, *in camera*).

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375. The cost coverage ratio for St. Luke's, including only Medicare and Medicaid, which represent approximately [redacted] percent of St. Luke's total revenue, was [redacted]. (RX56 at 000010, *in camera*).

376. In the first eight months of 2010, St. Luke's contract reimbursement rates with commercial payors, other than [redacted], exceeded its costs. (Dagen, Tr. 3239-3240, *in camera*; PX00512 at 001 (Aug. 2010 year-to-date payor cost ratio spreadsheet), *in camera*). In 2009, St. Luke's contract reimbursement rates with commercial payors exceeded its costs, except for [redacted] and [redacted]. PX00519 at 001, *in camera*).

377. The cost coverage ratio figures set forth in F. 373-375 indicate that St. Luke's payments, overall, were not covering St. Luke's total costs and were generating losses. (Den Uyl, Tr. 6440-6443, *in camera*).

378. St. Luke's unrestricted reserves decreased from [redacted] million at the end of 2007 to [redacted] at the end of 2009. (RX56 at 000016 (Table 9), *in camera*).

379. From the end of 2007 through the Joinder St. Luke's was using the reserve fund to fund losses and the capital commitments it needed. (Den Uyl, Tr. 6460, *in camera*).

380. Members of St. Luke's Board of Directors (hereafter, the "Board") were concerned about the use of cash reserves, although Mr. Wakeman estimated on March 31, 2010 that St. Luke's had "only accessed the reserves for about [redacted] million [in] the past 24 months to pay for part of the pension shortfall requirements and the new tax. That has been offset by gains of almost [redacted] million in the market in the past year." (PX00923 at 001, *in camera*).

381. "EBITDA" stands for earnings before interest, taxes, depreciation, and amortization. (Den Uyl, Tr. 6424-6425).

382. St. Luke's EBITDA margin was [redacted] percent in 2007, [redacted] percent in 2008, and [redacted] percent in 2009.

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The average EBITDA margin of comparably rated hospitals was 9.6 percent in 2007, 7.7 percent in 2008, and 8.1 percent in 2009. (Den Uyl, Tr. 6425; RX56 at 000006-000007 (Tables 3 and 4), *in camera*).

383. St. Luke's investment portfolio cash reserves earned [redacted] percent on its reserve fund over the ten year period ending December 31, 2009. (RX56 at 000041 (¶ 97), *in camera*).

384. St. Luke's investment portfolio cash reserves lost [redacted] percent on its reserve fund over the three year period ending December 31, 2009. (RX56 at 000041 (¶ 97), *in camera*).

385. For the period of 2005 through 2008, St. Luke's capital expenditures were over [redacted] million per year. Because cash reserves were declining, in 2009 St. Luke's reduced its capital expenditures in 2009, to about [redacted] million, in order to preserve liquidity. (Den Uyl, Tr. 6461, *in camera*).

386. An August 10, 2009 document, prepared for St. Luke's Hospital ("SLH") Board of Directors ("Board") by St. Luke's senior leadership and entitled "Framing the SLH Strategy Discussion for Dan Wakeman and the Board" ("Strategy Discussion" document), posed the question, "What led us to where we are at today?" Answering that question, the document states: "exclusive managed care networks and a decrease in SLH core physicians (and perhaps and aging facility)" had caused a volume problem for St. Luke's and that this volume problem "caused St. Luke's to be a taker in managed care negotiations, not a setter [of rates]." (PX01390 at 001), *in camera*; Wakeman, Tr. 2640, 2643, *in camera*).

387. The Strategy Discussion document identified in F. 386 states that through advertising and increasing physicians, St. Luke's had been able to increase its volume, but that "due to a lack of negotiating power with managed care companies we are now straddled with significantly low reimbursement rates as set forth in our managed care contracts." (PX01390 at 002 (¶ 5), *in camera*).

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388. In August 2009, St. Luke's key strategic issue in the near term was identified as "extremely low reimbursement rates from third party payors." (PX01390 at 002 (¶ 6), *in camera*).

389. In August 2009, St. Luke's had two options in the short term: "(1) St. Luke's develops a compelling argument to increase contracted rates with its major managed care customers (MMOH, Anthem, Aetna, etc.) as an independent. (2) St. Luke's enters into an affiliation/partnership with a local health system with the express purpose to raise reimbursement rates to the level of our competitors. This affiliation may be as simple a partnering on clinical service lines or one that is more fully integrated. (PX01390 at 002, *in camera*; Wakeman, Tr. 2640, 2643, *in camera*).

390. In August or September 2009, a presentation was given to the Board, prepared by St. Luke's senior leadership and entitled "Options for St. Luke's – St. Luke's is now at a crossroads" ("Options Presentation"). (PX01018 at 001, *in camera*; Wakeman, Tr. 2655-2656, *in camera*).

391. The Options Presentation advised the Board that "St. Luke's is being grossly underpaid. St. Luke's has tried to gain revenue through volume. Even though volume has increased due to strategic initiatives, [it] has not been enough to offset costs and still have acceptable margin." (PX01018 at 003, *in camera*).

392. The Options Presentation advised the Board that: "There is no perfect option. Going it alone is extremely challenging. In respect to collaboration, some organizations are a better fit culturally (along with mission); others are a better fit strategically/ financially." (PX01018 at 007, *in camera*).

393. The Options Presentation described St. Luke's first option as: "Remain independent. Surgically remove all financially losing services/ programs until accepted margin is realized." With respect to this option, the Options Presentation noted that St. Luke's was already the low cost provider in the area, and further cuts would be "very painful," including "cut[ting] major services and programs (downsizing), not just rightsizing." St. Luke's would become a "limited" provider and

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no longer able to fulfill its mission of fully serving the community. (PX01018 at 008, *in camera*; PX01283 at 002 (noting that major reductions to get St. Luke's to "break even will have to come from massive program reduction, like stop hearts, OB and implants").

394. The Options Presentation identified a second option for St. Luke's as: "Push the payors. Provide compelling argument to raise SLH reimbursement rates to an acceptable margin. In essence, the message would be pay us now (a little bit more) or pay us later (at the other hospital system contractual rates)." With regard to this option of getting increased reimbursement rates, the Board was advised that St. Luke's needed to be "prepared to fall back on a 'collaborating partner strategy.'" (PX01018 at 009, *in camera*).

395. The Options Presentation identified three additional options, involving affiliation with either ProMedica, Mercy or UTMC. (PX01018 at 014-017).

396. With regard to the option of affiliating with ProMedica, the Options Presentation advised the Board that ProMedica would bring, among other things, strong managed care contracts, a "huge" cash inflow, directly, and indirectly through inclusion in Paramount network; likelihood of upgrade to St. Luke's campus; improved information technology ("IT") systems; a good history of execution; and a greater likelihood of local control, due to ProMedica's system being regionally owned and controlled. (PX01018 at 014, *in camera*).

397. As stated in the Options Presentation, the option of affiliating with Mercy would bring, among other things, a mission that was "in line" with St. Luke's mission, high quality, some upgrading of St. Luke's campus, and some cash inflow, although not as much as St. Luke's believed ProMedica would supply. The document also noted a history of inconsistent execution and that local control would be less, due to the system being governed out of Cincinnati. (PX01018 at 015, *in camera*).

398. With regard to the option of affiliating with UTMC, the Options Presentation noted that St. Luke's and UTMC were

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“already down the path as to what an affiliation might look like.” (PX01018 at 016, *in camera*). UTMC began exploring an affiliation with St. Luke’s in late 2008, and signed a non-exclusive Memorandum of Understanding in April 2009. (PX02203 at 001; Wakeman, Tr. 2857; Gold, Tr. 224-225, 239).

399. Factors relating to the option of affiliating with UTMC included: the largest and most stable employer in the area, with state of Ohio backing; a source of physicians and other health professionals; with 4 of 8 board members to be representatives from St. Luke’s/OhioCare, the “[o]ppportunity for this new Board to truly govern the medical facilities on both campuses”; and UTMC’s “low patient satisfaction with academic/union corporate culture,” and whether an affiliation with UTMC would give St. Luke’s “enough managed care clout.” (PX01018 at 016-017, *in camera*).

400. The Options Presentation identified 8 factors for determining an acceptable partner: (1) cultural compatibility; (2) capital access; (3) expense management; (4) affordable physician strategy; (5) vision for competitive community services (especially at the St. Luke’s campus); (6) projected risk and opportunity in a “reformed” health-care market (such as limited dependence on insurance products); (7) advantages over “go it alone” / other partner options (such as “multi-market”); (8) do-able (legal, regulatory considerations); (9) quality; and (10) impact on community. (PX01018 at 021, *in camera*).

401. The Board determined not to undertake service cuts. Potential service cuts as an option for going forward were not “a major topic of discussion” because the idea was distasteful to the Board. (Black, Tr. 5703-5704).

402. An October 30, 2009 update regarding St. Luke’s affiliation options, entitled “Affiliation Analysis Update, St. Luke’s Board of Directors” (the “October 2009 Affiliation Update”) identified 13 factors for determining an acceptable partner: (1) cultural compatibility; (2) overall effect on employees; (3) governance; (4) capital access; (5) expense management; (6) revenue / reimbursement enhancement; (7) effective physician strategy; (8) vision for competitive community

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services (especially at the St. Luke's campus); (9) projected risk and opportunity in a "reformed" health-care market (such as limited dependence on insurance products); (10) advantages over "go it alone" / other partner options (such as "multi-market"); (11) do-able (legal, regulatory considerations); (12) quality; and (13) impact on community. (PX01030 at 007, *in camera*; Wakeman, Tr. 2959-2960, *in camera*; Black, Tr. 5634-5635, *in camera*).

403. All of the factors identified in F. 402 were important to the Board, and the ranking reflected the overall opinion of the Board as to the relative importance of each factor. (Black, Tr. 5635, *in camera*).

404. The October 2009 Affiliation Update summarized the various ongoing affiliation discussions with Mercy, UTMC and ProMedica. Preliminary discussions with Board leadership of hospital systems began prior to August 2008. Discussions began with regard to a joint venture with Mercy in August 2008. Discussions with UTMC began in February 2009, with respect to a shared governance model. Discussions began with ProMedica upon signing a non-exclusive, confidentiality agreement in July 2009. (PX01030 at 002-006, *in camera*).

405. The October 2009 Affiliation Update evaluated in considerable detail the advantages and disadvantages of an affiliation with each Mercy, UTMC and ProMedica, applying each of the 13 factors noted in F. 402. (PX01030 at 015-017, *in camera*).

406. By October 2009, Mr. Wakeman seriously questioned whether it would "really make sense for our best ability to service this community long term to stay independent" given St. Luke's "very disappointing" financial performance, health-care reform requirements, capital demands, difficulty with recruitment, below market compensation, and a plant that needed updating. (PX01283 at 002, *in camera*; Wakeman, Tr. 2949-2950, *in camera*).

407. At a November 4, 2009 Board meeting, St. Luke's Board directed management to "vigorously pursue specific service line joint ventures with provider systems in the community." (Wakeman, Tr. 2965-2966, *in camera*).

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408. St. Luke's CEO, Mr. Wakeman, did not agree with the Board's approach on November 4, 2009, as he believed it was not sufficiently focused to resolve St. Luke's serious financial problems. He believed that the November 4 board meeting "was an example of how large boards have an arduous time making difficult decisions. They are struggling with losses of \$2 million a month and holding onto independence." (RX880 at 000001; Wakeman, Tr. 2967, *in camera*).

409. The Board received another update on affiliation at a Board meeting on December 15, 2009. (PX01016 at 001, *in camera*) (the "December 2009 Affiliation Update").

410. The December 2009 Affiliation Update included updates on certain of St. Luke's financial metrics, such as net patient care revenue and operating expenses, which indicated that, while both had increased since 2007, operating expenses were still exceeding net patient care revenue. A detailed analysis of cost and revenue per case further showed that in 2008, St. Luke's cost per case exceeded net revenue, and that St. Luke's was the only hospital in the area where this was true. (PX01016 at 002, 008, *in camera*).

411. The December 2009 Affiliation Update also reported certain corrective actions St. Luke's had implemented, including its readmission to Anthem's network as of July 2009. (PX01016 at 005).

412. The December 2009 Affiliation Update reports that despite positive results in a variety of areas, "[t]he Bottom Line is...We have a major insurance/managed care payment issue." (PX01016 at 008, *in camera*).

413. As part of the December 2009 Affiliation Update, St. Luke's management presented St. Luke's Average Payor Rates Compared to Market Median, which concluded that St. Luke's managed care contracts yielded a weighted average of [redacted] percent below the Toledo market median for inpatient services. The overall rates from MMO, St. Luke's largest payor, were noted to be approximately [redacted] percent below the Toledo market

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median. When evaluated by service line, it was determined that, as to St. Luke's top 8 commercial payors, the more high-end commercial services St. Luke's performed, the more money it lost. (PX01016 at 010-011, *in camera*)).

414. As part of the December 2009 Affiliation Update, St. Luke's management presented the following "pressing concerns" to St. Luke's Board: Debt service coverage ratio: in non-compliance; IT upgrade: [redacted] million net dollars (without operational expenses); Moody's Investors Service, Inc. ("Moody's") possible bond downgrade; SLH employee pay rates falling behind; Building upgrades: SLH average age of plant ratio nearly [redacted] well over the 75th percentile benchmark; defined benefit pension funding / expense; New state of Ohio hospital tax; continued increase in bad debt/charity care; and impending health-care reform. (PX01016 at 014, *in camera*; Wakeman, Tr. 2992, *in camera*).

415. At the end of 2009, St. Luke's CEO Wakeman advised the Board that under then-current conditions, St. Luke's would be able to survive between three and five years, and that if St. Luke's was able to get rate increases under contracts with two of St. Luke's largest commercial payers, St. Luke's could survive four to seven years. (Wakeman, Tr. 2624-2625).

416. In its December 23, 2009 "Material Event Notice," to its bond insurer Ambac Assurance Corp. ("AMBAC") (F. 907), St. Luke's stated that its "plan to address its future covenant compliance is to attempt to negotiate new, or renegotiate existing contracts with its insurance carriers." St. Luke's also stated that it "may explore other options, including but not limited to exploring an affiliation with another health system." (RX183 at 000004; Gordon, Tr. 6816-6817, *in camera*).

417. At the December 15, 2009 St. Luke's Board of Directors meeting, three St. Luke's Board members, Mr. Bachey, Mr. Schultz, and Dr. Houston, expressed the view that for St. Luke's an affiliation was inevitable; St. Luke's would have to merge with somebody within the next three years. (Wakeman, Tr. 2999-3000, *in camera*).

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418. The December 2009 Affiliation Update described the pros and cons of affiliating with ProMedica, Mercy or UTMC. (PX01016 at 023-024, *in camera*).

419. As to the option of affiliating with Mercy, the December 2009 Affiliation Update to the Board identified the “pros” as: a mission and culture of quality consistent with St. Luke’s; some favorable insurance contracts; some investment in St. Luke’s campus; and financial stabilization of organization’s ability to serve and expand. The “cons” of St. Luke’s affiliating with Mercy were identified as: very limited local governance and control, with the “system” having a priority over local circumstances; recent history of poor physician decisions/relations; and could increase prices/cost to the community. (PX01016 at 023, *in camera*).

420. As to the option of affiliating with UTMC, the December 2009 Affiliation Update to the Board identified the “pros” as: exciting/compelling vision for the future; some opportunity for St. Luke’s to make a mark re: a future health-care system; history of working together; access to future physicians; and benefit to the community. The “cons” of St. Luke’s affiliating with UTMC were identified as: limited help with regard to insurance contracts; bureaucracy resulting from being a state institution; difficulty working together on many levels; and could increase prices/cost to the community. (PX01016 at 024, *in camera*; see also PX01018 at 008, 016).

421. As to the option of affiliating with ProMedica, the December 2009 Affiliation Update to the Board identified the “pros” as: favorable insurance contracts (also Paramount); access to capital; investment in St. Luke’s campus; potential for local governance and control; solid physician strategy and infrastructure; and financial stabilization of organization’s ability to serve and expand. The “cons” of St. Luke’s affiliating with ProMedica were identified as: some quality measures are poor; history of poor relations with partners/affiliates; and could increase prices/cost to the community. (PX01016 at 023, *in camera*).

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422. On December 15, 2009 St. Luke's CEO, Mr. Wakeman, recommended to the St. Luke's and OhioCare's Board of Directors that St. Luke's pursue affiliating with ProMedica. (Wakeman, Tr. 2996, *in camera*).

423. On December 15, 2009, St. Luke's Board of Directors voted to pursue exclusive discussions with ProMedica for ninety days with an intent to enter into a joinder. (PX01457 at 004, *in camera*; Black, Tr. 5646-5647, *in camera*).

424. St. Luke's Board decided not to pursue affiliation with Mercy based upon several issues, including concerns about a lack of local governance and [redacted], and was an issue for the Board. (Wakeman, Tr. 2560-2561, 2980-2982, *in camera*; Black, Tr. 5647-5648, *in camera*; PX01583 at 002, *in camera*; PX01457 at 004, *in camera*; Shook, Tr. 1000-1001, *in camera*; RX16 at 024-025 (Bazeley, Dep. at 91-94)).

425. St. Luke's Board decided not to pursue affiliation with UTMC principally because UTMC's proposed board structure was not acceptable to St. Luke's, due to UTMC's wanting to maintain full veto power; and the potential cultural incompatibility between UTMC's state institution and union culture with St. Luke's culture. (Wakeman, Tr. 2556-2557; Black, Tr. 5648, *in camera*).

426. ProMedica and St. Luke's signed a Memorandum of Understanding on January 15, 2010 to "provide a framework for their discussions" for a proposed transaction in which OhioCare and its subsidiaries including St. Luke's "would become an integral part of ProMedica." (Hanley, Tr. 4545; RX1912 at 000001, *in camera*; Oostra, Tr. 5849).

427. ProMedica and St. Luke's signed the Joinder Agreement on May 25, 2010. (PX00058 at 001; Hanley, Tr. 4628, *in camera*).

428. The Joinder Agreement commits ProMedica to "maintain [St. Luke's] using its current name and identity and at its current location for a minimum of ten (10) years . . . as a fully operational acute-care hospital providing the following services:

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emergency room, ambulatory surgery, inpatient surgery, obstetrics, inpatient nursing and a CLIA certified laboratory.” (PX00058 at 023, 045-046; Hanley, Tr. 4631-4632, *in camera*; Oostra, Tr. 5856).

429. In the Joinder Agreement, ProMedica agreed to provide St. Luke’s \$30 million in capital to fund capital projects such as those that St. Luke’s had deferred because it lacked the funds needed to pay for them. (Hanley, Tr. 4628, *in camera*; PX00058 at 021, 056; Johnston, Tr. 5351-5352, 5372).

430. The capital commitment referred to in F. 429 was to be used for capital projects at St. Luke’s, including converting semi-private rooms to private rooms, updating St. Luke’s IT systems, constructing an outpatient lobby, renovating the heart center, moving administrative services, expanding surgical areas, and increasing the private postpartum area and well infant nursery. (Hanley, Tr. 4628, *in camera*; PX00058 at 056).

431. The Joinder Agreement maintains St. Luke’s existing medical staff, bylaws, rules, and regulations. (PX00058 at 046).

432. The Joinder Agreement provides that St. Luke’s would become a participating provider in Paramount upon closing. (Hanley, Tr. 4631, *in camera*; PX00058 at 022-023).

433. A stated objective in the Joinder Agreement is optimization of health benefits by continued local board governance and oversight of charitable assets. (PX00058 at 007).

434. Pursuant to the Joinder Agreement, St. Luke’s would hold 25 of 27 board seats, reserving 2 to be appointed by ProMedica. ProMedica holds a reserve power to approve nominees for St. Luke’s Board, “which approval shall not be unreasonably withheld.” (PX00058 at 009). ProMedica also holds reserve powers to remove any director, trustee or other board member of St. Luke’s without cause, except that during an initial governance period of no less than 3 years, removal must be with cause. (PX00058 at 016-017).

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435. ProMedica's reserve powers under the Joinder Agreement also include the right to approve budgets, debt issuance, amendments to governing documents, and to appoint (or remove) St. Luke's president, secretary and/or treasurer, after prior consultation with St. Luke's. (PX00058 at 017-018).

436. The St. Luke's Board vote to approve the Joinder was unanimous, with one abstention. (Black, Tr. 5660, *in camera*; RX1235 at 004, *in camera*).

M. Competitive Effects

1. Competitive significance of St. Luke's

a. Hospitals' views on competitive significance of St. Luke's

437. ProMedica considers Mercy to be its most significant competitor in the Toledo area. (Oostra, Tr. 5803-5804; Wachsmann, Tr. 4866; Randolph, Tr. 6934-6935).

438. ProMedica considers Mercy to be its most significant competitor because of Mercy's size and backing by Catholic Health Partners, its access to capital, ability to make investments in communities, and re-entry into the physician employment business, and because it is a multi-hospital system that virtually mirrors the ProMedica system. (Oostra, Tr. 5803-5805).

439. Mercy considers ProMedica to be its most significant competitor in the Toledo area. (Shook, Tr. 1091-1092, *in camera*). Marketing studies commissioned by Mercy reflect a high-degree of competition between ProMedica and Mercy. (Shook, Tr. 1090-1091, *in camera*; PX02534 at 003, 006, 013, 020, 023, *in camera*; RX250 at 000005, 000013, 000018, *in camera*).

440. The CEOs of both ProMedica and St. Luke's agree that, before the Joinder, St. Luke's viewed ProMedica as its "most significant competitor." (Wakeman, Tr. 2511, 2523-2527; Oostra, Tr. 6040).

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441. St. Luke's CEO, Mr. Wakeman, after joining St. Luke's in 2008, had as his goal to regain volume from ProMedica in St. Luke's core and primary service areas. (Wakeman, Tr. 2504-2505).

b. MCOs' views of competitive significance of St. Luke's

442. MCOs believe that, because of their broad service offerings and geographic reach throughout the Toledo metropolitan area, MCOs must have either Mercy or ProMedica in their health plan. (RX27 at 000005 (Sheridan, Dep. at 15), *in camera*; PX02067 at 003, *in camera*).

443. While a ProMedica-UTMC network is attractive, a St. Luke's-UTMC network would not be attractive. (Town, Tr. 3785-3786, *in camera*).

444. United considers the ProMedica and Mercy hospitals to be extremely similar in terms of their location and the types of services and acuity of care they offer. (Sheridan, Tr. 6616-6618).

445. When [redacted] and ProMedica were unable to reach an agreement [redacted] substituted Mercy for ProMedica in its network. (PX01902 at 014 ([redacted], IHT at 48-49, *in camera*)).

446. MMO considers Mercy and ProMedica to be each other's primary competitor. (RX46 at 000008 (Pirc, IHT at 23-24), *in camera*).

447. All of the MCOs operating in Lucas County have had either ProMedica or Mercy or both in their networks. (Guerin-Calvert, Tr. 7329).

448. Patients cannot get all of the services they may need from only St. Luke's. (Buehrer, Tr. 3092).

449. MCOs could not replace ProMedica with St. Luke's. (Town, Tr. 4057, 4081; RX204 at 000004 (Pugliese Dep. at 11), *in camera*; RX205 at 000004 (Radzialowski, Dep. at 10-11), *in*

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camera). Because St. Luke's does not offer the high level services, such as transplants, MMO, for example, needs to include other hospitals in its network in order to meet all its members' needs. (Pirc, Tr. 2280).

c. Patients' views, as reflected in consumer preference surveys

450. A 2006 survey conducted for St. Luke's revealed that in St. Luke's core service area, St. Luke's (45%) and TTH (24%) were the top two hospitals that came to mind when consumers were asked about hospitals in the area. (PX01352 at 007; Wakeman, Tr. 2521). The consumer survey found that St. Luke's was preferred by 44% of consumers in the core service area and TTH was second, with 21%. (PX01352 at 007; Wakeman, Tr. 2522).

451. A 2008 survey conducted for St. Luke's revealed, similarly to 2006, that in St. Luke's core service area, St. Luke's and TTH were the top two hospitals that came to mind when consumers were asked about hospitals in the area, and the top two preferred hospitals. (PX01077 at 009-014; Wakeman, Tr. 2523).

Forty-two percent of residents in St. Luke's primary service area selected TTH as St. Luke's most direct competitor and another 8 percent selected Flower Hospital. (PX01169 at 042; Rupley, Tr. 1958-1959). UTMC was selected by 8 percent and St. Vincent by 16 percent of residents. (PX01169 at 042; Rupley, Tr. 1958-1959).

452. In the same 2008 survey as described in F. 451, St. Luke's was identified most often as the preferred hospital for "routine care," followed by TTH. (PX01169 at 015; Rupley, Tr. 1953-1955).

d. Diversion analysis substitutes

453. Diversion analysis is a commonly used method to quantify the degree of substitutability between hospitals or hospital systems. In the context of a hospital merger, the diversion ratio measures the predicted share of a hospital's

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patients that would go to a specific alternative if that hospital was no longer available. (Town, Tr. 3771, *in camera*).

454. Diversion analysis relies on hospital claims data, and estimates a hospital choice model by examining the choices patients make with respect to which hospital to use. (Town, Tr. 3772-3773, *in camera*; PX02148 at 046-047 (¶ 88) (Town Expert Report), *in camera*).

455. In a diversion analysis, the higher the diversion, the higher the substitutability of the hospitals. (Town, Tr. 3773, *in camera*; PX02148 at 046-047 (¶ 88) (Town Expert Report), *in camera*).

456. Complaint Counsel's expert, Professor Town, performed a diversion analysis to measure the predicted share of a specific hospital's patients that would go to a specific alternative hospital or hospital system if the first hospital were no longer available. Professor Town's analysis examined the entire Greater Toledo Area and reported the results for each MCO's member population. (PX02148 at 046-047 (¶ 88 and n.136) (Town Expert Report), *in camera*).

457. The diversion analysis described in F. 456 shows that if St. Luke's were not available, for [redacted] patients, [redacted] percent would go to a ProMedica hospital, [redacted] percent would go to a Mercy hospital and [redacted] percent would go to UTMC. (Town, Tr. 3775-3776, *in camera*; PX01850 at 020 (Table 3) (Town Rebuttal Report), *in camera*). Diversion analysis for [redacted] patients reveals that ProMedica is St. Luke's closest competitor. (Town, Tr. 3775-3776, *in camera*; PX01850 at 020 (Table 3) (Town Rebuttal Report), *in camera*).

458. The diversion analysis described in F. 456 shows that if ProMedica hospitals were not available, for [redacted] patients, the second largest number of patients [redacted] percent would have gone to St. Luke's. (Town, Tr. 3775-3776, *in camera*; PX01850 at 020 (Table 3) (Town Rebuttal Report), *in camera*).

459. Professor Town's diversion analysis (F. 456) demonstrates that for [redacted], ProMedica is St. Luke's closest

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substitute; for FrontPath, St. Luke's is ProMedica's closest substitute; and for [redacted], ProMedica is the second-closest substitute for St. Luke's. (Town, Tr. 3777, *in camera*; PX01850 at 020 (Table 3) (Town Rebuttal Report), *in camera*).

460. In a year-by-year diversion analysis (F. 456), [redacted] enrollees' diversion from St. Luke's to ProMedica is increasing, reflecting the relatively recent addition of ProMedica to [redacted] network. (Town, Tr. 3780-3781, *in camera*; PX01850 at 018 (Table 2) (Town Rebuttal Report), *in camera*).

461. Based on the diversion analysis (F. 456), Mercy is ProMedica's closest substitute and St. Luke's is ProMedica's second-closest substitute. (Town, Tr. 3777-3778, *in camera*; PX01850 at 020 (Table 3) (Town Rebuttal Report), *in camera*).

e. Other indicators of competitive significance of St. Luke's

462. St. Luke's is the third-largest hospital in the market based on commercial volume. St. Luke's had 2,846 commercial discharges between July 1, 2009 and March 31, 2010, exceeded only by St. Vincent and TTH. (PX02148 at 171 (Town Expert Report), *in camera*).

463. St. Luke's provides care to approximately ten commercially insured patients per day. (PX02137 at 055, *in camera*). By comparison, ProMedica's hospitals provide care to approximately 53 commercially insured patients per day. (PX02137 at 056, *in camera*).

464. ProMedica and St. Luke's competed to attract patients, especially those who reside between ProMedica's hospitals and St. Luke's. (Oostra, Tr. 6041-6042).

465. Prior to the Joinder, ProMedica and St. Luke's also competed to attract and retain physicians. (Oostra, Tr. 6040-6041).

466. Pursuant to the Joinder Agreement, St. Luke's was added to the provider network of ProMedica's health-insurance

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subsidiary, Paramount. (PX00058 at 022-023 (Joinder Agreement § 6.2(i)); PX00140 at 002).

467. ProMedica expected that volume shifts to St. Luke's away from ProMedica hospitals would "undoubtedly occur" after St. Luke's joined Paramount. (Randolph, Tr. 7099-7100, *in camera*). In particular, ProMedica expected patients residing in the area around St. Luke's to be most likely to switch from ProMedica hospitals to St. Luke's. (Randolph, Tr. 7100, *in camera*).

468. ProMedica estimated that [redacted] Paramount commercial inpatient admissions at ProMedica hospitals would be redistributed from ProMedica to St. Luke's if St. Luke's was added to Paramount's network. (PX00040 at 007, *in camera*).

469. ProMedica estimated if St. Luke's was included in the Paramount network, the potential risk of lost margin annually to Flower Hospital was [redacted] million if every Paramount discharge at Flower from St. Luke's primary zip codes left Flower for St. Luke's. (PX00240 at 002, *in camera*).

470. St. Luke's also believed that if it was readmitted to Paramount, it would gain patients currently going to TTH. (Rupley, Tr. 2010, *in camera*).

471. ProMedica estimated that St. Luke's readmission to Anthem's network in 2009 would cost ProMedica [redacted] million in gross margin annually. (PX00333 at 002, *in camera*).

f. Competitive significance of location in southwest Lucas County

(i) Demographics of southwest Lucas County

472. Southwest Lucas County is a desirable area for a hospital to be located. (Oostra, Tr. 6036-6037; PX00009 at 029 (ProMedica Credit Presentation) ("desirable section of the Toledo metro area where PHS lacks a physical presence"). St. Luke's CEO believes that St. Luke's location is "terrific" and places it in a "favorable" position. (Wakeman, Tr. 2477). St. Luke's is

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easily accessible from major highways, and its location provides it with access to a growing population of employed and commercially insured patients. (Wakeman, Tr. 2479-2481; PX01911 at 015 (Wakeman, IHT at 53-55), *in camera*; Oostra, Tr. 6036-6038; Nolan, Tr. 6287, *in camera* (St. Luke's is "in a highly visible area, right off the highway, good highway access, and it's an area with good demographics, reasonable population growth and good average household incomes.") PX01132 at 002-004 (St. Luke's evaluation), *in camera*).

473. The area surrounding St. Luke's is growing and "more and more [is] being built in the adjoining communities to Maumee." (Shook, Tr. 927). The area surrounding St. Luke's contains "very good demographics" with "a reasonably well-affluent community" and a "better insured population" than the rest of Lucas County. (Shook, Tr. 926-927; Wakeman, Tr. 2477, 2479).

474. The January 2011 study titled "Clinical Integration Strategy" developed for ProMedica by Navigant Consulting outlined clinical service consolidation recommendations for ProMedica. One of Navigant's recommendations is that: "SLH will serve as the gateway facility to the southern and western portions of the Toledo MSA." (PX02386 at 010, *in camera*). *See also* PX01215 at 003 (Navigant Presentation: ProMedica Health System Market and Facility Assessment Summary), *in camera* ("good access and visibility from the Interstate").

(ii) MCOs' views

475. MCOs recognize that a hospital's location within Lucas County is important because community members prefer hospitals close to them. (Pugliese, Tr. 1450-1452 (Anthem's Lucas County members "will stay closer to home for common services, preventative care services."); (Pirc, Tr. 2184 ("if a loved one is in the hospital, you'd rather be ten minutes away than an hour away . . .")); *cf.* Radzialowski, Tr. 634 (" . . . people do develop connections with their local hospital. You know, their babies, that's where they have babies. Their parents might have died there. They know people that work there. They sit on the board.")).

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476. MCOs believe that a hospital's location in Lucas County is an important factor in contract negotiations. (Radzialowski, Tr. 663; Pirc, Tr. 2199; Pugliese, Tr. 1451-1452, 1459).

477. Specifically, St. Luke's location was important to MCOs in configuring their networks. (Pirc, Tr. 2195-2196; Pugliese, Tr. 1442-1443; Radzialowski, Tr. 713-714, *in camera*; Sheridan, Tr. 6672-6673; *see also* Town, Tr. 3627, 3651).

478. MMO's Vice President of Network Management, believed that a network without St. Luke's would leave a fairly sizable geographic hole in MMO's network and that MMO needed St. Luke's in its network to have a marketable product at all. (Pirc, Tr. 2195, 2266-2267).

479. Greg Radzialowski, Senior Network Manager of Aetna, believes that Mercy is unable to cover the southwest portion of Lucas County and that the location of St. Luke's significantly increases ProMedica's leverage with Aetna. (Radzialowski, Tr. 713-714, *in camera*).

480. Jim Pugliese, Regional Vice President of Contracting and Provider Relations for Anthem, believes that the area around St. Luke's is an important customer base for Anthem. (Pugliese, Tr. 1442-1443).

481. Paramount's President believed that the addition of St. Luke's to Paramount's network in late 2010 made Paramount more attractive to employers in southwestern Lucas County and had a positive impact on Paramount. (Randolph, Tr. 7007-7008, 7061-7062).

482. An analysis prepared for ProMedica projected that adding St. Luke's to the Paramount network could net Paramount as many as [redacted] new members. (PX00040 at 008, *in camera*).

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(iii) Perspective from Mercy

483. A document developed by Mercy in 2010 in the ordinary course of business analyzed market shares for southwest Lucas County and determined that the hospitals in Lucas County had the following market shares: ProMedica, [redacted]; St. Luke's, [redacted]; Mercy, [redacted]; and UTMC, [redacted]. (PX02290 at 003, *in camera*; Shook, Tr. 1012-1013). Post-Joinder, ProMedica has a [redacted] share in southwestern Lucas County. (PX02290 at 003, *in camera*).

484. Based on Mercy's review of market share information, St. Luke's had a slim majority of the southwest Lucas County market, with "a fair degree of inpatient admissions going to Flower and Toledo." (Shook, Tr. 934).

485. Mercy does not have a hospital in southwestern Lucas County and has no plans to build one. (Shook, Tr. 963-965, 968; PX02068 at 002, 006 (¶¶ 8, 24) (Shook, Decl.), *in camera*); PX02148 at 064-065 (¶ 116) (Town Expert Report), *in camera*). [redacted]. (Shook, Tr. 988, *in camera*).

486. The joinder of St. Luke's with ProMedica gives ProMedica a significant locational advantage over Mercy because Mercy offers no direct counterpart to St. Luke's in southwest Lucas County. (PX02148 at 064-065 (¶ 116) (Town Expert Report), *in camera*; Sheridan, Tr. 6698, *in camera*).

(iv) Drive-time

487. Out of one hundred admissions at St. Luke's, 75 of those admissions travel less than 14 minutes to get to St. Luke's; 95 of those admissions travel less than 20 minutes. (Guerin-Calvert, Tr. 7336-7337).

488. The average drive-time for St. Luke's patients is approximately 12 minutes. (Guerin-Calvert, Tr. 7336-7337).

489. Looking at the incremental drive-time for patients located in each of St. Luke's top 10 zip codes from which it admits patients shows that, on average, the incremental drive-time

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for a St. Luke's patient to go to a different hospital is an 18 additional minutes. (Guerin-Calvert, Tr. 7335-7337).

490. Respondent's expert's drive-time analysis shows that many patients for whom St. Luke's is the closest hospital, travel to other hospitals that are farther away. (Guerin-Calvert, Tr. 7351-7352; RX71(A) at 000032-000034, 000186, *in camera*).

491. Patient origin data (discussed below, II.M.1.f.v.) and drive-time analyses show that patients do not necessarily go to the next closest hospital. (Guerin-Calvert, Tr. 7244-7245; RX71(A) at 000034, *in camera*).

(v) Patient origin

492. Data based on where the patients in a hospital reside (patient origin) demonstrates that approximately 60 percent of the patients who reside in St. Luke's service area travel to hospitals other than St. Luke's to receive GAC inpatient services; however, this may reflect in part the fact that Paramount insureds, for whom St. Luke's was not a network provider at the time the data was collected, were travelling to an in-network hospital. (PX02148 at 161 (Town Expert Report, Ex. 11); Town, Tr. 3938-3939, 4438-4439).

493. Based on patient origin data, patients in St. Luke's service area choose TTH the most, if they do not go to St. Luke's. (Rupley, Tr. 1945).

494. According to internal documents, in St. Luke's core service area, St. Luke's and ProMedica had the first and second highest inpatient market shares, respectively, for GAC inpatient services for all patients. (PX01235 at 003).

495. A December 2009 presentation to St. Luke's Board indicated that St. Luke's and ProMedica treated the first and second greatest percentages of all GAC patients in St. Luke's core service area. (Rupley, Tr. 1978-1983, *in camera*; PX01016 at 003, *in camera*).

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496. St. Luke's internal documents also indicate that in 2007, ProMedica and St. Luke's accounted for 66 percent of the inpatient market share for all patients in St. Luke's core service area, compared to 13 percent for UTMC and only 8 percent for Mercy St. Vincent's. (Wakeman, Tr. 2519; PX01352 at 006). Since 2007, St. Luke's inpatient market share in its core service area has increased. (Wakeman, Tr. 2519-2520).

497. Based on Respondent's expert's calculations, in St. Luke's top ten zip codes by volume, (accounting for 64 percent of admissions), ProMedica, (43 percent) and St. Luke's (26 percent) rank first and second in market shares. (PX02148 at 076 (¶ 137) (Town Expert Report), *in camera*; PX02123 at 042 (Guerin-Calvert, Decl. Exhibits)). In eight of St. Luke's top ten zip codes, and in all of St. Luke's "core" zip codes, St. Luke's and ProMedica had the first and second highest shares of the GAC inpatient service market. (PX02123 at 042 (Guerin-Calvert, Decl. Exhibits); PX02148 at 043, 064-065, 161 (¶ 82, 116-117, Exhibit 11) (Town Expert Report), *in camera*).

498. Based on market shares, Professor Town concluded that patients residing in St. Luke's core service area prefer St. Luke's and ProMedica for inpatient services. (Town, Tr. 3753-3754, *in camera*). Mercy and UTMC have much lower market shares and are therefore preferred less by patients in St. Luke's core service area. (Town, Tr. 3754-3755, *in camera*).

2. Pre-Joinder pricing

a. Background

(i) Terminology

499. A hospital chargemaster is a list of the prices for the hospital's services. (Radzialowski, Tr. 761; Randolph, Tr. 6959).

500. The price at which a party perceives it would be just as well off not reaching an agreement is that party's "walk-away" point. (PX02148 at 015-016 (¶ 26) (Town Expert Report), *in*

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camera; PX01914 at 015-016 (Pirc, IHT at 51-53), *in camera*; Radzialowski, Tr. 660).

501. The contract “term” identifies the length of time in which the contract is in force, such as one-year or multi-year terms. (Wachsman, Tr. 4898-4899).

502. A most-favored nation (“MFN”) clause is a contractual provision that prohibits a hospital provider that has agreed to rates with one MCO from agreeing to lower rates with competing MCOs unless they also extend the same rates to the first MCO. (Pugliese, Tr. 1549, 1580)

503. “DRG” stands for Diagnosis Related Group. It is a billing methodology that was implemented by Medicare in the 1970s and 1980s and is commonly used today by MCOs. (Radzialowski, Tr. 673; Pugliese, Tr. 1473, *in camera*).

504. A DRG code is assigned to a patient based on the event for which the patient was admitted or the services that the patient obtained. (Guerin-Calvert, Tr. 7161-7162).

505. An “escalator” provision is a negotiated term that allows an adjustment to the contract reimbursement rates, based on an index, such as one of the U.S. Department of Labor’s official Consumer Price Indexes. (Radzialowski, Tr. 761; Sandusky, Tr. 1320; Wachsman, Tr. 4904-4905).

506. “Outlier threshold” refers to contract provisions designed to protect providers against catastrophic cases that incur charges outside the range of services covered by a DRG rate, by providing reimbursement for those cases that reach “outlier” status. (Wachsman, Tr. 4901-4902).

507. “Ancillary” services include physician and facility services that are not part of the hospital, including long-term care facilities, home health services, durable medical equipment, pharmacy services, and outpatient surgery centers. Rates for ancillary services are separate from the inpatient and outpatient rates in a contract, and there is a rate attached to each ancillary service. (Wachsman, Tr. 4906).

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508. A “cost coverage ratio” identifies for each MCO what percentage of a hospital’s operating costs, or direct costs, that MCO is covering. It is calculated by taking all of the operating costs attributed to an MCO and comparing those costs to the actual payments received from that MCO, then the payments are divided by the costs to yield the ratio. (Wachsman, Tr. 4947-4948, *in camera*).

(ii) Rate negotiations

509. Reimbursement rates for hospital services are determined through the bargaining process between hospitals and MCOs. (PX02148 at 014-015 (¶ 24) (Town Expert Report), *in camera*; Pugliese, Tr. 1472, *in camera*, 1547-1548; Radzialowski, Tr. 658-661; Korducki, Tr. 527-528; Shook, Tr. 948-950).

510. MCOs negotiate rates for hospital services on behalf of their customers, who are both self-insured and fully-insured employers. (Pugliese, Tr. 1432-1433, 1547; PX01914 at 014 (Pirc, IHT at 49); Radzialowski, Tr. 748; PX02148 at 15 (¶ 25) (Town Expert Report), *in camera*; Sandusky, Tr. 1297).

511. Prior to the Joinder, both ProMedica and St. Luke’s independently engaged in extensive negotiations with MCOs over rates for services, and other contractual terms, with the goal of reaching a multi-year contract with each MCO. (PX02148 at 015 (¶ 25) (Town Expert Report), *in camera*; Radzialowski, Tr. 681-687, *in camera*; Pugliese, Tr. 1474-1476, *in camera*).

512. Negotiations between hospitals and MCOs cover many contractual terms including: claims adjudication procedures, payment outliers, payment escalators, hold-harmless provisions, chargemaster limits, reimbursement methods, renewal or renegotiation provisions, grievance procedures, medical necessity provisions, coordination of benefits provisions, pay-for-performance provisions, pre-certification requirements, nondiscrimination provisions, “never event” provisions, contract length provisions, termination provisions, and other specific provisions that may be important to the hospital or the MCO. (Shook, Tr. 949-950, 1074; Pugliese, Tr. 1550-1553; McGinty,

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Tr. 1240-1241, 1258; Pirc, Tr. 2206-2207, 2288-2290; Radzialowski, Tr. 760-763; Radzialowski, Tr. 804, *in camera*; Sheridan, Tr. 6627; Randolph, Tr. 6950-6951).

513. Out of all the contract terms that are negotiated, reimbursement rates, and the contractual terms that impact the total amount of reimbursement, are the most critical. (Wachsman, Tr. 5139-5140, *in camera*; Sandusky, Tr. 1318-1319; Radzialowski, Tr. 660; Pugliese, Tr. 1514, *in camera*; Sheridan, Tr. 6703, *in camera*).

514. An example of a contractual term that impacts reimbursement is reimbursement methodology. The DRG reimbursement methodology is geared toward cases that have a lower level of charges than cases that fall into outlier categories. (Wachsman, Tr. 4903-4904).

515. MCOs and hospitals may negotiate a fixed price list that is based on the DRG codes, (Sandusky, Tr. 1319-1320); however, the DRG rate alone does not fully represent a contract's reimbursement level because a high outlier methodology may cause cases that exceed the DRG rate, but fall short of the outlier threshold, to go unpaid. (Wachsman, Tr. 4903-4904).

516. To gain revenue in a negotiation, a hospital can increase its unit price for particular services in the MCO agreement or can negotiate a higher threshold in terms of its chargemaster allowance, which is the cost that they would be able to pass through the chargemaster. (Pugliese, Tr. 1455).

517. Medicare and Medicaid reimbursements do not cover the costs of providing hospital services to Medicare and Medicaid patients. (Wachsman, Tr. 4848; Guerin-Calvert, Tr. 7298-7299; RX71(A) at 000128, 000133, *in camera*).

518. Medicare reimbursed hospitals, on average, 89 to 90 percent of the hospital's cost of treating Medicare patients in 2009. (Guerin-Calvert, Tr. 7302-7303; RX71(A) at 000133, *in camera*).

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519. Because Medicare and Medicaid reimbursement rates cover less than the provider's costs, providers must subsidize the difference between the government reimbursement rates and the provider's costs. (Wachsman, Tr. 4847-4848).

520. Compensation received by hospitals from private MCOs not only covers hospital costs for patients covered by MCOs, but also provides some contribution toward covering the insufficient funding provided to hospitals from Medicare and Medicaid. (Guerin-Calvert, Tr. 7304).

b. ProMedica pricing

521. At the time of the Joinder, ProMedica was in-network with MMO, Anthem, FrontPath, United, Paramount, and Aetna. (F. 136, 157, 173, 191, 204, 222).

522. ProMedica seeks to obtain reimbursement rates from MCOs that [redacted]. ProMedica has established a [redacted]. (RX1854 at 000005, *in camera*; Wachsman, Tr. 4949-4950, 5140, *in camera*).

523. Cost coverage ratios consider both the direct and indirect costs that a hospital incurs as a result of providing care. (Den Uyl, Tr. 6438, *in camera*).

524. ProMedica's commercial reimbursement rates pre-Joinder were among the highest in Lucas County. (Radzialowski, Tr. 684, *in camera*; Pugliese, Tr. 1484-1485, 1513, 1656-1657, *in camera*; Pirc, Tr. 2238, *in camera*; PX02148 at 145 (Town Expert Report, Ex. 7), *in camera*; *see also* [redacted], Tr. 6658-6659, *in camera* (stating that Bay Park's rate with [redacted] "reflects an absolutely ridiculously high base rate for the MS-DRG ...").

525. ProMedica was informed by Anthem that its rates were among the highest in the state of Ohio. (Oostra, Tr. 5996; *see also* PX00153 at 001 (ProMedica Jan. 2009 e-mail) ("we hear from payors we are among the most expensive in [O]hio")).

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526. ProMedica had the largest market shares and the highest reimbursement rates; Mercy, the next-largest system, had the second highest rates; UTMC, the third largest system, had the third highest prices; and St. Luke's, with the smallest market share, had the lowest prices in the market. (PX02148 at 039 (¶ 71)); *see also* Pugliese, Tr. 1513).

527. ProMedica's prices cannot be explained by competitively-benign factors such as cost or quality. (PX01850 at 057-059 (¶¶ 89-90) (Town Rebuttal Report), *in camera*).

c. St. Luke's pricing

528. At the time of the Joinder, St. Luke's was in-network with MMO, Anthem, FrontPath, United, and Aetna. (F. 139, 160-162, 191, 204, 222).

529. On December 15, 2009, St. Luke's reported to the Board the findings of Navigant Consulting that (1) St. Luke's average payor rates for inpatient services were [redacted] percent below the Toledo market median; (2) St. Luke's overall rates with MMO were [redacted] percent of the Toledo market median; and (3) if St. Luke's were to be paid at the Toledo market median, this would result in an additional [redacted] million in reimbursement (PX01016 at 010).

530. St. Luke's commercial reimbursement rates are significantly lower than those of ProMedica and Mercy. (Pirc, Tr. 2238, 2241, *in camera*; Radzialowski, Tr. 684, 687-688, 698-700, *in camera*; Sandusky, Tr. 1338-1340, 1347-1348, *in camera*; *see* Pugliese, Tr. 1512-1513, *in camera*; McGinty, Tr. 1210).

531. As of August 31, 2010, Anthem and MMO were St. Luke's two largest MCOs, comprising more than [redacted] percent of St. Luke's net revenue and more than [redacted] percent of its commercial revenue. (RX56 at 000010, *in camera*).

532. St. Luke's was being paid less than its comparable sized hospitals throughout the nation that were members of

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Voluntary Hospitals of America (“VHA”). St. Luke’s was receiving just over [redacted] per case-adjusted inpatient admission whereas on average a VHA hospital was receiving over \$6500. (PX01018 at 002, *in camera*; Wakeman, Tr. 2904-2906, *in camera*).

533. St. Luke’s was being paid less than comparably sized hospitals in St. Luke’s region that were part of the VHA including Flower, Oakwood Hospital and Medical Center, and Akron Medical Center. St. Luke’s was receiving just over [redacted] per case-adjusted inpatient admission whereas these area hospitals were each receiving over \$7000. (PX01018 at 002, *in camera*; Wakeman, Tr. 2904-2906, *in camera*).

534. In the fall of 2009, St. Luke’s engaged Navigant Consulting to do an “insurance assessment” of the marketplace that would evaluate St. Luke’s reimbursement rates in comparison with the average rates paid in the local market. St. Luke’s received the final copy of this study on November 25, 2009. (Wakeman, Tr. 2986-2987, *in camera*; PX01029, *in camera*).

535. The November 25, 2009 Navigant study concluded that St. Luke’s inpatient commercial insurance rates were about [redacted] percent below the market average. (PX01029 at 007, *in camera*; Wakeman, Tr. 2988-2989, *in camera*; RX37 at 000015 (Machin, IHT at 53)).

536. Prior to the Joinder, St. Luke’s had concluded that it was grossly underpaid, and that an increase in volume had been insufficient to offset costs and have an acceptable margin. (PX01018 at 003, *in camera*; Wakeman Tr. 2907-2908, *in camera*).

537. Prior to the Joinder, St. Luke’s believed that its “reimbursement rates were below those of other organizations, not only in [its] area, but throughout the region.” (Wakeman, Tr. 2657, *in camera*).

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(i) MMO

538. MMO paid St. Luke's [redacted] of any of St. Luke's MCOs. (Wakeman, Tr. 2936, *in camera*).

539. [redacted]. (PX02280 at 014; Guerin-Calvert, Tr. 7417-7418, *in camera*; Pirc, Tr. 2345-2346, *in camera*).

540. St. Luke's contract with MMO originated in 1995 and was amended several times since then. The last amended contract had an effective date of October 1, 2006 and a termination date of December 31, 2010. (Pirc, Tr. 2339-2340, *in camera*; Wakeman, Tr. 2933-2934, *in camera*).

541. In 2009, St. Luke's requested a renegotiation of rates from MMO prior to the contract's expiration in December 2010. (Guerin-Calvert, Tr. 7415-7416, *in camera*).

542. Contract negotiations between St. Luke's and MMO began in 2009 and continued into early 2010. (Pirc, Tr. 2339, 2353, *in camera*).

543. St. Luke's and MMO negotiated reimbursement rates, bonus formulas, escalator rates, and contract duration, among other terms. (Pirc, Tr. 2349-2353, *in camera*; Wakeman, Tr. 2932-2935, *in camera*, PX02275, *in camera*).

544. MMO's proposed reimbursement rate increase, plus bonus formula, represented an approximately [redacted] percent rate increase and would have given St. Luke's an additional [redacted] million in payments after the first full year. With compounding, payments go from [redacted] million in 2009 for MMO inpatient payments to about [redacted] million in 2012, which represents just under a [redacted] percent increase. (Guerin-Calvert, Tr. 7424-7426, *in camera*; Pirc, Tr. 2350-2351, *in camera*).

545. MMO rejected St. Luke's proposal that MMO agree to the increase referred to in F. 544 [redacted]. (Pirc, Tr. 2354-2356, *in camera*; PX02284 at 001, *in camera*; PX01016 at 012-013; Guerin-Calvert, Tr. 7422-7423, *in camera*).

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(ii) Anthem

546. The agreement between Anthem and St. Luke's on PPO rates, effective July 1, 2008, had a [redacted]. (Wakeman, Tr. 2650, *in camera*; PX02276 at 002, *in camera*; Pugliese, Tr. 1614-1615, *in camera*, 1620-1621, *in camera*; PX02408 at 001, *in camera*).

547. In January 2010, St. Luke's sought [redacted] percent increase in its rates from Anthem. (Pugliese, Tr. 1512, 1640, *in camera*; PX02382 at 001, *in camera*).

548. When Anthem considered St. Luke's proposal referred to in F. 547, among other things, [redacted]. (Pugliese, Tr. 1641, *in camera*; RX965 at 000003, *in camera*).

549. Anthem [redacted]. (Pugliese, Tr. 1510-1511, *in camera*; PX02382 at 001, *in camera*).

(iii)FrontPath

550. [redacted]. (Sandusky, Tr. 1386-1387, *in camera*; Guerin-Calvert, Tr. 7433-7434, *in camera*).

551. [redacted]. (Sandusky, Tr. 1386-1388, *in camera*).

552. [redacted]. (Sandusky, Tr. 1386-1388, *in camera*; RX782 at 000001, *in camera*).

553. [redacted]. (Guerin-Calvert, Tr. 7433-7434, *in camera*).

3. Post-Joinder bargaining leverage

a. General terms relating to bargaining leverage

554. The rates and terms of the contracts that are negotiated by a hospital and an MCO are a function of the bargaining leverage that each party brings to bear in the negotiation. (Pirc, Tr. 2208; Radzialowski, Tr. 658-660; Shook, Tr. 978, *in camera*;

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PX01914 at 015 (Pirc, IHT at 53), *in camera* (“Q: Do the rates that are ultimately agreed upon in a negotiation between [MMO] and a given hospital depend on the relative bargaining leverage that [each has]? A: . . . That’s a primary factor, yes.”); Town, Tr. 3637, 3640-3641).

555. In an economic sense, “equilibrium” occurs within a bargaining framework when both parties to the negotiation conclude that they are better off with the deal than without the deal. (Town, Tr. 3846-3847).

556. The bargaining leverage of each party and, therefore, the terms of the agreement depend principally upon how each party evaluates how it would fare if it failed to enter into an agreement with the other party. In other words, each party considers the cost it would face if the negotiations failed. (PX02148 at 015-016 (¶ 26) (Town Expert Report), *in camera*; Town, Tr. 3641-3642; Pirc, Tr. 2208-2211; Sandusky, Tr. 1323-1324; Wachsman, Tr. 5123-5126).

557. A hospital’s bargaining leverage with an MCO depends on how much the MCO perceives it would lose if the MCO failed to reach agreement with the hospital. (Town, Tr. 3641; Pirc, Tr. 2210-2211; Radzialowski, Tr. 665-666; Pugliese, Tr. 1458-1461).

558. The success or failure of a negotiation depends on the hospital’s and the MCO’s respective “walk-away” points. (PX02148 at 015-016 (¶ 26) (Town Expert Report), *in camera*; PX01914 at 015-016 (Pirc, IHT at 51-53), *in camera*; Radzialowski, Tr. 659-660).

559. If a hospital demands rates above an MCO’s walk-away point, the MCO will refuse to contract with the hospital. (PX02148 at 015-016 (¶ 26) (Town Expert Report), *in camera*; Radzialowski, Tr. 675-677; Pirc, Tr. 2207-2208; Sheridan, Tr. 6688).

560. If an MCO refuses to pay rates above a hospital’s walk-away point, the hospital will decline to contract with the

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MCO. (PX02148 at 015-016 (¶ 26) (Town Expert Report), *in camera*; Radzialowski, Tr. 675-677).

b. MCOs believe that the Joinder increases ProMedica's bargaining leverage

561. The addition of St. Luke's to ProMedica will give ProMedica more hospitals and greater geographic coverage in Lucas County, Ohio. (Pugliese, Tr. 1524-1525, *in camera*).

562. Pre-Joinder competition between St. Luke's and ProMedica's Lucas County hospitals benefited MCOs' members, because competition generally allowed MCOs to obtain lower rates. (Pirc, Tr. 2260-2261, *in camera*).

563. With respect to [redacted], the Joinder has given ProMedica increased bargaining leverage that allows ProMedica to obtain higher reimbursement rates from [redacted]. ([redacted], Tr. 1524-1525, *in camera*; PX01919 at 014 ([redacted], Dep. at 51), *in camera*).

564. With respect to MMO, [redacted]. A network with only Mercy and UTMC leaves a "hole" in southwest Lucas County. (Pirc, Tr. 2195, 2261-2263, *in camera*).

565. No MCO in at least the last ten years has offered a network comprised of only UTMC and Mercy. (JX00002A at ¶ 9; Response to RFA at ¶ 14). Respondent's expert agreed that a Mercy-UTMC network been never been used in the last twenty years. (Guerin-Calvert, Tr. 7895).

566. MCOs believe that a network consisting of only the Mercy Hospitals and UTMC, without St. Luke's or the other, pre-Joinder, ProMedica Hospitals, would not be sufficiently marketable in Lucas County to be commercially viable. (Radzialowski, Tr. 715-716, *in camera*; PX01917 at 020 (Radzialowski, Dep. at 75-76), *in camera* (Aetna); Pugliese, Tr. 1477-1478, *in camera* (Anthem); Pirc, Tr. 2261-2262, *in camera* (MMO); Sandusky, Tr. 1351, *in camera* (FrontPath); PX01902 at 018 (Sheridan, IHT at 63), *in camera* (United)).

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567. MCOs believe that a network consisting of only the Mercy Hospitals and UTMC, omitting St. Luke's and the other, pre-Joinder, ProMedica Hospitals, would not be sufficiently marketable in Lucas County to be commercially viable, even if offered at a lower price than a broad network, and that membership would decline. (Pugliese, Tr. 1577-1578 (Anthem); (Pirc, Tr. 2313, *in camera* (MMO); Sandusky, Tr. 1324 (FrontPath).

568. MMO believes that a network consisting of only the Mercy Hospitals and UTMC, without St. Luke's or the other, pre-Joinder ProMedica Hospitals, would not be sufficiently marketable in Lucas County to be commercially viable, in part, because it would require members in southwest Lucas County to travel too far to receive care. (Pirc, Tr. 2199-2200, 2262, *in camera* (MMO)).

569. MMO believes that [redacted]. (Pirc, Tr. 2261-2263, *in camera*; PX01944 at 027 (Pirc, Dep. at 103), *in camera*).

570. With respect to Aetna, the Joinder has made the prospect of walking away from ProMedica substantially more unattractive for Aetna because the attractiveness of Aetna's network would fall to a greater degree from the loss of not only ProMedica's three hospitals, but also from the loss of St. Luke's, which would leave Aetna without coverage in southwestern Lucas County because Mercy does not have a hospital there. (Radzialowski, Tr. 712-713, *in camera*; PX01917 at 020, 023 (Radzialowski, Dep. at 75-76, 86), *in camera*).

571. With respect to FrontPath, ProMedica is a "significant" provider and FrontPath's business "would suffer significantly" from the absence of ProMedica from FrontPath's network. (Sandusky, Tr. 1323-1324).

572. FrontPath could not viably market a network consisting only of Mercy and UTMC, as it would account for [redacted] percent of FrontPath's current utilization in Lucas County. (Sandusky, Tr. 1351, *in camera*).

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573. With respect to Humana, the Joinder increased ProMedica's "ability to leverage us [Humana] for rates for all of their hospitals and St. Luke's now as well." (McGinty, Tr. 1209; PX02073 at 003 (¶ 11) (McGinty, Decl.), *in camera*).

574. With respect to [redacted], "ProMedica would find its bargaining power greater after the acquisition than before[.]" ([redacted], Tr. 6698-6700, *in camera*). [redacted] would face more difficulty serving its membership without ProMedica and St. Luke's than it would without ProMedica's pre-Joinder hospital network in Lucas County. ([redacted], Tr. 6687).

575. Prior to entering into a contract with ProMedica [redacted] failed to grow its membership in Toledo by marketing a network that consisted of only Mercy, UTMC, and St. Luke's. ([redacted], Tr. 6691-6693, *in camera*). If ProMedica did not rejoin the [redacted] network, [redacted]. ([redacted], Tr. 6693, *in camera*).

c. Walk-away networks

576. Prior to the Joinder, the MCOs' "walk-away" network with respect to St. Luke's, *i.e.*, the network they had if they failed to reach agreement with St. Luke's in a negotiation, consisted of ProMedica's Lucas County hospitals, Mercy's Lucas County hospitals, and UTMC. (Town, Tr. 3660-3661).

577. Prior to the Joinder, the MCOs' "walk-away" network with respect to ProMedica's Lucas County hospitals, *i.e.*, the network they had if they failed to reach agreement with ProMedica, consisted of St. Luke's, Mercy's Lucas County hospitals, and UTMC. (Town, Tr. 3656-3657).

578. As a result of the Joinder, the MCOs' "walk-away" network with respect to ProMedica's Lucas County hospitals, which now includes St. Luke's, is Mercy's Lucas County hospitals and UTMC. (Town, Tr. 3656-3658; PX02067 at 004, 006 (¶¶ 13, 21) (Radzialowski, Decl.), *in camera*; PX02073 at 004 (¶ 15) (McGinty, Decl.), *in camera*; see PX02148 at 064-065 (¶ 116) (Town Expert Report), *in camera*).

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579. Because St. Luke's is valued by health plan members, an MCO's failure to contract with ProMedica after the Joinder will be more costly for the MCO, because their walk-away network must exclude both St. Luke's and ProMedica's Lucas County hospitals, and becomes significantly less valuable than a network that excludes only ProMedica. (Town, Tr. 3657-3659; Radzialowski, Tr. 664-665, 715-716, *in camera*; McGinty, Tr. 1201; Sandusky, Tr. 1312-1313, 1351, *in camera*; Pugliese, Tr. 1477-1478, 1481-1482, *in camera*; Pirc, Tr. 2201-2203, 2262-2263, *in camera*).

580. Because ProMedica's Lucas County hospitals are valued by health plan members, an MCO's failure to contract with St. Luke's has become much more costly for an MCO as a result of the Joinder, because their walk-away network must exclude both St. Luke's and ProMedica's Lucas County hospitals, and is less valuable than a network that excludes only St. Luke's. (Town, Tr. 3660-3663; *see* Sheridan, Tr. 6693, *in camera*; Pirc, Tr. 2262, *in camera*; Radzialowski, Tr. 715-716, *in camera*; McGinty, Tr. 1201; Sandusky, Tr. 1348-1349, 1351, *in camera*; Pugliese, Tr. 1477-1478, 1523-1525, *in camera*).

581. A post-Joinder ProMedica, with St. Luke's in its system, has more bargaining leverage than ProMedica without St. Luke's in its system. (Radzialowski, Tr. 712-713, *in camera*; McGinty, Tr. 1209-1210; Pugliese, Tr. 1523-1525, *in camera*; *see also* Neal, Tr. 2111; Pirc, Tr. 2262-2263, *in camera*).

582. A post-Joinder ProMedica, with St. Luke's in its system, has more bargaining leverage than ProMedica without St. Luke's in its system, in part because a network without ProMedica or St. Luke's would leave no non-ProMedica alternatives in southwest Lucas County. (Radzialowski, Tr. 713-714, *in camera*; Pirc, Tr. 2195; *see also* Neal, Tr. 2168).

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4. Likelihood of post-Joinder price increases

a. MCOs believe that the Joinder will likely lead to higher rates

583. The Joinder will likely lead to higher health-care costs because St. Luke's has been absorbed into a larger health-care system, ProMedica, with a great deal of leverage that ProMedica can exercise during the contract negotiation process. (Pugliese, Tr. 1524-1525, *in camera*).

584. Prior to the Joinder, the reimbursement rates that [redacted] paid to St. Luke's were "competitive" with (*i.e.*, comparable to) the rates that [redacted] paid to other community hospitals in Ohio and were "significantly lower" than the rates [redacted] paid to ProMedica's community hospitals, Flower and Bay Park. ([redacted], Tr. 1505-1506, *in camera*).

585. Anthem is concerned that ProMedica will raise the rates that Anthem pays to St. Luke's closer to the rates that Anthem pays to ProMedica's community hospitals in Lucas County. (Pugliese, Tr. 1517, *in camera*).

586. [redacted] conducted an analysis of the change in reimbursements to St. Luke's that would result if [redacted] rates to St. Luke's were increased to equal [redacted] rates to ProMedica's Flower, Bay Park, and TTH. ([redacted], Tr. 1506-1508, *in camera*; PX02380, *in camera*). According to that analysis, if ProMedica brings [redacted] rates to St. Luke's in line with [redacted] rates to Flower and Bay Park, [redacted] rates to St. Luke's will "increase significantly," between roughly [redacted] and [redacted] percent. ([redacted], Tr. 1517-1519, *in camera*; PX02380, *in camera*).

587. Prior to the Joinder, competition between St. Luke's and ProMedica's Lucas County hospitals benefited MMO's members, because competition generally allows MMO to obtain lower rates. (Pirc, Tr. 2260-2261, *in camera*).

588. [redacted] believes that acquiring St. Luke's allows ProMedica to "demand their price" – that is, to seek

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“extraordinary” reimbursement rates for inpatient services. ([redacted], Tr. 2261-2262, *in camera*; PX01944 at 013-014 ([redacted], Dep. at 49-50, *in camera*)).

589. Aetna believes that ProMedica’s additional leverage from the Joinder gives ProMedica the ability to raise the reimbursement rates that Aetna pays both to St. Luke’s and to ProMedica’s other Lucas County hospitals. (Radzialowski, Tr. 712-713, *in camera*).

590. Aetna expects that ProMedica, as a first step, will increase Aetna’s rates to St. Luke’s to the level of Aetna’s rates to ProMedica and, as a second step, will use the additional leverage it gained from the Joinder to raise rates even further. (PX01938 at 023 (Radzialowski, Dep. at 88-89), *in camera*).

591. In 2010, Aetna performed an analysis in October 2010 of the Joinder’s impact on Aetna’s rates to St. Luke’s. This analysis was based on costs in Aetna’s different contracts and on the typical pattern experienced by Aetna, that the acquiring system would raise the acquired hospital’s rates to the system-wide rates. Aetna’s analysis projected a [redacted] percent increase in Aetna’s rates to St. Luke’s if these were to rise to the level of Aetna’s rates to ProMedica, accounting for differences of variation and severity between ProMedica and St. Luke’s. (Radzialowski, Tr. 704, *in camera*, 848-49; *see also* PX01938 at 026 (Radzialowski, Dep. at 99), *in camera*).

592. Aetna believes that the actual impact on rates could be higher, because its analysis did not account for the additional bargaining leverage that the Joinder gave to ProMedica as a whole. (Radzialowski, Tr. 843, *in camera*; *see also* PX01938 at 023 (Radzialowski, Dep. at 89), *in camera*).

593. In early [redacted], ProMedica asked [redacted] to increase St. Luke’s reimbursement rates to the level of those paid to ProMedica. ([redacted], Tr. 717, *in camera*).

594. Prior to the Joinder, Humana used its negotiated rates with St. Luke’s as a benchmark in negotiations with ProMedica. The Joinder eliminated Humana’s ability to leverage St. Luke’s

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independence against ProMedica and increased ProMedica's "ability to leverage us [Humana] for rates for all of their hospitals and St. Luke's now as well." (McGinty, Tr. 1209; PX02073 at 003 (¶ 11) (McGinty, Decl.), *in camera*).

595. After the Joinder was announced, [redacted] expected that rates at St. Luke's would likely increase because "ProMedica's rate structure [redacted] was so substantially higher than St. Luke's to begin with" and because [redacted] believed that "ProMedica would find its bargaining power greater after the acquisition than before[.]" ([redacted], Tr. 6698-6700, *in camera*; PX01902 at 018 ([redacted], IHT at 62), *in camera*).

596. MCO representatives testified that their firms would have little choice but to pass on any rate increases at St. Luke's or ProMedica's hospitals after the Joinder to both the MCOs' self-insured and fully-insured members. (Pugliese, Tr. 1554; Pirc, Tr. 2174; PX01944 at 020 (Pirc, Dep. at 76), *in camera*; Radzialowski, Tr. 779; Sandusky, Tr. 1296; McGinty Tr. 1210-1211; PX02073 at 004 (¶ 16) (McGinty, Decl.), *in camera*; Sheridan, Tr. 6701, *in camera*; PX01900 at 011 (Mullins, IHT at 39-40), *in camera*).

b. St. Luke's anticipated its rates to increase to ProMedica's rates

597. A St. Luke's planning document, dated August 10, 2009, notes that an option for St. Luke's would be to "enter[] into an affiliation/partnership with a local health system with the express purpose to raise reimbursement rates to the level of our competitors." (PX01390 at 002; Wakeman, Tr. 2640, 2643, *in camera*).

598. A 2009 presentation regarding potential affiliation partners, made to St. Luke's Hospital ("SLH") Board of Directors by Mr. Wakeman and other members of St. Luke's leadership team, states: "An SLH affiliation with ProMedica has the greatest potential for higher hospital rates. A ProMedica-SLH partnership would have a lot of negotiating clout." (PX01030 at 020, *in camera*; Wakeman, Tr. 2689-2690, *in camera*; Black, Tr. 5634, *in camera*). This statement conveyed the belief that

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“ProMedica had a significant leverage on negotiations with some of the [health plans],” that this leverage would allow St. Luke’s to obtain higher reimbursement rates, and that an affiliation with ProMedica could, in the short term, “[h]arm the community by forcing higher hospital rates on them.” (Wakeman, Tr. 2698-2700, *in camera*; Rupley, Tr. 2003, *in camera* (discussing PX01124 at 009, which contains the contents of PX01030 at 020)).

599. Members of St. Luke’s due diligence team, who were in charge of finding the best affiliation options for St. Luke’s, expressed their belief that a ProMedica or Mercy affiliation could “stick it to employers, that is, to continue forcing high rates on employers and insurance companies” and thereby perpetuate high health-care costs in the area. (PX01130 at 005), *in camera*; Rupley, Tr. 2013-2014, *in camera*).

600. St. Luke’s believed that among the advantages of a joinder with ProMedica was the ability to increase St. Luke’s reimbursement rates. (Wakeman, Tr. 2685-2686; PX01125 at 002, *in camera* (noting the advantage of ProMedica’s “strong market/capital position” and St. Luke’s resulting “incredible access to outstanding pricing on managed care agreements”); *see also* PX01018 at 014 (Options for St. Luke’s: St. Luke’s is now at a cross-roads), *in camera*, stating: “Option 3: Affiliate with ProMedica. What do they bring? Strong managed care contracts.”).

601. Mr. Wakeman hoped that an affiliation with ProMedica would allow St. Luke’s to obtain the higher reimbursement rates that ProMedica was receiving. (Wakeman, Tr. 2685-2686, *in camera*).

602. St. Luke’s recognized prior to the Joinder that “an independent St. Luke’s Hospital keeps the systems a little more honest” and that “MCOs lose clout if St. Luke’s is no longer independent.” (PX01144 at 003).

603. St. Luke’s anticipated as much as [redacted] in additional revenues from MMO, Anthem, and Paramount as a result of joining ProMedica. (PX01231, *in camera* (“Yes we

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asked [redacted] for [redacted], but if we go over to the dark green side [*i.e.*, ProMedica] ... we may pick up as much as [redacted] in additional [redacted] and Paramount fees’’)).

c. Correlation between market power and pricing

604. Prior to the Joinder, ProMedica acknowledged its market dominance in Lucas County in its ordinary course of business documents. A Standard & Poor’s credit presentation stated: “ProMedica Health System has market dominance in the Toledo MSA.” (PX00270 at 025; *see also* Oostra, Tr. 5964-5965, 5973-5974). In a “strengths, weaknesses, opportunities and threats” (“SWOT”) analysis, ProMedica listed its “[d]ominant market share” as a strength. (PX00319 at 001 (“TTH Medical Executive Committee SWOT Analysis Results 2007’’)).

605. Using Respondent’s expert’s calculations, the Joinder increased ProMedica’s shares in the market for GAC inpatient services anywhere from 42 to 49 percent pre-acquisition to 53 to 58 percent post-acquisition. *See* F. 357-360.

606. Prior to the Joinder, ProMedica had the highest market shares for GAC inpatient services and the highest prices in Lucas County. (PX02148 at 143 (Ex. 6), 145 (Ex. 7) (Town Expert Report).

607. Professor Town utilized a case-mix adjustment to analyze hospital prices. A case-mix adjustment controls for variation in case-mix, severity, and patient demographics across hospitals, and to allow for an apples-to-apples comparison of prices. PX02148 at 037 (¶68, n. 107) (Town Expert Report), *in camera*; Town, Tr. 3722-3725, *in camera*).

608. Case-mix adjustment is a concept that tries to compare patient volumes at different hospitals when patients have different severities of illness. It is a calculation that takes into account the resources needed to treat patients, with the theory being that patients with more complicated illnesses utilize more resources than those who are not as ill. The methodology is tied to the DRG reimbursements. Thus, the case-mix adjustment number is

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a weighted factor used by MCOs to make an apples-to-apples comparison between various rates at each hospital. (Radzialowksi, Tr. 684, 687-688, 698-700, *in camera*, 848-849; Sandusky, Tr. 1338-1348, 1350, *in camera*; *see* Pugliese, Tr. 1512-1513, *in camera*; Wakeman, Tr. 3036-3037; Pirc, Tr. 2238-2242, *in camera*).

609. Professor Town's examination of hospital prices in Lucas County prior to the Joinder demonstrates that ProMedica's average price was [redacted] percent higher than Mercy's, [redacted] percent higher than UTMC's, and [redacted] percent higher than St. Luke's. (PX02148 at 037 (¶ 68), 145 (Ex. 7) (Town Expert Report), *in camera*).

610. Professor Town's examination of hospital prices and market shares in Lucas County prior to the Joinder demonstrates a high correlation between market shares and prices. ProMedica, the system with the highest market share, had the highest prices. Mercy, the system with the second-highest share, had the second-highest prices. UTMC, with the third-highest share, had the third-highest prices and St. Luke's, with the smallest share, had the lowest prices. (PX02148 at 039 (¶ 71), 147 (Ex. 8) (Town Expert Report), *in camera*).

611. MCOs confirmed Professor Town's analysis of the relative price difference between ProMedica and St. Luke's by testifying that ProMedica's rates are the highest and St. Luke's rates are the lowest in Lucas County. (Pirc, Tr. 2238-2242, *in camera*; Radzialowski, Tr. 684, 687-688, 698-700, *in camera*; Sandusky, Tr. 1338-1348, 1350, *in camera*; PX02296 at 001, *in camera*; *see* Pugliese, Tr. 1512-1513, *in camera*; McGinty, Tr. 1210).

d. Professor Town's econometric model

612. Complaint Counsel's expert, Professor Town, utilized an econometric, or merger simulation model, called the "willingness to pay" model, to try to predict what the change in price would be to MCOs from the Joinder. (Guerin-Calvert, Tr. 7485-7486).

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613. The willingness to pay model is a method that economists use to quantify bargaining leverage. It measures the incremental value consumers place on having access to a hospital or system given the availability of alternative hospitals. The more important it is to an MCO to have a hospital in its network, the more an MCO will be willing to pay to have that hospital in-network. (Town, 3655, 3798-3799, *in camera*, 3861-3862; PX02148 at 103 (Technical Appendix ¶ 11) (Town Expert Report), *in camera*).

614. The willingness to pay model is not a tool to forecast prices into future years. Rather, the willingness to pay model is a tool to predict the effect of the elimination of competition on prices; that is, to isolate and quantify the Joinder's impact on the bargaining leverage of the merged hospitals. (Town, Tr. 3883).

615. Professor Town used five steps in the willingness to pay model to calculate price changes that will likely result from the Joinder: (1) measure price; (2) measure bargaining power; (3) determine the impact of bargaining power on price; (4) estimate the increase in bargaining power on price; and (5) calculate the price impact of the Joinder. (PX02148 at 103 (Town Expert Report), *in camera*). At each step, there are a series of calculations. Put simply, step one identifies price differences that exist and creates a database; steps two and three try to explain the price differences and isolate the factors that the Joinder changes; and steps four and five measure the effect of the Joinder. (Guerin-Calvert, Tr. 7487-7488). These five steps are described in greater detail in F. 616-621 below.

616. In step one of the willingness to pay model, Professor Town used MCO data for discharges at greater Toledo area hospitals from January 1, 2004 through December 31, 2009, which includes inpatient discharges from Aetna, Anthem, BCBS of Michigan, MMO, FrontPath, Paramount, Cigna and United. Professor Town used the average case-mix-adjusted hospital prices to control for differences in age, gender, diagnostic code, and length of stay. (Town, Tr. 3722-3723, *in camera*, 4205; PX02148 at 103-105) (Town Expert Report), *in camera*; Guerin-Calvert, Tr. 7488; Town, Tr. 4208-4209).

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617. Professor Town excluded all discharges from hospitals outside of Lucas County, except WCH and FCHC; data for managed care organization/hospital-year combinations for which there were fewer than 30 discharges; discharges for Medicare Advantage patients; discharges coded MDC 0, 19, 20 and -1⁸; discharges in which the amount paid to the hospital by the MCO was less than \$100; and 2004 discharges reimbursed by Aetna and CIGNA. (Town, Tr. 4210-4212). Professor Town then used the remaining data to run a regression that shows the difference in prices between hospitals, but not any hospital-specific factors that account for any of these differences in the hospital prices. (Town, Tr. 4212-4215).

618. In step two of the willingness to pay model, Professor Town measured the bargaining power possessed by each hospital in its price negotiations with each payer. These measures of bargaining power, called “willingness to pay,” are determined using inpatient discharge data and reflect the value-added that patients place upon having in-network access to a hospital, given the other hospitals that are already in the network, and thus measure the incremental importance of the hospital to the MCO. (Town, Tr. 4206; PX02148 at 105-108 (Town Expert Report), *in camera*; Guerin-Calvert, Tr. 7485-7486, 7489-7490).

619. In step three of the willingness to pay model, Professor Town determined the impact of bargaining power on price by using the average case-mix adjusted inpatient prices and the hospital willingness to pay measures to assess the relationship between willingness to pay and the price of inpatient care. Professor Town then used his predicted prices and his willingness to pay measures, controlling for other factors including an MCO’s size, year fixed effects, MCO fixed effects, interns per bed and average cost in the regression. (Town, Tr. 4206; PX02148 at 108-109) (Town Expert Report), *in camera*; Guerin-Calvert, Tr. 7492-7493).

⁸ These MDC categories correspond to missing/invalid, pre-MDC, mental diseases and disorders, and alcohol and drug-induced disorders, respectively. (Town, Tr. 4027-4028). Professor Town dropped these categories because the services within each do not qualify as GAC inpatient services. (Town, Tr. 4027-4028).

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620. In step four of the willingness to pay model, Professor Town estimated the increase in bargaining power resulting from the Joinder by calculating the willingness to pay induced by the Joinder. To do this, Professor Town incorporated St. Luke's as the fourth hospital in ProMedica's Lucas County network and recalculated the willingness to pay for ProMedica. (PX02148 at 104 (Technical Appendix ¶ 14) (Town Expert Report), *in camera*; Town, Tr. 4204, 4285).

621. In step five of the willingness to pay model, Professor Town calculated the price impact of the Joinder by using the estimated relationship between willingness to pay and inpatient rates, along with the change in willingness to pay resulting from the Joinder, to calculate the likely impact of the Joinder on the price of inpatient care. (PX02148 at 104 (Technical Appendix ¶ 14) (Town Expert Report), *in camera*); Town, Tr. 4206).

622. Professor Town's analysis of willingness to pay shows that, before the Joinder, MCOs' consumers placed 22 percent more value on having in-network access to ProMedica than to Mercy's Lucas County hospitals. (PX02148 at 066 (¶ 118), 165 (Ex. 13) (Town Expert Report), *in camera*).

623. Professor Town's analysis of willingness to pay shows that the Joinder has increased MCOs' willingness to pay for ProMedica by 50 percent. (PX02148 at 066 (¶ 118), 165 (Ex. 13) (Town Expert Report), *in camera*).

624. Professor Town's analysis of willingness to pay demonstrates that the Joinder has increased ProMedica's bargaining leverage by 13.5 percent. (PX02148 at 066 (¶ 118), 165 (Ex. 13) (Town Expert Report), *in camera*).

625. Professor Town's willingness to pay model predicts that the volume-weighted average (across ProMedica and St. Luke's) price will increase by 16.2 percent. (PX02148 at 110 (¶ 33) (Town Expert Report), *in camera*); Guerin-Calvert, Tr. 7495-7496).

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626. Respondent's expert, Ms. Guerin-Calvert took Professor Town's willingness to pay model that predicted a price increase of 16.2 percent, added five variables to it, and predicted a price increase of 7.3 percent. (RX71(A) at 000080-000081; Guerin-Calvert, Tr. 7525-7526, 7928; RRCCFF 1185 ("Ms. Guerin-Calvert is estimating a price increase of 7.3 percent.")).

627. Professor Town's willingness to pay model also uses diversion ratios to allocate proportions of harm between ProMedica and St. Luke's by taking allocated harm attributed to St. Luke's to compare it to St. Luke's existing pre-Joinder rates and calculating the percentage change. (PX02148 at 110 (Town Expert Report), *in camera*; Guerin-Calvert, Tr. 7495-7497).

628. Professor Town's willingness to pay merger simulation model predicts that inpatient reimbursement rates paid by third-party MCOs to ProMedica will increase by 10.8 percent and that inpatient reimbursement rates paid by third-party MCOs to St. Luke's will increase by between 38.4 percent and 56.2 percent. (PX02148 at 101, 110 (Town Expert Report), *in camera*; Guerin-Calvert, Tr. 7497).

629. Professor Town finds that even if St. Luke's pre-Joinder rates had been higher, the willingness to pay merger simulation model predicts that the Joinder will still lead to significant rate increases for St. Luke's, ranging from 33.2 percent to 48.6 percent, and that 33.2 percent of this increase is due solely to the Joinder's elimination of competition and that the incremental 15.4 percent is due solely to St. Luke's enjoying ProMedica's unique price-influencing characteristics. (PX02148 at 102 (¶ 6) (Town Expert Report), *in camera*).

630. Professor Town's merger simulation results are consistent with the testimony from MCOs. (PX01850 at 060 (¶ 92) (Town Rebuttal Report), *in camera*).

631. Professor Town's merger simulation results are consistent with the high concentration in the undisputed relevant geographic market in this matter. (PX01850 at 060 (¶ 92) (Town Rebuttal Report), *in camera*).

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632. Professor Town's merger simulation results are consistent with the existing academic literature which shows that hospital mergers in highly concentrated markets typically lead to significant price increases. (PX02148 at 111 (Technical Appendix ¶ 37) (Town Expert Report), *in camera*).

633. The willingness to pay model has been peer-reviewed and published in two prestigious economics journals. (PX01850 at 059 (¶ 91) (Town Rebuttal Report), *in camera*).

634. The willingness to pay model is consistent with the standard economic theory on mergers in differentiated products markets described in the Merger Guidelines. (PX01850 at 062 (¶ 94) (Town Rebuttal Report), *in camera*).

5. ProMedica's aim of increasing rates

a. ProMedica's reimbursement rates

635. ProMedica seeks to maximize its revenues and its reimbursement rates from commercial MCOs. (Wachsman, Tr. 5145-5146, *in camera*; PX01906 at 066 (Oostra, IHT at 259-260), *in camera*).

636. ProMedica seeks to obtain reimbursement rates from MCOs that [redacted]. (RX1854 at 000005, *in camera*; Wachsman, Tr. 4949-4950, 5140, *in camera*).

637. ProMedica's cost coverage ratios for significant third-party, commercial MCOs range from [redacted] to [redacted]. ProMedica's aggregate cost coverage ratio for all commercial payors in 2009 was close to [redacted] percent. (PX00233 at 001 (ProMedica's Annualized Cost Coverage Ratios for 2009), *in camera*; PX01927 at 010 (Wachsman, Dep. at 35-36), *in camera*).

638. ProMedica's internal analyses show that its average cost coverage ratio for third-party commercial MCOs was higher than the [redacted] percent target in 2009 and 2010, exceeding [redacted] percent in June 2010. (Wachsman, Tr. 5141-5143, *in camera*; PX00233 at 001 (ProMedica's Annualized Cost

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Coverage Ratios for 2009), *in camera*; PX00443 at 002 (ProMedica's Cost Coverage Ratios for YTD June 2010), *in camera*).

639. ProMedica seeks to achieve a positive operating margin, *i.e.*, the relationship of operating income to revenues, for its hospitals, continuing care service entities, long-term care services entities, and ProMedica's home health entity, of about [redacted] percent, or an overall cost coverage ratio of [redacted] percent. (RX1854 at 00005, *in camera*; Hanley, Tr. 4505-4506, 4582).

640. ProMedica's operating margin is significantly above the [redacted] percent target for the system as a whole, which includes operations that lose money or have low margins. (PX01947 at 012 (Oostra, Dep. at 39), *in camera*).

641. ProMedica's operating margin through September 30, 2010 was [redacted] percent, which is above the [redacted] percent target, and a fact significant enough to be presented by ProMedica to investors in January 2011. (PX00532 at 005 (ProMedica Investor Presentation); PX01947 at 012 (Oostra, Dep. at 38-39), *in camera*).

b. Post-Joinder pricing

642. ProMedica negotiated a new contract with United, on behalf of St. Luke's, to be effective January 1, 2011. (Guerin-Calvert, Tr. 7432-7433, *in camera*).

643. In the first year of the new contract with United, St. Luke's rates increased approximately [redacted] percent; in the second year, rates increased [redacted] percent, for a total of about a [redacted] percent increase over [redacted] years. (Guerin-Calvert, Tr. 7432-7433, *in camera*).

644. ProMedica informed United that it had the right to continue its existing contract with St. Luke's while the Hold Separate Agreement was in effect. (Wachsman, Tr. 5074, 5227-5228, *in camera*; RX759).

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645. United negotiated these rates even though it could have chosen to keep St. Luke's rates as they were until this litigation was resolved. (Guerin-Calvert, Tr. 7433, *in camera*).

646. ProMedica has not sought to terminate St. Luke's contract with Anthem since the Joinder. (Pugliese, Tr. 1584).

647. Since the Joinder, ProMedica has not sought to modify any of St. Luke's rates to be comparable to the rates that ProMedica is presently getting from Anthem for any of its hospitals. (Pugliese, Tr. 1583-1584).

648. MMO and ProMedica negotiated a new contract for St. Luke's between November 2010 and January 2011. (Pirc, Tr. 2249-2250, *in camera*).

649. The final agreement reached between MMO and ProMedica for St. Luke's provided for [redacted] percent rate increases in 2011 and 2012. In 2013, increases would be [redacted] and in 2014, rates would increase by [redacted] percent. (PX02385 at 032-034, *in camera*; Wachsmann, Tr. 5064, *in camera*). The contract to which MMO and ProMedica agreed for St. Luke's [redacted]. (Pirc, Tr. 2251, *in camera*; PX02385 at 032-034, *in camera*).

650. The contract to which MMO and ProMedica agreed for St. Luke's resulted in a [redacted] percent increase in payments to St. Luke's for the 2009 to 2012 time period. (Guerin-Calvert, Tr. 7429-7430, *in camera*).

6. Costs to employers and employees

651. Employers cite health-care costs as one of their largest expenses. (Caumartin, Tr. 1846-1847 (health insurance is a "very significant" expense); Buehrer, Tr. 3073 (health insurance is the "second highest expense behind payroll"); Neal, Tr. 2118 (health-care is "the largest fixed cost for [Chrysler's] bargaining unit employees when we negotiate a collective bargaining agreement with the UAW"); Lortz, Tr. 1707-1708 ("health care is one of the big pieces" in collective bargaining)).

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652. Inpatient care is a significant contributor to the cost of health-care, although there are many other factors that affect or influence the cost of medical coverage including: the cost of outpatient services, physician services, and ancillary services; the number of employees and family members covered; the benefit design offering; the demographic mix and health history of covered members; prescription drug usage trend; and employees' utilization rate. (Lortz, Tr. 1733-1735; Neal, Tr. 2121-2122, 2140-2142; Caumartin, Tr. 1867, 1872; Buehrer, Tr. 3084-3086; Pugliese, Tr. 1561-1562; McGinty, Tr. 1246-1247; Pirc, Tr. 2292-2294; Town, Tr. 3949-3952).

653. The cost of GAC inpatient hospital services accounts for approximately 20 to 25 percent of the amount of health insurance premiums; the cost of outpatient services, including imaging services and durable medical equipment, accounts for approximately 15 to 30 percent; physician costs account for approximately 25 to 30 percent; and pharmacy costs account for approximately 10 to 15 percent, with administrative fees comprising the remainder. (Pirc, Tr. 2292; Randolph, Tr. 6918-6920).

a. Self-insured employers

654. Unlike fully-insured employers who pay fixed monthly premiums to MCOs, self-insured employers pay the full cost of their employees' health-care. (F. 50-51). Thus, increases in hospital reimbursement rates impact self-insured employers directly. (Sandusky, Tr. 1296; McGinty, Tr. 1243-1244; Radzialowski, Tr. 625-626, 840-841, *in camera* ("Local employers ... [whose] members receive services at St. Luke's, especially the self-insured employers, would feel a direct impact from unexpected [rate] increases."); Town, Tr. 3612-3613; PX02148 at 011-013 (¶ 18) (Town Expert Report), *in camera*).

655. Respondent admits that, for its health insurance subsidiary Paramount, "if the reimbursement rate Paramount pays to hospitals changes, that change is ultimately passed on to the self-insured customer because self-insured customers pay their own claims. ... [A]ny reimbursement rate change affects

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self-insured customers on the effective date of the new contract between Paramount and a hospital.” (Response to RFA at ¶ 35).

656. If St. Luke’s rates increased post-Joinder and self-insured employers’ “volume stayed the same, they would pay higher costs per unit.” (Wakeman, Tr. 2687, *in camera*).

657. If a Lucas County hospital or hospital system increases its rates to commercial MCOs, those increased costs are “passed on straightforward” to self-insured employers. (Oostra, Tr. 6144).

658. In Lucas County, a large proportion of MCO commercial insurance business is with self-insured employers. (F. 134, 154, 169, 185-186, 216, 229).

b. Fully-insured employers

659. For fully-insured employers, where the employer pays a premium to an MCO and the MCO pays the costs of medical care received by employees, when an MCO incurs a rate increase from a hospital, it will pass down the increased costs to employers in the form of higher premiums. (Buehrer, Tr. 3063, 3086; Radzialowski, Tr. 625-626, 779; PX01938 at 030 (Radzialowski, Dep. at 114) (“With the fully insured, I can’t see any circumstance where we would not automatically pass [a rate increase] on through the premium increase.”); *in camera*; Pugliese, Tr. 1558, 1559-1560; PX01942 at 025 (Pugliese, Dep. at 94), *in camera*; McGinty, Tr. 1210, 1242-1243; Pirc, Tr. 2174; PX01944 at 020 (Pirc, Dep. at 76), *in camera*; Sheridan, Tr. 6701-6702, *in camera*; Town, Tr. 3614; PX02148 at 011-013 (¶ 18) (Town Expert Report), *in camera*).

660. Jack Randolph, the President of Paramount, ProMedica’s health insurance subsidiary, acknowledged that when Paramount has to pay increased reimbursement rates to providers, at some point, it has to pass on those increased costs to its customers. (Randolph, Tr. 7108-7109).

661. When advising the St. Luke’s Board regarding possible affiliation with ProMedica, St. Luke’s CEO assumed that

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if St. Luke's rates increased to MCOs, the MCOs would pass those increases on to the employers and the community. (Wakeman, Tr. 2687, *in camera*).

c. Employees

662. When health-care costs increase, some employers might absorb the increase, if they are in a position to do so; but more typically, employers will be required to reduce their costs by restricting health benefits or by increasing the employees' share contributions, via increased premium share, copays, deductibles, out-of-pocket maximums, or otherwise revise compensation or benefits to reduce employer costs. (Neal, Tr. 2114-2117, 2158; Buehrer, Tr. 3072, 3064-3066; Caumartin, Tr. 1837; Lortz, Tr. 1713; Pugliese, Tr. 1559-1560; Radzialowski, Tr. 782; Town, Tr. 3614; PX02148 at 011-013 (¶ 18) (Town Expert Report), *in camera*).

663. When costs for employee health insurance coverage increase for employers with union members, in order to offset the increased costs, employers may seek a collective bargaining agreement that will reduce service levels, increase the amount the union members must pay, reduce wages, or make other tradeoffs. (Lortz, Tr. 1706-1707, 1711-1713; Neal, Tr. 2118).

7. Constraints on price increases

a. Excess hospital bed capacity

664. There were approximately 2,200 staffed beds in Lucas County hospitals in 2009. (Guerin-Calvert, Tr. 7276; *see* F. 55, n.1).

665. All hospitals in Lucas County, except Bay Park, have many more registered beds than staffed beds ("beds-in-use"). (Guerin-Calvert, Tr. 7276-7277, 7283-7284; RX71(A) at 000208, *in camera*; F. 55, n.1).

666. MCO configurations in the past have excluded about 40 percent to 50 percent of the bed capacity in the market at any point in time. (Guerin-Calvert, Tr. 7277-7278).

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667. Mercy believes that, from a community need standpoint, all of St. Luke's beds could be eliminated from the Toledo area and not be missed. (PX02288 at 002-003 (¶ 5), *in camera*; Shook, Tr. 1112, *in camera*).

668. Based upon the number of staffed beds per thousand area residents, which is a standard metric used in health-care, the Toledo metropolitan area, as compared to other similar metropolitan areas in the United States, has substantially more beds per thousand residents. (Guerin-Calvert, Tr. 7278-7279).

669. Toledo has 3.63 beds per thousand residents, while Grand Rapids, Michigan, an area similar to Toledo, has just over 2 beds per thousand residents, and Detroit has approximately 2.5 beds per thousand residents. (Guerin-Calvert, Tr. 7279-7283; RX71(A) at 000150, *in camera*).

670. The number of staffed beds per thousand residents ratio indicates that there are more beds than patients in Toledo, and is a measure of excess capacity. (Guerin-Calvert, Tr. 7278-7279, 7283).

671. The number of registered beds greater than staffed beds indicates the number of beds that are not being deployed to meet patient demand, and therefore is also an indicator of excess capacity. (Guerin-Calvert, Tr. 7283-7284).

672. With the exception of Bay Park, the majority of Lucas County hospitals have numbers of staffed beds that are well under their registered beds. This indicates that hospitals have adjusted to a decline in demand for inpatient hospital services by reducing their staffing levels. (Guerin-Calvert, Tr. 7276-7278).

673. Hospitals could make use of registered, but unused, beds and accommodate any increase in demand, to the extent they can provide the level of staffing required for those registered beds. (Guerin-Calvert, Tr. 7276-7277, 7279, 7283-7284; Shook, Tr. 1042).

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674. ProMedica has no plans to eliminate or reduce bed capacity as a result of the Joinder. (Guerin-Calvert, Tr. 7762-7763).

675. Another metric of excess capacity for Toledo area hospitals is the occupancy rate, which divides the average daily census of a hospital by the number of staffed beds or registered beds. (Guerin-Calvert, Tr. 7284-7285).

676. Occupancy rates for hospital beds in Lucas County, based upon an average daily census of inpatient bed use, are significantly below available staffed bed capacity. (Guerin-Calvert, Tr. 7284-7286, 7289-7290; RX71(A) at 000208, *in camera*).

677. Low occupancy rates indicate that hospitals have the capacity to reposition to attempt to attract additional volume and to serve the patients. (Guerin-Calvert, Tr. 7286-7287).

678. Mercy's Toledo area hospitals could treat additional patients, but it would be limited to the number of beds that they could staff. (Shook, Tr. 1042).

679. If UTMC wanted to make use of more of its registered beds, it would have to convert and refurbish spaces that are now occupied by support services, such as vascular ultrasound, and find another location for those support services. (Gold, Tr. 199-200).

680. UTMC is currently renovating to convert all of its two-bed rooms to private, one-bed rooms, which will decrease available beds. (Gold, Tr. 224).

681. UTMC has no plans to increase its capacity in response to the Joinder. (Gold, Tr. 224).

b. Steering

682. "Steering" means providing incentives to patients or physicians to pursue health-care with specific providers. (Radzialowski, Tr. 723). "Hard" steerage means providing

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financial incentives to a member to go to a particular provider. “Soft” steerage is providing information to members and physicians to try to change where care is provided. (Radzialowski, Tr. 723-724).

683. In-network steering occurs when MCOs charge different prices to members for accessing in-network hospitals, based on the price the MCO pays to the hospital for its members’ inpatient care. (Town, Tr. 3809-3810, *in camera*).

(i) Physicians’ referrals

684. Admitting privileges allow a physician to admit and see patients, prescribe medications, and perform procedures at the hospital. (Andreshak, Tr. 1752).

685. Most physicians have privileges at multiple hospitals in Lucas County. (Gbur, Tr. 3105; RX35 at 006-007 (Hammerling, IHT at 16-18); Read Tr. 5274; Pugliese, Tr. 1466, 1573-1574).

686. Physicians obtain privileges at multiple hospitals for various reasons, including personal preference and convenience, access to adequate medical and surgical facilities to treat their patients, and for business reasons, such as the ability to cover for partners in their practice. (Andreshak, Tr. 1754-1755; Marlowe, Tr. 2428-2429).

687. Physicians also obtain privileges at multiple hospitals to respond to patient preferences and to serve patients whose health insurance plans or MCOs may not have certain hospitals in their networks. (Andreshak, Tr. 1754-1755, 1807; Marlowe, Tr. 2398; Read, Tr. 5268).

688. Physicians employed by a hospital system tend to admit patients to that hospital system. (Marlowe, Tr. 2393-2394; Beck, Tr. 400; Kordecki, Tr. 497-498; *see generally* Shook, Tr. at 1057).

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689. Employed physicians are expected to admit patients to the hospital system that employs the physician. (Pugliese, Tr. 1468).

690. Physicians consider various factors when choosing a hospital to admit their patients, including the physicians' preferences, patient preferences, insurance coverage, and location. (Gold, Tr. 205-206).

691. Having privileges at multiple hospitals allows a physician to direct a patient to an in-network hospital for treatment so the patient may minimize out-of-pocket expenses. (Andreshak, Tr. 1805-1807).

692. When deciding whether to admit a patient to a hospital, physicians consider whether the hospital is in-network for purposes of the patient's insurance coverage. However, physicians are not generally aware of hospital pricing. (Marlowe, Tr. 2417; Read, Tr. 5293; Andreshak, Tr. 1782-1783, 1805-1806, Gbur, Tr. 3105, 3107; PX01932 at 033 (Bazeley, Dep. at 127), *in camera*; PX01948 at 044-045 (Peron, Dep. at 166-167, 169-170), *in camera*).

693. Physicians are not aware of the rates that hospitals charge MCOs. (Gold, Tr. 206-207; Andreshak, Tr. 1782; Gbur, Tr. 3109; Marlowe, Tr. 2417; Read, Tr. 5293; *see also* Pirc, Tr. 2379, *in camera*; Pugliese, Tr. 1467-1468; Sandusky, Tr. 1325).

694. Physicians in Lucas County do not have access to contracts between MMO and Lucas County hospitals. (Pirc, Tr. 2378-2379, *in camera*).

695. Because physicians in Anthem's network are not party to the contracts that Anthem negotiates with hospitals in Lucas County, there is no apparent means by which physicians can routinely access the contracted hospital reimbursement rates. (Pugliese, Tr. 1467-1468).

696. Physicians are not aware of the rates that FrontPath has negotiated with the Lucas County hospitals. (Sandusky, Tr. 1325).

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697. Physicians are not sensitive to the rates hospitals charge MCOs. (Town, Tr. 3819, *in camera*).

(ii) MCO steering

698. MCOs currently place greater emphasis on open-access networks than they did prior to 2008, to meet what MCOs' believe to be member preferences for access to all Lucas County hospitals. (Radzialowski, Tr. 615, 657-658, Pugliese, Tr. 1544; PX02148 at 064 (¶ 121) (Town Expert Report)).

699. MCOs believe that patients do not like health plans steering them to particular hospitals. (Radzialowski, Tr. 657-658; Pugliese, Tr. 1465, 1544-1545; PX01917 at 018 (Radzialowski, Dep. at 68), *in camera*).

700. Higher-priced providers have displayed resistance to steering. Such resistance arises as part of contract discussions. Higher-priced hospitals resist steering because they may lose business. (Pugliese, Tr. 1466).

701. Some MCOs use pricing transparency programs to steer patients to lower-cost providers. (Wachsman, Tr. 5167, *in camera*).

702. MMO does not steer its members to use certain hospitals within MMO's network based on the reimbursement rates that MMO pays. (Pirc, Tr. 2213-2214; PX01944 at 019 (Pirc, Dep. at 72), *in camera*).

703. Mr. Pirc's sales staff had informed him of employer interest in steering options and he was told it would be helpful for sales if MMO developed this capability. (Pirc, Tr. 2307, *in camera*).

704. MMO has no plans to implement a program to steer members to certain in-network providers using financial incentives. (Pirc, Tr. 2214; PX01944 at 022 (Pirc, Dep. at 82), *in camera*)). MMO has never implemented a tiered hospital network and has no plans to do so in the future. (Pirc, Tr. 2216).

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705. Anthem has never used steering – in the sense of affirmative financial incentives – to entice members to use particular, low-cost hospitals. (Pugliese, Tr. 1465; PX01942 at 003 (Pugliese, Dep. at 8), *in camera*).

706. Anthem provides online tools that allow members to access quality and cost information about hospitals. (PX01919 at 004 (Pugliese, Dep. at 12-13)).

707. Aetna uses soft steerage in Lucas County. Its soft steering efforts have not been effective at steering members to low-cost hospitals. Informational and transparency measures at Aetna “don’t have teeth, [so] they haven’t had [an] impact[.]” (Radzialowski, Tr. 723-724; PX01938 at 004 (Radzialowski, Dep. at 11-12), *in camera*).

708. In January 2011, Aetna started a pilot hard-steering program for up to 100 Aetna employees in Toledo. In the pilot program, hospitals are “tiered” into low cost (*i.e.*, lower rates) “first tier” hospitals, which provide a more financially-advantageous benefit for members, and high cost (*i.e.*, higher rates) “second tier” hospitals, which require members to pay a higher copay. (Radzialowski, Tr. 724-725).

709. Aetna’s lower-cost hospital tier includes St. Luke’s, UPMC, Bay Park, St. Charles, and St. Anne. (Radzialowski, Tr. 776).

710. There is insufficient data at this point to conclude whether Aetna’s steering program successfully steers members to lower-cost hospitals. (Radzialowski, Tr. 725-726).

711. At the end of the year (2011), Aetna will evaluate the effectiveness of the steering program and determine whether to expand it to include other members and markets. (Radzialowski, Tr. 776-777).

712. Aetna has received “a good number of complaints from the members not liking to have steerage imposed on them[.]” (Radzialowski, Tr. 726).

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713. Hospitals have complained to Aetna about its pilot program. Hospitals did not like being identified as a high-cost or low-cost hospital and have complained about being put in tier two, rather than tier one. (Radzialowski, Tr. 726; PX01938 at 004 (Radzialowski, Dep. at 11), *in camera*)).

714. ProMedica complained to Aetna that TTH and Flower were not in tier one. (PX01938 at 004 (Radzialowski, Dep. at 11), *in camera*).

715. A United executive testified that she was not aware of any United programs with tiered benefits. (PX01939 at 007 (Sheridan, Dep. at 23), *in camera*).

716. Humana does not have any plans in Lucas County or Ohio that have incentives to use one in-network provider over another in-network provider (*i.e.*, tiered network). (McGinty, Tr. 1184-1185).

717. FrontPath's agreements with providers have provisions that prevent the use of steering. (Sandusky, Tr. 1328-1329).

718. In contract discussions, ProMedica has a policy of discouraging any strategies to steer patients away from ProMedica facilities through the use of financial incentives, and tries to get protections in its contracts preventing payors from using benefit differentials. (PX01945 at 013 (Wachsman, Dep. at 42-44), *in camera*).

719. ProMedica has anti-steering provisions in its contracts with [redacted] and [redacted], the two [redacted] payers in Lucas County besides ProMedica's own MCO, Paramount. (Wachsman, Tr. 5162-5163, *in camera*). ProMedica has also negotiated a contract with [redacted] for St. Luke's that includes an anti-steering provision. (Wachsman, Tr. 5165-5166, *in camera*).

720. ProMedica does not object to informational steering through transparency. (Wachsman, Tr. 4879-4881).

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(iii) Other steering

(a) Hospital employers

721. It is fairly common for hospital employers to provide a higher level of health-care coverage for their employees who obtain services at their own hospitals. This is similar to an employee discount in other types of industries. (Randolph, Tr. 7006-7007).

722. UTMC offers its employees' health insurance benefits. (Gold, Tr. 259). UTMC employees can choose from three health insurance plans: FrontPath, MMO, and Paramount. The plans contain incentives for insured members to seek services from UTMC's faculty physicians. (Gold, Tr. 259).

723. Mercy's health plan for its employees puts its provider hospitals into three tiers in order to steer, or incentivize, its employees to seek services from Mercy's hospitals instead of other Lucas County hospitals. (Shook, Tr. 1068; Marlowe, Tr. 2427-2428; Read, Tr. 5287-5288; Guerin-Calvert, Tr. 7294-7295; Town, Tr. 4383, *in camera*; Guerin-Calvert, Tr. 7395, *in camera*).

724. In Mercy's health plan for its employees, tier one is the preferred tier and includes Mercy's facilities. (Shook, Tr. 1072).

(b) Lucas County government

725. Physicians Health Collaborative ("PHC") is a network of Mercy physicians and Lucas County hospitals that markets to self-insured employers in Lucas County. St. Luke's is a member of PHC, but ProMedica is not. (Shook, Tr. 1092, *in camera*).

726. PHC competes with other provider networks that are marketed in Toledo, such as MMO and Paramount. (Shook, Tr. 1095, *in camera*).

727. One of the self-insured employers to which PHC markets its network is the Lucas County government. (Shook, Tr. 1093-1094, *in camera*).

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728. Lucas County government represents approximately 3,000-4,000 covered members, making it the eighth largest employer in the Toledo area. (Randolph, Tr. 7039-7040, *in camera*; RX261 at 000004, *in camera*).

729. Lucas County government offers its employees three MCO networks from which to enroll, including Paramount, FrontPath, and PHC. (Shook, Tr. 1093-1096, *in camera*).

730. In 2011, the Lucas County government contributed a greater percentage to its employees' health-care costs if they chose to enroll with PHC instead of their two other options, Paramount or FrontPath. (Guerin-Calvert, Tr. 7294-7295; Shook, Tr. 1095-1096, *in camera*; Guerin-Calvert, Tr. 7395-7396 *in camera*).

731. Specifically, PHC was offered by the Lucas County government with a 90/10 benefit coverage and \$1,000/\$2,000 out-of-pocket maximums. Paramount was offered with a 75/25 benefit coverage, and \$1,500/\$3,000 out-of-pocket maximums. FrontPath was offered with a 70/30 benefit coverage and \$2,000/\$4,000 out-of-pocket maximums. (Randolph, Tr. 7042-7043, *in camera*; PX00524 at 001, *in camera*).

732. Paramount's two-year agreement with the Lucas County government, from March 2010 through February 2012, contains a stipulation that the Lucas County government would offer all health insurance plans with similar benefits. (PX00524 at 001, *in camera*).

733. The changes that the Lucas County government made to its employee health benefits resulted in a steering program that financially penalized Lucas County employees for using Paramount's plan. (Oostra, Tr. 5940, *in camera*).

734. Although ProMedica objected to the Lucas County government's actions, ProMedica could not prevent it from steering employees to other hospitals. (Oostra, Tr. 5941-5942, *in camera*).

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735. As a result of the altered benefit offering, Mercy's PHC Lucas County government member enrollment went from [redacted] employees to [redacted] employees between 2010 and 2011, while Paramount and FrontPath both declined in membership. Paramount lost approximately [redacted] members; and FrontPath lost approximately [redacted] members. (Randolph, Tr. 7043, 7050, *in camera*).

736. Mercy is transitioning PHC into HealthSpan, which is also a network for self-insured employers that is operated by the Mercy network out of Cincinnati and is currently marketing a PPO product to self-insured employers in Lucas County. (Shook, Tr. 1092-1093, *in camera*).

c. Demographic and economic conditions

737. The population in the greater Toledo area is stagnant to declining, aging, and not forecast to grow. (Shook, Tr. 1040).

738. The declining population of the Toledo area means that there are fewer patients overall. (Guerin-Calvert, Tr. 7274-7275).

739. Toledo has substantially declining commercially insured hospital admissions. (Guerin-Calvert, Tr. 7272-7275). Today, only 29 percent of Lucas County hospital patients have commercial insurance. (Town, Tr. 3609).

740. With an aging population in Toledo, the percentage of hospital patients covered by Medicare will increase. (Guerin-Calvert, Tr. 7303, 7272-7275).

741. Toledo has high unemployment and has had an exodus of employers, which leads to a decline in patients covered by commercial insurance. (Guerin-Calvert, Tr. 7274-7275).

742. The unemployment rate in Toledo was between 7 percent and 8 percent from the recession in 2001 to the start of the recession in 2008. (Guerin-Calvert, Tr. 7292-7296).

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743. During the recession of 2008, the unemployment rate in Toledo peaked at over 13 percent, coming down only to approximately 9.5 percent in 2011. (Guerin-Calvert, Tr. 7292-7296).

744. The number of commercially insured patients in the Toledo area has declined since 2004 to 2009 from 45,000 to 35,000. (Guerin-Calvert, Tr. 7300).

745. To the extent that a higher percentage of the hospital's revenue comes from the government, which does not cover a hospital's total cost of providing care, the factors set forth in F. 737-744 put increasing financial pressures on hospitals to attract MCOs and their commercially insured patients in order to cover costs. (Guerin-Calvert, Tr. 7274-7275, 7302-7303, 7297-7298).

746. Ongoing health-care reform efforts also will impact the competitive conditions in the Toledo area, because, among other things, the rate of reimbursement from Medicare will continue to decrease and there will be less inpatient care and more outpatient care, thereby putting additional financial pressure on hospitals. (Guerin-Calvert, Tr. 7307-7309).

d. Mercy's [redacted]

747. Mercy has a plan, [redacted]. (Shook, Tr. 971, 981-982, *in camera*; PX02288 at 004-005, *in camera*).

748. Mercy's plan for [redacted]. (Shook, Tr. 985, *in camera*).

749. Mercy pursued [redacted] seriously once it learned of the likely joinder of St. Luke's and ProMedica. (Shook, Tr. 973, *in camera*; PX02288 at 001, *in camera*).

750. Mercy's [redacted]. (PX02288, *in camera*; Shook, Tr. 981-986, *in camera*).

751. In furtherance of [redacted]. (Shook, Tr. 983, *in camera*; RX295, *in camera*). Mercy is continuing to [redacted]. (Shook, Tr. 1018-1019, *in camera*).

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752. After the Joinder, Mercy purchased one of St. Luke's physician practices located in Swanton, Ohio, about 13 miles west of St. Luke's. (Wakeman, Tr. 2667-2668, *in camera*).

753. Mercy recruits physicians with the hope that the physicians will refer patients to Mercy's hospitals for inpatient services. (Shook, Tr. 1056).

754. In November 2009, Mercy had a tentative timeline [redacted] for accomplishing [redacted]. (RX286 at 000015, *in camera*). However, [redacted]. (PX01940 at 008 (Shook, Dep. at 28), *in camera*).

755. At the time of the adjudicative hearing, Mercy had not signed any agreements with any of the physicians it was actively engaged in recruiting. (Shook, Tr. 1019, *in camera*).

756. Mercy has not noticed any measurable market share impact [redacted]. (Shook, Tr. 988, *in camera*).

8. Quality effects

757. Hospitals compete on the basis of clinical quality, amenities, and patient experience. (Joint Stipulations of Law and Fact, JX00002A ¶ 11; Response to RFA at ¶ 20; *see also* PX2148 at 084-085 (Town Expert Report) ¶ 155, *in camera*; Town, Tr. 3605-3606).

758. St. Luke's was recognized as a low-cost, high-quality hospital before the Joinder with ProMedica. (Answer ¶ 9; Wakeman, Tr. 2494-2496; Sandusky, Tr. 1310-1311; PX00390 at 001; PX01072 at 001; PX01914 at 016 (Pirc, IHT at 55-56), *in camera*).

759. Prior to the Joinder, St. Luke's ranked as the highest quality, lowest cost hospital in the Toledo market. (PX01018 at 012 (Options for St. Luke's), *in camera*; PX01072 at 001 (St. Luke's Key Messages); Rupley, Tr. 1920, 1924-1925; Wakeman, Tr. 2482-2483, 2494).

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760. ProMedica believes that St. Luke's is a high-quality hospital. (Answer ¶ 33; Oostra, Tr. 6027-6028; PX01913 at 032 (Hammerling, IHT at 119), *in camera* (St. Luke's has a "good reputation historically" for quality and patient care); PX01903 at 033 (Hanley, IHT at 123), *in camera* ("I think St. Luke's has strong quality of care [.]"); PX01949 at 018 (Riordan Dep. at 64-65)).

761. ProMedica documents reflect patients' awareness that St. Luke's was a high-quality hospital, often scoring better than ProMedica in quality rankings. (PX00399 at 024, *in camera*; PX00272; PX01138 at 001).

762. Navigant, the health-care consulting firm that ProMedica hired to analyze the Joinder with St. Luke's, found St. Luke's to have high quality levels based on respected third-party quality rating organizations. (PX01946 at 008 (Nolan, Dep. at 24)).

763. St. Luke's "is regularly recognized by third-party quality ratings organizations that rank St. Luke's within the top 10% of hospitals nationally, based on outcomes, cost and patient satisfaction." (PX00390 at 001 (ProMedica News Release May 26, 2010); *see also* PX01073 at 001 (St. Luke's Press Release Healthgrades.com)).

764. Third-party quality ranking organizations also regularly praise St. Luke's for its value, *i.e.*, its combination of high quality and low costs. (Rupley, Tr. 1933-1934; PX02300 at 001; PX01170 at 013-014).

765. St. Luke's believed that part of its value as an independent hospital was that it challenged other hospital systems "to keep service levels up." (PX01170 at 020; Wakeman, Tr. 2540-2541; Rupley, Tr. 1935-1936).

766. Despite St. Luke's rapid growth in patient volume in 2010, patient satisfaction and quality were unaffected and remained at very high levels. (Wakeman, Tr. 2495-2497; Black, Tr. 5685, 5690).

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767. By some measurements, St. Luke's achievements in clinical quality exceed those of TTH and Flower. (Rupley, Tr. 1984-1985, 1991-1993, *in camera*; PX01016 at 006, *in camera*; PX01172, *in camera* (“[I]n the Commonwealth scoring on quality, SLH was the best, just a hair shy of the top 10% nationally, with Toledo Hospital dead last and well below the state average.”); PX01030 at 018-019, *in camera*). Flower ranked sixth in Lucas County for overall quality. (Rupley, Tr. 2002, *in camera*; PX01030 at 018, *in camera*).

768. Respondent's executives and expert witness confirm that competition between hospitals benefits the local community through better customer service, higher-quality care, better access for patients, and improved facilities. (Oostra, Tr. 6039; Guerin-Calvert, Tr. 7792; Waschsman, Tr. 5116-5118; PX01905 at 033 (Waschsman, IHT at 127), *in camera*).

769. Prior to the Joinder, St. Luke's had concerns about poor quality outcomes and measures at ProMedica's hospitals. (Wakeman, Tr. 2674-2677, *in camera*; Black, Tr. 5720, *in camera*; PX01932 at 019 (Bazeley, Dep. at 69-70), *in camera*); PX01130 at 002, *in camera* (“Some of ProMedica's quality outcomes/measures are not very good. Would not want them to bring poor quality to St. Luke's.”); *see* PX01016 at 023 (St. Luke's Affiliation Update Dec. 2009), *in camera*).

770. ProMedica executives admit their approach to quality was not keeping pace and that they “needed to catch up.” They have described their quality program as involving “too much discussion, process, pages/documents, reporting structures, committees, charts, [and] meetings.” (PX00527 at 001; Oostra, Tr. 6015-6019, 6024-6025).

771. Employees at ProMedica found the system's quality program to be confusing. ProMedica's Chief Medical Officer noted that “audiences after hearing quality presentations leave meetings glassy eyed and very confused” and that few employees “can fully explain the PHS approach to quality much less feel compelled to follow.” (PX00527 at 001; Oostra, Tr. 6025-6026).

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772. MCOs consider hospital quality when considering a hospital's inclusion in the MCO's network. (Radzialowski, Tr. 655; Sheridan, Tr. 6622; Pugliese, Tr. 1455; McGinty, Tr. 1173; PX01944 at 006 (Pirc, Dep. at 18-19), *in camera*).

773. MCO customers expect quality to be high at all providers within the offered network. (Pugliese, Tr. 1449-1450).

774. MMO considers that all hospitals in Lucas County do well in terms of quality. (Pirc, Tr. 2296).

775. Aetna believes that all hospitals in Lucas County are high-quality hospitals. (Radzialowski, Tr. 640).

776. FrontPath considers all hospitals in Lucas County to be quality hospitals. (Sandusky, Tr. 1402).

777. Quality of care can be measured using various data, including mortality rates, patient satisfaction scores, and other common measures of hospitals and hospital systems across the country. (RX18 at 000014 (Marcus, Dep. at 46), *in camera*).

778. There are varying degrees of reliability for quality metrics. (RX1652). Quality measures can be too "nebulous" to be meaningful. (Pirc, Tr. 2213-2214).

779. Some of ProMedica's best practices are outdated and not on-par with the practices at St. Luke's. (*E.g.*, PX01611 at 001; PX01610 at 001-003).

780. Complaint Counsel's expert witness, Professor Town, concluded, based upon economic literature, that decreased competition reduces incentives to compete on non-price dimensions. Quality is a non-price dimension. (Town, Tr. 3605-3606).

781. Professor Town concluded, based upon economic literature, that competition between hospitals leads to better quality of care. (Town, Tr. 3634-3635).

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N. St. Luke's Financial Condition

782. The most important time period for analyzing St. Luke's financial viability is the time period when Mr. Wakeman arrived in 2008 through when the Joinder occurred in 2010. (Dagen, Tr. 3337-3338).

783. In analyzing the financial viability of St. Luke's as a stand-alone community hospital, absent the Joinder, it would be inappropriate to incorporate any financial effects attributable only to the Joinder, *i.e.*, effects that St. Luke's would not have accomplished on its own. (Dagen, Tr. 3353-3354).

1. Operating margins

784. Operating margins reflect total net operating revenue minus total operating expense, divided by net operating revenue, stated in a percentage, and reflect the actual profitability from operations of a company. (Hanley, Tr. 4580)

785. OhioCare, St. Luke's parent, experienced operating losses from 2007 through the Joinder in 2010. OhioCare's operating loss was [redacted] million in 2007, [redacted] million in 2008, [redacted] million in 2009, and [redacted] million in the first eight months of 2010. This amounted to operating margins of [redacted] percent in 2007, [redacted] percent in 2008, [redacted] percent in 2009, and [redacted] percent for the first eight months of 2010. (Den Uyl, Tr. 6418-6419; RX56 at 000006 (¶ 17), *in camera*).

786. St. Luke's was experiencing operating losses from 2007 through the date of the Joinder in 2010. St. Luke's loss was [redacted] million in 2007, [redacted] million in 2008, [redacted] million in 2009, and [redacted] million for the first eight months of 2010. This amounted to operating margins of [redacted] percent in 2007, [redacted] percent in 2008, [redacted] percent in 2009, and [redacted] percent in the first eight months of 2010. (PX02129 at 002; Den Uyl, Tr. 6418-6419; RX56 at 000006 (¶ 17), *in camera*; Dagen, Tr. 3304-3305).

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787. St. Luke's operating performance was significantly below that of other Ohio hospitals. St. Luke's had negative operating margins in the years leading up to the Joinder, while other Ohio hospitals were profitable. The average operating margin for Ohio hospitals was 4.0 percent in 2007, 1.5 percent in 2008, and 5 percent in 2009. (Den Uyl, Tr. 6420-6421; RX56 at 000006 (Table 2), *in camera*).

788. St. Luke's operating performance was significantly below that of similarly sized (100-249 beds) nonprofit urban hospitals. St. Luke's had negative operating margins in the years leading up to the Joinder, while those similarly sized hospitals were profitable. The average operating margin for similarly sized nonprofit urban hospitals was 3.2 percent in 2007, 1.8 percent in 2008, and 3 percent in 2009. (Den Uyl, Tr. 6420-6421; RX56 at 000006 (Table 2), *in camera*).

789. St. Luke's operating performance was significantly below that of hospitals with comparable Moody's bond ratings as St. Luke's. St. Luke's had negative operating margins in the years leading up to the Joinder, while those hospitals with comparable Moody's bond ratings were profitable. The average operating margin for Moody's A-2 rated hospitals was 2.6 percent in 2007, when St. Luke's bond rating was A-2; the average operating margin for Moody's Baa1 rated hospitals was 0.3 percent in 2008 and 1.6 percent in 2009, when St. Luke's bond rating was Baa1. (Den Uyl, Tr. 6420-6422; RX56 at 000006 (Table 2), *in camera*).

790. In August 2010, St. Luke's earned a positive operating margin of \$7,000 on \$36.7 million in gross revenue, which Mr. Wakeman described as "not impressive, but it is better than a loss." (PX00170 at 001).

791. In reporting St. Luke's August 2010 positive operating margin to the Board, Mr. Wakeman cited "high activity" in excess of the prior year that "produced a positive operating margin. . . . This positive margin confirms that we can run in the black if activity stays high. After much work, we have built our volume up to a point where we can produce an operating margin and keep our variable expenses under control. (PX00170 at 001).

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2. EBITDA

792. The “earnings before interest, taxes, depreciation, and amortization,” or EBITDA, and the EBITDA margin of OhioCare were negative from 2008 through the Joinder. (Dagen, Tr. 3313-3314). OhioCare’s EBITDA was [redacted] million in 2007, [redacted] million in 2008, [redacted] million in 2009, and [redacted] million for the first eight months of 2010. OhioCare’s EBITDA margin was [redacted] percent in 2007, [redacted] percent in 2008, [redacted] percent in 2009, and [redacted] percent for the first eight months of 2010. (RX56 at 000006-000007 (¶ 19), *in camera*).

793. Having a negative EBITDA as OhioCare did in 2008, 2009, and the first eight months of 2010 is very unusual for a hospital. (Den Uyl, Tr. 6591-6592, *in camera*).

794. St. Luke’s EBITDA was [redacted] million in 2007, [redacted] million in 2008, [redacted] million in 2009 and nearly [redacted] million as of August 31, 2010. This translates into EBITDA margins of [redacted] percent in 2007, [redacted] percent in 2008, [redacted] percent in 2009, and [redacted] percent as of August 31, 2010. (RX56 at 000006-000007 (¶ 19), *in camera*).

795. St. Luke’s EBITDA margin, in the time leading up to the Joinder, was below the EBITDA of Moody’s comparably rated hospitals. The average EBITDA margin of comparably rated hospitals was 9.6 percent in 2007, 7.7 percent in 2008, and 8.1 percent in 2009. (RX56 at 000007 (¶ 20), *in camera*).

3. Operating cash flow less capital expenditures

796. “Operating cash flow” takes operating income and adds back interest, depreciation, and amortization, similar to the accounting calculation, “EBITDA.” EBITDA is another measure of a firm’s profitability. (Hanley, Tr. 4694-4695; Den Uyl, Tr. 6424-6425; RX56 at 000006 (¶ 19) (Den Uyl Expert Report) *in camera*).

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797. EBITDA does not consider capital expenditures. (Den Uyl, Tr. 6427-6428).

798. It is important to consider capital expenditures as part of the measurement of a hospital's true cash flow. Hospitals are very capital intensive. They need to spend money on capital to maintain their equipment, to provide new systems, and avoid decline. Hospitals need to spend a lot of capital, "just to stay even." (Den Uyl, Tr. 6430-6432).

799. OhioCare's operating cash flow minus capital expenditures was negative from 2007 through the Joinder: it was [redacted] million in 2007, [redacted] million for 2008, [redacted] million for 2009, and [redacted] million for the first eight months of 2010. (RX56 at 000008 (¶ 22), *in camera*).

4. Personnel restrictions

800. In February 2009, St. Luke's began restricting hiring to those essential positions that affected patient care. (Wakeman, Tr. 2574, 2841-2842; PX01597). St. Luke's hiring freeze continues to the present time and was not part of St. Luke's Three-Year Plan. (*see* F. 920; Wakeman, Tr. 2843-2844; PX01026).

801. During the period of hiring restrictions, St. Luke's patient volume increased, so it generally did not make sense to conduct layoffs. Instead, St. Luke's cut pay, cut benefits, and froze pay. (Wakeman, Tr. 2572-2573).

802. St. Luke's froze employee compensation in 2008, including step increases and merit pay increases, for all employees; at the time of the Joinder, employees had not received pay increases for two years. (Johnston, Tr. 5317; Wakeman, Tr. 2841-2842; Black, Tr. 5608; RX1226 at 000002-000003).

803. In 2009, all of St. Luke's executives took a 10 percent pay cut. (Johnston, Tr. 5317).

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5. Capital investment needs

804. ProMedica understood that St. Luke's had significant capital needs for information technology, electronic medical records ("EMR"), outpatient surgery, private rooms, and investing in its OB program. (Hanley, Tr. 4548; Oostra, Tr. 5854-5855).

a. Deferred projects

805. In 2009, in order to conserve cash, St. Luke's began deferring some capital expenditures, including routine and ongoing upgrades of facilities and replacement of equipment, such as the replacement of air handlers, regular hospital beds and birthing beds, surgical tables, a nurse call system, and a sleep lab system. (Johnston, Tr. 5351-5355, 5362-5363; RX56 at 000015-000016, *in camera*).

806. The estimated combined cost of the deferred items identified in F. 805 is [redacted] million. (RX56 at 000016 (¶ 42), *in camera*; see also Johnston, Tr. 5357-5363).

807. St. Luke's also had to defer several information technology infrastructure projects, including: data center cooling, wireless networking, and PC purchases. St. Luke's had estimated that upgrading its data center's cooling system would have cost approximately [redacted], and that upgrading its wireless network would have cost approximately [redacted]. (RX22 at 015 (Perron, Dep. at 50-52, *in camera*)).

808. Prior to 2009, St. Luke's normal annual capital expenditures were approximately [redacted] million. In 2009, St. Luke's capital expenditures were about [redacted] million. (Johnston, Tr. 5352; Den Uyl, Tr. 6461, *in camera*)).

809. In Fall 2010, St. Luke's departments identified [redacted] million of necessary capital projects for budgeting purposes, with [redacted] million for critical projects for 2011 alone. (Johnston, Tr. 5411-5412, *in camera*).

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b. Age of plant

810. Age of plant “basically tells you how old your hospital is” and is indicative of how well you are maintaining the hospital; it is also one of the statistics that Moody’s uses to evaluate hospitals. (Den Uyl, Tr. 6470-6471, *in camera*).

811. The average age of plant of a hospital will increase if capital expenditures are slowed down. (Den Uyl, Tr. 6470-6471, *in camera*).

812. Slowing down capital expenditures would not be sustainable in the long term for St. Luke’s. (Den Uyl, Tr. 6469-6470, *in camera*).

813. St. Luke’s was built in 1972. Undertaking routine capital maintenance and improvements is necessary for St. Luke’s ongoing business. (RX56 at 000017-000018 (¶ 44), *in camera*).

814. During due diligence, ProMedica learned that St. Luke’s average age of plant was [redacted] years at the end of 2009, as compared to industry norms of about 10 or 11 years. (Hanley, Tr. 4608; PX01016 at 014, *in camera*).

815. St. Luke’s age of plant was greater than that of comparable Moody’s rated hospitals and the difference was increasing in the years leading up to the Joinder. In 2007, St. Luke’s average age of plant was [redacted] whereas that of comparably rated Moody’s hospitals was 9.5. In 2008, St. Luke’s average age of plant was [redacted] whereas that of comparably rated Moody’s hospitals was 10.0. In 2009, St. Luke’s average age of plant was [redacted] whereas that of comparably rated Moody’s hospitals was 10.5. After the first eight months of 2010 St. Luke’s average age of plant was [redacted]. (RX56 at 000017-000018, *in camera*).

c. Space conversion/private rooms

816. The standard of care has changed from semi-private to private rooms. This is because: (1) inpatients tend to be sicker today than in the past because outpatient care has improved; (2)

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there is more technology and equipment in hospital rooms than in the past and private rooms provide the space for that equipment; (3) private rooms improve infection control; and (4) private rooms ensure greater patient privacy as mandated by HIPAA regulations. (Nolan, Tr. 6277-6278, *in camera*; Johnston, Tr. 5376; Guerin-Calvert, Tr. 7287-7289; Black, Tr.5584-5585).

817. UTMC is in the process of converting all of its semi-private rooms to private rooms. Mercy is making extensive renovations at St. Vincent to add more private rooms, and also added about 75 private rooms in its Regional Heart and Vascular Center at St. Vincent in 2007. (Gold, Tr. 224; Shook, Tr. 904, 1116, *in camera*).

818. St. Luke's percentage of private rooms prior to the Joinder was 29 percent, which is very low, but typical for a hospital of St. Luke's age. (Nolan, Tr. 6276-6277, *in camera*; PX01216 at 025, *in camera*).

819. Prior to the Joinder, St. Luke's wanted to convert excess space and semi-private rooms into approximately 50 private rooms. The projected cost for that project was approximately \$1.8 million. (Black, Tr. 5695).

820. The lack of private rooms impacted St. Luke's emergency room (ER) diversion rate, because ER patients with contagious infections or other conditions requiring isolation must be placed in private rooms. In addition, opposite genders cannot be placed in the same semi-private room. (Johnston, Tr. 5370; Guerin-Calvert, Tr. 7287-7288).

d. Electronic medical records

821. St. Luke's realized that to accomplish its Three-Year Plan (F. 920) it would also need to make significant investments in its information technology ("IT") capabilities to keep up with the rest of the marketplace. (Wakeman, Tr. 2816-2817).

822. The Health Information Technology for Economic and Clinical Health Act ("HITECH") passed in 2009, provides hospitals with increased Medicare reimbursement if they

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implement and upgrade their EMR systems and achieve statutory “meaningful use” requirements by certain deadlines. (Johnston, Tr. 5343-5344; Wakeman, Tr. 2849-2850; RX22 at 013-014 (Perron, Dep. at 45-46)).

823. The “meaningful use” requirements of the HITECH Act mean that the different technological systems related to a patient’s care need to be connected and able to share information back and forth. (Johnston, Tr. 5343).

824. “Meaningful use” under HITECH not only requires that health-care providers employ EMR systems, but also that the EMRs in each patient setting have the ability to connect with one another to create an overall EHR, or electronic health record, for each patient. (Johnston, Tr. 5343-5344, 5520-5521).

825. St. Luke’s has numerous IT systems that are implicated by the “meaningful use” requirements, including, for example, its patient registration, patient billing, nursing documentation, radiology, laboratory, surgery, pharmacy, cardiac catheter lab, and pulmonary medicine systems. (Johnston, Tr. 5345-5346).

826. In addition to the IT systems described in F. 825, St. Luke’s also requires network and infrastructure systems. New laptops and desktop work stations are also needed to work with the new systems. (Johnston, Tr. 5346).

827. St. Luke’s cannot simply update its current systems. Many are no longer supported by the manufacturers and creating new interfaces between the old systems is costly and inefficient. (Johnston, Tr. 5346; RX22 at 012 (Perron, Dep. at 39-41)).

828. Hospitals that meet “meaningful use” requirements by 2013 will receive additional Medicare reimbursements for being compliant. But hospitals that fail to do so by 2015 will face penalties in the form of reduced Medicare reimbursements. (Johnston, Tr. 5344-5345; RX22 at 022 (Perron, Dep. at 81)).

829. In addition to “meaningful use,” St. Luke’s IT systems required significant investments to meet requirements for health

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information exchanges, HIPPA 5010, ICD-10, patient centered medical home, and accountable care. (RX22 at 013 (Perron, Dep. at 43)).

830. St. Luke's had selected Eclipsys as the vendor for its hospital-based EMR system. (Johnston, Tr. 5347).

831. On November 4, 2009, Eclipsys estimated a total cost for the EMR system of approximately \$21 million over seven years. (PX01495; PX01496 at 003; Den Uyl, Tr. 6453, *in camera*). In June 2010, shortly before the Joinder, Eclipsys reduced the quote by approximately \$1 million. (PX01502 at 001).

832. Under the American Recovery and Reinvestment Act of 2009 ("ARRA"), there are financial incentives for meeting "meaningful use" targets for EMR implementation. St. Luke's believed if it met the requirements of ARRA, it would receive \$6.3 million in stimulus funds for the project. (PX01281 at 007-012; PX01928 at 014 (Perron, Dep. at 47-48), *in camera*).

833. With the financial incentives under AARA (F. 832), the total cost for its EMR system could be reduced to approximately \$14 million; however, St. Luke's would first have to pay the full cost of purchasing and implementing the system before the required deadline in order to qualify for any available subsidies. (Johnston, Tr. 5349; Black, Tr. 5694-5695).

834. Upgrading St. Luke's foundation information technology applications was part of the Eclipsys project. (PX01928 at 011 (Perron, Dep. at 36, *in camera*)).

835. The EMR quote referred to in F. 831 did not account for the operational expenses associated with implementing and maintaining that system, such as training clinical and non-clinical staff. (PX01496; RX22 at 027-029 (Perron, Dep. at 101-106); Johnston, Tr. 5348-5349).

836. The estimated costs associated with the incremental hardware and personnel needed to put in place the EMR system total approximately [redacted] million over the first three years of

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the EMR project. (Den Uyl, Tr. 6454–6455, *in camera*; RX56 at 000013-000014 (¶ 36), *in camera*).

837. Patient centered medical home regulations, promulgated in July 2010, mean that St. Luke's would also have to ensure that its ambulatory and hospital-based EMR systems can communicate with each other, requiring the purchase of additional middleware products from a vendor. (PX01928 at 032-033 (Perron, Dep. at 120-124)).

838. St. Luke's CFO through the end of 2009, David Oppenlander, and St. Luke's Computer Information Systems Director, Eric Perron, recommended that St. Luke's move forward with beginning to implement EMR in 2010. (PX01933 at 039 (Oppenlander, Dep. at 147-148), *in camera*; (PX01928 at 021, 023, 030 (Perron, Dep. at 75-76, 84-85, 113), *in camera*)).

839. St. Luke's had budgeted [redacted] million for 2010 to begin implementation of the EMR system, but funds to purchase a new system were not allocated. (Wakeman, Tr. 2851-2852; PX01928 at 008 (Perron, Dep. at 23, *in camera*)).

840. St. Luke's Chief Financial and Operating Officer believes that St. Luke's would have required financial support to fund the EMR project absent the Joinder. (Johnston, Tr. 5482-5483, *in camera*).

6. Pension funding obligations

841. St. Luke's has two pension plans, a defined benefit pension plan and a 403(b) defined contribution pension plan. (Johnston, Tr. 5331).

842. St. Luke's defined benefit pension plan promises certain benefits, payable over a period of years, upon retirement, to employees. That promise is backed by the assets in the pension plan account. The employer must contribute enough money to the plan to have sufficient assets to live up to the pension plan's obligations. (Arjani, Tr. 6729).

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843. Employers who offer a defined benefit pension plan face various risks, including the risk that plan assets may shrink through investment losses and that benefit obligations may increase due to higher salaries, longer life expectancies, or extended employee tenures. (Arjani, Tr. 6730).

844. The contributions that St. Luke's is required to make to its defined benefit pension plan are cash contributions. (Johnston, Tr. 5397, *in camera*).

845. At a board meeting on January 27, 2009, the Board was advised by Mr. Wakeman concerning the "Pension Challenge we are currently facing. Mr. Wakeman explained that the pain this is causing is due to the external market and not the organization. Mr. Wakeman stated we had to make benefit cuts in a year that our employees did a fabulous job. Total revenue went up by 3.7% but bad debt was over 20%. Over the last quarter, the investments depreciated causing the pension plan to become underfunded going from 111.7% at the end of 2007, to today of 64.7%. If the funded status reaches 60% the hospital must freeze the plan, due to regulatory requirements." (RX1226 at 002).

846. Defined benefit pension funding and expense were "pressing concerns" identified in the December 2009 Affiliation Update to the Board. (F. 414).

847. Each year, actuaries are required to certify the funding level of St. Luke's defined benefit pension plan. (Johnston, Tr. 5333, 5337-5338).

848. Under the Employee Retirement Income Security Act ("ERISA") as modified by the federal Pension Protection Act ("PPA"), if St. Luke's defined benefit pension plan is less than 100 percent funded, it is required to amortize the amount of the under-funding and make payments over seven years to bring the plan to 100 percent funding. (Arjani, Tr. 6736-6737; Den Uyl, Tr. 6446-6447, *in camera*).

849. The "funding target" is an assessment for ERISA purposes of the benefit obligations of the pension plan. It is

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calculated by examining the census of plan participants, which provides data on how long employees have been with the employer and the level of their accrued pension benefits, as well as the level of accrued benefits for retirees and terminated vested employees who are entitled to future benefits. (Arjani, Tr. 6779).

850. Keeping a defined benefit pension plan above the 80 percent funding level eliminates the danger of having the plan labeled “at risk” under ERISA. (Arjani, Tr. 6758-6759, *in camera*; RX56 at 000011-000012 (¶ 31), *in camera*).

851. If a defined benefit pension plan falls below 80 percent funding, an employer may be required to accelerate contributions or payments into the plan in order to get the plan above the 80 percent level. (Johnston, Tr. 5336-5337).

852. Accelerating payments means that payments made during the current plan year are re-allocated to the prior plan year for purposes of measuring the funding level of the defined benefit pension plan as of January 1st of the current year. (Arjani, Tr. 6739).

853. In order to be certified as 80 percent funded as of January 1, 2010, St. Luke’s had to accelerate contributions to its defined benefit pension plan for year 2010 into plan year 2009 and also had to apply or “forfeit” a credit balance from a prior year’s payment. (Arjani, Tr. 6739-6740; PX01397).

854. St. Luke’s applied approximately \$800,000 in defined benefit pension plan contributions from its 2010 plan year contributions back to the 2009 plan year. At the same time, St. Luke’s also forfeited its prior credit balance of approximately \$1.4 million dollars. (Arjani, Tr. 6739-6740; PX01397; Johnston, Tr. 5401, *in camera*; PX01392 at 005, *in camera*).

855. St. Luke’s was required to make an accelerated contribution to its defined benefit pension plan of [redacted] million in order to reach the 80 percent funded level as of January 1, 2011, which St. Luke’s made prior to the applicable deadline of March 31, 2011. (Johnston, Tr. 5406, *in camera*; Arjani, Tr. 6749, *in camera*; PX00474 at 001, *in camera*).

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856. At the close of the Joinder, St. Luke's defined benefit pension plan was under-funded from both an accounting and funding perspective. (Johnston, Tr. 5336).

857. St. Luke's actuaries estimate that St. Luke's will need to make annual contributions to its defined benefit pension plan of at least [redacted] million until 2016 to meet minimum funding requirements, assuming St. Luke's achieves a projected 8 percent return on the plan's assets, and depending on other variables, including discount rates, employee terminations and employee retirements. The required contribution may be less than the estimated [redacted] million. (Arjani, Tr. 6751-6752, 6765, 6767, *in camera*; PX01943 at 016 (Arjani, Dep. at 54-55), *in camera*).

858. On December 31, 2009, St. Luke's froze its employee defined benefit pension plan and shifted its employees to a contribution plan. (Johnston, Tr. 5331; Arjani, Tr. 6730). This change resulted in cost savings for St. Luke's. (Wakeman, Tr. 2872).

859. After St. Luke's defined benefit pension plan was frozen, St. Luke's still had an obligation to make up the difference between the funding target, the present value of the plan's obligations, and the plan's assets. (Arjani, Tr. 6731).

860. Even if St. Luke's is able to make current payments to its defined benefit pension plan beneficiaries, it must still restore the plan to full funding. (Johnston, Tr. 5342-5343).

861. Even though St. Luke's froze its defined benefit pension plan at the end of 2009, St. Luke's still faced all of the financial commitments to the plan that it had made through 2009. (Den Uyl, Tr. 6451-6452, *in camera*).

7. Cash reserves

862. St. Luke's reserve fund (cash reserves) balance on August 31, 2010 was [redacted] million of which [redacted] million was "trustee restricted." (RX56 at 000029 (¶ 71), *in camera*).

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863. Trustee restricted funds are those funds that are earmarked for malpractice insurance and one year's debt service on St. Luke's bonds and capital leases. While it is technically possible to reclassify funds from restricted to unrestricted in order to fund capital expenditures and operating losses, it would not be financially prudent to do so, given the ongoing need to make insurance and bond payments. Excess or surplus funds in the restricted fund might be transferred, and one year St. Luke's did transfer surplus trustee funds to St. Luke's pension plan. (PX01951 at 047-048 (Den Uyl, Dep. at 183-187, *in camera*); PX01933 at 044 (Perron, Dep. at 166-167); PX00038 at 006, *in camera*).

864. St. Luke's unrestricted reserves were [redacted] million as of August 31, 2010, at the time of the Joinder, down from [redacted] million in 2009, [redacted] million in 2008, and [redacted] million in 2007. (RX56 at 000015-000016 (¶ 41), *in camera*).

865. From the end of 2007 through the Joinder, St. Luke's was using the reserve fund to fund losses and the capital commitments it needed. (Den Uyl, Tr. 6460, *in camera*).

866. As of August 31, 2010, St. Luke's held a total of at least \$65 million in cash and investment balances. (Joint Stipulations of Law and Fact, JX00002A ¶ 34).

867. A hospital's cash reserves are used for capital expenditures, strategic capital expenditures, or for unforeseen events that may arise outside of normal operations. (Den Uyl, Tr. 6457, *in camera*; PX01933 at 042 (Oppenlander, Dep. at 161) (stating that St. Luke's reserves could be used to purchase "any types of capital . . . equipment, a table, chairs, anything that essentially is capital"), *in camera*; PX01908 at 009 (Deacon, IHT at 26-28, *in camera*, Johnston Tr. 5521-5522).

868. "Days cash on hand" reflects the unrestricted cash and investments, both short-term and long-term, that are available to pay the operating costs of a company, based on average expenses per day. Days cash on hand measures how many days a

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company could last, assuming no further cash comes in. It is a measure of liquidity and stability. (Hanley, Tr. 4583-4584).

869. The metric that St. Luke's and bond rating agencies use to evaluate the state of its cash reserve fund is days cash on hand. (Johnston, Tr. 5526-5527).

870. In 2008, St. Luke's days cash on hand was 135. In 2009, St. Luke's days cash on hand was 109. As of August 31, 2010, St. Luke's cash on hand was 104 days. In 2000, St. Luke's cash on hand had been 358 days. (PX02129 at 002; Hanley, Tr. 4584).

871. The amount of days cash on hand held by Aa-rated institutions is about double what St. Luke's currently holds. St. Luke's days cash on hand is about half of other hospitals its size. (Johnston, Tr. 5527).

8. Moody's downgrade

872. Moody's Investors Service, Inc. ("Moody's") assigns a credit rating by performing a holistic qualitative and quantitative analyses of the borrower. (PX01370 at 001; PX02146 at 009-010 (¶ 15) (Brick Expert Report)). Moody's examines certain variables over time and in relation to the industry generally. (PX01370 at 005; PX02146 at 009-010 (¶ 15) (Brick Expert Report)).

873. Moody's downgraded St. Luke's Series 2004 revenue bonds by two grades in November 2008, from "A2" to "Baa1." (PX00379 at 001).

874. A possible further bond rating downgrade was identified as one of the "pressing concerns" in the December 2009 Affiliation Update presented to the St. Luke's Board. (F. 414; PX01016 at 014, *in camera*).

875. In February 2010, during the time that ProMedica was conducting due diligence on St. Luke's, Moody's downgraded St. Luke's bond rating from a Baa1 to a Baa2, with a negative outlook. (Hanley, Tr. 4590, 4592-4594; PX00053 at 001).

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876. A Baa2 bond rating is “two notches away from junk bond” status. (Hanley, Tr. 4705-4706).

877. “Obligations rated Baa are subject to moderate credit risk. They are considered medium grade and as such may possess certain speculative characteristics.” (PX01371 at 009).

878. A Moody’s survey indicates that in 2009, approximately 100 out of 401, or 28%, not-for-profit freestanding hospitals and single-state health-care systems had a bond rating between Baa1 and Baa3. (PX01368 at 022; PX02146 at 005-006 (¶ 9) (Brick Expert Report)).

879. A “negative outlook” means that it is more likely that there will be a further bond rating downgrade, rather than an upgrade, in the future. (Den Uyl, Tr. 6463, *in camera*).

880. According to Moody’s, the downgrade of St. Luke’s bond rating in February 2010 “reflect[ed] larger operating losses and operating cash flow deficit[s] through 11 months of fiscal year (FY) 2009 resulting in insufficient debt service coverage despite a very low debt load. The outlook remains negative reflecting lower but continued operating losses expected through FY 2010 and ongoing challenges to negotiate favorable commercial contracts as competitive pressures continue. The outlook also reflects our concern that cash reserves could decline if operating cash flow deficits continue . . .” (PX01372 at 001).

881. Among St. Luke’s “strengths” identified by Moody’s were a “very low debt position” with 8.3 million rated debt outstanding, a “very strong” cash-to-debt coverage of 412 percent, “adequate” liquidity measures with 123 days cash on hand; “relatively favorable payor mix” with low Medicaid and self-pay patients; and the Memorandum of Understanding executed between St. Luke’s and ProMedica. (PX01372 at 001-002).

882. St. Luke’s cash-to-debt coverage of 412 percent compared to an average of just over 100 percent for all Moody’s-rated hospitals. (PX01372 at 002; Brick, Tr. 3474).

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883. When Moody's downgraded St. Luke's bond rating in February 2010, it described St. Luke's "Challenges," including: third consecutive year of large operating losses and an operating cash flow deficit posted for the first time through 11 months of FY 2009 (-9.8% operating margin and -2.0% operating cash flow margin); currently unfavorable commercial contracts and ongoing challenges with negotiating higher commercial reimbursement rates; a relatively aggressive investment allocation relative to the hospital's rating level and the need for more predictable returns to support operations and debt as operating losses continue to grow; a "very competitive market with the presence of a number of hospitals that are part of two larger and financially stronger systems, ProMedica Health System (Aa3-rated) and Mercy Health Partners (owned by A1-rated Catholic Health Partners)"; and weak demographics in the primary service area, which is characterized by declining volume trends, high unemployment levels, and low median income levels. (PX01372 at 001).

884. When Moody's downgraded St. Luke's bond rating in February 2010, it noted: "What could change the rating – UP - Continued growth and stability of inpatient and outpatient volume trends; significantly improved and sustainable operating performance for multiple years; strengthening of debt coverage measures and liquidity balance; improved market share. What could change the rating – DOWN - Continued weak operating performance; sustained weak debt coverage level; weakening of liquidity; sizable unexpected debt issuance; significant loss in market share." (PX01372 at 003).

885. Typically, Moody's looks for three years of sustained operating performance when it comes to a potential upgrade. (Brick, Tr. 3544).

886. With respect to operating performance, "a hospital's ability to generate and sustain a level of earnings that ensures ongoing operations, debt service repayment, provides a source of capital for facility needs and strategic initiatives, and increases cash reserves is critical" to Moody's credit analysis. (PX01370 at 016).

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887. Data collected by Respondent's bond-rating expert, Errol Brick, shows that "Baa" rated hospitals and health-care systems issued \$2.6 billion in debt from January 2010 through January 2011, (ranging from \$25 million to \$527 million per hospital). In addition, data collected by Brick pertaining to ten bond issues by Baa rated hospitals since August 31, 2010 shows the actual interest rates paid by these hospitals. (PX02146 at 005-006, 015-035 (¶¶ 9-10 and Appendices 1 and 2) (Brick Expert Report); Brick, Tr. 3480-3483).

888. Based on his analysis of the data described in F. 887, Brick concluded that, in August 2010, St. Luke's would have been able to access the tax-exempt capital markets for up to \$75 million in debt for a reasonable interest rate of no more than 7 percent. (Brick, Tr. 3483-3490).

889. When there is negative cash flow, the choice is to draw down cash reserves or borrow money, but borrowing money is difficult for a company that is struggling financially. (Den Uyl, Tr. 6434).

890. Ms. Hanley, ProMedica's CFO who evaluated St. Luke's financials, believes that as a result of the downgrade, future borrowing by St. Luke's would involve more constraints, such as a higher interest rate, more stringent covenants, and/or a debt-service funds escrow. Although St. Luke's was not seeking to borrow money in February 2010 when it was downgraded by Moody's, "you look at a company for the future sustainability long term of a company, not just . . . that point in time." (Hanley, Tr. 4707).

891. St. Luke's did not attempt to issue new bond debt any time between January 1, 2009 and August 31, 2010. (Joint Stipulations of Law and Fact, JX00002A ¶¶ 37-38).

892. St. Luke's was not seeking to borrow money in 2010 because, as Respondent's expert witness opined, St. Luke's was running losses and "to borrow more money would put more leverage on the hospital, . . . [and] would put them in a more difficult position." (Den Uyl, Tr. 6547).

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9. Bond covenant non-compliance

893. During due diligence, ProMedica learned that St. Luke's was not in compliance with certain covenants for bonds that were insured by AMBAC. (Hanley, Tr. 4600; *see* RX906 at 000001).

894. St. Luke's debt service coverage ratio was negative so St. Luke's was in technical default. (Hanley, Tr. 4600-4601; RX906 at 000001-000002).

895. AMBAC required St. Luke's to retain an independent consultant, but St. Luke's did not do so and, subsequently, AMBAC notified St. Luke's that it was in default on March 11, 2010. (Hanley, Tr. 4601-4602).

896. AMBAC completed a credit analysis of St. Luke's bonds in late 2008 and early 2009 and downgraded St. Luke's credit from an A- to a BBB+ rating. (Gordon, Tr. 6791-6792, 6799-6800, *in camera*; RX177).

897. As part of this credit analysis of St. Luke's, in late 2008 and early 2009 AMBAC evaluated the Moody's and S&P's ratings for St. Luke's bonds and three years of financial metrics including admissions, net patient service revenue, operating margin, EBITDA margin, and debt coverage. (Gordon, Tr. 6792-6796, *in camera*; RX177).

898. In the credit analysis, described in F. 896, AMBAC highlighted that St. Luke's operating margin was negative "and getting larger in the negative direction." (Gordon, Tr. 6796-6797, *in camera*; RX177).

899. In the credit analysis, described in F. 896, AMBAC's, First Vice President Bruce Gordon ("Mr. Gordon"), who had the primary responsibility for tracking the performance of St. Luke's series 2004 Bonds, recommended that St. Luke's rating be put on a downward trend, because "[St. Luke's] financial performance was clearly trending down or in a negative direction during this three-year period." (Gordon, Tr. 6784, 6789, 6798, *in camera*; RX177).

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900. Based upon the credit analysis described in F. 896, Mr. Gordon recommended that St. Luke's rating be put on a downward trend, despite the fact that St. Luke's EBITDA margin and days cash on hand were "relatively strong for this particular entity." (Gordon, Tr. 6797-6799, *in camera*; RX177).

901. In his review of the rating analysis, described in F. 896, Mr. Gordon's supervisor downgraded St. Luke's to BBB+ and agreed with Mr. Gordon's downward trend recommendation. (Gordon, Tr. 6799-6800, *in camera*; RX177).

902. The debt service coverage ratio measures a hospital's cash flow for a given year divided by the principal and interest that is payable on its debt for that same year. (Gordon, Tr. 6808, *in camera*).

903. From a credit standpoint, it is important that the debt service coverage ratio is above one, meaning that a company has sufficient cash flow to pay the principal and interest on its bonds. (Gordon, Tr. 6808-6809, *in camera*).

904. St. Luke's bond covenants required that it maintain a debt service coverage ratio of 1.3 as of the end of any fiscal year. (RX906 at 000001; PX01542 at 001).

905. St. Luke's informed AMBAC that its 2008 debt service coverage ratio was [redacted]. (RX10 at 026 (Gordon, Dep. at 97)).

906. For 2009, St. Luke's debt service coverage ratio was at least negative [redacted]. (PX02355 at 001; Gordon, Tr. 6806-6809, *in camera*).

907. On December 23, 2009, St. Luke's filed a "Material Event Notice" formally notifying AMBAC, the bond insurer; the Huntington Bank, the trustee; and the City of Maumee, the issuing authority, that St. Luke's had violated its debt service coverage ratio covenants for 2008 and 2009. (RX183 at 000004; Gordon, Tr. 6815-6816, *in camera*).

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908. In its December 23, 2009 “Material Event Notice,” St. Luke’s stated that its “plan to address its future covenant compliance is to attempt to negotiate new, or renegotiate existing contracts, with insurance carriers.” And, St. Luke’s stated that it “may explore other options, including but not limited to exploring an affiliation with another health care system.” These statements did not give AMBAC comfort that St. Luke’s financial condition would improve. (RX183 at 000004; Gordon, Tr. 6816-6817, *in camera*).

909. When St. Luke’s informed AMBAC that St. Luke’s violated its debt service coverage ratio covenants in 2008 and 2009, Mr. Gordon “was certainly concerned that the default might be an indication of a deteriorating financial situation.” (Gordon, Tr. 6811, *in camera*).

910. Based on his review of St. Luke’s financial statements in December 2009, and upon internal tracking of five or six years of financials, Mr. Gordon concluded that St. Luke’s financial “trends were negative, indicating that the financial performance of the hospital was deteriorating.” Mr. Gordon was particularly concerned “with the accelerated deterioration in the hospital’s performance during 2008 and year-to-date 2009.” (Gordon, Tr. 6814-6815, *in camera*).

911. “Defeasance” of bonds means that the outstanding bonds are retired for purposes of financial reporting. When a bond issue is “defeased,” typically an escrow is established with a trustee and the amount is held in safe investments, in such amount that the principal and the earnings off of those investments is sufficient to repay the principal and the interest on the original bonds over the life of the bonds. (Gordon, Tr. 6803-6804).

912. To resolve St. Luke’s default described in F. 894, AMBAC proposed that St. Luke’s defease its bonds rather than pay down the full amount because St. Luke’s bonds were not callable. Because they were non-callable bonds, it would have cost St. Luke’s more to defease the bonds than the face value of the bonds outstanding, which would not have been financially prudent. In addition, St. Luke’s was trying to conserve cash.

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(Gordon, Tr. 6825-6826, *in camera*; Den Uyl, Tr. 6465-6466, *in camera*).

913. It would not have been financially prudent for St. Luke's to purchase the balance of its outstanding bonds prior to the Joinder because: (1) St. Luke's was trying to maintain its liquidity and conserve cash; (2) the amount of the bonds was relatively small and the interest rate was fairly low; and (3) it would have been expensive to repurchase them because they are non-callable bonds. (Den Uyl, Tr. 6465-6466, *in camera*).

914. Based upon a credit review of pre-2010 financial data, on April 27, 2010 AMBAC downgraded St. Luke's internal rating from BBB+ to BBB and gave St. Luke's a "negative outlook." (Gordon, Tr. 6835, *in camera*; RX179, *in camera*).

915. AMBAC's April 27, 2010 credit review of St. Luke's lists a number of [redacted]. (RX179 at 000003-000004, *in camera*).

916. St. Luke's owed less than \$11 million in total bond debt as of August 31, 2010. (JX00002A ¶ 33).

917. As of August 31, 2010, St. Luke's outstanding bond debt was [redacted] million. (Response to RFA at ¶ 47).

918. At the time of the latest Moody's downgrade, F. 875, St. Luke's level of bonds outstanding was fairly low. (Dagen, Tr. 3312).

919. As of August 31, 2010, St. Luke's had enough cash and investments on its financial statement to pay off all of its outstanding debt. (JX00002A at ¶ 24).

10. Three-Year Plan and improvements pre-Joinder

a. Strategic Plan

920. In June 2008, soon after taking the CEO position with St. Luke's in February 2008, Mr. Wakeman developed St. Luke's Hospital's Three-Year Plan (2008-2010) ("Three-Year Plan") that

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contained growth goals for patient revenues and patient volume. The plan was based on five strategic pillars: “Growth, People, Quality, Service, and Finance/Corporate.” The five pillars contained associated goals and benchmarks. (Wakeman, Tr. 2812-2813; JX00002A ¶ 39; PX01026).

921. St. Luke’s growth goals stated in the Three-Year Plan included: increasing inpatient net revenue by \$3.5 million per year, within three years; increasing outpatient net revenue by \$5 million per year, within 3 years; achieving 40% inpatient market share in core service area, within 3 years; and establishing 2 signature clinical lines. Strategies to meeting these goals included obtaining 90% access to area managed care enrollees within three years and growing its physician staff. (PX01026 at 001-002).

922. St. Luke’s pursued a strategy of acquiring physician practices because it expected “that the physicians would generate inpatient and outpatient revenues at St. Luke’s.” (Joint Stipulations of Law and Fact, JX00002A ¶ 42).

923. Employing physicians had both one time and recurring costs, including initial capitalization, insurance coverage, physician salaries, practice operational expenditures and capital expenditures, such as the AllScripts EMR system. (Wakeman, Tr. 2803-2804, 2819-2820).

924. By August 31, 2010, St. Luke’s achieved the growth goal of increasing inpatient net revenue by more than \$3.5 million per year on average. (Joint Stipulations of Law and Fact, JX00002A ¶ 40; RX1858 at 000018 (Respondent’s Answers to Complaint Counsel’s Interrogatories ¶ 17)).

925. By August 31, 2010, St. Luke’s achieved the growth goal of increasing outpatient net revenue by more than \$5 million per year on average. (Joint Stipulations of Law and Fact, JX00002A ¶ 41; RX1858 at 000018-000019 (Respondent’s Answers to Complaint Counsel’s Interrogatories ¶ 17)).

926. St. Luke’s inpatient net revenues increased in each calendar year from 2008 through 2010. (JX00002A ¶ 32).

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927. St. Luke's outpatient net revenues increased in each calendar year from 2008 through 2010. (JX00002A ¶ 31).

928. By August 31, 2010, St. Luke's achieved its growth goal of obtaining more than 40% market share in its core service area. (RX1858 at 000018-000019 (Respondent's Answers to Complaint Counsel's Interrogatories ¶ 17)).

929. In a memorandum to the St. Luke's Board of Directors, dated September 24, 2010, Mr. Wakeman wrote: "If there was one pillar [St. Luke's] attained a high level of success in [its] strategic plan in the past two years, it would be growth. The hard numbers prove that out, [in] almost every service." (PX00170 at 006). The Chairman of St. Luke's Board, James Black, agreed with this statement. (Black, Tr. 5686).

930. St. Luke's overall occupancy rate in the twelve months prior to the Joinder increased by approximately [redacted] percent. (PX01920 at 010 (Wakeman, Dep. at 31), *in camera*).

931. By the time of the Joinder, St. Luke's had achieved four of the five pillars set forth in its Three-Year Plan. (Wakeman, Tr. 2593-2594; PX01326).

932. By the time of the Joinder, St. Luke's was successful on three of the four specific goals identified for "Growth" set forth in its Three-Year Plan. (RX1858 at 000018-000019 (Respondent's Answers to Complaint Counsel's Interrogatories at ¶ 17)).

933. St. Luke's "service" goals stated in the Three-Year Plan included, among other things, systematically converting all St. Luke's double-bed patient rooms to single-bed patient rooms, in order to improve St. Luke's infection control, patient safety, and patient satisfaction. In addition, it was important for St. Luke's to make this conversion to stay competitive locally and keep up with national standards. (PX01010 at 003; Wakeman, Tr. 2815; Black, Tr. 5584-5585). St. Luke's did not accomplish the Three-Year Plan goal of "[w]ithin three years, systematically convert all St. Luke's double-bed patient rooms to single-bed

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patient rooms.” (PX01010 at 003; Wakeman, Tr. 3018-3020, *in camera*).

934. St. Luke’s finance/corporate goals for the Three-Year Plan included, among others, achieving a break-even operating margin by the end of 2009, then 2% to 4% for subsequent years; achieving 200 days cash on hand; maintaining St. Luke’s “A” rating with Moody’s; achieving net revenue growth per case (case-mix adjusted⁹) of 3% to 5% per year; and achieving an average age of plant consistent with Moody’s “A” rated hospitals. (PX01026 at 003-004).

935. St. Luke’s realized that to accomplish its Three-Year Plan it would also need to make significant investments in its IT capabilities to keep up with the rest of the marketplace. (Wakeman, Tr. 2816-2817).

936. St. Luke’s did not achieve the key financial metrics outlined in the Three-Year Plan. (Wakeman, Tr. 3018-3019, *in camera*).

937. St. Luke’s did not achieve the financial goal outlined in the Three-Year Plan of achieving 200 days cash on hand. (PX01010 at 004; Wakeman, Tr. 3018-3019, *in camera*).

938. St. Luke’s did not achieve the financial goal outlined in the Three-Year Plan of a break- even margin by the end of 2009 and did not achieve the desired margins. (PX01026 at 003-004; PX01010 at 003-004; Wakeman, Tr. 3018-3019, *in camera*).

939. St. Luke’s did not accomplish the financial goal outlined in the Three-Year Plan to “Maintain St. Luke’s “A” rating with Moody’s.” (PX01010 at 003-004; Wakeman, Tr. 3018-3019, *in camera*). St. Luke’s bond rating was downgraded by two grades in November 2008, from “A2” to “Baa1,” and downgraded again in February 2010 to Baa2. (F. 873, 875).

⁹ See F. 608.

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940. St. Luke's did not accomplish the Three-Year Plan goal to "[a]chieve an average age of plant consistent with Moody's "A" rated hospitals." (PX01026 at 003-004; Wakeman, Tr. 3018-3019, *in camera*; F. 814-815).

941. By the time of the Joinder, St. Luke's debt service coverage ratio was 3.7, which exceeded the financial goal in the Three-Year Plan of a debt service ratio of 2.0. (PX01026 at 004; PX02129 at 002).

b. Cost coverage ratios

942. A "cost coverage ratio" measures whether the payments a hospital is receiving covers its costs of providing care. For example, "if you're being paid a thousand dollars by a particular [MCO] and your costs are a thousand, you have a cost coverage ratio of 1. If you have a ratio that's less than 1, you're not covering the costs of providing care, and if it's more than 1, you're more than covering your costs." (Den Uyl, Tr. 6438, *in camera*).

943. Cost coverage ratios consider both the direct and indirect costs that a hospital incurs as a result of providing care. (Den Uyl, Tr. 6438, *in camera*). Direct costs are those costs that are directly related to treating a patient, such as medications, supplies, laundry, and labor. (Dagen, Tr. 3189). Indirect costs are not fixed and rise as volume increases. (Den Uyl, Tr. 6476, *in camera*).

944. St. Luke's overall cost coverage ratio was below one, meaning St. Luke's was not generating sufficient reimbursement to cover its total costs, through the time of the Joinder on August 31, 2010. (Den Uyl, Tr. 6422-6423).

945. St. Luke's internal financial systems provide reports that allow it to track its revenue per discharge on a case-mix adjusted basis as well as its cost per discharge on a case-mix adjusted basis. Earnings per case-mix adjusted discharge is also referred to as "earnings per adjusted discharge" or by the acronym "EPAD." (Johnston, Tr. 5318-5819).

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946. At the time of the Joinder, St. Luke's earnings per adjusted discharge figures showed that, on average, St. Luke's was losing money on its commercially insured patients. (Johnston, Tr. 5318-5322).

947. The overall cost coverage ratio for St. Luke's, across all payors, was only [redacted]. Considering all its payments, prior to the Joinder, St. Luke's was not generating enough reimbursement to cover its costs. (Den Uyl, Tr. 6440-6443, *in camera*; RX56 at 000010, *in camera*).

c. Other financial metrics

948. Mr. Wakeman's monthly report for August 2010 advised the Board that:

- St. Luke's activity exceeded its Operating Financial Plan (OFP) and last years' activity. "That activity has finally exceeded our fixed expense. . . ."
- The high activity produced a positive operating margin of \$7,000 on \$36.7 million in gross revenue. It is not impressive, but it is better than a loss.
- This positive margin confirms that we can run in the black if activity stays high. After much work, we have built our volume up to a point where we can produce an operating margin and keep our variable expenses under control.

(PX00170 at 001).

949. St. Luke's financial performance, as of the date of the Joinder, improved over its performance in 2008 and 2009. (F. 950-954, 957-958; PX02147 at 006).

950. St. Luke's operating margin for the time period January 1, 2010 through August 31, 2010 was an improvement over St. Luke's operating margin for calendar year 2009. (JX00002A at ¶ 30).

951. St. Luke's operating cash flow margin (*i.e.*, EBITDA margin) and operating income improved in the first eight months

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of 2010, prior to the Joinder, compared to 2009. (F. 794; PX02129 at 002; Wakeman, Tr. 2594-2596; JX00002A ¶ 29).

952. In the first eight months of 2010, prior to the Joinder, St. Luke's losses decreased and its operating cash flow improved. (F. 786, 794; Dagen, Tr. 3191-3193; PX01925 at 054-055 (Guerin-Calvert, Dep. 207-208)).

953. St. Luke's operating cash flow margin for the time period January 1, 2010 through August 31, 2010 was an improvement over St. Luke's operating cash flow margin for calendar year 2009. (JX00002A ¶ 28).

954. St. Luke's operating cash flow margin improved by [redacted] percent from the end of 2009 to August 31, 2010, from [redacted] percent to positive [redacted] percent. (Wakeman, Tr. 2703-2704, *in camera*, Wakeman, Tr. 3035; PX02129 at 002; RX56 at 000007, Table 3 (Den Uyl Expert Report), *in camera*; JX00002A ¶ 27).

955. EBITDA does not consider capital expenditures. At certain times, it also does not reflect pension expenses or gains and losses from investments. These items need to be examined as well to get a full picture of the true cash flow of a hospital. (Den Uyl, Tr. 6427-6428).

956. Improving EBITDA does not necessarily indicate financial strength. (Dagen, Tr. 3188).

957. As of August 31, 2010, St. Luke's showed increased revenue, due in part to referrals from newly added physician practices and recent access to Anthem members. (RX56 at 000011 (¶ 30), *in camera*; F. 162 (St. Luke's began participating in Anthem's network again in July 2009)).

958. As of August 31, 2010, St. Luke's showed decreased expenses, in part related to restrictions St. Luke's instituted with respect to salaries, hiring and pensions. (RX56 at 000011 (¶ 30), *in camera*; F. 800-803, 858).

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11. St. Luke's future viability

959. At the end of 2009, St. Luke's CEO Wakeman advised the Board of St. Luke's regarding how long St. Luke's would survive as an independent entity under different scenarios. Wakeman advised that under then-current conditions, St. Luke's would be able to survive between three and five years, and that if St. Luke's was able to get rate increases under contracts with two of St. Luke's largest commercial payers, St. Luke's could survive four to seven years. (Wakeman, Tr. 2624-2625).

960. These survival time periods set forth in F. 959 could expand, if all other factors were unchanged and equity markets and operating cash flow improved. (Wakeman, Tr. 2625-2627).

a. Complaint Counsel's expert

961. Complaint Counsel's proffered expert regarding St. Luke's financial condition, H. Gabriel Dagen, is Assistant Director of Accounting and Financial Analysis at the FTC. He has a Bachelor of Science degree in Psychology and a Masters in Business Administration with a concentration in Finance. He has completed 27 credit hours in accounting at Memphis State University and has an inactive Certified Public Accounting License. He has been with the FTC since 1998. Mr. Dagen's experience includes reviewing financial and related information for over a dozen hospitals, hospital systems and health-care providers. (PX2147 at 001-004 (¶¶ 1-3, 7) (Dagen Expert Report)).

962. Mr. Dagen concluded that the improvements in St. Luke's operating performance in 2010 compared to 2009 were "driven primarily by increases in volume." (Dagen. Tr. 3192-3193, 3197-3199).

963. Mr. Dagen's pro forma analysis predicts that volume growth could act as the primary driver for improved operating financial performance absent the Joinder, even to the point of profitability by 2013. (See PX02147 at 036-042 (¶¶ 65-76) (Dagen Expert Report); PX01950 at 042-043 (Dagen, Dep. at 161-162), *in camera*).

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964. Mr. Dagen concluded that because St. Luke's reimbursements covered its direct costs during the first eight months of 2010, growth in St. Luke's patient volume alone improved St. Luke's overall cost coverage ratio. (Dagen, Tr. 3191-3193, 3241-3242, *in camera* ("As patient volume increases . . . – as long as the reimbursement rates are higher than direct costs [-] the cost coverage ratio will improve.")).

965. Mr. Dagen concluded that St. Luke's payor reimbursements can fall short of covering its total costs but, as long as it covers its direct costs and makes some contribution to indirect costs, volume growth alone can improve St. Luke's profitability (even without increases in rates). According to Mr. Dagen this is because direct costs are variable in nature and indirect costs are more fixed. (Dagen, Tr. 3189-3193, 3198-3199, 3239-3242, *in camera* ("[a]s long as you're making a contribution to your indirect costs . . . it's beneficial to add the next patient"); PX01852 at 017 (¶ 25) (Dagen Rebuttal Report)).

966. Mr. Dagen concluded that, absent the Joinder, St. Luke's would not only be able to avoid service cuts, but would be able to continue to make growth-minded investments, implement EMR, convert semi-private rooms to private rooms, eliminate its outstanding bond debt, and still have approximately \$33 million in cash and reserves at the end of 2013. (Dagen, Tr. 3210-3214; PX02147 at 036 (¶ 65) (Dagen Expert Report)).

967. Mr. Dagen concluded that St. Luke's cash flow and reserve fund "ensure that, absent the Joinder, St. Luke's would have remained financially viable into the foreseeable future" and in particular "that St. Luke's would have been able to fund necessary capital improvements and growth-minded investments without any additional borrowing." (PX02147 at 006 (¶ 12) (Dagen Expert Report)).

968. Mr. Dagen concluded that St. Luke's was in the midst of a successful financial turnaround at the time of the Joinder. He concluded that Mr. Wakeman's Three-Year Plan was producing the desired results: increasing revenues, market share,

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and improving St. Luke's operating performance. (Dagen, Tr. 3229-3231; PX02147 at 006 (¶ 15) (Dagen Expert Report)).

969. Mr. Dagen concluded that “[a]bsent the Joinder, St. Luke's was heading toward further financial growth and stability in 2011 and beyond.” (PX02147 at 006-007 (¶ 16) (Dagen Expert Report)).

b. Respondent's expert

970. Respondent's proffered expert on St. Luke's financial condition, Bruce Den Uyl, is managing director for AlixPartners, LLP, a professional services firm. He has a Bachelor of Arts in Economics and a Masters in Resource Economics. He has over 25 years of experience providing valuation and financial consulting, and expert testimony, to a wide range of hospitals, MCOs, physician practices, and surgery centers, among other health-care and related entities. (RX56 at 001-002 (¶¶ 2-3), 046, *in camera*).

971. Mr. Den Uyl concluded that St. Luke's struggled financially as a stand-alone entity during the years leading up to the Joinder and faced significant financial obstacles in going forward as an independent hospital. (RX56 at 000003 (Den Uyl Expert Report), Section II.A., *in camera*).

972. Mr. Den Uyl was not asked to, and did not, analyze or provide an expert opinion on how long St. Luke's could have survived as a stand-alone hospital had it not been acquired by ProMedica. (Den Uyl, Tr. 6520-6522).

973. Mr. Den Uyl did not analyze whether St. Luke's would have been profitable as a stand-alone hospital in the future had it not been acquired by ProMedica. (Den Uyl, Tr. 6522).

974. Mr. Den Uyl offered no expert opinion on whether St. Luke's, as a stand-alone hospital, without the Joinder, could have issued additional debt. (Den Uyl, Tr. 6530-6531).

975. Mr. Den Uyl, was not asked to, and did not provide, an expert opinion in his expert report as to whether St. Luke's could

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have issued additional debt as a stand-alone organization; however, when nevertheless elicited during cross-examination, Den Uyl's opinions were that St. Luke's did not "have the wherewithal to borrow money" and that from a financial standpoint it would not have been prudent." St. Luke's was running losses, "[a]nd to borrow more money would put more leverage on the hospital, and put them in a more difficult position." (Den Uyl, Tr. 6530-6531, 6547-6548 (denying Motion to Strike)).

976. Mr. Den Uyl concluded that it is possible that St. Luke's might have become profitable as a stand-alone hospital, without the Joinder, within two years, but that it is unlikely. (Den Uyl, Tr. 6523).

977. Slowing down capital expenditures would not be sustainable in the long term for St. Luke's because a hospital must be maintained and eventually put in new systems. The average age of plant of a hospital will increase if capital expenditures are slowed down. (Den Uyl, Tr. 6469-6471, *in camera*).

978. The employee cost cutting measures that St. Luke's undertook in 2009 were not sustainable in the long term. "You eventually would have to pay your employees more to remain competitive in the marketplace." (Den Uyl, Tr. 6468, *in camera*).

979. Mr. Den Uyl concluded that St. Luke's cash flow losses from 2007 through the Joinder were not sustainable, because St. Luke's could not draw down on its reserves indefinitely. St. Luke's capital requirements would deplete St. Luke's cash reserves, if it was unable to generate positive cash flow. In addition, to funding its losses, St. Luke's was facing significant capital expenditures, and St. Luke's had to fund its underfunded pension plan. (Den Uyl, Tr. 6429, 6434-6435; RX56 at 000015, *in camera*).

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O. Pro-Competitive Benefits and Efficiencies

1. The Joinder provides St. Luke's with capital

980. As part of the Joinder, ProMedica has committed to contribute \$30 million over three years to St. Luke's Hospital. ProMedica has also contributed \$5 million to the St. Luke's Foundation. (Hanley, Tr. 4679; Johnston, Tr. 5375).

981. ProMedica set aside \$10 million in strategic capital and approximately [redacted] million in routine capital for St. Luke's for the 2011 budget year. (RX31 at 011 (Akenberger, Dep. at 39-40, *in camera*)).

982. ProMedica's \$10 million allocation of strategic capital to St. Luke's for 2011 was based upon the obligation ProMedica made to invest \$30 million in St. Luke's over a three-year period. (RX31 at 012 (Akenberger, Dep. at 41, *in camera*); Hanley, Tr. 4679; Johnston, Tr. 5375).

983. The \$10 million of strategic capital ProMedica allocated to St. Luke's for 2011 will be spent on priorities identified by the St. Luke's Board. (RX31 at 012 (Akenberger, Dep. at 41, *in camera*)).

984. ProMedica's preliminary 2012 budget for St. Luke's also provides St. Luke's with \$10 million in strategic capital and approximately [redacted] million in routine capital. (RX31 at 011-012 (Akenberger, Dep. at 40-41, *in camera*)).

985. ProMedica defines routine capital expenditures as capital that is currently in service with the various facilities and will need to be replaced; examples of routine capital expenditures include replacement of medical imaging machines, such as CT scanners, and replacement of carpeting in a facility. (RX31 at 009 (Akenberger, Dep. at 30)).

986. Routine capital is capital that needs to be replaced because its useful life is no longer operating at an appropriate level. (RX31 at 010 (Akenberger, Dep. at 34)).

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987. ProMedica defines strategic capital expenditures as reflecting investments that it is making in the community to provide support for ProMedica's strategic plan to meet patient and quality needs, employee needs, and financial needs. (RX31 at 010 (Akenberger, Dep. at 34)).

988. Strategic capital would be something that would require new investment of capital towards a new service, expansion of a service, or new technology. (RX31 at 010 (Akenberger, Dep. at 34)).

989. The capital commitment from ProMedica is to be used for capital projects at St. Luke's, including converting semi-private rooms to private rooms, updating St. Luke's IT systems, constructing an outpatient lobby, renovating the heart center, moving administrative services, expanding surgical areas, and increasing the private postpartum area and well infant nursery. (Hanley, Tr. 4628 *in camera*, 4679-4680, PX00058 at 056).

990. With the benefit of capital it received from ProMedica, St. Luke's plans to add 17 additional private rooms. (Johnston, Tr. 5372-5373, 5376-5377).

991. The current project budget for the additional 17 private rooms described in F. 990 is \$3 million. (Johnston, Tr. 5377).

992. Prior to the Joinder, St. Luke's projected the cost of its highest priority capital projects, EMR implementation and private room conversions, to be \$14 million and \$1.8 million, respectively. (Black, Tr. 5694-5695).

993. St. Luke's had \$65 million in cash and investments as of August 31, 2010, while its estimate for the cost of a private room conversion project was \$1.8 million. (*See* Joint Stipulations of Law and Fact, JX00002A ¶ 34; Black, Tr. 5695-5696). Mr. Black, St. Luke's Chairman, testified that St. Luke's had adequate capital to fund its private room conversion project as a stand-alone hospital. (Black, Tr. 5695-5696).

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994. ProMedica believes that St. Luke's has allocated part of its initial capital contribution of \$10 million toward IT investment to become compliant for "meaningful use." (For explanation and context on "meaningful use," see F. 822-824, 832; Hanley, Tr. 4679).

995. Although several of the components necessary to meet meaningful use requirements have been implemented, St. Luke's overall implementation of necessary systems is still in the planning stages. (Johnston, Tr. 5380-5381).

996. ProMedica will not start implementing EMR at St. Luke's until 2012 at the earliest. Mr. Perron, St. Luke's Computer Information Systems Director, was "[u]nsure" whether ProMedica could implement EMR at St. Luke's in time to take advantage of all federal ARRA financial incentives. (PX01928 at 037 (Perron, Dep. at 139), *in camera*; see also PX01912 at 068 (Akenberger, IHT at 262-263), *in camera*).

997. St. Luke's intended to begin implementing EMR in 2010, but stopped the process because of the Joinder. (Johnston, Tr. 5484, *in camera*; PX01928 at 023 (Perron, Dep. at 84), *in camera*; Den Uyl, Tr. 6575-6576, *in camera*).

998. ProMedica also provided approximately 55 individual employees who have assisted with the "meaningful use" conversion process. (Johnston, Tr. 5380).

999. ProMedica would not invest in St. Luke's without the Joinder. (Town, Tr. 4374; RX1855 at 000024, *in camera*).

2. St. Luke's became part of ProMedica's Obligated Group

1000. ProMedica's Obligated Group is the group that guarantees ProMedica's public debt. (Hanley, Tr. 4513).

1001. ProMedica's debt associated with its Obligated Group has bond ratings of "Aa3" from Moody's, with a stable outlook, and "Aa-" from Standard & Poor's with a positive outlook. (Hanley, Tr. 4514).

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1002. AMBAC, St. Luke's bond insurer (F. 893), believed that "the risk associated with the St. Luke's bonds that we insured would be much safer if St. Luke's was a part of ProMedica." (Gordon, Tr. 6824-6825, *in camera*).

1003. Among the positive developments noted by AMBAC in its April 27, 2010 credit review report for St. Luke's, which recommended downgrading St. Luke's credit from BBB+ to BBB (F. 914), was St. Luke's negotiation of a merger "with A+ rated ProMedica Health System." (RX179 at 000003, *in camera*.)

1004. On June 1, 2010, AMBAC, St. Luke's and ProMedica came to a Forbearance and Waiver Agreement to resolve St. Luke's debt covenant violation. (PX01542; Gordon, Tr. 6844-6855, *in camera*).

1005. In the 2010 Forbearance and Waiver Agreement, AMBAC agreed to waive its remedies against St. Luke's upon a Joinder between St. Luke's and ProMedica when ProMedica would become responsible for making payments on those bonds. If St. Luke's did not join with ProMedica, then St. Luke's would be required to defease the complete balance of the bonds by the end of the year, December 31, 2010. The Agreement required St. Luke's to set up an irrevocable escrow in case this defeasance would become necessary. (PX01542 at 003-004; Gordon, Tr. 6845-6855, *in camera*).

1006. St. Luke's default of its bond covenants (F. 894-895) was cured when St. Luke's joined with ProMedica. (Den Uyl, Tr. 6466, *in camera*).

1007. Effective at closing of the Joinder, St. Luke's became part of the ProMedica Obligated Group. (Hanley, Tr. 4513; Johnston, Tr. 5372).

1008. Subsequent to the Joinder, AMBAC granted a waiver to St. Luke's, which required that ProMedica's Obligated Group replace St. Luke's on the bond note. (Hanley, Tr. 4677; RX907).

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1009. On September 28, 2010, Moody's upgraded St. Luke's bond rating to ProMedica's rating because St. Luke's joined ProMedica's Obligated Group and took on its bond rating. (Hanley, Tr. 4676; RX350 at 000001).

3. Funding for St. Luke's pension plan

1010. Since the Joinder, ProMedica has helped fund contributions to St. Luke's defined benefit pension plan. (Hanley, Tr. 4678).

1011. ProMedica's goal is to keep its defined benefit pension plans fully funded and is committed to increase the funding to make St. Luke's defined benefit pension plan [redacted]. (Johnston, Tr. 5409, *in camera*).

1012. The accounting liability for St. Luke's defined benefit pension plan was [redacted] million at the end of December 2008 and [redacted] million at the end of December 2009. (Johnston, Tr. 5391, *in camera*).

1013. ProMedica's financial statements show that ProMedica's own defined benefit pension plan was underfunded in 2008 by [redacted] million and in 2009 by [redacted] million. (PX00015 at 32; Oostra, Tr. 6129-6130).

4. Reduction of some of St. Luke's costs

1014. St. Luke's was not large enough to fund a captive insurance company (an insurance company subsidiary) or to be a part of a captive insurance plan on its own. (Wakeman, Tr. 2837-2838).

1015. Following the Joinder, St. Luke's has saved about \$500,000 in malpractice insurance by becoming part of ProMedica's captive insurance company. (Hanley, Tr. 4680).

1016. Moving St. Luke's into ProMedica's captive insurance company had the effect of freeing up over \$8 million in cash as "unencumbered" on St. Luke's balance sheet. (Hanley, Tr. 4680).

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1017. St. Luke's has benefited from the Joinder through the consolidation of non-clinical backroom services such as billing services, legal services, physician practice management, and IT support for physician practices. (Wakeman, Tr. 3023-3025, *in camera*).

5. Revenues from Paramount members

1018. Prior to the Joinder, St. Luke's, and Mr. Wakeman personally, made serious attempts to have St. Luke's rejoin Paramount's network, but the attempts were unsuccessful. (Rupley, Tr. 1940-1941).

1019. On April 10, 2009, Paramount informed UTMC that Paramount would not add St. Luke's to its provider network because "[t]here is no benefit to ProMedica for inclusion of an additional hospital in all of Paramount's product lines." (PX00224 at 002, *in camera*).

1020. ProMedica believed that St. Luke's admission into Paramount would have hurt patient volume at ProMedica's Lucas County hospitals. (Oostra, Tr. 6045-6046; Randolph, Tr. 7076-7077; Rupley, Tr. 1941; PX00405 at 001; PX01233 at 005, *in camera*).

1021. Following the Joinder, St. Luke's became a participating provider in Paramount, and its volume of Paramount patients has increased significantly since then. (Hanley, Tr. 4678-4679; Johnston, Tr. 5374-5375, 5382; Wakeman, Tr. 3023-3025, *in camera*).

1022. The increased Paramount volume had a positive effect on St. Luke's bottom line, because Paramount pays St. Luke's above its costs. (Wakeman, Tr. 3023-3025, *in camera*; Johnston, Tr. 5512-5513, *in camera*).

1023. St. Luke's addition to the Paramount network was one reason St. Luke's financial performance improved after its Joinder with ProMedica. (Dagen, Tr. 3329).

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1024. Mr. Dagen estimates that St. Luke's addition to the Paramount network accounted for 23 percent of the total increase in St. Luke's revenues during the last four months of 2010. (*See* Dagen, Tr. 3243-3244, *in camera*, 3330).

6. Navigant Consulting's clinical service line consolidation recommendations

1025. Navigant Consulting, Inc. ("Navigant") is regarded as reliable and authoritative in health-care consulting. (Shook, Tr. 1110, *in camera*).

1026. ProMedica retained Navigant in mid-2010 to conduct a clinical integration study to determine how best to deploy services across the ProMedica system following the Joinder with St. Luke's. (Nolan, Tr. 6253, 6263; Hanley, Tr. 4670, *in camera*).

1027. The 2010 ProMedica project required Navigant to review the Toledo metropolitan marketplace and develop a set of recommendations as to the best distribution of services across ProMedica's facilities to meet community needs. (Nolan, Tr. 6253-6254).

1028. Clinical integration describes the process of when two organizations join together and combine their clinical capabilities in an optimal manner to provide high-quality and cost-effective health-care. (Nolan, Tr. 6254-6255).

1029. Clinical integration refers to consolidation of services in some circumstances, and refers to distribution of services in other cases. (Nolan, Tr. 6328, *in camera*).

1030. When making clinical integration recommendations, Navigant considers the market demographics and population projections, physical plants and facilities, anticipated health-care-related legislation, and emerging community needs. (Nolan, Tr. 6255-6256).

1031. In the course of its engagement by ProMedica, Navigant examined TTH, Toledo Children's Hospital, Flower, Bay Park, and St. Luke's. (Hanley, Tr. 4670, *in camera*).

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1032. During the initial months of the 2010 ProMedica engagement, Navigant created and presented interim progress reports to a steering committee, consisting of members of ProMedica's executive team and St. Luke's executive team, and a physician advisory committee to get continuous feedback and input from the client on preliminary findings and proposed recommendations. (Nolan, Tr. 6268-6270, *in camera*).

1033. Navigant produced its final report to ProMedica in January 2011 (hereafter "Navigant Report"). (Nolan, Tr. 6284, *in camera*; PX00479, *in camera*).

a. General recommendations

1034. The Navigant Report made key findings including that: (i) ProMedica's hospitals served the entire Toledo metropolitan area, but St. Luke's was unique because it was more focused in the southwest area, (ii) when combined, the volumes for all ProMedica hospitals, including St. Luke's, was sufficient to reach critical mass numbers, and (iii) physicians supported developing centers of excellence, particularly for complex tertiary or quaternary cases. (Nolan, Tr. 6286-6288, *in camera*; PX00479 at 007-008, *in camera*).

1035. Navigant believed it was important to consolidate complex cases in order to gain efficiencies and improve quality. (Nolan, Tr. 6289, *in camera*).

1036. Navigant recommended that ProMedica concentrate its high-acuity, complex, but lower-volume cases in one facility or location, but also recommended that ProMedica ensure its general low-acuity, high-volume services were available across the Toledo market so that they would be easily accessible to the population. (Nolan, Tr. 6291-6292, *in camera*; PX00479 at 009, *in camera*).

b. Recommendations by service line

1037. The Navigant Report focused specifically on nine service lines that Navigant developed with the assistance of

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ProMedica to cover the vast majority of patients and opportunities for integration. (Nolan, Tr. 6284-6285, *in camera*; PX00479 at 006, *in camera*).

1038. The nine service lines that Navigant reviewed in the Navigant Report were cancer, heart and vascular, neurosciences, orthopedics, women's obstetrics and gynecology, children's, gastroenterology/urology, psychiatry, and rehabilitation. (PX00479 at 006, *in camera*; Hanley, Tr. 4670-4671, *in camera*).

(i) Cancer

1039. The Navigant Report recommended that ProMedica [redacted]. (Nolan, Tr. 6301-6302, *in camera*).

1040. No existing services at St. Luke's were directly affected by the recommendations in the Navigant Report with respect to cancer services. (PX01946 at 019 (Nolan, Dep. at 67)).

(ii) Cardiovascular

1041. The Navigant Report recommended that ProMedica [redacted]. (Nolan, Tr. 6298-6303, *in camera*; Hanley, Tr. 4672, *in camera*).

1042. The leadership of the [redacted], with no change in capital investment. (RX31 at 034 (Akenberger, Dep. at 131-132, *in camera*)).

1043. Cardiac physicians believe that a hospital needs about 180 cardiac cases a year to break even. (RX26 at 017 (Riordan, Dep. at 59)).

1044. Prior to the Joinder, St. Luke's had about 150 cardiac cases a year and had been unable to raise it above that number. (RX26 at 017 (Riordan, Dep. at 60)).

1045. The consolidation described in F. 1041 entails [redacted]. (PX01931 at 034 (Akenberger, Dep. at 131), *in camera*). As a result, some patients who require [redacted]. (Nolan, Tr. 6331-6333, *in camera*). Also, patients who arrive at

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St. Luke's – or who are already there for another procedure – and then require [redacted]. (Nolan, Tr. 6330-6334, *in camera*; Hanley, Tr. 4743, 4745-4746, *in camera*).

1046. Dr. Gbur, an independent physician who performs interventional cardiology procedures at St. Luke's, testified that the elimination of open heart services at St. Luke's could add 10 to 15 minutes of additional transit time for some patients who experience a heart attack and must go to a hospital with open heart capabilities for treatment. (Gbur, Tr. 3112-3113).

1047. ProMedica did not explain how shifting St. Luke's heart and vascular volume to Flower Hospital would impact the revenues earned on those procedures. (PX2105 at 051 (Exhibits to Akenberger, Decl.).

1048. Given that ProMedica's reimbursement rates for services is on average higher than St. Luke's, a price increase resulting from this consolidation may exceed any actual cost savings generated by it. (PX02147 at 060-061 (¶ 111) (Dagen Expert Report)).

(iii)Neurosciences

1049. The Navigant Report recommended that ProMedica [redacted]. (Nolan, Tr. 6303, *in camera*).

1050. No existing services at St. Luke's were directly affected by the recommendations in the Navigant Report with respect to neuroscience services. (PX01946 at 019 (Nolan, Dep. at 68).

(iv)Orthopedics

1051. The Navigant Report recommended that ProMedica [redacted]. (Nolan, Tr. 6295, 6304, *in camera*).

1052. No existing services at St. Luke's were directly affected by the recommendations in the Navigant Report with respect to orthopedics services. (PX01946 at 019 (Nolan, Dep. at 68).

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(v) OB services

1053. The Navigant Report recommended that ProMedica [redacted]. (Nolan, Tr. 6304, *in camera*). Navigant also recommended [redacted]. (Hanley, Tr. 4672, *in camera*).

1054. With regard to [redacted], the Navigant Report recommended that ProMedica [redacted]. (Nolan, Tr. 6299, *in camera*).

1055. The Navigant Report recommended that [redacted] because of its location in a demographically attractive area. (Nolan, Tr. 6300, *in camera*).

(vi) Inpatient rehabilitation

1056. The Navigant Report recommended that ProMedica consolidate inpatient rehabilitation at Flower to develop a center of excellence, but also to maintain outpatient services in accessible locations around the community. (Nolan, Tr. 6305, *in camera*). A center of excellence is a specialized facility with specialized staff and equipment for a specific service or array of services. (Nolan, Tr. 6296, *in camera*).

1057. The Navigant Report also recommended that St. Luke's inpatient rehabilitation cases be redirected to Flower. The purpose of this recommendation was to free up space for St. Luke's to redeploy for its expanding OB program and to use when converting semi-private rooms into private rooms. (Nolan, Tr. 6299-6300, *in camera*).

1058. With the approval of the Federal Trade Commission, ProMedica consolidated inpatient rehabilitation services at Flower. This involved closing St. Luke's inpatient rehabilitation center and shifting those patients to Flower Hospital. (Wakeman, Tr. 3025-3026, *in camera*; PX02104 at 005-006 (¶ 9) (Akenberger, Decl.), *in camera*).

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1059. As of March 25, 2011, ProMedica and St. Luke's had consolidated St. Luke's inpatient rehabilitation program at Flower Hospital. (RX31 at 028 (Akenberger, Dep. at 108, *in camera*)).

1060. ProMedica and St. Luke's concluded that consolidating St. Luke's and Flower's inpatient rehabilitation programs at Flower, which utilized approximately 50 percent of its rehabilitation bed capacity and could accommodate St. Luke's cases, would enable St. Luke's to convert its inpatient rehabilitation beds to private rooms. (PX02105 at 011, *in camera*; Hanley, Tr. 4681).

1061. As a result of adding new beds in the previous inpatient rehabilitation unit, St. Luke's has been able to reduce its ER diversions virtually to zero. (Johnston, Tr. 5374).

1062. Shifting inpatient rehabilitation services from St. Luke's to Flower permits St. Luke's to convert its former inpatient rehabilitation beds to private rooms. (Hanley, Tr. 4681).

1063. After the consolidation described in F. 1059 above, patients who previously chose St. Luke's inpatient rehabilitation center no longer have St. Luke's as an option. (Nolan, Tr. 6351, *in camera*; Andreshak, Tr. 1796-1797; Dagen, Tr. 3256-3257, *in camera*).

1064. St. Luke's inpatient rehabilitation center provided high-quality care before it was closed and some patients – in particular, those who live in Maumee and Bowling Green – are inconvenienced by having to go to Flower Hospital instead of St. Luke's for these services. (Andreshak, Tr. 1797-1799).

1065. Revenue from patients who would have gone to St. Luke's inpatient rehabilitation center but must now go to more expensive Flower Hospital will generate approximately \$1.4 million in additional revenue for Flower Hospital compared to what these patients would have paid for the same services at St. Luke's. (PX00905 at 001 (spreadsheet containing calculations of various efficiencies), *in camera*; Dagen, Tr. 3257-3262, *in camera*).

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1066. ProMedica initially claimed [redacted] million in savings from consolidating inpatient rehabilitation services at Flower Hospital. (PX00020 at 011 (Compass Lexecon Report), *in camera*; PX02104 at 005-006 (¶ 9) (Akenberger, Decl.), *in camera*).

1067. ProMedica subsequently revised the savings that it claims may result from the inpatient rehabilitation consolidation from the original [redacted] million down to [redacted]. (PX02104 at 003 (Akenberger, Decl.), *in camera*).

(vii) Inpatient psychiatry

1068. The Navigant Report recommended that ProMedica [redacted] to align with a nationwide trend of fewer but larger providers of inpatient psychiatry. (Nolan, Tr. 6305-6306, *in camera*).

1069. The Navigant Report recommended that [redacted]. (Nolan, Tr. 6299-6300, *in camera*).

1070. St. Luke's provides very few inpatient psychiatry services, limited to 0.1 patients per day, and has zero psychiatric beds. (Nolan, Tr. 6328-6329, *in camera*; PX01931 at 042 (Akenberger, Dep. at 162), *in camera*).

c. Navigant's recommendations specific to St. Luke's

1071. During the course of its engagement by ProMedica, Navigant made recommendations for St. Luke's for the time period of 2011 to 2013 to include [redacted]. (Nolan, Tr. 6315-6316, *in camera*).

1072. Navigant also made recommendations for St. Luke's for 2014 to 2016 to include [redacted]. (PX0479 at 70; Nolan, Tr. 6316-6317, *in camera*).

d. Asserted cost savings from clinical integration

1073. ProMedica's Joinder with St. Luke's gives ProMedica more options and more opportunity to consolidate services across

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the system, as well as higher volumes to meet critical mass and develop centers of excellence. (Nolan, Tr. 6321-6322, *in camera*).

1074. The Navigant study reported that officials from St. Luke's and ProMedica estimated that the clinical integration strategy would result in operational efficiencies that would total [redacted] million annually. (PX0479 at 14; Nolan, Tr. 6355-6356, *in camera*).

1075. The [redacted] million in asserted efficiencies (F. 1074) is for the entire clinical integration. Many of the clinical integration projects and recommendations do not involve St. Luke's. (PX01946 at 019-023 (Nolan, Dep. at 67-85); Nolan, Tr. 6354-6355, *in camera*).

1076. Navigant did no independent analysis to determine the reasonableness of the estimated efficiencies of [redacted] million annually. Navigant only "had some discussions with [ProMedica] in terms of what some of their assumptions were." (Nolan, Tr. 6355-6356, *in camera*). Additionally, the cost of the clinical integration, over three years, is estimated to be [redacted] million. (PX01946 at 034 (Nolan, Dep. at 128)).

7. Quality programs and systems

1077. Each of ProMedica's hospitals, as well as Paramount and ProMedica Physician Group, has its own quality council. (PX01930 at 007 (Reiter, Dep. at 19)).

1078. ProMedica also has service line and institute quality councils for the cancer institute, the orthopedic institute, the heart and vascular institute, and a fourth related to critical care services. (PX01930 at 008 (Reiter, Dep. at 22-23)).

1079. ProMedica's corporate quality department provides quality report cards to measure how each hospital and business unit is doing based on valid quality metrics. (PX01930 at 007 (Reiter, Dep. at 19-20)).

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1080. ProMedica compares its performance with and sets its goals in comparison to national quality scores and best practices, as well as local and regional hospitals. (RX25 at 027 (Reiter, Dep. at 99-100)). In that way, ProMedica tracks the quality performance of each of its business units. (PX01930 at 007 (Reiter, Dep. at 20)).

1081. Following the Joinder, ProMedica began the process of bringing St. Luke's into its system-wide quality efforts. For example, ProMedica took steps to bring St. Luke's into its patient safety council, which includes the safety officers from all of ProMedica's provider organizations. (PX01930 at 016 (Reiter, Dep. at 56-57)).

1082. ProMedica also involved St. Luke's in its best practice standardization initiatives. (PX01930 at 016-017 (Reiter, Dep. at 57-58)).

1083. Some of ProMedica's best practices are outdated and not on-par with the practices at St. Luke's. (E.g., PX01611 at 001; PX01610 at 001-003).

1084. Prior to the Joinder, St. Luke's ranked as the highest quality, lowest cost hospital in the Toledo market. F. 758-759.

1085. Additional facts on ProMedica's and St. Luke's quality of care are found at II.M.8.

1086. Electronic Intensive Care Unit ("eICU") is a computerized telemonitoring system that allows ProMedica to monitor all of its ICU beds across the system from a central control tower. (PX01930 at 008 (Reiter, Dep. at 24)).

1087. ProMedica implemented eICU to achieve better critical care quality scores. (PX01930 at 047 (Reiter, Dep. at 180)).

1088. ProMedica determined that implementing its eICU program of remotely monitoring critical care patients saved [redacted] lives by the end of 2010. (PX00605 at 004, *in camera*).

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1089. St. Luke's did not have the eICU system before the Joinder. (RX25 at 019 (Reiter, Dep. at 66); PX01930 at 047 (Reiter, Dep. at 180-181)).

1090. In the early Joinder discussions, ProMedica identified the eICU as a potential benefit that St. Luke's would realize from joining the ProMedica system. (PX01930 at 047 (Reiter, Dep. at 180-181)).

1091. After the Joinder, St. Luke's is required to pay for all of the equipment and system upgrades itself. (PX01850 at 074 (¶ 108) (Town Rebuttal Report)).

1092. Smart pumps are computerized infusion pumps that allow for medication to be infused into the body through veins, like an IV. (RX25 at 018 (Reiter, Dep. at 65)).

1093. Unlike regular IVs, smart pumps are computerized allowing the hospital staff to set safe limits for drug doses and alerting the staff if the dosing exceeds those limits. (RX25 at 018 (Reiter, Dep. at 65)).

1094. ProMedica believes that smart pumps improve quality of care by reducing medication errors. (RX25 at 018 (Reiter, Dep. at 65)).

1095. St. Luke's did not have smart pumps before the Joinder. (RX25 at 019 (Reiter, Dep. at 66); PX01930 at 047 (Reiter, Dep. at 180-181)).

1096. St. Luke's had been planning to acquire smart pumps before the Joinder, had already obtained quoted prices, and was determining how to integrate the smart pumps into their EMR system. (PX1609; PX1613 at 002; PX01850 at 074 (¶ 108) (Town Rebuttal Report)).

1097. As a result of the Joinder, St. Luke's was able to join with other ProMedica system hospitals to lease infusion pumps at a favorable lease rate. (Johnston, Tr. 5412-5413, *in camera*).

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1098. St. Luke's may have been able to obtain discounts by purchasing smart pumps through a purchasing organization such as VHA, which St. Luke's used to reduce cost during its supply chain initiative. (PX01909 at 049 (Dewey, IHT at 189), *in camera*; PX01933 at 023, 028 (Oppenlander, Dep. at 82-84, 102-103), *in camera*).

8. Efficiencies identified by Compass Lexecon

1099. ProMedica began exploring efficiency opportunities related to its Joinder with St. Luke's in the spring of 2010 to develop ideas and quantify possibilities. (Hanley, Tr. 4619-4621, *in camera*; PX00421 at 010-011, *in camera*).

1100. ProMedica hired Compass Lexecon to help identify potential efficiencies. (Hanley, Tr. 4625, *in camera*; Oostra Tr. 5868, *in camera*).

1101. The May 6, 2010 "Efficiencies Analysis of the Proposed Joinder of ProMedica Health System and OhioCare Health System" ("Compass Lexecon Report") is a summary of the efficiencies analysis that was prepared by ProMedica management and the economic consulting firm Compass Lexecon. (PX00020 at 001-039 (Compass Lexecon Report), *in camera*; PX02104 at 002 (¶ 5) (Akenberger, Decl.), *in camera*; PX01906 at 075 (Oostra, IHT at 293), *in camera*).

1102. Mr. Akenberger, ProMedica's Senior Vice President of Finance, submitted a declaration that discussed ProMedica's claimed efficiencies. Mr. Akenberger's December 23, 2010 declaration is a more recent summary of efficiencies. (PX02104 (Akenberger, Decl.), *in camera*; PX02105 (Exhibits to Akenberger, Decl.), *in camera*).

1103. Kathleen Hanley, ProMedica's CFO, testified that Mr. Akenberger was one of the key employees familiar with the specifics and details of ProMedica's efficiencies analysis. (Hanley, Tr. 4729, *in camera*).

1104. Mr. Akenberger did not testify at trial. During his deposition, Mr. Akenberger described himself as the lead

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individual responsible for the financial analysis, substantiation, and verification of ProMedica's claimed efficiencies. He testified that, to the extent an efficiency required financial substantiation, he was responsible for the financial analysis and that either he or members of his staff reviewed the documentation to make sure it was appropriate. (PX01931 at 025, 026 (Akenberger, Dep. at 93, 100), *in camera*).

1105. The proposed efficiencies contained in the Compass Lexecon Report represent an "initial plan." (Oostra, Tr. 6148 ("first plan"); PX01906 at 074 (Oostra, IHT at 291), *in camera* ("initial plan")). Mr. Oostra, ProMedica's CEO, testified that the efficiencies contained in the report were "preliminary" and he felt that "if we don't find those efficiencies, we will find other efficiencies." (Oostra, Tr. 6145, 6148; PX01906 at 075 (Oostra, IHT at 294), *in camera*).

1106. Since the closing of the Joinder on August 31, 2010, ProMedica and St. Luke's have established a steering committee that has charged approximately 20 integration teams to further develop the efficiencies opportunities summarized in the Compass Lexecon Report and identify new opportunities not identified in the Compass Lexecon Report. (RX31 at 026 (Akenberger, Dep. at 97-98)).

1107. The efficiencies that Compass Lexecon helped to identify consisted of cost savings, backroom functions, and combining separate programs. (Hanley, Tr. 4648, *in camera*).

1108. The preliminary efficiency estimates in the Compass Lexecon Report were based on ProMedica's past experiences, and the best data ProMedica had at that time, but ProMedica did not consider them to be final projections because due diligence was still ongoing. (Hanley, Tr. 4650-4651, *in camera*).

1109. ProMedica estimated that it could achieve about [redacted] million in annual savings as a result of the Joinder with St. Luke's, as well as approximately [redacted] million in capital avoidance savings, and related operating cost savings of [redacted] million "resulting primarily from the avoidance of capital and operating costs associated with the construction and

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operation of a hospital at Arrowhead and a new bed tower at Flower Hospital.” (PX00020 at 004, *in camera*; Hanley, Tr. 4650, *in camera*). (Arrowhead hospital and Flower bed tower discussed *infra* F. 1120-1128).

1110. ProMedica viewed the preliminary efficiency estimates in the Compass Lexecon Report as a general road map to understand how St. Luke’s entry into its system may affect the system’s entities. (Hanley, Tr. 4652).

1111. ProMedica understood that the efficiencies estimates in the Compass Lexecon Report would evolve as due diligence continued and the parties could “drill down” further on the data. (Hanley, Tr. 4652-4653, *in camera*).

1112. Since ProMedica developed its preliminary efficiency analysis in the spring of 2010, ProMedica’s estimated efficiency gains from the Joinder have increased above the original [redacted] million estimate. (Hanley, Tr. 4728, *in camera*).

1113. ProMedica’s CFO, Kathleen Hanley, testified that the conclusions in the Compass Lexecon Report were “estimates” and based on a “gut feeling” that the Joinder would generate savings. (Hanley, Tr. 4728, *in camera*; PX01903 at 054 (Hanley, IHT at 206-207), *in camera*).

1114. Douglas Deacon, St. Luke’s Vice President of Professional Services, had not even seen the Compass Lexecon Report before his investigational hearing in September 2010. (PX01908 at 050 (Deacon, IHT at 191-192), *in camera*). His involvement with the development of the analysis was “nil,” even though he believed that such an analysis was “something [he] should be involved with.” (PX01908 at 050-051 (Deacon, IHT at 193-194), *in camera*).

1115. Eric Perron, St. Luke’s Computer Information Systems Director, testified that neither he nor his staff was involved in quantifying the information technology-related savings that ProMedica claims St. Luke’s may experience as a result of the Joinder. (PX01928 at 038 (Perron, Dep. at 145), *in camera*). When presented during his deposition with the portion of the

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Compass Lexecon Report containing ProMedica's claimed EMR savings for St. Luke's, Mr. Perron indicated that he had never seen the document and was unaware of the claimed savings. (PX01928 at 040 (Perron, Dep. at 150-151), *in camera*).

1116. Dennis Wagner, St. Luke's Interim Treasurer at the time of the Joinder, had never before seen the Compass Lexecon Report when he was presented with a copy during his investigational hearing in September 2010. (PX01915 at 040 (Wagner, IHT at 156), *in camera*). Mr. Wagner testified that the report's claimed savings for supply chain efficiencies involved "no[] or very little analysis." (PX01915 at 052 (Wagner, IHT at 204), *in camera*). He said of the speech-and-hearing services efficiency claim: "I don't believe this claim." (PX01915 at 045 (Wagner, IHT at 173), *in camera*).

1117. One ProMedica document states that the timeline in which to achieve efficiencies was deliberately revised to be "more aggressive" in order to meet the anticipated reaction of the FTC. (PX01136 at 001, *in camera*).

1118. Revenue enhancements that ProMedica claims will result from improving St. Luke's coding and charge capture practices have no impact on the quality or quantity of clinical services that St. Luke's provides to patients. (Hanley, Tr. 4733-4735, *in camera*; PX00020 at 030 (Compass Lexecon Report), *in camera*). These practices will merely increase the amount that is paid to St. Luke's by patients (or their insurers) for the same quantity and quality of services. (Hanley, Tr. 4733-4735, *in camera*).

1119. The bulk of the claimed efficiencies from the Joinder are avoided capital costs. (PX00020 at 006-007 (Compass Lexecon Report summary of efficiencies), *in camera*; PX02104 at 003-005 (chart summarizing claimed efficiencies in Mr. Akenberger's affidavit), *in camera*).

a. Construction of a hospital at Arrowhead

1120. ProMedica claims that, as a result of the Joinder, it may be able to avoid spending [redacted] million on constructing

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and equipping a new hospital at its Arrowhead property (located less than three miles from St. Luke's). (PX00020 at 035 (Compass Lexecon Report), *in camera*; PX02104 at 016-017 (¶ 30) (Akenberger, Decl.), *in camera*).

1121. ProMedica had identified developing the Arrowhead property on its 2008-2010 Strategic Goals and Implementation Plan but temporarily postponed its Arrowhead plans because of the recession which began in 2008. ProMedica has not needed to pursue these plans because of the Joinder. (PX02104 at 016-017 (¶ 30) (Akenberger, Decl.), *in camera*; RX114 at 251, *in camera*).

1122. ProMedica has owned the Arrowhead land for a decade. (PX01906 at 022 (Oostra, IHT at 82), *in camera*). The 2010-2012 Strategic Plan, the most recent such plan to be created prior to ProMedica's merger negotiations with St. Luke's, does not mention constructing a new hospital at Arrowhead. (Joint Stipulations of Law and Fact, JX00002A ¶ 49; Hanley, Tr. 4720-4721, *in camera*; PX00006 (ProMedica Hospitals' 2010-2012 Strategic Goals and Objectives), *in camera*; PX00007 (ProMedica 2010-2012 Strategic Goals and Objectives), *in camera*).

1123. Ms. Hanley, ProMedica's CFO, explained that the Joinder eliminated the need to construct a new hospital. (PX01903 at 063 (Hanley, IHT at 243-244), *in camera*).

1124. Mr. Akenberger, current Senior Vice President of Finance and a financial executive at ProMedica for most of the last decade, has seen little financial analysis of constructing a hospital at Arrowhead. (PX01931 at 038 (Akenberger, Dep. at 145-146), *in camera*; PX01912 at 004-005 (Akenberger, IHT at 9-11), *in camera*). Construction of a new ProMedica general acute-care hospital at Arrowhead Park was discussed in a past ProMedica central region capital budget that was not approved by the ProMedica Board. (RX31 at 039 (Akenberger, Dep. at 150-151, *in camera*)).

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b. Construction of a bed tower at Flower Hospital

1125. The Compass Lexecon Report indicates that the Joinder may enable ProMedica to avoid spending [redacted] million to construct a second bed tower to increase bed capacity at Flower Hospital. (PX00020 at 036 (Compass Lexecon Report), *in camera*; PX02104 at 17 (¶ 31) (Akenberger, Decl.), *in camera*).

1126. ProMedica's most recent pre-Joinder Strategic Plans did not evidence an intention to construct a second bed tower at Flower Hospital. (Joint Stipulations of Law and Fact, JX00002A ¶ 48 ("The construction of a new bed tower at Flower Hospital did not appear on ProMedica's 2010-2012 Strategic Plan."); PX00006 (ProMedica Hospitals' 2010-2012 Strategic Goals and Objectives), *in camera*; PX00007 (ProMedica 2010-2012 Strategic Goals and Objectives), *in camera*). At no time in the two to three years leading up to the Joinder did ProMedica generate any plans relating to construction of a new bed tower at Flower Hospital. (Hanley, Tr. 4542-4543).

1127. The construction of a new bed tower at Flower Hospital has not appeared on any capital budget approved by the ProMedica Board since January 1, 2007. (Joint Stipulations of Law and Fact, JX00002A ¶ 47). Ms. Hanley testified that the Flower Hospital bed tower project "did not end up ... at the top of the list from a capital allocation standpoint." (Hanley, Tr. 4541-4542). She also stated that ProMedica's plans for financing the project were "premature until . . . we prioritize [and] authorize [the project,]" and said that such plans had not yet reached the ProMedica Board level. (PX01903 at 064 (Hanley, IHT at 248-249), *in camera*).

1128. The proposed bed tower would add 136 beds to Flower Hospital, of which 92 would be classified as either psychiatric or skilled nursing facility beds. (PX01931 at 041 (Akenberger, Dep. at 158-160), *in camera*). However, St. Luke's has no skilled nursing facility or psychiatric beds. (PX01931 at 042 (Akenberger, Dep. at 161-162), *in camera*).

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9. Other asserted benefits

1129. St. Luke's employees received a 1 percent pay increase on January 1, 2011 and a second 1 percent pay increase in July 2011. (Johnston, Tr. 5373).

1130. In June 2011, all employees received a one-time financial thank-you. Full-time employees received \$200; part-time employees received \$100; and contingent employees received \$25. (Johnston, Tr. 5373).

1131. In the past, as its patient volumes increased before the Joinder, St. Luke's was forced to place many of its nursing staff on mandatory call. (Johnston, Tr. 5365). Mandatory call requires a nurse to be on call beyond their normal hours of work and in most cases being on call resulted in nurses being called in and required to work overtime. (Johnston, Tr. 5365).

1132. Being part of ProMedica enables St. Luke's to tap into the ProMedica staffing pool to help ramp up staffing at its facilities. (Johnston, Tr. 5373-5374). St. Luke's has been able to use ProMedica's nurse staffing pool and reduce the number of units that have mandatory call duty. (Johnston, Tr. 5386-5387).

1133. St. Luke's has been able to utilize the services of ProMedica's physician recruiters to help with physician recruitment. (Johnston Tr. 5374).

1134. Since the Joinder, ProMedica's recruiters have assisted three of St. Luke's physician groups with their recruitment efforts. (Johnston, Tr. 5386). ProMedica's recruiters have already helped recruit certified registered nurse anesthetists for St. Luke's anesthesiology group. (Johnston, Tr. 5385-5386).

1135. Through ProMedica's partnership with the University of Toledo, all full-time employees will receive free tuition to any undergraduate or graduate program. Part-time employees will receive 50 percent tuition. (Johnston, Tr. 5374).

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1136. St. Luke's has improved its cash-on-hand after payroll from \$1.6 million at the time of the Joinder to a current total of between \$3 and \$7 million. (Johnston, Tr. 5380).

1137. St. Luke's has been able to pool its investments with the ProMedica investment pool and reduce investment fees. (Johnston, Tr. 5373).

1138. St. Luke's deferred capital projects in 2009 including [redacted]. (RX56 at 024-025 (¶¶ 61-62)).

1139. Since the Joinder, St. Luke's has started or is about to start work on several deferred capital projects, including [redacted]. (Johnston, Tr. 5495-5497, *in camera*).

1140. Since the Joinder, [redacted]. (Johnston, Tr. 5496-5497, *in camera*).

1141. At the time of the Joinder, St. Luke's had \$65 million in cash and investments, compared to a total estimated cost of less than [redacted] million to complete the deferred projects identified in F. 1138 above. (Joint Stipulations of Law and Fact, JX00002A ¶ 34; Den Uyl, Tr. 6571-6572, *in camera*).

10. Expert testimony on efficiencies

1142. Neither of Respondent's expert witnesses conducted any analyses or offered any opinions on whether Respondent's claimed efficiencies are cognizable under the Merger Guidelines. Ms. Guerin-Calvert testified that she has not conducted an efficiencies analysis. (Guerin-Calvert, Tr. 7580; PX01925 at 013 (Guerin-Calvert, Dep. at 42)).

1143. Mr. Den Uyl testified that he did not analyze Respondent's claimed efficiencies to determine whether they are cognizable under the Merger Guidelines. For instance, Mr. Den Uyl did not analyze whether ProMedica's claimed efficiencies are merger-specific, and he has no expert opinion on the issue. Mr. Den Uyl testified that he would be qualified to conduct an efficiencies analysis in this case – if he were asked to do so – because he has conducted such analyses in numerous other cases,

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including cases involving hospital mergers. However, he was not asked to conduct such an analysis in this case. (Den Uyl, Tr. 6515-6516).

1144. Mr. H. Gabriel Dagen, Complaint Counsel's expert, is the only expert witness in this case who conducted an analysis of the efficiencies asserted by Respondent. Mr. Dagen is the only expert witness in this case who analyzed each of the claimed efficiencies to determine whether they are merger-specific and presented an expert opinion on whether ProMedica's claimed efficiencies are cognizable under the Merger Guidelines. (See Dagen, Tr. 3245, *in camera*).

III. ANALYSIS

A. Jurisdiction

The Complaint is brought pursuant to the provisions of the Federal Trade Commission Act ("FTC Act") and charges Respondent with violating Section 7 of the Clayton Act, 15 U.S.C. § 18. Section 7 of the Clayton Act provides:

No person subject to the jurisdiction of the Federal Trade Commission shall acquire, directly or indirectly, the whole or any part of the stock or other share capital . . . of another person . . . where in any line of commerce or in any activity affecting commerce in any section of the country, the effect of such acquisition may be substantially to lessen competition, or tend to create a monopoly.

15 U.S.C. § 18. The word "person" includes corporations and associations existing under or authorized by the laws of any state.

15 U.S.C. § 12(a). Pursuant to Section 11 of the Clayton Act, the Commission is expressly vested with jurisdiction to determine the legality of a corporate acquisition under Section 7. 15 U.S.C. § 21(b); *R.R. Donnelley & Sons Co.*, 1995 FTC LEXIS 450, at *11. Sections 7 and 11 of the Clayton Act apply to acquisitions involving nonprofit hospitals. *FTC v. University Health, Inc.*, 938 F.2d 1206, 1214-17 (11th Cir. 1991).

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The Complaint challenges the acquisition by ProMedica Health System, Inc. (“ProMedica”) of St. Luke’s Hospital (“St. Luke’s”) pursuant to a joinder agreement, dated May 25, 2010, and effective as of September 1, 2010 (“Joinder”). F. 9-11. ProMedica is a nonprofit health-care system incorporated in the state of Ohio and headquartered at 1801 Richard Road, Toledo, Ohio. F. 1. ProMedica’s health-care system serves northwestern and west-central Ohio and southeastern Michigan. F. 1. Prior to the Joinder, ProMedica’s hospitals in Lucas County were: The Toledo Hospital (“TTH”), Toledo Children’s Hospital, Flower Hospital (“Flower”), and Bay Park Community Hospital (“Bay Park”). F. 53. Prior to the Joinder, St. Luke’s was a nonprofit general acute-care community hospital located at 5901 Monclova Road, Maumee, Ohio, and a wholly-owned subsidiary of OhioCare Health System, Inc. (“OhioCare”). F. 6, 10. Pursuant to the Joinder, ProMedica became the sole corporate member or shareholder of St. Luke’s and other affiliated entities. F. 11. Pursuant to a voluntary Hold Separate Agreement, the parties agreed, pending the outcome of these administrative proceedings, to a number of provisions designed to temporarily preserve St. Luke’s viability, competitiveness, and marketability. F. 12-13. The Hold Separate Agreement prevents, among other things: (1) ProMedica’s termination of St. Luke’s health-plan contracts (while allowing health plans the option to extend their contracts with St. Luke’s past the termination date, if a new agreement is not reached); (2) the elimination, transfer, or consolidation of any clinical service at St. Luke’s; and (3) the termination of employees at St. Luke’s without cause. F. 13.

In its Answer to the Complaint, Respondent admits that ProMedica, through its relevant operating subsidiaries, is, and at all relevant times has been, engaged in commerce or in activities affecting commerce, within the meaning of the Clayton Act. Answer ¶ 10. Respondent further admits that the Joinder constitutes an acquisition under Section 7 of the Clayton Act. Answer ¶ 10. Further, the parties stipulate that ProMedica, including its relevant operating subsidiaries, is, and at all relevant times has been, engaged in activities in or affecting “commerce” as defined in Section 4 of the FTC Act, 15 U.S.C. § 44 (2006), and Section 1 of the Clayton Act, 15 U.S.C. § 12 (2006). Joint Stipulations of Law and Fact, JX00002A ¶ 53.

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Accordingly, the Commission has jurisdiction over Respondent and the subject matter of this proceeding, pursuant to Section 7 of the Clayton Act.¹⁰

B. Burden of Proof and Statutory Framework

The parties' burdens of proof are governed by Federal Trade Commission Rule 3.43(a), Section 556(d) of the Administrative Procedure Act ("APA"), and case law. Pursuant to Commission Rule 3.43(a), "[c]ounsel representing the Commission . . . shall have the burden of proof, but the proponent of any factual proposition shall be required to sustain the burden of proof with respect thereto." 16 C.F.R. § 3.43(a). Under the APA, "[e]xcept as otherwise provided by statute, the proponent of a rule or order has the burden of proof." 5 U.S.C. § 556(d). The APA, "which is applicable to administrative adjudicatory proceedings unless otherwise provided by statute, 'establishes . . . [the] preponderance-of-the evidence standard.'" *In re Rambus Inc.*, No. 9302, 2006 FTC LEXIS 101, at *45 (Aug. 20, 2006) (quoting *Steadman v. SEC*, 450 U.S. 91, 95-102 (1981)), *rev'd on other grounds*, 522 F.3d 456 (D.C. Cir. 2008), *cert. denied*, 129 S. Ct. 1318 (2009). See *In re Automotive Breakthrough Sciences, Inc.*, No. 9275, 1998 FTC LEXIS 112, at *37 n.45 (Sept. 9, 1998) (holding that each finding must be supported by a preponderance of the evidence in the record); *In re Adventist Health System/West*, No. 9234, 1994 FTC LEXIS 54, at *28 (Apr. 1, 1994) ("Each element of the case must be established by a preponderance of the evidence.").

Section 7 of the Clayton Act prohibits the acquisition of assets "in any line of commerce or in any activity affecting commerce in any section of the country, [where] the effect of such acquisition may be substantially to lessen competition, or to tend to create a monopoly." 15 U.S.C. § 18. Congress used the phrase "'may be substantially to lessen competition' to indicate that its concern

¹⁰ Nonprofit corporations, such as ProMedica, are not exempt from the FTC's jurisdiction under the Clayton Act. See *University Health*, 938 F.2d at 1214-17 (holding that 15 U.S.C. § 21 grants the FTC jurisdiction to enforce Clayton Act § 7 and contains no exemption for nonprofit corporations).

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was with probabilities, not certainties.” *FTC v. H.J. Heinz Co.*, 246 F.3d 708, 713 (D.C. Cir. 2001) (quoting *Brown Shoe Co. v. United States*, 370 U.S. 294, 323 (1962)). “Thus, to establish a violation of Section 7, the FTC need not show that the challenged merger or acquisition will lessen competition, but only that the loss of competition is a ‘sufficiently probable and imminent’ result of the merger or acquisition.” *FTC v. CCC Holdings, Inc.*, 605 F. Supp. 2d 26, 35 (D.D.C. 2009) (quoting *United States v. Marine Bancorp., Inc.*, 418 U.S. 602, 623 (1974)).

“Ephemeral possibilities” of anticompetitive effects, however, are not sufficient. *Marine Bancorp.*, 418 U.S. at 623; *see also* *FTC v. Tenet Health Care, Inc.*, 186 F.3d 1045, 1051 (8th Cir. 1999). Rather, “there must be ‘the reasonable probability’ of a substantial impairment of competition by an increase in prices above competitive levels to render a merger illegal under § 7. A ‘mere possibility’ will not suffice.” *United States v. Long Island Jewish Med. Center*, 983 F. Supp. 121, 136-37 (E.D.N.Y. 1997) (quoting *Fruehauf Corp. v. FTC*, 603 F.2d 345, 351 (2d Cir. 1979)).

The first step in analyzing a Section 7 case is to determine the “line of commerce” and the “section of the country”; in other words, to determine the relevant product and geographic markets. *United States v. Oracle Corp.*, 331 F. Supp. 2d 1098, 1110 (N. D. Cal. 2004); *R.R. Donnelley & Sons*, 1995 FTC LEXIS 450, at *37-38. *See United States v. General Dynamics Corp.*, 415 U.S. 486, 510 (1974) (“[D]elineation of proper geographic and product markets is a necessary precondition to assessment of the probabilities of a substantial effect on competition within them.”).

Complaint Counsel bears “the burden of proving a relevant market within which anticompetitive effects are likely as a result of the acquisition.” *R.R. Donnelley & Sons*, 1995 FTC LEXIS 450, at *38. *Accord Tenet Health Care*, 186 F.3d at 1052; *Adventist Health Sys./West*, 1994 FTC LEXIS 345, at *10.

The second step in analyzing a Section 7 case is to determine whether the effect of the acquisition “may be substantially to lessen competition, or to tend to create a monopoly.” 15 U.S.C. § 18. In *United States v. Baker Hughes, Inc.*, 908 F.2d 981, 982-83 (D.C. Cir. 1990), the D.C. Circuit adopted an analytical

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approach to Section 7 cases, which has been followed in subsequent cases. *E.g.*, *FTC v. Chicago Bridge*, 534 F.3d 410, 423 (5th Cir. 2008); *Heinz*, 246 F.3d at 715. That analytical framework, by which the government can establish the probable effect of an acquisition, has traditionally consisted of a burden shifting exercise with three parts.

First, the government must establish a prima facie case that an acquisition is unlawful. *Baker Hughes*, 908 F.2d at 982; *Heinz*, 246 F.3d at 715. Typically, the government establishes a prima facie case by showing that the transaction in question will significantly increase market concentration, thereby creating a presumption that the transaction is likely to substantially lessen competition. *Chicago Bridge*, 534 F.3d at 423; *Heinz*, 246 F.3d at 715. The government can establish a presumption that the transaction will substantially lessen competition by showing that the acquisition will lead to undue concentration in the relevant markets. *Baker Hughes*, 908 F.2d at 982.

Second, once the government establishes its prima facie case, the respondent may rebut it by producing evidence to cast doubt on the accuracy of the government's statistical evidence as predictive of future anticompetitive effects. *Chicago Bridge*, 534 F.3d at 423; *Baker Hughes*, 908 F.2d at 982. "Nonstatistical evidence which casts doubt on the persuasive quality of the statistics to predict future anticompetitive consequences may be offered to rebut the prima facie case made out by the statistics." *Kaiser Alum. & Chem. Corp.*, 652 F.2d 1324, 1341 (7th Cir. 1981). Factors which may be considered to rebut a prima facie case include "ease of entry into the market, the trend of the market either toward or away from concentration, and the continuation of active price competition." *Id.* In addition, courts and the Commission typically consider "efficiencies, including quality improvements, after the government has shown that the transaction is likely to reduce competition." *In re Evanston NW Healthcare Corp.*, No. 9315, 2007 FTC LEXIS 210, at *191 (Aug. 6, 2007) (citing *Heinz*, 246 F.3d at 715, 720). Rebuttal evidence may also include factors relating to competition in the relevant market or the competitive or financial weakness of the acquired company. *Baker Hughes, Inc.*, 908 F.2d at 985 (citing, *e.g.*, *Lektro-Vend Corp. v. Vendo Co.*, 660 F.2d 255, 276 (7th Cir.

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1981) (acquired company's deteriorating market position both before and after acquisition rebutted prima facie case); *United States v. International Harvester Co.*, 564 F.2d 769, 773-79 (7th Cir. 1977) (company successfully rebutted prima facie case by showing, inter alia, financial weakness of acquired company, de facto independence of acquired company from acquiring company, strong level of competition in relevant market, and tendency of the market toward even stronger levels of competition) (other citations omitted).

Third, and finally, if the respondent successfully rebuts the prima facie case, the burden of production shifts back to the government and merges with the ultimate burden of persuasion, which is incumbent on the government at all times. *Chicago Bridge*, 534 F.3d at 423; *Baker Hughes*, 908 F.2d at 983.

Courts recognize, however, that in practice, evidence is often considered all at once and the burdens are often analyzed together. *Chicago Bridge*, 534 F.3d at 424-25 (citing *University Health*, 938 F.2d at 1218-19). "The Ninth and Eleventh Circuits interpret *Baker Hughes*' burden-shifting language as describing a flexible framework, rather than an air-tight rule." *Chicago Bridge*, 534 F.3d at 424. As a practical matter, the distinction between the burden of production and the ultimate burden of persuasion can be elusive. See *Baker Hughes*, 908 F.2d at 991. Thus, in *Chicago Bridge*, where the government's prima facie case addressed why the respondent's rebuttal evidence was not sufficient or not credible, the court held that the Commission could conclude that the respondent's burden of production on rebuttal had not been satisfied, without having to formally switch the burden of production back to the government. *Chicago Bridge*, 534 F.3d at 424; *Evanston*, 2007 FTC LEXIS 210, at *141-42 ("Although the courts discuss merger analysis as a step-by-step process, the steps are, in reality, interrelated factors, each designed to enable the fact-finder to determine whether a transaction is likely to create or enhance existing market power.") (citing *Baker Hughes*, 908 F.2d at 984 (Section 7 inquiry is of a "comprehensive nature"))).

This more flexible approach of considering the evidence all at once and analyzing the burdens of proof together accommodates the practical difficulties in separating the burden to persuade and

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the burden to produce, and “allows the Commission to preserve the *prima facie* presumption if the respondent . . . fails to satisfy the burden of production in light of contrary evidence in the *prima facie* case.” *Chicago Bridge*, 534 F.3d at 425. *See also Oracle*, 331 F. Supp. 2d at 1111 (noting that the Supreme Court and appellate courts acknowledge the need to adopt a flexible approach in determining whether anticompetitive effects are likely to result from a merger, and that the Merger Guidelines view statistical and non-statistical factors as an integrated whole, avoiding the burden shifting presumptions of the case law).

C. The Relevant Market

1. Product market

a. Generally applicable standards

Proper definition of the product market is “a necessary precondition to assessment” of the effect of a merger or acquisition on competition. *General Dynamics*, 415 U.S. at 510; *see Brown Shoe*, 370 U.S. 294, 324 (1962) (interpreting the phrase “any line of commerce” in Section 7 of the Clayton Act to require determination of the product market). To prevail, Complaint Counsel bears the burden of identifying a relevant market. *FTC v. Lundbeck, Inc.*, 650 F.3d 1236, 1239 (8th Cir. 2011); *United States v. SunGard Data Sys.*, 172 F. Supp. 2d 172, 182-83 (D.D.C. 2001); *Long Island Jewish Med. Center*, 983 F. Supp. at 137 (“[T]he Government has the burden of identifying the credible properly defined relevant markets . . .”).

“Prerequisite to establishment of the *prima facie* case by the FTC is definition of the ‘relevant market’ within which the merged entity would have significant market power.” *FTC v. Butterworth Health Corp.*, 946 F. Supp. 1285, 1289-90 (W.D. Mich. 1996), *aff’d*, 1997 U.S. App. LEXIS 17422 (6th Cir. 1997) (citing *FTC v. Freeman Hosp.*, 69 F.3d 260, 268 (8th Cir. 1995)). A relevant market consists of “products that have reasonable interchangeability for the purposes for which they are produced – price, use and qualities considered.” *United States v. E.I. du Pont de Nemours Co.*, 351 U.S. 377, 404 (1956). “In determining relevant product markets, courts have traditionally considered two

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factors: ‘(1) the reasonable interchangeability of use and (2) the cross-elasticity of demand between the product itself and substitutes for it.’” *CCC Holdings Inc.*, 605 F. Supp. 2d at 38 (quoting *Brown Shoe*, 370 U.S. at 325). “Interchangeability of use and cross-elasticity of demand look to the availability of products that are similar in character or use to the product in question and the degree to which buyers are willing to substitute those similar products for the product.” *FTC v. Swedish Match*, 131 F. Supp. 2d 151, 157 (D.D.C. 2000) (citing *du Pont*, 351 U.S. at 393); *Evanston*, 2007 FTC LEXIS 210, at *144. Thus, “the relevant market is defined by identifying competitors who could provide defendants’ customers with alternative sources for defendants’ services in the event defendants, as the merged entity, attempted to exercise their market power by raising prices above competitive levels.” *Butterworth*, 946 F. Supp. at 1290 (citing *United States v. Mercy Health Services*, 902 F. Supp. 968, 975 (N.D. Iowa 1995), *vacated as moot*, 107 F.3d 632 (8th Cir. 1997)).

Under the 2010 revised Horizontal Merger Guidelines, the product market is defined by asking whether a hypothetical monopolist of the proposed product market could impose a small but significant and nontransitory increase in price (“SSNIP”) and not lose an amount of its sales to alternative products that would make the price increase unprofitable. U.S. Dep’t of Justice & Fed. Trade Comm’n, Horizontal Merger Guidelines, § 4.1 (Aug. 19, 2010) *available at* <http://www.ftc.gov/os/2010/08/100819hmg.pdf> (hereafter “Merger Guidelines § __”). *See, e.g., FTC v. Whole Foods Mkt.*, 548 F.3d 1028, 1038 (D.C. Cir. 2008); *Butterworth Health Corp.*, 946 F. Supp. at 1290, 1294. The Merger Guidelines provide that “what constitutes a ‘small but significant and nontransitory’ increase in price, commensurate with a significant loss of competition caused by the merger, depends on the nature of the industry and the merging firms’ positions in it.” Merger Guidelines § 4.1.2. Thus, while the Agencies most often use a SSNIP of five percent of the price paid by customers, “the Agencies may use a price increase that is larger or smaller than five percent.” Merger Guidelines § 4.1.2.

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While courts are not required to follow the Merger Guidelines' approach, many courts have applied either the hypothetical monopolist test or some related test that defines markets by determining the set of products over which a dominant or monopolist firm could exercise market power. *See, e.g., Coastal Fuels, Inc. v. Caribbean Petroleum Corp.*, 79 F.3d 182, 198 (1st Cir. 1996) ("The touchstone of market definition is whether a hypothetical monopolist could raise prices."); *Swedish Match*, 131 F. Supp. 2d at 160-61 (paraphrasing the Merger Guidelines and informally applying the hypothetical monopolist test).

Finally, courts continue to refer to "*Brown Shoe's* 'practical indicia' in determining the relevant market." *In re Polypore Int'l, Inc.*, No. 9327, 2010 FTC LEXIS 97, at *31 & n.19 (Dec. 13, 2010) (citations omitted); *see also CCC Holdings*, 605 F. Supp. 2d at 38 ("Courts have relied on several 'practical indicia' as aids in identifying the relevant product market[.]") (citations omitted). These indicia include industry or public recognition, the product's particular characteristics and uses, unique production facilities, distinct customers, distinct prices, and other factors. *CCC Holdings*, 605 F. Supp. 2d at 38.

b. Hospital context

A cluster of products or services can constitute a relevant market, even if the individual components of the cluster may not all be – and likely are not – interchangeable or substitutable. *See United States v. Philadelphia Nat'l Bank*, 374 U.S. 321, 356 (1963) (cluster of products and services constituting "commercial banking" constituted a relevant market); *FTC v. Staples*, 970 F. Supp. 1066, 1074 (D.D.C. 1997). As both experts in this case agreed, the purpose of the cluster market is to provide a convenient and efficient way to conduct a competitive analysis across a multitude of different services, instead of evaluating each individual service separately. (Guerin-Calvert, Tr. 7633; Town, Tr. 3666-3667). In cases analyzing hospital mergers, federal courts and the Commission have consistently held that general acute-care inpatient services are a "cluster of services" that constitute a relevant product market. *See, e.g., Freeman Hosp.*, 69 F.3d at 268; *University Health*, 938 F.2d at 1210-12; *United*

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States v. Rockford Mem'l Hosp., 898 F.2d 1278, 1284 (7th Cir. 1990); *Butterworth Health*, 946 F. Supp. at 1290-91; *Long Island Jewish Med. Center*, 983 F. Supp. at 138-40; *Evanston*, 2007 FTC LEXIS 210, at *146-48. A cluster market provides the ability to assess all services at once in the context of one market. (Guerin-Calvert, Tr. 7188). As set forth below, the record in this case does not support departing from this precedent.

c. Product market in this case

Both Complaint Counsel's and Respondent's expert witnesses agree that a cluster market approach is appropriate for defining the relevant product market in this case. (Guerin-Calvert, Tr. 7189; Town, Tr. 3665). The parties agree that a relevant product market is general acute-care ("GAC") inpatient hospital services. Complaint ¶ 12; Answer ¶ 12; CCB at 7; RB at 44-45.¹¹ Generally, the GAC inpatient hospital services offered by St. Luke's are also offered by the other hospitals or hospital systems operating in Lucas County, Ohio: ProMedica, Mercy Health Partners ("Mercy"), and University of Toledo Medical Center ("UTMC"). F. 56, 62, 66, 72, 80, 107. Services in the cluster market of all GAC inpatient hospital services use the same assets, the same operating rooms, the same beds, the same wards, the same nursing staff, and all require an overnight stay. F. 301.

The parties also agree that the "consumers" of these services are commercial health plans. Complaint ¶ 12 (defining a relevant market as GAC services "sold to commercial health plans"); Answer ¶ 12; CCB at 7; RB at 44-45. Commercial health plans, or managed care organizations ("MCOs"), include companies that negotiate provider networks with hospitals and offer health insurance products to employers. F. 45, 115. MCOs demand, and contract for, a broad array of inpatient hospital services together, such as medical/surgical care, on behalf of the members they insure. F. 304. When MCOs contract with hospitals, they do not distinguish between services available to commercially

¹¹ In addition, the parties agree that the following are excluded from the relevant product market: outpatient services, quaternary services, rehabilitation, skilled care, psychiatric care, detoxification services, and MDC Codes 2, 19, 20, and 17. F. 306.

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insured patients and government insured patients; they look at all services available at that hospital to any patient. F. 305.

The parties disagree on the following issues: 1) whether the product market includes complex tertiary services that St. Luke's does not provide; and 2) whether there is a separate relevant product market for inpatient obstetrical ("OB") services.

(i) Complex tertiary services that St. Luke's does not provide

Tertiary services generally involve highly-specialized treatments for higher acuity conditions, such as neurosurgery. F. 23. Respondent admits that St. Luke's provides few, if any, tertiary services and no quaternary services.¹² Respondent's Response to Request for Admission at ¶ 2 (hereafter, "Response to RFA"); Joint Stipulations of Law and Fact, JX00002A at ¶ 6. Thus, Complaint Counsel contends, tertiary services do not belong in the relevant service market. CCB at 11.¹³

Cases adjudicating hospital mergers are split on whether the GAC inpatient services market includes or excludes tertiary services, with some cases specifically excluding tertiary care. In *Butterworth*, the court defined the relevant market as general acute-care inpatient hospital services in part by rejecting "defendants' innovative effort to demonstrate that employers and third-party payors might respond to a price increase for primary and secondary acute-care services by steering outpatients and tertiary care patients away from the merged entity so as to inhibit or reverse such a price increase[.]" *Butterworth*, 946 F. Supp. at 1291. In *Long Island Jewish Medical Center*, where "[t]he

¹² Quaternary services are the most complex and include procedures such as transplants and tend to require very specific technologies. F. 25.

¹³ Complaint Counsel also argues that because patients are willing to travel farther to get certain tertiary services, those services do not belong in the relevant product market. CCB at 14. While it may be that the relevant geographic market for those tertiary services is broader than Lucas County, this does not provide a factual justification or legal basis for excluding those services from the relevant product market.

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Government's version of the product market [was] limited to primary and secondary care and exclude[d] tertiary care provided at the anchor hospitals," the court rejected the Government's "narrow definition" and found "that the Government failed to establish its definition of the relevant product market as an anchor hospital providing primary/secondary service." *Long Island Jewish Med. Center*, 983 F. Supp. at 137, 140.¹⁴

By contrast, other courts have included tertiary services. In *Sutter Health*, where the parties agreed that the relevant product market consisted of the cluster of services comprising acute inpatient care, the court noted, "the services and resources that hospitals provide tend to be similar across a wide range of primary, secondary, and tertiary inpatient services." *California v. Sutter Health Sys.*, 130 F. Supp. 2d 1109, 1119 (N.D. Cal. 2001). The court further noted that this product market included not only services provided by hospitals that offer the full range of general acute inpatient services, but also those available at "niche" hospitals, that compete with [the merging parties] in providing only part of the "cluster of services" that constitutes general acute inpatient care. *Id.* (citing *Forsyth v. Humana, Inc.*, 114 F.3d 1467, 1476 (9th Cir. 1997) ("Specialty shops which offer only a limited range of goods are generally considered in the same market with larger, more diverse, 'one-stop shopping' centers.")). Thus, in *Sutter Health*, the market was defined broadly enough to encompass services that were not offered by all hospitals in the relevant geographic market.

In *Evanston*, the relevant product market advanced by

¹⁴ Other cases cited by Complaint Counsel excluded tertiary care based on the agreement of the parties. *FTC v. Tenet Healthcare Corp.*, 17 F. Supp. 2d 937, 942 (E.D. Mo. 1998) ("The parties agree that the product market is general acute-care in-patient hospital services, including primary and secondary services, but not including tertiary or quaternary care hospital services."), *rev'd on other grounds*, 186 F.3d 1045 (8th Cir. 1999); *United States v. Mercy Health Servs.*, 902 F. Supp. 968, 976 (N.D. Iowa 1995) ("The parties have agreed that the relevant product market is acute-care inpatient services offered by both Mercy and Finley. This definition excludes inpatient psychiatric care, substance abuse treatment, rehabilitation services, and open heart surgery."), *vacated as moot*, 107 F.3d 632 (8th Cir. 1997) (transaction abandoned prior to decision on appeal). In *Mercy Health*, neither hospital offered tertiary care. *Id.* at 996.

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complaint counsel was “general acute-care hospital services, including primary, secondary, and tertiary services, sold to MCOs.” *Evanston*, 2007 FTC LEXIS 210, at *146. Whether the market should include tertiary services was not challenged by the respondent. *Id.* The Commission found that the acquired hospital there, similar to St. Luke’s here, did not provide the tertiary services provided by the acquiring hospital, but that this did not negate the interchangeability of the hospitals’ primary and secondary services. *Id.* at *197. In *University Health*, the court of appeals upheld the district court’s definition of the relevant product market as “in-patient services by acute-care hospitals,” even though the two merging hospitals “do not compete in every acute-care service,” stating that it did not appear that the district court intended to limit its market definition solely to the 19 major diagnostic categories in which these hospitals did compete. *University Health*, 938 F.2d at 1211 and n.11.

In seeking to exclude tertiary services on the basis that St. Luke’s does not supply complex tertiary services, Complaint Counsel seeks to shift the focus away from what customers demand toward what the sellers supply. It is well established, however, that market definition “focuses solely on demand substitution factors.” Merger Guidelines § 4 (defining a market by “customers’ ability and willingness to substitute away from one product to another in response to a price increase or a corresponding non-price change”). *See also Brown Shoe*, 370 U.S. at 325 (stating the “outer boundaries of a product market are determined by the reasonable interchangeability of use or the cross-elasticity of demand between the product itself and substitutes for it”). “In defining the relevant product market, the Court must consider what products or services a consumer, confronting a price increase, would reasonably substitute for the products or services of the merging parties.” *Long Island Jewish Med. Center*, 983 F. Supp. at 137. Therefore, it is important to look for what the consumer – here the MCOs – want or contract for.

The evidence in this case establishes that MCOs contract for a broad array of primary, secondary, and tertiary inpatient services from hospitals together in a single negotiated transaction. F. 304. The evidence also shows that the prices that MCOs negotiate for

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quaternary inpatient services, psychiatric and substance abuse services, and outpatient services are distinct from the prices for GAC inpatient services. F. 308-311. To narrow the product market to only those services that both St. Luke's and ProMedica actually provide is not what MCOs demand or contract to purchase from ProMedica, Mercy, or UTMC. Accordingly, the relevant product market will not be narrowed to exclude tertiary services that St. Luke's does not provide.

(ii) Inpatient OB services

In addition to a GAC inpatient hospital services market, the Complaint also alleges a separate market for inpatient OB services. Complaint ¶¶ 12, 14. Inpatient OB hospital services are a cluster of procedures relating to pregnancy, labor and delivery of newborns, and post-delivery care. F. 312. Complaint Counsel argues that it is appropriate to carve out inpatient OB services from the general acute-care cluster because the market participants and market structure for OB services differ significantly from the other GAC services. CCB at 16-17. In support, Complaint Counsel argues that, applying the hypothetical monopolist test of the Merger Guidelines, OB services is a separate relevant market because "no other services are reasonably interchangeable with, or substitutes for, inpatient obstetrical services." CCB at 20. In addition, Complaint Counsel cites evidence that two Lucas County hospitals, UTMC and Mercy St. Anne, do not provide OB services (F. 94, 110); that market participants separately track GAC and OB market shares (F. 314); and that ProMedica's and St. Luke's contracts with MCOs often specify different reimbursement rates for GAC inpatient services than for inpatient OB services (F. 317). CCB at 18-20.

In prior hospital merger cases, inpatient OB services have been included in the GAC inpatient services market. (Guerin-Calvert, Tr. 7229-7230). With the exception of the district court's opinion on the preliminary injunction related to this matter, no hospital merger case has recognized OB services as a separate product market. See *FTC v. ProMedica Health Sys. Inc.*, 2011 U.S. Dist. LEXIS 33434, at *147-49 (N.D. Ohio 2011).

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As Complaint Counsel pointed out in its Post-Trial Brief, the use of a cluster market of all GAC inpatient services is appropriate in hospital merger cases. CCB at 8 (“Because there are hundreds of inpatient medical and surgical services offered by general acute-care hospitals, it is analytically convenient, appropriate, and efficient to group these services in a single cluster market where ‘market shares and entry conditions are similar for each.’”). Nevertheless, Complaint Counsel seeks to carve out of the cluster market inpatient OB services because “no other services are reasonably interchangeable with, or substitutes for, inpatient obstetrical services.” CCB at 20. The argument that inpatient OB services constitute a separate product market because no other inpatient hospital services can substitute for them applies with equal force to other hospital services such as inpatient cardiac surgery, inpatient knee surgery, and inpatient gastro-intestinal services, but Complaint Counsel does not allege that those services constitute separate markets. That a patient seeking inpatient OB services cannot substitute an appendectomy for a Caesarian section utterly fails to provide a valid justification for carving out inpatient OB services into a separate product market. Indeed, to carve out individual hospital services would be contrary to the logic upon which the inpatient services “cluster market” rests. *See Sutter Health Sys.*, 130 F. Supp. 2d at 1119 (explaining that “[w]hile the treatments offered to patients within this cluster of services are not substitutes for one another (for example, one cannot substitute a tonsillectomy for heart bypass surgery), the services and resources that hospitals provide tend to be similar across a wide range of primary, secondary, and tertiary inpatient services”).

In addition, there is no basis in the evidence in this case for recognizing a separate product market for inpatient OB services. Negotiations between hospital providers and MCOs for inpatient services cover the full range of services that MCOs’ members may need, including inpatient OB services. F. 315. Many contracts with MCOs do not separately carve out OB rates from GAC inpatient rates. F. 316. That ProMedica and St. Luke’s analyze their market shares for OB services separately is of little significance, as the hospitals also track cardiac cases, orthopedics, and cancer services separately. F. 314.

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Furthermore, there is no evidence that hospitals can price-discriminate for inpatient OB services because inpatient OB services are provided in conjunction with other services, and the terms and conditions on which they are negotiated are very similar. F. 320. Thus, the potential for price discrimination does not provide a basis for carving out a separate inpatient OB services market. *See* Merger Guidelines § 4.1.4 (“If a hypothetical monopolist could profitably target a subset of customers for price increases, the Agency may identify relevant markets defined around those targeted customers, to whom a hypothetical monopolist would profitably and separately impose at least a [small but significant and non-transitory increase in price].”).

Accordingly, there is no basis in fact or law to deviate from many cases consistently finding GAC inpatient services to be a “cluster of services” that constitute a relevant product market or to carve out of this cluster one of those services. Complaint Counsel has failed to prove that inpatient OB services is a separate relevant product market, as is its burden. *See Tenet Health*, 186 F.3d at 1052; *Lundbeck*, 650 F.3d at 1239. Accordingly, the relevant product market in which to analyze the likely effects of the Joinder is all GAC inpatient hospital services – primary, secondary, and tertiary services – sold to commercial health plans.

2. Geographic market

The relevant geographic market is “the ‘area of effective competition . . . in which the seller operates, and to which the purchaser can practicably turn for supplies.’” *Philadelphia Nat’l Bank*, 374 U.S. at 359 (quoting *Tampa Elec. Co. v. Nashville Coal Co.*, 365 U.S. 320, 327 (1961)). To prove the relevant geographic market, Complaint Counsel must present evidence on “where consumers of hospital services could practicably turn for alternative services should the merger be consummated and prices become anticompetitive.” *Tenet*, 186 F.3d at 1052; *Freeman Hosp.*, 69 F.3d at 268.

In this case, Complaint Counsel and Respondent agree that the proper geographic market for GAC inpatient hospital services is

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Lucas County, Ohio. F. 322; CCB at 22; RB at 47. Because inpatient OB services do not constitute a separate product market (*see* Part III.C.1.c.ii., *supra*), argument and evidence relating to where consumers might turn for inpatient OB services is not relevant and, therefore, not addressed. With respect to the GAC inpatient services market, which includes OB services, the evidence establishes: no MCO has marketed a health plan to Lucas County customers without including at least one Lucas County hospital; a hypothetical monopolist controlling every hospital in Lucas County could increase the price of GAC inpatient services in Lucas County by at least 5 to 10 percent, a small but significant amount; with extremely rare exceptions, Lucas County residents do not use more distant providers of GAC inpatient hospital services; and hospitals in counties adjacent to Lucas County are not acceptable alternatives for one MCO's Lucas County members. F. 323-328, 332. Thus, the relevant geographic market in which to assess the likelihood of anticompetitive effects of the Joinder is Lucas County, Ohio.

D. Likelihood of Anticompetitive Effects

Although Complaint Counsel did not prove the relevant product markets advanced at trial, Complaint Counsel did prove one of the relevant product markets the Commission alleged in its Complaint: GAC inpatient hospital services sold to commercial health plans; and the relevant geographic market of Lucas County, Ohio. Complaint ¶¶ 12, 16. The analysis next turns to the likelihood of anticompetitive effects of the Joinder in this market, which includes primary, secondary, and tertiary services and inpatient OB services.

“[T]o satisfy section 7, the government must show a reasonable probability that the proposed transaction would substantially lessen competition in the future.” *University Health*, 938 F.2d at 1218 (citing *FTC v. Warner Communs. Inc.*, 742 F.2d 1156, 1160 (9th Cir. 1984)). “[A] merger which produces a firm controlling an undue percentage share 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

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to have such anticompetitive effects.” *Philadelphia Nat’l Bank*, 374 U.S. at 363. Thus, the government can establish a presumption that the transaction will substantially lessen competition by showing that the acquisition will lead to undue concentration in the relevant markets. *Chicago Bridge*, 534 F.3d at 423; *Baker Hughes*, 908 F.2d at 982.

In support of its position that the Joinder is likely to have anticompetitive effects, Complaint Counsel advances the following arguments: the Joinder is presumptively unlawful because it results in tremendous concentration in already highly-concentrated markets (CCB at 30-39); the Joinder eliminated close and vigorous competition between ProMedica and St. Luke’s (CCB at 39-50); the Joinder allows ProMedica to raise prices (CCB at 50-63); the Joinder will harm hospital quality (CCB at 63-66); and higher prices and lower quality will impact consumers directly (CCB at 66-68). These arguments, and Respondent’s counter-arguments thereto, are addressed, in turn, below.

1. Market shares and concentration

Calculation of market shares and market concentration provide the starting point for the analysis of whether a transaction is likely to substantially lessen competition. *CCC Holdings, Inc.*, 605 F. Supp. 2d at 46, 64. Market concentration is a function of the number of firms in the market and their respective market shares. *Butterworth*, 946 F. Supp. at 1294.

The Herfindahl-Hirschman Index (“HHI”) is the most prominent method of measuring market concentration, commonly used by the Department of Justice, the FTC, and courts in evaluating proposed mergers. *Butterworth*, 946 F. Supp. at 1294 (citing *University Health*, 938 F.2d at 1211, n.12; *FTC v. PPG Ind. Inc.*, 798 F.2d 1500, 1502-06 (D.C. Cir. 1986); *FTC v. Freeman Hosp.*, 911 F. Supp. 1213, 1218 (W.D. Mo. 1995), *aff’d* 69 F.3d 260 (8th Cir. 1995)). The HHI is calculated by squaring the market share of each competing firm in a market and adding the resulting numbers. Merger Guidelines § 5.3; *Butterworth*, 946 F. Supp. at 1294. Under the Merger Guidelines, a post-merger HHI above 2500 is deemed to reflect a highly

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concentrated market, and a merger resulting in a highly concentrated market and producing an increase in the HHI of between 100 and 200 points potentially raises significant competitive concerns. Merger Guidelines § 5.3.

However, “market share figures are not always decisive in a section 7 case.” *Hospital Corp. v. FTC*, 807 F.2d 1381, 1386 (7th Cir. 1986); *see also CCC Holdings*, 605 F. Supp. 2d at 64; Merger Guidelines § 5.3. “[T]he Supreme Court [has] cautioned that, although significant, statistics concerning market share and concentration are ‘not conclusive indicators of anticompetitive effects.’” *FTC v. Arch Coal, Inc.*, 329 F. Supp. 2d 109, 130 (D.D.C. 2004) (quoting *General Dynamics*, 415 U.S. at 498). Courts recognize that “determining the existence or threat of anticompetitive effects has not stopped at a calculation of market shares” and, therefore, “[a] finding of market shares and consideration of [the presumption created by market shares] should not end the court’s inquiry.” *Oracle*, 331 F. Supp. 2d at 1111; *see also Baker Hughes*, 908 F.2d at 992 (“The Herfindahl-Hirschman Index cannot guarantee litigation victories.”). Rather, the “structure, history, and probable future” of the market must be examined to determine whether market shares are indicative of likely anticompetitive effects from the Joinder. *General Dynamics*, 415 U.S. at 498.

Relying solely on market shares to analyze competitive effects is “especially problematic” when the transaction involves differentiated products, such as general acute-care inpatient services. *Oracle*, 331 F. Supp. 2d at 1122. “When dealing with a heterogeneous product or service, such as the full range of medical care, a reasonable finder of fact cannot infer monopoly power just from higher prices--the difference may reflect a higher quality more costly to provide--and it is always treacherous to try to infer monopoly power from a high rate of return.” *Blue Cross & Blue Shield United of Wis. v. Marshfield Clinic*, 65 F.3d 1406, 1411-12 (7th Cir. 1995).

The analysis turns next to the arguments and evidence advanced by the parties on market shares and concentration. Not surprisingly, the parties’ experts utilized different methods to arrive at their market share statistics. The experts differed in

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both their methods for calculating market shares in several areas and in the markets they used for calculating market shares.

With respect to the methodology used to determine market shares, Complaint Counsel's expert calculated market shares based on total patient days. F. 344. Respondent's expert calculated market shares based on billed charges and discharges. F. 344. Respondent additionally calculated market shares based on staffed beds and registered beds. F. 344. Respondent asserts that billed charges, rather than patient days, is a more appropriate measure of market shares, because billed charges reflect the fact that many diagnostic related groups ("DRGs") and service lines require care that costs hospitals more to provide, result in longer hospital stays, and generate higher revenue. RRB at 37. Complaint Counsel counters that billed charges do not give the most accurate view of the marketplace, because commercial insurers pay discounted prices for services, not the full chargemaster price.¹⁵ CRRFF 1054. Courts in hospital merger decisions have accepted various methods of measuring market shares. *E.g.*, *Butterworth*, 946 F. Supp. at 1294 (finding that the expert estimated the merging hospitals would control "47 to 65% of the market for general acute care inpatient hospital services . . . depending on whether market share is measured by licensed beds, discharges or inpatient revenues"); *Rockford Mem'l Hosp.*, 898 F.2d at 1283 (stating that "[t]he district judge estimated the combined market share of the parties to the merger . . . at between 64 and 72 percent, depending on whether beds, admissions, or patient days are used as the measure of output"). In this case, regardless of which method is used, the calculated market shares are not significantly different. *See* Part II.K.2., *supra*. Therefore, calculations of market shares are analyzed using each of the methods advanced by the parties.

With respect to the market used to determine market shares, the market used by Complaint Counsel's expert and Respondent's

¹⁵ A hospital chargemaster is a list of the prices for the hospital's services. F. 499.

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expert differed in two significant respects.¹⁶ First, Complaint Counsel's expert calculated market shares based on a market comprising only those GAC inpatient services (identified as diagnostic related groups) that both ProMedica and St. Luke's sold to MCOs, whereas the Complaint alleged the relevant market more broadly as "general acute-care inpatient hospital services sold to commercial health plans." (F. 342; *compare* PX02148 at 019-021 *with* Complaint ¶ 12). Respondent's expert included all available GAC inpatient services in her market share calculations.

F. 342. Second, Complaint Counsel's expert's calculation of market share for GAC inpatient hospital services excluded market shares for inpatient OB services. F. 343.¹⁷ Respondent's expert's calculations of shares of GAC inpatient hospital services included inpatient OB services. F. 343. As found in Part II.K.2., *supra*, and analyzed below, these differences in approaches do not significantly alter the conclusions one can draw from market share and concentration statistics.

Neither party's expert performed an HHI analysis on the market found to be the relevant product market in this case – all GAC inpatient hospital services – primary, secondary, and tertiary, and including inpatient OB services – sold to commercial health plans. This defect, however, is not fatal. Unlike in *Oracle*, where the court wholly rejected the plaintiff's proposed market definition and was left with no means of calculating market shares, 331 F. Supp. 2d at 1161, 1165, here there is sufficient data to evaluate whether Complaint Counsel is entitled to the presumption that the merger is likely to substantially lessen competition. Regardless of which method is used or how the GAC inpatient hospital services market is defined, the data overwhelmingly shows that the Joinder created market shares and concentrations in the relevant market that warrant a presumption

¹⁶ There were a number of other differences in the scope of the market used by the experts. However, because it is not material to the ultimate conclusion on market shares, these differences are not analyzed.

¹⁷ Complaint Counsel's expert calculated market shares and HHI for OB services separately and found markedly higher shares and concentration levels in its proposed inpatient OB services market. *E.g.*, PX02150 at 002. However, because inpatient OB services do not constitute a separate product market, discussion of these statistics is neither necessary nor appropriate.

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of illegality.

Complaint Counsel's expert's calculations for GAC inpatient hospital services, as Complaint Counsel's expert defined that market, show that post-Joinder, Respondent has a combined market share of 58.3%; the pre-Joinder HHI was 3312; the change in the HHI is 1078, which is well above the 200 point threshold of the Merger Guidelines; and the resulting post-Joinder HHI is 4391, which is well above the 2500 threshold to be considered "highly concentrated." F. 368.

Respondent's expert's calculations for GAC inpatient hospital services, as Respondent's expert defined that market, indicate that, post-Joinder, Respondent's combined market share is between 53% and 58%, whereas Mercy and UTMC's combined market share is between 38% and 45%. F. 357-360. Respondent's expert conceded that, using her relevant product market definition, the post-Joinder market is still highly concentrated and would be presumed to result in increased market power, with a post-Joinder HHI around 4000. F. 369.

In addition, as summarized by Complaint Counsel, the following alternative methods of viewing the market statistics could be used:

- Analyze market shares and HHIs based on the broader service and geographic markets proposed by Respondent's economic expert and add the University of Michigan Medical Center and the Cleveland Clinic as fringe competitors. Using this data, Respondent has a 43% market share, concentration increases by 560 points, and the resulting HHI is 2855.
- Analyze market shares and HHIs based on beds-in-use data prepared by Respondent's economic expert and add Wood County Hospital, Fulton County Health Center, Fremont Memorial Hospital, and H.B. Magruder Memorial as fringe competitors. Using this data, Respondent has a 47.8% market share, concentration increases by 662 points, and the resulting HHI is 3413.

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- Analyze market shares by expanding the geographic market to include Wood and Fulton counties. Using this data for GAC, Respondent has a 55.8% market share, concentration increases by 989 points, and the resulting HHI is 4037.
- Analyze market shares and HHIs in Lucas County based on all inpatient DRGs, including those that Respondent's expert excluded from her relevant service market definition and those DRGs that St. Luke's does not offer. Using this data, Respondent has a 58.7% market share in a combined GAC-OB market; concentration increases by 867 points in a combined GAC-OB market; and the resulting HHI is 4424 in a combined GAC-OB market. (Ohio Hospital Association Data; based on commercial patient days (7/09 – 3/10) including all Major Diagnostic Categories/DRGs).

(CCRB at 9-11). In addition, an internal document generated by ProMedica projected its GAC market share, combined with St. Luke's, to be 55% of the Toledo Metropolitan Statistical area, based on discharges. F. 363.

Under each one of the above scenarios, the statistics exceed the thresholds for presumptive illegality provided in the Merger Guidelines and *Philadelphia National Bank*, 374 U.S. at 364 (enjoining acquisition with 30 percent combined share and where many competitors remained). *See also University Health*, 938 F.2d at 1211 n.12, 1219 (prima facie case established where merger reduced competitors from five to four, and resulted in a combined market share of 43 percent, HHI increase of 630 points, and a post-merger HHI of 3200). Regardless of how the market shares are determined in this case, the Joinder results in a tremendous increase in concentration in a market that already was highly concentrated. The statistical evidence demonstrates that the Joinder results in a significant increase in the concentration of power in the GAC inpatient hospital service market and produces an entity controlling an undue share of the relevant product market.

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Respondent argues that the market share statistics in this case do not accurately predict the likelihood of anticompetitive effects because St. Luke's financial condition "suggests" that it would have been unable to sustain its market share in the future. RB at 50. "[A] defendant may rebut the government's prima facie case by showing that the government's market share statistics overstate the acquired firm's ability to compete in the future and that, discounting the acquired firm's market share to take this into account, the merger would not substantially lessen competition." *University Health*, 938 F.2d at 1221. According to Respondent, St. Luke's market share must be discounted by its financial weakness, which, absent the Joinder with ProMedica, would have limited its ability to continue to compete effectively in the market, and, thereby, would have diminished its competitive significance. RB at 54. However, to prevail on this argument, Respondent would have to make the "substantial showing" that St. Luke's purported financial weakness "would cause that firm's market share to reduce to a level that would undermine the government's prima facie case." *University Health*, 938 F.2d at 1221. For the following reasons, Respondent has failed to do so.

First, the competitive significance of removing an independent St. Luke's from the relevant market does not rest on St. Luke's percentage share of the relevant product market; indeed, it held the lowest market share among the four market participants in Lucas County. F. 357-360. Rather, as discussed below, despite St. Luke's relatively low market share, ProMedica's acquisition of St. Luke's has the effect of further concentrating an already concentrated market, by reducing the number of ProMedica's competitors from three to two. Part III.D.2.a., *infra*. In addition, as also discussed below, because of its location in Lucas County, St. Luke's is competitively significant, despite its relatively low market share. Part III.D.2.d., *infra*. Moreover, as discussed in Part III.E., *infra*, the evidence does not demonstrate that St. Luke's financial condition would render it competitively insignificant in the future. Thus, even if St. Luke's market share is discounted by its financial weakness, the evidence of the financial weakness of St. Luke's does not undermine the predictive value of Complaint Counsel's market share statistics. Accordingly, Complaint Counsel has established its prima facie case that the Joinder violates Section 7 of the Clayton Act.

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2. Elimination of competition between ProMedica and St. Luke's

More powerful than the market share and concentration statistics is the simple fact that after the Joinder, there are only two remaining competitors to ProMedica that provide GAC inpatient hospital services in Lucas County: Mercy and UTMC. The competitive significance of the elimination of St. Luke's as an independent entity is discussed below.

a. Two remaining competitors

The ProMedica hospital system, prior to the Joinder, included a children's hospital and three general population hospitals in Lucas County: The Toledo Hospital ("TTH"), Flower Hospital ("Flower"), and Bay Park Community Hospital ("Bay Park"). F. 53. TTH has approximately 550 staffed beds, offers all basic GAC services, as well as more specialized, higher-acuity tertiary services. F. 54-59. Flower has approximately 250 staffed beds, offers general acute-care, OB, outpatient radiation and chemotherapy, and post-acute services, but does not provide tertiary care. F. 60-65. Bay Park has approximately 86 staffed beds and is a full-service community hospital, offering all GAC services, including emergency, OB, and general medical-surgical services. F. 66-71. St. Luke's Hospital, prior to the Joinder, was a stand-alone, full-service community hospital with 178 staffed beds, which provided a range of outpatient and inpatient services, but performed few, if any, tertiary services. F. 72-78.

Of the two remaining competitors, one is a hospital system, Mercy, which includes three general population hospitals in Lucas County: St. Vincent, St. Anne, and St. Charles. F. 79. The other competitor is UTMC, a research and teaching hospital. F. 103-106. Within the Mercy system, St. Vincent has 445 staffed beds, and is a large, tertiary teaching facility with eight intensive care units, a Level I trauma center, a Level III OB unit, and a large cardiology service. F. 82-91. St. Anne has 96 staffed beds and is a general medical-surgical hospital with operating rooms. St. Anne does not offer tertiary services, OB services, psychiatric services, or serious emergency services. F. 92-97. St. Charles

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has approximately 150 staffed beds and is a general medical-surgical hospital that also offers Level II OB services. St. Charles is the only Lucas County hospital that offers Level II inpatient OB services, but does not offer tertiary services. F. 98-102. UTMC, a teaching hospital, has as its mission to support the academic needs of the University of Toledo, to deliver high-quality health-care, and to serve the tertiary and quaternary needs of the community. UTMC has approximately 224 staffed beds and provides GAC services, but does not offer inpatient OB services. UTMC is the only hospital in Lucas County that offers quaternary services. F. 103-113.

With the elimination of St. Luke's as an independent entity, only Mercy and UTMC remain in competition with ProMedica. Overwhelmingly, cases evaluating hospital mergers have not allowed a merger to proceed where the result is similar to this case -- to reduce the number of competitors from four to three. *E.g.*, *Hospital Corp.*, 807 F.2d at 1387, 1389 (holding that the reduction of the number of competing hospitals in the geographic market from 11 to 7, among other factors, supported the Commission's conclusion that the challenged acquisitions were likely to have anticompetitive effects); *Rockford Mem'l Hosp.*, 898 F.2d at 1284 (enjoining merger where there were four other acute-care hospitals remaining in the area); *University Health*, 938 F.2d at 1219 (enjoining merger where the acquirer would control approximately forty-three percent of the relevant market, and three smaller hospitals would share the remainder of the market). *But see Butterworth*, 946 F. Supp. at 1288, 1302 (allowing merger of four to three hospitals where defendants persuasively rebutted both the FTC's prima facie case and its additional evidence of anticompetitive effects).

In *Swedish Match*, the defendant argued that the two remaining manufacturers of loose leaf chewing tobacco would replace any competition lost by the acquisition and prevent the acquirer from unilaterally increasing prices. The court rejected this argument, holding that the weight of the evidence demonstrated that a unilateral price increase was likely because the acquisition would eliminate one of the acquirer's primary direct competitors. *Swedish Match*, 131 F. Supp. 2d at 168-69. As analyzed below, in this case, too, the evidence of the

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elimination of competition by St. Luke's, and the resulting effect upon ProMedica's bargaining power with MCOs, demonstrates a substantial likelihood of unilateral price increases by ProMedica.

b. Premerger competition between St. Luke's and ProMedica

The evidence shows that St. Luke's was a meaningful market participant in Lucas County. St. Luke's is the third-largest stand-alone hospital in Lucas County based on commercial volume, exceeded only by St. Vincent and TTH. F. 462. Although St. Luke's provided care only to approximately 10 commercially insured patients per day, ProMedica, by comparison, through its three general population hospitals, provided care to approximately 53 commercially insured patients per day. F. 463. The addition of ten commercially insured patients per day to ProMedica's total is not insignificant, as it amounts to a nearly 19 percent increase of commercially insured patients per day for ProMedica. The CEOs of both ProMedica and St. Luke's agree that, before the Joinder, St. Luke's viewed ProMedica as its "most significant competitor." F. 440. Furthermore, St. Luke's CEO testified that after he came to St. Luke's in 2008, his goal was to regain volume from ProMedica in St. Luke's core and primary service areas. F. 441.

As acknowledged by ProMedica in its own internal assessments, ProMedica saw St. Luke's as a competitor capable of taking significant patient volume away from ProMedica's nearby hospitals. F. 467-471. ProMedica calculated that St. Luke's readmission to Anthem's network in 2009 would cost ProMedica [redacted] million in gross margin annually. F. 471. Similarly, ProMedica believed that St. Luke's would draw Paramount patients away from ProMedica hospitals, once St. Luke's became part of Paramount's network pursuant to the Joinder Agreement. F. 467. ProMedica estimated that [redacted] Paramount commercial inpatient admissions at ProMedica hospitals would be redistributed to St. Luke's if St. Luke's was added to Paramount's network. F. 468. ProMedica also estimated that the impact on Flower Hospital could be [redacted] million of lost margin annually if St. Luke's was included in the Paramount network. F. 469.

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c. Elimination of a close substitute

With only two competitors to ProMedica remaining, Complaint Counsel argues that the elimination of St. Luke's as an independent entity will likely harm competition because St. Luke's was a close substitute for ProMedica's nearby hospitals. CCB at 38. Complaint Counsel posits that, under a unilateral effects theory, the merger of close substitutes leads to increased bargaining leverage and higher prices. CCB at 36. Respondent counters that Mercy, not St. Luke's, was ProMedica's closest competitor. RB at 58-61.

Cases and the Merger Guidelines recognize two types of anticompetitive effects: unilateral and coordinated.¹⁸ *Oracle*, 331 F. Supp. 2d at 1112-13; Merger Guidelines §§ 6, 7. Unilateral effects result when a merger leads to higher prices due to the loss of competition between the two merging firms, independent of the action of other firms in the market. *Evanston*, 2007 FTC LEXIS 210, at *157 (citations omitted). As the Merger Guidelines explain, “[u]nilateral price effects are greater, the more the buyers of products sold by one merging firm consider products sold by the other merging firm to be their next choice.” Merger Guidelines § 6.1. Therefore, the degree of and preferences regarding substitutability of hospitals in Lucas County are analyzed.

In evaluating whether buyers of hospital services consider services sold by ProMedica and St. Luke's to be close substitutes, an initial question is: from whose perspective should the issue of substitutability be evaluated? Respondent analyzes substitutability from the perspective of *the MCOs*, noting that MCOs do not consider St. Luke's to be a close substitute for the ProMedica hospital system. RB at 59. Complaint Counsel

¹⁸ Coordinated effects are reductions in competition caused by express or tacit interaction by the merged firm and the remaining firms in the market, with respect to competitive variables such as prices, price differentials, market shares, customers, or territories. *Oracle*, 331 F. Supp. 2d at 1113; *Evanston*, 2007 FTC LEXIS 210, at *157-58 (citation omitted). Complaint Counsel does not assert that the Joinder may result in coordinated effects and, therefore, the likelihood of coordinated effects need not be and is not addressed.

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analyzes substitutability from the perspective of the potential patient, asserting that *patients* who seek hospital services consider St. Luke's and one of ProMedica's hospitals to be close substitutes. CCRB at 12. Complaint Counsel's position appears somewhat inconsistent with the allegation in the Complaint that a relevant product market is GAC inpatient hospital services "sold to commercial health plans," Complaint ¶ 12, and the position of Complaint Counsel's expert that "[t]he competitive analysis properly focuses upon the Acquisition's impact on the hospital-MCO bargaining process," PX2148 at 014-015 (Town Expert Report), both of which focus on the perspective of the MCO.

In *Freeman*, the court of appeals addressed the issue of whose perspective governs as follows: "We realize that in the case of health care, the term 'consumers' often means not individual patients but large purchasers of health care such as managed care coalitions or third-party payors." *Freeman Hosp.*, 69 F.3d at 270 n.14. Nevertheless, in assessing the relevant geographic market, the court's inquiry focused upon "where patients could practicably turn for alternative sources of acute care inpatient hospital services." *Id.* at 270. The court in *Sutter Health System* also noted that the behavior of MCOs is important in analyzing where patients will seek acute-inpatient hospital services because "these organizations are to a large extent, the true consumer of acute inpatient services." *Sutter Health Sys.*, 130 F. Supp. 2d at 129 (citing *University Health*, 938 F.2d at 1213 n.13 (holding that the true customers of acute-inpatient services were third party payers)). But, "[a]n MCO's demand for hospital services is largely derived from an aggregation of the preferences of its employer and employee members." *Evanston*, 2007 FTC LEXIS 210, at *195. Accordingly, in this case, the perspectives of both the MCOs and the patients are relevant and are considered. See *Long Island Jewish Med. Center*, 983 F. Supp. at 134 (finding "that there [were] five categories of 'consumers' in [that] hospital merger case, including patients and MCOs).

As Respondent correctly points out, no MCO testified that, for purposes of its Toledo hospital provider network, it considers St. Luke's to be the "next best substitute" for ProMedica. RB at 59. Rather, all MCOs agreed that Mercy and ProMedica are each

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other's primary competitor. F. 442-447. The evidence further establishes that ProMedica's and Mercy's hospitals are similar in their locations and the types of services and acuity of care they offer. (*Compare* F. 53-71 *with* F. 79-102). For each ProMedica hospital, there is a Mercy hospital close by. *Id.* Each system has a large flagship hospital near downtown Toledo, a children's hospital, and two smaller community hospitals. *Id.* Because of their similar broad service offerings and geographic reach throughout the Toledo metropolitan area, MCOs believe that they must have either Mercy or ProMedica in their health plan. F. 442-447; 566-568. In contrast, St. Luke's is a small, stand-alone community hospital, offering a limited array of the least complex inpatient hospital services. F. 72-78.

The evidence further establishes that MCOs could not substitute St. Luke's for the ProMedica system. Prior to the Joinder, faced with an anticompetitive price increase, no MCO would have dropped ProMedica from its network in exchange for St. Luke's. F. 448-449. But MCOs can market, and successfully have marketed, networks with only one of the two main systems. F. 447. Thus, from the perspective of the MCOs when constructing a marketable network, the Mercy hospital system is the closest substitute to the ProMedica hospital system.

Complaint Counsel does not dispute that St. Luke's, as a single hospital, could not adequately replace ProMedica's three hospitals in the networks of the MCOs. CCRB at 13. Instead, Complaint Counsel asserts, the relevant inquiry is whether St. Luke's is a close substitute for any one of ProMedica's hospitals from the perspective of MCOs' members, because this is what affects ProMedica's bargaining leverage with MCOs. CCRB at 13. As acknowledged in *Evanston*, MCOs' demand for hospital services is largely derived from the preferences of their members. *Evanston*, 2007 FTC LEXIS 210, at *195-96 (noting that whether the MCO decides to drop a hospital that raises its prices depends on a potentially complex assessment of the preferences of its employer and membership base). There, the Commission concluded that the two merging hospitals were likely to be "close substitutes for MCOs' members and employers, and thus for the MCOs." *Evanston*, 2007 FTC LEXIS 210, at *196-97. Here, as in *Evanston*, the record demonstrates that the merging entities, St.

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Luke's and ProMedica, were close substitutes for employers and MCOs' members, and, thus, for the MCOs.

The evidence shows that MCOs enter contracts with hospitals or hospital systems in order to be able to offer employers, and their employees, a network for obtaining GAC inpatient hospital services. F. 234-235, 273-274. MCOs seek to offer marketable plans to employers, in terms of cost, geographical coverage, quality, and breadth of services, while at the same time staying competitive by, among other things, obtaining low reimbursement rates. F. 190, 203, 218, 231, 237-238, 278-279. Employers want a health plan that offers a network with broad provider access so that employees and their family members can use their preferred physician or hospital. F. 256, 281. MCOs believe that patients generally prefer to obtain basic or routine inpatient care in a hospital that is close to them. F. 283. Because MCOs must fulfill their members' preferences in order to be marketable, the question of where patients wish to turn for GAC inpatient hospital services is critical.

The question of where patients would turn is also integral to a diversion analysis. *Sutter Health Sys.*, 130 F. Supp. 2d at 1129-32. A diversion analysis seeks to quantify the extent of direct competition between a product sold by one merging firm and a second product sold by the other merging firm by estimating the diversion ratio from the first product to the second product. F. 453; Merger Guidelines § 6.1 ("Diversion ratios . . . can be very informative for assessing unilateral price effects, with higher diversion ratios indicating a greater likelihood of such effects."). *See also Swedish Match*, 131 F. Supp. 2d at 169 (stating that in determining the likelihood of a unilateral price increase, "the diversion ratio is important because it calculates the percentage of lost sales that go to [the acquired company]. High margins and high diversion ratios support large price increases, a tenet endorsed by most economists.").

In the context of a hospital merger, diversion analysis attempts to calculate the substitutability of one hospital for another; that is, it tries to answer the question: if a specific hospital was not available to patients, to which other hospitals would that hospital's patients go? F. 453. The diversion ratio measures the

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predicted share of a hospital's patients that would go to a specific alternative if that hospital was no longer available. F. 453.

Diversion analysis relies on actual choices of patients among hospitals, as reflected in the claims data routinely collected by MCOs. F. 454. The higher the diversion between two hospitals, the higher the substitutability of the hospitals. F. 455. A merger can produce significant price effects even though the merging parties do not have the highest diversions to one another. Merger Guidelines § 6.1; *Evanston*, 2007 FTC LEXIS 210, at *160 (stating that “[a] merger may produce significant unilateral effects even though a large majority of the substitution away from each merging product goes to non-merging products” (citing Merger Guidelines Commentary 27 and Jonathan B. Baker & Carl Shapiro, *Reinvigorating Horizontal Merger Enforcement* 10 (June 2007) (“[U]nilateral effects will arise so long as some customers of one of the merging firms consider its merger partner’s product as their second choice, even if more of the firms’ customers consider a third firm’s products to be their second choice.”))).

Professor Town performed a diversion analysis for specific health plans and concluded that for the members of five of the six major health plans in Lucas County, ProMedica is St. Luke’s next-best substitute.¹⁹ F. 459. That is, Town concluded, the highest share of those health plans’ members would go to a ProMedica hospital if St. Luke’s was unavailable. In performing this analysis, Town relied on data from the Greater Toledo Area. F. 456.

In summary, the diversion analysis supports the conclusion that St. Luke’s and one or more of the three ProMedica hospitals are close substitutes. It is not necessary, for purposes of finding unilateral effects, to demonstrate that St. Luke’s and ProMedica were the first and second choices for all consumers. *Evanston*, 2007 FTC LEXIS 210, at *160 (“[I]t is not necessary for the merged firms to be the closest substitutes for all customers, or

¹⁹ The sixth health plan is [redacted]. The fact that ProMedica was not the next-best substitute for St. Luke’s for [redacted] members may reflect the fact that, until recently, [redacted] was aligned with Mercy. (PX2148 at 047 (¶ 88) (Town Expert Report), *in camera*).

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even a majority of customers.”). Rather, if customers accounting for a “significant share of sales” view the merging parties as their first and second choices for a particular need, a merger can enable the merged firms to raise prices unilaterally. *Evanston*, 2007 FTC LEXIS 210, at *159. Thus, the fact that MCOs, when constructing a network, viewed the hospital systems of ProMedica and Mercy to be each other’s closest substitute is not a determinative issue.

d. Significance of St. Luke’s in southwest Lucas County

Southwest Lucas County is affluent, with a population that is “better insured” than the rest of Lucas County. F. 473. The area around St. Luke’s is one of the few around Toledo that is growing, with an increasing population of employed and commercially-insured patients. F. 473. St. Luke’s is easily accessible from major highways and is in a highly visible area. F. 473. Thus, St. Luke’s location in southwest Lucas County is a geographically desirable part of Lucas County. F. 473.

Complaint Counsel argues that the elimination of an independent St. Luke’s, as a result of the Joinder, is likely to have anticompetitive effects, in part, because of its location in southwest Lucas County, relying upon the importance to patients and MCOs of having a hospital located in southwest Lucas County. CCB at 41-43. Respondent counters that St. Luke’s location in southwest Lucas County is immaterial to any analysis of the competitive effects of the Joinder because the relevant geographic market is Lucas County in its entirety. Respondent further asserts that, even if the evidence shows patient preference for St. Luke’s within St. Luke’s service area, travel in the Toledo area is rapid and easy; hospitals in Lucas County are all located conveniently to patients, with short drive-times to and between any of the hospitals in Toledo; and patients frequently travel to more distant hospitals than the one closest to their homes. RB at 12, 53-54.

It must first be acknowledged that the relevant geographic market alleged in the Complaint, and found to be the geographic market in this case, is Lucas County, Ohio. *Supra* Part III.C.2.

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Southwest Lucas County, St. Luke's "core service area," or St. Luke's "primary service area" do not constitute the relevant geographic market.²⁰ Therefore, it would be inappropriate to rely on market shares derived solely from the subset of the market comprising St. Luke's core or primary service areas to conclude that, because ProMedica and St. Luke's have high market shares in this submarket, ProMedica now has market power. However, it is appropriate to rely on market shares in the subset comprising St. Luke's core or primary service area to evaluate patients' preferences, and, hence, the importance of St. Luke's to MCOs.

Complaint Counsel relies on consumer preference surveys that show that, for patients located near St. Luke's, St. Luke's and a ProMedica hospital were the most preferred. F. 450-452. According to St. Luke's internal documents, in St. Luke's core service area, St. Luke's and ProMedica had the first and second highest inpatient market shares, respectively, for GAC services for all patients. F. 494-496. According to Respondent's expert's calculations, in St. Luke's top ten zip codes by volume, accounting for 64 percent of admissions, ProMedica ranked first, with 43 percent, and St. Luke's ranked second, with 26 percent, of patient admissions. F. 497. Based on market shares, Professor Town concluded that patients residing in St. Luke's core service area prefer St. Luke's and ProMedica for inpatient services. F. 498. This conclusion is consistent with other courts' findings, in determining the relevant geographic market, that the hospital's distance from a patient's home is a consideration. *E.g., Rockford Mem'l Hosp.*, 898 F.2d at 1285 ("For the most part hospital services are local. People want to be hospitalized near their families and homes, in hospitals in which their own -- local -- doctors have hospital privileges.").

The average drive-time for St. Luke's patients is approximately 12 minutes. F. 488. Respondent points out that for patients located in each of St. Luke's top 10 zip codes from which it admits patients, the incremental drive-time to go to a

²⁰ St. Luke's defines its core service area as the eight zip codes surrounding St. Luke's, where 55 to 60 percent of the admission base comes from. St. Luke's defines its primary service area as the area where approximately 80 percent of St. Luke's patients come from. F. 362.

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different hospital is 18 additional minutes. F. 489. Respondent's expert's drive-time analysis shows that many patients for whom St. Luke's is the closest hospital travel to other hospitals that are farther away. F. 490. Thus, patient origin and drive-time analyses show that patients do not necessarily go to the next closest hospital. F. 491. This fact, however, does not contradict a finding that St. Luke's and ProMedica are the two most preferred hospitals in St. Luke's core service area.

In addition, the evidence shows that, in order to be saleable, networks offered by MCOs must have broad geographic coverage, including southwest Lucas County, to meet the preferences of their members. MCOs believe that patients generally prefer to obtain basic or routine inpatient care in a hospital that is close to them. F. 218, 278, 283, 475. For example, MMO's Vice President of Network Management, testified that MMO needed St. Luke's in its network to have a marketable product. F. 478. An analysis prepared for ProMedica projected that adding St. Luke's to the Paramount network could net Paramount as many as [redacted] new members. F. 482. Paramount's President testified that the addition of St. Luke's to Paramount's network in late 2010 made Paramount more attractive to employers in southwestern Lucas County and had a positive impact on Paramount. F. 481.

Although southwest Lucas County is not itself the relevant geographic market in this case, because it is important to MCOs for their networks to include a hospital in southwest Lucas County, the elimination of an independent hospital in southwest Lucas County is competitively significant. The significance of this fact directly relates to ProMedica's increased bargaining leverage in negotiations with MCOs, as more fully discussed below.

3. The Joinder gives ProMedica greater bargaining leverage

As discussed above, for many patients, St. Luke's and one of ProMedica's hospitals are patients' top two choices for GAC inpatient hospital services. Because many MCOs' members view St. Luke's as a close substitute to ProMedica's Flower Hospital

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and Toledo Hospital, before the Joinder patients could still have access to their first-choice or second-choice hospital – St. Luke’s – even if the MCO failed to reach an agreement with ProMedica. Similarly, because many MCOs’ members view ProMedica’s Flower or Toledo Hospitals as a close substitute for St. Luke’s, before the Joinder patients could still have access to their first-choice or second-choice hospital – a ProMedica hospital – even if the MCO failed to reach an agreement with St. Luke’s.

After the Joinder, St. Luke’s is no longer available as an alternative if an MCO fails to reach an agreement with ProMedica. As a result, MCOs that fail to reach an agreement with ProMedica can offer only a provider network consisting of UTMC and Mercy, which fails to include the top two hospital choices for many patients and which, the evidence shows, is believed to be less marketable. *See* Part II.M.1. In addition, after the Joinder, St. Luke’s is no longer an independent alternative for obtaining the geographic coverage that MCOs want in southwest Lucas County. F. 475-480. Even if patients *could* switch to more distant hospitals within Lucas County, MCOs competing to successfully market their products must fulfill their members’ *preference* not to travel too far and, specifically, the *preference* of their members in southwest Lucas County to go to either St. Luke’s, Flower, or TTH. Thus, the Joinder gives ProMedica greater bargaining leverage, as further explained below.

Similar evidence was relied upon in *Evanston* to find that the merger enabled the combined firm unilaterally to exercise market power. There, the Commission found:

If the MCO drops the hospital, it may cause some members who have a strong preference for that hospital to switch to another MCO, and cause employers with a significant number of such members to drop the MCO altogether. If a significant portion of an MCO’s members view a hospital that raises its prices as particularly important, the MCO likely will be more willing to pay some or all of the increase.

Evanston, 2007 FTC LEXIS 210, at *195-96.

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“Bargaining leverage” may be defined as the advantage, or perception of advantage, of a particular entity at the bargaining table to try to make use of certain attributes in the negotiation. F. 267. A hospital’s bargaining leverage with an MCO depends on how much the MCO perceives it would lose if the MCO failed to reach agreement with the hospital. F. 287-289, 557. The success or failure of a negotiation depends on the hospital’s and MCO’s respective “walk-away” points. F. 558. If a hospital demands rates above an MCO’s walk-away point, the MCO will refuse to contract with the hospital. F. 559.

Prior to the Joinder, the MCOs’ “walk-away” network with respect to St. Luke’s, *i.e.*, the network they had if they failed to reach agreement with St. Luke’s, consisted of ProMedica’s Lucas County hospitals, Mercy’s Lucas County hospitals, and UTMC. F. 576. Also prior to the Joinder, the MCOs’ “walk-away” network with respect to ProMedica’s Lucas County hospitals, *i.e.*, the network they had if they failed to reach agreement with ProMedica, consisted of St. Luke’s, Mercy’s Lucas County hospitals, and UTMC. F. 577.

As a result of the Joinder, the MCOs’ “walk-away” network with respect to ProMedica’s Lucas County hospitals, which now includes St. Luke’s, is Mercy’s Lucas County hospitals and UTMC. F. 578. MCOs believe that a network consisting of only the Mercy Hospitals and UTMC, without St. Luke’s and the ProMedica hospitals, would not be sufficiently marketable in Lucas County to be commercially viable. F. 566-567. For example, United believed it would face more difficulty serving its membership without ProMedica and St. Luke’s than it would without ProMedica’s pre-Joinder hospital network in Lucas County. F. 574. *See also* F. 575 (United representative testifying that [redacted]). Also, MMO believed that while it could have marketed insurance products that excluded ProMedica’s three Lucas County hospitals, it could not have marketed insurance products that excluded both ProMedica and St. Luke’s. F. 568. *See also* F. 588 (MMO representative testifying that ProMedica’s increased bargaining leverage enables ProMedica to name its price). MCOs unanimously agreed that a health plan consisting of only Mercy and UTMC would leave

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them without coverage in southwest Lucas County and, thus, would be unmarketable. F. 563-575.

Respondent, relying on *Tenet*, *Oracle*, and *Arch Coal*, argues that testimony of MCOs and employers regarding post-Joinder price effects is suspect and urges that their testimony be discredited because it is based solely on preferences and apprehensions. RB at 72-74. In *Tenet*, the court noted that “large, sophisticated third-party buyers can and do resist price increases” and stated that MCOs’ testimony that they would unhesitatingly accept a price increase was contrary to their economic interests and, therefore, suspect. *Tenet*, 186 F.3d at 1054. The court of appeals there criticized the district court’s reliance on the testimony of managed care payers, in the face of contrary evidence, that the for-profit entities would unhesitatingly accept a price increase rather than send their members to other hospitals. *Id.* at 1054. In *Oracle*, the court stated that “unsubstantiated customer apprehensions do not substitute for hard evidence.” *Oracle*, 331 F. Supp. 2d at 1131. There, the customer witnesses testified “with a kind of rote, that they would have no choice but to accept a ten percent increase.” *Id.* In *Arch Coal*, the court noted that “antitrust authorities do not accord great weight to the subjective views of customers in the market,” and stated that the concern expressed by the customers there “is little more than a truism of economics: a decrease in the number of suppliers may lead to a decrease in the level of competition in the market.” *Arch Coal*, 329 F. Supp. 2d at 145-46. There, the customer witnesses made only simple and conclusory statements about their concerns. *Id.* at 146.

In this case, unlike in *Tenet*, the evidence does not indicate that MCOs can easily send their customers to other hospitals. *E.g.*, F. 332 (hospitals in counties adjacent to Lucas County are not acceptable alternatives); F. 567 (a network consisting of only Mercy and UTMC would not be marketable). Furthermore, the MCOs did not give merely conclusory opinions, as in *Oracle* and *Arch Coal*, that they could not constrain unreasonable rate requests by ProMedica post-Joinder. Instead, the MCOs used general market knowledge, feedback from the field, and/or claims utilization data to determine the attractiveness and marketability of their offerings (F. 280) and provided explanations to support

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their beliefs. *E.g.*, F. 568 (MMO representative explaining that MMO could not market a product without ProMedica and St. Luke's due to travel distances); F. 570 (Aetna representative explaining that Aetna's network would lose more marketability without ProMedica and St. Luke's together by leaving Aetna without coverage in southwest Lucas County). In addition, MCO witnesses in this case relied on reviews of utilization data and pricing analyses, experience negotiating with health plans and evaluating provider networks, and their understanding of bargaining dynamics and provider-network marketability in Lucas County. *See, e.g.*, F. 586 ([redacted] conducted an analysis of the change in reimbursement rates); F. 591 (Aetna performed statistical analysis based on Aetna's contract rates and the typical pattern experienced by Aetna that the acquiring system would raise the acquired hospital's rate to the system-wide rate). Testimony from MCOs relating to expected price increases is also consistent with economic expert testimony, including the econometric and diversion analyses (*infra* Part III.D.4) that were lacking in *Oracle*. 331 F. Supp. 2d at 1172. Accordingly, the testimony of MCOs here is not completely unsubstantiated, is less suspect than the testimony given in the cases cited by Respondent, and is, therefore, given due weight.

Furthermore, the MCOs' beliefs that they could not market a network consisting of only Mercy and UTMC is entirely consistent with their real world experience. Indeed, as Respondent has stipulated, "[i]n at least the last ten years, no commercial health plan has offered a product with a hospital network consisting only of UTMC and Mercy." F. 565. *See also* F. 565 (Respondent's expert agreeing that a Mercy-UTMC network has never been used in the last twenty years). By way of example, FrontPath could not viably market a network consisting only of Mercy and UTMC, as it would account for less than [redacted] percent of FrontPath's current utilization in Lucas County. F. 572. One MCO, [redacted], prior to entering into a contract with ProMedica [redacted], failed to grow its membership in Toledo by marketing a network that consisted of only Mercy, UTMC, and St. Luke's. F. 575. Because a network consisting only of UTMC and Mercy is not marketable, ProMedica now has even greater bargaining leverage in its negotiations with the MCOs. Respondent's contrary argument,

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that MCOs can avoid any attempt by ProMedica to raise prices to anticompetitive levels by walking away from ProMedica and forming a UTMC-Mercy network, RB at 81-83; RRB at 55-56, is, therefore, rejected. This greater bargaining leverage allows ProMedica to increase rates (*i.e.*, prices) to MCOs, as analyzed below.

4. The Joinder gives ProMedica the ability to raise prices

Complaint Counsel argues that prior to the Joinder, ProMedica was already the dominant provider, charging the highest prices, and that the Joinder enables ProMedica to raise prices further. CCB at 50-59. Respondent counters that Complaint Counsel must show that the Joinder will enable (or has enabled) ProMedica to increase prices to supracompetitive levels and that Complaint Counsel has not met its burden of demonstrating that the Joinder will empower ProMedica to raise prices above competitive levels. RB at 42-44, 63-70.

Section 7 of the Clayton Act forbids mergers that are likely to hurt consumers by making it easier for the firms in the market to price above or farther above the competitive level. *Rockford Mem'l Hosp.*, 898 F.2d at 1283-84 (citing *Hospital Corp.*, 807 F.2d at 1386). However, “[s]ection 7 does not require proof that a merger or other acquisition has caused higher prices in the affected market. All that is necessary is that the merger create an appreciable danger of such consequences in the future. A predictive judgment, necessarily probabilistic and judgmental rather than demonstrable is called for.” *Hospital Corp.*, 807 F.2d at 1389 (internal citation omitted).

“In making a determination as to whether a merger will result in an anti-competitive effect, the courts have focused on whether the merger would likely cause the merged entity to wield sufficient market power to enable it to profitably increase prices.” *Long Island Jewish Med. Center*, 983 F. Supp. at 142 (citing *du Pont*, 351 U.S. at 391; *United States v. Archer-Daniels-Midland Co.*, 866 F.2d 242, 246 (8th Cir. 1988)). Thus, the starting point for evaluating whether the Joinder enables ProMedica to profitably increase prices is ProMedica’s market power.

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a. Market power

As analyzed above, before the Joinder ProMedica's market share was already higher than its competitors' market shares, whether calculated by registered beds, beds-in-use, or occupancy.

F. 356. Using Respondent's expert's calculations, ProMedica had between 42 and 49 percent of the market for GAC inpatient hospital services in Lucas County. F. 357-360. These same calculations by Respondent's expert show the following shares of the GAC inpatient hospital services market for ProMedica's three competitors: Mercy, 29 to 35 percent; UTMC, 9 to 11 percent; and St. Luke's, 5 to 12 percent. F. 357-360. After the Joinder, using these same calculations, ProMedica's GAC market share is anywhere from 53 to 58 percent. F. 357-360.

Market shares themselves can be an important indicator of market power. *See Brown Shoe*, 370 U.S. at 322 n.38 ("Statistics reflecting the shares of the market controlled by the industry leaders and the parties to the merger are, of course, the primary index of market power[.]"). As explained in *Rockford Memorial Hospital*:

Market share is the fraction of that output that is controlled by a particular supplier or particular suppliers whose market power we wish to assess. The higher the aggregate market share of a small number of suppliers, the easier it is for them to increase price above the competitive level without losing so much business to other suppliers as to make the price increase unprofitable; this is the power we call market power.

Rockford Mem'l Hosp., 898 F.2d at 1283.

In this case, Professor Town's examination of pre-Joinder hospital prices in Lucas County reveals a correlation between market shares and prices. F. 610. Professor Town found that ProMedica had the largest market shares and the highest reimbursement rates; Mercy, the next-largest system, had the second highest rates; UTMC, the third largest system, had the third highest prices; and St. Luke's, with the smallest market share, had the lowest prices in the market. F. 610. The

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increases in ProMedica's market shares, and the resulting increase in market concentration, create a strong presumption of enhanced market power as a result of the Joinder. (PX02148 at 035-036 (¶ 63) (Town Expert Report), *in camera*). In addition, as discussed below, the expectations of ProMedica's customers and the expectations of St. Luke's, as well as the economic analysis undertaken by Complaint Counsel's expert, support the conclusion that ProMedica wields sufficient market power to enable it to profitably increase rates (*i.e.*, prices).

b. Likely increase of St. Luke's rates to ProMedica's rates

Professor Town examined differences in the case-mix adjusted hospital prices in Lucas County prior to the Joinder and determined that ProMedica's average price was [redacted] percent higher than St. Luke's.²¹ F. 609. MCOs confirmed Professor Town's analysis of the relative price difference between ProMedica and St. Luke's by testifying that ProMedica's rates are the highest and St. Luke's rates are the lowest in Lucas County. F. 611. Respondent's own documents show that St. Luke's inpatient commercial insurance rates were about [redacted] percent below the market average. F. 535. Based on the evidence, as analyzed below, it is reasonable to expect that ProMedica will raise prices at St. Luke's to prices paid to ProMedica's other community hospitals in Lucas County, Flower and Bay Park.

MCOs expected ProMedica to raise prices at St. Luke's to prices paid at other ProMedica community hospitals. For example, Aetna expected ProMedica to raise the rates it pays to St. Luke's to the level of rates it pays to ProMedica. F. 590. Aetna performed an analysis of the Joinder's impact on Aetna's rates to St. Luke's and projected a [redacted] percent increase in

²¹ Case-mix adjustment is a calculation that takes into account the resources needed to treat patients, with the theory being that patients with more complicated illnesses utilize more resources than those who are not as ill. The methodology is tied to the DRG reimbursements. Thus, the case mix adjustment number is a weighted factor used by MCOs to make an apples-to-apples comparison between various rates at each hospital. F. 608.

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Aetna's rates to St. Luke's if these were to rise to the level of Aetna's rates to ProMedica. F. 591. [redacted] also conducted an analysis of the change in reimbursements to St. Luke's that would result if [redacted] rates to St. Luke's were increased to [redacted] rates to ProMedica's Flower, Bay Park, and TTH, and predicted that [redacted] rates to St. Luke's would "increase significantly," between roughly [redacted] and [redacted] percent. F. 586.

St. Luke's also anticipated that its reimbursement rates would be increased to the level of ProMedica's. F. 597-603. A presentation regarding potential affiliation partners, made to St. Luke's Board of Directors by Mr. Wakeman and other members of St. Luke's leadership team, states: "ProMedica had a significant leverage on negotiations with some of the [health plans]," and that this leverage would allow St. Luke's to obtain higher reimbursement rates. F. 598. A St. Luke's planning document, dated August 10, 2009, notes that an option for St. Luke's would be to "enter[] into an affiliation/partnership with a local health system with the express purpose to raise reimbursement rates to the level of our competitors." F. 597. Mr. Wakeman hoped that an affiliation with ProMedica would allow St. Luke's to obtain the higher reimbursement rates that ProMedica was receiving. F. 601. By joining ProMedica, St. Luke's anticipated as much as [redacted] million in additional revenues from [redacted], and Paramount. F. 603.

Because ProMedica's case-mix adjusted prices are [redacted] percent higher than St. Luke's rates as a volume-weighted average (F. 609), the likely increase of St. Luke's rates to ProMedica's rates alone is a significant rate increase in Lucas County. It must, however, be acknowledged that St. Luke's rates were below market. F. 535 (results of a 2009 study performed for St. Luke's by Navigant Consulting concluded that St. Luke's inpatient commercial insurance rates were about [redacted] percent below the market average); CCRFF 1789-1791. St. Luke's, as of August 2009, recognized that it had "extremely low reimbursement rates from third party payors," and viewed itself as having two options in the short term: "(1) St. Luke's develops a compelling argument to increase contracted rates with its major managed care customers (MMO, Anthem, Aetna, etc.) as an

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independent. (2) St. Luke's enters into an affiliation/partnership with a local health system with the express purpose to raise reimbursement rates to the level of our competitors." F. 389. See also Part II.L, *supra* (facts on St. Luke's financial condition as it considered whether to enter an affiliation with another partner). Indeed, Respondent's expert concluded "that a reasonable price increase at St. Luke's but-for the Joinder would have been in the range of 15 to 36% over the period 2011 through 2012." RX71(A) at 00052. Thus, because St. Luke's likely would have increased rates regardless of the Joinder, a finding that the Joinder is likely to result in price increases at St. Luke's does not, alone, satisfy Complaint Counsel's burden of showing that the Joinder is likely to cause anticompetitive price increases in the relevant market. However, Complaint Counsel has also shown, through its expert, that the Joinder enables ProMedica to raise rates at not only St. Luke's, but throughout the ProMedica hospital system, as discussed below.

c. Significant price increases predicted throughout the ProMedica system

As found in Part III.D.3., *supra*, ProMedica now has greater bargaining leverage in its negotiations with MCOs on rates for GAC inpatient hospital services. Complaint Counsel's expert, Professor Town, modeled the bargaining relationship between hospitals and MCOs in a GAC inpatient services market and used the "willingness to pay" model to measure the value that a hospital brings to a health plan's network, as perceived by the MCO's members. F. 612-613. The willingness to pay model is a tool to predict the effect of the elimination of competition on prices – that is, to isolate and quantify the Joinder's impact on the bargaining leverage of the merged hospitals. F. 613.

Professor Town's willingness to pay model predicts that the volume-weighted average (across ProMedica and St. Luke's) price will increase by 16.2 percent. F. 625. Allocating this increase between St. Luke's and ProMedica yielded predicted price increases of between 38.4 to 56.2 percent at St. Luke's and 10.8 percent at ProMedica's other hospitals.²² F. 628.

²² Professor Town recognized that ProMedica has claimed that St. Luke's was under-reimbursed by MCOs and, thus, also used a higher, pre-Joinder price

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Respondent and its expert criticize Professor Town's analysis. Although there may be flaws with Professor Town's model, none are so severe as to substantively undercut its predictive value. When Respondent's expert, Ms. Guerin-Calvert, added several variables to Professor Town's model, even those additions resulted in a projected price increase of 7.3 percent. F. 626. Complaint Counsel's expert's prediction of price increases is also consistent with the testimony of the MCOs who were unequivocal in testifying that ProMedica will be able to increase rates due to its newly enhanced bargaining leverage.

d. Post-Joinder pricing

Respondent asserts that its post-Joinder contract negotiations with MCOs do not show anticompetitive price increases and, therefore, support a conclusion that the Joinder will not enable ProMedica to raise rates beyond competitive levels. For example, ProMedica negotiated a new contract on behalf of St. Luke's with United, to be effective January 1, 2011, which results in rate increases for St. Luke's totaling about [redacted]; ProMedica negotiated a new contract with MMO for St. Luke's between November 2010 and January 2011, which resulted in a [redacted]; and pursuant to the Hold Separate Agreement (F. 13), ProMedica has not sought to terminate St. Luke's contract with Anthem, or increase St. Luke's rates to Anthem to be comparable to the rates that ProMedica is presently getting from Anthem for any of its hospitals. F. 642-643, 646-647, 650.

The post-Joinder contracts were negotiated under the auspices of the Hold Separate Agreement between FTC staff and ProMedica that constrained ProMedica's leverage by allowing health plans to extend their current contracts at existing rates. Thus, the rates that ProMedica has negotiated for St. Luke's do not necessarily reflect the full and unrestrained market power that ProMedica ultimately will have and can exercise as a result of the Joinder.

for St. Luke's, to predict an increase in St. Luke's price between 33.2 and 48.6 percent. F. 629.

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Moreover, it is well-settled that post-acquisition evidence that is subject to manipulation by the merging parties is entitled to little weight. As the Supreme Court explained in *General Dynamics*:

In *FTC v. Consolidated Foods Corp.*, 380 U.S. 592, 598, this Court stated that postacquisition evidence tending to diminish the probability or impact of anticompetitive effects might be considered in a § 7 case. . . . But in *Consolidated Foods* . . . and in *United States v. Continental Can Co.* . . . , the probative value of such evidence was found to be extremely limited, and judgments against the Government were in each instance reversed in part because “too much weight” had been given to postacquisition events. The need for such a limitation is obvious. If a demonstration that no anticompetitive effects had occurred at the time of trial or of judgment constituted a permissible defense to a § 7 divestiture suit, violators could stave off such actions merely by refraining from aggressive or anticompetitive behavior when such a suit was threatened or pending.

General Dynamics, 415 U.S. at 504-05. The probative value of post-acquisition evidence is deemed limited not just when evidence is actually subject to manipulation, but “whenever such evidence *could arguably* be subject to manipulation.” *Chicago Bridge*, 534 F.3d at 435 (citing *Lektro-Vend Corp.*, 660 F.2d at 276 (“The post-acquisition evidence in this case is the type which *cannot arguably have been subject to the defendant’s deliberate manipulation*, nor is it likely that the market was less competitive after the acquisition than it would have been otherwise.”); *Hospital Corp.*, 807 F.2d at 1384 (“Post-acquisition evidence *that is subject to manipulation* by the party seeking to use it is entitled to little or no weight.”) (emphasis added).

Applying the foregoing principles, the post-Joinder pricing evidence upon which Respondent relies is of the type that is subject to manipulation. It cannot credibly be disputed that any and all negotiations since the Joinder were under scrutiny. The negotiations took place during the FTC’s investigation and challenge of the Joinder and under the restrictions of the Hold

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Separate Agreement between the FTC and ProMedica, which obligated ProMedica to give health plans the option to extend their existing rates with ProMedica throughout the duration of the Hold Separate Agreement. F. 13. As such, ProMedica could “stave off” the alleged violations charged in this case “by refraining from aggressive or anticompetitive behavior,” *General Dynamics*, 415 U.S. at 505. Thus, in this case, evidence of Respondent’s post-Joinder negotiations with MCOs is arguably subject to manipulation and, therefore, entitled to little, if any, weight. *See Chicago Bridge*, 534 F.3d at 434-35.

e. Effect in the relevant GAC inpatient hospital services market

Respondent argues that the complexity and breadth of negotiations between MCOs and hospitals prevents Respondent from exercising its increased market power in the relevant market.

Respondent states: “But the negotiations between MCOs and hospital providers in Lucas County over the rates paid for inpatient hospital services do not occur in a vacuum – that is, in isolation from their negotiations for all other services the hospitals provide to an MCO’s insureds. Rather, MCOs and hospitals negotiate both reimbursement rates and other non-compensation terms and conditions to reach agreement for a single contract that covers all services the hospital offers (inpatient, outpatient, physician, and ancillary) for a variety of products marketed by the MCO.” RB at 55. Accordingly, Respondent argues, “no presumption about the joinder’s competitive effects can be drawn from the hospitals’ [market] shares [in the relevant market], which represent a small component of the services about which MCOs and hospitals negotiate and for which they contract.” RB at 56.

The evidence shows that hospital-MCO negotiations are complex and that each side tries to obtain the best rates it can. *See, e.g.*, 234-236, 509-516. In addition, hospitals typically strive for total reimbursement that exceeds the total cost of treatment of an MCO’s insureds so that the hospital can subsidize the care it provides to Medicare and Medicaid patients – reimbursement for whom does not cover the hospital’s costs – plus a margin for re-investment in the hospital’s infrastructure. F. 292, 517-520.

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Although there are various factors that affect negotiations between hospitals and MCOs and those negotiations encompass far more than GAC inpatient hospital services rates, these facts do not negate the simple fact that because ProMedica now has St. Luke's in its hospital system, and because MCOs need either ProMedica or St. Luke's in their networks, ProMedica now has market power to demand increased rates from MCOs for GAC inpatient hospital services. This market power did not exist prior to the Joinder.

Based on the evidence of increased market power, the importance to MCOs of having either St. Luke's or ProMedica in their networks, and the economic models that persuasively predict significant price increases, Complaint Counsel has demonstrated on the whole that it is likely that the Joinder enables ProMedica to exercise market power and increase prices. In addition, as analyzed below, Complaint Counsel has also demonstrated that consumers and employers would be directly impacted by any increase in rates charged by ProMedica to MCOs.

5. Higher prices impact consumers

The higher reimbursement rates that ProMedica can demand from MCOs will directly harm the employers and employees who use Lucas County hospitals. Self-insured employers, accounting for a large percentage of commercial business in Lucas County, directly pay the full cost of their employees' health-care claims to MCOs. F. 50, 654, 658. As ProMedica's CEO explained, if a Lucas County hospital or hospital system increases its rates to commercial MCOs, those increased costs are "passed on straightforward" to self-insured employers. F. 657. Thus, increases in hospital reimbursement rates impact self-insured employers directly.

Fully-insured employers pay a premium to an MCO and the MCO pays the costs of medical care received by employees. F. 47, 659. For fully-insured employers, when an MCO incurs a rate increase from a hospital, the MCO passes down the increased costs to employers in the form of higher premiums. F. 659. As one MCO representative made clear, "[w]ith the fully insured, I

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can't see any circumstance where we would not automatically pass [a rate increase] on through the premium increase." F. 659.

Health-care costs are a significant expense for businesses. F. 651. Inpatient hospital services account for approximately 20 to 25 percent of the total cost of health insurance premiums. F. 652-653. When employers face increased health-care costs, some employers might absorb the increase, but more typically, employers will be required to reduce their costs by restricting health benefits or by increasing the employees' share of the costs, through increased premium contribution, copays, deductibles, out-of-pocket maximums, or by otherwise revising compensation or benefits to reduce employer costs. F. 662. When costs for employee health insurance coverage increase for employers with union members, in order to offset the increased costs, employers may seek a collective bargaining agreement that will reduce service levels, increase the amount the union members must pay, reduce wages, or make other tradeoffs. F. 663.

6. Quality of care

Complaint Counsel contends that the Joinder will likely lead to higher prices and lower quality for consumers. CCB at 30. Complaint Counsel further argues that the Joinder will harm non-price competition by eliminating a high-quality independent hospital. Complaint Counsel asserts that, because hospitals compete on non-price dimensions, such as quality, the elimination of St. Luke's, a high-quality competitor that challenged other hospitals to keep service levels up, will result in diminished incentives for ProMedica and the other Lucas County hospitals to provide better services and improve quality. CCB at 60.

Respondent counters that there is no evidence indicating that the Joinder will, in fact, cause St. Luke's quality to decrease from its pre-Joinder levels. RRB at 47. To the contrary, Respondent asserts, the Joinder of ProMedica and St. Luke's will allow both ProMedica and St. Luke's to improve quality in the future. RB at 101-104.

The evidence shows that hospitals compete to be in an MCO's network. F. 239-241, 757. Once in that network, they compete

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to attract patients, including on the basis of quality. F. 242, 245, 772-773. In addition, the evidence shows that competition between hospitals tends to result in a higher quality of care. F. 781. According to Professor Town, decreased competition among hospitals reduces incentives to compete on such non-price dimensions as quality. F. 780.

Evidence of likely reduced incentives to compete on quality, however, does not necessarily translate into proof that quality among Lucas County hospitals is likely to decrease as a result of the Joinder. As the Commission noted in *Evanston*: “[q]uality of medical care is not easily defined or measured.” *Evanston*, 2007 FTC LEXIS 210, at *134. Further, “[t]he case law provides no clear answers regarding how, or whether, . . . claimed qualitative benefits ought to fit into a competitive effects analysis.” *Evanston*, 2007 FTC LEXIS 210, at *225. The Commission, in *Evanston*, noted that the district court, in *Rockford Memorial Corp.*, was of the opinion that “weighing the claimed quality improvements against the merger’s anticompetitive effects would require a ‘value choice . . . beyond the ordinary limits of judicial competence.’” *Evanston*, 2007 FTC LEXIS 210, at *225 n.97 (quoting *Rockford Memorial Corp.*, 717 F. Supp. 1251, 1288 (N.D. Ill. 1989), *aff’d*, 898 F.2d 1278 (7th Cir. 1990)). The Commission further noted, “[o]ther courts have been more receptive to quality-of-care arguments, but those decisions shed little light on how qualitative benefits are to be weighed against the competitive harm shown to result from a merger.” *Evanston*, 2007 FTC LEXIS 210, at *225-26 (citing *Tenet Healthcare*, 186 F.3d at 1053-54).

Under Section 7 of the Clayton Act, Complaint Counsel must show a reasonable probability that the proposed transaction would substantially lessen competition in the future. *University Health*, 938 F.2d at 1218. Typically, the government does so by making a prima facie case showing that the acquisition would produce a firm controlling an undue percentage share of the relevant market, and would result in a significant increase in the concentration of firms in that market. *Id.* Complaint Counsel has done so in this case. Complaint Counsel has also shown the likelihood of increased prices as a result of the Joinder. It is not necessary to also prove that the Joinder will likely harm the quality of hospital

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care. Accordingly, this decision need not, and does not, conclude whether the evidence demonstrates the likelihood of the anticompetitive effect of decreases in quality as well.²³

Respondent in this case asserts that the Joinder allows ProMedica and St. Luke's to make quality improvements which, according to Respondent, constitute procompetitive benefits of the Joinder that outweigh any anticompetitive effects. RB at 99-102.

The arguments and evidence on the issue of whether quality will increase are addressed in Part III.F., *infra*, which evaluates Respondent's asserted procompetitive benefits.

7. Asserted constraints upon ProMedica's exercise of market power

Respondent argues that the Joinder will not enable ProMedica to raise prices because various market forces and competitive conditions in the Toledo area will operate as competitive constraints, including: (1) excess inpatient hospital capacity and resulting repositioning by rivals, specifically Mercy's [redacted], RB at 75-80; RRB at 52-55; RRB at 59-62; *see also* RB at 79-80; and (2) the ability of MCOs, employers and physicians to "steer" patients to lower cost hospitals, RB at 80-81, 84-85; RRB at 56-59. As further explained below, Respondent's arguments are either legally or factually insufficient, and, therefore, do not outweigh Complaint Counsel's showing of likely anticompetitive effects.

a. Excess capacity and repositioning

The evidence demonstrates that there is excess inpatient hospital bed capacity in Lucas County. F. 664-672, 676. Based upon the number of staffed beds per thousand area residents, which is a standard metric used in health-care, the Toledo metropolitan area, as compared to other similar metropolitan areas in the United States, has substantially more beds per thousand

²³ Although the Complaint also alleged that the Joinder was likely to result in decreased breadth of available services, Complaint Counsel did not submit proposed findings or provide briefing on the allegation. As Complaint Counsel has declined to pursue that claim, this Initial Decision contains no findings or conclusions on the issue.

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residents. F. 668. Toledo has 3.63 beds per thousand residents, while Grand Rapids, Michigan, an area similar to Toledo, has just over 2 beds per thousand residents, and Detroit has approximately 2.5 beds per thousand residents. F. 669. In addition, the number of registered beds greater than staffed beds is an indicator of excess capacity because it also shows the number of beds that are not being deployed to meet patient demand. F. 670-671. With the exception of Bay Park, the majority of Lucas County hospitals have numbers of staffed beds that are well under their numbers of registered beds. F. 672. Another metric of excess capacity for Toledo area hospitals is the occupancy rate, which divides the average daily census of a hospital by the number of staffed beds or registered beds. F. 675. Occupancy rates for hospital beds in Lucas County, based upon an average daily census of inpatient bed use, are significantly below available staffed bed capacity. F. 676. Toledo's stagnant population further indicates that community need for inpatient hospital beds will not increase in the near future. F. 737-739. The foregoing evidence confirms Mercy's belief that "from a community need standpoint, all of St. Luke's beds could be eliminated from the Toledo area and not be missed." F. 667. Not surprisingly, neither Mercy nor UTMC have any plans to build more inpatient facilities in Lucas County. F. 485, 681, 750.

In addition, the evidence demonstrates that, due to Toledo's aging population, the number of Medicare patients will increase. F. 737, 740. At the same time, Toledo has a high unemployment rate and has experienced an exodus of employers, which translates into a decline in the number of commercially insured patients. F. 739, 742-744.

The evidence shows that Mercy intends [redacted]. F. 747. Mercy is [redacted]. F. 751, 753. Mercy's [redacted]. F. 750. In November 2009, Mercy had a tentative timeline [redacted] for accomplishing [redacted]. F. 754. However, currently, [redacted]. F. 754.

Respondent claims that the excess capacity of inpatient beds, and concomitant increased competition for commercially insured patients, means that rival hospitals will be in a position to, and will have to, compete aggressively for patients through

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repositioning, and that this response will militate against ProMedica raising prices. RB at 75. Respondent points to Mercy's [redacted] as evidence of such repositioning. *Id.* In support of its theory, Respondent cites the Horizontal Merger Guidelines. The Merger Guidelines recognize that "[a] merger is unlikely to generate substantial unilateral price increases if non-merging parties offer very close substitutes for the products offered by the merging firms. In some cases, non-merging firms may be able to reposition their products to offer close substitutes for the products offered by the merging firms." Merger Guidelines § 6.1. The Merger Guidelines further note that "[r]epositioning is evaluated much like entry, with consideration given to timeliness, likelihood, and sufficiency." Merger Guidelines § 6.1. Thus, Respondent must show that the purported repositioning will be timely, likely, and sufficient. Merger Guidelines § 9.

Applying the foregoing principles, Respondent's "repositioning" theory fails. Although the evidence discussed above shows that there is excess capacity and a declining supply of commercially insured patients in the Toledo area, Respondent's conclusion that the Joinder is, therefore, unlikely to lead to unilateral price increases is unpersuasive. In addition, the evidence regarding Mercy's [redacted] does not support a conclusion that Mercy's [redacted] (F. 747) is likely to replace the competition lost by the Joinder, or that any such replacement would be timely and sufficient.

b. Steering

"Steering" means providing incentives to patients or physicians to pursue health-care with specific providers. F. 682. "Hard" steering means providing financial incentives to a member to go to a particular provider. F. 682. "Soft" steering is providing information to members and physicians to try to change where care is provided. F. 682. Respondent contends that physicians, employers, and MCOs each have the ability to direct patients to less costly providers, and, thereby, constrain ProMedica from raising prices to anticompetitive levels. RRB at 56-59.

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i. Physician referrals

The evidence shows that most physicians have admitting privileges at multiple hospitals in Lucas County. F. 685. One of the reasons physicians obtain privileges at multiple hospitals is to be able to serve patients whose MCOs may not have certain hospitals in their networks. F. 686-687. Although having privileges at multiple hospitals allows a physician to direct a patient to an in-network hospital for treatment so that the patient may minimize out-of-pocket expenses, and physicians do attempt to accommodate a patient's insurance needs, physicians are not generally aware of, or sensitive to, the prices that hospitals charge for services. F. 684, 690-693, 697. Thus, the evidence does not support the conclusion that physicians can steer their patients to lower cost hospitals, and, thereby, help defeat attempted price increases by ProMedica.

c. *Employer programs*

The evidence shows that UTMC and Mercy, like many hospital employers, provide a higher level of health-care coverage for their employees who obtain services at their own hospitals. F. 722-723. This is similar to an employee discount in other types of industries. F. 721. The evidence also shows that the Lucas County government, a self-insured large employer, has a program through which it contributes a greater percentage to its employees' health-care costs if they choose to enroll with the preferred provider, Physicians Health Collaborative, instead of their two other options, Paramount or FrontPath. F. 728-731. These limited examples of employer steering are insufficient to support a conclusion that employer steering in Lucas County could constrain ProMedica from imposing anticompetitive price increases.

d. *MCO steering*

In-network steering occurs when MCOs charge different prices to members for accessing in-network hospitals, based on the price the MCO pays to the hospital for its members' inpatient care. F. 683. The evidence shows that MCOs are not likely to constrain anticompetitive price increases by ProMedica. First,

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MCOs perceive that patients prefer open access and dislike steering that uses financial incentives (*i.e.*, “hard” steering). F. 699. Thus, except for an ongoing 100 person pilot program by Aetna, discussed below, MCOs in Lucas County do not employ hard steering methods. F. 702-706, 715-717.

In January 2011, Aetna started a pilot hard-steering program for up to 100 Aetna employees in Toledo. In the pilot program, hospitals are “tiered” into low-cost (*i.e.*, lower rates) “first tier” hospitals, which provide a more financially-advantageous benefit for members, and high-cost (*i.e.*, higher rates) “second tier” hospitals, which require members to pay a higher copay. F. 708.

Aetna’s lower-cost hospital tier includes St. Luke’s, UTMC, Bay Park, St. Charles, and St. Anne. F. 709. There is insufficient data at this point for Aetna to conclude whether its steering program successfully steers members to lower-cost hospitals, although Aetna has received complaints about the program from members and hospitals. F. 710-713. In addition, while some MCOs use pricing transparency programs to steer patients to lower-cost providers, the evidence does not demonstrate that such transparency programs are effective. F. 701, 706-707.

Moreover, ProMedica has a policy of discouraging any strategies to steer patients away from ProMedica facilities through the use of financial incentives, and tries to get protections in its contracts preventing payors from using benefit differentials. F. 718. For example, ProMedica has anti-steering provisions in its contracts with [redacted] and [redacted] and also has negotiated a contract with [redacted] for St. Luke’s that includes an anti-steering provision. F. 719. ProMedica expressed its dislike of steering programs when it complained to Aetna that TTH and Flower were not in the preferred “tier one” in Aetna’s pilot program. F. 714.

For all the foregoing reasons, the evidence does not support the conclusion that MCOs are likely to make use of steering programs or that such programs would be effective to counter the impact of likely price increases by ProMedica. Respondent, therefore, has not demonstrated that market participants can constrain ProMedica from raising rates. Respondent’s defenses, that absent the Joinder, St. Luke’s competitive significance would

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decrease, and that the Joinder has resulted in, and will continue to yield, procompetitive benefits are addressed next.

E. Weakened Competitor Justification

Respondent argues that evaluating the likely competitive effects of the Joinder requires consideration of what St. Luke's competitive strength would be absent the Joinder. According to Respondent, the evidence shows that, absent the Joinder with ProMedica, St. Luke's competitive significance would diminish. RB at 90. Specifically, Respondent argues that St. Luke's concluded that it would have to cut services in order to stay independent; that key financial metrics, such as its operating margins, credit rating, and pension funding obligations, among others, show a financially weakened company; that St. Luke's poor financial condition hampered its ability to make the capital investments needed to compete effectively in the future; and that St. Luke's was poorly positioned to react to a changing health-care environment. RB 90-96.

Complaint Counsel responds that Respondent has failed to make the evidentiary showing required for a defense based on weakened financial condition. According to Complaint Counsel, the evidence shows that prior to the Joinder, St. Luke's was gaining market share; that due to a successful strategic plan instituted in 2008, St. Luke's profitability as of the date of the Joinder had improved significantly over 2009; that Respondent did not have significant pension obligations or debt; and that Respondent had sufficient cash reserves to make necessary capital investments, including those necessary for health-care reform requirements. CCB at 89-102. Complaint Counsel further argues that St. Luke's had other alternatives to the Joinder with ProMedica, such as merging with UTMC or Mercy, or staying independent for "years to come." CCB at 102-103.

1. Overview of applicable law

The Supreme Court has held that, in determining whether an acquisition is substantially likely to lessen competition, it is proper to consider the competitive weakness of the acquired company. *General Dynamics*, 415 U.S. at 503-04. As the

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Seventh Circuit explained in *United States v. International Harvester*, evaluating the weakness of the acquired company is an appropriate part of the competitive effects analysis because “only a further examination of the particular market - its structure, history and probable future - can provide the appropriate setting for judging the probable anticompetitive effect of the merger.” *Int’l Harvester*, 564 F.2d at 773- 74 (quoting *Brown Shoe*, 370 U.S. at 322 n.38).

While the precise standard for establishing a “weakened competitor” defense is unclear, it is a fact-specific inquiry. In *Evanston*, the Commission held that “[t]he precise standard for evaluating a weakened company justification [was] not material” because the facts in that case regarding the pre-merger financial condition of the acquired hospital, Highland Park, including its operating income and losses, and available cash and assets in relation to the hospital’s debt and anticipated capital expenditures evidence, did not substantiate Respondent’s contention that Highland Park’s pre-merger financial condition “prevented it from competing effectively,” but instead showed Highland Park’s financial condition to be “essentially sound.” *Evanston*, 2007 FTC LEXIS 210, at *218.

Despite the lack of a clear standard for establishing a financial weakness defense, it is clear that the defense is strongly disfavored. As the court stated in *Kaiser Aluminum*, “[f]inancial weakness, while perhaps relevant in some cases, is probably the weakest ground of all for justifying a merger” and “certainly cannot be the primary justification” for permitting one. 652 F.2d at 1339, 1341; *accord University Health*, 938 F.2d at 1221; *Arch Coal*, 329 F. Supp. 2d at 154; *Evanston*, 2007 FTC LEXIS 210 at *216. “Moreover, a weak company defense would extend the failing company doctrine, a defense which the Supreme Court in *General Dynamics* observed has strict limits.” *Kaiser Aluminum*, 652 F.2d at 1339; *accord FTC v. Warner Communs.*, 742 F.2d at 1164.

2. Summary of evidence and expert opinion

The evidence shows that St. Luke’s, and its parent, OhioCare, were consistently losing money on operations from at least 2007

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through the date of the Joinder. St. Luke's lost [redacted] million in 2007, [redacted] million in 2008, [redacted] million in 2009, and [redacted] million during the first eight months of 2010. F. 784-786. These losses reflected negative operating margins of [redacted] percent in 2007, [redacted] percent in 2008, [redacted] percent in 2009, and [redacted] percent in the first eight months of 2010. F. 786; *see also* F. 785. St. Luke's operating performance was significantly below that of other Ohio hospitals, which averaged operating margins of 4.0 percent in 2007, 1.5 percent in 2008, and 5 percent in 2009. F. 787. Thus, St. Luke's had negative operating margins in the years leading up to the Joinder, while other Ohio hospitals were profitable. *See* F. 786-787. St. Luke's operating performance was also significantly below similarly sized hospitals and hospitals with comparable bond ratings. F. 788-789.

"Operating cash flow" takes operating income and adds back interest, depreciation, and amortization, similar to the accounting calculation "EBITDA," (earnings before interest, depreciation, taxes and amortization) and provides another measure of profitability. F. 796. St. Luke's experienced positive EBITDA margins in 2007 and 2008; a negative margin of [redacted] in 2009, but that increased to positive [redacted] percent as of August 31, 2010. F. 794. These margins fell significantly below the average EBITDA margins of Moody's comparably rated hospitals, which were 9.6 percent in 2007, 7.7 percent in 2008, and 8.1 percent in 2009. F. 795. St. Luke's also had a relatively low debt load, with St. Luke's owing less than \$11 million in total bond debt as of August 31, 2010, of which [redacted] million was outstanding bond debt. F. 881, 916-918.

Based upon the EBITDA data set forth above, St. Luke's operating performance appears to have been improving as of the time of the Joinder. F. 794, 951. In addition, the data shows that St. Luke's losses had decreased and operating income improved as of the time of the Joinder. F. 952. St. Luke's operating cash flow margin from January 1, 2010 through August 31, 2010 was an improvement over St. Luke's operating cash flow margin for calendar year 2009. F. 953. As a result of achieving many of the "growth" goals targeted in St. Luke's Three-Year Plan, F. 920, net patient revenues also improved between 2009

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and the date of the Joinder. F. 924-927.

Based on the foregoing, it appears that St. Luke's financial performance, as of the date of the Joinder, was improved over its performance in 2008 and 2009. F. 949. However, the conclusion drawn by Complaint Counsel's expert witness, FTC accounting and financial analyst H. Gabriel Dagen, that at the time of the Joinder, St. Luke's was in the "midst of a successful financial turnaround," F. 968, exaggerates the state of St. Luke's finances prior to the Joinder. Mr. Dagen's opinion unduly focuses on the first eight months of 2010, in which St. Luke's experienced increased patient revenue and positive EBITDA, *e.g.*, F. 794, 926-927, 968, despite St. Luke's previous history of consistent operating losses and financial under-performance, *e.g.*, F. 786-789, 794-795. As Complaint Counsel's expert acknowledged, improving EBITDA does not necessarily indicate financial strength. F. 956. EBITDA does not consider capital expenditures, and may not always reflect pension expenses or investment gains or losses. F. 955.

It is important to consider capital expenditures as part of the measurement of a hospital's true cash flow, as hospitals are very capital intensive. F. 798. Hospitals must spend money on capital to maintain their equipment, to provide new systems, and to avoid decline. F. 798. In 2009, in order to conserve cash, St. Luke's began deferring capital expenditures, including routine and ongoing upgrades of facilities and replacement of equipment, such as the replacement of air handlers, regular hospital beds and birthing beds, surgical tables, a nurse call system, and a sleep lab system, which were estimated to cost a total of [redacted] million.

F. 805-806. St. Luke's also needed significant additional capital investments, including conversion to "meaningful use" of electronic medical records ("EMR"), at a total cost of [redacted] million depending on the availability of federal subsidies (F. 831-832) and not including various operational expenses associated with implementing and maintaining that system (F. 835), and conversion from semi-private to private rooms in the approximate amount of \$1.8 million. F. 819. In the fall of 2010, St. Luke's departments identified [redacted] million of necessary capital projects for budgeting purposes, with [redacted] million for critical projects for 2011 alone. F. 809. St. Luke's desire to

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get access to capital was a recurring factor in St. Luke's evaluation of whether or not to affiliate, and with which one of its potential partners. F. 396-397, 400, 402. As part of the Joinder, ProMedica agreed to provide \$30 million in capital contribution, for, among other things, converting semi-private rooms to private rooms, and updating St. Luke's information technology ("IT") systems. F. 429-430, 980.

St. Luke's is required to make cash contributions to its defined benefit pension plan. F. 841-842. Under the Employee Retirement Income Security Act ("ERISA"), as modified by the federal Pension Protection Act ("PPA"), if St. Luke's defined benefit pension plan is less than 100 percent funded, it is required to make payments, based on a formula, to bring the plan to 100 percent funding. F. 848. The state of St. Luke's defined benefit funding was one of the "pressing concerns" identified in the December 2009 Affiliation Update to St. Luke's Board. F. 846. In order to be certified as 80 percent funded as of January 1, 2010, St. Luke's had to accelerate contributions, and forfeit a credit balance, in the combined total of [redacted] million. F. 853-854.

In order to reach the 80 percent funded level as of January 1, 2011, St. Luke's was required to make an accelerated contribution to its defined benefit pension plan of [redacted] million. F. 855. At the time of the Joinder, St. Luke's defined benefit pension plan was under-funded from both an accounting and funding perspective. F. 856. Depending on such variables as employee retirements and the performance of the market, St. Luke's may need to make annual contributions of at least [redacted] million until 2016 to meet minimum funding requirements. F. 857.

St. Luke's unrestricted cash reserves are available for capital expenditures, strategic capital expenditures, or for unforeseen events that may arise outside of normal operations. F. 867. St. Luke's unrestricted cash reserves declined by half from 2007 to the date of the Joinder, [redacted] million in 2007 to [redacted] million as of August 31, 2010. F. 864. Including the value of investments, as of August 31, 2010, St. Luke's had approximately \$65 million in cash and investment balances. F. 866. St. Luke's available cash reserves declined from 2007 through 2010, as St. Luke's drew down its cash reserves to cover operational losses, as well as to make necessary capital expenditures. F. 864-865. It

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is undisputed, however, that as of August 31, 2010, St. Luke's had enough cash and investments on its financial statement to pay off all of its outstanding debt. F. 919.

"Days cash on hand" is another measure of liquidity and stability. F. 868. As of the date of the Joinder, St. Luke's cash position translated into only 104 days cash on hand, *i.e.*, the number of days St. Luke's could last without additional revenue. F. 868-870. St. Luke's days cash on hand, as of the date of the Joinder, was about half the amount of days cash on hand held by hospitals of similar size to St. Luke's. F. 871. St. Luke's days cash on hand also had declined steadily from 2007 to the date of the Joinder. F. 870. To cut expenses, St. Luke's had imposed restrictions with respect to hiring and had frozen pay and pension benefits. F. 800-803.

Independent entities evaluated St. Luke's financial condition negatively prior to the Joinder. In February 2010, Moody's Investors Service, Inc. ("Moody's") downgraded St. Luke's bond rating from Baa1, to Baa2 (close to "junk bond" status), with a negative outlook, pointing to three consecutive years of large operating losses and an operating cash flow deficit, at a margin -2.0%; unfavorable commercial contracts and ongoing challenges with negotiating higher commercial reimbursements; an unsuitably aggressive investment allocation; a "very competitive market" with the larger systems of ProMedica and Mercy; and weak demographics in the primary service area, characterized by declining volume trends, high unemployment levels, and low median income levels. F. 875-884. St. Luke's bond insurer, Ambac Assurance Corp. ("AMBAC"), also downgraded St. Luke's credit rating, from an A- to a BBB+ rating, after completing a credit analysis of St. Luke's bonds in late 2008 and 2009, and viewed St. Luke's as having a "downward trend." F. 896-899. St. Luke's debt coverage ratio of approximately [redacted] for 2009, a decrease from [redacted] in 2008, resulted in St. Luke's being in material technical default of its bond covenants. F. 905-907. AMBAC found, based on its review of St. Luke's financial statements, that St. Luke's financial trends were negative and its performance was deteriorating. F. 910. Based upon a credit review of pre-2010 financial data, on April 27, 2010, AMBAC downgraded St. Luke's internal rating from

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BBB+ to BBB and gave St. Luke's a "negative outlook." F. 914.

The totality of the evidence supports the conclusions, as stated by Respondent's health-care financial expert witness, Mr. Bruce Den Uyl, that St. Luke's was struggling financially as a stand-alone entity during the years leading up to the Joinder and faced significant financial obstacles to going forward as an independent hospital, including, among other challenges over the next few years, as much as [redacted] million in accelerated pension payments (F. 857), approximately [redacted] million in capital expenditures (F. 806, 819, 831-832), an aging plant requiring future outlays (F. 811-814), declining cash reserves (F. 864-865), and perhaps most critical, below-cost reimbursement rates contributing to operating losses (F. 372-377). To be sure, continuing losses, depleting cash reserves, deferring capital expenditures, and employee cost cutting measures are not a sustainable path for a hospital. F. 812, 977-979.

However, notwithstanding the Moody's downgrade and negative outlook, it would have been possible for St. Luke's to borrow money to address its financial challenges, and, thereby, stay competitive in the future, although such borrowing may have proved to be difficult and would not necessarily be on the most favorable terms. F. 888-890, 892. A Moody's survey indicates that in 2009, approximately 100 out of 411, or 28%, not-for-profit freestanding hospitals and single-state health-care systems had a bond rating between Baa1 and Baa3. F. 878. Data collected by Complaint Counsel's bond-rating expert, Errol Brick, shows that "Baa" rated hospitals and health-care systems issued \$2.6 billion in debt from January 2010 through January 2011 (ranging from \$25 million to \$527 million per hospital). F. 887. In addition, data collected by Mr. Brick pertaining to ten bond issues by Baa rated hospitals since August 31, 2010 shows the actual interest rates paid by these hospitals. F. 887. The data supports Mr. Brick's conclusion that, in August 2010, St. Luke's would have been able to access the tax-exempt capital markets for up to \$75 million in debt for a reasonable interest rate of no more than 7 percent. F. 888.

Although St. Luke's was struggling and facing significant challenges, St. Luke's cash reserves of up to \$65 million as of

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August 31, 2010 could be sufficient to pay off all of St. Luke's obligations, including debt and pension obligations, and meet its capital investment needs, even without additional borrowing, as concluded by Complaint Counsel's expert, F. 806-807, 819, 838-839, 857, 919, 966-967, 993, particularly if St. Luke's operating cash flow and decreased losses continued to improve and, thereby, slow the previous rate of cash depletion. F. 377-379, 952-953. The evidence does not, however, clearly answer the question of whether or not, given the totality of St. Luke's financial circumstances, it would be appropriate for St. Luke's to spend down its cash reserves in this manner. *See, e.g.*, F. 862-863 (trustee-restricted funds are dedicated to bond and insurance payments), F. 870 (St. Luke's days cash on hand as of August 31, 2010 was 104 days).

Moreover, the evidence demonstrates that St. Luke's experienced increased patient volume. F. 924-927. Although St. Luke's overall payor ratio was insufficient to cover its total costs, F. 371-377, 413, increased patient volume appears to have played a role in St. Luke's decreasing losses and improved operating cash flow in 2010 and, thus, as concluded by Mr. Dagen, such increased volume can drive St. Luke's to profitability in the future. F. 962-965. Mr. Dagen's opinion that patient volume can drive profitability appears consistent with Mr. Wakeman's statements to the St. Luke's Board in September 2010 that St. Luke's "high activity" produced a positive operating margin in August 2010, thereby confirming that "we can run in the black if activity stays high. After much work, we have built our volume up to a point where we can produce an operating margin and keep our variable expenses under control." F. 948.

Based on St. Luke's improving cash flow and cash reserves, Mr. Dagen concluded that "absent the joinder, St. Luke's would have remained financially viable into the foreseeable future." F. 967. This open-ended prediction of the "foreseeable future" is vague and overreaches, looking at the evidentiary record as a whole. In comparison, Mr. Wakeman estimated that, under the conditions current in December 2009, St. Luke's would be able to survive between three and five years, and that if St. Luke's was able to get rate increases under contracts with two of St. Luke's largest commercial payers, St. Luke's could survive four to seven

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years. F. 959. Mr. Den Uyl was not asked to, and did not, analyze or provide an expert opinion on how long St. Luke's could have survived as a stand-alone hospital had it not been acquired by ProMedica. F. 972.

In summary, the evidence demonstrates that St. Luke's had been struggling financially prior to the Joinder and faced significant financial challenges going forward. The evidence further shows that St. Luke's losses had declined and operating cash flow had improved by the time of the Joinder and that St. Luke's cash reserves, along with potential future borrowing, would be available to meet St. Luke's challenges going forward. However, the evidence does not support a conclusion that, absent the Joinder, St. Luke's would be a viable hospital for the foreseeable future; rather, the evidence demonstrates that, while St. Luke's was not in imminent danger of failure, absent the Joinder, St. Luke's future viability beyond the next several years is uncertain.²⁴

3. Analysis

In support of its weakened competitor defense, Respondent relies chiefly upon *FTC v. Arch Coal, Inc.*, 329 F. Supp. 2d 109 (D.D.C. 2004). In *Arch Coal*, the court refused to enjoin the acquisition by Arch Coal of Triton, both mine owners and operators. Among other reasons, the court held that Triton was a "relatively weak competitor" in the relevant market "with no convincing prospects for improvement." 329 F. Supp. 2d at 157. The court relied on the facts that Triton "has high costs, has low [coal] reserves, has at best uncertain prospects for loans or new [coal] reserves, is in a weakened financial condition, and has no realistic prospects for other buyers." *Id.* Based on the foregoing, the court concluded that the FTC's "claims of Triton's past and future competitive significance in the [relevant] market [have] been far overstated." *Id.*

²⁴ While in August 2009, St. Luke's considered service cuts in lieu of pursuing affiliation with other hospitals, *see* F. 393, the evidence does not warrant the conclusion that St. Luke's was likely to undertake service cuts absent the Joinder. Potential service cuts were not considered a serious option for an independent St. Luke's, and the idea was rejected by the Board. F. 401.

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Unlike *Arch Coal*, the evidence in this case shows that prior to the Joinder, St. Luke's succeeded in significantly raising its patient volume and market share, F. 924-932, and by these measures was a strong competitor. Also in contrast to the facts in *Arch Coal*, St. Luke's has prospects for improvement, based upon 2010 positive EBITDA and decreased losses, strong volume, cash reserves, and the potential for new borrowing, as discussed above.

In addition, unlike *Arch Coal*, the evidence in this case shows that St. Luke's had merger options other than ProMedica. F. 395-399, 405, 418-420. In this regard, it should be noted, however, that if St. Luke's were to have merged with Mercy, as Complaint Counsel suggests was an option, such a merger would also likely have been subject to antitrust scrutiny. According to Respondent's calculations, using Complaint Counsel's market shares for GAC inpatient services, a Mercy-St. Luke's merger would result in a post-merger HHI of 3975 and a UTMC-St. Luke's merger would result in a post-merger HHI of 3614. Both alternative mergers would result in highly concentrated markets as measured by HHI. RRB at 17 n.10 (citing Merger Guidelines, § 5.3 (HHI above 2500 considered highly concentrated)).

Respondent correctly notes that, as in *Arch Coal*, St. Luke's "consistently lost money," and that a "company with a positive EBITDA but a negative net income is not sustainable for the long term." 327 F. Supp. 2d at 155. However, unlike the transaction in *Arch Coal*, where the acquired company was at risk of exiting the market, St. Luke's was still competing in the market and, thus, the Joinder reduced the number of competitors. Moreover, unlike *Arch Coal*, St. Luke's competitive viability is not dependent on a finite, and depleted, natural resource such as coal reserves. In addition, the statistical and HHI evidence in this case is much stronger than that in *Arch Coal*, where the transaction "just barely" raised competitive concerns. 329 F. Supp. 2d at 128-30, 155-56.

On balance, therefore, *Arch Coal* is insufficiently analogous to provide precedent to allow the Joinder in this case on the basis of St. Luke's being a "weakened competitor." Accordingly, Respondent's weakened competitor justification is rejected.

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4. Conclusion

St. Luke's clearly was struggling financially prior to the Joinder and faced significant financial challenges to remaining independent in the future. There were signs of some improvement in operating performance by the time of the Joinder, as well as relatively low debt, cash reserves, and potential borrowing to help St. Luke's move forward; however, absent significant and sustained improvements in St. Luke's financial condition, its viability as an independent hospital, beyond the next few years, is by no means clear. Nevertheless, current case law, applied to the facts of this case, does not provide support for allowing the Joinder to proceed on the basis of St. Luke's weakened financial condition. This conclusion is especially mindful of the admonition from the courts that financial weakness "cannot be the primary justification" for permitting a merger. *Kaiser*, 652 F.2d at 1339, 1341; *University Health*, 938 F.2d at 1221.²⁵

F. Asserted Procompetitive Benefits and Efficiencies

The procompetitive benefits and efficiencies asserted by

²⁵ It should be noted that St. Luke's financial condition prior to the Joinder was considerably weaker than the hospital that the Commission deemed "essentially sound" in *Evanston*, 2007 FTC LEXIS 210, at *218. Highland Park had "historically achieved strong financial results compared to the median of not-for-profit hospitals," *id.* at *218-19, while, as discussed above, St. Luke's was consistently losing money and its financial results were below other hospitals. Highland Park's cash and unrestricted investments totaled approximately \$218 million, while St. Luke's were only \$65 million. F. 866. Highland Park had 444 days cash on hand, which was 2.4 times the national average for "A" rated hospitals, while St. Luke's had 104 days cash on hand as of the date of the Joinder, which constituted half the amount held by Moody's Aa-rated hospitals, and half the amount held by hospitals of comparable size to St. Luke's. F. 870-871. In addition, Highland Park's management believed that Highland Park would "remain financially strong over the foreseeable future," *id.* at *219-20, while St. Luke's management believed that St. Luke's had only two options – raise reimbursement rates or affiliate with a hospital system. F. 389. Highland Park had a long-range capital budget that included over \$100 million for various strategic initiatives and capital investments, *id.* at *220, while St. Luke's was deferring capital projects. F. 805, 807. The evidence in *Evanston* also showed, unlike the instant case, that Highland Park had wealthy benefactors to help fund its capital projects. *Id.* at *220.

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Respondent fail to outweigh the likely anticompetitive effects of the Joinder. Respondent urges that, as a result of the Joinder, St. Luke's is a stronger competitor than it would have been without the Joinder. RB at 98. Respondent, thus, asserts that the Joinder has resulted in procompetitive benefits because it has improved St. Luke's financial condition and will continue to do so. RB at 98-101. In addition, Respondent asserts that the Joinder results in other benefits and efficiencies. RB at 101-106.

“[E]vidence that a proposed acquisition would create significant efficiencies benefiting consumers is useful in evaluating the ultimate issue -- the acquisition's overall effect on competition.” *University Health*, 938 F.2d at 1222. Courts and the Commission in merger cases typically “consider efficiencies, including quality improvements, after the government has shown that the transaction is likely to reduce competition.” *Evanston*, 2007 FTC LEXIS 210, at *191 (citing *Heinz*, 246 F.3d at 715, 720). “A defendant who seeks to overcome a presumption that a proposed acquisition would substantially lessen competition must demonstrate that the intended acquisition would result in significant economies and that these economies ultimately would benefit competition and, hence, consumers.” *University Health*, 938 F.2d at 1223. Respondent “has the burden of production to show that efficiencies offset any likely anticompetitive effects of the increase in market power produced by the merger.” *Evanston*, 2007 FTC LEXIS 210, at *191 (citing *Heinz*, 246 F.3d at 715, 720; *Staples, Inc.*, 970 F. Supp. at 1088-89).

“Efficiencies are cost savings generated by the increased economies of scale which result from mergers.” *FTC v. Cardinal Health, Inc.*, 12 F. Supp. 2d 34, 61 (D.D.C. 1998). As stated in the Merger Guidelines, “[c]ognizable efficiencies are merger-specific efficiencies that have been verified and do not arise from anticompetitive reductions in output or service. Cognizable efficiencies are assessed net of costs produced by the merger or incurred in achieving those efficiencies.” Merger Guidelines § 10. As the Commission explained in *Evanston*, the claimed efficiencies must be:

- (1) verifiable; (2) merger-specific, *i.e.*, ones that could not practicably be achieved without the proposed merger; and

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(3) greater than the transaction's substantial anticompetitive effects. *See Merger Guidelines* § 4; *see also Heinz*, 246 F.3d at 721-22 (finding that, among other things, asserted efficiencies must be “merger-specific”).

Evanston, 2007 FTC LEXIS 210, at *226-27.

Furthermore, “‘a rigorous analysis’ is required to ensure that [Respondent’s] claims of offsetting procompetitive benefits ‘represent more than mere speculation.’” *Evanston*, 2007 FTC LEXIS 210, at *234 (citing *Heinz*, 246 F.3d at 721). “[S]peculative, self-serving assertions” will not suffice. *University Health*, 938 F.2d at 1223; *Staples*, 970 F. Supp. at 1089-90 (rejecting claimed efficiencies that were “unverified” and not supported by “credible evidence”).

Cases with high market concentration levels “require, in rebuttal, proof of extraordinary efficiencies.” *Heinz*, 246 F.3d at 720 (citing *University Health*, 938 F.2d at 1223; *Merger Guidelines* § 4 (stating that “efficiencies almost never justify a merger to monopoly or near-monopoly”). In the instant case, Respondent’s expert concedes that the pre-HHI meets the *Merger Guidelines*’ presumption of a highly concentrated market and that the post-HHI would be around 4000. F. 369. With these high concentration levels, Respondent must show “extraordinary” efficiencies. *See Heinz*, 246 F.3d at 720.

As analyzed below, the evidence shows that as a result of the Joinder, St. Luke’s is a stronger hospital. A St. Luke’s that is financially well-off is more beneficial to the community than a hospital that is struggling financially. However, based upon applicable legal principles, it cannot be concluded that the benefits and efficiencies generated from the Joinder represent “significant economies” that ultimately would benefit competition and, hence, consumers, or that the benefits and efficiencies asserted are greater than the likely anticompetitive effects of the increase in market power produced by the Joinder, where St. Luke’s is no longer a competitor to ProMedica.

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1. Benefits to St. Luke's

Respondent asserts that the Joinder has improved St. Luke's competitive position, stabilized St. Luke's finances, and enhanced St. Luke's ability to compete in Lucas County. RB at 98-99. This argument, and the evidence offered in support thereof, is addressed below.

a. Capital contribution to St. Luke's

The Joinder Agreement obligates ProMedica to contribute \$10 million in each of the years 2011 through 2013 to fund capital projects at St. Luke's. F. 980-982. The capital commitment from ProMedica is to be used for capital projects at St. Luke's including private room expansion, facility upgrades, and IT upgrades relating to St. Luke's "meaningful use" compliance.²⁶ F. 989, 994. With respect to private rooms, St. Luke's has budgeted \$3 million of the capital it received from ProMedica to create 17 new private rooms. F. 990-991. Prior to the Joinder, St. Luke's projected the cost of its private room conversions to be \$1.8 million. F. 992. With respect to IT upgrades, ProMedica believes that St. Luke's has allocated a portion of its initial \$10 million investment from ProMedica to implement a new EMR system and meet "meaningful use" requirements. F. 994. However, it is not clear that St. Luke's could not have implemented these measures but for the Joinder. St. Luke's had \$65 million in cash and investments as of August 31, 2010, while its estimate for the cost of a private room conversion project was \$1.8 million and for EMR implementation was \$14 million. F. 992-993. Prior to the Joinder, St. Luke's had intended to begin implementing EMR in 2010 and had budgeted [redacted] million for it in 2010, but stopped the process because of the Joinder. F. 838-840, 997. Further, St. Luke's Computer Information Systems Director, was "[u]nsure" whether ProMedica could implement EMR at St. Luke's in time to take advantage of all financial incentives under the federal American Recovery and Reinvestment Act of 2009 ("ARRA"). F. 995. Thus,

²⁶ The HITECH Act, passed in 2009, provides hospitals with increased Medicare reimbursement rates if they implement and upgrade their emergency medical records ("EMR") systems and achieve statutory "meaningful use" requirements by certain deadlines. F. 822.

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Respondent has not demonstrated that the capital contribution to St. Luke's allows St. Luke's to make improvements that St. Luke's could not have made but for the Joinder.

b. Access to Paramount

As part of the Joinder Agreement, St. Luke's became an in-network provider with Paramount. F. 1021. This has led to greater patient volume and has increased St. Luke's revenues. Paramount patients have a positive effect on St. Luke's bottom line because [redacted]. F. 1021-1022. Thus, Respondent argues, the additional Paramount revenues will help St. Luke's remain viable and improve St. Luke's services and facilities. RB at 100.

Prior to the Joinder, St. Luke's, and Mr. Wakeman personally, made serious attempts to have St. Luke's rejoin Paramount's network, but those attempts were unsuccessful. F. 1018. Paramount, as it stated to UTMC, would not add St. Luke's to its provider network because "[t]here is no benefit to ProMedica for inclusion of an additional hospital in all of Paramount's product lines." F. 1019. Indeed, ProMedica believed that St. Luke's admission into Paramount would have hurt patient volume at ProMedica's Lucas County hospitals. F. 1020. This claimed efficiency could have been accomplished without the Joinder if Paramount, which is owned by Respondent, had chosen to contract with St. Luke's. (Dagen, Tr. 3289-3290, *in camera*; PX02147 at 080-081 (¶ 158) (Dagen Expert Report)). As a result, any financial benefits that St. Luke's enjoyed from being permitted to join the Paramount provider network are not merger-specific. (See Dagen, Tr. 3289-3290, *in camera*; PX02147 at 080-081 (¶ 158) (Dagen Expert Report)).

c. Access to ProMedica's Obligated Group

The evidence shows that as a result of the Joinder, St. Luke's became part of ProMedica's Obligated Group, which is the group that guarantees ProMedica's public debt. F. 1000, 1007. As a result, Moody's increased its rating of St. Luke's outstanding bonds. F. 1009. The Joinder also resulted in curing St. Luke's bond default with AMBAC, because of the greater the credit

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security provided by ProMedica. F. 1004-1006. Accordingly, the Joinder was beneficial to St. Luke's credit rating, thereby improving its ability to access capital through borrowing.

d. Responsibility for underfunded defined benefit pension plan

At the close of the Joinder, St. Luke's defined benefit pension plan was under-funded from both an accounting and funding perspective. F. 856. Respondent notes that "ProMedica plans to allocate capital to St. Luke's pension plan to keep it [redacted]." RB at 100; *see* F. 1011. Notably, ProMedica did not keep its own pension plan 100% funded during the economic downturn – it was underfunded in 2008 by [redacted] million and in 2009 by [redacted] million, compared to underfunding at St. Luke's of [redacted] million and [redacted] million in the same years. F. 1012-1013. Respondent's claimed "plans" to fund St. Luke's pension plan, even if implemented, do not outweigh the Joinder's likely substantial anticompetitive effects.

e. Lowering of expenses

Respondent asserts that the Joinder has already allowed St. Luke's to reduce St. Luke's expenses and that ProMedica and St. Luke's expect the Joinder to generate significant additional future savings and efficiencies. RB at 101. Respondent notes that following the Joinder, St. Luke's saved about a half million dollars in professional liability insurance by becoming part of ProMedica's captive insurance company. F. 1015. In addition to reduced insurance premiums, joining ProMedica's captive insurance plan and spreading risk has had the effect of freeing up \$8 million on St. Luke's balance sheet. F. 1016. These claimed savings are similar to those rejected in *Arch Coal* and are similarly rejected here because the majority of these savings are not merger-specific. *Arch Coal*, 329 F. Supp. 2d at 152.²⁷

²⁷ In *Arch Coal*, Arch claimed that it received quotes for insurance to cover Triton's property, including the risk of business interruption, at no additional cost to it, and, thus, that savings would be achieved. *Arch Coal*, 329 F. Supp. 2d at 152. The court found that only a fraction of those savings were merger-specific because Triton could have been able to realize over 80% of those savings on its own and another potential purchaser of Triton might

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Respondent asserts, in addition, that St. Luke's has been able to reduce expenses through the consolidation of non-clinical backroom services such as billing services, legal services, physician practice management, and IT support. RB at 101. However, Respondent does not identify by how much St. Luke's has been able to reduce expenses, nor does Respondent identify whether any costs were required to achieve the consolidation, and, thus, whether there are any net savings to St. Luke's. In addition, Respondent identifies no evidence that any such costs savings could be achieved only by St. Luke's joining ProMedica. In fact, Respondent admitted that "*any* St. Luke's affiliation with *any* potential partner, including UTMC, may have led to certain efficiencies[.]" (Response to RFA at ¶ 12 (emphasis added)). Thus, these savings are not merger-specific and Respondent has not met its burden on these claims.

2. Costs and quality

Respondent asserts that the addition of St. Luke's will allow ProMedica to consolidate clinical services to optimize ProMedica's and St. Luke's services and facilities to best meet community needs, as well as produce other efficiencies, and that the Joinder will provide other benefits. RB at 101-106. These arguments, and the evidence offered in support thereof, are addressed below.

a. Consolidation of clinical services

Respondent asserts that the Joinder gives ProMedica the opportunity to assess community needs and optimize the delivery of care based on its network of hospitals and facilities located across the Toledo area. Respondent states that, to aid in its integration efforts, ProMedica retained Navigant Consulting ("Navigant") in mid-2010 to conduct a clinical integration study and recommend how best to distribute services across the ProMedica system following the Joinder with St. Luke's. F. 1026-1027. Most of Respondent's claims that the Joinder

have been able to achieve those same savings. *Id.*

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enables it to optimize the delivery of care are based on the recommendations of Navigant. At the outset, it should be noted that ProMedica has been prohibited by the Hold Separate Agreement from consolidating services provided at St. Luke's, with one exception relating to inpatient rehabilitation, discussed below. F. 12-13, 1058. Thus, Navigant's "recommendations," (Part II.O.6.) are only recommendations and ProMedica is under no obligation to follow them.

Moreover, while the Navigant study reported that officials from St. Luke's and ProMedica estimated that the clinical integration strategy would result in operational efficiencies that would total [redacted] million annually, this amount of savings is for the entire clinical integration. F. 1074. Many of the clinical integration projects and recommendations do not involve St. Luke's. F. 1075. Navigant did no independent analysis to determine the reasonableness of the estimated efficiencies of [redacted] million annually, but instead "had some discussions with [ProMedica] in terms of what some of their assumptions were." F. 1076. Additionally, the cost of the clinical integration, over three years, is estimated to be [redacted] million. F. 1076.

In support of its position that the Joinder allows ProMedica to optimize its services and facilities, Respondent points to the following examples: (1) shift of inpatient rehabilitation services from St. Luke's to Flower; (2) clinical integration of [redacted]; (3) expansion and improvement of OB services; (4) potential to reconfigure services at ProMedica; (5) access for St. Luke's to ProMedica's quality program aimed at increasing patient safety; and (6) access for St. Luke's to ProMedica's quality-related technologies. RB at 101-104. These examples are discussed below.

(i) Shift of inpatient rehabilitation services

On October 15, 2010, the FTC granted ProMedica's request for a modification to the Hold Separate Agreement to allow ProMedica to move inpatient rehabilitation beds from St. Luke's to Flower Hospital to create additional medical/surgical rooms at St. Luke's. F. 1058. ProMedica's shift of inpatient rehabilitation services from St. Luke's to Flower increases

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utilization of Flower's existing inpatient rehabilitation services capacity. F. 1060. This move increased St. Luke's capacity and virtually eliminated the need to temporarily close St. Luke's emergency room to new patients. F. 1061. In addition, it allowed St. Luke's to convert its former inpatient rehabilitation spaces into private rooms. F. 1062. However, as a result of this consolidation, patients who previously chose to go to St. Luke's inpatient rehabilitation center no longer have that option and, instead, must now go to the more expensive Flower Hospital. F. 1063, 1065. ProMedica's claimed savings from the inpatient rehabilitation consolidation, while originally claimed to be [redacted] million, is now estimated to be only [redacted]. F. 1066-1067. Thus, the evidence does not demonstrate that the elimination of services at one hospital, and the transfer of those services to another hospital results in "significant economies" (*University Health*, 938 F.2d at 1223) that benefit consumers.

(ii) Clinical integration of [redacted]

Respondent points to [redacted] as an example of beneficial clinical integration. RB at 102. Prior to the Joinder, St. Luke's did not have a sufficient number of [redacted] to maintain quality thresholds or break even, financially. F. 1044-1045. Respondent states that it [redacted]. RB at 102-103. If St. Luke's [redacted]. F. 1045-1046. Given that ProMedica's reimbursement for services is on average higher than St. Luke's, a price increase resulting from this consolidation may exceed any actual cost savings generated by it. F. 1047-1048. And, as with the shift of rehabilitation services, the evidence does not support the conclusion that the elimination of services from one hospital to transfer them to another hospital results in "significant economies" (*University Health*, 938 F.2d at 1223) that benefit consumers.

(iii) Expansion and improvement of [redacted] at St. Luke's

Another example of beneficial clinical integration that the Joinder may facilitate, according to Respondent, relates to [redacted]. RB at 103. Navigant recommended that ProMedica

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[redacted]. F. 1053-1054. If implemented, this would benefit the [redacted]. Accordingly, it is an efficiency that would be generated from the Joinder.

(iv) Potential to reconfigure services at ProMedica

Respondent states that ProMedica could not achieve the integration benefits outlined in Navigant's plan without the Joinder because it needs St. Luke's to achieve a critical mass of patients in some service lines, and it needs St. Luke's facility as a location at which it can reposition services to achieve an optimal distribution of services across the market. RB at 103. Complaint Counsel counters, "[p]ut differently, rather than compete with St. Luke's for additional patients – by improving quality and service and lowering prices – ProMedica prefers to enhance its market share and dominant position through the Acquisition and then transfer services around its system to achieve some nebulous 'optimal distribution.'" CCRB at 47. Citing as support only to its own response to a Civil Investigative Demand, Respondent asserts that "St. Luke's could not have achieved integration benefits without the joinder because it would not have had another entity with which to integrate or transfer underutilized services." RB at 103. Complaint Counsel argues that an affiliation with UTMC or Mercy could have brought similar results. CCRB at 48. Regardless of whether ProMedica could have achieved the integration benefits without St. Luke's or whether St. Luke's could have obtained the benefits by affiliating with UTMC or Mercy, the claimed efficiencies are not greater than the transaction's substantial likely anticompetitive effects.

(v) Access for St. Luke's to ProMedica's quality program

Respondent also asserts that the Joinder gives St. Luke's access to ProMedica's comprehensive quality program and technologies aimed at increasing patient safety. RB at 104. ProMedica has quality councils for each of its hospitals, for Paramount Health Care, and for ProMedica Physician Group, as well as four service line quality councils for cancer, orthopedics, heart and vascular, and critical care. F. 1077-1078. ProMedica's corporate quality department provides report cards

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based on valid quality metrics to each hospital, enabling ProMedica to monitor and track the quality performance of each of its hospitals. F. 1079. Following the Joinder, ProMedica began the process of bringing St. Luke's into its system-wide quality programs. F. 1081.

The evidence indicates, however, that, based on some measurements, St. Luke's quality was superior to ProMedica's. Some of ProMedica's best practices are outdated and not on-par with the practices at St. Luke's. F. 1083. By some measurements, St. Luke's achievements in clinical quality exceed those of TTH and Flower. F. 767. ProMedica's own executives remarked that ProMedica has not kept pace and needed to catch up; and ProMedica's Chief Medical Officer noted that "very few people . . . can fully explain the [ProMedica Health System] approach to quality much less feel compelled to follow it." F. 770-771.

Moreover, there are varying degrees of reliability for quality metrics; quality measures can be too "nebulous" to be meaningful. F. 777-778; *see also Evanston*, 2007 FTC LEXIS 210, at *134 ("quality of medical care is not easily defined or measured"). Although the Joinder gives St. Luke's access to ProMedica's quality program, this does not constitute verifiable evidence that any improvement from such program is of sufficient magnitude to offset the competitive harm that is likely to result from the Joinder.

(vi) Access for St. Luke's to ProMedica's quality-related technologies

Respondent claims, in addition, that the Joinder gives St. Luke's access to ProMedica's quality-related technologies, such as electronic Intensive Care Units ("eICU") and smart pumps. RB at 104. Respondent asserts that "St. Luke's has access to those technologies only because of the joinder." RB at 104.

The eICU is a computerized telemonitoring system that allows hospitals to monitor its ICU beds across the system from a central control tower. F. 1086. Smart pumps are computerized infusion pumps that allow hospital staff to set safe limits for drug doses

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and alert the staff if the dosing exceeds those limits. F. 1092. St. Luke's did not have the eICU or smart pumps before the Joinder. F. 1089, 1095. However, St. Luke's had been planning to acquire smart pumps before the Joinder, had already obtained quoted prices, and was determining how to integrate the smart pumps into their electronic medical records system. F. 1096. And, while as a result of the Joinder St. Luke's was able to join with other ProMedica system hospitals to lease infusion pumps at a favorable lease rate, St. Luke's may have been able to obtain discounts by purchasing smart pumps through a purchasing organization like Voluntary Hospitals of America. F. 1097-1098. Furthermore, after the Joinder, St. Luke's is still required to pay for all of the equipment and system upgrades, such as eICU, itself. F. 1091. Thus, the evidence does not demonstrate that St. Luke's has access to those technologies only because of the Joinder.

b. Additional claimed efficiencies

Respondent asserts that ProMedica and St. Luke's began exploring efficiency opportunities in early 2010 in order to develop ideas and quantify possibilities. RB at 105. In this regard, ProMedica created teams of individuals from ProMedica and St. Luke's to identify potential efficiencies opportunities and hired Compass Lexecon to identify efficiencies from cost savings, backroom functions, and combining separate programs. F. 1099-1100, 1106-1107. Compass Lexecon issued a report on May 6, 2010, titled "Efficiencies Analysis of the Proposed Joinder of ProMedica Health System and OhioCare Health System." (Compass Lexecon Report). F. 1101. However, some of Respondent's key personnel had little or no involvement in developing many of the claimed efficiencies, and, in some instances, St. Luke's executives actually disputed claimed efficiencies. F. 1113-1116. One document indicates that the size of the purported efficiencies and time period in which to achieve them was deliberately revised to meet the FTC's anticipated reaction to the Joinder. F. 1117.

Based on the Compass Lexecon Report, in the spring of 2010, ProMedica estimated that the Joinder could achieve approximately [redacted] in annual savings, approximately

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[redacted] in capital avoidance savings, and related operating cost savings of [redacted]. F. 1109. Following the Joinder, ProMedica and St. Luke's established a steering committee to oversee approximately 20 integration teams to further develop the efficiencies opportunities that Compass Lexecon identified, and to identify new opportunities. F. 1106. Since first estimating efficiencies in the spring of 2010, ProMedica's projected efficiencies from the Joinder have [redacted] the original annual projection of [redacted]. F. 1112.

While Respondent claims [redacted] in capital avoidance savings and related operating-cost savings of [redacted], as stated in the Compass Lexecon Report, these claimed efficiencies result "primarily from the avoidance of capital and operating costs associated with the construction and operation of a hospital at Arrowhead and a new bed tower [to increase capacity] at Flower Hospital." F. 1109. The evidence in the record fails to show, however, that ProMedica actually intended to build the Arrowhead hospital absent the Joinder. F. 1122, 1124. *See also* Dagen, Tr. 3279-3280, *in camera* (no strategic plans, capital budgeting documents, or permits for constructing a hospital at Arrowhead); PX02147 at 046-049 (¶¶ 85-89) (Dagen Expert Report); PX02148 at 094-095 (¶¶ 172-173) (Town Expert Report), *in camera*). In addition, ProMedica's most recent pre-Joinder Strategic Plans did not evince an intention to construct a second bed tower at Flower Hospital. F. 1126-1127. At no time in the two to three year period leading up to the Joinder did ProMedica generate any plans relating to construction of a new bed tower at Flower Hospital. F. 1126.

Although avoiding undertaking the major expense of building a new facility or bed tower is a cognizable efficiency (*e.g.*, *Butterworth*, 946 F. Supp. at 1300-01), the evidence shows that ProMedica had no concrete plans to actually proceed with building the Arrowhead hospital or new bed tower at Flower. Accordingly, Respondent's claims of [redacted] in capital avoidance savings and related operating-cost savings of [redacted] resulting "primarily from the avoidance of capital and operating costs associated with the construction and operation of a hospital at Arrowhead and a new bed tower at Flower Hospital" (F. 1109) are unpersuasive.

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In addition, the bulk of the claimed efficiencies from the Joinder are avoided capital costs. F. 1119. In general, capital cost avoidance claims are not cognizable efficiencies. (Town, Tr. 3928-3929 (“removing an expenditure that would create value [is not] an efficiency”); PX02148 at 094 (¶ 172) (Town Expert Report), *in camera*). Firms invest in their businesses to better compete and, thus, enhance consumer welfare, and if these competition-driven investments are “avoided,” consumers generally are left worse off. (PX02148 at 094 (¶ 172) (Town Expert Report), *in camera*). To the extent that avoided capital investments would have benefitted the community, capital avoidance with respect to those investments are not efficiencies, but rather constitute anticompetitive harm resulting from the Joinder. (Town, Tr. 3928-3929; PX02148 at 094 (¶ 172) (Town Expert Report), *in camera*). Thus, Respondent has failed to provide sufficient proof of cognizable efficiencies.

c. Other benefits

As additional benefits of the Joinder, Respondent points to evidence that St. Luke’s employees have received and will continue to receive pay increases in 2011 (F. 1129); St. Luke’s has gained ProMedica’s assistance for its physician recruitment efforts and ProMedica’s recruiters have already helped recruit anesthesiologists for St. Luke’s (F. 1133-1134); and St. Luke’s has started or is about to start work on several deferred capital projects, including [redacted]. F. 1139.

Respondent cites no authority to support a conclusion that lifting a salary freeze to give two one percent pay increases and “thank-you checks” to St. Luke’s employees ranging from \$25 to \$200 (F. 1129-1130) are legally cognizable merger benefits. Further, even if St. Luke’s has started or is about to start work on the above described deferred capital projects, St. Luke’s had \$65 million in cash and investments at the time of the Joinder, compared to a total estimated cost of less than [redacted] million to complete St. Luke’s deferred projects. F. 1141. In any event, Respondent has not shown that these claimed efficiencies are greater than the transaction’s substantial likely anticompetitive effects.

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3. Summary

In *Cardinal Health*, the defendants, after performing a due diligence study, represented that the proposed mergers would result in cost savings and other efficiencies of roughly 82 million dollars per year and represented that they would pass through at least half of the projected cost savings to consumers. *Cardinal Health*, 12 F. Supp. 2d at 62. The FTC did not contest that the proposed mergers would result in large-scale efficiencies, some of which will be passed on to the consumer. *Id.* at 63. Weighing the evidence, the court found that the defendants had sufficiently proved that significant efficiencies would likely result from the proposed mergers, but that the evidence presented by the FTC strongly suggested that much of the savings anticipated from the mergers could also be achieved through continued competition. *Id.* The court then stated: “The critical question raised by the efficiencies defense is whether the projected savings from the mergers are enough to overcome the evidence that tends to show that possibly greater benefits can be achieved by the public through existing, continued competition. The Defendants simply have not made their case on this point.” *Id.*

In this case, Respondent has demonstrated that the Joinder would make St. Luke’s a stronger hospital and would achieve some efficiencies, but those efficiencies are insufficient to legally justify the Joinder. Complaint Counsel has pointed out deficiencies in Respondent’s estimates of efficiencies and has shown that some of the efficiencies identified by Respondent are not merger-specific or are speculative. Overall, Respondent has not demonstrated that the Joinder has resulted in “significant economies” (*University Health*, 938 F.2d at 1223) that benefit consumers or that the benefits are greater than the transaction’s substantial likely anticompetitive effects. Accordingly, Respondent has not met its burden of showing “extraordinary” procompetitive benefits or of demonstrating that the asserted efficiencies offset the likely anticompetitive effects of the increase in market power produced by the Joinder.

G. Remedy

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1. Introduction

Complaint Counsel has proved that Respondent's Joinder with St. Luke's constitutes an illegal acquisition in violation of Section 7 of the Clayton Act. As a remedy for Respondent's unlawful Joinder with St. Luke's, Complaint Counsel seeks an order requiring ProMedica to completely divest its ownership of St. Luke's "at no minimum price . . . to an Acquirer that receives the prior approval of the Commission and . . . pursuant to a Divestiture Agreement that receives the prior approval of the Commission." Complaint Counsel's proposed order, Paragraph II.A.1.; *see* CCB at 105-107. Respondent objects to ordering divestiture in this case, and proposes entry of an alternative order, requiring, *inter alia*, that ProMedica create a second "firewalled" negotiation team that will negotiate and administer MCO contracts exclusively for St. Luke's, independent of ProMedica's other Lucas County hospitals. RRB at 81-82, and Exhibit A thereto. Because MCOs would be free to contract with St. Luke's alone, and not with ProMedica, if they so choose, Respondent argues its proposal will reverse ProMedica's increased bargaining power resulting from the Joinder and restore St. Luke's as an independent competitive restraint. *Id.* at 83.

Respondent further objects to divestiture to an acquirer, as provided in Complaint Counsel's proposed order, rather than divestiture through an unwinding of the Joinder transaction. RRB at 86-87. Finally, Respondent objects to two of the ancillary provisions in Complaint Counsel's proposed order: (1) the requirement that Paramount maintain St. Luke's, and its affiliate SurgiCare, as participating network providers for a period of one year after the effective date of divestiture, Complaint Counsel's proposed order, Paragraph II.N.; and (2) the notification requirements of Paragraph IX of Complaint Counsel's proposed order. RRB at 87-88.²⁸

All provisions of the order proposed by Complaint Counsel, as well as Complaint Counsel's arguments in support thereof have

²⁸ As noted above, Respondent's alternative proposed order, as well as its objections to Complaint Counsel's proposed order, were set forth in Respondent's Reply Brief. Complaint Counsel did not seek leave to submit a surreply to Respondent's Reply Brief.

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been fully considered. This Initial Decision has also fully considered Respondent's alternative proposed order and arguments in support thereof, as well as Respondent's objections to Complaint Counsel's proposed order and supporting arguments. As more fully explained below, the order proposed by Complaint Counsel will be issued herewith as the Order in this case (hereafter "Order"), except that Paragraph II.N. of Complaint Counsel's proposed order will not be included. As so modified, the order proposed by Complaint Counsel is supported by the record and applicable case law.

2. Applicable legal principles

Pursuant to Section 11(b) of the Clayton Act:

If upon such hearing the Commission . . . shall be of the opinion that any of the provisions of [Section 7] have been or are being violated, it shall . . . issue and cause to be served on such person an order requiring such person to cease and desist from such violations, and divest itself of the . . . assets, held . . . in the manner and within the time fixed by said order.

15 U.S.C. § 21(b).

The Commission, in *Evanston*, summarized the law regarding remedies for unlawful mergers, as follows:

The goal of a remedy for a Section 7 violation is to impose relief that is "necessary and appropriate in the public interest to eliminate the effects of the acquisition offensive to the statute." *United States v. E.I. du Pont de Nemours & Co.*, 353 U.S. 586, 607, 77 S. Ct. 872, 1 L. Ed. 2d 1057 (1957). Thus, we attempt to craft a remedy that will create a competitive environment that would have existed in the absence of the violations. *In re RSR Corp.*, 88 F.T.C. 800, 893 (1976), *aff'd*, *RSR Corp. v. FTC*, 602 F.2d 1317 (9th Cir. 1979). "The antitrust laws would deserve little respect if they permitted those who violated them to escape with the fruits of their misconduct on the grounds that imposition of an effective remedy would incidentally result

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in even a substantial monetary loss.” *RSR*, 88 F.T.C. at 895.

Structural remedies are preferred for Section 7 violations. See *United States v. E.I. du Pont de Nemours & Co.*, 366 U.S. 316, 329, 81 S. Ct. 1243, 6 L. Ed. 2d 318 (1961) (calling divestiture “a natural remedy” when a merger violates the antitrust laws). As we recently said, “[m]uch of the case law has . . . found divestiture the most appropriate means for restoring competition lost as a consequence of a merger or acquisition.” *In re Chicago Bridge & Iron Co.*, No. 9300, 138 F.T.C. 1024, 2005 WL 120878, at 93 (FTC Jan. 6, 2005). Divestiture is desirable because, in general, a remedy is more likely to restore competition if the firms that engaged in pre-merger competition are not under common ownership. There are also usually greater long-term costs associated with monitoring the efficacy of a conduct remedy than with imposing a structural solution.

Evanston, 2007 FTC LEXIS 210, at *244-46.

Although divestiture is the preferred remedy, unusual circumstances may necessitate some departure from this norm. *Evanston*, 2007 FTC LEXIS 210, at *245-46; *In re RSR Corp.*, No. 8959, 1976 FTC LEXIS 40, at *208 (1976). In determining a remedy, the Commission does not:

. . . minimize the practical difficulties that may militate against divestiture or other structural relief in particular cases. Despite the breadth of its powers, the Commission would not attempt to apply remedies so drastic, or inequitable, that the cure would be worse than the disease. Thus, while divestiture is normally the appropriate remedy in a Section 7 proceeding, on occasion it may possibl[y] be impracticable or inadequate, or impose unjustifiable hardship

In re Ekco Prods. Co., No. 8122, 65 F.T.C. 1163, 1964 FTC LEXIS 115, at *126-27 (June 30, 1964). “In cases where several equally effective remedies are available short of a complete

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divestiture, a due regard should be given to the preservation of substantial efficiencies or important benefits to the consumer in the choice of an appropriate remedy.” *In re Retail Credit Co.*, No. 8290, 92 F.T.C. 1, 1978 FTC LEXIS 246, at *260 (July 7, 1978).

“[T]he burden rests with respondent to demonstrate that a remedy other than full divestiture would adequately redress any violation which is found.” *In re Fruehauf Corp.*, No. 8972, 1977 FTC LEXIS 9, at *3 n.1, 90 F.T.C. 891 (Dec. 21, 1977); *In re Chicago Bridge & Iron*, No. 9300, 2003 FTC LEXIS 96, at **277 (June 18, 2003), *modified by* 2005 FTC LEXIS 215 (Jan. 6, 2005). *See also In re Diamond Alkali, Co.*, No. 8572, 72 F.T.C. 700, 742, 1967 FTC LEXIS 44, at *88-89 (Oct. 2, 1967) (“In the absence of proof to the contrary the assumption of this Commission must be that ‘only divestiture can reasonably be expected to restore competition and make the affected markets whole again.’”) (quoting *National Tea Company*, 69 F.T.C. 226, 1966 FTC LEXIS 41, at *88 (March 4, 1966)). Where, as in this case, “the Government has successfully borne the considerable burden of establishing a violation of law, all doubts as to the remedy are to be resolved in its favor.” *du Pont*, 366 U.S. at 334.

3. Analysis

a. Alternative remedy to divestiture

The remedy proposed by Respondent is patterned after the remedy ordered in *Evanston*. In *Evanston*, the Commission applied existing legal standards to the facts of that case and ultimately determined that the merger at issue presented “the highly unusual case in which a conduct remedy, rather than divestiture, is more appropriate.” 2007 FTC LEXIS 210, at *246. The Commission required respondent *Evanston Northwestern Healthcare* (“ENH”) “to establish separate and independent negotiating teams -- one for *Evanston and Glenbrook Hospitals* . . . and another for *Highland Park*.” *Evanston*, 2007 FTC LEXIS 210, at *249. The Commission reasoned:

While not ideal, this remedy will allow MCOs to negotiate separately again for these competing hospitals, thus

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re-injecting competition between them for the business of MCOs. Further, ENH should be able to implement the required modifications to its contract negotiating procedures in a very short time. In contrast, divesting Highland Park after seven years of integration would be a complex, lengthy, and expensive process.

Id. at *249.

Respondent makes a cogent argument that enabling MCOs to contract separately with St. Luke's, independent of ProMedica's other Lucas County hospitals, through separate, firewalled, MCO negotiating teams, would restore ProMedica's bargaining power to its pre-Joinder state and preserve St. Luke's as a competitive constraint. In addition, an *Evanston*-style remedy would enable St. Luke's to continue to benefit from ProMedica's stronger financial resources, and, thereby, preserve St. Luke's viability, to the benefit of consumers. See *In re Retail Credit Co.*, 1978 FTC LEXIS 246, at *260 ("due regard should be given to the preservation of substantial efficiencies or important benefits to the consumer"). However, the reasoning of *Evanston* was based upon the extensive integration of Highland Park into the ENH system over the seven years that had elapsed from the time of the merger, during which ENH had integrated the operations of Highland Park into the ENH system. ENH had also made two significant improvements to Highland Park -- the development and implementation of a cardiac surgery program and implementation at Highland Park of "EPIC, the state-of-the-art medical record computer system." *Evanston*, 2007 FTC LEXIS 210, at *248.

Analogizing to *Evanston*, Respondent points to the freeing of space for the addition of private rooms, as a result of the shift of St. Luke's rehabilitation services to Flower, and the allocation by St. Luke's of part of ProMedica's initial capital contribution toward implementing meaningful use of an EMR system. RRB at 84-85. In this regard, the evidence shows that, with the approval of the FTC, ProMedica and St. Luke's had consolidated St. Luke's inpatient rehabilitation program at Flower Hospital and that shifting inpatient rehabilitation services from St. Luke's to Flower permits St. Luke's to convert its former inpatient

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rehabilitation beds to private rooms. F. 1058-1060. The evidence further shows that ProMedica “believes” that St. Luke’s has allocated part of its initial capital contribution of \$10 million toward IT investment to become compliant for “meaningful use.” F. 994. Although several of the necessary components to meet meaningful use requirements have been implemented, St. Luke’s overall implementation of the system is still in the planning stages. F. 995. Thus, the evidence does not demonstrate, as it did in *Evanston*, that divestiture in this case would be a “complex, lengthy, and expensive process.” *Evanston*, 2007 FTC LEXIS 210, at *249. Instead, because of the Hold Separate Agreement, the extensive integration that occurred in *Evanston* has not occurred here. Where, as here, “it is relatively clear that the unwinding of a hospital merger would be unlikely to involve substantial costs, all else being equal, the Commission likely would select divestiture as the remedy.” *Evanston*, 2007 FTC LEXIS 210, at *250. Respondent has failed to meet its burden of proving that a remedy other than the usual remedy of divestiture should be ordered in this case, and the Order therefore provides for divestiture.

b. Divestiture order

Respondent objects to an order requiring divestiture of St. Luke’s to a willing acquirer, as proposed by Complaint Counsel, *see* proposed order, Paragraph II.A., rather than requiring a simple unwinding of the Joinder transaction and returning St. Luke’s to its pre-Joinder status. RRB at 86-87. Considering St. Luke’s weakened financial condition, as found in Part II.N. and analyzed in Part III.E. of this Initial Decision, St. Luke’s viability beyond the next few years is uncertain and, therefore, returning St. Luke’s to its pre-Joinder status may not be an effective remedy in the long term. An order that could result in St. Luke’s ultimate demise is not a remedy that is “necessary and appropriate in the public interest to eliminate the effects of the acquisition. . . .” *du Pont*, 353 U.S. at 607.

Respondent specifically objects to a divestiture of St. Luke’s to Mercy or UTMC, arguing that a Joinder with either entity will raise its own anticompetitive concerns. There is record evidence that St. Luke’s believed an affiliation with Mercy, and to a far

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lesser extent, UTMC, would result in HHI's that could trigger antitrust enforcement, and that an affiliation with either entity could result in increased prices. (PX01030 at 017; PX01016 at 023-024); *see* Merger Guidelines § 5.3. However, the proposed order does not, and the Order will not, limit potential acquirers to Mercy or UTMC. Thus, there is no basis for Respondent's conclusion that divestiture to a willing acquirer, rather than a "spinoff" of St. Luke's "would create the same competitive harms that they assert exist in this case." RRB at 87.

c. Other provisions

Respondent objects to Paragraph II.N. of Complaint Counsel's proposed order. That Paragraph provides that, from the date this Order becomes final and until one (1) year from the effective date of divestiture, and for so long as ProMedica offers any Paramount insurance product, ProMedica may not terminate any agreement with St. Luke's pursuant to which St. Luke's, and its affiliate SurgiCare, shall be participating providers with Paramount, at rates comparable to ProMedica's analogous facilities, as provided in the Joinder Agreement documents. Respondent argues that such provisions give St. Luke's a competitive advantage that it did not have prior to the Joinder, and go beyond the remedial purpose of returning the competitive environment to what it would have been prior to the Joinder. RRB at 87.

The Supreme Court has recognized that "[t]he relief which can be afforded" from an illegal acquisition "is not limited to the restoration of the status quo ante." *Ford Motor Co. v. United States*, 405 U.S. 562, 573 n.8 (1972). However, "the relief must be directed to that which is 'necessary and appropriate in the public interest to eliminate the effects of the acquisition offensive to the statute.'" *Id.* In addition, although the Commission has broad discretion to determine the type of order necessary to remedy the unlawful conduct found to exist, the provisions must be reasonably related to the violation. *Jacob Siegal Co. v. FTC*, 327 U.S. 608, 611-13 (1946). Complaint Counsel provides no support for this provision, since Complaint Counsel's Post-Trial Brief does not even address, much less explain, how requiring ProMedica to include St. Luke's and its affiliate in the Paramount

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network, as set forth in Paragraph II.N., is necessary or appropriate, or reasonably related to the unlawful Joinder.

The evidence shows that St. Luke's was not a member of Paramount's network from January 1, 2001 until the Joinder Agreement with ProMedica in September 2010. F. 177-179. There is no claim, however, and there has been no finding, that Respondent's failing to include St. Luke's in its Paramount networks prior to the Joinder constituted unlawful conduct. Under such circumstances, Respondent should not be ordered to contract with St. Luke's, which after divestiture, will return to its status as ProMedica's competitor. *See Verizon Communs., Inc. v. Law Offices of Curtis V. Trinko, LLP*, 540 U.S. 398, 408 (2004) (noting the general rule that an entity is free to choose with whom to deal, and the qualified right to refuse to deal with rivals). Accordingly, the provisions of Paragraph II.N. are unsupported by the record and are not included in the Order.

Moreover, the evidence shows that St. Luke's considered inclusion in the Paramount network to be a significant advantage to an affiliation with ProMedica. F. 396, 421. In addition, both St. Luke's and ProMedica believed that inclusion of St. Luke's in the Paramount network would take volume, and dollars, away from ProMedica. F. 467-470. Paramount has an arrangement with ProMedica, resulting in a limited network of hospitals that excluded the Mercy hospitals and, prior to the Joinder, St. Luke's. F. 172-173. Although Paramount's network did include UTMC (F. 173), and could have included St. Luke's, if Paramount had chosen to include St. Luke's, the evidence does not demonstrate that St. Luke's would have become a participating provider with Paramount absent the Joinder. The foregoing evidence supports the conclusion that requiring ProMedica to include St. Luke's in the Paramount network would confer a competitive advantage that did not exist prior to the Joinder. For this reason, Paragraph II.N. from Complaint Counsel's proposed order is rejected and is not included in the Order.

Finally, Respondent objects to Paragraph IX of Complaint Counsel's proposed order, which states: "ProMedica shall notify the Commission at least thirty (30) days prior to (1) any proposed dissolution of ProMedica, (2) any proposed acquisition, merger,

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or consolidation of ProMedica, or (3) any other change in ProMedica that may affect compliance obligations arising out of this Order, including but not limited to assignment, the creation or dissolution of subsidiaries, or any other change in ProMedica.” RRB at 88. Respondent argues that the foregoing provision is overbroad because it would require ProMedica to report to the Commission on its activities with regard to all its hospitals, several of which are located outside the relevant geographic market of Lucas County. RRB at 88; *see* F. 3-5. Respondent’s argument is unpersuasive. The notification provisions are reasonably necessary to monitor Respondent’s future conduct, and to this extent, are reasonably related to the unlawful practice found to exist in this case. *Jacob Siegal*, 327 U.S. at 611-13. Any doubt regarding remedy is to be resolved in favor of Complaint Counsel. *du Pont*, 366 U.S. at 334. Accordingly, Paragraph IX is included in the Order.

4. Conclusion

Upon consideration of the entire record, relief designed to remedy the violation of law found to exist is hereby ordered. The Order is designed to restore competition as it existed prior to the Respondent’s unlawful conduct and to remedy the anticompetitive effects arising therefrom.

IV. SUMMARY OF CONCLUSIONS OF LAW

1. The Commission has jurisdiction over Respondent ProMedica Health System (“Respondent” or “ProMedica”) and the subject matter of this proceeding, pursuant to Sections 7 and 11 of the Clayton Act. 15 U.S.C. §§ 18, 21(b).
2. Respondent is, and at all times relevant herein, has been, engaged in “commerce” as defined in Section 1 of the Clayton Act, as amended, 15 U.S.C. § 12.
3. On May 25, 2010, Respondent and St. Luke’s Hospital (“St. Luke’s”) entered into a Joinder Agreement, effective as of September 1, 2010, pursuant to which ProMedica became the sole corporate member or shareholder of St.

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Luke's and its other affiliated entities (hereafter, "Joinder"). The Joinder constitutes an "acquisition" subject to Section 7 of the Clayton Act. 15 U.S.C. § 18.

4. Section 7 of the Clayton Act prohibits acquisitions, "where in any line of commerce or in any activity affecting commerce in any section of the country, the effect of such acquisition may be substantially to lessen competition, or tend to create a monopoly." 15 U.S.C. § 18.
5. Section 11(b) of the Clayton Act, 15 U.S.C. § 21(b), expressly vests the Commission with jurisdiction to determine the legality of a corporate acquisition under Section 7 and, if warranted, to order divestiture.
6. To establish a violation of Section 7, it is not necessary to show that the challenged acquisition *will* lessen competition. It is sufficient to show a reasonable probability that the proposed transaction would substantially lessen competition in the future.
7. The appropriate line of commerce within which to evaluate the probable competitive effects of the Joinder is general acute-care ("GAC") inpatient hospital services sold to commercial health plans, referred to as managed care organizations ("MCOs") (the "relevant product market").
8. Complaint Counsel failed to demonstrate a separate line of commerce consisting of the sale of inpatient obstetrical ("OB") services to MCOs.
9. The appropriate section of the country within which to evaluate the probable competitive effects of the Joinder is Lucas County, Ohio (the "relevant geographic market").
10. Complaint Counsel has proven that there is a reasonable probability that the Joinder will substantially lessen competition in the relevant market for the sale of GAC inpatient hospital services to MCOs in Lucas County, Ohio.

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11. The government can establish a presumption that a transaction will substantially lessen competition by showing that an acquisition will lead to undue concentration in the relevant market. However, market share and concentration data provide only the starting point for analyzing the competitive impact of an acquisition. Other market factors that pertain to likely competitive effects are also assessed.
12. The Joinder between St. Luke's and ProMedica reduces the number of competitors in the market for the sale of GAC inpatient hospital services to MCOs in Lucas County, Ohio from four to three, and increases ProMedica's market share. The statistical evidence demonstrates that the Joinder causes a significant increase in the concentration of power in the relevant market and enables Respondent to control an undue percentage share of the relevant market. Accordingly, the Joinder is presumptively illegal.
13. Complaint Counsel has proven that, from the perspective of MCOs competing to meet the demands of their customers, St. Luke's and one or more of the ProMedica hospitals are close substitutes, and an MCO network that consists only of ProMedica's remaining competitors, University of Toledo Medical Center ("UTMC") and Mercy Health Partners ("Mercy"), would not be marketable in Lucas County. Thus, the Joinder would eliminate ProMedica's close competitor and provide ProMedica with increased bargaining leverage with MCOs.
14. Complaint Counsel has proven that the Joinder enables ProMedica to acquire, and exercise, the power to charge supracompetitive reimbursement rates for the provision of GAC inpatient hospital services provided by ProMedica's Lucas County hospitals, and that increases in Respondent's prices to MCOs would be passed on to MCOs' employer-customers and/or employee-customers, in the form of higher overall health care costs. Thus,

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Complaint Counsel has proven a likelihood of anticompetitive effects resulting from the Joinder.

15. Having proven the likelihood of the anticompetitive effect of price increases in the relevant market, it is not necessary that Complaint Counsel also prove that the Joinder would result in the non-price anticompetitive effect of reduced quality.
16. Respondent asserted a defense based upon the ability of market participants to reposition themselves so as to constrain Respondent from imposing price increases. The Merger Guidelines recognize that “[i]n some cases, non-merging firms may be able to reposition their products to offer close substitutes for the products offered by the merging firms.” Merger Guidelines § 6.1. The Merger Guidelines further note that “[r]epositioning is evaluated much like entry, with consideration given to timeliness, likelihood, and sufficiency.” Merger Guidelines § 6.1. Thus, Respondent must show that the purported repositioning will be timely, likely, and sufficient. The evidence fails to show that market participants are likely to reposition, as claimed by Respondent, or that such repositioning would be timely or sufficient. Respondent’s repositioning defense is rejected.
17. Respondent presented a defense based on the asserted weakened financial condition of St. Luke’s at the time of the Joinder. Evaluating the weakness of the acquired company is an appropriate part of the competitive effects analysis because only a further examination of the particular market - its structure, history and probable future - can provide the appropriate setting for judging the probable anticompetitive effect of the merger.
18. While the precise standard for establishing a “weakened competitor” defense is unclear, the law is clear that financial weakness is probably the weakest ground of all for justifying a merger and certainly cannot be the primary justification for permitting one.

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19. Although St. Luke's was struggling financially prior to the Joinder and its future viability as an independent hospital, beyond the next few years, is by no means certain, current case law does not permit allowing the Joinder to proceed on the basis of St. Luke's weakened financial condition. Respondent's weakened competitor defense is rejected.
20. Respondent raised defenses based upon asserted procompetitive benefits and efficiencies of the Joinder. Claimed efficiencies must be: (1) verifiable; (2) merger-specific, *i.e.*, ones that could not practicably be achieved without the proposed merger; and (3) greater than the transaction's substantial anticompetitive effects.
21. To overcome a presumption that a proposed acquisition would substantially lessen competition, a respondent must demonstrate that the intended acquisition would result in significant economies and that these economies ultimately would benefit competition and, hence, consumers.
22. Although a financially well-off St. Luke's is more beneficial to the community than a hospital that is struggling financially, based upon applicable legal principles, it cannot be concluded that the benefits and efficiencies generated from the Joinder represent "significant economies" that ultimately would benefit competition and, hence, consumers, or that the asserted benefits and efficiencies are greater than the likely anticompetitive effects of the Joinder. Respondent's defenses based upon asserted procompetitive benefits and efficiencies resulting from the Joinder are rejected.
23. The goal of a remedy for a Section 7 violation is to impose relief that is necessary and appropriate in the public interest to eliminate the anticompetitive effects of the unlawful acquisition. The appropriate remedy seeks to create a competitive environment that would have existed in the absence of the violation.

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24. Divestiture is the preferred remedy for a Section 7 violation. Although divestiture is the preferred remedy, unusual circumstances may necessitate some departure from this norm. The burden is on the respondent to demonstrate that a remedy other than full divestiture would adequately redress the violation found to exist.
25. Respondent proposed an alternative remedy, patterned after the remedy ordered in *Evanston*, pursuant to which ProMedica would create a second “firewalled” negotiation team that would negotiate and administer MCO contracts exclusively for St. Luke’s, independent of ProMedica’s other Lucas County hospitals.
26. Respondent has not met its burden of demonstrating unusual circumstances justifying a departure from the preferred remedy of divestiture. Although an *Evanston*-style remedy would likely restore ProMedica’s bargaining power to its pre-Joinder state, preserve St. Luke’s as a competitive constraint, and secure St. Luke’s financial viability, to the benefit of consumers, the facts of the instant case are not sufficiently analogous to the unusual circumstances presented in *Evanston*. Respondent’s proposed alternative remedy is rejected, and divestiture of St. Luke’s is ordered.
27. Although the Commission has broad discretion to determine the type of order necessary to remedy the unlawful conduct found to exist, the provisions must be reasonably related to the violation.
28. Complaint Counsel’s proposal that ProMedica be ordered to maintain St. Luke’s and St. Luke’s affiliate as providers with ProMedica’s health insurance subsidiary Paramount, as promised under the Joinder Agreement, is rejected. There is no claim, and there has been no finding, that Respondent’s failing to include St. Luke’s in its Paramount networks prior to the Joinder constituted unlawful conduct. Under such circumstances, Respondent should not be ordered to contract with St. Luke’s, which after divestiture, will return to its status as

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ProMedica's competitor. In addition, requiring ProMedica to include St. Luke's in the Paramount network confers a competitive advantage that did not prior to the Joinder.

29. The Order entered herein is necessary and appropriate to remedy the violations of law found to exist.

ORDER**I.**

IT IS ORDERED that, as used in this Order, the following definitions shall apply:

- A. "ProMedica" means ProMedica Health System, Inc., its directors, officers, employees, agents, representatives, successors, and assigns; and its joint ventures, subsidiaries (including, but not limited to, ProMedica Health Insurance Corporation), divisions, groups, and affiliates controlled by ProMedica Health System, Inc., and the respective directors, officers, employees, agents, representatives, successors, and assigns of each.
- B. "St. Luke's Hospital" means the Acute-Care Hospital operated at 5901 Monclova Road, Maumee, Ohio 43537.
- C. "Commission" means the Federal Trade Commission.
- D. "Acquirer" means the Person that acquires, with the prior approval of the Commission, the St. Luke's Hospital Assets from ProMedica pursuant to Paragraph II, or from the Trustee pursuant to Paragraph VII of this Order.

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- E. “Acquirer Hospital Business” means all activities relating to general Acute-Care Hospital services and other related health-care services to be conducted by the Acquirer in connection with the St. Luke’s Hospital Assets.
- F. “Acute-Care Hospital” means a health-care facility licensed as a hospital, other than a federally-owned facility, having a duly organized governing body with overall administrative and professional responsibility, and an organized professional staff, that provides 24-hour inpatient care, that may also provide outpatient services, and having as a primary function the provision of General Acute-Care Inpatient Hospital Services.
- G. “Direct Cost” means the cost of direct material and direct labor used to provide the relevant assistance or service.
- H. “Divestiture Agreement” means any agreement, including all exhibits, attachments, agreements, schedules and amendments thereto, that has been approved by the Commission pursuant to which the St. Luke’s Hospital Assets are divested by ProMedica pursuant to Paragraph II, or by the Divestiture Trustee pursuant to Paragraph VII of this Order.
- I. “Divestiture Trustee” means the Person appointed pursuant to Paragraph VII of this Order to divest the St. Luke’s Hospital Assets.
- J. “Effective Date of Divestiture” means the date on which the divestiture of the St. Luke’s Hospital Assets to an Acquirer pursuant to Paragraph II or Paragraph VII of this Order is completed.
- K. “General Acute-Care Inpatient Hospital Services” means a broad cluster of basic medical and surgical diagnostic and treatment services for the medical

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diagnosis, treatment, and care of physically injured or sick persons with short term or episodic health problems or infirmities, that includes an overnight stay in the hospital by the patient. General Acute-Care Inpatient Hospital Services include what are commonly classified in the industry as primary, secondary, and tertiary services, but exclude: (i) services at hospitals that serve solely military and veterans; (ii) services at outpatient facilities that provide same-day service only; (iii) those services known in the industry as specialized tertiary services and quaternary services; and (iv) psychiatric, substance abuse, and rehabilitation services.

- L. “Hospital Provider Contract” means a contract between a Payor and any hospital to provide General Acute-Care Inpatient Hospital Services and related health-care services to enrollees of health plans.
- M. “Intangible Property” means intangible property relating to the Operation of St. Luke’s Hospital including, but not limited to, Intellectual Property, the St. Luke’s Hospital Name and Marks, logos, and the modifications or improvements to such intangible property.
- N. “Intellectual Property” means, without limitation: (i) all patents, patent applications, inventions, and discoveries that may be patentable; (ii) all know-how, trade secrets, software, technical information, data, registrations, applications for governmental approvals, inventions, processes, best practices (including clinical pathways), formulae, protocols, standards, methods, techniques, designs, quality-control practices and information, research and test procedures and information, and safety, environmental and health practices and information; (iii) all confidential or proprietary information, commercial information, management systems, business processes and practices, patient lists, patient information, patient records and files, patient communications,

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procurement practices and information, supplier qualification and approval practices and information, training materials, sales and marketing materials, patient support materials, advertising and promotional materials; and (iv) all rights in any jurisdiction to limit the use or disclosure of any of the foregoing, and rights to sue and recover damages or obtain injunctive relief for infringement, dilution, misappropriation, violation, or breach of any of the foregoing.

- O. “Joinder” means the Operation of St. Luke’s Hospital by ProMedica pursuant to the Joinder Agreement.
- P. “Joinder Agreement” means the agreement by and among ProMedica Health System, Inc., OhioCare Health System, Inc., St. Luke’s Hospital, and St. Luke’s Hospital Foundation, Inc., dated May 25, 2010, and all subsequent amendments thereto.
- Q. “Licensed Intangible Property” means Intangible Property licensed to ProMedica or to St. Luke’s Hospital from a third party relating to the Operation of St. Luke’s Hospital including, but not limited to, Intellectual Property, software, computer programs, patents, know-how, goodwill, technology, trade secrets, technical information, marketing information, protocols, quality-control information, trademarks, trade names, service marks, logos, and the modifications or improvements to such intangible property that are licensed to ProMedica or to St. Luke’s Hospital (“Licensed Intangible Property” does not mean modifications and improvements to intangible property that are not licensed to ProMedica).
- R. “Monitor” means the Person appointed pursuant to Paragraph VI of the Order and with the prior approval of the Commission.

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- S. “Monitor Agreement” means the agreement ProMedica enters into with the Monitor and with the prior approval of the Commission.
- T. “Operation of St. Luke’s Hospital” means all activities relating to the business of St. Luke’s Hospital, operating as an Acute-Care Hospital, including, but not limited to, the activities and services provided at outpatient facilities.
- U. “Ordinary Course of Business” means actions taken by any Person in the ordinary course of the normal day-to-day Operation of St. Luke’s Hospital that is consistent with past practices of such Person in the Operation of St. Luke’s Hospital, including, but not limited to, past practice with respect to amount, timing, and frequency.
- V. “Payor” means any Person that purchases, reimburses for, or otherwise pays for medical goods or services for themselves or for any other person, including, but not limited to: health insurance companies; preferred provider organizations; point-of-service organizations; prepaid hospital, medical, or other health-service plans; health maintenance organizations; government health-benefits programs; employers or other persons providing or administering self-insured health-benefits programs; and patients who purchase medical goods or services for themselves.
- W. “Person” means any natural person, partnership, corporation, association, trust, joint venture, government, government agency, or other business or legal entity.
- X. “Physician” means a doctor of allopathic medicine (“M.D.”) or a doctor of osteopathic medicine (“D.O.”).
- Y. “ProMedica Medical Protocols” means medical protocols promulgated by ProMedica, whether in hard copy or embedded in software, that have been in effect

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at any ProMedica Hospital, excluding St. Luke's Hospital, at any time since Joinder; *provided, however*, that "ProMedica's Medical Protocols" does not mean medical protocols adopted or promulgated, at any time, by any Physician or by any Acquirer, even if such medical protocols are identical, in whole or in part, to medical protocols promulgated by ProMedica.

- Z. "Post-Joinder Hospital Business" means all activities relating to the provision of General Acute-Care Inpatient Hospital Services and other related health-care services conducted by ProMedica after Joinder including, but not limited to, all health-care services, including outpatient services, offered in connection with the St. Luke's Hospital Business.
- AA. "Pre-Joinder St. Luke's Hospital Business" means all activities relating to the provision of General Acute-Care Inpatient Hospital Services and other related health-care services that St. Luke's Hospital was offering as an Acute-Care Hospital prior to Joinder.
- BB. "Real Property of St. Luke's Hospital" means all real property interests (including fee simple interests and real property leasehold interests including all rights, easements and appurtenances, together with all buildings, structures, facilities) that ProMedica acquired pursuant to the Joinder Agreement, whether or not located at St. Luke's Hospital or whether or not related to the Operation of St. Luke's Hospital. Real Property of St. Luke's Hospital includes, but is not limited to, the assets which are identified and listed on confidential Appendix 1 to this Order.
- CC. "St. Luke's Hospital Assets" means all of ProMedica's right, title, and interest in and to St. Luke's Hospital and all related health-care and other assets, tangible or intangible, business, and properties, including any improvements or additions thereto made subsequent to

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Joinder, relating to the operation of the Post-Joinder Hospital Business, including, but not limited to:

1. All Real Property of St. Luke's Hospital;
2. All Tangible Personal Property, including Tangible Personal Property related to the Operation of St. Luke's Hospital, whether or not located at St. Luke's Hospital, and Tangible Personal Property located at the Real Property of St. Luke's Hospital;
3. All consumable or disposable inventory, including but not limited to, janitorial, office, and medical supplies, and at least thirty (30) treatment days of pharmaceuticals;
4. All rights under any contracts and agreements (*e.g.*, leases, service agreements such as dietary and housekeeping services, supply agreements, and procurement contracts), including, but not limited to, all rights to contributions, funds, and other provisions for the benefit of St. Luke's Hospital pursuant to the Joinder Agreement;
5. All rights and title in and to use of the St. Luke's Hospital Name and Marks on a permanent and exclusive basis;
6. St. Luke's Medicare and Medicaid provider numbers, to the extent transferable;
7. All Intellectual Property; *provided, however*, that St. Luke's Hospital Medical Protocols do not include ProMedica Medical Protocols;
8. All governmental approvals, consents, licenses, permits, waivers, or other authorizations to the extent transferable;
9. All rights under warranties and guarantees, express or implied;

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10. All items of prepaid expense; and
11. Books, records, files, correspondence, manuals, computer printouts, databases, and other documents relating to the Operation of St. Luke's Hospital, electronic and hard copy, located on the premises of St. Luke's Hospital or in the possession of the ProMedica Employee responsible for the Operation of St. Luke's Hospital (or copies thereof where ProMedica has a legal obligation to maintain the original document), including, but not limited to:
 - a. documents containing information relating to patients (to the extent transferable under applicable law), including, but not limited to, medical records, including, but not limited to, any electronic medical records system,
 - b. financial records,
 - c. personnel files,
 - d. St. Luke's Hospital Physician Contracts, Physician lists, and other records of St. Luke's Hospital dealings with Physicians,
 - e. maintenance records,
 - f. documents relating to policies and procedures,
 - g. documents relating to quality control,
 - h. documents relating to Payors,
 - i. documents relating to Suppliers, and
 - j. copies of Hospital Provider Contracts and contracts with Suppliers, unless such contracts cannot, according to their terms, be disclosed to

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third parties even with the permission of ProMedica to make such disclosure.

- DD. “St. Luke’s Hospital Contractor” means any Person that provides Physician or other health-care services pursuant to a contract with St. Luke’s Hospital or ProMedica (including, but not limited to, the provision of emergency room, anesthesiology, pathology, or radiology services) in connection with the Operation of St. Luke’s Hospital.
- EE. “St. Luke’s Hospital Physician Contracts” means all agreements to provide the services of a Physician in connection with the Operation of St. Luke’s Hospital, regardless of whether any of the agreements are with a Physician or with a medical group, including, but not limited to, agreements for the services of a medical director for St. Luke’s Hospital and joiner agreements with Physicians in the same medical practice as a medical director of St. Luke’s Hospital.
- FF. “St. Luke’s Hospital Employee” means any individual who was employed by St. Luke’s Hospital prior to Joinder or was employed by ProMedica after Joinder in connection with the Operation of St. Luke’s Hospital, and who has worked part-time or full-time on the premises of St. Luke’s Hospital at any time since Joinder, regardless of whether that individual has also worked on the premises of ProMedica.
- GG. “St. Luke’s Hospital License” means: (i) a worldwide, royalty-free, paid-up, perpetual, irrevocable, transferable, sublicensable, exclusive license under all Intellectual Property owned by or licensed to St. Luke’s Hospital relating to operation of the Post-Joinder Hospital Business at St. Luke’s Hospital (that is not included in the St. Luke’s Hospital Assets) and (ii) such tangible embodiments of the licensed rights (including, but not limited to, physical and electronic copies) as may be necessary or appropriate to enable the Acquirer to utilize the rights.

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- HH. “St. Luke’s Hospital Medical Protocols” means medical protocols promulgated by St. Luke’s Hospital, whether in hard copy or embedded in software, that were in effect at any time prior to Joinder with ProMedica.
- II. “St. Luke’s Hospital Medical Staff Member” means any Physician or other health-care professional who: (1) is not a St. Luke’s Hospital Employee and (2) is a member of the St. Luke’s Hospital medical staff, including, but not limited to, any St. Luke’s Hospital Contractor.
- JJ. “St. Luke’s Hospital Name and Marks” means the name “St. Luke’s Hospital” and any variation of that name, in connection with the St. Luke’s Hospital Assets, and all other associated trade names, business names, proprietary names, registered and unregistered trademarks, service marks and applications, domain names, trade dress, copyrights, copyright registrations and applications, in both published works and unpublished works, relating to the St. Luke’s Hospital Assets.
- KK. “Software” means executable computer code and the documentation for such computer code, but does not mean data processed by such computer code.
- LL. “Supplier” means any Person that has sold to ProMedica any goods or services, other than Physician services, for use in connection with the Operation of St. Luke’s Hospital; *provided, however*, that “Supplier” does not mean an employee of ProMedica.
- MM. “Tangible Personal Property” means all machinery, equipment, spare parts, tools, and tooling (whether customer specific or otherwise); furniture, office equipment, computer hardware, supplies and materials; vehicles and rolling stock; and other items of tangible personal property of every kind whether owned or

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leased, together with any express or implied warranty by the manufacturers, sellers or lessors of any item or component part thereof, and all maintenance records and other documents relating thereto.

- NN. “Transitional Administrative Services” means administrative assistance with respect to the operation of an Acute-Care Hospital and related health-care services, including but not limited to assistance relating to billing, accounting, governmental regulation, human resources management, information systems, managed care contracting, and purchasing.
- OO. “Transitional Clinical Services” means clinical assistance and support services with respect to operation of an Acute-Care Hospital and related health-care services, including but not limited to cardiac surgery, oncology services, and laboratory and pathology services.
- PP. “Transitional Services” means Transitional Administrative Services and Transitional Clinical Services.

II.

IT IS FURTHER ORDERED that:

- A. ProMedica shall:
1. No later than one hundred and eighty (180) days from the date this Order becomes final and effective, divest absolutely and in good faith, and at no minimum price, the St. Luke’s Hospital Assets to an Acquirer that receives the prior approval of the Commission and in a manner, including pursuant to a Divestiture Agreement, that receives the prior approval of the Commission;

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2. Comply with all terms of the Divestiture Agreement approved by the Commission pursuant to this Order, which agreement shall be deemed incorporated by reference into this Order; and any failure by ProMedica to comply with any term of the Divestiture Agreement shall constitute a failure to comply with this Order. The Divestiture Agreement shall not reduce, limit or contradict, or be construed to reduce, limit or contradict, the terms of this Order; *provided, however*, that nothing in this Order shall be construed to reduce any rights or benefits of any Acquirer or to reduce any obligations of ProMedica under such agreement; *provided further*, that if any term of the Divestiture Agreement varies from the terms of this Order (“Order Term”), then to the extent that ProMedica cannot fully comply with both terms, the Order Term shall determine ProMedica’s obligations under this Order. Notwithstanding any paragraph, section, or other provision of the Divestiture Agreement, any failure to meet any condition precedent to closing (whether waived or not) or any modification of the Divestiture Agreement, without the prior approval of the Commission, shall constitute a failure to comply with this Order.
- B. Prior to the Effective Date of Divestiture, ProMedica shall not rescind the Joinder Agreement or any term of the Joinder Agreement necessary to comply with any Paragraph of this Order.
 - C. Prior to the Effective Date of Divestiture, ProMedica shall restore to St. Luke’s Hospital any assets of St. Luke’s Hospital as of the date of Joinder that were removed from St. Luke’s Hospital at any time from the date of Joinder through the Effective Date of Divestiture, other than Inventories consumed in the Ordinary Course of Business. To the extent that:

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1. The St. Luke's Hospital Assets as of the Effective Date of Divestiture do not include (i) assets that ProMedica acquired on the date of Joinder, (ii) assets that replaced those acquired on the date of Joinder, or (iii) any other assets that ProMedica acquired and has used in or that are related to the Post-Joinder Hospital Business, then ProMedica shall add to the St. Luke's Hospital Assets additional assets (of a quality that meets generally acceptable standards of performance) to replace the assets that no longer exist or are no longer controlled by ProMedica;
2. After the date of Joinder and prior to the Effective Date of Divestiture, ProMedica terminated any clinical service, clinical program, support function, or management function (i) performed by the Pre-Joinder St. Luke's Hospital Business, or (ii) performed by the Post-Joinder Hospital Business, then ProMedica shall restore such service, program, or function (of a quality that meets generally acceptable standards of care or performance), no later than the Effective Date of Divestiture of the St. Luke's Hospital Assets or any other date that receives the prior approval of the Commission.

Provided, however, that ProMedica shall not be required to replace any asset or to restore any service, program, or function described by Paragraphs II.C.1. or II.C.2. of this Order if and only if in each instance ProMedica demonstrates to the Commission's satisfaction: (i) that such asset, service, program, or function is not necessary to achieve the purpose of this Order; and (ii) that the Acquirer does not need such asset, service, program, or function to effectively operate the Acquirer Hospital Business in a manner consistent with the purpose of this Order, and if and only if the Commission approves the divestiture without the replacement or restoration of such asset, service, program, or function.

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- D. No later than the Effective Date of Divestiture, ProMedica shall grant to the Acquirer a St. Luke's Hospital License for any use in the Acquirer Hospital Business, and shall take all actions necessary to facilitate the unrestricted use of the St. Luke's Hospital License.
- E. ProMedica shall take all actions and shall effect all arrangements in connection with the divestiture of the St. Luke's Hospital Assets necessary to ensure that the Acquirer can conduct the Acquirer Hospital Business in substantially the same manner as St. Luke's Hospital has operated as the Post-Joinder Hospital Business, and in full compliance with the March 29, 2011, order issued by Judge Katz in *Federal Trade Commission, et al. v. ProMedica Health System*, Civil No. 3:11 CV 47, at St. Luke's Hospital, with an independent full-service medical staff capable of providing General Acute-Care Inpatient Hospital Services, and an independent full-service hospital staff and management, including, but not limited to, providing:
1. Assistance necessary to transfer to the Acquirer all governmental approvals needed to operate the St. Luke's Hospital Assets as an Acute-Care Hospital;
 2. Transitional Services;
 3. The opportunity to recruit and employ St. Luke's Hospital Employees; and
 4. The opportunity to recruit, contract with, and extend medical staff privileges to any St. Luke's Hospital Medical Staff Member, including as provided in Paragraphs II.I, II.J, and II.K of this Order.
- F. ProMedica shall convey as of the Effective Date of Divestiture to the Acquirer the right to use any

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Licensed Intangible Property (to the extent permitted by the third-party licensor), if such right is needed for the Operation of St. Luke's Hospital by the Acquirer and if the Acquirer is unable, using commercially-reasonable efforts, to obtain equivalent rights from other third parties on commercially-reasonable terms and conditions.

G. ProMedica shall:

1. Place no restrictions on the use by the Acquirer of the St. Luke's Hospital Assets;
2. On or before the Effective Date of Divestiture, provide to the Acquirer contact information about Payors and Suppliers for the St. Luke's Hospital Assets;
3. Not object to the sharing of Payor and Supplier contract terms relating to the St. Luke's Hospital Assets: (i) if the Payor or Supplier consents in writing to such disclosure upon a request by the Acquirer, and (ii) if the Acquirer enters into a confidentiality agreement with ProMedica not to disclose the information to any third party; and
4. With respect to contracts with St. Luke's Hospital Suppliers, at the Acquirer's option and as of the Effective Date of Divestiture:
 - a. if such contract can be assigned without third-party approval, assign its rights under the contract to the Acquirer; and
 - b. if such contract can be assigned to the Acquirer only with third-party approval, assist and cooperate with the Acquirer in obtaining:
 - (1) such third-party approval and in assigning the contract to the Acquirer; or

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(2) a new contract.

H. At the request of the Acquirer, for a period not to exceed twelve (12) months from the Effective Date of Divestiture, except as otherwise approved by the Commission, and in a manner (including pursuant to an agreement) that receives the prior approval of the Commission:

1. ProMedica shall provide Transitional Services to the Acquirer sufficient to enable the Acquirer to conduct the Acquirer Hospital Business in substantially the same manner that ProMedica has conducted the Post-Joinder Hospital Business at St. Luke's Hospital; and
2. ProMedica shall provide the Transitional Services required by this Paragraph II.H. at substantially the same level and quality as such services are provided by ProMedica in connection with its operation of the Post-Joinder Hospital Business.

Provided, however, that ProMedica shall not (i) require the Acquirer to pay compensation for Transitional Services that exceeds the Direct Cost of providing such goods and services, (ii) terminate its obligation to provide Transitional Services because of a material breach by the Acquirer of any agreement to provide such assistance, in the absence of a final order of a court of competent jurisdiction, or (iii) include a term in any agreement to provide Transitional Services that limits the type of damages (such as indirect, special, and consequential damages) that the Acquirer would be entitled to seek in the event of ProMedica's breach of such agreement.

I. ProMedica shall allow the Acquirer an opportunity to recruit and employ any St. Luke's Hospital Employee in connection with the divestiture of the St. Luke's Hospital Assets so as to enable the Acquirer to

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establish an independent, full-service medical staff, hospital staff and management, including as follows:

1. No later than five (5) days after execution of a divestiture agreement, ProMedica shall (i) identify each St. Luke's Hospital Employee, (ii) allow the Acquirer an opportunity to interview any St. Luke's Hospital Employee, and (iii) allow the Acquirer to inspect the personnel files and other documentation relating to any St. Luke's Hospital Employee, to the extent permissible under applicable laws.
2. ProMedica shall (i) not offer any incentive to any St. Luke's Hospital Employee to decline employment with the Acquirer, (ii) remove any contractual impediments that may deter any St. Luke's Hospital Employee from accepting employment with the Acquirer, including, but not limited to, any non-compete or confidentiality provisions of employment or other contracts with ProMedica that would affect the ability of the St. Luke's Hospital Employee to be employed by the Acquirer, and (iii) not otherwise interfere with the recruitment of any St. Luke's Hospital Employee by the Acquirer, including, but not limited to, by refusing or threatening to refuse to extend medical staff privileges at any ProMedica Acute-Care Hospital.
3. ProMedica shall (i) vest all current and accrued pension benefits as of the date of transition of employment with the Acquirer for any St. Luke's Hospital Employee who accepts an offer of employment from the Acquirer no later than thirty (30) days from the Effective Date of Divestiture and (ii) if the Acquirer has made a written offer of employment to any key personnel, as identified and listed on confidential Appendix 2 to this Order, provide such key personnel with reasonable financial incentives to accept a position with the

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Acquirer at the time of the Effective Date of Divestiture, including, but not limited to (and subject to Commission approval), payment of an incentive equal to up to three (3) months of such key personnel's base salary to be paid only upon such key personnel's completion of one (1) year of employment with the Acquirer.

4. For a period ending two (2) years after the Effective Date of Divestiture, ProMedica shall not, directly or indirectly, solicit, hire, or enter into any arrangement for the services of any St. Luke's Hospital Employee employed by the Acquirer, unless such St. Luke's Hospital Employee's employment has been terminated by the Acquirer; *provided, however*, this Paragraph II.I.4 shall not prohibit ProMedica from: (i) advertising for employees in newspapers, trade publications, or other media not targeted specifically at the St. Luke's Hospital Employees, (ii) hiring employees who apply for employment with ProMedica, as long as such employees were not solicited by ProMedica in violation of this Paragraph II.I.4, or (iii) offering employment to a St. Luke's Hospital Employee who is employed by the Acquirer in only a part-time capacity, if the employment offered by ProMedica would not, in any way, interfere with that employee's ability to fulfill his or her employment responsibilities to the Acquirer.
- J. ProMedica shall allow the Acquirer an unimpeded opportunity to recruit, contract with, and otherwise extend medical staff privileges to any St. Luke's Hospital Medical Staff Member in connection with the divestiture of the St. Luke's Hospital Assets so as to enable the Acquirer to establish an independent, complete, full-service medical staff, including as follows:
 1. No later than the date of execution of a divestiture agreement, ProMedica shall (i) identify each St.

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Luke's Hospital Medical Staff Member, (ii) allow the Acquirer an opportunity to interview any St. Luke's Hospital Medical Staff Member, and (iii) allow the Acquirer to inspect the files and other documentation relating to any St. Luke's Hospital Medical Staff Member, to the extent permissible under applicable laws.

2. ProMedica shall (i) not offer any incentive to any St. Luke's Hospital Medical Staff Member to decline to join the Acquirer's medical staff; (ii) remove any contractual impediments that may deter any St. Luke's Hospital Medical Staff Member from joining the Acquirer's medical staff, including, but not limited to, any non-compete or confidentiality provisions of employment or other contracts with ProMedica that would affect the ability of the St. Luke's Hospital Medical Staff Members to be recruited by the Acquirer; and (iii) not otherwise interfere with the recruitment of any St. Luke's Hospital Medical Staff Member by the Acquirer, including, but not limited to, by refusing or threatening to refuse to extend medical staff privileges at any ProMedica Acute-Care Hospital.
- K. With respect to each Physician who has provided services to St. Luke's Hospital pursuant to any St. Luke's Hospital Physician Contract in effect at any time preceding the Effective Date of Divestiture ("Contract Physician"), ProMedica shall not offer any incentive to the Contract Physician, the Contract Physician's practice group, or other members of the Contract Physician's practice group to decline to provide services to St. Luke's Hospital, and shall eliminate any confidentiality restrictions that would prevent the Contract Physician, the Contract Physician's practice group, or other members of the Contract Physician's practice group from using or transferring to the Acquirer of the St. Luke's Hospital Assets any information relating to the Operation of St. Luke's Hospital.

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- L. Except in the course of performing its obligations under this Order, ProMedica shall:
1. not provide, disclose, or otherwise make available any trade secrets or any sensitive or proprietary commercial or financial information relating to the Acquirer or the Acquirer Hospital Business to any Person other than the Acquirer, and shall not use such information for any reason or purpose;
 2. disclose trade secrets or any sensitive or proprietary commercial or financial information relating to the Acquirer or the Acquirer Hospital Business to any Person other than the Acquirer (i) only in the manner and to the extent necessary to satisfy ProMedica's obligations under this Order and (ii) only to Persons who agree in writing to maintain the confidentiality of such information; and
 3. enforce the terms of this Paragraph II.L as to any Person and take such action as is necessary, including training, to cause each such Person to comply with the terms of this Paragraph II.L., including any actions that ProMedica would take to protect its own trade secrets or sensitive or proprietary commercial or financial information.
- M. No later than the Effective Date of Divestiture, ProMedica shall assign to the Acquirer any Hospital Provider Contract for the provision of services in connection with the Operation of St. Luke's Hospital that is in effect as of the date the divestiture provisions of this Order become final and effective; *provided, however,* that nothing in this Paragraph II.M. shall preclude ProMedica from completing any post-termination obligations relating to any Hospital Provider Contract.

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- N. The purpose of the divestiture of the St. Luke's Hospital Assets is to ensure the continued Operation of St. Luke's Hospital by the Acquirer, independent of ProMedica, and to remedy the lessening of competition resulting from ProMedica's acquisition of St. Luke's Hospital.

III.**IT IS FURTHER ORDERED** that:

- A. From the date this Order becomes final and effective (without regard to the finality of the divestiture requirements herein) until the Effective Date of Divestiture, ProMedica shall not:
1. Sell or transfer any St. Luke's Hospital Assets, other than in the Ordinary Course of Business;
 2. Eliminate, transfer, or consolidate any clinical service offered in connection with the Post-Joinder Hospital Business;
 3. Fail to maintain the employment of all St. Luke's Hospital Employees or otherwise fail to keep the Post-Joinder Hospital Business staffed with sufficient employees; *provided, however,* that ProMedica may terminate employees for cause consistent with the Operation of St. Luke's Hospital on the day before Joinder (in which event ProMedica shall replace such employees);
 4. Modify, change, or cancel any Physician privileges in connection with the Post-Joinder Hospital Business; *provided, however,* that ProMedica may revoke the privileges of any individual Physician consistent with the practices and procedures in place in connection with the Operation of St. Luke's Hospital on the day before Joinder; or

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5. Terminate, or cause or allow termination of any contract between any Payor and St. Luke's Hospital. For any contract between a Payor and St. Luke's Hospital that expires during the term of this Order, ProMedica shall offer to extend such contract at rates for services in connection with the Post-Joinder Hospital Business that shall be increased no more than the highest year-over-year escalator percentage as provided in such contract.

IV.**IT IS FURTHER ORDERED** that:

- A. From the date this Order becomes final and effective (without regard to the finality of the divestiture requirements herein) until the Effective Date of Divestiture, ProMedica shall take such actions as are necessary to maintain the viability, marketability, and competitiveness of the St. Luke's Hospital Assets and the Post-Joinder Hospital Business relating to the St. Luke's Hospital Assets. Among other things that may be necessary, ProMedica shall:
 1. Maintain the operations of the Post-Joinder Hospital Business relating to the St. Luke's Hospital Assets in the Ordinary Course of Business and in accordance with past practice (including regular repair and maintenance of the St. Luke's Hospital Assets).
 2. Use best efforts to maintain and increase revenues of the Post-Joinder Hospital Business relating to the St. Luke's Hospital Assets, and to maintain at budgeted levels for the year 2010 or the current year, whichever are higher, all administrative, technical, and marketing support for the Post-Joinder Hospital Business relating to the St. Luke's Hospital Assets.

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3. Use best efforts to maintain the current workforce and to retain the services of employees and agents in connection with the Post-Joinder Hospital Business relating to the St. Luke's Hospital Assets, including payment of bonuses as necessary, and maintain the relations and goodwill with patients, Physicians, Suppliers, vendors, employees, landlords, creditors, agents, and others having business relationships with the Post-Joinder Hospital Business relating to the St. Luke's Hospital Assets.
 4. Assure that ProMedica's employees with primary responsibility for managing and operating the Post-Joinder Hospital Business relating to the St. Luke's Hospital Assets are not transferred or reassigned to other areas within ProMedica's organization, except for transfer bids initiated by employees pursuant to ProMedica's regular, established job-posting policy (in which event ProMedica shall replace such employees).
 5. Provide sufficient working capital to maintain the Post-Joinder Hospital Business relating to the St. Luke's Hospital Assets as an economically viable and competitive ongoing business and shall not, except as part of a divestiture approved by the Commission pursuant to this Order, remove, sell, lease, assign, transfer, license, pledge for collateral, or otherwise dispose of the St. Luke's Hospital Assets.
- B. No later than thirty (30) days from the date this Order becomes final and effective (without regard to the finality of the divestiture requirements herein), ProMedica shall file a verified written report to the Commission that identifies (i) all assets included in the St. Luke's Hospital Assets, (ii) all assets originally acquired or that replace assets originally acquired by ProMedica as a result of Joinder, (iii) all assets relating to the Post-Joinder Hospital Business that are not

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included in the St. Luke's Hospital Assets, and (iv) all clinical services, support functions, and management functions that ProMedica discontinued at St. Luke's Hospital after Joinder (hereafter "Accounting").

V.

IT IS FURTHER ORDERED that no later than five (5) days from the date this Order becomes final and effective (without regard to the finality of the divestiture requirements herein), ProMedica shall provide a copy of this Order and Complaint to each of ProMedica's officers, employees, or agents having managerial responsibility for any of ProMedica's obligations under Paragraphs II, III, and IV of this Order.

VI.

IT IS FURTHER ORDERED that:

- A. At any time after this Order becomes final and effective (without regard to the finality of the divestiture requirements herein), the Commission may appoint a Person ("Monitor") to monitor ProMedica's compliance with its obligations under this Order, consult with Commission staff, and report to the Commission regarding ProMedica's compliance with its obligations under this Order.
- B. If a Monitor is appointed pursuant to Paragraph VI.A of this Order, ProMedica shall consent to the following terms and conditions regarding the powers, duties, authorities, and responsibilities of the Monitor:
 - 1. The Monitor shall have the power and authority to monitor ProMedica's compliance with the terms of this Order, and shall exercise such power and authority and carry out the duties and responsibilities of the Monitor pursuant to the terms of this Order and in a manner consistent with the purposes of this Order and in consultation with the Commission or its staff.

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2. Within ten (10) days after appointment of the Monitor, ProMedica shall execute an agreement that, subject to the approval of the Commission, confers on the Monitor all the rights and powers necessary to permit the Monitor to monitor ProMedica's compliance with the terms of this Order in a manner consistent with the purposes of this Order. If requested by ProMedica, the Monitor shall sign a confidentiality agreement prohibiting the use or disclosure to anyone other than the Commission (or any Person retained by the Monitor pursuant to Paragraph VI.B.5. of this Order), of any competitively-sensitive or proprietary information gained as a result of his or her role as Monitor, for any purpose other than performance of the Monitor's duties under this Order.
3. The Monitor's power and duties under this Paragraph VI shall terminate three (3) business days after the Monitor has completed his or her final report pursuant to Paragraph VI.B.8. of this Order or at such other time as directed by the Commission.
4. ProMedica shall cooperate with any Monitor appointed by the Commission in the performance of his or her duties, and shall provide the Monitor with full and complete access to ProMedica's books, records, documents, personnel, facilities, and technical information relating to compliance with this Order, or to any other relevant information, as the Monitor may reasonably request. ProMedica shall cooperate with any reasonable request of the Monitor. ProMedica shall take no action to interfere with or impede the Monitor's ability to monitor ProMedica's compliance with this Order.

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5. The Monitor shall serve, without bond or other security, at the expense of ProMedica, on such reasonable and customary terms and conditions as the Commission may set. The Monitor shall have the authority to employ, at the expense of ProMedica, such consultants, accountants, attorneys, and other representatives and assistants as are reasonably necessary to carry out the Monitor's duties and responsibilities. The Monitor shall account for all expenses incurred, including fees for his or her services, subject to the approval of the Commission.
6. ProMedica shall indemnify the Monitor and hold the Monitor harmless against any losses, claims, damages, liabilities, or expenses arising out of, or in connection with, the performance of the Monitor's duties, including all reasonable fees of counsel and other expenses incurred in connection with the preparation for, or defense of, any claim, whether or not resulting in any liability, except to the extent that such losses, claims, damages, liabilities, or expenses result from the Monitor's gross negligence or willful misconduct. For purposes of this Paragraph VI.B.6., the term "Monitor" shall include all Persons retained by the Monitor pursuant to Paragraph VI.B.5. of this Order.
7. If at any time the Commission determines that the Monitor has ceased to act or failed to act diligently, or is unwilling or unable to continue to serve, the Commission may appoint a substitute to serve as Monitor in the same manner as provided by this Order.
8. The Monitor shall report in writing to the Commission (i) every sixty (60) days from the date this Order becomes final, (ii) no later than thirty (30) days from the date ProMedica completes its obligations under this Order, and (iii) at any other

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time as requested by the staff of the Commission, concerning ProMedica's compliance with this Order.

- C. ProMedica shall submit the following reports to the Monitor: (i) no later than twenty (20) days after the date the Monitor is appointed by the Commission pursuant to Paragraph VI.A. of this Order, a copy of the Accounting required by Paragraph IV.B. of this Order; and (ii) copies of all compliance reports filed with the Commission.
- D. ProMedica shall provide the Monitor with: (i) prompt notification of significant meetings, including date, time and venue, scheduled after the execution of the Monitor Agreement, relating to the regulatory approvals, marketing, sale and divestiture of the St. Luke's Hospital Assets, and such meetings may be attended by the Monitor or his representative, at the Monitor's option or at the request of the Commission or staff of the Commission; and (ii) the minutes, if any, of the above-referenced meetings as soon as practicable and, in any event, not later than those minutes are available to any employee of ProMedica.
- E. The Commission may, on its own initiative or at the request of the Monitor, issue such additional orders or directions as may be necessary or appropriate to assure compliance with the requirements of this Order.
- F. The Monitor appointed pursuant to this Order may be the same Person appointed as Divestiture Trustee pursuant to Paragraph II of this Order.

VII.**IT IS FURTHER ORDERED** that:

- A. If ProMedica has not divested, absolutely and in good faith, the St. Luke's Hospital Assets pursuant to the requirements of Paragraph II of this Order, within the

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time and manner required by Paragraph II of this Order, the Commission may at any time appoint one or more Persons as Divestiture Trustee to divest the St. Luke's Hospital Assets, at no minimum price, and pursuant to the requirements of Paragraph II of this Order, in a manner that satisfies the requirements of this Order.

- B. In the event that the Commission or the Attorney General of the United States brings an action pursuant to § 5(l) of the Federal Trade Commission Act, 15 U.S.C. § 45(l), or any other statute enforced by the Commission, ProMedica shall consent to the appointment of a Divestiture Trustee in such action. Neither the appointment of a Divestiture Trustee nor a decision not to appoint a Divestiture Trustee under this Paragraph VII shall preclude the Commission or the Attorney General from seeking civil penalties or any other relief available to it, including appointment of a court-appointed Divestiture Trustee, pursuant to § 5(l) of the Federal Trade Commission Act, or any other statute enforced by the Commission, for any failure by the ProMedica to comply with this Order.
- C. If a Divestiture Trustee is appointed by the Commission or a court pursuant to this Paragraph VII, ProMedica shall consent to the following terms and conditions regarding the Divestiture Trustee's powers, duties, authority, and responsibilities:
1. Subject to the prior approval of the Commission, the Divestiture Trustee shall have the exclusive power and authority to effect the divestiture pursuant to the requirements of Paragraph II of this Order and in a manner consistent with the purposes of this Order.
 2. Within ten (10) days after appointment of the Divestiture Trustee, ProMedica shall execute an agreement that, subject to the prior approval of the Commission and, in the case of a court-appointed

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Divestiture Trustee, of the court, transfers to the Divestiture Trustee all rights and powers necessary to permit the Divestiture Trustee to effect the divestiture and perform the requirements of Paragraph II of this Order for which he or she has been appointed.

3. The Divestiture Trustee shall have twelve (12) months from the date the Commission approves the agreement described in Paragraph VII.C.2. of this Order to accomplish the divestiture, which shall be subject to the prior approval of the Commission. If, however, at the end of the twelve-month period the Divestiture Trustee has submitted a plan of divestiture or believes that divestiture can be achieved within a reasonable time, the divestiture period may be extended by the Commission, or, in the case of a court appointed Divestiture Trustee, by the court.
4. ProMedica shall provide the Divestiture Trustee with full and complete access to the personnel, books, records, and facilities related to the assets to be divested, or to any other relevant information, as the Divestiture Trustee may request. ProMedica shall develop such financial or other information as the Divestiture Trustee may reasonably request and shall cooperate with the Divestiture Trustee. ProMedica shall take no action to interfere with or impede the Divestiture Trustee's accomplishment of the divestiture. Any delays in divestiture caused by ProMedica shall extend the time for divestiture under this Paragraph in an amount equal to the delay, as determined by the Commission or, for a court-appointed Divestiture Trustee, by the court.
5. The Divestiture Trustee shall use his or her best efforts to negotiate the most favorable price and terms available in each contract that is submitted to the Commission, but shall divest expeditiously at

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no minimum price. The divestiture shall be made only to an Acquirer that receives the prior approval of the Commission, and the divestiture shall be accomplished only in a manner that receives the prior approval of the Commission; *provided, however*, if the Divestiture Trustee receives bona fide offers from more than one acquiring entity, and if the Commission determines to approve more than one such acquiring entity, the Divestiture Trustee shall divest to the acquiring entity or entities selected by ProMedica from among those approved by the Commission; *provided further*, that ProMedica shall select such entity within ten (10) business days of receiving written notification of the Commission's approval.

6. The Divestiture Trustee shall serve, without bond or other security, at the cost and expense of ProMedica, on such reasonable and customary terms and conditions as the Commission or a court may set. The Divestiture Trustee shall have the authority to employ, at the cost and expense of ProMedica, such consultants, accountants, attorneys, investment bankers, business brokers, appraisers, and other representatives and assistants as are necessary to carry out the Divestiture Trustee's duties and responsibilities. The Divestiture Trustee shall account for all monies derived from the divestiture and all expenses incurred. After approval by the Commission of the account of the Divestiture Trustee, including fees for his or her services, all remaining monies shall be paid at the direction of the ProMedica, and the Divestiture Trustee's power shall be terminated. The Divestiture Trustee's compensation may be based in part on a commission arrangement contingent on the Divestiture Trustee's divesting the assets.
7. ProMedica shall indemnify the Divestiture Trustee and hold the Divestiture Trustee harmless against any losses, claims, damages, liabilities, or expenses

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arising out of, or in connection with, the performance of the Divestiture Trustee's duties, including all reasonable fees of counsel and other expenses incurred in connection with the preparation for, or defense of any claim, whether or not resulting in any liability, except to the extent that such liabilities, losses, damages, claims, or expenses result from gross negligence or willful misconduct by the Divestiture Trustee. For purposes of this Paragraph VII.C.7., the term "Divestiture Trustee" shall include all Persons retained by the Divestiture Trustee pursuant to Paragraph VII.C.6. of this Order.

8. If the Divestiture Trustee ceases to act or fails to act diligently, the Commission may appoint a substitute Divestiture Trustee in the same manner as provided in this Paragraph VII for appointment of the initial Divestiture Trustee.
 9. The Divestiture Trustee shall have no obligation or authority to operate or maintain the assets to be divested.
 10. The Divestiture Trustee shall report in writing to the Commission every sixty (60) days concerning the Divestiture Trustee's efforts to accomplish the divestiture.
- D. The Commission or, in the case of a court-appointed Divestiture Trustee, the court, may on its own initiative or at the request of the Divestiture Trustee issue such additional orders or directions as may be necessary or appropriate to accomplish the divestiture required by this Order.
- E. The Divestiture Trustee appointed pursuant to this Paragraph may be the same Person appointed as the Monitor pursuant to Paragraph VI of this Order.

VIII.

Initial Decision

IT IS FURTHER ORDERED that:

- A. ProMedica shall file a verified written report with the Commission setting forth in detail the manner and form in which it intends to comply, is complying, and has complied with this Order (i) no later than thirty (30) days from the date this Order becomes final and effective (without regard to the finality of the divestiture requirements herein), and every thirty (30) days thereafter until the divestiture of the St. Luke's Hospital Assets is accomplished, and (ii) thereafter, every sixty (60) days (measured from the Effective Date of Divestiture) until the date ProMedica completes its obligations under this Order; *provided, however,* that ProMedica shall also file the report required by this Paragraph VIII at any other time as the Commission may require.
- B. ProMedica shall include in its compliance reports, among other things required by the Commission, a full description of the efforts being made to comply with the relevant Paragraphs of this Order, a description (when applicable) of all substantive contacts or negotiations relating to the divestiture required by Paragraph II of this Order, the identity of all parties contacted, copies of all written communications to and from such parties, internal documents and communications, and all reports and recommendations concerning the divestiture, the date of divestiture, and a statement that the divestiture has been accomplished in the manner approved by the Commission.

IX.

IT IS FURTHER ORDERED that ProMedica shall notify the Commission at least thirty (30) days prior to (1) any proposed dissolution of ProMedica, (2) any proposed acquisition, merger, or consolidation of ProMedica, or (3) any other change in ProMedica that may affect compliance obligations arising out of this Order, including but not limited to assignment, the creation or

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dissolution of subsidiaries, or any other change in ProMedica.

X.

IT IS FURTHER ORDERED that, for the purpose of determining or securing compliance with this Order, and subject to any legally recognized privilege, and upon written request with reasonable notice, ProMedica shall permit any duly authorized representative of the Commission:

- A. Access, during office hours of ProMedica, and in the presence of counsel, to all facilities and access to inspect and copy all books, ledgers, accounts, correspondence, memoranda, and all other records and documents in the possession, or under the control, of ProMedica relating to compliance with this Order, which copying services shall be provided by ProMedica at its expense; and
- B. To interview officers, directors, or employees of ProMedica, who may have counsel present, regarding such matters.

Initial Decision

CONFIDENTIAL APPENDIX 1

**[Redacted From the Public Record Version,
But Incorporated By Reference]**

CONFIDENTIAL APPENDIX 2

**[Redacted From the Public Record Version,
But Incorporated By Reference]**

Complaint

**IN THE MATTER OF
SCANSCOUT, INC.****CONSENT ORDER, ETC. IN REGARD TO ALLEGED VIOLATIONS OF
SEC. 5 OF THE FEDERAL TRADE COMMISSION ACT**

*Docket No. C-4344; File No. 102 3185
Filed, December 14, 2011 — Decision, December 14, 2011*

This consent order addresses allegations that ScanScout deceived consumers by misrepresenting the extent to which consumers could prevent companies from collecting data about their online browsing activities. The complaint alleges that ScanScout's privacy policy falsely represented that consumers could opt out of receiving ScanScout's cookies by changing their browser settings. However, users could not opt out of receiving the Flash cookies that ScanScout utilized. The complaint alleges that ScanScout's representations regarding consumers' ability to opt out of receiving cookies were false and misleading, in violation of the FTC Act. The order prohibits ScanScout from misrepresenting the extent to which data on its users' online activities is collected, used, disclosed, or shared; and the extent to which users may exercise control over the use of this data. The order further requires ScanScout to notify users that it collects browser activity data to deliver targeted ads and to provide users with the ability to opt out of this feature.

Participants

For the *Commission*: *Jamie Hine and Kandi Parsons.*

For the *Respondent*: *Howard Morse, Cooley LLP.*

COMPLAINT

The Federal Trade Commission, having reason to believe that ScanScout, Inc. has violated the provisions of the Federal Trade Commission Act, and it appearing to the Commission that this proceeding is in the public interest, alleges:

1. Respondent ScanScout, Inc. ("ScanScout") is a Delaware corporation with its principal office or place of business at 295 Devonshire Street, Boston, MA 02110.

Complaint

2. The acts and practices of ScanScout as alleged in this complaint have been in or affecting commerce, as “commerce” is defined in Section 4 of the Federal Trade Commission Act.

SCANSCOUT’S BUSINESS PRACTICES

3. ScanScout is a video advertising network, which acts as an intermediary between website publishers (“publishers”) and advertisers. ScanScout purchases advertising space on websites and contracts with advertisers to place their video advertisements on these websites. In addition, ScanScout works with other third parties, including ad servers, to deliver advertising campaigns.

4. At times, ScanScout decides which video advertisements should be delivered to users’ browsers by engaging in online behavioral advertising. Online behavioral advertising is the practice of collecting and storing information about users’ online activities in order to deliver advertising targeted to their interests.

5. Online behavioral advertising often utilizes HTTP cookies, which are small text files that can be used to collect and store information about a user’s online activities, including information such as the content or advertisements viewed or the pages visited within a particular website. These cookies contain a unique identification number that allows an advertising network to recognize the user’s computer and correlate the computer to online activity. When a user visits a website within an advertising network’s group of publishers, the advertising network may set a new HTTP cookie in the computer’s browser or automatically receives a previously set HTTP cookie from the computer’s browser. The advertising network then may add information about the user’s web browsing activities to information already collected via the cookie, and may use such information to serve online advertisements that are targeted to the user’s interests as indicated by the user’s web browsing history. Users can delete existing HTTP cookies or block the delivery of new HTTP cookies by changing their browsers’ privacy settings.

6. From April 2007 until September 2009, ScanScout used Flash local shared objects, also known as “Flash cookies”— as opposed to HTTP cookies – to collect and store user data and

Complaint

facilitate online behavioral targeting of video advertisements. Flash cookies, like HTTP cookies, can be used to store data correlated with a unique identification number on a computer. Flash cookies store such data in a different location on a computer than HTTP cookies. At the time that ScanScout used Flash cookies, they were not controlled through a computer's browser. Accordingly, if users changed their browsers' privacy settings to delete or block cookies, Flash cookies were unaffected.

7. During the time that ScanScout utilized Flash cookies, from April 2007 until September 2009, users could not prevent Scanscout from collecting data about their online activities or from serving them targeted video advertisements by changing their browser settings to delete or block HTTP cookies.

SCANSCOUT'S STATEMENTS

8. From April 2007 until September 2009, ScanScout disseminated, or caused to be disseminated, a privacy policy on its website, which stated:

General user data, such as your computer's Internet Protocol (IP) address, operating system and browser type, pages you visited, and the date and time of your visit, is automatically collected through the use of "cookies". Cookies are small files that are stored on your computer by a website to give you a unique identification. Cookies also keep track of services you have used, record registration information regarding your login name and password, record your preferences and keep you logged into the Site. You can opt out of receiving a cookie by changing your browser settings to prevent the receipt of cookies. Since each web browser is different, we recommend that you please look through your browser "Help" file to learn the correct way to modify your cookies set up. . . We may use automatically collected information and cookies information for a number of purposes, including but not limited to. . . provide custom, personalized content, and information; monitor the effectiveness of our marketing campaigns. . . (emphasis added)

Complaint

VIOLATION OF THE FTC ACT

9. Through the means described in Paragraph 8, ScanScout represented, expressly or by implication, that consumers could prevent ScanScout from collecting data about their online activities by changing their browser settings to prevent the receipt of cookies.

10. In truth and in fact, as described in Paragraphs 6 and 7, consumers could not prevent ScanScout from collecting data about their online activities by changing their browser settings to prevent the receipt of cookies. Therefore, the representation set forth in Paragraph 9 was false or misleading.

11. The acts and practices of ScanScout, as alleged in this complaint, constitute deceptive acts or practices in or affecting commerce in violation of Section 5(a) of the Federal Trade Commission Act.

THEREFORE, the Federal Trade Commission this fourteenth day of December, 2011, has issued this complaint against respondent.

By the Commission.

DECISION AND ORDER

The Federal Trade Commission having initiated an investigation of certain acts and practices of the Respondent named in the caption hereof, and the Respondent having been furnished thereafter with a copy of a draft Complaint that the Bureau of Consumer Protection proposed to present to the Commission for its consideration and which, if issued by the Commission, would charge the Respondent with violation of the Federal Trade Commission Act, 15 U.S.C. § 45 *et seq*;

Decision and Order

The Respondent, its attorney, and counsel for the Commission having thereafter executed an Agreement Containing Consent Order (“Consent Agreement”), an admission by the Respondent of all the jurisdictional facts set forth in the aforesaid draft Complaint, a statement that the signing of said Consent Agreement is for settlement purposes only and does not constitute an admission by Respondent that the law has been violated as alleged in such Complaint, or that the facts as alleged in such Complaint, other than jurisdictional facts, are true, and waivers and other provisions as required by the Commission’s Rules; and

The Commission having thereafter considered the matter and having determined that it has reason to believe that the Respondent has violated the said Act, and that a Complaint should issue stating its charges in that respect, and having thereupon accepted the executed Consent Agreement and placed such Consent Agreement on the public record for a period of thirty (30) days for the receipt and consideration of public comments, now in further conformity with the procedure described in Section 2.34 of its Rules, the Commission hereby issues its Complaint, makes the following jurisdictional findings and enters the following Order:

1. ScanScout is a Delaware corporation with its principal office or place of business at 295 Devonshire Street, Boston, MA 02110.
2. Respondent admits all the jurisdictional facts set forth in the draft complaint.

ORDER**DEFINITIONS**

For purposes of this order, the following definitions shall apply:

1. Unless otherwise specified, “respondent” shall mean ScanScout, Inc., a corporation, and its parent, Tremor Video, Inc., and each of their subsidiaries, successors or assigns.

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2. “Clear(ly) and prominent(ly)” shall mean:
 - a. In textual communications (e.g., printed publications or words displayed on the screen of a computer or device), the required disclosures are of a type, size, and location sufficiently noticeable for an ordinary consumer to read and comprehend them, in print that contrasts highly with the background on which they appear;
 - b. In communications disseminated orally or through audible means (e.g., radio or streaming audio), the required disclosures are delivered in a volume and cadence sufficient for an ordinary consumer to hear and comprehend them;
 - c. In communications disseminated through video means (e.g., television or streaming video), the required disclosures are in writing in a form consistent with subparagraph (A) of this definition and shall appear on the screen for a duration sufficient for an ordinary consumer to read and comprehend them, and in the same language as the predominant language that is used in the communication; and
 - d. In all instances, the required disclosures: (1) are presented in an understandable language and syntax; and (2) include nothing contrary to, inconsistent with, or in mitigation of any other statements or disclosures provided by respondent.
3. “Commerce” shall mean as defined in Section 4 of the Federal Trade Commission Act, 15 U.S.C. § 44.
4. “Computer” or “device” shall mean any desktop or laptop computer, handheld device, telephone, or other product or device, through which a consumer can access the Internet.

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5. “Collection of data” or “collecting data” shall mean the practice of receiving any information or data from a computer or device, whether transmitted by a web browser or otherwise, and retaining that information, whether on the user’s computer or on a server. “Data collected” shall mean any information or data received from a computer or device, whether transmitted by a web browser or otherwise, and retained, whether on the user’s computer or respondent’s server(s).
6. “User” shall mean any consumer, computer, or device that respondent has uniquely identified.
7. “Online behavioral advertising” shall mean the practice of collecting data about a user’s online activities in order to deliver advertising targeted to the user’s interests.
8. “Permissible uses” shall mean uses of collected data that can be associated with a particular user, or that contains any unique identifier, including user ID or Internet Protocol (IP) address, for the following purposes and no other, provided that such data shall be retained by respondent no longer than reasonably necessary for such purpose and is not used for online behavioral advertising: (a) determining the number of times a specific user has been served or has responded to a specific advertisement within a period of time; (b) fraud prevention; (c) providing a service requested by a user; or (d) verifying a user’s age before serving an age-restricted advertisement. For purposes of (d), such data shall be retained by respondent no longer than the duration of the applicable browsing session, and in no instance no longer than twenty-four (24) hours.

I.

IT IS ORDERED that respondent and its officers, agents, representatives, and employees and all other persons in active concert or participation with any of them, who receive actual

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notice of this Order by personal service or otherwise, whether acting directly or through any entity, in connection with the online advertising, marketing, promotion, offering for sale, sale, or dissemination of any product or service, in or affecting commerce, shall not misrepresent in any manner, expressly or by implication: (A) the extent to which data from or about a particular user or the user's online activities is collected, used, disclosed, or shared; or (B) the extent to which users may exercise control over the collection, use, disclosure, or sharing of data collected from or about them, their computers or devices, or their online activities.

II.

IT IS FURTHER ORDERED that, for so long as respondent engages in online behavioral advertising, respondent, directly or through any entity, in connection with the online advertising, marketing, promotion, offering for sale, sale, or dissemination of any product or service on websites other than respondent's, in or affecting commerce, shall:

- A. Within thirty (30) days after the date of service of this order, place a clear and prominent notice, including a hyperlink, on the homepage(s) of its website(s), which states, "We collect information about your activities on certain websites to send you targeted ads. To opt out of our targeted advertisements click here." When selected, the hyperlink shall take consumers directly to the mechanism required by Part II.B of the order;
- B. Within thirty (30) days after the date of service of this order, provide a clearly and prominently disclosed mechanism that enables users to prevent respondent: from collecting data that can be associated with a particular user, or that contains any unique identifier, including user ID or Internet Protocol (IP) address; from redirecting users' browsers to third parties that collect data, absent a click or other affirmative action by such user; and from associating any previously collected data with the user. *Provided, however,* respondent may collect data that can be associated with a particular user, or that contains a unique

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identifier: (1) to implement the user's choice to prevent respondent from collecting such data; and (2) for permissible uses;

- C. The mechanism set forth in Part II.B shall require no more than one action by the user (e.g., one click or one change to a browser setting) after the user is directed to such mechanism. The user's choice shall remain in effect for a minimum time period of five (5) years, unless the user disables the mechanism. Within close proximity to the mechanism, respondent shall clearly and prominently disclose: (1) that respondent collects information about users' activities on certain websites in order to deliver advertising targeted to users' interests; (2) that if the user implements the mechanism, respondent will not collect this information for the purpose of delivering advertising targeted to the user's interests; (3) the current status of the user's choice (e.g., "not opted out" or "opted out"); and (4) any circumstances that, if initiated by the user, would disable the mechanism or require the user to implement the mechanism again in order to maintain the user's choice (e.g., use of a different browser, use of a different device, or deletion of cookies);
- D. Within ninety (90) days after the date of service of the order, within or immediately adjacent to any display advertisement that respondent serves as part of online behavioral advertising, include a hyperlink that takes consumers directly to the mechanism required by Part II.B of this order. The hyperlink text shall clearly and prominently disclose to consumers that selecting the hyperlink will give them choices about receiving advertising targeted to their interests.
- E. Undertake reasonable efforts to develop and implement, within or immediately adjacent to any video advertisement that respondent serves as part of online behavioral advertising, a clear and prominent hyperlink that directs consumers to the mechanism required by Part II.B of this order, and discloses to

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consumers that they can opt out of receiving advertising targeted to their interests, and report on such efforts as set forth in Part VI of this order.

III.

IT IS FURTHER ORDERED that respondent shall maintain, and upon request make available to the Federal Trade Commission for inspection and copying, unless respondent asserts a valid legal privilege, a print or electronic copy of:

- A. For a period of five (5) years from the entry of this order or from the date of preparation, whichever is later:
1. Consumer complaints or inquiries directed to respondent or forwarded to respondent by a third party concerning: (a) any collection of data by respondent; (b) the use, disclosure, or sharing of such data by respondent; or (c) opt-out practices or any other mechanism to limit or prevent such collection of data or the use, disclosure, or sharing of data collected by respondent, as well as any responses to such complaints or inquiries;
 2. Documents that are sufficient to demonstrate compliance with each provision of this order, including, but not limited to, relevant policies and procedures, documents demonstrating respondent's efforts to develop and implement a clear and prominent hyperlink for video advertisements pursuant to Part II.E, and all reports submitted to the Commission pursuant to this order;
 3. Documents that contradict, qualify, or call into question respondent's compliance with this order; and
- B. For a period of five (5) years after the last public dissemination thereof by respondent, respondent's terms of use, form end-user license agreements,

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frequently asked questions, privacy policies, and other documents publicly disseminated by respondent relating to: (a) collection of data by respondent; (b) the use, disclosure or sharing of such data by respondent; or (c) opt-out practices and other mechanisms to limit or prevent such collection of data or the use, disclosure, or sharing of data collected by respondent.

IV.

IT IS FURTHER ORDERED that respondent shall deliver a copy of this order to all principals, officers, directors, and managers, and to all employees, agents, and representatives having supervisory responsibilities with respect to the subject matter of this order. Respondent shall deliver this order to such current personnel within thirty (30) days after the date of service of the order, and to such future personnel within thirty (30) days after the person assumes such position or responsibilities.

V.

IT IS FURTHER ORDERED that respondent shall notify the Commission at least thirty (30) days prior to any change in the corporation that may affect compliance obligations arising under this order, including, but not limited to, a dissolution, assignment, sale, merger, or other action that would result in the emergence of a successor corporation; the creation or dissolution of a subsidiary, parent, or affiliate that engages in any acts or practices subject to this order; the proposed filing of a bankruptcy petition; or a change in the corporate name or address. *Provided, however,* that with respect to any proposed change in the corporation about which respondent learns less than thirty (30) days prior to the date such action is to take place, respondent shall notify the Commission as soon as is practicable after obtaining such knowledge. Unless otherwise directed by a representative of the Commission in writing, all notices required by this order shall be sent by hand delivery or overnight courier (not the U.S. Postal Service) to the Associate Director of Enforcement, Bureau of Consumer Protection, Federal Trade Commission, 600 Pennsylvania Avenue NW, Washington, DC 20580, with the subject line In the Matter of ScanScout, Inc. FTC File No.

Decision and Order

1023185. *Provided, however*, that, in lieu of hand delivery or overnight courier, a notice may be sent by first-class mail, but only if an electronic version of such notice is contemporaneously sent to the Commission by e-mail to DEbrief@ftc.gov.

VI.

IT IS FURTHER ORDERED that respondent shall, within ninety (90) days after service of the order, file with the Commission a true and accurate report, in writing, setting forth the manner and form in which respondent has complied with this order, including but not limited to compliance with the requirements of Part II.E of this order. Every six (6) months thereafter, and continuing until respondent reports it has implemented the hyperlink set forth in Part II.E of this order for every different format of video advertisement that respondent serves as part of online behavioral advertising, respondent shall submit an additional true and accurate report, in writing, setting forth the manner and form in which respondent has complied with the requirements of Part II.E of this order. Within ten (10) business days of receipt of written notice from a representative of the Federal Trade Commission at such other times as the Federal Trade Commission may require, respondent shall submit additional true and accurate written reports.

VII.

This order will terminate on December 14, 2031, or twenty (20) years from the most recent date that the United States or the Federal Trade Commission files a complaint (with or without an accompanying consent decree) in federal court alleging any violation of the order, whichever comes later; *provided, however*, that the filing of such a complaint will not affect the duration of:

- A. Any Part of this order that terminates in less than twenty (20) years; and
- B. This order if such complaint is filed after the order has terminated pursuant to this Part.

Analysis to Aid Public Comment

Provided further, that if such complaint is dismissed or a federal court rules that the respondent did not violate any provision of the order, and the dismissal or ruling is either not appealed or upheld on appeal, then the order will terminate according to this Part as though the complaint had never been filed, except that this order will not terminate between the date such complaint is filed and the later of the deadline for appealing such dismissal or ruling and the date such dismissal or ruling is upheld on appeal.

By the Commission.

ANALYSIS OF CONSENT ORDER TO AID PUBLIC COMMENT

The Federal Trade Commission has accepted, subject to final approval, a consent agreement from ScanScout, Inc. (“ScanScout”).

The proposed consent order has been placed on the public record for thirty (30) days for receipt of comments by interested persons. Comments received during this period will become part of the public record. After thirty (30) days, the Commission will again review the agreement and the comments received, and will decide whether it should withdraw from the agreement and take appropriate action or make final the agreement’s proposed order.

ScanScout is a video advertising network that engages in online behavioral advertising, the practice of collecting and storing information about consumers’ online activities across websites in order to deliver advertising targeted to their interests as inferred from their online activities. ScanScout acts as an intermediary between website publishers and advertisers that wish to have their video advertisements placed on websites. As a general matter, when a consumer visits a website within an online behavioral advertiser’s network of website publishers, the online advertising network sets an HTTP cookie, which is a small text

Analysis to Aid Public Comment

file, into the consumer's browser or automatically receives a cookie it has previously set in the consumer's browser. The cookie contains a unique identifier that allows the network to recognize the consumer's computer and correlate the computer to online activity across websites. The advertising network uses the cookie to collect and store information about the consumer's online activities, including content or advertisements viewed and the pages visited within a particular website.

By contrast, from at least April 2007 to September 2009, ScanScout used Flash cookies, also known as Flash local shared objects, instead of HTTP cookies to conduct online behavioral advertising. ScanScout's privacy policy stated that by changing their browser settings, consumers could opt out of receiving cookies; however, at that time, users could not use their browser settings to block the placement of Flash cookies. Accordingly, the complaint alleges that ScanScout deceived consumers and violated Section 5 of the FTC Act by stating that consumers could prevent the company from collecting data about their online activities by changing their browser settings to prevent the receipt of cookies. The Commission alleges that representations ScanScout made in its privacy policy regarding consumers' ability to opt out of receiving cookies were false or misleading.

Part I of the proposed order prohibits ScanScout¹ from misrepresenting (1) the extent to which data about users or their online activities is collected, used, disclosed, or shared and (2) the extent to which users may exercise control over the collection, use, disclosure, or sharing of data collected from or about them, their computers or devices or their online activities. Part II of the proposed order requires the company to take a number of steps to improve the transparency of, and users' ability to control, its collection of user data for online behavioral advertising. First, within thirty (30) days after service of the proposed order, ScanScout must place a clear and prominent notice with a

¹ In November 2010, ScanScout merged with Tremor Media, Inc., now known as Tremor Video, Inc. Tremor Video, Inc. is included in the definition of respondent in the order. In addition, the order includes a representation by ScanScout that any parents, subsidiaries, and successors necessary to effectuate the relief contemplated by the order are bound to the order as if they had signed the agreement and were made parties to the proceeding.

Analysis to Aid Public Comment

hyperlink on the homepage of its website that states: “We collect information about your activities on certain websites to send you targeted ads. To opt out of our targeted advertisements, click here.” The notice must direct users to a mechanism that allows them to prevent the company from (1) collecting information that can be associated with them or contains a unique identifier, (2) redirecting their browsers to third parties that collect data, absent an affirmative action, and (3) associating any previously collected data with them. Such choice must remain in effect for a minimum of five (5) years. ScanScout may, however, collect data that can be associated with a particular user or that contains a unique identifier for certain permissible uses specified in the order – for example, to effectuate the consumer’s opt out choice or to limit the number of times an advertisement is displayed.

Second, within close proximity to the mechanism, the company must disclose: (1) that it collects information about users’ activities on certain websites to deliver targeted ads; (2) that by opting out, the company will not collect this information to deliver such ads; (3) users’ current choice status (i.e., whether opted out or not opted out); and (4) any circumstances that, if initiated by the user, would disable the mechanism or require the user to implement the mechanism again to maintain his or her choice (i.e., if they switch browsers or devices, or if they delete cookies, they will have to opt out again).

Third, within or immediately adjacent to any behaviorally targeted display advertisement that the company serves, it must include a hyperlink that takes users directly to the required choice mechanism. The hyperlink text must disclose to consumers that selecting the hyperlink will give them choices about receiving targeted ads.

Fourth, due to technical limitations ScanScout cannot currently incorporate a hyperlink to the choice mechanism into all its video advertisements; therefore the order requires the company to undertake reasonable efforts to develop and implement a hyperlink for video advertisements that directs users to the choice mechanism, and the company must report regularly to the Commission regarding those efforts.

Analysis to Aid Public Comment

Parts III through VII of the proposed order are reporting and compliance provisions. Part III requires ScanScout to retain documents relating to its compliance with the order. Part IV requires dissemination of the order to all current and future principals, officers, directors, managers, employees, agents, and representatives having supervisory responsibilities relating to the subject matter of the order. Part V ensures notification to the FTC of changes in corporate status. Part VI mandates that ScanScout submit reports to the Commission detailing its compliance with the order. Part VII provides that the order expires after twenty (20) years, with certain exceptions.

The purpose of the analysis is to aid public comment on the proposed order. It is not intended to constitute an official interpretation of the proposed order or to modify its terms in any way.

INTERLOCUTORY, MODIFYING,
VACATING, AND MISCELLANEOUS
ORDERS

PHOEBE PUTNEY HEALTH SYSTEM, INC., PHOEBE
PUTNEY MEMORIAL HOSPITAL, INC., PHOEBE NORTH,
INC., HCA INC., PALMYRA PARK HOSPITAL, INC.,
AND
HOSPITAL AUTHORITY OF ALBANY-DOUGHERTY
COUNTY

Docket No. D-9348.

Order, July 15, 2011

Order granting Respondents' motion to stay the administrative proceedings under Commission Rule 3.22(a), pending the outcome of an appeal to the Eleventh Circuit in a collateral federal court action on the issue of state action immunity.

ORDER GRANTING RESPONDENTS' UNOPPOSED MOTION TO STAY
PROCEEDING

On July 1, 2011, Respondents filed an unopposed Motion to Stay the proceedings in this matter under Commission Rule 3.22(a). On July 7, 2011, the Administrative Law Judge certified that motion to the Commission. For the reasons that follow, the Commission has determined to grant the Motion.

The administrative trial in this matter is scheduled to begin on September 19, 2011. Respondents assert that "there is no benefit to undergoing the burdens and expense of continuing this administrative proceeding given" the pendency of an appeal to the Eleventh Circuit in collateral federal court litigation on the "critical issue" in this proceeding, namely state action immunity. (Motion ¶ 8.) Respondents assert that if the Eleventh Circuit were to rule in the FTC's favor, these administrative "proceedings can resume with no prejudice." (*Id.*) Complaint Counsel does not oppose Respondents' Motion.

The Commission's Rules of Practice allow the Commission to stay the administrative proceedings while a collateral federal court proceeding is ongoing upon a showing of good cause. *See* Rule

Interlocutory Orders, Etc.

3.41(f), 16 C.F.R. § 3.41(f) (“The pendency of a collateral federal court action that relates to the administrative adjudication shall not stay the proceeding unless a court of competent jurisdiction, or the Commission for good cause, so directs.”). While the Commission has a strong interest in completing Part 3 proceedings expeditiously,¹ here the Commission finds good cause to grant a stay of this proceeding. The applicability of the state action doctrine is a key issue in this proceeding and will be addressed by the Eleventh Circuit on an expedited basis. The Eleventh Circuit’s grant of an injunction pending appeal will help ensure that the status quo is preserved and the proposed acquisition is not consummated. Under these circumstances, staying these proceedings will avoid a waste of resources and will not prejudice either side.

Accordingly,

IT IS ORDERED that Respondents’ Unopposed Motion to Stay be, and it hereby is, **GRANTED**.

By the Commission, Commissioner Rosch abstaining.

¹ See Rule 3.1, 16 C.F.R. § 3.1 (“[T]he Commission’s policy is to conduct [adjudicative] proceedings expeditiously.”); Rule 3.41(b), 16 C.F.R. § 3.41(b) (“Hearings shall proceed with all reasonable expedition”); Rules of Practice Amendments, 61 Fed. Reg. 50,640 (FTC Sept. 26, 1996) (“[A]djudicative proceedings shall be conducted expeditiously and . . . litigants shall make every effort to avoid delay at each stage of a proceeding.”).

Interlocutory Orders, Etc.

UNIVERSAL COMPUTERS AND ELECTRONICS, INC.,
D/B/A APPLIANCEBESTBUYS.COM
AND D/B/A UNIVERSALLCDTV.COM

Docket No. D-9347.

Order, August 4, 2011

Order granting parties' joint motion to withdraw the matter from adjudication to enable the Commission to consider a proposed consent agreement.

ORDER WITHDRAWING MATTER FROM ADJUDICATION FOR THE
PURPOSE OF CONSIDERING A PROPOSED CONSENT AGREEMENT

Complaint Counsel and Respondents having jointly moved that this matter be withdrawn from adjudication to enable the Commission to consider a proposed Consent Agreement; and

Complaint Counsel and Respondents having submitted a proposed Consent Agreement containing a proposed Order, executed by the Respondents and by Complaint Counsel and approved by the Director of the Bureau of Consumer Protection which, if accepted by the Commission, would resolve this matter in its entirety;

IT IS ORDERED, pursuant to Rule 3.25(c) of the Commission Rules of Practice, 16 C. F.R. § 3.25(c) (2011), that this matter in its entirety be, and it hereby is, withdrawn from adjudication, and that all proceedings before the Administrative Law Judge be, and they hereby are, stayed pending a determination by the Commission with respect to the proposed Consent Agreement, pursuant to Rule 3.25(f), 16 C. F.R. § 3.25(f); and

IT IS FURTHER ORDERED, pursuant to Rule 3.25(b) of the Commission Rules of Practice, 16 C.F.R. § 3.25(b), that the proposed Consent Agreement shall not be placed on the public record unless and until it is accepted by the Commission.

By the Commission.

Interlocutory Orders, Etc.

THE NORTH CAROLINA BOARD OF DENTAL
EXAMINERS*Docket No. D-9343.**Order, August 12, 2011*

Order granting parties' joint motion to withdraw the matter from adjudication to enable the Commission to consider a proposed consent agreement.

ORDER ON RESPONDENT'S MOTION FOR EXTENSION OF TIME

Respondent North Carolina Board of Dental Examiners has filed a Motion for Extension of Time, in which it requests an additional two weeks to file its appeal brief to the Commission. Complaint Counsel do not oppose the motion so long as Complaint Counsel receives a comparable extension to file its answering brief. For the reasons described below, the Commission grants the parties an additional ten days to file their respective appeal and answering briefs.

Commission Rule 3.52(b), 16 C.F.R. § 3.52, gives parties 30 days from service of the Initial Decision to file an appeal brief to the Commission. The time periods prescribed by the Commission Rules of Practice ordinarily should afford parties to FTC proceedings sufficient time to file pleadings and briefs of sufficient quality and detail to aid in the preparation of Commission opinions and orders. Absent a Commission order granting an extension of time to the parties in this case, Respondent's appeal brief would be due on August 15, 2011.

Respondent has requested that its time to file an appeal brief be extended two weeks and for Complaint Counsel's time to file an answering brief likewise be extended an additional two weeks. Respondent seeks additional time because "Respondent's Counsel moved to new office space on July 22, 2011. . . . Respondent's Counsel and staff have necessarily been engaged in packing and unpacking activity, and as a consequence have not been able to devote the full amount of time contemplated by the FTC's rules as being adequate for the preparation of Respondent's opening appeal brief." (Motion ¶¶ 1-2.)

Interlocutory Orders, Etc.

Under these circumstances, the Commission is willing to grant Respondent additional time to prepare its appeal brief. Respondent's request for a two week extension, however, appears excessive, particularly in light of the late hour of Respondent's motion. In addition, the Commission is mindful that in any litigation involving alleged anti competitive conduct, unnecessary procedural delays may increase the risk of ongoing injury to consumers and competition. Accordingly,

IT IS ORDERED that Respondent shall file its appeal brief on or before Thursday, August 25, 2011 and that Respondent's appeal shall be deemed perfected for purposes of Rule 3.51(a), 16 C.F.R. § 3.51(a), if Respondent files its appeal brief by that date;

IT IS FURTHER ORDERED that Complaint Counsel shall file their answering brief on or before Tuesday, October 4, 2011;

IT IS FURTHER ORDERED that Respondent shall file its reply brief within seven days after service of Complaint Counsel's answering brief.

By the Commission, Commissioner Brill recused.

Interlocutory Orders, Etc.

TOPS MARKET LLC

Docket No. C-4295. Order, September 26, 2011

Order granting respondent a 90-day extension by which respondent must divest assets under the consent order.

COMMISSION LETTER EXTENDING DIVESTITURE PERIOD

Dear Mr. Morris:

This is in response to the September 13, 2011, letter you filed as Divestiture Trustee in this matter seeking an extension of the divestiture period for ninety (90) days in order to accomplish the divestiture of the supermarket identified in Schedule A of the above-referenced Order and located at 404 West Morris Street, Bath, New York. The Commission has determined to grant your request. Accordingly, the divestiture period is extended until December 27, 2011.

In granting its approval, the Commission has relied on the information you submitted and has assumed it to be accurate and complete.

By direction of the Commission.

Interlocutory Orders, Etc.

THE DOW CHEMICAL COMPANY

Docket No. C-4243. Order, September 30, 2011

Order approving respondent's request to modify lease and asset purchase agreement incorporated into the consent order.

COMMISSION LETTER MODIFYING ORDER

Dear Mr. Cary:

Pursuant to Rule 2.41(f) of the Commission's Rules of Practice and Paragraph III.G. of the Decision and Order in this matter, the Commission has determined to approve the request of The Dow Chemical Company (July 6, 2011) to modify the Torrance Tank Area Lease and the Asset Purchase Agreement (July 31, 2009) incorporated into the Decision and Order in this matter by approving the Tank Lease Amendment and the LPP Amendment. In according its approval to Dow's Petition, the Commission has relied upon the information submitted by Dow, and the Commission has assumed that information to be accurate and complete.

By direction of the Commission.

Interlocutory Orders, Etc.

CONOCO, INC. AND PHILLIPS PETROLEUM COMPANY

*Docket No. C-4058.**Order, November 14, 2011*

Order approving respondent's request to modify lease and asset purchase agreement incorporated into the consent order.

ORDER REOPENING AND MODIFYING ORDER

ConocoPhillips Company filed its "Petition of ConocoPhillips to Reopen and Modify the Decision and Order and for Approval of Amended Agreement" in this matter on June 20, 2011. ConocoPhillips is seeking the modification to allow it to change its license agreement with Holly Corp. (the acquirer of the divested Woods Cross refinery), which will extend the term of the license agreement. ConocoPhillips bases its request to reopen and modify the Order on both changed facts and public interest. For the reasons stated below, the Commission has determined to grant the Petition to reopen and modify the Order.¹

I. BACKGROUND

Conoco Inc.'s 2002 merger with Phillips Petroleum Company created ConocoPhillips. The Commission reviewed the proposed merger and concluded that it would adversely affect competition in multiple product and geographic markets. The parties agreed to divestitures and other relief to remedy those anticompetitive effects. Of concern here is the remedy in the market for the bulk supply of light petroleum products in northern Utah.²

To remedy the likely anticompetitive effects in that market, the Commission ordered ConocoPhillips to divest Phillips' refinery in Woods Cross, Utah, by August 2, 2003. As defined by the order, ConocoPhillips was required to divest the refinery,

¹ The Commission has also determined to approve the amended agreement and does so in a separate letter to ConocoPhillips from Donald Clark, Secretary, Federal Trade Commission.

² See Complaint, ¶¶ 20 *et seq.*, available at <http://www.ftc.gov/os/2002/08/conocophillipscmp.pdf>.

Interlocutory Orders, Etc.

an interest in refinery tanks, all crude pipelines connected to the refinery, a refined products pipeline, interests in nearby terminals, loading facilities, and all intellectual property, licenses, plans, agreements and joint ventures relating to the operation of the refinery. The Commission found no anticompetitive effects at the retail gasoline sales level, but to assure the viability of the refinery in the bulk supply market the Commission ordered ConocoPhillips to divest the Phillips 66 retail network that was supplied from the refinery. That included the Phillips-owned gasoline stations in Utah, Wyoming, Idaho, and Montana and all Phillips 66 supply agreements with the independent marketers that supplied the other Phillips 66 brand retailers in those four states.

So that the acquirer could continue to use the Phillips 66 brand name, the order required ConocoPhillips to license the acquirer, on an exclusive basis for ten years, the right to use in those four states all brand names owned by or licensed to Phillips and used in those states as of August 2, 2002, in connection with the sale of gasoline. This would enable the acquirer to continue to supply the stations it acquired in the divestiture as well as the independent marketers. To assure access to the brand beyond the ten years (and beyond the term of the Commission's order), the Commission also required that ConocoPhillips enter into discussion with the Commission-approved acquirer regarding the renewal of the brand licensing agreement at the end of the ninth year.

ConocoPhillips entered into an agreement to divest the required assets to Holly and to license the brand to Holly on an exclusive basis for the ten-year period required in the Order. ConocoPhillips went beyond the provisions of the order and agreed to discuss extension of the agreement at any time during the ten-year term of the license rather than only after the ninth year. Furthermore, ConocoPhillips agreed to use best efforts to negotiate the terms of a renewal for at least a five-year term.³

³ See Exhibit I, Trademark License Agreement, ¶ 7.02. Paragraph II.G. requires that in the event that the acquirer of the Woods Cross Assets ceases to use the Phillips brand in Utah, Idaho, Wyoming and Montana, ConocoPhillips retains the right to use that Phillips brand in Utah, Idaho, Wyoming, and Montana beginning two years after the acquirer ceases to use that Phillips brand in Utah, Idaho, Wyoming, and Montana. Under the Trademark License

Interlocutory Orders, Etc.

ConocoPhillips petitioned the Commission for approval of its proposed divestiture of the Woods Cross assets to Holly in January 2003. The Commission reviewed the proposed divestiture and approved it in May 2003.⁴ Holly acquired the assets on June 1, 2003. ConocoPhillips granted the ten-year exclusive license to Holly,⁵ and the license agreement complied with all other provisions of the Commission's order.⁶ The license agreement expires on June 1, 2013.⁷

Since that time, according to Holly, Holly has been successfully operating the refinery.⁸ It increased capacity at the refinery in 2008 and is in the process of constructing a pipeline from Salt Lake City to Las Vegas, which will improve its ability to supply Las Vegas from the refinery. Although Holly sold the 25 company-owned stations to independent dealers, it has continued to serve the majority of them from the Woods Cross refinery.⁹ It has also continued to serve the marketers whose contracts it acquired in the divestiture. It has devoted more resources to developing and expanding its presence in Utah and Idaho than it has in Wyoming and Montana, but it has continued to serve its customers in Wyoming and Montana. ConocoPhillips views Holly as a successful supplier.¹⁰

Beginning last year, several of the Phillips 66 retailers that Holly supplies began expressing concern to Holly about

Agreement, Phillips retains ownership of the trademarks.

⁴ See Petition at <http://www.ftc.gov/os/2003/01/conocopetition.pdf> (hereinafter "Petition"); see Press Release, May 23, 2003, at <http://www.ftc.gov/opa/2003/05/fyi0334.shtm>.

⁵ See Exhibit I, Trademark License Agreement, ¶¶ 2.01 and 7.01 and Exhibit L, Branded Ancillary Products Purchase Agreement, ¶ 6.

⁶ See Exhibit I, Trademark License Agreement Opening Paragraph.

⁷ The Order terminates February 13, 2013.

⁸ See Declaration of Gregory A. White, Vice President, Holly Refining & Marketing Company LLC (hereinafter "Holly Declaration"), ¶ 4.

⁹ Holly Declaration, ¶ 3.

¹⁰ Petition at 4; Holly Declaration, ¶ 5.

Interlocutory Orders, Etc.

post-2013 supply. Holly, thus, sought to negotiate an extension to its license agreement with ConocoPhillips as early as possible. Consistent with the order and the license agreement, ConocoPhillips entered into negotiations with Holly in 2009 to extend the terms of the license agreement. These negotiations led to a signed letter of intent in July 2010 and an executed license extension in February 2011.

The new agreement will extend the license to Holly for an additional seven years in the four states beginning when the current license expires in June 2013, on a non-exclusive basis, with a mutual option to extend for an additional five years. In return for the extension now in the four-state area, Holly agreed to modify the divestiture agreement to give up exclusivity in Wyoming and Montana as soon as the Commission approves the modification, rather than retaining it until June 2013 as required by the Order. ConocoPhillips agreed not to attempt to rebrand any of the retailers currently served by Holly in those two states until June 2013, but ConocoPhillips will obtain the right to brand any other retailers in those two states as soon as the agreement is effective. Holly will retain exclusivity in Utah and Idaho until June 2013 as required by the Order. Because the elimination of exclusivity in Wyoming and Montana prior to June 2013 would be inconsistent with the Commission's Order, ConocoPhillips has requested that the Commission reopen and modify the order to allow the modification.

II. CONOCOPHILLIPS' PETITION

Paragraph II.C.1.a. of the Order requires ConocoPhillips to grant a ten-year exclusive license for use in the four states, and ConocoPhillips is now in compliance with that obligation. A modification to the license agreement that eliminates exclusivity in Wyoming and Montana prior to the end of the ten-year period in June 2013 would be inconsistent with the Commission's Order.

ConocoPhillips, thus, proposes adding the following proviso to Paragraph II.C.2. of the Commission's order:

Provided, however, that Respondents and the acquirer may agree, prior to the end of the ninth year and subject to the

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Commission's prior approval, to modify the terms of the agreement entered pursuant to Paragraph II.C.I. in order to provide a nonexclusive license in Montana and Wyoming for the remainder of the ten-year period, notwithstanding the provisions of Paragraphs II.C.I. and II.G, as long as the modification is consistent with the purpose of the Order.

With the above modification to the Commission's Order, ConocoPhillips asserts that the proposed amendment to the license will not violate the Order.

ConocoPhillips maintains that the proposed amendment and modification will be pro-competitive, will not adversely affect the refinery's viability, and will thus serve the public interest. Holly will continue to supply exclusively in Idaho and Utah through June 2013. Although Holly will give up exclusivity immediately in Wyoming and Montana, ConocoPhillips will agree not to compete for the stations Holly currently supplies in those two states through the initial contract period. Thus, Holly will continue to supply all the stations it currently supplies, maintaining the same level of service as it currently has with no impact on its viability. On the other hand, ConocoPhillips could begin competing in Wyoming and Montana immediately, thereby injecting additional competition into those states.

In addition, ConocoPhillips asserts that changed facts and circumstances require approval of the modification and amended agreement and that approval will further the purposes of the order.

After operating in the market for over eight years, Holly has determined that exclusivity in Wyoming and Montana is not necessary to maintain viable operations at the refinery. Extending the license agreement for up to 12 additional years now, however, will enable Holly to give its retailers and marketers the assurances they are seeking and further enhance the refinery's viability. Enhancing the refinery's viability will further the objectives of the Commission's order.

ConocoPhillips filed its Petition on June 20, 2011. It was available for public comment for thirty days until July 27, 2011. No public comments were filed.

Interlocutory Orders, Etc.

III. STANDARD FOR REOPENING AND MODIFYING A FINAL ORDER

A final order may be reopened and modified on the grounds set forth in § 5(b) of the Federal Trade Commission Act, 15 U.S.C. § 45(b). First, Section 5(b) provides that the Commission shall reopen an order to consider whether it should be modified if the respondent “makes a satisfactory showing that changed conditions of law or fact” so require.¹¹ A satisfactory showing sufficient to require reopening is made when a request to reopen identifies significant changes in circumstances and shows that the changes eliminate the need for the order or make continued application of it inequitable or harmful to competition.¹² The Commission’s Rule 2.51(b) requires such “satisfactory showing” to include affidavits setting forth admissible facts.¹³

Second, Section 5(b) provides that the Commission may also reopen and modify an order when, although changed circumstances would not require reopening, the Commission determines that the public interest so requires. Respondents are therefore invited in petitions to reopen to show how the public interest warrants the requested modification.¹⁴ In the case of “public interest” requests, Rule 2.51(b) requires an initial “satisfactory showing” of how modification would serve the public interest before the Commission determines whether to reopen an order and consider all of the reasons for and against its modification.

¹¹ See also *Supplementary Information*, Amendment to the Commission’s Rules of Practice § 2.51(b), 16 C.F.R. 2.51(b) (August 15, 2001).

¹² S. Rep. No. 96-500, 96th Cong., 2d Sess. 9 (1979) (significant changes or changes causing unfair disadvantage); *Louisiana-Pacific Corp.*, Docket No. C-2956, Letter to John C. Hart (June 5, 1986), at 4 (unpublished) (“Hart Letter”). See also *United States v. Louisiana-Pacific Corp.*, 967 F.2d 1372, 1376-77 (9th Cir. 1992) (“A decision to reopen does not necessarily entail a decision to modify the Order. Reopening may occur even where the petition itself does not plead facts requiring modification.”).

¹³ 16 C.F.R. § 2.51(b).

¹⁴ Hart Letter at 5; 16 C.F.R. § 2.51.

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A “satisfactory showing” requires, with respect to public interest requests, that the requester make a *prima facie* showing of a legitimate public interest reason or reasons justifying relief. A request to reopen and modify will not contain a “satisfactory showing” if it is merely conclusory or otherwise fails to set forth by affidavit(s) specific facts demonstrating in detail the reasons why the public interest would be served by the modification.¹⁵ This showing requires the requester to demonstrate, for example, that there is a more effective or efficient way of achieving the purposes of the order, that the order in whole or part is no longer needed, or that there is some other clear public interest that would be served if the Commission were to grant the requested relief. Just as for petitions based on changed conditions, this showing must be supported by evidence that is credible and reliable.

If, after determining that the requester has made the required showing, the Commission decides to reopen the order, the Commission will then consider and balance all of the reasons for and against modification. In no instance does a decision to reopen an order oblige the Commission to modify it,¹⁶ and the burden remains on the requester in all cases to demonstrate why the order should be reopened and modified. The petitioner's burden is not a light one in view of the public interest in repose and the finality of the Commission's orders.¹⁷ All information and material that the requester wishes the Commission to consider shall be contained in the request at the time of filing.¹⁸

IV. THE ORDER WILL BE REOPENED AND MODIFIED

The Commission has determined to reopen and modify the Order as requested by ConocoPhillips. Reopening the Order to eliminate the exclusive licensing requirement in the manner that ConocoPhillips proposes will relieve ConocoPhillips of a specific

¹⁵ 16 C.F.R. § 2.51.

¹⁶ See *United States v. Louisiana-Pacific Corp.*, 967 F.2d 1372, 1376-77 (9th Cir. 1992) (reopening and modification are independent determinations).

¹⁷ See *Federated Department Stores, Inc. v. Moitie*, 425 U.S. 394 (1981) (strong public interest considerations support repose and finality).

¹⁸ 16 C.F.R. § 2.51(b).

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obligation in the Commission's Order; the Commission must thus determine whether reopening the Order is warranted. In this case, it is clear that elimination of the requirement in the manner proposed by ConocoPhillips will not affect the viability of Holly's refinery operations and thus the effectiveness of the Commission's remedy, but it will instead have two immediate procompetitive consequences.

First, it will inject immediate competition into Wyoming and Montana without jeopardizing Holly's operations. And, second, and perhaps more important, in exchange for the immediate elimination of exclusivity in these two states, ConocoPhillips has agreed to provide Holly additional rights by extending the brand licensing agreement in the entire four-state area for up to 12 more years. This will enable Holly to assure its customers now of post-2013 supply, further enhancing Holly's viability and further benefitting competition. The resulting benefits to competition justify reopening the Order and modifying it to eliminate that obligation now.

The Order was premised on the Complaint's allegation that the merger of Conoco and Phillips would be unlawful in the bulk supply of light petroleum products in Northern Utah.¹⁹ As the Order explicitly states:

The purpose of this Paragraph is to ensure that the Phillips Woods Cross Assets remain in the market and to remedy the lessening of competition in the refining, terminaling and bulk supply of Motor Fuels and other petroleum products resulting from the proposed Merger as alleged in the Commission's Complaint. A further purpose of this Paragraph is to ensure that the acquirer of the Phillips Woods Cross Assets has the same capabilities and incentives as did Phillips prior to the Merger to expand and develop alternative sources of Motor Fuels and other light petroleum products for the Northern Utah market as alleged in the Commission's Complaint and is able to take control of the assets and, with minimal additional

¹⁹ The Complaint alleges: "After the Merger, the combined firm could effectively coordinate to reduce supply, slow growth of supply, and raise prices in the market for LPP bulk supply in Northern Utah." Complaint, ¶ 30.

Interlocutory Orders, Etc.

investment, compete as aggressively as did Phillips prior to the Merger.²⁰

To remedy the anticompetitive effects alleged in the Complaint, the Commission ordered divestiture of the refinery supplying the relevant geographic market. But to assure the viability of the refinery and to enable the acquirer to “compete as aggressively as” Phillips had prior to the merger, the Commission also ordered divestiture of the marketing assets supplied from the refinery and a ten-year exclusive brand license covering the four-state area supplied from the refinery.

Eight years later, it is clear that the Order has achieved its remedial objectives in this regard. Divestiture of the refinery to Holly was intended to replace the competition lost in the bulk supply of light petroleum products in Northern Utah as a result of the merger of Conoco and Phillips, and it did so. Divestiture of the marketing assets and the four-state ten-year exclusive license was intended to enhance the viability of the refinery to assure effective relief in that market, and it did so as well. The inclusion of the marketing assets and the exclusive license in all four states has served its purpose. Holly has effectively operated the refinery for eight years and has now determined that continued exclusivity in Montana and Wyoming is not necessary for viable operations of the refinery. The proposed agreement, although eliminating exclusivity in Montana and Wyoming immediately, will preserve Holly’s footprint there by prohibiting ConocoPhillips from competing for the stations that Holly currently serves in those two states through June 2013. On the other hand, by eliminating Holly’s exclusivity in Montana and Wyoming now, the modification will enable ConocoPhillips to compete for additional marketers in those two states thereby injecting additional competition immediately without jeopardizing the effectiveness of the remedy.

In addition, ConocoPhillips has agreed to extend the license agreement throughout the entire four-state area for up to 12 years if Holly agrees to the elimination of exclusivity in Montana and

²⁰ Order, ¶ I.I.M.

Interlocutory Orders, Etc.

Wyoming immediately and if the Commission reopens and modifies the Order to allow the change. Thus, by reopening and modifying the Order as ConocoPhillips requests, the Commission will facilitate the valuable benefit that Holly will obtain by being able to assure the retailers and marketers that it presently serves in the four-state area that it will be able to supply them for up to another 12 years. The assurance now that Holly will remain a viable supplier in this market will enhance its competitiveness and thus assure the effectiveness of the Commission's remedy.²¹

Accordingly, the Petition satisfies the standard for reopening and modifying the Order under the "public interest" provision of Rule 2.51(b) of the FTC Rules of Practice and Section 5 of the FTC Act. ConocoPhillips has established that reopening the Order is in the public interest in light of the pro-competitive benefits that will be obtained. ConocoPhillips has also shown that the Order should be modified as it proposes by demonstrating

²¹ Reopening and modifying this Order is consistent with the Commission's action in Solvay S.A., Docket No. C-4046, Order Reopening and Modifying Order at: <http://www.ftc.gov/opa/2003/04/solvayord.pdf>, in which the Commission reopened the final hold separate order and eliminated a two-year ban on hiring a named employee, finding that the Hold Separate Order had been effective in facilitating the acquirer's efforts to retain necessary employees. Based on those facts, the Commission concluded:

In determining whether to modify the Hold Separate Order, the Commission must consider and balance all the reasons for and against the modification. Although the Hold Separate Order's two year ban on Solvay employing the Solvay Fluoropolymers Business promoted the important goal of encouraging the employees of the divested business to accept employment with Dyneon, its decision not to hire Mr. Mularski renders the employment ban obsolete and unnecessary. The employment ban now imposes an unintended harm to Mr. Mularski's personal financial and employment interests because the employment ban prevents Solvay from hiring Mr. Mularski. In balancing and weighing the reasons for and against modifying the Hold Separate Order, it appears that Mr. Mularski will suffer personal harm if the Hold Separate Order is not modified, but that declining to modify the Hold Separate Order will not promote any competitive or public purpose.

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that the modification will have no impact on Holly's viability but will instead inject additional competition into the market.²²

Accordingly,

IT IS ORDERED that the Order in Docket No. C-4058 be, and it hereby is, reopened; and

IT IS FURTHER ORDERED that the Order be, and it hereby is, modified by making the following changes to Paragraph II.C. 2.:

(Deletions noted with strike through and new text bold and underlined)

~~at~~ **on or before** the end of the ninth year after the Effective Date of Divestiture of the Phillips Woods Cross Assets, Respondents shall offer to meet with the acquirer to discuss a renewal of the agreement;

and by adding the following proviso to Paragraph II.C.2.:

Provided, however, that Respondents and the acquirer may agree, prior to the end of the ninth year and subject to the Commission's prior approval, to modify the terms of the agreement entered pursuant to Paragraph II.C.I. in order to provide a nonexclusive license in Montana and Wyoming for the remainder of the ten-year period, notwithstanding the provisions of Paragraphs II.C.I. and II.G, as long as the modification is consistent with the purpose of the Order.

By the Commission.

²² Having determined that ConocoPhillips' Petition satisfies the public interest test, the Commission need not consider whether the Petition has made a satisfactory showing of changed conditions of fact.

Interlocutory Orders, Etc.

CONOCO, INC. AND PHILLIPS PETROLEUM COMPANY

Docket No. C-4058. Order, November 14, 2011

Order approving respondent's amended agreement.

COMMISSION LETTER APPROVING AMENDED AGREEMENT

Dear Mr. Cary and Mr. Byrne:

This letter responds to the Petition of ConocoPhillips To Reopen and Modify the Decision and Order and for Approval of Amended Agreement filed by ConocoPhillips Company on June 20, 2011. The Petition was placed on the public record for comments until July 27, 2011, and no comments were received.

In its Order Modifying Order, issued on November 14, 2011, the Commission has determined to reopen the Order in this matter and modify it as requested by ConocoPhillips. ConocoPhillips has also requested that, pursuant to Section 2.41 of the Federal Trade Commission's Rules of Practice and Procedure, 16 C.F.R. § 2.41(2011), the Commission approve the Amended Agreement described in the Petition.

After consideration of the Amended Agreement as set forth in the Petition and supplemental documents, as well as other available information, and consistent with the Order as modified by the Order Modifying Order, the Commission has determined to approve the Amended Agreement. In according its approval, the Commission has relied upon the information submitted and representations made in connection with ConocoPhillips' Petition, and has assumed them to be accurate and complete.

By direction of the Commission.

Interlocutory Orders, Etc.

BASF SE

*Docket No. C-4253.**Order, November 15, 2011*

Commission letter approving the modification of the toll manufacturing agreement, which is incorporated into the the divestiture agreement required pursuant to the Commission's order.

COMMISSION LETTER APPROVING MODIFIED AGREEMENT

Dear Mr. Schlossberg:

This is in reference to the "Petition of BASF SE for Approval of IB Toll Manufacturing Agreement Extension" ("Petition"), dated September 20, 2011, and filed by BASF SE ("BASF"). Pursuant to the Decision and Order in the above matter, BASF requests approval of a proposed change in the toll manufacturing agreement, a document that is part of the divestiture agreement included in the Decision and Order.

After consideration of BASF's Petition and other available information, the Commission has determined to approve the proposed change as set forth in BASF's Petition. In according its approval, the Commission has relied upon the information submitted and the representations made in connection with BASF's Petition and has assumed them to be accurate and complete.

By direction of the Commission.

Interlocutory Orders, Etc.

TOPS MARKET LLC

Docket No. C-4295. Order, December 9, 2011

Order granting respondent a second 90-day extension by which respondent must divest assets under the consent order.

COMMISSION LETTER EXTENDING DIVESTITURE PERIOD

Dear Mr. Morris:

This is in response to the November 23, 2011, letter you filed as Divestiture Trustee in this matter seeking an extension of the divestiture period for ninety (90) days in order to accomplish the divestiture of the supermarket identified in Schedule A of the above-referenced Order and located at 404 West Morris Street, Bath, New York. The Commission has determined to grant your request. Accordingly, the divestiture period is extended until March 26, 2012.

In granting its approval, the Commission has relied on the information you submitted and has assumed it to be accurate and complete.

By direction of the Commission.

Interlocutory Orders, Etc.

UNIVERSAL HEALTH SERVICES, INC.

*Docket No. C-4309.**Order, December 27, 2011*

Commission letter approving the divestiture of assets in Las Vegas, Nevada, by Universal Health Services to Strategic Behavioral Health, LLC.

COMMISSION LETTER APPROVING DIVESTITURE

Dear Mr. Barbur and Mr. Belelieu:

This letter responds to the Application for Approval of Divestiture of the Las Vegas Divestiture Assets filed by Universal Health Services, Inc., on November 7, 2011. The Application requests that the Commission approve, pursuant to the order in this matter, Universal's proposed divestiture of the Las Vegas Divestiture Assets to Strategic Behavioral Health, LLC. The application was placed on the public record for comments until December 12, 2011, and no comments were received.

After consideration of the proposed divestiture as set forth in Universal's Application and supplemental documents, as well as other available information, the Commission has determined to approve the proposed divestiture. In according its approval, the Commission has relied upon the information submitted and representations made in connection with Universal's Application and has assumed them to be accurate and complete.

By direction of the Commission.

Interlocutory Orders, Etc.

UNIVERSAL HEALTH SERVICES, INC.

Docket No. C-4309.

Order, December 27, 2011

Commission letter denying Respondent's request to extend the time to divest its Las Vegas assets to a Commission-approved acquirer because the Respondent failed to demonstrate either that its efforts to divest the assets or its efforts to resolve staff concerns were sufficient to warrant an extension.

COMMISSION LETTER DENYING MOTION FOR EXTENSION OF TIME
TO DIVEST LAS VEGAS DIVESTITURE ASSETS

Dear Messrs. Barbur and Belelieu:

This letter responds to Universal Health Services, Inc.'s Motion For Extension of Time to Divest the Las Vegas Divestiture Assets ("Motion"), filed by you on behalf of Respondents Alan B. Miller and Universal Health Services, Inc., *et al.* (collectively, "Universal" or "Respondents") in the above-captioned matter on October 3, 2011. In its Motion, Universal seeks an extension of time to divest until March 31, 2012. Under the terms of the Decision and Order ("Order") issued in this matter, which were agreed to by Respondents, Universal is required to divest the Las Vegas Divestiture Assets no later than six months after the date the Order became final, *i.e.*, by October 31, 2011, to an acquirer that receives the Commission's prior approval, and in a manner that also receives the Commission's prior approval. Universal has failed to complete the required divestiture within the Order's deadline. For the reasons discussed below, Universal has not met its burden under the Commission's Rules and the applicable legal standards for showing good cause why its Motion should be granted. Accordingly, the Commission has denied the Motion.

In reaching its decision, the Commission has reviewed Universal's Motion and other available information, including that provided by Universal in its periodic reports of compliance, its applications seeking prior approval of proposed divestitures and in supplemental submissions. The Commission has also reviewed Universal's efforts to divest the Las Vegas Divestiture Assets as required by the terms of the Order.

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The Order, which became final on April 29, 2011,¹ was issued to resolve competitive concerns arising from Universal's acquisition of Psychiatric Solutions, Inc., which combined two of the largest providers of acute inpatient psychiatric services in three relevant geographic markets: the Las Vegas, Nevada, Metropolitan Statistical Area; the State of Delaware; and the Commonwealth of Puerto Rico. The Order requires Universal to divest the Divestiture Assets, as defined,² within specified time periods,³ in each of the Relevant Areas, as defined:⁴ the State of Delaware; the Las Vegas, NV, MSA; and the Commonwealth of Puerto Rico. In particular, Paragraph III.A. of the Order requires Universal to divest the Las Vegas Divestiture Assets, as defined,⁵ "[n]o later than six (6) months after the date [the] Order becomes final" (*i.e.*, by October 31, 2011), only to an acquirer that receives the prior approval of the Commission, and only in a manner that receives the prior approval of the Commission.⁶ Paragraph VIII.A. of the Order provides that the Commission may appoint a trustee ("Divestiture Trustee") to, among other things, divest the Las Vegas Divestiture Assets if Respondents have not fully complied with the obligations imposed by Paragraph III. of the Order.

On May 20, 2011, Universal filed an application ("May 20th application") seeking the Commission's prior approval to divest the Las Vegas Divestiture Assets to Signature Healthcare

¹ On November 15, 2010, the Commission accepted an Agreement Containing Consent Orders in this matter for public comment. The Commission subsequently issued a modified final Decision and Order (*i.e.*, the Order) on April 19, 2011, which became final on April 29, 2011.

² Order ¶ I.O.

³ Order ¶¶ IIA., III.A., IV.A.

⁴ Order ¶ I.DD.

⁵ Order ¶¶ I.T., V., CC.

⁶ Pursuant to a consent settlement with the State of Nevada, Universal must comply with essentially identical divestiture obligations according to the terms of a Final Judgment, filed on November 15, 2010, by the Attorney General for the State of Nevada ("Nevada Attorney General"), in the United States District Court for the District of Nevada.

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Services, LLC (“Signature”), an entity wholly owned by Dr. Soon Kim. As described below, the Commission’s staff engaged in detailed discussions with Universal and with Signature concerning the proposed divestiture to Signature, and conducted an extensive review of Signature as a “Prospective Acquirer,” as defined,⁷ of the Las Vegas Divestiture Assets. On September 15, 2011, Universal filed a Notice of Withdrawal of the May 20th application.

In its Motion, Universal requests that the Commission extend the time for divestiture until March 31, 2012, pursuant to Section 4.3(b) of the Commission’s Rules of Practice and Procedure, 16 C.F.R. § 4.3(b). Commission Rule 4.3(b) provides that “the Commission, for good cause shown, may extend any time limit prescribed by the rules in this chapter or order of the Commission.” Under applicable precedent, Universal has the burden of demonstrating good cause, and granting an extension of time rests in the discretion of the Commission.⁸ As the Commission’s publicly-available guidance makes clear, failure to consummate a required divestiture within the time limit set by the Order (*i.e.*, not just file for approval) is a violation of the Order and can result in liability for civil penalties and other relief pursuant to Section 5(l) of the Federal Trade Commission Act.⁹ The Commission has consistently held respondents to a high standard when considering granting an extension of time to divest because, by granting such a request, the Commission would forgo its ability to seek civil penalties or other relief for the period of the extension. Good cause to extend the Order’s deadline could include a persuasive showing of extraordinary or unforeseen circumstances not reasonably within a respondent’s control that prevented the timely completion of the divestiture, or a showing of some harm that would result from denial of the motion. Conversely, indications of a respondent’s lack of diligent efforts to complete a Commission-ordered divestiture as expeditiously as

⁷ Order ¶ I.X.

⁸ *United States v. Swingline, Inc.*, 371 F. Supp. 37, 45 (E.D.N.Y. 1974).

⁹ 15 U.S.C. § 45(l) *See* Statement of the Federal Trade Commission’s Bureau of Competition on Negotiating Merger Remedies, at n.30 and accompanying text, <http://www.ftc.gov/bc/bestpractices/bestpractices030401.htm>.

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possible could negate assertions of good cause to extend the divestiture deadline.¹⁰

Universal states in its Motion that it has worked diligently to divest the Divestiture Assets, and points to its timely divestiture of the Delaware Divestiture Assets,¹¹ and substantial progress toward a timely divestiture of the Puerto Rico Divestiture Assets,¹² as factors the Commission should take into account in assessing its requested extension of time to divest the Las Vegas Divestiture Assets. Universal's compliance with its obligations regarding the Delaware Divestiture Assets and its compliance efforts regarding the Puerto Rico Divestiture Assets are an indication of Universal's diligence and efforts to comply with the Order's requirements, but do not excuse Universal's failure to have *fully* complied by completing the required divestiture of the Las Vegas Divestiture Assets on time. The Commission has never found partial compliance with an Order's requirements alone to constitute sufficient good cause for extending the time to divest. Universal expressly represented to the Commission in settling this matter that it could accomplish the full relief contemplated by the Order,¹³ and is presumed to have understood the obligations it undertook when it signed the consent agreement.

The circumstances surrounding Universal's failure to divest the Las Vegas Divestiture Assets on time were neither

¹⁰ See, e.g., Letter re: *In the Matter of Service Corporation International, Inc., et al.*, Docket No. C-4174 (April 25, 2008), <http://www.ftc.gov/os/caselist/0610156/080501letter.pdf>.

¹¹ Universal was required to divest the Delaware Divestiture Assets by October 31, 2011 (Order ¶ II.A.). It filed an application for approval to divest to PHC, Inc., which was approved by the Commission on June 3, 2011. The divestiture closed on July 1, 2011.

¹² Universal is required to divest the Puerto Rico Divestiture Assets by January 30, 2012 (Order ¶ IV.A.). It filed an application for approval to divest the assets to United Medical Corporation and related individuals and entities on September 28, 2011. Commission action on the application is pending.

¹³ Paragraph 13 of the Agreement Containing Consent Orders executed in this matter by Respondents states that, “[b]y signing this Consent Agreement, Proposed Respondents represent and warrant that they can accomplish the full relief contemplated by the attached Decision and Order (including effectuating all required divestitures, assignments, and transfers).”

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extraordinary nor unforeseen so as to constitute sufficient “good cause” under Commission Rule 4.3(b) to justify extending the time to divest. In late March 2011, before Universal filed the May 20th application seeking Commission approval of Signature to acquire the Las Vegas Divestiture Assets, the Commission’s staff, working in coordination with staff of the Office of the Nevada Attorney General (“NV-AG staff”), notified Universal that, based on publicly-available information, Signature already had plans to enter the relevant Las Vegas, NV, MSA market as a provider of acute inpatient psychiatric services. Staff explained its view that divestiture to Signature, with its apparent imminent plans to enter at a substantial scale, would fail to achieve the remedial deconcentrating effect and purpose of the Order’s divestiture requirement in the relevant market. Universal disagreed with staff’s assessment and filed the May 20th application.

The Commission’s staff and NV-AG staff then conducted a coordinated, in-depth review of Signature as a Prospective Acquirer of the Las Vegas Divestiture Assets. This included review of confidential documents and information submitted by Signature pursuant to compulsory process issued by the Office of the Nevada Attorney General, interviews with third parties, and numerous conversations with representatives of Signature and Universal. Throughout its review, staff regularly and repeatedly informed Universal (and Signature) that, based on information it was receiving, staff continued to have serious concerns about Signature as a committed entrant into the Las Vegas area. Nonetheless, both Universal and Signature persisted in presenting arguments that Signature should still be considered an acceptable acquirer of the Las Vegas Divestiture Assets.¹⁴ Finally, the Commission’s staff and NV-AG staff determined that further review would likely yield no new information that would resolve or eliminate staff’s concerns. In view of the rapidly-approaching divestiture deadline, the Commission’s staff (along with NV-AG staff) informed Universal on August 22, 2011, that staff was prepared to recommend that the Commission deny Universal’s application for approval of its proposed divestiture to Signature. Universal subsequently withdrew its May 20th application on

¹⁴ See Motion at ¶ 9.

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September 15, 2011. Although it immediately began the process to find another candidate to acquire the Las Vegas Divestiture Assets, and filed an application for approval of its proposed divestiture to a new Prospective Acquirer on November 7, 2011,¹⁵ Universal failed to satisfy its obligation to divest the Las Vegas Divestiture Assets by October 31, 2011, as required by the Order.

Based on the foregoing, Universal has not demonstrated that its divestiture efforts prior to the Order's divestiture deadline were sufficient to justify the relief requested. Nor has Universal identified any harm, such as harm to the public, if the Commission denies the Motion.¹⁶ Although Universal was free to continue to urge staff to support its proposed divestiture to Signature, Universal must accept the risk that prolonged discussion, especially in light of the staff's repeated expressions of concern about the proposal that were never resolved by Universal, would adversely affect Universal's ability to complete the divestiture by the Order's deadline. Accordingly, the Commission has determined to deny Universal's Motion.¹⁷

Failure to complete a divestiture by the Order's deadline is a violation of the Order and creates the potential liability for civil penalties and other relief pursuant to Section 5(l) of the FTC Act.¹⁸ As provided in Paragraph VIII. of the Order, neither the appointment of a Divestiture Trustee nor a decision by the Commission not to appoint a Divestiture Trustee relieves Respondents of their potential liability for civil penalties. In

¹⁵ On November 7, 2011, Universal filed an application seeking Commission approval for divestiture of the Las Vegas Divestiture Assets to Strategic Behavioral Health, LLC and related entities.

¹⁶ The requirements of the Order to Hold Separate and Maintain Assets, and the oversight of the Hold Separate Trustee appointed by the Commission, will help assure the continued viability, competitiveness and marketability of the Divestiture Assets pending divestiture. They are not substitutes, however, for a timely divestiture, which remains the core remedy in this Order.

¹⁷ In reaching its decision, the Commission, through staff, worked in close coordination with the Office of the Nevada Attorney General. The Commission's decision does not, however, bind or necessarily represent the views of the State of Nevada.

¹⁸ 15 U.S.C. § 45(l).

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denying Universal's Motion, however, the Commission has made no determination to seek a trustee to accomplish the divestiture of the Las Vegas Divestiture Assets at this time, nor has it made a determination to seek civil penalties or other relief for Universal's failure to comply with this divestiture obligation in a timely fashion. Although Universal has not shown that its efforts prior to the divestiture deadline were sufficient to justify the requested time extension, its substantial progress toward proposing a new Prospective Acquirer weighs in favor of allowing Universal to continue the process already underway rather than risk further delay by introducing a Divestiture Trustee at this juncture. The Commission will closely monitor Universal's efforts to complete the process of divesting the Las Vegas Divestiture Assets as expeditiously as possible, consistent with its Order obligations.

The Commission reserves the right to appoint a Divestiture Trustee or take such further action as circumstances warrant.

By direction of the Commission.

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