

Complaint

IN THE MATTER OF

**READING HEALTH SYSTEM  
AND  
SURGICAL INSTITUTE OF READING**COMPLAINT AND ORDER IN REGARD TO ALLEGED VIOLATIONS OF  
SECTION 5 OF THE FEDERAL TRADE COMMISSION ACT AND  
SECTION 7 OF THE CLAYTON ACT*Docket No. 9353; File No. 121 0155**Complaint, November 16, 2012 – Decision, December 7, 2012*

This case addresses the \$43 million acquisition by Reading Health System of Surgical Institute of Reading. The complaint alleges that the acquisition, if consummated, would violate Section 5 of the Federal Trade Commission Act and Section 7 of the Clayton Act by significantly reducing competition in the markets for inpatient orthopedic/spine surgery; outpatient orthopedic/spine surgery; outpatient general surgery; and outpatient ear, nose, and throat (“ENT”) surgery in the Reading, Pennsylvania area. The order dismisses the Administrative Complaint without prejudice because Respondents abandoned the proposed acquisition and the Commission is not reaching a decision on the merits.

*Participants*

For the *Commission*: Maggie DiMoscato, Janelle Filson, Kevin Hahm, Douglas Litvack, Jeremy Morrison, Paul Nolan, Sean Pugh and Stephanie Reynolds.

For the *Respondents*: Joanne M. Judge, Neil Schur, and Joseph Wolfson, Stevens & Lee; Jeffrey Brennan, McDermott, Will & Emery.

**COMPLAINT**

Pursuant to the provisions of the Federal Trade Commission Act, and by virtue of the authority vested in it by the Act, the Federal Trade Commission (“Commission”), having reason to believe that Respondents Reading Health System (“RHS”) and Surgical Institute of Reading (“SIR”), having executed an asset purchase agreement in violation of Section 5 of the Federal Trade Commission Act (“FTC Act”), 15 U.S.C. § 45, and which if consummated would violate Section 7 of the Clayton Act, as

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amended, 15 U.S.C. § 18, and it appearing to the Commission that a proceeding by it in respect thereof would be in the public interest, hereby issues its complaint pursuant to Section 11(b) of the Clayton Act, 15 U.S.C. § 21(b), and Section 5(b) of the Federal Trade Commission Act, 15 U.S.C. § 45(b), stating its charges as follows:

### I.

#### **NATURE OF THE CASE**

1. RHS's acquisition of SIR (the "Acquisition") will substantially lessen competition for critical surgical services in the Reading, Pennsylvania area, leading to increased healthcare costs for local residents and reduced quality of care. SIR, a surgical specialty hospital, opened in 2007 and immediately challenged RHS's dominance in the Reading area. Specifically, by offering lower rates to health plans and higher quality to patients and physicians, SIR has drawn away significant volumes of commercially-insured patients in important surgical service lines from RHS. For its part, RHS did not take this new competitive threat lying down; it chose to compete head-to-head with SIR by offering to lower its rates and aggressively seeking to improve its quality to attract patients back to its facilities from SIR. As evidenced by their competitive interactions, SIR considered RHS to be its "primary competitor" and RHS, in turn, described SIR as its "nemesis." Not surprisingly, then, in high-level, internal communications, RHS described the Acquisition as a "defensive and offensive" strategy designed to "protect the hospital's market share." If the Acquisition proceeds, these benefits of the head-to-head competition between RHS and SIR described above – lower costs and quality improvements – will vanish.

2. One of RHS's principal motivations in acquiring SIR is to protect its market share. Ordinary-course-of-business documents reveal that RHS was concerned by "notable losses in surgical volumes" to SIR. Executives were alarmed that market shares in key surgical service lines were "not a pretty picture with SIR in the mix" and that patients were "choosing to go to SIR" over RHS. RHS responded vigorously to SIR's competitive threat by offering reimbursement rate discounts to health plans in exchange for the plans' agreement to exclude SIR from their provider

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networks. It also planned to “improve [its] services so that patients will want to come to [RHS]” instead of SIR. This competitive rivalry – which would be eliminated by the Acquisition – has produced substantial benefits for local employers and patients in Reading.

3. Notably, most health plans declined RHS’s discount offers, which were contingent on excluding SIR from their provider networks. SIR contracted with health plans at significantly lower rates than RHS and successfully attracted patients from RHS because of its lower prices, high quality, and convenience. Rate increases impose a significant burden on local employers and employees, either directly or indirectly through higher health insurance premiums, co-pays, and other out-of-pocket healthcare expenses. Higher costs, in turn, force employers to reduce or eliminate health insurance coverage for their employees, or take other cost-cutting measures, such as reducing wages. These effects are not purely financial; increases in already-high healthcare costs ultimately force individuals to drop their health insurance, and even those that maintain insurance may delay or forgo medical care that they cannot afford.

4. The Acquisition threatens competitive harm in four relevant markets where RHS and SIR compete to offer services to commercially-insured patients: (1) inpatient orthopedic surgical services; (2) outpatient orthopedic surgical services; (3) outpatient ear, nose, and throat (“ENT”) surgical services; and (4) outpatient general surgical services. The relevant geographic market in which to analyze the effects of the Acquisition for each relevant service market is the area corresponding to Reading Hospital’s primary service area.

5. The Acquisition reduces the number of significant competitors from three to two – a virtual duopoly – for the inpatient orthopedic surgical services market, with St. Joseph Medical Center (“St. Joseph”) as the only other meaningful competitor in the Reading area. The markets for outpatient general surgical services and outpatient ENT surgical services would each also be left with only one other significant competitor. In the fourth relevant market, outpatient orthopedic surgical services, the Acquisition reduces the number of significant competitors from four to three.

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6. The Acquisition is presumptively unlawful in each of the four affected markets under the relevant case law and the U.S. Department of Justice and Federal Trade Commission Horizontal Merger Guidelines (“Merger Guidelines”). Post-Acquisition market shares in each of the four relevant markets are extraordinarily high, ranging from 49 percent to 71 percent, with correspondingly high concentration levels.

7. Health plans with members in the Reading area believe that the Acquisition will increase RHS’s already immense bargaining leverage, subjecting their members to higher rates. For some health plans, an increase in SIR’s rates to those of RHS equates to a \_\_\_\_\_, and thousands more dollars in out-of-pocket costs for many individual patients. For example, for one local health plan’s members, a hip and knee replacement would cost a patient with 20 percent co-insurance \_\_\_\_\_ more if performed at RHS’s rates rather than SIR’s rates. In addition, two health plans are currently negotiating to bring SIR into their provider networks; for these health plans, RHS will be able to demand and obtain much higher rates than SIR could independently. Local employers are equally concerned that the Acquisition will burden them with even higher employee healthcare costs, potentially forcing them to cut benefits.

8. The Acquisition also would eliminate important competition between SIR and RHS to maintain and improve the quality of their facilities and services. SIR’s high quality and patient satisfaction is likely to be diminished under RHS’s more bureaucratic management. The Acquisition also eliminates RHS’s acknowledged incentive to improve its own quality to compete with SIR.

9. Entry or expansion by other providers of the relevant surgical services will not mitigate the loss of price and non-price competition in the near future, if ever. Hospitals in the area surrounding the Reading area, and the existing ambulatory surgery centers within the Reading area, are unable to and uninterested in expanding their services due to, among other things, RHS’s dominance over primary care physicians and a shortage of surgical specialists in the area. Even St. Joseph, the only other general acute-care hospital in the Reading area, has had

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difficulty recruiting specialists for services included in the relevant service markets, and thus could not likely increase its surgical capacity. In addition, because the Patient Protection and Affordable Care Act (“PPACA”) precludes the building of any new physician-owned hospitals, as well as expansion of existing physician-owned hospitals, a group of physicians cannot replicate SIR’s entry for inpatient services. There are no verifiable or merger-specific efficiencies or quality claims that would come close to offsetting the serious competitive harm threatened by the Acquisition.

**II.****BACKGROUND****A.****Jurisdiction**

10. RHS and SIR are, and at all relevant times have been, engaged in commerce or in activities affecting commerce, within the meaning of the FTC Act and the Clayton Act. The Acquisition constitutes an acquisition under Section 7 of the Clayton Act.

**B.****Respondents**

11. Respondent RHS is a not-for-profit healthcare system incorporated under and by virtue of the laws of Pennsylvania. RHS is headquartered at 300 South 6th Avenue, West Reading, Pennsylvania 19611. RHS owns and operates Reading Hospital, a general acute-care hospital that has 735 licensed beds. RHS also owns a 112-bed post-acute rehabilitation center and a continuing care retirement community facility. RHS is by far the largest employer of physicians in the Reading area, employing about 332 physicians. During fiscal year 2011, RHS generated \$47 million in operating income with \$132 million in EBITDA income. RHS currently holds approximately \$1.05 billion of unrestricted cash and investments.

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12. RHS is also a 50 percent owner of SurgiCenter at Spring Ridge (“SurgiCenter”), an outpatient ambulatory surgery center with eight operating rooms, and of Berkshire Health Partners (“BHP”), a provider network that contracts with employers and health plans and does credentialing of physicians and organizations to participate in the network. RHS negotiates reimbursement rates with health plans on behalf of SurgiCenter and it has significant control over SurgiCenter’s daily operations. In the ordinary course of business, RHS treats SurgiCenter as its own facility in competitive analyses and market share calculations. Thus for purposes of the competitive analysis, and for measuring market shares and market concentration, SurgiCenter is properly included as part of RHS. Similarly, BHP is effectively controlled by RHS. For example, BHP’s CEO reports directly to RHS’s CEO.

13. Respondent SIR, organized as a limited partnership under the laws of Pennsylvania, is a for-profit specialty surgical hospital located at 2752 Century Boulevard, Wyomissing, Pennsylvania 19610. SIR has 15 licensed beds and provides a variety of inpatient and outpatient surgical services, including ENT, orthopedic, spine, neurological, and general surgery procedures. A group of 16 physicians owns 85 percent of SIR, with the remaining 15 percent owned by Nueterra Healthcare LLC (“Nueterra”), a developer and manager of surgery centers. During fiscal year 2011, SIR generated \_\_\_\_\_ in operating revenue and its net income totaled over \_\_\_\_\_

### C.

#### **The Acquisition**

14. Under the terms of the asset purchase agreement signed on May 21, 2012, RHS will acquire all of SIR’s assets, including Nueterra’s 15 percent ownership interest. Accordingly, RHS will control SIR’s strategic planning, contracting and pricing decisions, operating and capital budgets, large unbudgeted expenditures, and borrowing and contracting decisions.

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RHS agreed to pay \_\_\_\_\_ to acquire SIR than the next-highest bidder.

**D.****Competition Between Healthcare Facilities**

15. Competition between hospitals occurs in two stages. In the first stage, hospitals compete to be selected as in-network providers to commercial health plans' members. To become an in-network provider, each hospital engages in negotiations with each health plan and enters into a contract. Reimbursement rates that apply when the health plan's members obtain care at the facility or from its employed physicians are the chief contractual terms to be negotiated and agreed upon.

16. Hospitals benefit from in-network status by gaining access to the health plan's members as patients. Health plans benefit by being able to create commercially marketable and appealing provider networks, with geographic coverage and a scope of services sufficient to attract and satisfy a localized group of members, typically employers and their employees.

17. Changes in the reimbursement rates negotiated between the facilities and the health plans impact the health plan's members, *i.e.*, local employers and their employees, greatly. "Self-insured" employers rely on the health plan for access to the provider network and the health plan's negotiated rates, but such employers pay their employees' health care claims directly. Thus, self-insured employers, not commercial health insurance companies, bear the full burden of any increases in the rates applicable to services used by their employees. "Fully-insured" employers and their employees pay premiums, co-pays, and deductibles in exchange for access to a health plan's provider network and also for insurance against the cost of care. Nevertheless, when the cost of care rises, for example due to rate increases, health plans ultimately pass on some or all of the increases to their fully-insured customers. Regardless of whether an employer is self-insured or fully-insured, the health plan acts on its behalf – and by extension acts on behalf of its employees – in creating provider networks that offer convenience, high quality of care, and negotiated reimbursement rates.

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18. In the second stage of competition, each hospital or facility competes with other in-network providers to attract patients. Health plans typically seek to offer multiple in-network providers with similar out-of-pocket costs. Providers included in the same network must compete to attract patients by offering better services, amenities, convenience, quality of care, and patient satisfaction than their competitors.

### III.

#### **ANTICOMPETITIVE EFFECTS**

##### **A.**

#### **Loss of Price Competition and Increased Bargaining Leverage of RHS**

19. The Acquisition will eliminate significant head-to-head competition between the Respondents and therefore increase RHS's ability and incentive to unilaterally demand higher reimbursement rates from commercial health plans.

20. RHS already is the dominant healthcare provider in the Reading area due to its market share and its ownership of the largest hospital, several outpatient facilities, two large physician groups, and a local provider network. Health plans, credit rating agencies, and RHS's own executives agree that RHS is dominant in the area. A consumer survey commissioned by RHS reflected the views of local residents, who describe RHS as "dominating," "power hungry," "large and expensive," and "taking over everything."

21. As the dominant provider in the Reading area, RHS already has significant bargaining leverage during contract negotiations with health plans, enabling it to extract very high rates for its services. Indeed, it is one of the most expensive healthcare providers in central Pennsylvania. RHS is widely recognized by health plans as having the highest rates in the Reading area and for making aggressive rate increase demands, relative to other hospitals. RHS's CFO provided testimony that it uses its leverage over health plans to receive the highest rates possible.

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22. SIR entered the market in 2007 as a small but potent challenger to RHS's dominance. SIR offers substantially lower rates to health plans for its services than RHS and also offers a convenient, high-quality alternative for patients. Competition from RHS has helped to keep SIR's rates low in the years since its opening.

23. Even before SIR opened, RHS prepared for the impact it would have on its revenue and volumes. In January 2007 – on the virtual eve of SIR's entry – RHS executives projected losing 60 percent of their surgical cases at Reading Hospital and 80 percent of cases at RHS's SurgiCenter facility.

24. Shortly after SIR's opening, there was indeed a significant shift in patient volume for surgical services from RHS to SIR. RHS's former CFO testified that "SIR's entry had a significant impact on both RHS's patient volume and revenue." A third-party analysis, commissioned by RHS in 2010, notes "declines in surgical procedures, as high as 80 [percent]" at RHS between 2008 and 2010 and attributes these "notable losses of volume" to SIR's increased presence in the market. The report highlighted losses in ENT, orthopedics, and general surgery. A 2010 assessment of surgical services similarly notes that "the largest loss of surgical share occurred in the Primary Service Area and the Northeast SSA [Secondary Service Area] due primarily to the opening of the Surgical Institute of Reading." In 2011, a RHS strategic plan noted that "RHS is seeing a significant decrease in elective joint replacement surgery directly due to the physician-owned Surgical Institute of Reading."

25. RHS executives were alarmed by the loss of volume to SIR. In early 2009, RHS's Director of Marketing wrote that "it is clear that anyone who is not impacted by [insurance issues] is choosing to go to SIR. Ouch." In May 2009, the same executive wrote, "Our real nemesis at this point is SIR!!" and observed that "by service line [it's] even a harder hit . . . [SIR has] 10% of the overall inpatient orthopaedic market share in Berks County." Another RHS executive, reviewing market shares for inpatient orthopedic surgical services, noted it was "not a pretty picture with SIR in the mix."

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26. SIR's ordinary-course-of-business documents also underscore the close competition between RHS and SIR for patients needing surgical services. An analysis conducted by a third party, based on information provided by SIR, describes RHS as SIR's "[p]rimary competitor." SIR's internal documents addressing the local marketplace overwhelmingly focus on competition with RHS, noting, among other things, the wide differences in rates that the two charge health plans for the same services as well as the higher patient satisfaction scores for services provided at SIR.

27. RHS responded vigorously to the loss of surgical volume to SIR. First, RHS offered discounted rates to several major health plans in exchange for excluding SIR from their provider networks. Most health plans declined the rate discounts because of the importance of SIR to their provider networks and to their members. Accordingly, due to competition between SIR and RHS, health plans in the Reading area had a choice between two beneficial options: (1) to exclude SIR from their provider network and receive a discount from the more expensive, dominant RHS; or (2) to contract with SIR at significantly lower rates than RHS, lowering costs and increasing access for their membership. After the Acquisition, both options are lost.

28. RHS also responded to competition from SIR by using its influence with BHP to steer patients to RHS and away from SIR, including excluding SIR as an in-network provider for its employees. RHS is the largest employer in the Reading area and, thus, a substantial number of individuals in the Reading area could not receive in-network coverage for services provided at SIR. Similarly, RHS's employed primary care physicians refused to refer patients to SIR specialists unless they agreed to perform the necessary surgeries at a RHS-owned facility, rather than SIR.

29. Ultimately, RHS decided that it made more sense to respond to the competition from SIR by seeking to acquire it and thereby eliminate it as a competitor. RHS's CEO admitted as much, confessing in internal company documents that the acquisition of SIR was both "defensive and offensive," believing that if SIR were acquired by another entity, even more volume would leave RHS. Elsewhere, he described the Acquisition as "a smart defensive move to protect the hospital's market share." The

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fact that RHS was willing to pay a considerable premium to purchase SIR – than the next highest bidder – indicates that the Acquisition offers significant additional value to RHS because it eliminates a close competitor, and also prevents that competitor from being acquired by a potential rival.

30. The Acquisition of SIR makes it all the more essential for Reading area employers and health plan members to have access to RHS facilities. As such, RHS will have greater leverage in negotiations with health plans – and the ability to demand higher reimbursement rates – after the Acquisition than before.

31. One of SIR's motivations for entering into the Acquisition was SIR's physician owners privately acknowledged that an affiliation with a "large Medical System" in the area (*i.e.*, RHS) would cause reimbursement rates to

32. Health plans likewise anticipate a significant increase in SIR's rates, even to RHS's current rates, for the same services as a result of the Acquisition. An increase in SIR's rates to the level of RHS's rates would cause

for services obtained at SIR. For some procedures, such as hip and knee replacements, patients with co-insurance would have to pay thousands of dollars more out-of-pocket for procedures performed at SIR.

33. SIR's current contracts with the major health plans are

As such, once the Acquisition closes, RHS will be able to terminate SIR's contracts and demand higher reimbursement rates from health plans at SIR in short order.

34. SIR does not currently have contracts with the health plans

If consummated, the Acquisition would allow RHS to extract much higher reimbursement rates from than SIR could independently.

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35. The costs of rate increases resulting from the Acquisition will be borne directly by or passed on to local employers and their employees. In the Reading area, the majority of commercial health-plan membership is comprised of self-insured employers. Self-insured employers rely on health plans only to negotiate rates and provide administrative support; the employers themselves pay the full cost of their employees' healthcare. As a result, self-insured employers immediately and directly bear the full burden of higher rates. Meanwhile, health plans pass on some or all costs of hospital rate increases to their fully-insured customers.

36. Employers, in turn, generally must pass on their increased healthcare costs to their employees, in whole or in part. Employees will bear these increased costs in the form of higher premiums, higher co-payments, reduced coverage, restricted services, or reductions in wages or other benefits. Some Reading area residents may therefore forgo or delay necessary healthcare services because of the higher costs, while others may drop their insurance coverage altogether.

## **B.**

### **The Acquisition Eliminates Vital Quality Competition**

37. Since SIR's entry into the Reading area in 2007, local residents have benefited from vigorous head-to-head competition between RHS and SIR to improve the quality of care offered in the Reading area. In fact, SIR entered the market because its physician owners felt that the other Reading area providers – where they were previously performing surgeries – were not “providing adequate care for [their] patients.” Thus, SIR was created as a “patient-focused hospital,” offering 24-hour visitation, quick schedule times, private rooms, and lower infection rates.

38. Currently, SIR not only offers lower rates than its acquirer, RHS, but it also provides a high quality of care and better patient service. Through its excellent service and high quality of patient care, SIR has achieved patient satisfaction rates that are above national standards. Indeed, a recent federal government report revealed that SIR had significantly higher patient satisfaction rates than RHS and St. Joseph.

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39. RHS's ownership and management threaten to diminish SIR's patient satisfaction levels and quality of care. The Acquisition will likely reduce SIR's patient satisfaction levels, or at a minimum reduce the competitive incentive to maintain and improve these levels, and thus lower the quality of care offered to Reading area residents. Much of SIR's high quality and exceptional service can be attributed to its physician-driven management that is less bureaucratic than RHS. One of the SIR owners stated

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40. The Acquisition will also dampen RHS's incentive to improve its own quality and efficiency to compete with SIR. RHS noted in an internal document that it "struggles to provide the same level of service and amenities as competing [ambulatory centers and specialty facilities]." Another RHS document describes the loss of "higher-reimbursed patients" to SIR, concluding that "[w]e must be aggressive in our response to improve our services so that patients will want to come to [Reading Hospital]." Similarly, another document states that RHS must "combat" SIR by "provid[ing] the best patient experience as well as continue to provide the best clinical outcomes."

## IV.

**THE RELEVANT SERVICE MARKETS**

41. The direct evidence above demonstrates the vigorous head-to-head competition between RHS and SIR that will be lost if the Acquisition is consummated, leading to higher prices and lower quality for Reading area residents. It can be inferred from this evidence alone that the Acquisition will result in serious competitive harm. In this case, however, the direct evidence is consistent with, and provides strong additional support for, the presumption of harm under the case-law and Merger Guidelines that is triggered by the substantial increases in market share and market concentration that the Acquisition would create in each of the four relevant markets discussed below. Each market consists of a cluster of surgical services that both RHS and SIR offer in

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head-to-head competition with each other to commercially-insured residents of the Reading area.

**A.**

**Inpatient Orthopedic Surgical Services**

42. The first relevant service market is inpatient orthopedic surgical services contracted for by commercial health plans. The service market encompasses a cluster of basic orthopedic and spine surgical services offered by both RHS and SIR that require an overnight hospital stay, such as knee, hip, and joint replacement surgeries and spinal fusions. This market accounts for the vast majority of SIR's inpatient surgical cases. The services included in the inpatient orthopedic surgical services market are performed by board-certified orthopedic surgeons and neurosurgeons.

43. Although the Acquisition's likely effect on competition could be analyzed separately for each of the dozens of affected medical procedures, it is appropriate to evaluate the Acquisition's likely effects across this cluster of services because the group of services is offered to Reading area residents under similar competitive conditions. For example, the inpatient orthopedic services are offered by the same set of competitors. Thus, the Acquisition is likely to impact competition, and patients, in the same way for each of the services involved in the relevant cluster.

44. The inpatient orthopedic surgical services market does not include outpatient services – those not requiring an overnight hospital stay – because the competitive environment surrounding those services is different, including that they are offered by a different set of competitors in the Reading area. In addition, inpatient services must be provided in a hospital setting, unlike outpatient procedures, which may be offered in a hospital or ambulatory surgical center.

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**B.****Outpatient Orthopedic Surgical Services**

45. The second relevant market in which the Acquisition threatens substantial competitive harm is outpatient orthopedic surgical services contracted for by commercial health plans. This market encompasses a cluster of orthopedic surgical services offered by both RHS and SIR that do not require an overnight hospital stay, including carpal tunnel surgery, knee and shoulder arthroscopic surgeries, rotator cuff surgery, and surgical procedures that affect the spinal column or neck. The services included in the outpatient orthopedic surgical services market are performed by board-certified orthopedic surgeons and neurosurgeons.

46. It is appropriate to evaluate the Acquisition's likely effects across this cluster of services, rather than analyzing each outpatient orthopedic service independently, because the group of services is offered to Reading area residents by a unique set of providers under similar competitive conditions.

**Outpatient Ear, Nose, and Throat Surgical Services**

47. The third relevant market in which the Acquisition threatens substantial competitive harm is the market for outpatient ENT surgical services contracted for by commercial health plans. This market encompasses a cluster of ENT surgical services offered by both RHS and SIR that do not require an overnight hospital stay, including tonsillectomies, nasal septum surgeries, thyroid procedures, and sinus endoscopies. The services included in the outpatient ENT surgical services market are performed by board-certified otolaryngologists.

48. It is appropriate to evaluate the Acquisition's likely effects across this cluster of services, rather than analyzing each outpatient ENT service independently, because the group of services is offered to Reading area residents by a unique set of providers under similar competitive conditions.

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## C.

**Outpatient General Surgical Services**

49. The fourth relevant market in which the Acquisition threatens substantial competitive harm is the market for outpatient general surgical services contracted for by commercial health plans. This market encompasses a cluster of outpatient general surgery procedures offered by both RHS and SIR that do not require an overnight hospital stay, including hernia repair, cholecystectomy (*i.e.*, gall bladder removal), breast lesion removal and biopsies, and black lesion excisions. Outpatient general surgical services are performed by board-certified general surgeons.

50. It is appropriate to cluster these services together as they are offered under similar competitive conditions, including being offered by a unique set of competitors. That set of competitors differs from the set of competitors for the other two outpatient relevant service markets but is similar to the set of competitors that offers inpatient orthopedic surgical services market. However, the respective market shares of the overlapping competitors (namely, Reading Hospital, SIR, and St. Joseph) differ between outpatient general surgical services market and the inpatient orthopedic surgical services market, and RHS's SurgiCenter competes in this market, unlike the inpatient orthopedic services market. Also, outpatient general surgical services need not be performed in a hospital, unlike the services in the inpatient orthopedic surgical services market.

## V.

**THE RELEVANT GEOGRAPHIC MARKET**

51. The relevant geographic market in which to analyze the effects of the Acquisition for each relevant service market is the area corresponding to Reading Hospital's primary service area, which is defined by RHS in the ordinary course of business as the set of zip codes from which Reading Hospital draws approximately 85 percent of its patients (the "Reading area"). This area encompasses most of Berks County.

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52. In a merger case, the appropriate geographic market is “the area in which consumers can practically turn for alternative sources of the product [or service] and in which the antitrust defendants face competition.” A relevant test to determine the boundaries of the geographic market is whether a hypothetical monopolist of the relevant services within the geographic area could profitably raise prices by a small but significant amount. If so, the boundaries of the geographic area are an appropriate geographic market. Defining the geographic market is a “pragmatic undertaking” and it should “correspond to the commercial realities of the industry.”

53. The Respondents’ own ordinary course of business documents reveal that they do not regard hospitals or ambulatory surgery centers outside of the Reading area as meaningful competitors for the relevant services at issue. Instead, Respondents focus their competitive efforts relating to these services on providers located in the Reading area, and especially each other.

54. RHS analyzes competitors and market shares for the affected services in the Reading area (*i.e.*, its primary service area) separately from other geographic areas. RHS has also used the Reading area as the basis for negotiations with health plans to exclude competitors from provider networks. Health plans, when preparing to negotiate with RHS, also analyze competition within the Reading area.

55. Reading area residents prefer to obtain surgical services that make up each of the four relevant markets locally. Health plans must therefore include hospitals and ambulatory surgery centers located in the Reading area in their provider networks in order to meet their members’ needs and desires for choice. Patients would not go to hospitals or ambulatory surgery centers outside of the Reading area in sufficient numbers to defeat a post-Acquisition anticompetitive rate increase within the Reading area in any of the four relevant service markets. As such, a hypothetical monopolist that controlled all of the relevant facilities in the Reading area could profitably raise rates by at least a small but significant amount.

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**VI.****MARKET STRUCTURE AND THE ACQUISITION'S  
PRESUMPTIVE ILLEGALITY****A.****Inpatient Orthopedic Surgical Services Market**

56. The Acquisition will reduce the number of significant providers of inpatient orthopedic surgical services in the Reading area from three to two. The only additional providers are of little competitive significance, each with a market share of less than four percent.

57. Under the relevant case law and the Merger Guidelines, the Acquisition is presumptively unlawful by a wide margin as it would significantly increase concentration in a market that already is highly concentrated.

58. RHS's post-Acquisition market share in the inpatient orthopedic surgical services market will be 66.5 percent (as measured by procedures), easily surpassing levels held to be presumptively unlawful by the Supreme Court. Post-Acquisition, two competitors, RHS and St. Joseph, would control about 78 percent of the inpatient orthopedic surgical services market in the Reading area, effectively a duopoly.

59. The Merger Guidelines measure market concentration using the Herfindahl-Hirschman Index ("HHI"). A merger or acquisition is presumed likely to create or enhance market power, and thus is presumed illegal, when the post-merger HHI exceeds 2500 points and the merger or acquisition increases the HHI by more than 200 points. Here, the market concentration levels exceed these thresholds by a wide margin. The post-Acquisition HHI in the inpatient orthopedic surgical services market will be 4585, an increase of 2050 points. The HHI figures for the inpatient orthopedic surgical services market are summarized in the table below.

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| <b>INPATIENT ORTHOPEDIC SURGICAL SERVICES</b> |                                  |                         |
|-----------------------------------------------|----------------------------------|-------------------------|
| <b>Provider</b>                               | <b>Market Share (procedures)</b> | <b>Post-Acquisition</b> |
| <b>Reading Hospital</b>                       | <b>42.2%</b>                     | <b>66.5%</b>            |
| <b>SIR</b>                                    | <b>24.3%</b>                     |                         |
| St. Joseph                                    | 11.2%                            | 11.2%                   |
| Lehigh Valley                                 | 3.9%                             | 3.9%                    |
| Hershey                                       | 3.2%                             | 3.2%                    |
| Thomas Jefferson                              | 2.4%                             | 2.4%                    |
| Pottstown Memorial                            | 1.6%                             | 1.6%                    |
| <b>HHI</b>                                    | <b>2535</b>                      | <b>4585</b>             |
| <b>Delta</b>                                  | <b>2050</b>                      |                         |

**B.****Outpatient Orthopedic Surgical Services**

60. The Acquisition will reduce the number of meaningful outpatient orthopedic surgical service competitors from four to three in the Reading Area. The only other providers of outpatient orthopedic surgical services in the Reading area, which each have a market share of 2.6 percent or less, are not significant competitors.

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61. Under the relevant case law and the Merger Guidelines, the Acquisition raises significant competitive concerns in the outpatient orthopedic surgical services market. Based on outpatient orthopedic procedures, RHS's post-Acquisition market share will be 48.5 percent.

62. Under the Merger Guidelines' market concentration test, the Acquisition will result in a highly concentrated market, and is presumptively illegal, because the post-Acquisition HHI increases 978 points to 2856. The HHI figures for outpatient orthopedic surgical services are summarized in the table below.

| <b>OUTPATIENT ORTHOPEDIC SURGICAL SERVICES</b> |                                  |                          |                         |
|------------------------------------------------|----------------------------------|--------------------------|-------------------------|
| <b>Provider</b>                                | <b>Market Share (procedures)</b> | <b>Share (by entity)</b> | <b>Post-Acquisition</b> |
| <b>SurgiCenter</b>                             | <b>19.9%</b>                     | <b>34.2%</b>             | <b>48.5%</b>            |
| <b>Reading Hospital</b>                        | <b>14.3%</b>                     |                          |                         |
| <b>SIR</b>                                     | <b>14.3%</b>                     |                          |                         |
| Reading Surgery Center                         | 20.1%                            | 20.1%                    | 20.1%                   |
| St. Joseph                                     | 8.9%                             | 8.9%                     | 8.9%                    |
| Hershey                                        | 2.6%                             | 2.6%                     | 2.6%                    |
| Premier Podiatric                              | 2.2%                             | 2.2%                     | 2.2%                    |
| Lehigh Valley                                  | 1.8%                             | 1.8%                     | 1.8%                    |

## Complaint

|                    |             |      |             |
|--------------------|-------------|------|-------------|
| Pottstown Memorial | 1.5%        | 1.5% | 1.5%        |
| <b>HHI</b>         | <b>1878</b> |      | <b>2856</b> |
| <b>Delta</b>       | <b>978</b>  |      |             |

## C.

**Outpatient Ear, Nose, and Throat Surgical Services**

63. The Acquisition will reduce the number of significant competing providers of outpatient ENT surgical services from three to two in the Reading area, creating an effective duopoly of RHS and Pennsylvania Eye and Ear Surgical Center, together controlling over 84 percent of the market. The only other providers of outpatient ENT surgical services in the Reading area, which each have market shares of 2.3 percent or less, are not significant competitors.

64. Based on outpatient ENT procedures, RHS's post-Acquisition market share will be 58.2 percent. Already a highly concentrated market before the Acquisition, the post-Acquisition HHI in the outpatient ENT surgical services market will be 4085, an increase of 1614 points. Thus, by a wide margin, the Acquisition is presumed illegal in this market as well as under the Merger Guidelines. The HHI figures for the outpatient ENT surgical services market are summarized in the table below.

| <b>OUTPATIENT EAR, NOSE, &amp; THROAT SURGICAL SERVICES</b> |                                  |                          |                         |
|-------------------------------------------------------------|----------------------------------|--------------------------|-------------------------|
| <b>Provider</b>                                             | <b>Market Share (procedures)</b> | <b>Share (by entity)</b> | <b>Post-Acquisition</b> |
| <b>SIR</b>                                                  | <b>35.4%</b>                     | <b>35.4%</b>             | <b>58.2%</b>            |

## Complaint

|                            |              |              |             |
|----------------------------|--------------|--------------|-------------|
| <b>SurgiCenter</b>         | <b>11.8%</b> | <b>22.8%</b> |             |
| <b>Reading Hospital</b>    | <b>11.0%</b> |              |             |
| Penn. Eye & Ear            | 26.1%        | 26.1%        | 26.1%       |
| Hershey                    | 2.3%         | 2.3%         | 2.3%        |
| University of Pennsylvania | 2.1%         | 2.1%         | 2.1%        |
| St. Joseph                 | 2.0%         | 2.0%         | 2.0%        |
| Pottstown Memorial         | 1.8%         | 1.8%         | 1.8%        |
| <b>HHI</b>                 | <b>2471</b>  |              | <b>4085</b> |
| <b>Delta</b>               | <b>1614</b>  |              |             |

**D.****Outpatient General Surgical Services**

65. The Acquisition will eliminate significant competition in the outpatient general surgical services market by reducing the number of significant competitors from three to two – again creating a virtual duopoly – with RHS and St. Joseph together controlling over 84 percent of the outpatient general surgical services market in the Reading area. The additional providers of outpatient general surgical services in the Reading area, which each have market shares of 1.4 percent or less, are not significant competitors.

66. The Acquisition is once again presumptively illegal under the relevant case law and the Merger Guidelines. RHS's post-

## Complaint

Acquisition market share in the outpatient general surgical services market will be 71.5 percent (as measured by procedures), far surpassing levels held to be presumptively unlawful by the Supreme Court. The post-Acquisition HHI also exceeds the presumption of illegality in the Merger Guidelines by a wide margin, with an increase of 2001 points to 5287. The HHI figures for the outpatient general surgical services market are summarized in the table below.

| OUTPATIENT GENERAL SURGERY |                           |                   |                  |
|----------------------------|---------------------------|-------------------|------------------|
| Provider                   | Market Share (procedures) | Share (by entity) | Post-Acquisition |
| Reading Hospital           | 35.3%                     | 52.4%             | 71.5%            |
| SurgiCenter                | 17.1%                     |                   |                  |
| SIR                        | 19.1%                     | 19.1%             |                  |
| St. Joseph                 | 12.9%                     | 12.9%             | 12.9%            |
| Reading Surgery Center     | 1.4%                      | 1.4%              | 1.4%             |
| Lehigh Valley              | 1.4%                      | 1.4%              | 1.4%             |
| Pottstown Memorial         | 1.4%                      | 1.4%              | 1.4%             |
| HHI                        | 3286                      |                   | 5287             |
| Delta                      | 2001                      |                   |                  |

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67. In each of the four relevant markets there is a presumption of illegality because the Acquisition results in the merged entity controlling a large percentage share for each relevant market and yields a significant increase in market concentration. Plaintiffs need only meet their burden with respect to one of the relevant markets to warrant relief from this Court.

## VII.

### **ENTRY BARRIERS**

68. Neither entry by new firms nor expansion by the few small remaining competitors will deter or counteract the Acquisition's likely serious competitive harm in the relevant service markets.

69. First, new entry or meaningful expansion into the relevant markets at issue is difficult and thus unlikely because of the foreclosure of surgical referrals from local primary care physicians. The vast majority of Reading area primary care physicians are employed by RHS or already affiliated with other existing facilities. Without adequate primary care physician referrals, it is impossible for a surgical facility to establish itself or grow an adequate patient base to become a meaningful competitor.

70. Another barrier to entry or expansion is access to the requisite surgical specialists (*e.g.*, orthopedic and neurosurgeons for the inpatient and outpatient orthopedic surgical service markets, otolaryngologists for the outpatient ENT surgical services market, and general surgeons for the outpatient general surgical services market). Most surgical specialists in the Reading area are already affiliated with a facility and contractually restricted from performing surgeries elsewhere. Even RHS attempted but failed to recruit additional surgical specialists to better compete with SIR. Similarly, St. Joseph attempted to expand its orthopedic surgery program, but was unable to find sufficient orthopedic surgeons in the area. Thus, a new entrant or a competitor expanding its service offerings in the relevant service markets likely could not recruit the necessary additional surgical specialists.

## Complaint

71. RHS's ownership of BHP and control over its contracting practices creates another entry barrier. BHP offers a preferred provider organization to self-insured employers, including RHS itself, the largest employer in the Reading area. RHS has implemented a tiered BHP plan that places RHS facilities in a preferred tier, financially incentivizing RHS employees to utilize RHS providers. Thus, RHS employees pay significantly higher out-of-pocket costs to use competing facilities and therefore rarely seek services outside the RHS system. Accordingly, a new entrant or competitor attempting to expand its services would be unable to attract patients from the area's largest employer, hampering its ability to generate sufficient patient volume to be viable.

72. An additional barrier to entry or significant expansion in the inpatient orthopedic surgical services market arises from restrictions contained in the PPACA. Based on recent history, the most likely entrant into this market would be another physician-owned specialty hospital. Under PPACA, however, no new physician-owned hospitals can be built, and all physician-owned hospitals that were completed by the end of 2010, are prohibited from expanding the number of beds, operating rooms, or procedure rooms. Because most, if not all, of the ambulatory surgery centers in the Reading area are at least partially owned by physicians, they are precluded from converting their facilities into hospitals and expanding their services to offer inpatient orthopedic surgical services.

73. Even if entry into the relevant markets were likely, it could not occur in a timely manner. Construction of an ambulatory surgery center requires between two and three years from the planning stages to being able to accept commercially-insured patients. It takes even longer to construct a hospital. Significant expansion of services takes several years as well, and requires time-consuming recruitment of additional professional staff and many modifications to an existing facility.

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**VIII.****EFFICIENCIES**

74. Extraordinary merger-specific efficiencies are necessary to justify the Acquisition in light of its vast potential to harm competition. No court ever has found, without being reversed, that efficiencies rescue an otherwise illegal transaction. Here, Respondents did not quantify or even consider efficiencies when contemplating the Acquisition, instead acknowledging that “the acquisition is unlikely to create any significant efficiencies.” Indeed, the likely outcome of the Acquisition is that SIR will be folded into RHS’s less efficient, more bureaucratic structure.

**IX.****VIOLATIONS**

75. The allegations of Paragraphs 1 through 74 above are incorporated by reference as though fully set forth.

76. The Acquisition, if consummated, may substantially lessen competition in the relevant markets in violation of Section 7 of the Clayton Act, as amended, 15 U.S.C. § 18, and is an agreement constituting an unfair method of competition in violation of Section 5 of the FTC Act, as amended, 15 U.S.C. § 45.

**NOTICE**

Notice is hereby given to the Respondents that the sixteenth day of April, 2013, at 10:00 a.m. is hereby fixed as the time, and Federal Trade Commission offices, 600 Pennsylvania Avenue, N.W., Room 532, Washington, D.C. 20580 as the place, when and where an evidentiary 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 and the Clayton 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.

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You are notified that the opportunity is afforded you to file with the Commission an answer to this complaint on or before the fourteenth (14<sup>th</sup>) day after service of it upon you. An answer in which the allegations of the complaint are contested shall contain 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 facts 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 and conclusions under Rule 3.46 of the Commission's Rules of Practice for Adjudicative Proceedings.

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 the answer is filed by the Respondents. 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., Room 532, Washington, D.C. 20580. Rule 3.21(a) requires a meeting of the parties' counsel as early as practicable before the pre-hearing scheduling conference (but in any event no later than five (5) days after the answer is filed by the Respondents). Rule 3.31(b) obligates counsel for each party, within five (5) days of receiving the Respondents' answer, to make certain initial disclosures without awaiting a discovery request.

## Complaint

**NOTICE OF CONTEMPLATED RELIEF**

Should the Commission conclude from the record developed in any adjudicative proceedings in this matter that the Acquisition challenged in this proceeding violates Section 5 of the Federal Trade Commission Act, as amended, and Section 7 of the Clayton Act, as amended, the Commission may order such relief against Respondents as is supported by the record and is necessary and appropriate, including, but not limited to:

1. Divestiture or reconstitution of all associated and necessary assets, in a manner that restores two or more distinct and separate, viable and independent businesses in the relevant markets, with the ability to offer such products and services as RHS and SIR were offering and planning to offer prior to the Acquisition.
2. A prohibition against any transaction between RHS and SIR that combines their businesses in the relevant markets, except as may be approved by the Commission.
3. A requirement that, for a period of time, RHS and SIR provide prior notice to the Commission of acquisitions, mergers, consolidations, or any other combinations of their businesses in the relevant markets with any other company operating in the relevant markets.
4. A requirement to file periodic compliance reports with the Commission.
5. Any other relief appropriate to correct or remedy the anticompetitive effects of the transaction or to restore SIR as a viable, independent competitor in the relevant markets.

**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 sixteenth day of November, 2012.

By the Commission.

Final Order

**ORDER DISMISSING COMPLAINT**

On November 16, 2012, the Federal Trade Commission issued the Administrative Complaint in this matter, having reason to believe that the proposed acquisition of Surgical Institute of Reading (“SIR”) by Reading Health System (“Reading”), if consummated, would violate Section 5 of the Federal Trade Commission Act, as amended, 15 U.S.C. § 45, and Section 7 of the Clayton Act, as amended, 15 U.S.C. § 18. Complaint Counsel and Respondents have now filed a Joint Motion to Dismiss Complaint, which states that Respondents have abandoned the proposed acquisition of SIR by Reading, and have committed to provide notice to Commission staff 30 days prior to consummating any transaction between the Respondents.<sup>1</sup>

The Commission has determined to dismiss the Administrative Complaint without prejudice, as the most important elements of the relief set out in the Notice of Contemplated Relief in the Administrative Complaint have been accomplished without the need for further administrative litigation.<sup>2</sup> In particular, Respondents have abandoned the proposed acquisition and have bound themselves to provide prior notice in the future, rendering them unable to effect the proposed transaction without first providing 30 days’ notice to Commission staff.

For the foregoing reasons, the Commission has determined that the public interest warrants dismissal of the Administrative Complaint in this matter. The Commission has determined to do so without prejudice, however, because it is not reaching a decision on the merits. Accordingly,

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1 See Joint Motion To Dismiss Complaint (November 30, 2012), at <http://www.ftc.gov/os/adjpro/d9353/121130jointmodismisscmt.pdf>.

2 See, e.g., *In the Matter of Omnicare, Inc.*, Docket No. 9352, Order Dismissing Complaint (February 22, 2012), at <http://www.ftc.gov/os/adjpro/d9352/120223omnicareorder.pdf>; *In the Matter of Thoratec Corporation and HeartWare International, Inc.*, Docket No. 9339, Order Dismissing Complaint (August 11, 2009), at <http://www.ftc.gov/os/adjpro/d9339/090811thoatecorder.pdf>.

Final Order

**IT IS ORDERED THAT** the Administrative Complaint in this matter be, and it hereby is, dismissed without prejudice.

By the Commission, Commissioner Rosch abstaining.

Complaint

IN THE MATTER OF

**WATSON PHARMACEUTICALS INC.,  
ACTAVIS INC.,  
ACTAVIS PHARMA HOLDING 4 EHF.,  
AND  
ACTAVIS S.Á.R.L.**

CONSENT ORDER, ETC. IN REGARD TO ALLEGED VIOLATIONS OF  
SECTION 5 OF THE FEDERAL TRADE COMMISSION ACT AND  
SECTION 7 OF THE CLAYTON ACT

*Docket No. C-4373; File No. 121 0132*

*Complaint, October 15, 2012 – Decision, December 13, 2012*

This consent order addresses the \$5.9 billion acquisition by Watson Pharmaceuticals, Inc. of certain assets of Actavis Inc., Actavis Pharma Holding 4 ehf., and Actavis S.à.r.l. The complaint alleges that the acquisition, if consummated, would violate Section 7 of the Clayton Act and Section 5 of the Federal Trade Commission Act by lessening current and future competition in U.S. markets for the following generic pharmaceutical products: (1) extended release bupropion hydrochloride tablets; (2) extended release diltiazem hydrochloride capsules (generic Cardizem CD); (3) fentanyl transdermal system; (4) lorazepam tablets; (5) metoclopramide hydrochloride tablets; (6) extended release morphine sulfate capsules; (7) extended release nifedipine tablets; (8) extended release amphetamine salts capsules; (9) extended release diltiazem hydrochloride capsules (generic Tiazac); (10) extended release oxymorphone non-tamper resistant tablets; (11) extended release glipizide tablets; (12) isradipine capsules; (13) loxapine succinate capsules; (14) extended release methylphenidate hydrochloride tablets; (15) ursodiol tablets; (16) adapalene and benzoyl peroxide topical gel; (17) dextromethorphan hydrobromide and quinidine sulfate capsules; (18) extended release morphine sulfate and naltrexone combination capsules; (19) extended release oxycodone tamper resistant tablets; (20) extended release rivastigmine film; and (21) varenicline tartrate tablets. The consent order requires Watson and Actavis are required to divest either Watson's or Actavis's rights and assets related to eighteen of the twenty-one products (all but extended release morphine sulfate and naltrexone combination capsules, isradipine capsules, and loxapine succinate capsules).

*Participants*

For the Commission: Lisa D. DeMarchi Sleight, William Huynh, and David Von Nirschl.