New York Law Journal

WWW.NYLJ.COM

An ALM Publication

VOLUME 249—NO. 52

TUESDAY, MARCH 19, 2013

ANTITRUST TRADE AND PRACTICE

Expert Analysis

Impact of 'Phoebe Putney': What's Old Is New Again

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On Feb. 19, 2013, the U.S. Supreme Court issued its opinion in *Federal Trade Commission v. Phoebe Putney Health System*,[1] holding that the state action doctrine does not immunize the Hospital Authority of Albany-Dougherty County's purchase and lease of its only competitor hospital from federal antitrust liability because its general grant of corporate powers under Georgia law fails to clearly articulate permission to use those powers for such an anticompetitive transaction. The decision signals to lower courts the need to arrest the frequency with which state action immunity shields the application of federal antitrust law. Conversely, it behooves state legislatures to assess whether their enabling statutes sufficiently evidence an intention to immunize certain desired anticompetitive activity from federal scrutiny.

Proposed Transaction

Phoebe arose out of the merger between two hospitals in Georgia, Phoebe Putney Memorial Hospital (PPMH) and Palmyra Park Hospital.[2] PPMH is owned by the Hospital Authority of Albany-Dougherty County, which leases PPMH to Phoebe Putney Health System (PPHS), a nonprofit private corporation that operates the hospital.[3] Palmyra is a subsidiary of HCA, a private for-profit corporation.

PPHS began discussions with HCA regarding the possible acquisition of Palmyra in summer 2010.[4] Because of financing and antitrust concerns, PPHS proposed a transaction structure whereby the Authority would purchase Palmyra and lease it to PPHS under terms similar to the PPMH lease.[5] In December 2010, the Authority approved the purchase of Palmyra and, in April 2011, approved the terms of the lease of Palmyra to PPHS.[6] Shortly thereafter, on April 20, 2011, the FTC sought to enjoin the transaction in the U.S. District Court for the Middle District of Georgia, alleging that the merger would result in a near monopoly for the provision of inpatient general acute services by "eliminating competition between [PPMH] and Palmyra, the only two major hospitals that service not only the Albany, Dougherty County, community, but the communities of the surrounding six counties."

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State Action Doctrine

The defendants filed motions to dismiss, arguing that the transaction was shielded from federal antitrust liability by the state action doctrine. Driven by respect for the principle of federalism, and first articulated by the Supreme Court in *Parker v. Brown*, the state action doctrine shields states from federal antitrust liability when they restrain trade "as an act of government."[7] This *Parker* immunity does not extend, however, to private actors and political subdivisions because, unlike states, they are not afforded the deference of a sovereign.[8] Nevertheless, pursuant to *California Retail Liquor Dealers Ass'n v. Midcal Aluminum*, for private actors to be immunized, their challenged conduct must be "clearly articulated and affirmatively expressed as state policy," and "the policy must be actively supervised by the state itself."[9] Moreover, in *Town of Hallie v. Eau Claire* the Supreme Court declared that political subdivisions acting in accordance with statutory authorization need not satisfy *Midcal*'s 'active supervision' prong to have their conduct insulated from federal antitrust scrutiny.[10]

In this case, the defendants argued that the Authority is a political subdivision of Georgia that is expressly authorized by statute to acquire, operate and control hospitals within a defined district.[11] In turn, because the Authority was authorized to acquire and operate hospitals within a limited area, anticompetitive effects were foreseeable, putting the challenged conduct within the ambit of state action immunity.

The district court agreed with the defendants and dismissed the FTC's case, finding it clear that the Authority was a political subdivision authorized by statute to engage in hospital acquisitions and operations. The focus of the inquiry was whether the alleged anticompetitive conduct, including "a private entity taking managerial and operational control of its only former competitor through a management agreement and lease granted to it by a hospital authority," was reasonably foreseeable to the Georgia Legislature when it passed the statute granting power to the Authority. Ultimately, the district court found that the potentially anticompetitive acquisition and lease of the hospital to a private corporation was foreseeable, and that, in turn, the conduct of entities involved in executing the acquisition and lease qualified for state action immunity.

On appeal, the U.S. Court of Appeals for the Eleventh Circuit affirmed the decision. Citing *Hallie*, not *Midcal*, the court noted that the Authority's immunity "turns on whether the state has authorized the Authority's acquisition of Palmyra and, in doing so, clearly articulated a policy to displace competition."[12] Further, such a policy is clearly articulated if the anticompetitive effect is foreseeable or "reasonably anticipated," and

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"need not be one that ordinarily occurs, routinely occurs, or is inherently likely to result from the empowering legislation."[13]

First in applying this immunity framework to the facts, Judge Gerald Bard Tjoflat found that the legislature's grant of the power to "acquire by purchase, lease or otherwise…projects…makes clear that the Authority is authorized to acquire and lease Palmyra."[14] Finally, he surmised that "the Georgia legislature must have anticipated anticompetitive harm when it authorized hospital acquisitions by authorities. It defies imagination to suppose the legislature could have believed that every geographic market in Georgia was so replete with hospitals that authorizing acquisitions by the authorities could have no serious anticompetitive consequences."[15]

Supreme Court's Decision

Nevertheless, the U.S. Supreme Court unanimously rejected the Eleventh Circuit's line of reasoning and reversed. At the outset of her opinion, Justice Sonia Sotomayor made clear that although the *Midcal* two-pronged test frames her analysis, the court would not reach the "actively supervised" question because the Authority's proposed transaction failed to satisfy the initial "clearly articulated and affirmatively expressed" prong.

First, the court found that, "there is no evidence the State affirmatively contemplated that hospital authorities would displace competition by consolidating hospital ownership."[16] Although the Hospital Authorities Law grants the Authority broad powers typically ascribed to corporations, mere authorization to enter into business transactions was insufficient to create state-action immunity. The court reasoned, "while the Law does allow the Authority to acquire hospitals, it does not clearly articulate and affirmatively express a state policy empowering the Authority to make acquisitions of existing hospitals that will substantially lessen competition."[17]

Second, the court chided the Eleventh Circuit for applying the "foreseeability" concept in the clear articulation test "too loosely." Sotomayor narrowed the Eleventh Circuit's "reasonable anticipation" proxy for "foreseeability" and simultaneously reaffirmed the notion that a state-sanctioned displacement of competition is "foreseeable" if it is the "inherent, logical or ordinary result of the exercise of authority delegated by the state legislature."[18] In other words, "a reasonable legislature's ability to anticipate [a potentially undesirable] possibility falls well short of articulating an affirmative state policy to displace competition with a regulatory alternative."[19]

Third, the court rejected Judge Tjoflat's suggestion that certain market exigencies foreseeably give rise to anticompetitive effects when political subdivisions act based on grants of general authority. Justice Sotomayor was similarly unmoved by respondents' suggestions that Georgia's broader regulatory framework naturally restrains competition among housing authorities and other market participants by requiring a certificate of need whenever one seeks to establish or substantially expand certain medical facilities.

In this case, the court emphasized that the enabling legislation authorized much more than merely the acquisition of hospitals, and even if the analysis focused exclusively on the Authority's acquisition and leasing powers, "the power to acquire hospitals still does not ordinarily produce anticompetitive effects."[20] Moreover, "regulation of an industry, and even the authorization of discrete forms of anticompetitive conduct pursuant to a regulatory structure, does not establish that the State has affirmatively contemplated other forms of anticompetitive conduct that are only tangentially related."[21]

Lower courts must grapple more earnestly with whether potentially anticompetitive conduct is the 'inherent,' 'logical,' and 'ordinary' result of statutory grants of power to political subdivisions or private parties.

Implications

Outgoing FTC Chairman Jon Leibowitz hailed the ruling as "a big victory for consumers who want to see lower health care costs" and predicted that it "will ensure competition in a variety of industries as well."[22] Be that as it may, the decision does not appear to signal a sea change or substantial clarification of the unsettled state action immunity jurisprudence.

In the face of increasingly lax judicial application of the "clearly articulated" *Midcal* prong, the Supreme Court attempts to use *Phoebe Putney* to remind lower courts that state action immunity is generally disfavored, and that the immunized conduct must fall more directly within the scope of conduct contemplated by legislatures.

In the Supreme Court's eschewing of the Eleventh Circuit's broader "reasonably anticipated" concept of "foreseeability," lower courts must grapple more earnestly with whether potentially anticompetitive conduct is the "inherent," "logical," and "ordinary" result of statutory grants of power to political subdivisions or private parties. In echoing Supreme Court precedent, Sotomayor acknowledges the impracticability of requiring that legislatures explicitly afford specific sets of anticompetitive conduct antitrust immunity in their enabling statutes.[23] However, the failure of Georgia's Hospital Authority Law to even suggest that the Authority could use its purchasing or leasing authorization to create a monopoly is the apparently fatal inadequacy in the Authority's immunity armor. These two realities are difficult to reconcile.

Short of such express authorization, we would think that an examination of industry-specific factors would critically guide judicial determination of whether potentially anticompetitive conduct is an inherent, logical or ordinary result of enabling regulation. However, the court gives short shrift to the Eleventh Circuit's reasoning that "[i]t defies imagination to suppose the [state] legislature could have believed that every geographic market in Georgia was so replete with hospitals that authorizing acquisitions by authorities could have no serious anticompetitive consequences."[24] For example, the court does not discuss whether the Legislature's knowledge of Georgia's population density or concentration of hospitals in various counties logically suggests that the state contemplated immunizing the hospital's exercise of its purchasing and leasing power from federal antitrust scrutiny. In effect, the court appears to shift the goal posts to an analysis of whether the conduct predominates the grant of statutory authority.

The court merely notes, "only a relatively small subset of conduct permitted as a matter of state law by [the Housing Authority Law] has the potential to negatively affect competition." Consequently, lower courts must now find a way to determine what is an "inherent" anticompetitive result while paying scant regard to realities that shape the ordinary contours of market dynamics.

For the moment, it appears that increased federal antitrust scrutiny buttressed by the continued ambiguousness of the state action doctrine may cause some legislatures and their political subdivisions to reevaluate whether certain desired, but potentially anticompetitive activities are immunized from federal scrutiny by statutory authorizations that sufficiently evince such an intent. The *Phoebe* decision moves the needle just enough on the state action doctrine to make that clear.

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1. 568 U.S.___, 2013 U.S. LEXIS 1064 (2013).
2. In our September, 2012 column, we outlined the transaction facts and district court posture of *Phoebe* when the Supreme Court granted certiorari. We have chosen to reprint that outline here. See Neal R. Stoll & Shepard Goldfein, "Antitrust and the Supreme Court's Upcoming Term," 248 NYLJ, 50 (Sept. 11, 2012).
3. *FTC v. Phoebe Putney Health Sys.*, 663 F.3d 1369, 1373 (11th Cir. 2011) (*Phoebe* Appeals Court Decision).
4. *FTC v. Phoebe Putney Health Sys.*, 793 F.Supp.2d 1356, 1361 (M.D. Ga. 2011) (*Phoebe* District Court Decision).
5. *Phoebe* Appeals Court Decision, 663 F.3d at 1373.
6. *Phoebe* District Court Decision, 793 F.Supp.2d at 1360.
7. *Parker v. Brown*, 317 U.S. 341, 352 (1943).
8. See *Lafayette v. Louisiana Power and Light Co.*, 435 U.S. 389, 411-413 (1978) (plurality opinion).
9. 445 U.S. 97, 105 (1980).
10. 471 U.S. 34 (1985).
11. *Phoebe* District Court Decision, 793 F.Supp.2d at 1366.
12. *Phoebe* Appeals Court Decision, 663 F.3d at 1376 (citing *Town of Hallie*, 471 U.S. at 40).
13. Id. at 1375-76 (citing *Lee County*, 38 F.3d at 1188).
14. Id. at 1377.
15. *Phoebe* Appeals Court Decision, 663 F.3d at 1377.
16. 568 U.S.___, 2013 U.S. LEXIS 1064, at *20.
17. Id. at *23.
18. Id. at *24.
19. Id. at *27.
20. Id. at * 29.
21. Id. at *34.
22. Press Release, Statement of FTC Chairman Jon Leibowitz on the U.S. Supreme Court Ruling in Favor of the Commission in the Phoebe Putney/Palmyra Park Hospital Case (Feb. 19, 2013).
23. 568 U.S.___, 2013 U.S. LEXIS 1064, at *23.
24. *Phoebe* Appeals Court Decision, 663 F.3d at 1377.

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