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LEGAL DEVELOPMENTS

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THE FEDERAL TRADE COMMISSION SEEKS DIVESTITURE AND DISGORGEMENT THREE YEARS AFTER COMPLETION OF HART-SCOTT-RODINO PRE-MERGER REVIEW PROCESS

On April 4, 2001, the Federal Trade Commission ("FTC") took the unusual step of voting to file a complaint in the United States District Court for the District of Columbia against The Hearst Trust, its subsidiary The Hearst Corporation, and First DataBank, a wholly owned subsidiary of The Hearst Corporation (collectively "Hearst"), seeking: (1) an order requiring Hearst to create a new competitor to replace MediSpan, Inc., which Hearst acquired, after expiration of the Hart-Scott-Rodino ("HSR") waiting period, in 1998; (2) disgorgement of profits; and (3) civil penalties for violation of the HSR Act.

This case stands as a reminder that even after a merging party clears the HSR review process, the government will continue to monitor the competitive effects of the acquisition and if they are negative, will not hesitate to take action.

In 1997, Hearst filed a pre-merger notification and report form (the "Form") in accordance with the HSR Act in connection with its proposed acquisition of Medispan from J. Bruce Laughrey, Inc. MediSpan, the Commission alleges, was First DataBank's only significant competitor in the market for electronic integratable drug information databases. The databases contain comprehensive clinical and pricing information on prescription and non-prescription drugs in a form that can be integrated with other electronic databases, such as records maintained by pharmacies of their patients' medications. Pharmacists, hospital staff, and health plans use the data to manage health care. Significantly, the data files are used to provide prescribers with warnings of any dangerous interactions between prescriptions for new medications with those currently used by the patients.

Hearst, however, neglected to include in its pre-merger filing several high-level corporate documents prepared to evaluate the acquisition and its competitive effects as required by Item 4(c) in the Form.

Perhaps the FTC would never have learned of the omission but for Hearst's dramatic price increases after the acquisition: prices for some customers increased well over 100 percent. The customers had no alternative source for the data and thus were forced to pay the higher rates. Those dramatic price

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increases caused the FTC to investigate the merger and, in the course of that investigation, discover the documents omitted from the pre-merger filing.

The FTC, by a 3 to 2 vote, decided to file the action alleging Hearst violated Section 5 of the FTC Act and Section 7 of the Clayton Act by acquiring its competitor with the intent of monopolizing the market and causing "drastic" price increases for the databases. The Commission also charged Hearst with violating subsection (a) of Section 7A of the Clayton Act for withholding the Item 4(c) documents.

The majority -- Chairman Robert Pitofsky and Commissioners Sheila Anthony and Mozelle Thompson -- found that this case was one of those exceptional cases where disgorgement was an appropriate remedy because the alternative -- only a divestiture -- would allow Hearst to "walk off with the profits gained as a result of its allegedly illegal behavior." Republican Commissioners Orson Swindle and Thomas Leary, however, dissented. Most significantly, they thought disgorgement was an inappropriate remedy because private remedies are adequate to ensure that Hearst does not benefit from its wrongdoing and that its customers would be made whole. The dissent also disagreed with the decision to bring a complaint in federal court at this time. They believe that continued negotiations with Hearst would have resulted in an agreement on substantial penalties for violation of the HSR Act and a divestiture would restore competition in the market.

This case, whether or not the Commission is successful, provides some powerful lessons for merging parties: First, the Commission, at least as presently constituted, can and will challenge acquisitions that have "cleared" the HSR process where anticompetitive effects appear. (Given the change in Commissioners as Chairman Pitofsky is replaced with President Bush's choice of Tim Muris, there may be a shift in the remedies sought.) Second, if after the acquisition you want to raise prices substantially, consider whether you are able to do so due to market power gained as a result of the acquisition and if so, whether it would be wise to flaunt that market power. Third, take the Item 4(c) instructions seriously. Carefully and thoroughly search for and include all responsive documents.

Please contact any of us at Axinn, Veltrop & Harkrider LLP if you would like to explore the issues raised by this case further.