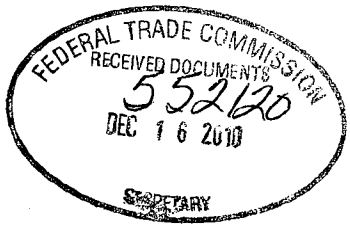

UNITED STATES OF AMERICA
BEFORE FEDERAL TRADE COMMISSION

In the Matter of	
LABORATORY CORPORATION OF AMERICA	**Docket No. 9345**
and	**REDACTED PUBLIC VERSION**
LABORATORY CORPORATION OF AMERICA HOLDINGS, Corporations.	

ANSWER OF RESPONDENTS LABORATORY CORPORATION OF AMERICA AND LABORATORY CORPORATION OF AMERICA HOLDINGS

Pursuant to 16 C.F.R. § 3.12, Respondents Laboratory Corporation of America and Laboratory Corporation of America Holdings (collectively referred to as "LabCorp") hereby answer the Federal Trade Commission's December 1, 2010 Complaint as follows.

PRELIMINARY STATEMENT

LabCorp's acquisition of Westcliff does not violate the Clayton Act. The FTC's Complaint completely ignores the realities of competition for clinical laboratory services in California and, in so doing, sets aside reasoned economic analysis of the *actual data* regarding competitive effects that has been available to the Commission for months in favor of a handful of documents drafted by LabCorp employees not responsible for ultimate decision-making and untested third-party declarations *drafted by the FTC.* As one Commissioner already has recognized, the FTC has no empirical evidence to support its contorted market definition. Moreover, the FTC has no evidence to support its allegations of anticompetitive effects, and has ignored evidence of efficiencies and imminent entry. The Commission also tries to sidestep the fact that, but for LabCorp's purchase of Westcliff's bankrupt assets, *those assets would have left*

the market entirely or likely devolved to Quest Diagnostics, which is by far the dominant clinical lab in California. The FTC has overreached. Competition for clinical laboratory services in California is robust; far from harming competition, this acquisition will make LabCorp a stronger competitor against Quest, which will benefit customers and ultimately patients.

In May 2010, Westcliff filed its Chapter 11 bankruptcy petition. Westcliff was in steep financial decline at that time. Despite actively soliciting interest from about 25 prospective buyers throughout 2009 and early 2010, only LabCorp had made an acceptable bid. Indeed, in a declaration filed with the bankruptcy court in California, Westcliff's Chief Restructuring Officer predicted that, if unable to consummate the sale to LabCorp on an expedited basis, Westcliff would "have to shut down [its] business and liquidate." The bankruptcy court agreed that sale to LabCorp was the best way to preserve Westcliff's assets as a going concern, and entered a Sale Order approving the sale for $57 million on June 9, 2010.

Despite knowing about the transaction since June 2, 2010, the FTC did nothing to stop the entry of that Sale Order. Instead, the FTC attempted to circumvent the bankruptcy court's authority by instigating a second round of bidding behind the scenes. With Westcliff's financial condition further deteriorating to the point where it was in serious risk of not being able to meet basic obligations, including payroll for its employees, LabCorp closed its transaction with Westcliff on June 16, 2010.

Westcliff's failing assets have been frozen in time since the close of the transaction. The FTC now seeks to unwind the transaction altogether. But unwinding the transaction and forcing LabCorp to divest Westcliff's assets would not help Westcliff or competition. Setting aside the fact that there are no alternative purchasers or divestees for Westcliff's failing assets, the FTC does not have a case. The FTC has alleged an overly narrow market so that it can claim that

concentration is high. As Commissioner Rosch recognized, the FTC's alleged market definition fails "both as a matter of law and common sense." The FTC claims the market should include only "[t]he sale of capitated clinical laboratory testing services to physician groups." The FTC's alleged market thus focuses on the part of LabCorp's and Westcliff's business that comprises just [redacted] of their respective revenues. The alleged market ignores entirely the fee-for-service business that comprises the vast majority of the remaining [redacted] of their respective revenues. But capitated and fee-for-service billing arrangements are merely two ways of paying for the *same exact* clinical laboratory services, and capitated rates are influenced by the potential for getting additional discretionary fee-for-service business. Indeed, as the FTC admitted in a previous case involving the same services in the same part of the country:

> "[P]ull-through" [a/k/a discretionary fee-for-service] business is an important determinant of the profitability of capitated contracts. Physician groups that participate in capitated plans for some of their customers also frequently participate in fee-for-service plans for other customers. Under fee-for-service plans, physicians are paid for each procedure. When Laboratory Services are needed for a patient with a fee-for-service plan, the health plan pays the laboratory directly but the physician chooses which laboratory covered by the plan will be used. The Laboratory Services provider for the capitated business of a physician group frequently has a significant advantage in winning a substantial amount of the "pull-through" fee-for-service business of the group, because physicians are familiar with the laboratory and it is easier to deal with one laboratory for all patients. Laboratory Services providers take into account the potential for pull-through business when determining their bids for capitated contracts.

Analysis of Agreement Containing Consent Orders to Aid Public Comment, *In re Quest Diagnostics Inc. and Unilab Corp.*, FTC Docket No. C-4074 (Feb. 27, 2003). As the FTC acknowledged and as the Merger Guidelines,[1] the case law,[2] economists,[3] and Commissioner

[1] U.S. Dep't of Justice & FTC, *Horizontal Merger Guidelines*, § 4.1.1 n.4. (2010).

Rosch[4] all also have recognized, when a company sells a product at a deflated price (e.g., capitated business) with the increased opportunity for subsequent higher-margin sales of closely-related products (e.g., discretionary fee-for-service business), the products should be included in the same market. Including fee-for-service business in the market as should be done here sweeps in *all* clinical labs in California because all clinical labs actively compete for discretionary physician business. Rather than rebut these arguments (which LabCorp has repeatedly made to Staff for months) the FTC's Complaint and the declaration of the FTC's expert completely ignore this aspect of competition for clinical lab services.

The FTC has based its case largely on the bald assertion that the structural features of its incorrectly-identified product market create a presumption of illegality. Overconfident in its mistaken presumption, the FTC gives short shrift to actual evidence of anticompetitive effects. As a threshold matter, even if the FTC's relevant market were correct (it is not), the FTC is not entitled to a rebuttable presumption of competitive harm based on the alleged market share and market concentration statistics that it alleges. In fact, courts have routinely held that shares

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[2] *See, e.g., United States v. Phillipsburg Nat'l Bank & Trust Co.*, 399 U.S. 350 (1970); *United States v. Philadelphia Nat'l Bank*, 374 U.S. 321 (1963); *see also Kentmaster Mfg. Co. v. Jarvis Prods. Corp.*, 146 F.3d 691 (9th Cir. 1998) ("[O]nly an idiot would think of the cost of A without taking into account the cost of B.... There is a single product, sold over time; the rationally-calculated price is the price of [the two products] together."), *amended by* 164 F.3d 1243 (9th Cir. 1999); *JBL Enters., Inc. v. Jhirmack Enterps., Inc.*, 698 F.2d 1011, 1016 (9th Cir. 1983) ("In determining what the field of competition is, courts are not free to accept whatever market is suggested by the plaintiff, but must examine the commercial realities within the industry in question.") (citation and internal quotation omitted); *M.A.P. Oil Co. v. Texaco Inc.*, 691 F.2d 1303, 1308 (9th Cir. 1982) ("Customers can choose between direct delivery of gasoline and delivery through distributors or commission agents, but in the final analysis they purchase a single product-gasoline.").

[3] *See, e.g.,* David A. Huettner, *Product Market Definition in Antitrust Cases When Products are Close Substitutes or Close Complements*, 47 Antitrust Bull. 133, 140-42 (2002) ("DOJ Merger Guidelines focus solely on substitute relationships to define antitrust product markets but contain no guidance for economic practitioners when products are complements.... Economists are aware that complementary relationships lead to a number of interesting marketing and business practices including loss leaders, full line forcing by furniture and other manufacturers, naturally tying products, and tying and bundling arrangements forced by contract.").

[4] Dissenting Statement of Commissioner J. Thomas Rosch, *In re Laboratory Corporation of America and Laboratory Corporation of America Holdings*, FTC Docket No. 9345 (Nov. 30, 2010).

under 30 percent are insufficient to create such a presumption.[5]

In the absence of statistical evidence, the FTC cherry-picks select portions of a handful of LabCorp documents to try to cobble together an argument that prices will somehow increase post-acquisition. Paradoxically, the FTC argues that Westcliff was a price-cutting, "maverick" when the uncontested evidence clearly demonstrates both: [redacted]. The evidence further demonstrates that LabCorp and Westcliff rarely, if ever, competed with each other for capitated business. [redacted]. This Court should not rely on a handful of hopeful and unsubstantiated statements written by non-decision-making LabCorp businesspeople or untested declarations drafted by the FTC and signed by coerced customers and competitors with suspect motives. There is actual price data, actual bid data, and robust natural experiments (including Westcliff's entry) from which to draw conclusions. The FTC and the FTC's expert ignore all of this evidence.

Furthermore, there is no evidence that the acquisition would result in coordinated effects. Capitated rates were low before Westcliff entered in 2007, and they will remain low post-acquisition. As thousands of documents the FTC does *not* cite in its pleadings prove,

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[5] *See* U.S. Dep't of Justice & FTC, *Horizontal Merger Guidelines*, § 2.211 (1992) (35 percent combined market share required for unilateral effects); *see also United States v. Philadelphia Nat'l Bank,* 374 U.S. 321 at 363 (30 percent threshold for undue concentration); *United States v. Baker Hughes, Inc.*, 908 F.2d 981 (D.C. Cir. 1990) (rejecting merger challenge where combined market share exceeded 35 percent); *FTC v. Butterworth Health Corp.*, 121 F.3d 708 (6th Cir. 1997) (rejecting merger challenge where combined market share exceeded 47 percent); *United States v. Waste Mgmt., Inc.*, 743 F.2d 976 (2d Cir. 1984) (rejecting merger challenge where combined market share exceeded 48.8 percent); *Lektro-Vend Corp. v. Vendo Co.*, 660 F.2d 255 (7th Cir. 1981) (rejecting merger challenge where combined market share exceeded 35.6 percent); *United States v. Oracle Corp.*, 331 F. Supp. 2d 1098, 1123 (N.D. Cal. 2004) ("A presumption of anticompetitive effects from a combined share of 35% in a differentiated products market is unwarranted."); *United States v. Sunguard Data Systems*, 172 F. Supp. 2d 172 (D.D.C. 2001) (rejecting merger challenge where combined market share exceeded 35 percent).

competition between LabCorp and Quest is extraordinarily fierce, and this transaction does nothing to alter that competition. Moreover, the FTC ignores the multitude of documents citing competition for fee-for-service business with dozens of other competitors – competition that currently impacts competition for physician group contracts and which will continue to do so post-acquisition.

As demonstrated by Westcliff's expansion [redacted] since 2007, barriers to entry and expansion in the market alleged by the FTC are low. The Commission contradicts itself by alleging that barriers to entry are high, while admitting that Westcliff was easily and successfully able to expand from doing only fee-for-service business to offering capitated contracts. To the extent the Commission believes that Westcliff was a successful entrant, multiple clinical and pathology laboratories in Southern California are in the same position that Westcliff was before it began serving physician groups under capitated contracts. They are poised to begin competing for capitated business particularly because of the potential for increased lucrative discretionary fee-for-service business that they might receive. [redacted]. Offering capitated contracts does not require any specialized equipment, facilities, or scale. The tests are exactly the same whether the payment method is capitated or fee-for-service. In addition, establishing a network of patient service centers to serve an IPA is as easy as renting a room with running water. Existing laboratories (as well as new ones) easily can offer capitated contracts.

LabCorp estimated [redacted] in recurring, annual efficiencies from the $57 million acquisition. These efficiencies are to be achieved in large part by [redacted]

[redacted]. While the anticipated efficiencies that would have occurred over the past six months have been delayed and can never be recouped, the efficiency gains still exist and can be captured in the future if this acquisition is allowed to proceed. In addition, as mentioned above, customers will immediately achieve [redacted] annually in quantifiable cost savings as a result of moving from higher-priced Westcliff contracts to existing LabCorp contracts. These efficiencies far outweigh the mythical anticompetitive price increases that the FTC claims will result from the acquisition.

The FTC's Complaint fails as a matter of law. The FTC's structural case does not create a presumption of anticompetitive effects because the market shares and market concentration levels alleged in the Complaint are inadequate to support such a presumption. And in any event, the alleged relevant market does not reflect the realities of competition for clinical lab services in California. The FTC also has ignored empirical evidence that LabCorp and Westcliff are not close competitors and that LabCorp will be unable to increase prices post-acquisition. Instead, the FTC has cherry-picked portions of a handful of documents from LabCorp employees *who have no authority to set prices* to allege absurdly that the acquisition will result in price increases. Robust competition with Quest kept capitated rates at just above marginal cost both before and after Westcliff's entry; such competition will keep capitated rates low after this acquisition is complete. There is no reason to suspect that the acquisition creates an increased risk of coordination: Westcliff was no "maverick" – [redacted] – and the threat of entry and expansion by new or existing clinical laboratories will easily counter any potential anticompetitive effects from the acquisition. Westcliff was (and continues to be) a failing, bankrupt firm. LabCorp's acquisition of Westcliff will take those failing assets and turn them into real efficiencies and cost savings for consumers that

dramatically outweigh any potential harm the FTC has alleged (even assuming the FTC could prove its allegations). This acquisition will do nothing but increase the intense competition among clinical laboratories that provide lab services to physicians in California.

RESPONSES TO THE FTC'S ALLEGATIONS

The FTC's unnumbered introductory paragraph contains only legal conclusions to which no response is necessary. To the extent a response is required, LabCorp denies the allegations of the introductory paragraph.

SUMMARY

1. LabCorp denies the allegations in Paragraph 1.

2. LabCorp denies the allegations in the final sentence of paragraph 2. LabCorp admits the remaining allegations in Paragraph 2.

3. LabCorp lacks knowledge or information sufficient to admit or deny the allegation in the first sentence of Paragraph 3. LabCorp denies all remaining allegations of Paragraph 3.

4. LabCorp denies the allegations in Paragraph 4.

5. LabCorp denies the allegations in Paragraph 5.

THE RESPONDENT

6. LabCorp admits the allegations in Paragraph 6.

7. LabCorp admits the allegations in Paragraph 7, except to the extent that Paragraph 7 contains legal conclusions to which no response is required.

THE ACQUISITION

8. LabCorp admits that LabWest, Inc. (formerly known as Wave NewCo) entered into an Asset Purchase Agreement dated May 17, 2010, with Westcliff Medical Laboratories, Inc.

and BioLabs, Inc. in which Westcliff agreed to sell substantially all of its business assets to LabWest, Inc. for $57.5 million. The Asset Purchase Agreement speaks for itself. LabCorp denies the remaining allegations in Paragraph 8.

THE RELEVANT MARKET

9. LabCorp admits the allegations in the third sentence of Paragraph 9. LabCorp admits that the FTC has defined the term "Physician group" as set forth in the fourth sentence of Paragraph 9. LabCorp denies the remaining allegations in Paragraph 9.

10. LabCorp admits the allegations in Paragraph 10.

11. LabCorp lacks knowledge or information sufficient to admit or deny the allegation in the first sentence of Paragraph 11. LabCorp denies all remaining allegations of Paragraph 11.

12. LabCorp denies the allegations in Paragraph 12.

13. LabCorp denies the allegations in Paragraph 13.

14. LabCorp lacks knowledge or information sufficient to admit or deny the allegation in the fourth sentence of Paragraph 14. LabCorp denies the remaining allegations in Paragraph 14.

15. LabCorp admits that LabCorp, Westcliff, and Quest, among others, serve physician groups in the region defined by the Complaint as Southern California. LabCorp denies the remaining allegations in Paragraph 15.

MARKET STRUCTURE

16. LabCorp admits that it is the second-largest independent clinical laboratory in the United States with total 2009 revenues of $4.69 billion, of which [redacted] was derived

from its operations in the region that the Complaint defines as Southern California. LabCorp further admits that it has a network of 104 patient service centers and six STAT laboratories in Southern California and has capitated contracts with [redacted] physician groups in Southern California covering nearly [redacted] patient lives. LabCorp further admits that capitated business represents [redacted] percent of its Southern California revenues and [redacted] percent of its Southern California accessions. LabCorp denies the remaining allegations of Paragraph 16.

17. LabCorp admits that Westcliff had approximately $97.3 million in total revenues in 2009, including approximately [redacted] derived from its Southern California operations. LabCorp further admits that, prior to the acquisition, Westcliff had a network of over 140 patient service centers and six STAT laboratories in Southern California, that Westcliff has capitated contracts that cover [redacted] physician groups in Southern California covering nearly [redacted] patient lives, and that Westcliff's capitated business in 2009 represented [redacted] percent of its Southern California revenues and [redacted] percent of its Southern California accessions. LabCorp denies the remaining allegations in Paragraph 17.

18. LabCorp admits that Quest has a substantial share of clinical laboratory testing services in Southern California. LabCorp lacks knowledge or information sufficient to admit or deny the remaining allegations in Paragraph 18.

19. LabCorp admits that Westcliff had [redacted] capitated contracts in 2007 and has [redacted] capitated contracts in 2010. LabCorp denies the remaining allegations in Paragraph 19.

20. LabCorp admits that American Medical Analysis Laboratory and Consolidated Medical Bio-analysis, among others, compete for capitated contracts in Southern California. LabCorp denies the remaining allegations in Paragraph 20.

21. The allegation that the alleged "post-merger market concentration, as well as the increase in concentration produced by the Acquisition, is well above the range where a transaction is presumed to produce anticompetitive effects" is a legal conclusion to which no response is necessary. LabCorp denies the remaining allegations in Paragraph 21.

22. LabCorp admits that Westcliff had [redacted] capitated contracts in 2007 and has [redacted] capitated contracts in 2010. LabCorp further admits that LabCorp has won [redacted] capitated contracts in the region the Complaint defines as Southern California during the period May 2007 to October 2010. LabCorp denies the remaining allegations in Paragraph 22.

23. LabCorp denies the allegations in Paragraph 23.

ANTICOMPETITIVE EFFECTS

24. LabCorp admits that the statements quoted in Paragraph 24 were made in documents produced to the FTC. The documents speak for themselves. To the extent the FTC alleges the quoted statements are admissions by LabCorp, they are denied. LabCorp denies the remaining allegations in Paragraph 24.

25. LabCorp admits that the statement quoted in Paragraph 25 was made in a document submitted to the FTC. The document speaks for itself. To the extent the FTC alleges the quoted statement is an admissions by LabCorp, it is denied. LabCorp denies the remaining allegations in Paragraph 25.

26. LabCorp admits that the statements quoted in Paragraph 26 were made in documents submitted to the FTC, except that LabCorp denies that any of the quoted documents contain the statement [redacted] LabCorp admits that the document designated PX 1143 by the FTC contains the statement [redacted]

[redacted] In all other respects, the documents from which the statements are taken speak for themselves. To the extent the FTC alleges the quoted statements are admissions by LabCorp, they are denied. LabCorp denies the remaining allegations in Paragraph 26.

27. The second sentence of paragraph 27 is a legal conclusion to which no response is required. LabCorp denies the remaining allegations in Paragraph 27.

28. LabCorp admits that the statements quoted in Paragraph 28 were made in documents produced to the FTC, except that LabCorp denies that the statement contained in the fifth sentence of Paragraph 28 contains the word "higher" therefore the insertion of the word "higher" by the FTC is inappropriate. The documents from which these statements were taken speak for themselves. To the extent the FTC alleges the quoted statements are admissions by LabCorp, they are denied. LabCorp denies the remaining allegations in Paragraph 28.

BARRIERS TO ENTRY AND EXPANSION

29. LabCorp denies the allegations in Paragraph 29.

30. LabCorp admits that the statements quoted in Paragraph 30 were made in a document submitted to the FTC. The document from which the statements were taken speaks for itself. To the extent the FTC alleges the quoted statements are admissions by LabCorp, they are denied. LabCorp denies the remaining allegations in Paragraph 30.

31. LabCorp denies first sentence of Paragraph 31. LabCorp lacks knowledge or information sufficient to admit or deny the remaining allegations in Paragraph 31.

32. LabCorp denies first sentence of Paragraph 32. LabCorp lacks knowledge or information sufficient to admit or deny the remaining allegations in Paragraph 32.

33. LabCorp lacks knowledge or information sufficient to admit or deny the allegations in the first and second sentences of Paragraph 33. LabCorp denies the remaining allegations in Paragraph 33.

34. LabCorp lacks knowledge or information sufficient to admit or deny the allegations in the first and second sentences of Paragraph 34. LabCorp denies the remaining allegations in Paragraph 34, except that the reference to "competitive requirement in the relevant market" contained in the final sentence of Paragraph 34 is a legal conclusion to which no response is necessary. To the extent a response is required, that allegation is denied

35. LabCorp admits the allegation in the second sentence of Paragraph 35. LabCorp further admits that the current Medi-Cal moratorium is scheduled to expire on January 26, 2011. LabCorp lacks knowledge or information sufficient to admit or deny that the moratorium has been regularly renewed. LabCorp denies the remaining allegations in Paragraph 35.

36. LabCorp denies the allegations in Paragraph 36.

EFFICIENCIES

37. LabCorp denies the allegations in Paragraph 37.

FAILING FIRM

38. The allegations in Paragraph 38 are legal conclusions to which no response is necessary. To the extent a response is required, those allegations are denied.

39. LabCorp denies the allegations in Paragraph 39.

40. The first sentence of Paragraph 40 is a legal conclusion to which no response is necessary. To the extent a response is required, that allegation is denied. LabCorp denies the remaining allegations in Paragraph 40.

41. LabCorp denies the allegations in Paragraph 41.

VIOLATIONS

42. Except as where specifically admitted above, the allegations contained in paragraphs 1-41 of the Complaint are denied.

43. The allegations in Paragraph 43 are legal conclusions to which no response is necessary. To the extent a response is required, those allegations are denied.

44. Except as where specifically admitted above, the allegations contained in paragraphs 1-41 of the Complaint are denied.

45. The allegations in Paragraph 45 are legal conclusions to which no response is necessary. To the extent a response is required, those allegations are denied.

NOTICE OF CONTEMPLATED RELIEF

LabCorp denies that any of the relief set forth in the Complaint's Notice of Contemplated Relief, or the subparts thereto, is justified by fact, law, or equity.

AFFIRMATIVE DEFENSES

The inclusion of any ground within this section does not constitute an admission that LabCorp bears the burden of proof on each or any of the matters, nor does it excuse Complaint counsel from establishing each element of its purported claim for relief.

1. The Complaint fails to state a claim on which relief can be granted.

2. The contemplated relief would not be in the public interest because it would, among other things, harm consumers.

3. Efficiencies and other pro-competitive benefits resulting from the acquisition outweigh any and all proffered anticompetitive effects.

4. At the time of the acquisition, Westcliff was a failing firm. Westcliff faced the imminent prospect of business failure, and it could not have been restructured as a going concern,

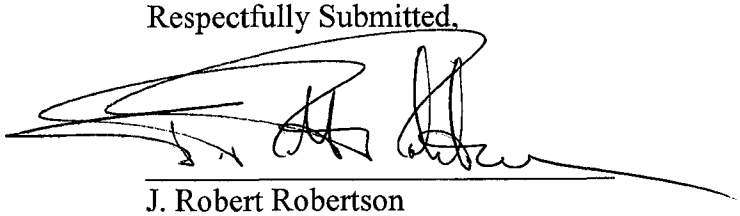
as an independent laboratory under Chapter 11. The sale to LabCorp (through its subsidiary LabWest, Inc.) was the only means to prevent Westcliff's failing assets from exiting the marketplace. Westcliff diligently explored dozens of other potential purchasers, but in light of Westcliff's severe and deteriorating situation prior to the acquisition, the risk, uncertainty, and delay inherent in the terms contemplated by the other potential purchasers would have prevented Westcliff from remaining a viable business. On information and belief, no other bid would have resulted in a sale that would have put Westcliff in a position that would have increased competition substantially more than the challenged acquisition in any meaningful sense, in any relevant market, or would have resulted in any lower prices or better service than would be achieved by the challenged acquisition. Indeed, the challenged acquisition would lead to greater competition between LabCorp and Quest and others than any of the hypothetical acquisitions that the FTC claims might have occurred.

5. LabCorp reserves the right to assert any other defenses as they become known to LabCorp.

WHEREFORE, respondents Laboratory Corporation of America and Laboratory Corporation of America Holdings respectfully request that the Court (i) deny the FTC's contemplated relief, (ii) dismiss the Complaint in its entirety with prejudice, (iii) award respondents their costs of suit, including attorneys' fees, and (iv) award such other and further relief as the Court may deem proper.

Dated: December 16, 2010

Respectfully Submitted,



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CERTIFICATE OF SERVICE

I hereby certify that I caused to be filed via hand delivery an original with signature and one paper copy, and via electronic mail a .PDF copy that is a true and correct copy of the paper original of the foregoing ***Public Answer of Respondents Laboratory Corporation of America and Laboratory Corporation of America Holdings*** with:

Donald S. Clark
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I also certify that I caused to be delivered by hand delivery and electronic mail a copy of the foregoing ***Public Answer of Respondents Laboratory Corporation of America and Laboratory Corporation of America Holdings*** to:

D. Michael Chappell
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I also certify I delivered via electronic mail a copy of the foregoing ***Public Answer of Respondents Laboratory Corporation of America and Laboratory Corporation of America Holdings*** to:

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Date: December 16, 2010

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