

# **FEDERAL TRADE COMMISSION DECISIONS**

**FINDINGS, OPINIONS, AND ORDERS  
JULY 1, 2005 TO DECEMBER 31, 2005**

PUBLISHED BY THE COMMISSION

**VOLUME 140**



Compiled by  
The Office of the Secretary  
Ami Joy Rop, Editor

**MEMBERS OF THE FEDERAL TRADE COMMISSION**  
**DURING THE PERIOD JULY 1, 2005 TO DECEMBER 31, 2005**

DEBORAH PLATT MAJORAS, *Chairman*  
Took oath of office August 16, 2004.

THOMAS B. LEARY, *Commissioner\**  
Took oath of office November 17, 1999.

PAMELA JONES HARBOUR, *Commissioner*  
Took oath of office August 4, 2003.

JON LEIBOWITZ, *Commissioner*  
Took oath of office September 3, 2004.

DONALD S. CLARK, *Secretary*  
Appointed August 28, 1988.

\*Resigned, effective December 31, 2005

## CONTENTS

---

	<b>Page</b>
Members of the Commission .....	II
Table of Cases .....	III
Findings, Opinions, and Orders .....	1
Orders .....	1125
Advisory Opinion .....	1186
Response to Petitions to Quash .....	1195

## TABLE OF CASES

---

<b>Dkt. No.</b>	<b>Name</b>	<b>Page</b>
C-4147	Advertising.com, Inc. doing business as, Teknosurf.com, and John Ferber . . . . .	220
C-4148	BJ's Wholesale Club, Inc. . . . .	465
C-4144	Chevron Corporation, et al. . . . .	100
C-4146	Cytodyne, Llc, Evergood Products Corp., and Melvin L. Rich . . . . .	191
C-4152	Davita Inc. . . . .	609
C-4154	Johnson & Johnson . . . . .	1062
9312	North Texas Specialty Physicians . . . . .	715
C-4150	Novartis AG . . . . .	480
C-4139	Occidental Petroleum Corporation and Vulcan Materials Company . . . . .	1
C-4149	Partners Health Network, Inc. . . . .	244
C-4143	Penn National Gaming, Inc. . . . .	540
C-4151	Procter & Gamble Company, The and the Gillette Company, . . . . .	944
C-4153	Superior Mortgage Corp. . . . .	926
9313	Telebrands Corp., TV Savings, LLC, and Ajit Khubani . . . . .	278
C-4145	Tropicana Products, Inc. . . . .	176
9305	Union Oil Company of California . . . . .	123

C-4141	Valero L.P., et al. . . . .	40
--------	-----------------------------	----

**ORDERS**

9300	Chicago Bridge & Iron Company N.V. Order Approving Respondents' Application for Approval of Monitor Trustee and Monitor Trustee Agreement . . .	1137
	Order Granting in Part and Denying in Part Respondents' Motion for <i>in Camera</i> Treatment of Material Previously Designated as Confidential . . . . .	1152
	Order Clarifying Respondents' Obligations as to the Pitt- Des Moines and CB&I Corporate Names . . . . .	1155
	Order Granting in Part and Denying in Part Respondents' Petition for Reconsideration of the Final Order . . . . .	1161
C-3998	Entergy Corporation Order Reopening and Setting Aside Order . . . . .	1125
9315	Evanston Northwestern Healthcare Corporation Order Granting in Part and Denying in Part Joint Motion for Extension of Time and Length of Appeal Briefs . . . .	1179
	Order Granting Expedited Motion and Permitting Enlargement of Lengths of Appeal Briefs . . . . .	1183
9309	Kentucky Household Goods Carriers Association, Inc. Order Denying Respondent's Motion for Reconsideration or, in the Alternative, for a Stay of Final Order Pending Review by U.S. Court of Appeals . . . . .	1142
C-4082	Nestlé Holdings, Inc. Order Reopening and Modifying Order . . . . .	1130
9302	Rambus Incorporated Order Reopening the Record to Admit into Evidence the Supplemental Evidence Filed by the Parties in Accordance with the Provisions of the Commission's Order of May 13, 2005, as Amended, and Directing Briefing of Issues Related to Such Supplemental Evidence . . . . .	1138

Order Denying Complaint Counsel’s Petition to Modify  
the Schedule in the Commission’s July 20, 2005 Order . 1140

C-4130 White Sands Health Care System, L.L.C.  
Order Reopening and Modifying Order . . . . . 1174

**ADVISORY OPINIONS**

Funeral Rule, 16 C.F.R. § 453.1(b) . . . . . 1186

**PETITIONS TO QUASH**

0510131 Aloha Petroleum, Ltd. . . . . 1195

0523092 BlueHippo Funding, LLC . . . . . 1214

0323237 Garden of Life, Inc. . . . . 1200

0523182 Voice Mail Broadcasting Corp. . . . . 1210

0423127 Wingard , Steve . . . . . 1201

Complaint

IN THE MATTER OF

**OCCIDENTAL PETROLEUM CORPORATION AND  
VULCAN MATERIALS COMPANY**

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

*Docket C-4139; File No. 0510009  
Complaint, July 13, 2005--Decision, July 13, 2005*

This consent order addresses the acquisition by Respondent Occidental Chemical Company of the chemical assets of Respondent Vulcan Materials Company. The order, among other things, requires the respondents to divest a facility owned by Vulcan in Port Edwards, Wisconsin -- and assets relating to the research, development, marketing, sales, and production of chemicals produced at that facility, including chlorine, caustic soda (sodium hydroxide), KOH (potassium hydroxide), APC (anhydrous potassium carbonate), and hydrochloric acid ("Port Edwards business") -- to ERCO Worldwide ("ERCO") or to another buyer approved by the Commission. An accompanying Order to Maintain Assets requires the respondents to preserve the Port Edwards business as a viable, competitive, and ongoing operation until the divestiture is achieved.

*Participants*

For the Commission: *John B. Warden, Susan Huber, Wallace W. Easterling, Kristina Martin, April Tabor, Eric D. Rohlck, Jacqueline Tapp, Sara S. Brown, Ria M. Williams, Michael H. Knight, Daniel P. Ducore, Louis Silvia, and Mark Frankena.*

For the Respondent: *Deborah L. Feinstein and Mark R. Merley, Arnold & Porter LLP and Joseph P. Larson, Wachtell, Lipton, Rosen & Katz.*

**COMPLAINT**

Pursuant to the Federal Trade Commission Act and the Clayton Act, and by virtue of the authority vested in it by said Acts, the Federal Trade Commission ("Commission"), having reason to believe that Occidental Petroleum Corporation, a corporation subject to the jurisdiction of the Commission, has entered into an agreement

## Complaint

to acquire the chemicals business of Vulcan Materials Company, a corporation subject to the jurisdiction of the Commission, and that the acquisition, if consummated, would result in a violation of Section 5 of the Federal Trade Commission Act, 15 U.S.C. § 45, and Section 7 of the Clayton Act, 15 U.S.C. § 18, and it appearing to the Commission that a proceeding in respect thereof would be in the public interest, hereby issues its complaint, stating its charges as follows:

## A. THE RESPONDENTS

1. Respondent Occidental Petroleum Corporation (“Occidental”) is a corporation organized, existing, and doing business under and by virtue of the laws of the State of Delaware with its headquarters and principal place of business at 10889 Wilshire Boulevard, Los Angeles, CA. It is the parent company of Occidental Chemical Corporation (“OxyChem”), whose headquarters and principal place of business is located at Occidental Tower, 5005 LBJ Freeway, Dallas, Texas 75244.

2. Occidental, through its subsidiary OxyChem, owns and operates eight U.S. chloralkali plants and holds a 76 percent interest in OxyVinyls LP which has two additional U.S. chloralkali plants. The large majority of chloralkali plants produce chlorine and caustic soda (sodium hydroxide or NaOH); however, some chloralkali facilities produce chlorine and KOH (potassium hydroxide or caustic potash). OxyChem produces KOH at its chloralkali facilities in Delaware City, Delaware; Mobile, Alabama; and Muscle Shoals, Alabama. OxyChem is the largest producer of KOH in the United States.

3. OxyChem owns 50 percent of Armand Products Company (“Armand”), a joint venture with Church & Dwight. Armand produces potassium carbonate (“potcarb”) and potassium bicarbonate at a facility in Muscle Shoals, Alabama that is operated by OxyChem and located next to OxyChem’s Muscle Shoals chloralkali facility. Armand is the largest producer of potcarb in the



Complaint

United States. Most of Armand's production is of the solid form of potcarb, known as APC or anhydrous potassium carbonate.

4. Respondent Occidental is, and at all times relevant herein has been, engaged in commerce, as "commerce" is defined in Section 1 of the Clayton Act, 15 U.S.C. § 12, and is a corporation whose business is in or affecting commerce as "commerce" is defined in Section 4 of the Federal Trade Commission Act, 15 U.S.C. § 44.

5. Respondent Vulcan Materials Company ("Vulcan") is a corporation organized, existing, and doing business under and by virtue of the laws of the State of New Jersey, with its headquarters and principal place of business located at 1200 Urban Center Drive, Birmingham, Alabama 35242.

6. Respondent Vulcan's chemicals business consists of three chloralkali plants and related assets. Vulcan's plants are located in Port Edwards, Wisconsin; Geismar, Louisiana; and Wichita, Kansas. In addition, Vulcan and Mitsui & Co. Ltd. are joint venture partners in a second chloralkali plant and an ethylene dichloride plant in Geismar, Louisiana. Vulcan produces KOH and potcarb at its Port Edwards, Wisconsin facility and sells these chemicals to customers in the United States. Vulcan produces the second largest volume of potassium hydroxide and potassium carbonate in the United States.

7. Respondent Vulcan is, and at all times relevant herein has been, engaged in commerce, as "commerce" is defined in Section 1 of the Clayton Act, 15 U.S.C. § 12, and is a corporation whose business is in or affecting commerce as "commerce" is defined in Section 4 of the Federal Trade Commission Act, 15 U.S.C. § 44.

## B. THE PROPOSED TRANSACTION

8. On October 12, 2004, Respondents announced that they had entered into an agreement whereby Occidental, through its subsidiary OxyChem, would purchase Vulcan's chemical business, including Vulcan's three plants and related transportation and distribution assets and assume certain liabilities. Included in the transaction is

## Complaint

the Vulcan-Mitsui joint venture at Geismar. The purchase price is \$214 million plus certain contingent future payments, projected to equal approximately \$145 million. Throughout this Complaint this transaction is referred to as “the proposed transaction.”

## C. THE RELEVANT MARKETS

9. For the purposes of this Complaint, the relevant product markets in which to analyze the effects of the proposed transaction are research, marketing, manufacture, and sale of (1) potassium hydroxide (also known as KOH); (2) potcarb; and (3) anhydrous potassium carbonate or APC.

10. KOH is a chemical made by the electrolytic decomposition of potassium chloride brine into chlorine and KOH. It is the most commonly used intermediate form in which inorganic potassium chemicals are manufactured. KOH is the raw material for the production of many potassium chemicals, such as potassium carbonate, potassium permanganate, citrate, acetate, cyanide, benzoate, iodide, and sorbate.

11. Potcarb is the highest volume potassium chemical produced using KOH. It is produced through the carbonation of KOH. End uses for potcarb include nutrition supplements for dairy cattle, video glass for television and computer monitors, other specialty glass, potassium silicates, fertilizers, gas processing, industrial intermediaries, photographic development processes, detergents, and food products.

12. Potcarb can be produced in liquid or solid form. The solid form is known as anhydrous potassium carbonate or APC. The majority of total potcarb production in the United States is of APC. APC requires a more sophisticated production process and greater capital investment than does liquid potcarb production. Most APC users cannot economically substitute liquid potcarb for APC.

13. The relevant geographic market in which to assess the impact of the proposed acquisition is no broader than the United States.

Complaint

Competition is national in scope, with U.S. producers of the relevant products marketing and selling their products to customers throughout the United States. Imports of the relevant products are limited. The potential for increased imports is limited by transportation costs and by customer requirements for security and timeliness of supply.

D. MARKET STRUCTURE

a. KOH

14. The market for KOH is highly concentrated. In 2004, there were three producers of KOH in the United States: OxyChem, Vulcan, and ASHTA Chemicals (“ASHTA”). In that year, production by OxyChem and Vulcan accounted for over 80% of total U.S. production and capacity.

15. In 2005, Olin Corp. entered the domestic KOH market. Olin partially converted half of its chloralkali facility in Tennessee to be able to produce either KOH or caustic soda. With the addition of Olin’s KOH capacity, the combined KOH capacity of OxyChem and Vulcan is approximately 70% of total U.S. capacity. It is expected that Olin’s production in 2005 will represent a small portion of total U.S. production.

16. As measured by capacity, including Olin, the proposed transaction would increase the Herfindahl-Hirschman Index (“HHI”) of concentration in domestic KOH by over 1300 points to over 5000.

b. PotCarb

17. The market for potcarb is highly concentrated. There are four producers of potcarb in the United States: Armand, Vulcan, ASHTA, and Na-Churs/Alpine Solutions. ASHTA and Na-Churs produce only liquid potcarb. Armand and Vulcan together accounted the great majority of potcarb produced in the United States in 2004 and controlled over 80% of total capacity. Imports of potcarb account for less than 2% of total potcarb sales.

## Complaint

18. If the proposed transaction is consummated, OxyChem will own the potcarb production assets of Vulcan. Because of the relationship between Armand and OxyChem, they are not independent competitors and their capacity and production are considered jointly for concentration analysis.

19. The proposed transaction would increase the HHI for potcarb, as measured by capacity, by over 1800 points to a postmerger HHI of over 7000 points.

c. APC

20. The market for APC is very highly concentrated. Armand and Vulcan are the only two producers of APC in the United States. Together they accounted for all of the APC produced and over 95% of the APC sold in the United States. ASHTA also owns a facility that can produce APC; however, the company idled the facility at the end of 2002.

21. For APC, the proposed transaction would increase the HHI for production to 10,000 points, an increase of over 2000 points. Taking into account the available capacity of ASHTA's idled APC facility, the transaction would result in an HHI of over 8500 and an increase of over 2000 points.

## E. COMPETITION

22. KOH and potcarb are commodity products. The majority of customers have no preference based on product composition for KOH or potcarb from a particular manufacturer, although customers may require products of differing granularity.

23. OxyChem and Vulcan are direct competitors in the sale of KOH in the United States. Many KOH customers obtain bids or quotes from both companies and use competition between them to obtain better pricing.

Complaint

24. OxyChem, through Armand, and Vulcan are direct competitors in the sale of potcarb and APC in the United States. The companies compete with one another to supply customers with potcarb and APC, often participating in competitive bidding processes to be a particular customer's supplier of potcarb and/or APC.

F. ENTRY CONDITIONS

25. New entry will not be timely, likely, or sufficient to constrain OxyChem from exercising market power if the proposed transaction is consummated. To constrain OxyChem sufficiently, entry or expansion would have to be of a size and scope that would replicate the competitive impact of Vulcan.

26. New entry will not be timely, likely, or sufficient in the KOH market. Prior to Olin's entry into the KOH market in 2005, the most recent entrant into the KOH market had been Vulcan, which entered the market in the mid-1980s, also through conversion of caustic soda capacity at an existing chloralkali plant. Only caustic soda production facilities using mercury cell or membrane technology are suitable for conversion to KOH for the U.S. market. These production technologies account for less than 35% of U.S. caustic soda capability and a number of plants are too large to be viably converted to KOH production for the smaller KOH market. There are at least two caustic soda manufacturers with facilities theoretically suitable for conversion, in whole or part, to the production of KOH; however, it is unlikely that either of these would enter the KOH market, even if KOH pricing increases a small but significant amount as a result of the proposed transaction. *De novo* construction of a KOH facility is extremely unlikely and would not be timely. It would require a significant capital expenditure and take over two years to complete.

27. Entry into the potcarb market will not be timely, likely, or sufficient. The vast majority of potcarb customers in the U.S. require APC, the solid form of potcarb; therefore, a new producer of liquid potcarb would not be sufficient to replace the competition lost

## Complaint

by the exit of Vulcan as a result of the proposed transaction. It is very unlikely a manufacturer without its own source of KOH would find it economically viable to invest in an APC production facility and compete with manufacturers with internal sources of product.

28. Market conditions in the potcarb market are not conducive to additional APC entry. There is excess APC capacity in the United States due to a decrease in demand over the past several years. Further, available KCl for use in KOH production is extremely tight due to increasing demand in the agricultural market and it is unlikely that increased supplies will be available at least over the next 12 to 24 months. Given the current market conditions and other factors, it is unlikely that either Olin or ASHTA would find it economically viable to enter the APC market within the next two years, even in response to a small but significant increase in price. Further, unless Olin were to make the decision to enter relatively quickly, its putative entry would not be timely as it can take up to 2 years to construct an APC facility.

## G. EFFECTS OF THE PROPOSED ACQUISITION

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

- a. It will substantially increase concentration in the markets for KOH, potcarb and APC;
- b. It will eliminate Vulcan as the most significant competitor in the KOH market and the only significant competitor in the potcarb and APC markets; and
- c. It will lead to a reduction in competition and an increase in the likelihood that OxyChem and Armand will increase prices in the markets for KOH, potcarb, and APC.

Complaint

H. VIOLATIONS CHARGED

30. The proposed transaction between Occidental and Vulcan violates Section 5 of the Federal Trade Commission Act, as amended, 15 U.S.C. § 45.

31. The proposed transaction between Occidental and Vulcan, 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.

WHEREFORE, THE PREMISES CONSIDERED, the Federal Trade Commission on this 13<sup>th</sup> day of July, 2005, issues its Complaint against said Respondents.

Decision and Order

**DECISION AND ORDER**

The Federal Trade Commission (“Commission”) having initiated an investigation of the proposed acquisition by Respondent Occidental Petroleum Corporation, hereinafter referred to as “Respondent Oxy,” of three chemical plants and related assets from Vulcan Chloralkali, LLC and Vulcan Materials Company, hereinafter collectively referred to as “Respondent Vulcan,” and Respondent Oxy and Respondent Vulcan (“Respondents”) having been furnished thereafter with a draft of Complaint that the Bureau of Competition proposed to present to the Commission for its consideration and that, if issued by the Commission, would charge Respondents with violations of Section 7 of the Clayton Act, as amended, 15 U.S.C. § 18, and Section 5 of the Federal Trade Commission Act, as amended, 15 U.S.C. § 45; and

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

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



Decision and Order

Decision and Order (“Order”):

1. Respondent Occidental Petroleum Corporation is a publicly traded company, organized, existing and doing business under and by virtue of the laws of the State of Delaware, with its office and principal place of business located at 10889 Wilshire Boulevard, Los Angeles, California 90024-4201.

2. Respondent Vulcan Materials Company is a publicly traded company, organized, existing and doing business under and by virtue of the laws of the State of New Jersey with its office and principal place of business located at 1200 Urban Center Dr., Birmingham AL 35242.

3. The Federal Trade Commission has jurisdiction of the subject matter of this proceeding and of Respondents, and the proceeding is in the public interest.

4. ERCO Worldwide (USA) Inc. is a company organized, existing, and doing business under and by virtue of the laws of Delaware, with its office and principal place of business located at 302 The East Mall, Suite 200, Toronto, Ontario, Canada, M9B 6C7, and is a subsidiary of Superior Holdings (USA) Inc., which is a subsidiary of Superior Plus, Inc. (a Canadian company).

**ORDER**

**I.**

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

- A. “Respondent Oxy” or “Oxy” means Occidental Petroleum Corporation, a corporation, its directors, officers, employees, agents, attorneys, representatives, predecessors, successors, and assigns; its joint ventures, including Armand Products Company, subsidiaries, including Occidental Chemical Corporation (“OxyChem”) and Basic Chemicals Company, LLC, divisions, groups and affiliates controlled by Occidental Petroleum Corporation, and the respective directors, officers, employees, agents, attorneys, representatives, predecessors, successors, and assigns of each.

## Decision and Order

- B. “Respondent Vulcan” or “Vulcan” means Vulcan Materials Company, a corporation, its directors, officers, employees, agents, attorneys, representatives, predecessors, successors, and assigns; its joint ventures, including Vulcan Chloralkali LLC, subsidiaries, divisions, groups and affiliates controlled by Vulcan Materials Company, and the respective directors, officers, employees, agents, attorneys, representatives, predecessors, successors, and assigns of each.
- C. “ERCO” means ERCO Worldwide (USA) Inc., a corporation organized and doing business under the laws Delaware, with its executive offices at 302 The East Mall, Suite 200, Toronto, Ontario, Canada, M9B 6C7, and which is a subsidiary of Superior Holdings (USA) Inc. which is a subsidiary of Superior Plus, Inc. (a Canadian company).
- D. “Commission” means the Federal Trade Commission.
- E. “Acquirer” means either ERCO or any other entity that receives the prior approval of the Commission to acquire the Port Edwards Assets pursuant to Paragraphs II or V of this Order.
- F. “Acquisition” means the proposed acquisition by Respondent Oxy of three chloralkali plants and related assets in Geismar, Louisiana, Port Edwards, Wisconsin, and Wichita, Kansas, from Vulcan pursuant to and as described in the Asset Purchase Agreement dated October 11, 2004, between Basic Chemicals Company, LLC, and Vulcan.
- G. “Acquisition Date” means the date the Acquisition is consummated.
- H. “Assigned Contract Customer” means a KOH or potassium carbonate customer of the Acquirer whose contract was assigned as a part of the Divestiture Agreement and is listed in Confidential Appendix C.
- I. “Confidential Business Information” means all information that is not in the public domain related to research, development, manufacture, marketing, commercialization, distribution, importation, cost, pricing, supply, sales, sales support, or use of the particular assets.
- J. “Divestiture Agreement” means either the ERCO Acquisition Agreement or any other agreement that receives the prior approval of the Commission between Respondents

Decision and Order

and an Acquirer (or between a Divestiture Trustee and an Acquirer), as well as all amendments, exhibits, attachments, agreements, and schedules thereto, related to the divestiture of the Port Edwards Assets pursuant to Paragraphs II or V of this Order.

- K. “Divestiture Trustee” means any trustee appointed by the Commission pursuant to Paragraph V of this Order.
- L. “Designated Vulcan Staff” means those persons, or persons filling the positions, identified in Confidential Appendix A to this Order.
- M. “Dual Contract Customer” means an Assigned Contract Customer who, at the time this Order is issued, is supplied either KOH or potassium carbonate, by contract or otherwise, by Respondent Oxy and is listed in Confidential Appendix C.
- N. “ERCO Acquisition Agreement” means the April 11, 2005, Asset Purchase and Sale Agreement, with amendments, attachments, exhibits, and schedules, between Basic Chemicals Company, LLC, and ERCO Worldwide (USA) Inc. attached as Confidential Appendix B to this Order.
- O. “Effective Date of Divestiture” means the date on which Respondents (or a Divestiture Trustee) divests to the Acquirer the Port Edwards Business completely and as required by Paragraphs II or V of this Order.
- P. “Governmental Entity” means any Federal, state, local or non-U.S. government or any court, legislature, governmental agency or governmental commission or any judicial or regulatory authority of any government.
- Q. “Person” means any individual, partnership, association, company or corporation.
- R. “Port Edwards Assets” means the chlorine, KOH (potassium hydroxide), caustic soda (sodium hydroxide), hydrochloric acid, and potassium carbonate manufacturing facility, located at 100 State Highway 73, Port Edwards, Wisconsin, 54469, and includes:
  - 1. all tangible and real assets used in the operation of the facility, including any leasehold, ownership, fee, or any other interest in real estate at the facility grounds in Port Edwards, Wisconsin, and in the production or

## Decision and Order

- distribution of the products produced at the facility, and includes, but is not limited to,
- a. the main plants;
  - b. rail cars, trucks, and other vehicles owned by Respondents related to the transportation and distribution of products produced or used in the facility; and
  - c. raw materials, work-in-process inventories, stores and spares, inventories, packaging materials, finished goods inventories, finished goods in transit to offsite storage or to customers, and offsite inventory.
2. all books, records, and documents, including but not limited to electronically stored documents and records produced in an electronically readable form, together with all necessary instructions and software, or access to software licenses to the Acquirer, relating to the facility and to the production, marketing, distribution, or sale of products produced at the facility; *PROVIDED, HOWEVER*, that if any such books, records, or documents also include matters not related to the facility or products produced at the facility, then only those portions of the books records and documents that relate to the facility or the products produced at the facility shall be included;
  3. an exclusive right to all intellectual property used solely in the operation of the facility or in the production, marketing, distribution, or sale of the products produced at the facility, and a non-exclusive right to all other intellectual property used in the operation of the facility and in the production, marketing, distribution, or sale of the products produced at the facility;
  4. all licenses and permits used in the operation of the facility and in the production, marketing, distribution, or sale of the products produced at the facility;
  5. at the Acquirer's option, all contracts, agreements, and understandings, other than Shared Customer Contracts and Shared Terminal Contracts, relating to the manufacture, transportation, storage, terminaling, marketing, distribution, or sale of the products produced

Decision and Order

- at the facility, which includes but is not limited to:
- a. agreements under which the facility receives potassium and sodium salts, electricity, natural gas, and carbon dioxide or other inputs at or for the facility;
  - b. agreements for services provided to the facility, including, but not limited to, rail, trucking, capital maintenance, and technology;
  - c. agreements and contracts with customers for products produced exclusively by the facility;
  - d. agreements and contracts with terminals for products produced exclusively by the facility;
6. all joint ventures relating to the operation of the facility and the production, marketing, distribution, or sale of the products produced at the facility;
  7. all plans (including proposed and tentative plans, whether or not adopted), specifications, drawings, and other assets (including the non-exclusive right to use patents, know-how, and other intellectual property relating to such plans) related to the operation of the facility;
  8. existing easements and rights of way;
  9. related facilities required for the operation or the storage of products produced or used at the facility including, but not limited to, truck, rail, and pipeline facilities, including truck and rail racks, for the receipt and delivery of products produced or used at the facility;
  10. approximately 34 acres of land located at 100 State Highway 73, Port Edwards, Wisconsin, 54469, on which the Port Edwards facility sits, including the parcels described in Schedule 2.1(a) to the ERCO Acquisition Agreement;
  11. all licenses, permits, contracts, agreements, and understandings relating to the ownership and operation of the facility.
- S. "Potash Contract" means the Product Supply Agreement entered into on March 15, 2005, between PCS Sales (USA), Inc. and OxyChem for the supply of potassium chloride chicklets.

## Decision and Order

- T. “Shared Customer Contracts” means contracts under which customers receive Hydrochloric Acid, Chlorine, or Caustic Soda produced both by the Port Edwards facility and by other chemical facilities owned by Vulcan prior to the Acquisition Date that are not subject to divestiture under this order.
- U. “Shared Terminal Contracts” means contracts or agreements with terminals, including those owned by Vulcan, for storage of products produced both by the Port Edwards facility and by other chemical facilities owned by Vulcan prior to the Acquisition Date that are not subject to divestiture under this order.
- V. “Terminaling Agreement” means an agreement between the Acquirer and Respondent Oxy in which the Acquirer will use a terminal or facility owned by Respondent Oxy to store or transfer products produced by the Acquirer at the Port Edwards facility.

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

- A. Within ten (10) days after the Acquisition Date, Respondents shall divest the Port Edwards Assets in good faith to ERCO, pursuant to and in accordance with the ERCO Acquisition Agreement (which agreement shall not vary or contradict, or be construed to vary or contradict, the terms of this Order, it being understood that nothing in this Order shall be construed to reduce any rights or benefits of ERCO or to reduce any obligations of Respondents under such agreements), and such agreement, if approved by the Commission as the Divestiture Agreement, is incorporated by reference into this Order and made a part hereof as Confidential Appendix B.
- PROVIDED, HOWEVER*, at the option of the Acquirer and with approval of the Commission, Respondent Oxy may (1) agree to a long-term lease for the real estate upon which the Port Edwards facility sits, as a substitute for an acquisition of the real estate; and (2) exclude the divestiture of the groundwater collection, monitoring, and treatment systems.
- PROVIDED, FURTHER, HOWEVER*, with respect to assets

Decision and Order

that are to be divested or agreements entered into pursuant to this paragraph at the Acquirer's option, Respondents need not divest such assets or enter into such agreements only if the Acquirer chooses not to acquire such assets or enter into such agreements and the Commission approves the divestiture without such assets or agreements.

- B. If, at the time the Commission determines to make this Order final, the Commission notifies Respondents that ERCO is not an acceptable acquirer of the Port Edwards Assets or that the manner in which the divestiture was accomplished is not acceptable, then, after receipt of such written notification:
1. Respondent Oxy shall immediately notify ERCO of the notice received from the Commission and shall as soon as practicable effect the rescission of the ERCO Acquisition Agreement; and
  2. Respondents shall, within six (6) months from the date this Order becomes final, divest the Port Edwards Assets absolutely and in good faith, at no minimum price, to an acquirer that receives the prior approval of the Commission and in a manner that receives the prior approval of the Commission. *PROVIDED, HOWEVER*, at the option of the Acquirer and with approval of the Commission, Respondent Oxy may (1) agree to a long-term lease for the real estate upon which the Port Edwards facility sits, as a substitute for an acquisition of the real estate; and (2) exclude the divestiture of the groundwater collection, monitoring, and treatment systems. *PROVIDED, FURTHER, HOWEVER*, with respect to assets that are to be divested or agreements entered into pursuant to this paragraph at the Acquirer's option, Respondents need not divest such assets or enter into such agreements only if the Acquirer chooses not to acquire such assets or enter into such agreements and the Commission approves the divestiture without such assets or agreements.
  3. The Commission may appoint a Monitor pursuant to Paragraph IV of this Order to assist Respondents in:
    - a. effectuating modifications to the Divestiture

## Decision and Order

- Agreement or manner of divestiture of the Port Edwards Assets (including, but not limited to, entering into additional agreements or arrangements) as the Commission may determine are necessary to satisfy the requirements of this Order; and
- b. taking such actions as are necessary to maintain the full economic viability, marketability and competitiveness of the Port Edwards Assets, including, but not limited to, monitoring the exchange of Confidential Business Information about the Port Edwards Assets to and between Respondents, to minimize any risk of loss of competitive potential for the businesses associated with the Port Edwards Assets, and to prevent the destruction, removal, wasting, deterioration, or impairment of any of the Port Edwards Assets except for ordinary wear and tear.
- C. Any Divestiture Agreement that has been approved by the Commission between the Respondents (or a Divestiture Trustee) and an Acquirer of the Port Edwards Assets shall be deemed incorporated into this Order, and any failure by Respondents to comply with any term of such Divestiture Agreement shall constitute a failure to comply with this Order.
- D. Until the Effective Date of Divestiture, Respondents shall:
1. take such actions as are necessary to maintain the viability and marketability of the Port Edwards Assets and to prevent the destruction, removal, wasting, deterioration, or impairment of the Port Edwards Assets, except for ordinary wear and tear; and
  2. not sell, transfer, encumber or otherwise impair the full economic viability, marketability, or competitiveness of the Port Edwards Assets.
- E. No later than the Effective Date of Divestiture, Respondents shall secure all assignments, consents, and waivers, including rights of approval and rights of first refusal, from all private and Governmental Entities that are necessary for the divestiture of the Port Edwards Assets to the Acquirer.
- F. Respondent Oxy shall, no later than the Effective Date of



Decision and Order

Divestiture and as part of the Divestiture Agreement, assign the Potash Contract to the Acquirer.

- G. Respondents shall, at the option of the Acquirer, no later than the Effective Date of Divestiture, and as part of the Divestiture Agreement, enter into one or more transition agreements for the short-term provision of services provided by Respondents to the Acquirer.
- H. Respondents and Respondents's employees shall not receive, or have access to, or use or continue to use any Confidential Business Information about the Port Edwards Assets or about the production, transportation, delivery, storage, distribution, marketing, and sale of products of the Acquirer from the Port Edwards facility except:
1. As otherwise allowed in the Order to Maintain Assets or this Order;
  2. As provided for in a transition services agreement;
  3. As consented to by the Acquirer for provision to Respondent Vulcan;
  4. As required by law;
  5. To the extent that necessary information is exchanged in the course of consummating the Acquisition;
  6. In negotiating agreements to divest assets pursuant to this Order and engaging in related due diligence;
  7. In complying with this Order or the Order to Maintain Assets;
  8. To the extent necessary to allow Respondents to comply with the requirements and obligations of the laws of the United States and other countries;
  9. In defending legal claims, investigations or enforcement actions threatened or brought against or related to the Port Edwards Assets;
  10. In obtaining legal advice.
- Respondents shall require any Persons with access to Confidential Business Information to immediately enter into agreements with the Respondents and Acquirer not to disclose any Confidential Business Information to the Respondents or to any third party except for the purposes set forth this paragraph.
- I. The purposes of this Paragraph are (1) to ensure the

## Decision and Order

continuation of Port Edwards Assets as a going concern in the same manner in which it conducted business as of the date the Consent Agreement is signed, and (2) to remedy the lessening of competition resulting from the Acquisition as alleged in the Commission's Complaint.

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

- A. For Shared Customer Contracts, Respondents shall, no later than the Effective Date of Divestiture of the Port Edwards Assets and as part of the Divestiture Agreement, assign Shared Customer Contracts in whole or in part, or contribute to the Acquirer additional customer contracts held by them, or modify the Shared Customer Contracts or other customer contracts held by them, to insure that, as a result of the divestiture, the Acquirer receives:
1. customers of comparable financial strength as measured by credit rating or some other similar widely accepted measure;
  2. customers requiring delivery to locations at distances similar to or shorter than the delivery distances for products from the Port Edwards facility prior to the divestiture and consistent with the historical delivery distances for products delivered by the Port Edwards facility;
  3. customers requiring quantities similar to or exceeding the quantities of product delivered by the Port Edwards facility prior to the divestiture and consistent with historical amounts of product delivered by the Port Edwards facility; and
  4. customer contracts of similar or longer lengths of time for the products delivered by the Port Edwards facility prior to the divestiture.
- B. Respondents shall, no later than the Effective Date of Divestiture of the Port Edwards Assets, at the option of the Acquirer, and as part of the Divestiture Agreement, assign Shared Terminal Contracts in whole or in part, modify current Shared Terminal Contracts or enter into new

Decision and Order

terminal contracts to insure that, as a result of the divestiture, the Acquirer receives:

1. the same terminals as, or terminals of a quality similar to, those retained by Respondent Oxy;
2. terminal space equal to or exceeding the capacity of terminal space used for products delivered by the Port Edwards facility prior to the divestiture and consistent with historical amounts of products delivered by the Port Edwards facility;
3. terminal contracts of similar or longer lengths of time that existed for the products delivered by the Port Edwards facility prior to the divestiture; and
4. terminal capacity in locations similar to the locations used for products delivered by the Port Edwards facility prior to the divestiture.

C. Respondents shall:

1. not receive Confidential Business Information about the transportation, delivery, storage, distribution, marketing, and sale of product by the Acquirer at a terminal owned by Respondents and used by the Acquirer, *PROVIDED, HOWEVER*, individual employees of the Respondents may receive and use Confidential Business Information only to the extent required for the operation of a Terminaling Agreement or to the extent necessary to allow Respondents to comply with the requirements and obligations of the laws of the United States and other countries, and to prepare consolidated financial reports, tax returns, reports required by securities laws, and personnel reports. Respondents shall require any Persons with access to Confidential Business Information to immediately enter into agreements with the Respondents and Acquirer not to disclose any Confidential Business Information to the Respondents or to any third party except for the purposes set forth this paragraph.
2. include in any Terminaling Agreement:
  - a. a provision prohibiting Respondents or any employee of Respondents from receiving Confidential Business Information about the transportation, delivery,

## Decision and Order

- storage, distribution, marketing, and sale of product by the Acquirer at a terminal owned by Respondents and used by the Acquirer, except at otherwise provided in this Paragraph III.C.; and
- b. a provision consistent with the proviso in Paragraph III.C.1., above, regarding non-disclosure of Confidential Business Information.
- D. The purposes of this Paragraph are (1) to ensure the continuation of the Port Edwards Assets as a going concern in the same manner in which it conducted business as of the date the Consent Agreement is signed, and (2) to remedy the lessening of competition resulting from the Acquisition as alleged in the Commission's Complaint.

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

- A. At any time after Respondents sign the Consent Agreement in this matter, the Commission may appoint a Monitor to assure that Respondents expeditiously comply with all of their obligations and perform all of their responsibilities as required by this Order;
- B. The Commission shall select the Monitor, subject to the consent of Respondents, which consent shall not be unreasonably withheld. If the Respondents have not opposed, in writing, including the reasons for opposing, the selection of a proposed Monitor within ten (10) days after notice by the staff of the Commission to Respondents of the identity of any proposed Monitor, Respondents shall be deemed to have consented to the selection of the proposed Monitor.
- C. Not later than ten (10) days after appointment of the Monitor, Respondents shall execute an agreement that, subject to the prior approval of the Commission, confers on the Monitor all the rights and powers necessary to permit the Monitor to monitor Respondents's compliance with the relevant terms of the Order in a manner consistent with the purposes of the Order.
- D. If a Monitor is appointed pursuant to this Paragraph IV,

Decision and Order

Respondents shall consent to the following terms and conditions regarding the powers, duties, authorities, and responsibilities of the Monitor:

1. The Monitor shall have the power and authority to monitor the Respondents's compliance with the terms of the Order, and shall exercise such power and authority and carry out the duties and responsibilities of the Monitor in a manner consistent with the purposes of the Order and in consultation with the Commission including, but not limited to:
  - a. Assuring that Respondents expeditiously comply with all of their obligations and perform all of their responsibilities as required by the Order to Maintain Assets and the Decision and Order in this matter;
  - b. Monitoring Terminating Agreements;
  - c. Monitoring any transition services agreements;
  - d. Assuring that Confidential Business Information is not received or used by Respondents or Acquirer, except as allowed in the Order to Maintain Assets and the Decision and Order in this matter.
2. The Monitor shall act in a fiduciary capacity for the benefit of the Commission.
3. Subject to any demonstrated legally recognized privilege, the Monitor shall have full and complete access to Respondents's personnel, books, documents, records kept in the normal course of business, facilities and technical information, and such other relevant information as the Monitor may reasonably request, related to Respondents's compliance with their obligations under the Order. Respondents shall cooperate with any reasonable request of the Monitor and shall take no action to interfere with or impede the Monitor's ability to monitor Respondents's compliance with the Order.
4. The Monitor shall serve, without bond or other security, at the expense of Respondents on such reasonable and customary terms and conditions as the Commission may set. The Monitor shall have authority to employ, at the expense of the Respondents, such consultants,

## Decision and Order

- accountants, attorneys and other representatives and assistants as are reasonably necessary to carry out the Monitor's duties and responsibilities. The Monitor shall account for all expenses incurred, including fees for services rendered, subject to the approval of the Commission.
5. Respondents shall indemnify the Monitor and hold the Monitor harmless against any losses, claims, damages, liabilities, or expenses arising out of, or in connection with, the performance of the Monitor's duties, including all reasonable fees of counsel and other reasonable expenses incurred in connection with the preparations for, or defense of, any claim, whether or not resulting in any liability, except to the extent that such losses, claims, damages, liabilities, or expenses result from misfeasance, gross negligence, willful or wanton acts, or bad faith by the Monitor.
  6. The Monitor Agreement shall state that within one (1) month from the date the Monitor is appointed pursuant to this paragraph, and every sixty (60) days thereafter, the Monitor shall report in writing to the Commission concerning performance by Respondents of their obligations under the Order.
  7. Respondents may require the Monitor and each of the Monitor's consultants, accountants, attorneys, and other representatives and assistants to sign a customary confidentiality agreement; *PROVIDED, HOWEVER*, such agreement shall not restrict the Monitor from providing any information to the Commission.
- E. The Commission may, among other things, require the Monitor and each of the Monitor's consultants, accountants, attorneys, and other representatives and assistants to sign an appropriate confidentiality agreement relating to Commission materials and information received in connection with the performance of the Monitor's duties.
- F. If the Commission determines that the Monitor has ceased to act or failed to act diligently, the Commission may appoint a substitute Monitor in the same manner as provided in this Paragraph IV.

Decision and Order

- G. The Commission may on its own initiative, or at the request of the Monitor, issue such additional orders or directions as may be necessary or appropriate to assure compliance with the requirements of the Order.
- H. A Monitor appointed pursuant to this Order may be the same person appointed as the monitor appointed pursuant to the Order to Maintain Assets in this matter or the Divestiture Trustee pursuant to the relevant provisions of this Order.

**V.**

**IT IS FURTHER ORDERED** that:

- A. If Respondents have not fully complied with the obligations to divest the Port Edwards Assets as required by Paragraph II of this Order, the Commission may appoint a Divestiture Trustee to divest the Port Edwards Assets in a manner that satisfies the requirements of Paragraph II.  
In the event that the Commission or the Attorney General brings an action pursuant to § 5(l) of the Federal Trade Commission Act, 15 U.S.C. § 45(l), or any other statute enforced by the Commission, Respondents shall consent to the appointment of a Divestiture Trustee in such action to divest the Port Edwards Assets. Neither the appointment of a Divestiture Trustee nor a decision not to appoint a Divestiture Trustee under this Paragraph V shall preclude the Commission or the Attorney General from seeking civil penalties or any other relief available to it, including a court-appointed Divestiture Trustee, pursuant to § 5(l) of the Federal Trade Commission Act, or any other statute enforced by the Commission, for any failure by Respondents to comply with this Order.
- B. The Commission shall select the Divestiture Trustee, subject to the consent of Respondents, which consent shall not be unreasonably withheld. The Divestiture Trustee shall be a person with experience and expertise in acquisitions and divestitures. If Respondents have not opposed, in writing, including the reasons for opposing, the selection of any proposed Divestiture Trustee within ten (10) days after

## Decision and Order

notice by the staff of the Commission to Respondents of the identity of any proposed Divestiture Trustee, Respondents shall be deemed to have consented to the selection of the proposed Divestiture Trustee.

- C. Not later than ten (10) days after the appointment of a Divestiture Trustee, Respondents shall execute a trust agreement that, subject to the prior approval of the Commission, transfers to the Divestiture Trustee all rights and powers necessary to permit the Divestiture Trustee to effect the divestitures required by this Order.
- D. If a Divestiture Trustee is appointed by the Commission or a court pursuant to this Paragraph V, Respondents shall consent to the following terms and conditions regarding the Divestiture Trustee's powers, duties, authority, and responsibilities:
1. Subject to the prior approval of the Commission, the Divestiture Trustee shall have the exclusive power and authority to divest the Port Edwards Assets.
  2. The Divestiture Trustee shall have one (1) year after the date the Commission approves the trust agreement described herein to divest the Port Edwards Assets absolutely and in good faith, at no minimum price, to an Acquirer that receives the prior approval of the Commission and in a manner that receives the prior approval of the Commission. If, however, at the end of the one (1) year period, the Divestiture Trustee has submitted a plan of divestiture or believes that the divestiture can be achieved within a reasonable time, the divestiture period or periods may be extended by the Commission; *PROVIDED, HOWEVER*, the Commission may extend the divestiture period only two (2) times.
  3. Subject to any demonstrated legally recognized privilege, the Divestiture Trustee shall have full and complete access to the personnel, books, records and facilities related to the relevant assets that are required to be divested by this Order and to any other relevant information, as the Divestiture Trustee may request. Respondents shall develop such financial or other



Decision and Order

information as the Divestiture Trustee may request and shall cooperate with the Divestiture Trustee.

Respondents shall take no action to interfere with or impede the Divestiture Trustee's accomplishment of the divestiture. The Divestiture Trustee shall have the right and authority to negotiate and modify contracts to satisfy the provisions of Paragraph III of this Order.

Any delays in divestiture caused by Respondents shall extend the time for divestiture under this Paragraph V in an amount equal to the delay, as determined by the Commission.

4. The Divestiture Trustee shall use best efforts to negotiate the most favorable price and terms available in each contract that is submitted to the Commission, subject to Respondents's absolute and unconditional obligation to divest expeditiously and at no minimum price. The divestiture shall be made in the manner and to an acquirer as required by this Order;  
*PROVIDED, HOWEVER*, if the Divestiture Trustee receives bona fide offers from more than one acquiring entity, and if the Commission determines to approve more than one such acquiring entity, the Divestiture Trustee shall divest to the acquiring entity selected by Respondents from among those approved by the Commission;  
*PROVIDED FURTHER, HOWEVER*, that Respondents shall select such entity within five (5) days after receiving notification of the Commission's approval.
5. The Divestiture Trustee shall serve, without bond or other security, at the cost and expense of Respondents, on such reasonable and customary terms and conditions as the Commission or a court may set. The Divestiture Trustee shall have the authority to employ, at the cost and expense of Respondents, such consultants, accountants, attorneys, investment bankers, business brokers, appraisers, and other representatives and assistants as are necessary to carry out the Divestiture Trustee's duties and responsibilities. The Divestiture Trustee shall account for all monies derived from the

## Decision and Order

divestiture and all expenses incurred. After approval by the Commission of the account of the Divestiture Trustee, including fees for the Divestiture Trustee's services, all remaining monies shall be paid at the direction of the Respondents, and the Divestiture Trustee's power shall be terminated. The compensation of the Divestiture Trustee shall be based at least in significant part on a commission arrangement contingent on the divestiture of all of the relevant assets that are required to be divested by this Order.

6. Respondents shall indemnify the Divestiture Trustee and hold the Divestiture Trustee harmless against any losses, claims, damages, liabilities, or expenses arising out of, or in connection with, the performance of the Divestiture Trustee's duties, including all reasonable fees of counsel and other expenses incurred in connection with the preparation for, or defense of, any claim, whether or not resulting in any liability, except to the extent that such losses, claims, damages, liabilities, or expenses result from misfeasance, gross negligence, willful or wanton acts, or bad faith by the Divestiture Trustee.
7. The Divestiture Trustee shall have no obligation or authority to operate or maintain the relevant assets required to be divested by this Order.
8. The Divestiture Trustee shall act in a fiduciary capacity for the benefit of the Commission.
9. The Divestiture Trustee shall report in writing to Respondents and to the Commission every sixty (60) days concerning the Divestiture Trustee's efforts to accomplish the divestiture.
10. Respondents may require the Divestiture Trustee and each of the Divestiture Trustee's consultants, accountants, attorneys and other representatives and assistants to sign a customary confidentiality agreement; *PROVIDED, HOWEVER*, such agreement shall not restrict the Divestiture Trustee from providing any information to the Commission.
11. The Commission may, among other things, require the

Decision and Order

- Divestiture Trustee and each of the Divestiture Trustee's consultants, accountants, attorneys, and other representatives and assistants to sign an appropriate confidentiality agreement relating to Commission materials and information received in connection with the performance of the Divestiture Trustee's duties.
- E. If the Commission determines that a Divestiture Trustee has ceased to act or failed to act diligently, the Commission may appoint a substitute Divestiture Trustee in the same manner as provided in this Paragraph V.
- F. The Commission or, in the case of a court-appointed Divestiture Trustee, the court, may on its own initiative or at the request of the Divestiture Trustee issue such additional orders or directions as may be necessary or appropriate to accomplish the divestiture required by this Order.
- G. The Divestiture Trustee(s) appointed pursuant to Paragraph V of this Order may be the same Person appointed as the Monitor pursuant to Paragraph IV of this Order.

**VI.**

**IS FURTHER ORDERED** that until December 31, 2006, Respondent Oxy, including, but not limited to, its agents and Armand Products Company, shall not solicit any Assigned Contract Customer in an attempt to sell, currently or in the future, such customer KOH (if the contract assigned to the Assigned Contract Customer was for KOH) or potassium carbonate (if the contract assigned to the Assigned Contract Customer was for potassium carbonate) including, but not limited to, making offers pursuant to a "meet or release" or "competitive price" or similar clause in customer contracts. *PROVIDED, HOWEVER*, Respondent Oxy may discuss the terms of Respondent Oxy's contract or supply with a Dual Contract Customer, but shall not otherwise solicit an Assigned Contract Customer as prohibited by this Paragraph VI. *PROVIDED, FURTHER, HOWEVER*, if an Assigned Contract Customer is no longer under contract with the Acquirer, this Paragraph VI no longer applies to Respondent Oxy in relation to that Assigned Contract Customer.

## Decision and Order

**VII.**

**IT IS FURTHER ORDERED** that Respondents shall facilitate the hiring of any Designated Vulcan Staff by the Acquirer prior to the Effective Date of Divestiture by:

- A. Allowing the Acquirer an opportunity to interview each person identified as Designated Vulcan Staff before they are hired pursuant to this Paragraph VII;
- B. Allowing the Acquirer to inspect the personnel files and other documentation relating to the Designated Vulcan Staff, to the extent permissible under applicable laws, before they are hired pursuant to this Paragraph VII;
- C. Not offering any incentive to the Designated Vulcan Staff to decline employment with the Acquirer;
- D. Not interfering with any negotiations by the Acquirer to employ any Designated Vulcan Staff;
- E. Removing any contractual impediments with the Respondents that may deter any Designated Vulcan Staff from accepting employment with the Acquirer and assigning any confidentiality agreements or restrictions, except as to information related solely to products or businesses not transferred to the Acquirer and any non-compete agreements; and
- F. Vesting all pension rights, current and accrued, of any Designated Vulcan Staff as of the date of transition to employment with the Acquirer.

**VIII.**

**IT IS FURTHER ORDERED** that for a period of ten (10) years from the date this Order is issued, Respondent Oxy, including its joint venture, Armand Products Company, shall not, without providing advance written notification to the Commission in the manner described in this Paragraph VIII, directly or indirectly:

- A. Acquire any stock, share capital, equity or other interest in any Person, corporate or non-corporate that produces, or assets used in the production or sale of, potassium hydroxide, potassium carbonate, or potash; or

Decision and Order

- B. Enter into any contracts to manage or operate any Person that produces potassium hydroxide, potassium carbonate, or potash.

Said notification shall be given on the Notification and Report Form set forth in the Appendix to Part 803 of Title 16 of the Code of Federal Regulations as amended (herein referred to as “the Notification”), and shall be prepared and transmitted in accordance with the requirements of that part, except that no filing fee will be required for any such notification, notification shall be filed with the Secretary of the Commission, notification need not be made to the United States Department of Justice, and notification is required only of Respondent Oxy and not of any other party to the transaction. Respondent Oxy shall provide the Notification to the Commission at least thirty days prior to consummating the transaction (hereinafter referred to as the “first waiting period”). If, within the first waiting period, representatives of the Commission make a written request for additional information or documentary material (within the meaning of 16 C.F.R. § 803.20), Respondent Oxy shall not consummate the transaction until thirty days after submitting such additional information or documentary material. Early termination of the waiting periods in this paragraph may be requested and, where appropriate, granted by letter from the Bureau of Competition.

*PROVIDED, HOWEVER*, that prior notification shall not be required by this paragraph for a transaction for which Notification is required to be made, and has been made, pursuant to Section 7A of the Clayton Act, 15 U.S.C. § 18a.

*PROVIDED, FURTHER, HOWEVER*, that prior notification shall not be required by this paragraph for an acquisition, if Respondent Oxy acquires no more than one percent of the outstanding securities or other equity interest in an entity described in subparagraphs VIII.A and VIII.B.

**IX.**

**IT IS FURTHER ORDERED** that:

- A. Within thirty (30) days after the date this Order becomes final, and every sixty (60) days thereafter until Respondents have fully complied with Paragraphs II and V of this Order,

## Decision and Order

Respondents shall submit to the Commission a verified written report setting forth in detail the manner and form in which they intend to comply, are complying, and have complied with this Order. Respondents shall submit at the same time a copy of their report concerning compliance with this Order to the Divestiture Trustee or the Monitor, if any Divestiture Trustee or Monitor has been appointed pursuant to this Order. Respondents shall include in their reports, among other things that are required from time to time, a full description of the efforts being made to comply with the relevant Paragraphs of the Order, including a description of all substantive contacts or negotiations related to the divestiture of the relevant assets and the identity of all parties contacted. Respondents shall include in their reports copies of all written communications to and from such parties, all internal memoranda, and all reports and recommendations concerning completing the obligations.

- B. Within thirty (30) days after the date this Order is issued, and annually for ten (10) years on the anniversary of the date this Order is issued, Respondents shall submit to the Commission a verified written report setting forth in detail the manner and form in which they have complied, are complying, and will comply with this Order. Respondents shall include in their compliance reports, among other things that are required from time to time, a full description of the efforts being made to comply with the Order and copies of all written communications to and from all persons relating to this Order.

*PROVIDED, HOWEVER:* Respondents Vulcan shall submit annual reports pursuant to this Paragraph IX.B for two (2) years on the anniversary of the date this Order is issued.

*PROVIDED FURTHER, HOWEVER,* if either Paragraph II.B or Paragraph V come into effect, Respondent Vulcan shall submit annual reports pursuant to this Paragraph IX.B for five (5) years on the anniversary of the date this Order is issued.

Decision and Order

**X.**

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

**XI.**

**IT IS FURTHER ORDERED** that, for the purpose of determining or securing compliance with this Order, and subject to any legally recognized privilege, and upon written request with reasonable notice, Respondents shall permit any duly authorized representative of the Commission:

- A. access, during office hours of Respondents and in the presence of counsel, to all facilities and access to inspect and copy all books, ledgers, accounts, correspondence, memoranda and all other records and documents in the possession or under the control of Respondents related to compliance with this Order; and
- B. upon five (5) days' notice to Respondents and without restraint or interference from Respondents, to interview officers, directors, or employees of Respondents, who may have counsel present, regarding such matters.

**XII.**

**IT IS FURTHER ORDERED** that this Order shall terminate ten (10) years from the date it is issued.

By the Commission.

Decision and Order

**CONFIDENTIAL APPENDIX A****[Redacted From the Public Record Version But Incorporated  
By Reference]****CONFIDENTIAL APPENDIX B****[Redacted From the Public Record Version But Incorporated  
By Reference]****CONFIDENTIAL APPENDIX C****[Redacted From the Public Record Version But Incorporated  
By Reference]**



Analysis

**Analysis of the Complaint and Proposed Consent Order to  
Aid Public Comment**

**I. Introduction**

The Federal Trade Commission (“FTC” or “Commission”) has accepted, subject to final approval, an Agreement Containing Consent Orders (“Consent Agreement”) from Occidental Chemical Company (“OxyChem”) and Vulcan Materials Company (“Vulcan”) (collectively “Respondents”). The Consent Agreement is intended to resolve anticompetitive effects stemming from OxyChem’s proposed acquisition of the chemical assets of Vulcan. The Consent Agreement includes a proposed Decision and Order (“Order”) which requires Respondents to divest Vulcan’s facility in Port Edwards, Wisconsin and assets relating to the research, development, marketing, sales, and production of chemicals produced at the facility including chlorine, caustic soda (sodium hydroxide), KOH (potassium hydroxide), APC (anhydrous potassium carbonate), and hydrochloric acid (“Port Edwards business”). The Order calls for divestiture of the Port Edwards business to ERCO Worldwide (“ERCO”) or, in the event the Commission requires rescission of such acquisition, another approved buyer. The Consent Agreement also includes an Order to Maintain Assets, which requires Respondents to preserve the Port Edwards business as a viable, competitive, and ongoing operation until the divestiture is achieved.

The Consent Agreement, if finally accepted by the Commission, would settle charges that OxyChem’s proposed acquisition of Vulcan’s chemical assets may have substantially lessened competition in the markets for KOH, potassium carbonate, and APC. The Commission has reason to believe that OxyChem’s proposed acquisition of Vulcan’s Port Edwards business would have violated Section 7 of the Clayton Act and Section 5 of the Federal Trade Commission Act.

**II. The Proposed Complaint**

## Analysis

According to the Commission's proposed complaint, the relevant product markets in which to analyze the effects of OxyChem's proposed acquisition of Vulcan's chemical assets are the production and sale of KOH, potassium carbonate, and APC. KOH is the raw material for the production of many potassium chemicals, such as potassium permanganate, citrate, acetate, cyanide, benzoate, iodide, and sorbate. The largest end use of KOH is the production of potassium carbonate, commonly known as potash. End uses for potassium carbonate include nutrition supplements for dairy cattle, video glass for television and computer monitors, other specialty glass, potassium silicates, fertilizers, gas processing, industrial intermediaries, photographic development processes, detergents; and food products. Potassium carbonate can be produced in liquid or flake (solid) form. Over 90% of total potcarb production in the United States is of the flake form, known as APC. For most APC customers, liquid potassium carbonate is not an economically viable substitute.

The proposed complaint alleges that the markets for KOH, potcarb, and APC are highly concentrated and that OxyChem and Vulcan have been the primary competitors in these markets for many years and are the only producers of APC in the U.S. As the proposed Complaint describes, customers have relied on the competition between these companies to maintain competitive pricing levels. The proposed complaint alleges that OxyChem's proposed acquisition of Vulcan's chemical assets would reduce competition by eliminating direct competition between these two companies. The proposed complaint further alleges that entry into the relevant markets would not be timely, likely, or sufficient to deter or offset the acquisition's adverse competitive effects.

**III. Terms of the Proposed Order**

The proposed Order also requires that, within 10 days of OxyChem's acquisition of Vulcan's chemical assets, OxyChem divest the Port Edwards business to ERCO Worldwide (USA) Inc., an indirect subsidiary of Superior Plus, Inc., a Canadian company. The Port Edwards business will become part of ERCO Worldwide,

Analysis

a division of Superior Plus whose parent, Superior Plus Income Fund, is a Canadian income fund. Superior Plus, Inc. has four divisions: Superior Propane; ERCO Worldwide; Winroc; and Superior Energy Management. The market value of the fund is Cdn \$2.5 billion. ERCO's total revenues in 2004 were Cdn \$396 million.

The assets to be divested under the proposed Order include Port Edwards's manufacturing facilities, related transportation assets (including railcars and terminal contracts), raw material supply agreements, and customer contracts. Port Edwards is Vulcan's only manufacturing facility that has the capacity to produce KOH and APC. The divested assets are sufficient to allow ERCO to effectively continue the production and marketing of KOH, APC, HCl, caustic soda, and chlorine at Port Edwards in amounts, and under terms, equivalent to the historical production and sale of these chemicals from the facility.

The Order further provides that if, at the time the Commission makes this Order final, the Commission notifies Respondents that ERCO is not an acceptable acquirer of the Port Edwards business or that the manner in which the divestiture was accomplished is not acceptable, then, the divestiture to ERCO shall be rescinded and within a six-month period, OxyChem shall divest the Port Edwards business to an acquirer acceptable to the Commission. If, following this six month period, the Port Edwards Assets have not been divested, then the Commission may appoint a Divestiture Trustee to divest the assets in a manner acceptable to the Commission.

The proposed Order to Maintain Assets that is also included in the Consent Agreement requires that Respondents maintain the Port Edwards business as a viable and competitive operation until the business is transferred to ERCO or another Commission-approved acquirer. Furthermore, the order contains measures designed to ensure that no material confidential information is exchanged between Respondents and the Port Edwards business (except as otherwise provided in the Order to Maintain Assets) and measures designed to prevent interim harm to competition in the relevant markets pending divestiture.

## Analysis

The proposed Order also provides for the Commission to appoint a Monitor Trustee to oversee OxyChem's compliance with the terms of the order, and in the Order to Maintain Assets, the Commission appoints Richard M. Klein as Monitor Trustee. Mr. Klein has a Ph.D in Inorganic Chemistry and was the President and CEO of Sybron Chemicals from 1979 to 2001. He serves on the boards of a number of companies and has been appointed by the Commission as Monitor Trustee or Hold Separate Trustee in other FTC matters.

Within thirty (30) days after the date this Order becomes final, and every sixty (60) days thereafter until Respondents have fully divested the Port Edwards business, Respondents are required to submit a verified written report describing how they are complying, have complied, and intend to comply with the terms of the Order. Further, within thirty (30) days after the date this Order is issued, and annually for ten (10) years on the anniversary of the date this Order is issued, Respondent OxyChem must submit a verified written report to the Commission describing how it is complying, has complied, and intends to comply with the terms of the Order. Finally, within thirty (30) days after the date this Order is issued and annually for two (2) years on the anniversary of the date this Order is issued, Respondent Vulcan shall submit to the Commission a verified written report describing how it has complied, is complying, and will comply with this Order; however, if either Paragraph II.B or Paragraph V of the Order come into effect, Respondent Vulcan shall submit annual reports for five (5) years on the anniversary of the date this Order is issued.

#### **IV. Opportunity for Public Comment**

The proposed Order has been placed on the public record for thirty (30) days to receive comments by interested persons. Comments received during this period will become part of the public record. After thirty (30) days, the Commission will review the Consent Agreement and comments received and decide whether to withdraw its agreement or make final the Consent Agreement's proposed Order and Order to Maintain Assets.

Analysis

The purpose of this analysis is to facilitate public comment on the proposed Order. This analysis is not intended to constitute an official interpretation of the Consent Agreement, the proposed Order, or the Order to Maintain Assets, or in any way to modify the terms of the Consent Agreement, the proposed Order, or the Order to Maintain Assets.

Complaint

IN THE MATTER OF

**VALERO L.P., ET. AL.**CONSENT ORDER, ETC., IN REGARD TO ALLEGED VIOLATIONS OF  
SEC. 7 OF THE CLAYTON ACT AND SEC. 5 OF THE FEDERAL TRADE  
COMMISSION ACT*Docket C-4141; File No. 0510022  
Complaint, June 14, 2005--Decision, July 22, 2005*

This consent order addresses the acquisition by Respondents Valero L.P. and Valero Energy Corporation -- collectively engaged in the transportation and storage of crude oil, and in the refining, transportation, and marketing of petroleum products and related petrochemical products -- of Respondents Kaneb Services LLC and Kaneb Pipe Line Partners, L.P., which collectively own and operate refined petroleum product pipelines and petroleum and specialty liquids storage and terminaling facilities. The order, among other things, requires the respondents to divest three Kaneb petroleum terminals in the Greater Philadelphia, Pennsylvania area; to divest a Kaneb pipeline system that originates in Casper, Wyoming, and terminates in Rapid City, South Dakota (and includes Kaneb petroleum terminals in Rapid City, South Dakota, Cheyenne, Wyoming, Denver, Colorado, and Colorado Springs, Colorado); and to divest Kaneb petroleum terminals in Martinez and Richmond, California. The consent order also requires Respondent Valero L.P. to ensure that customers and prospective customers have non-discriminatory access to commingled terminaling of ethanol at its retained San Francisco Bay terminals - on terms and conditions no less advantageous than those given to Valero Energy -- and to create firewalls that prevent the transfer of competitively sensitive information between the merged firm and Valero Energy.

*Participants*

For the Commission: *Peter Richman, Marc W. Schneider, Robert E. Friedman, Brian J. Telpner, Vadim M. Brusser, Natasha Allen, Jacob Swanton, Sara S. Brown, Nick Pedersen Phillip L. Broyles, Naomi Licker, Elizabeth A. Piotrowski, Daniel P. Ducore, Mark D. Williams, Louis Silvia and Mark Frankena.*

For the Respondents: *Ilene Knable Gotts, Wachtell, Lipton, Rosen & Katz, and Daniel Wellington, Fulbright & Jaworski LLP*

Complaint

## **COMPLAINT**

Pursuant to the provisions of the Federal Trade Commission Act and the Clayton Act, and by virtue of the authority vested in it by said Acts, the Federal Trade Commission (“FTC” or “Commission”), having reason to believe that Respondents Valero L.P. and Valero Energy Corporation and Respondents Kaneb Services LLC and Kaneb Pipe Line Partners, L.P. (together “Kaneb”) have entered into agreements and plans of merger whereby Valero L.P. proposes to acquire all of the outstanding common stock of Kaneb, that such agreement and plan of merger violates 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, and it appearing to the Commission that a proceeding in respect thereof would be in the public interest, hereby issues its complaint, stating its charges as follows:

### **I. RESPONDENTS**

#### **Valero L.P.**

1. Respondent Valero L.P. is a publicly-traded limited partnership organized, existing, and doing business under and by virtue of the laws of the state of Delaware, with its office and principal place of business located at One Valero Way, San Antonio, Texas 78249.
2. Respondent Valero L.P. is, and at all times relevant herein has been, a diversified transportation and terminaling company engaged, either directly or through affiliates, in the transportation and terminaling of crude oil, intermediate refinery feed stocks, finished petroleum product blend components, gasoline, diesel fuel, and aviation fuel; and other related businesses.
3. Valero GP, LLC is the general partner of Riverwalk Logistics, L.P., which is in turn the general partner of Valero L.P. Valero GP, LLC manages the operations and employs the full-time

## Complaint

personnel of Valero L.P. Riverwalk Logistics, L.P. owns a two percent general partnership interest in Valero L.P. At all times relevant herein, Valero GP, LLC and Riverwalk Logistics, L.P. have been indirect wholly owned subsidiaries of Valero Energy Corporation.

4. Respondent Valero L.P. is, and at all times relevant herein has been, engaged in commerce as “commerce” is defined in Section 1 of the Clayton Act, as amended, 15 U.S.C. § 12, and is an entity whose business is in or affecting commerce as “commerce” is defined in Section 4 of the Federal Trade Commission Act, as amended, 15 U.S.C. § 44.

Valero Energy Corporation

5. Respondent Valero Energy Corporation is a corporation organized, existing, and doing business under and by virtue of the laws of the state of Delaware, with its office and principal place of business located at One Valero Way, San Antonio, Texas 78249.
6. Respondent Valero Energy Corporation is, and at all times relevant herein has been, a diversified energy company engaged, either directly or through affiliates, in the refining of crude oil into refined petroleum products, including gasoline, aviation fuel, and other light petroleum products; the transportation, terminaling, and marketing of gasoline, diesel fuel, and aviation fuel; and other related businesses.
7. Respondent Valero Energy Corporation is, and at all times relevant herein has been, engaged in commerce as “commerce” is defined in Section 1 of the Clayton Act, as amended, 15 U.S.C. § 12, and is a corporation whose business is in or affecting commerce as “commerce” is defined in Section 4 of the Federal Trade Commission Act, as amended, 15 U.S.C. § 44.



Complaint

Kaneb Pipe Line Partners, L.P.

8. Respondent Kaneb Pipe Line Partners, L.P. is a publicly-traded limited partnership organized, existing, and doing business under and by virtue of the laws of the state of Delaware, with its office and principal place of business located at 2435 North Central Expressway, Richardson, Texas 75080.
9. Respondent Kaneb Pipe Line Partners, L.P. is, and at all times relevant herein has been, a diversified transportation and terminaling company engaged, either directly or through affiliates, in the transportation and terminaling of crude oil, intermediate refinery feed stocks, finished petroleum product blend components, gasoline, diesel fuel, and aviation fuel; and other related businesses.
10. Respondent Kaneb Pipe Line Partners, L.P. is, and at all times relevant herein has been, engaged in commerce as “commerce” is defined in Section 1 of the Clayton Act, as amended, 15 U.S.C. § 12, and is an entity whose business is in or affecting commerce as “commerce” is defined in Section 4 of the Federal Trade Commission Act, as amended, 15 U.S.C. § 44.

Kaneb Services LLC

11. Respondent Kaneb Services LLC is a publicly-traded limited liability company organized, existing, and doing business under and by virtue of the laws of the state of Delaware, with its office and principal place of business located at 2435 North Central Expressway, Richardson, Texas 75080.
12. Respondent Kaneb Services LLC is, and at all times relevant herein has been, a company that manages and operates a refined petroleum products and anhydrous ammonia pipeline business and a terminaling of petroleum products and specialty liquids business through the general

## Complaint

partner interest owned by one of its subsidiaries in Kaneb Pipe Line Partners, L.P., a Delaware limited partnership, which in turn owns those systems and facilities through its subsidiaries, and other related businesses.

13. Respondent Kaneb Services LLC is, and at all times relevant herein has been, engaged in commerce as “commerce” is defined in Section 1 of the Clayton Act, as amended, 15 U.S.C. § 12, and is a corporation whose business is in or affecting commerce as “commerce” is defined in Section 4 of the Federal Trade Commission Act, as amended, 15 U.S.C. § 44.

## **II. THE MERGERS**

14. Pursuant to (1) the Agreement and Plan of Merger, dated as of October 31, 2004, by and among, Valero L.P.; Riverwalk Logistics, L.P.; Valero GP LLC; VLI Sub A LLC; and Kaneb Services LLC; and (2) the Agreement and Plan of Merger, dated as of October 31, 2004, by and among Valero L.P.; Riverwalk Logistics, L.P.; Valero GP LLC; VLI Sub B LLC; Kaneb Pipe Line Partners, L.P.; and Kaneb Pipe Line Company LLC, Valero L.P. intends to acquire all of the equity interests of Kaneb Services LLC and Kaneb Pipe Line Company, L.P. in exchange for cash, Valero L.P. partnership units, or a combination of cash and Valero L.P. partnership units. The value of the transaction at the time of the agreements was approximately \$2.8 billion. The surviving entity is to be called Valero L.P.

## **III. TRADE AND COMMERCE**

### *Relevant Product Markets*

15. A line of commerce in which to analyze the effect of the proposed transaction is the provision of terminaling services for light petroleum products, fuel blending components, intermediate feed stocks for refinery units, and crude oil.

Complaint

16. A line of commerce in which to analyze the effect of the proposed transaction is the pipeline transportation of light petroleum products.
17. A line of commerce in which to analyze the effect of the proposed transaction is the bulk supply of light petroleum products.
18. Light petroleum product terminals are specialized facilities with large storage tanks used to receive light petroleum products by pipeline, by water, or direct from refinery production; for storage; and for redistribution by pipeline, water carrier, or local distribution by truck.
19. Terminating services consist of a cluster of services related to the storage and throughput of petroleum products. Terminals receive, store, and handle bulk quantities of light petroleum products for redelivery by pipeline, into water vessels, or across truck racks in tankwagon quantities. They also perform value-added services, such as handling and injection of motor fuel additives (including ethanol) as light petroleum products are redelivered across the truck rack. Terminals also receive, store, and redeliver bulk quantities of crude oil, refinery feedstocks, and other blending components for finished fuels.
20. Light petroleum products include motor gasoline, distillates, and jet fuel.
21. Motor gasoline is produced in various grades and types, including conventional unleaded gasoline, reformulated gasoline, CARB gasoline, and others. Reformulated gasoline is gasoline formulated for use in motor vehicles, the composition and properties of which meet the requirements of the reformulated gasoline regulations promulgated by the U.S. Environmental Protection Agency under Section 211K of the Clean Air Act. Reformulated

## Complaint

gasoline also includes oxygenated fuels program reformulated gasoline. CARB gasoline is gasoline meeting the specifications of the California Air Resources Board, and which also meet or exceed U.S. Environmental Protection Agency gasoline specifications for the areas in which they are used. There is no substitute for gasoline as a fuel for automobiles and other vehicles that are designed to use gasoline.

22. Diesel fuel is a petroleum distillate with the referenced sulfur specification to meet on-road, off-road, or home heating uses. There is no substitute for the appropriate diesel fuel as a fuel for trucks, railroad engines, farm equipment, other vehicles and equipment designed to burn diesel fuel. Jet fuel is a kerosene product meeting the specifications for use as turbojet and turboprop engines. Military jet fuel meets the specifications for kerosene products designated for military use (JP-8 and JP-5).
23. Blend components are petroleum products and other chemicals blended with unfinished gasoline to produce finished gasoline. Examples of common blend components include CARBOB, reformat, alkylate, MTBE, and ethanol. Ethanol is an anhydrous denatured aliphatic alcohol. The use of ethanol as a gasoline blending component and oxygenate has become increasingly prevalent in some parts of the country, especially as some states, (*e.g.*, California, New York) have recently prohibited the use of oxygenates such as MTBE.
24. Crude oil is the primary feedstock distilled and further refined to produce finished fuel products and other refined products. Intermediate feedstocks are semi-refined petroleum products used as feedstocks to blend into finished petroleum products.

Complaint

*Relevant Geographic Markets*

25. Relevant sections of the country in which to analyze the proposed transaction are the following:
  - a. Greater Philadelphia Area, consisting of the metropolitan statistical areas (“MSAs”) of Philadelphia, Pennsylvania, Wilmington, Delaware, and Camden, New Jersey, where the mergers would reduce competition in terminaling services for, and among bulk suppliers of, light petroleum products, as alleged below;
  - b. Colorado Front Range, consisting of the portion of Colorado east of the Continental Divide, including the MSAs of Denver, Colorado Springs, Fort Collins, and Boulder, Colorado, where the mergers would reduce competition in pipeline transportation and terminaling services for, and among bulk suppliers of, light petroleum products, as alleged below; and
  - c. Northern California, consisting of California counties north of, but not including, San Luis Obispo, Kern, and San Bernardino counties, and narrower markets contained therein, where the mergers would reduce competition in terminaling services for crude oil, light petroleum products, blend components, and intermediate refinery feedstocks, and among bulk suppliers of light petroleum products and blend components (including ethanol), as alleged below.

*Market Structure*

Greater Philadelphia Area

26. Refineries produce light petroleum products and deliver them either into storage tanks or terminals on the refinery premises or into pipelines or deepwater marine vessels, that, in turn, deliver the fuel products into terminals located near the final consumer.

## Complaint

27. Refineries, deepwater-capable terminals, and pipeline terminals are direct horizontal competitors from which firms produce or to which firms deliver bulk supplies of light petroleum products. In the Greater Philadelphia Area, local refiners and bulk suppliers sell to independent discount gasoline retailers, oil companies, and wholesalers of light petroleum products.
28. Bulk suppliers of light petroleum products require terminals that can receive, store, and transfer the products to marine vessel, pipeline or truck. There is no substitute for light petroleum products terminals for bulk suppliers.
29. Firms that purchase truck-load quantities of light petroleum products to supply their retail or commercial pumps have no effective alternative to using local light petroleum product terminals.
30. Valero and Kaneb are direct horizontal competitors in the provision of terminaling services for bulk suppliers in the Greater Philadelphia Area.
31. Kaneb is an independent commercial terminal operator. Kaneb does not own or sell any light petroleum products to retail or commercial customers. Thus, in Philadelphia, Kaneb derives its revenue solely from the provision of terminaling services, including receipt and throughput of bulk supplies.
32. Bulk suppliers may purchase light petroleum products from an integrated refiner and terminal operator in the Greater Philadelphia Area (“local suppliers”). The local suppliers in the Philadelphia area include Valero, ConocoPhillips, Premcor, Sunoco, ExxonMobil, and Hess.
33. A reasonable substitute for bulk suppliers to purchasing light petroleum products made by local refineries in the

Complaint

Greater Philadelphia Area for a significant portion of the time is the purchase of wholesale light petroleum products produced outside the area and physically delivered by a pipeline or marine vessel. The primary sources of these imports are refiners located in the U.S. Gulf Coast region (“Gulf Coast”) and outside the United States.

34. Valero L.P. owns a light petroleum products terminal in Paulsboro, New Jersey, from which light petroleum products are delivered by truck into, among other places, the Greater Philadelphia Area. The Valero L.P. terminal is supplied by Valero Energy’s Paulsboro refinery.
35. Kaneb owns three terminals in the greater Philadelphia area: two in Philadelphia and one in Paulsboro, New Jersey. Kaneb’s “north” Philadelphia terminal is connected to the Colonial Pipeline and is capable of receiving bulk shipments of light petroleum products produced in the Gulf Coast. The terminal also has a dock that permits it to receive bulk marine shipments by barge. Kaneb’s “south” Philadelphia terminal is connected to the Colonial Pipeline but does not currently have access to marine shipments. Kaneb’s Paulsboro terminal can receive bulk shipments both from the Colonial Pipeline and from deepwater tankers.
36. On April 25, 2005, Valero Energy announced its intent to acquire Premcor Inc. in a transaction valued at approximately \$8 billion. The transaction includes Premcor’s Delaware City, Delaware, refinery. For the purposes of analyzing the proposed Valero/Kaneb transaction, the Commission assumes a combined Valero, Kaneb, and Premcor.
37. Post-merger, the combined Valero, Kaneb, and Premcor will control a significant share of bulk supply and terminaling services for light petroleum products in the greater Philadelphia area. The proposed transaction would

## Complaint

significantly increase market concentration, and post-merger the market would be highly concentrated. Without Premcor, post-merger, the combined Valero and Kaneb would still control a significant share of bulk supply and terminaling services for light petroleum products in the Greater Philadelphia area.

38. As an independent terminal operator, Kaneb today provides Philadelphia area customers access to bulk supply originating outside the area. Without this competitive constraint, Philadelphia prices, generally limited by either Gulf Coast prices plus pipeline tariff or New York Harbor prices adjusted by the water-borne transportation costs, could rise.
39. Kaneb's terminals are the only Philadelphia area terminals accessible to independent delivery, storage, and throughput of bulk imports of light petroleum products delivered by marine vessel (deepwater and barge) and Colonial Pipeline into the Greater Philadelphia area. Loss of access would reduce the total supply to the Greater Philadelphia area and increase wholesale prices for light petroleum products.
40. After the mergers, the combined firm could effectively coordinate with the other providers in the Greater Philadelphia area to raise prices in bulk supply of and terminaling services for light petroleum products in the greater Philadelphia area.

Colorado Front Range

41. Valero and Kaneb are direct horizontal competitors in the provision of pipeline transportation to and terminaling services for bulk suppliers of light petroleum products in the Colorado Front Range and in narrower markets contained therein. Other providers of bulk supply and terminaling services for light petroleum products in the Colorado Front Range are Sinclair, Suncor, ConocoPhillips, and Magellan.



Complaint

42. Kaneb is an independent pipeline and terminal operator in the Colorado Front Range. Kaneb does not own or sell any of the product that it transports on its pipeline or stores in its terminal. Thus, Kaneb derives its revenue solely from providing pipeline transportation and terminaling services.
43. Bulk supply customers in Denver may purchase light petroleum products from local suppliers. The local suppliers in the Colorado Front Range are Valero, Suncor, ConocoPhillips, and Sinclair.
44. For bulk supply customers, a reasonable substitute for purchasing from local refiners for a significant portion of the time is purchasing wholesale light petroleum products from refineries located outside of the Colorado Front Range and physically delivered into the area by pipeline. Refiners outside of the area, in Montana, Wyoming, Kansas, and Texas, that supply the Colorado Front Range are Frontier, Sinclair, ExxonMobil, ConocoPhillips, and CHS.
45. Valero L.P. owns the McKee-Denver pipeline that originates at the Valero Energy refinery in McKee, Texas, and serves Denver. Valero L.P. has a partial interest in the Borger-Denver pipeline. This pipeline runs from the ConocoPhillips refinery in Borger, Texas, through the Valero Energy refinery in McKee, Texas, and connects to a Valero L.P. terminal in Denver, Colorado.
46. Kaneb owns the West Pipeline system, which originates in Casper, Wyoming, and runs to terminals in Fountain, Colorado (near Colorado Springs), and Dupont, Colorado (near Denver), among other locations. The West Pipeline connects to a Frontier refinery in Cheyenne, Wyoming; a Sinclair refinery in Casper, Wyoming; and the Seminole Pipeline, from which it receives light petroleum products from the ExxonMobil, ConocoPhillips, and CHS refineries in Billings, Montana.

## Complaint

47. Post-merger, the combined Valero and Kaneb will control a significant share of bulk supply, and of terminaling services for bulk suppliers, of light petroleum products in the Colorado Front Range. The proposed transaction would significantly increase market concentration, and post-merger the market would be highly concentrated. The proposed transaction would result in Valero having a monopoly in the Colorado Springs area.
48. After the mergers, the combined firm could effectively coordinate with others to raise prices in the markets for bulk supply of, and terminaling services for, light petroleum products in the Colorado Front Range, or unilaterally in parts contained therein.
49. Kaneb's West Pipeline, along with Magellan's Chase Pipeline, provides the only independent access to pipeline deliveries of light petroleum products from refineries outside of the Colorado Front Range. Loss of independent access would reduce the number of competitors capable of supplying the Colorado Front Range, reduce the amount of supply in the market and increase wholesale prices for light petroleum products.

Northern California

50. Valero and Kaneb are direct horizontal competitors in the provision of terminaling services for bulk suppliers of refining components, most blending components, and light petroleum products in Northern California. The other participants are Tesoro, ConocoPhillips, Shell, and Chevron. BP and IMTT also participate in this market. However, these terminals have constrained access to the Kinder Morgan pipeline system.
51. Kaneb is an independent commercial terminal operator. Kaneb does not own or sell any light petroleum products to

Complaint

wholesale or commercial customers. Thus, Kaneb derives its revenue solely from the provision of terminaling services, including receipt of bulk supplies.

52. Kinder Morgan owns the only common carrier pipeline that serves the interior of Northern California. This pipeline provides the only economic means of distributing light petroleum products to Northern California terminals outside of the East Bay.
53. Bulk supply of light petroleum products in Northern California comes from two sources: (1) domestic production by integrated refiner/terminal operators in Northern California and (2) imports via marine vessel by petroleum product traders, largely on behalf of, or for the integrated refiner/marketers in California.
54. Kaneb owns three terminals that participate in this market: Martinez, Richmond, and Selby. All three of the terminals are both accessible to the Kinder Morgan pipeline system and capable of receiving deepwater marine vessels.
55. Valero owns a refinery at Benicia and associated storage tanks. The refinery and associated tanks are used by Valero for its own terminaling and bulk supply needs. Valero L.P. controls crude storage facilities.
56. Post-transaction, Valero and Kaneb will control a significant share of bulk supply and terminaling services for light petroleum products in Northern California. The proposed transaction would significantly increase market concentration, and post-merger the market would be highly concentrated.

## Complaint

57. After the transaction, the combined firm could more effectively coordinate with others to raise prices in the market for bulk supply of and terminaling services for refining components, blending components, and light petroleum products in Northern California.
58. The Kaneb terminals are the only independent marine-accessible terminals with unconstrained access to the Kinder Morgan pipeline system. The Kaneb terminals are therefore the only terminals through which a products trader and other marketers can import and distribute light petroleum products throughout Northern California. Wholesale bulk prices in Northern California would likely increase without access to the Kaneb terminals. In addition, Kaneb provides storage to some Northern California refiners for blending components and feedstocks. Loss of access to this storage would likely result in reduced production at these refineries.

Northern California Bulk Ethanol Terminaling

59. The U.S. Environmental Protection Agency and the California Air Resources Board have mandated the use of oxygenates at various times and in various places in California. Federal regulations require oxygenated gasoline year round in the counties of Los Angeles, Ventura, San Bernardino (partial), Riverside (partial), San Diego, Sacramento, Yolo, El Dorado (partial), Placer (partial), Solano (partial), and Sutter (partial). California regulations require oxygenated gasoline year round in the counties listed above and in Imperial County from November 1 through February 2.
60. California has prohibited the use of oxygenates such as methyl tert butyl ether ("MTBE"). Ethanol is the oxygenate of choice in areas where oxygenated gasoline is required by the U.S. Environmental Protection Agency.

*Complaint*

61. Ethanol requires its own storage and cannot be commingled with other light petroleum products. Ethanol can be shipped in bulk quantities from production facilities into California only by rail or by marine vessel. Ethanol cannot be brought into the state by pipeline. Once bulk ethanol shipments have been placed in storage, tank trucks transport ethanol to outlying terminals, where it can be placed in smaller storage tanks pending final blending with pre-oxygenated gasoline (“CARBOB”) at the truck rack.
62. Kaneb’s Richmond, Selby, and Stockton terminals are the only terminals in Northern California not associated with refineries capable of receiving and distributing bulk volumes of ethanol. Northern California terminals could not be economically supplied with ethanol trucked from Southern California or other locations.
63. Because satellite terminals must receive ethanol supplies by truck, trucking economics strongly influence which bulk ethanol terminal will supply ethanol to finished gasoline terminals.
64. Valero Energy is a significant user and supplier of ethanol for its own finished gasoline sales.
65. After the proposed transaction, Valero could increase prices for or deny access to bulk ethanol terminaling services, causing increased prices for, or reduced supply of, ethanol or finished CARB gasoline.

*Entry*

66. Entry into the relevant markets into relevant sections of the country would be difficult and would not be likely, timely, or sufficient to prevent the anticompetitive effects that are likely to result from the proposed transaction.

Complaint

**IV. VIOLATIONS CHARGED****First Violation Charged**

67. Valero L.P. and Kaneb are competitors in the market for terminaling services for bulk suppliers of light petroleum products in the Greater Philadelphia Area.
68. The effect of the proposed transaction, if consummated, may be substantially to lessen competition in the provision of terminaling services for light petroleum products and the bulk supply of light petroleum products in the Greater Philadelphia Area, in violation of Section 7 of the Clayton Act, as amended, 15 U.S.C. § 18, and Section 5 of the Federal Trade Commission Act, as amended, 15 U.S.C. § 45, in the following ways, among others:
  - a. by eliminating direct competition between Valero and Kaneb in the provision of terminaling services for bulk suppliers of light petroleum products;
  - b. by increasing the likelihood of, or facilitating, collusion or coordinated interaction between the combination of Valero and Kaneb and their competitors in the provision of terminaling services for bulk suppliers; and
  - c. by increasing the likelihood of, or facilitating, collusion or coordinated interaction between Valero and the other bulk suppliers of light petroleum products;each of which increases the likelihood that the wholesale price of light petroleum products will increase in the relevant section of the country.

Complaint

**Second Violation Charged**

69. Valero and Kaneb are competitors in pipeline transportation and terminaling services for bulk suppliers of light petroleum products in the Colorado Front Range.
70. The effect of the proposed transaction, if consummated, may be substantially to lessen competition in the provision of terminaling services for light petroleum products and the bulk supply of light petroleum products to the Colorado Front Range, and in narrower markets contained therein, in violation of Section 7 of the Clayton Act, as amended, 15 U.S.C. § 18, and Section 5 of the Federal Trade Commission Act, as amended, 15 U.S.C. § 45, in the following ways, among others:
  - a. by eliminating direct competition between Valero and Kaneb in the provision of pipeline transportation and terminaling services for bulk suppliers of light petroleum products;
  - b. by increasing the likelihood of, or facilitating, collusion or coordinated interaction between the combination of Valero and Kaneb and their competitors in the provision of pipeline transportation and terminaling services for bulk suppliers;
  - c. by increasing the likelihood that the combination of Valero and Kaneb will unilaterally exercise market power in the provision of pipeline transportation and terminaling services for bulk suppliers of light petroleum products in the Colorado Springs area; and
  - d. by increasing the likelihood of, or facilitating, collusion or coordinated interaction between Valero and the other bulk suppliers of light petroleum products;

## Complaint

each of which increases the likelihood that wholesale prices of light petroleum products will increase in the relevant sections of the country.

**Third Violation Charged**

71. Valero and Kaneb are competitors in terminaling services for bulk suppliers of refining components, blending components, and light petroleum products in Northern California.
72. The effect of the proposed transaction, if consummated, may be substantially to lessen competition in the provision of terminaling services for crude oil, light petroleum products, blend components, and intermediate refinery feedstocks, and the bulk supply of light petroleum products and blend components (including ethanol) in Northern California, in violation of Section 7 of the Clayton Act, as amended, 15 U.S.C. § 18, and Section 5 of the Federal Trade Commission Act, as amended, 15 U.S.C. § 45, in the following ways, among others:
  - a. by eliminating direct competition between Valero and Kaneb in the provision of terminaling services for bulk suppliers of crude oil, refining components, light petroleum products, blend components, and intermediate refinery feedstocks,
  - b. by increasing the likelihood of, or facilitating, collusion or coordinated interaction between the combination of Valero and Kaneb and their competitors in the provision of terminaling services for bulk suppliers; and
  - c. by increasing the likelihood of, or facilitating, collusion or coordinated interaction between Valero and the other bulk suppliers of light petroleum products;



Complaint

each of which increases the likelihood that wholesale prices of light petroleum products will increase in the relevant section of the country.

**Fourth Violation Charged**

73. Kaneb provides services in the upstream market for terminaling for bulk ethanol in Northern California through its terminals at Selby and Stockton. No other independent terminals in Northern California can economically receive and distribute bulk supplies of ethanol.
74. Valero Energy is a significant user of ethanol for the oxygenation of gasoline and a significant seller in the downstream market for CARB gasoline in Northern California.
75. Valero could use information on the use of Kaneb's ethanol terminaling facilities to facilitate collusion in the bulk supply of CARB gasoline in Northern California.
76. The effect of the proposed transaction, if consummated, may be substantially to lessen competition in bulk supply of CARB gasoline in Northern California, in violation of Section 7 of the Clayton Act, as amended, 15 U.S.C. § 18, and Section 5 of the Federal Trade Commission Act, as amended, 15 U.S.C. § 45, by increasing the likelihood of collusion, which would increase prices of CARB gasoline in the relevant section of the country.

**Statutes Violated**

The proposed transaction between Valero L.P. and Kaneb violates Section 5 of the Federal Trade Commission Act, as amended, 15 U.S.C. § 45, and would, if consummated, violate Section 7 of the Clayton Act, as amended, 15 U.S.C. § 18, and Section 5 of the Federal Trade Commission Act, as amended, 15 U.S.C. § 45.

## Complaint

WHEREFORE, THE PREMISES CONSIDERED, the Federal Trade Commission on this fourteenth day of June, 2005, issues its complaint against said Respondents.

Decision and Order

## **DECISION AND ORDER**

The Federal Trade Commission (“Commission”), having initiated an investigation of the proposed acquisition by Respondent Valero L.P. of Respondent Kaneb Services LLC and Respondent Kaneb Pipe Line Partners, L.P., and Respondents having been furnished thereafter with a copy of a draft of Complaint that the Bureau of Competition proposed to present to the Commission for its consideration and which, if issued by the Commission, would charge Respondents with violations of Section 7 of the Clayton Act, as amended, 15 U.S.C. § 18, and Section 5 of the Federal Trade Commission Act, as amended, 15 U.S.C. § 45; and

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

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

## Decision and Order

1. Respondent Valero Energy Corporation is a corporation, organized, existing, and doing business under and by virtue of the laws of the state of Delaware, with its office and principal place of business located at One Valero Way, San Antonio, Texas 78249.

2. Respondent Valero L.P. is a publicly-traded limited partnership, organized, existing, and doing business under and by virtue of the laws of the state of Delaware, with its office and principal place of business located at One Valero Way, San Antonio, Texas 78249.

3. Respondent Kaneb Pipe Line Partners, L.P. is a publicly-traded limited partnership, organized, existing, and doing business under and by virtue of the laws of the state of Delaware, with its office and principal place of business located at 2435 North Central Expressway, Richardson, Texas 75080.

4. Respondent Kaneb Services LLC is a publicly-traded limited liability company, organized, existing, and doing business under and by virtue of the laws of the state of Delaware, with its office and principal place of business located at 2435 North Central Expressway, Richardson, Texas 75080.

5. The Federal Trade Commission has jurisdiction of the subject matter of this proceeding and of Respondents, and the proceeding is in the public interest.

**ORDER****I.**

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

- A. “Valero” means Valero L.P., its general partners, directors, officers, employees, agents, representatives, predecessors, successors, and assigns; its joint ventures, subsidiaries, divisions, groups and affiliates controlled by Valero, and

Decision and Order

the respective directors, officers, employees, agents, representatives, predecessors, successors, and assigns of each. Valero includes Riverwalk Logistics, L.P., and Valero G.P., LLC. Valero does not include VEC.

- B. “VEC” means Valero Energy Corporation, its directors, officers, employees, agents, representatives, predecessors, successors, and assigns; its joint ventures, subsidiaries, divisions, groups and affiliates controlled by VEC, and the respective directors, officers, employees, agents, representatives, predecessors, successors, and assigns of each. VEC does not include Riverwalk Logistics, L.P., Valero GP, LLC, or Valero.
- C. “KPP” means Kaneb Pipe Line Partners, LP, its general partners, directors, officers, employees, agents, representatives, predecessors, successors, and assigns; its joint ventures, subsidiaries, divisions, groups and affiliates controlled by KPP, and the respective directors, officers, employees, agents, representatives, predecessors, successors, and assigns of each.
- D. “KSL” means Kaneb Services LLC, its directors, officers, employees, agents, representatives, predecessors, successors, and assigns; its joint ventures, subsidiaries, divisions, groups and affiliates controlled by KSL; and the respective partners, directors, officers, employees, agents, representatives, successors, and assigns of each.
- E. ”Acquirer” means a Person that receives the prior approval of the Commission to acquire assets to be divested pursuant to Paragraphs II., III., IV., or V. of this Order.
- F. ”Alternative San Francisco Bay Terminals” means the San Francisco Bay Terminals and the Selby Terminal.
- G. “Commission” means the Federal Trade Commission.

## Decision and Order

- H. “Kaneb” means Kaneb Services LLC and Kaneb Pipe Line Partners, L.P., collectively and individually.
- I. “Merger” means the merger of Valero and Kaneb pursuant to: (1) the Agreement and Plan of Merger, dated as of October 31, 2004, by and among Valero L.P.; Riverwalk Logistics, L.P.; Valero GP LLC; VLI Sub A LLC; and Kaneb Services LLC; and (2) the Agreement and Plan of Merger, dated as of October 31, 2004, by and among Valero L.P.; Riverwalk Logistics, L.P.; Valero GP LLC; VLI Sub B LLC; Kaneb Pipe Line Partners, L.P.; and Kaneb Pipe Line Company LLC.
- J. “Non-Public Customer Information” means any information that is not in the public domain relating to the shipment (including but not limited to volume information, timing of shipments, and end-customer identification), receipt, scheduling, rates, or inventory of products by customers of the Retained San Francisco Bay Terminals.
- K. “Person” means any individual, partnership, firm, trust, association, corporation, joint venture, unincorporated organization, or other business or governmental entity.
- L. “Philadelphia Area Terminals” means Kaneb’s one Paulsboro, New Jersey, and two Philadelphia, Pennsylvania, refined petroleum product storage and distribution terminals and all assets relating to each of the terminals, including but not limited to:
1. all of Kaneb’s rights, title, and interest in and to all tangible assets that are located at, or used in connection with Terminaling at, the terminals, including but not limited to:
    - a. real estate, including existing rights or way and easements;
    - b. storage tanks;
    - c. local connector pipelines;

Decision and Order

- d. loading and unloading racks, equipment and facilities;
  - e. inventory, equipment, pumps, compressors, machinery, fixtures, tools, and spare parts;
  - f. all books, records, and files relating to the terminals;
  - g. offices, buildings, and warehouses; and
  - h. all other tangible assets;
2. an exclusive right to all intellectual property used solely in the operation of the terminals, and a non-exclusive license to all other intellectual property necessary for the operation of the terminals;
  3. all governmental licenses and permits used in the operation of the terminals;
  4. all storage, throughput, and Terminaling contracts, and all other contracts, agreements or understandings relating to the terminals or their operation; and
  5. all other intangible assets.
- M. “Respondents” means:
1. before the Merger, Valero, VEC, KSL, and KPP, individually and collectively, and
  2. after the Merger, Valero, VEC, and the entity surviving after the Merger.
- N. “Retained San Francisco Bay Terminals” means:
1. If the San Francisco Bay Terminals are divested pursuant to Paragraph IV.A. of the Order, the terminals located at Stockton and Selby, California, which at the time of the Merger were owned by Kaneb; but
  2. If the Alternative San Francisco Bay Terminals are divested pursuant to Paragraph V.C.3. of this Order, the terminal located at Stockton, California, which at the time of the Merger was owned by Kaneb.
- O. “San Francisco Bay Terminals” means Kaneb’s Martinez and Richmond, California, refined petroleum product storage and distribution terminals and all assets relating to the two terminals, including but not limited to:

## Decision and Order

1. all of Kaneb's rights, title, and interest in and to all tangible assets that are located at, or used in connection with Terminaling at, the two terminals, including but not limited to:
    - a. real estate, including existing rights or way and easements;
    - b. storage tanks;
    - c. local connector pipelines;
    - d. loading and unloading racks, equipment and facilities;
    - e. inventory, equipment, pumps, compressors, machinery, fixtures, tools, and spare parts;
    - f. all books, records, and files relating to the two terminals;
    - g. offices, buildings, and warehouses; and
    - h. all other tangible assets;
  2. an exclusive right to all intellectual property used solely in the operation of the terminals, and a non-exclusive license to all other intellectual property necessary for the operation of the terminals;
  3. all governmental licenses and permits used in the operation of the terminals;
  4. all storage, throughput, and Terminaling contracts, and all other contracts, agreements or understandings relating to the terminals or their operation; and
  5. all other intangible assets.
- P. "Selby Terminal" means the Kaneb terminal located at 90 San Pablo Avenue, Crockett, California 94525.
- Q. "Terminaling" means the services performed by a facility that provides temporary storage of refined petroleum products received via pipeline, marine vessel, tank trucks, rail, or transport trailers, and the re-delivery of refined petroleum products from storage tanks into tank trucks, rail cars, transport trailers, or pipelines.
- R. "West Pipeline System" means Kaneb's West Pipeline System of approximately 550 miles of refined petroleum



Decision and Order

products pipelines, originating near Casper, Wyoming, and terminating in Rapid City, South Dakota, and Colorado Springs, Colorado; four refined petroleum products terminals; and numerous pump stations; and all assets relating to Kaneb's West Pipeline System, including but not limited to:

1. all of Kaneb's rights, title, and interest in and to all tangible assets relating to Kaneb's West Pipeline System, including but not limited to all of Kaneb's rights, title, and interest in and to all tangible assets that are located at, or used in connection with Terminaling at, all terminals owned by Kaneb located anywhere on the West Pipeline System (including the Kaneb terminals in Rapid City, South Dakota; Cheyenne, Wyoming; Dupont, Colorado; and Fountain, Colorado), including but not limited to:
  - a. real estate, including existing rights or way and easements;
  - b. storage tanks;
  - c. local connector pipelines;
  - d. loading and unloading racks, equipment and facilities;
  - e. inventory, equipment, pumps, compressors, machinery, fixtures, tools, and spare parts;
  - f. all books, records, and files relating to the West Pipeline System or the terminals;
  - g. offices, buildings, and warehouses; and
  - h. all other tangible assets relating to the West Pipeline System;
2. an exclusive right to all intellectual property used solely in the operation of the West Pipeline System and the terminals located on that system, and a non-exclusive license to all other intellectual property necessary for the operation of the West Pipeline System and the terminals located on that system;
3. all governmental licenses and permits used in the operation of the West Pipeline System and the terminals located on that system;

## Decision and Order

4. all storage, throughput, and Terminaling contracts, and all other contracts, agreements or understandings relating to the West Pipeline System or the terminals located on that system or their operation; and
5. all other intangible assets relating to the West Pipeline System and the terminals located on that system.

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

- A. Respondents shall divest the West Pipeline System absolutely and in good faith, at no minimum price, within six (6) months after the date on which the Merger is effectuated.
- B. Respondents shall divest the West Pipeline System only to a single Acquirer that receives the prior approval of the Commission and only in a manner that receives the prior approval of the Commission.
- C. In the event that Respondents are unable to satisfy all conditions necessary to divest any intangible asset, Respondents shall: (1) with respect to permits, licenses or other rights granted by governmental authorities (other than patents), provide such assistance as the Acquirer may reasonably request in the Acquirer's efforts to obtain comparable permits, licenses or rights, and (2) with respect to other intangible assets (including patents and contractual rights), substitute equivalent assets or arrangements, subject to the prior approval of the Commission. A substituted asset or arrangement will not be deemed to be equivalent unless it enables the pipeline or terminal to perform the same function at the same or less cost.
- D. The purpose of this Paragraph II. is to ensure the continued use of the West Pipeline System in the same business in

Decision and Order

which it was engaged at the time of the announcement of the proposed Merger and to remedy the lessening of competition in the pipeline transportation and Terminaling of light petroleum products resulting from the proposed Merger, as alleged in the Commission's Complaint.

**III.**

**IT IS FURTHER ORDERED** that:

- A. Respondents shall divest the Philadelphia Area Terminals absolutely and in good faith, at no minimum price, within six (6) months after the date on which the Merger is effectuated.
- B. Respondents shall divest the Philadelphia Area Terminals only to a single Acquirer that receives the prior approval of the Commission and only in a manner that receives the prior approval of the Commission.
- C. In the event that Respondents are unable to satisfy all conditions necessary to divest any intangible asset, Respondents shall: (1) with respect to permits, licenses or other rights granted by governmental authorities (other than patents), provide such assistance as the Acquirer may reasonably request in the Acquirer's efforts to obtain comparable permits, licenses or rights, and (2) with respect to other intangible assets (including patents and contractual rights), substitute equivalent assets or arrangements, subject to the prior approval of the Commission. A substituted asset or arrangement will not be deemed to be equivalent unless it enables the pipeline or terminal to perform the same function at the same or less cost.
- D. The purpose of this Paragraph III. is to ensure the continued use of the Philadelphia Area Terminals in the

## Decision and Order

same business in which they were engaged at the time of the announcement of the proposed Merger and to remedy the lessening of competition in the Terminaling of light petroleum products resulting from the proposed Merger, as alleged in the Commission's Complaint.

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

- A. Respondents shall divest the San Francisco Bay Terminals absolutely and in good faith, at no minimum price, within six (6) months after the date on which the Merger is effectuated.
- B. Respondents shall divest the San Francisco Bay Terminals only to a single Acquirer that receives the prior approval of the Commission and only in a manner that receives the prior approval of the Commission.
- C. In the event that Respondents are unable to satisfy all conditions necessary to divest any intangible asset, Respondents shall: (1) with respect to permits, licenses or other rights granted by governmental authorities (other than patents), provide such assistance as the Acquirer may reasonably request in the Acquirer's efforts to obtain comparable permits, licenses or rights, and (2) with respect to other intangible assets (including patents and contractual rights), substitute equivalent assets or arrangements, subject to the prior approval of the Commission. A substituted asset or arrangement will not be deemed to be equivalent unless it enables the pipeline or terminal to perform the same function at the same or less cost.
- D. The purpose of this Paragraph IV. is to ensure the continued use of the San Francisco Bay Terminals in the same business in which they were engaged at the time of the announcement of the proposed Merger and to remedy

Decision and Order

the lessening of competition in the Terminaling of refining components, blending components, and light petroleum products resulting from the proposed Merger, as alleged in the Commission's Complaint.

V.

**IT IS FURTHER ORDERED** that:

- A. If Respondents have not divested the West Pipeline System, the Philadelphia Area Terminals, or the San Francisco Bay Terminals, absolutely and in good faith, as required by Paragraphs II., III., or IV., respectively, of this Order, the Commission may appoint a trustee to divest the applicable assets as described in Paragraph V.C. below, in a manner that satisfies the requirements of Paragraphs II., III., or IV., of this Order, whichever is applicable.
- B. In the event that the Commission or the U.S. Attorney General brings an action pursuant to § 5(*l*) of the Federal Trade Commission Act, 15 U.S.C. § 45(*l*), or any other statute enforced by the Commission, Respondents shall consent to the appointment of a trustee in such action to divest the respective assets in accordance with the terms of this Order. Neither the appointment of a trustee nor a decision not to appoint a trustee under this Paragraph shall preclude the Commission or the U.S. Attorney General from seeking civil penalties or any other relief available to it, including a court-appointed trustee, pursuant to § 5(*l*) of the Federal Trade Commission Act, or any other statute enforced by the Commission, for any failure by Respondents to comply with this Order.
- C. If Respondents have not satisfied the requirements of
  1. Paragraphs II.A and II.B. of this Order, the Commission may appoint a trustee to divest the West Pipeline System;

## Decision and Order

2. Paragraphs III.A. and III.B. of this Order, the Commission may appoint a trustee to divest the Philadelphia Area Terminals
  3. Paragraphs IV.A. and IV.B. of this Order, the Commission may appoint a trustee to divest the San Francisco Bay Terminals or the Alternative San Francisco Bay Terminals.
- D. The Commission shall select the trustee, subject to the consent of Valero, which consent shall not be unreasonably withheld. The trustee shall be a person with experience and expertise in acquisitions and divestitures. If Valero has not opposed, in writing, including the reasons for opposing, the selection of any proposed trustee within ten (10) days after notice by the staff of the Commission to Valero of the identity of any proposed trustee, Valero shall be deemed to have consented to the selection of the proposed trustee.
- E. Within ten (10) days after appointment of a trustee, Valero shall execute a trust agreement that, subject to the prior approval of the Commission, transfers to the trustee all rights and powers necessary to permit the trustee to effect the divestiture required by this Order.
- F. If a trustee is appointed by the Commission or a court pursuant to this Order, Respondents shall consent to the following terms and conditions regarding the trustee's powers, duties, authority, and responsibilities:
1. Subject to the prior approval of the Commission, the trustee shall have the exclusive power and authority to divest assets as required by this Order.
  2. The trustee shall have twelve (12) months from the date the Commission approves the trust agreement described herein to accomplish the required divestiture, which shall be subject to the prior approval of the Commission. If,

Decision and Order

however, at the end of the twelve (12) month period, the trustee has submitted a divestiture plan or believes that the divestiture can be achieved within a reasonable time, the divestiture period may be extended by the Commission; *provided, however*, the Commission may extend the divestiture period for no more than two (2) additional periods of twelve (12) months each.

3. The trustee shall have full and complete access to the personnel, books, records, and facilities related to the assets to be divested and to any other relevant information, as the trustee may request. Respondents shall develop such financial or other information as the trustee may request and shall cooperate with the trustee. Respondents shall take no action to interfere with or impede the trustee's accomplishment of the divestiture. Respondents shall cooperate with the efforts of the trustee to divest the required assets. Any delays in divestiture caused by Respondents shall extend the time for divestiture under this Paragraph V. in an amount equal to the delay, as determined by the Commission.
4. The trustee shall use commercially reasonable best efforts to negotiate the most favorable price and terms available in each contract that is submitted to the Commission, subject to Respondents absolute and unconditional obligation to divest expeditiously and at no minimum price. The divestiture shall be made only in a manner that receives the prior approval of the Commission and only to an Acquirer that receives the prior approval of the Commission; *provided, however*, if the trustee receives bona fide offers from more than one acquiring entity, and if the Commission determines to approve more than one such acquiring entity, the trustee shall divest to the acquiring entity selected by Valero from among those approved by the Commission; *provided further, however*, that Valero shall select such

## Decision and Order

entity within five (5) days of receiving notification of the Commission's approval.

5. The trustee shall serve, without bond or other security, at the cost and expense of Valero, on such reasonable and customary terms and conditions as the Commission may set. The trustee shall have the authority to employ, at the cost and expense of Valero, such consultants, accountants, attorneys, investment bankers, business brokers, appraisers, and other representatives and assistants as are necessary to carry out the trustee's duties and responsibilities. The trustee shall account for all monies derived from the divestiture and all expenses incurred. After approval by the Commission, of the account of the trustee, including fees for the trustee's services, all remaining monies shall be paid at the direction of Valero, and the trustee's power shall be terminated. The compensation of the trustee shall be based at least in significant part on a commission arrangement contingent on the divestiture of assets as required by this Order.
6. Valero shall indemnify the trustee and hold the trustee harmless against any losses, claims, damages, liabilities, or expenses arising out of, or in connection with, the performance of the trustee's duties, including all reasonable fees of counsel and other expenses incurred in connection with the preparation for, or defense of, any claim, whether or not resulting in any liability, except to the extent that such losses, claims, damages, liabilities, or expenses result from misfeasance, gross negligence, willful or wanton acts, or bad faith by the trustee.
7. The trustee shall have no obligation or authority to operate or maintain the assets required to be divested pursuant to this paragraph.



Decision and Order

8. The trustee shall act in a fiduciary capacity for the benefit of the Commission.
  9. The trustee shall report in writing to the Commission every sixty (60) days concerning the trustee's efforts to accomplish the divestiture.
  10. Valero may require the trustee and each of the trustee's consultants, accountants, attorneys, and other representatives and assistants to sign a customary confidentiality agreement; *provided, however*, such agreement shall not restrict the trustee from providing any information to the Commission.
- G. If the Commission determines that a trustee has ceased to act or failed to act diligently, the Commission may appoint a substitute trustee in the same manner as provided in this Paragraph V.
- H. The Commission may on its own initiative or at the request of the trustee issue such additional orders or directions as may be necessary or appropriate to accomplish the divestiture required by this Order.

**VI.**

**IT IS FURTHER ORDERED** that:

- A. Valero shall not, directly or indirectly, provide, disclose, or otherwise make available any Non-Public Customer Information to VEC; *provided, however*, that Valero may provide Non-Public Customer Information only to VEC personnel whose responsibilities do not involve refining, supply, or marketing operations in the State of California and only for the purposes listed below:
1. to ensure compliance with legal and regulatory requirements; to perform required auditing functions; to

## Decision and Order

provide accounting, information technology and credit-underwriting services, to provide legal services associated with actual or potential litigation and transactions; and to monitor and ensure compliance with governmental environmental, health, and safety requirements; or

2. for inclusion within the periodic financial reports that Valero may provide VEC but only to the extent that any Non-Public Customer Information is aggregated so that data as to individual customers are not disclosed.

B. VEC shall not use any Non-Public Customer Information obtained from Valero except for the purposes listed in VI.A.2., above.

C. Respondents shall operate the Retained San Francisco Bay Terminals in a reasonable and non-discriminatory manner and shall ensure that all customers and prospective customers of commingled Terminaling of ethanol at the Retained San Francisco Bay Terminals have access to commingled Terminaling of ethanol on terms and conditions consistent with past practices, but in no event on terms and conditions less advantageous than those given VEC for like services under like circumstances. The terms and conditions Respondent will maintain include, but are not limited to:

1. Respondents shall provide access to the Retained San Francisco Bay Terminals to offload into or withdraw from the commingled tanks ethanol on a first-come-first-serve nondiscriminatory basis, subject, where applicable, to (1) standard notice of readiness and scheduling procedures for all products, and (2) preference for shipments of the U.S. Department of Defense.
2. Respondent shall continue the current procedure of permitting a customer to withdraw from the commingled

Decision and Order

tanks the ethanol inventory of another customer, upon written approval of both affected customers.

- D. Respondents shall take steps to ensure that all of their employees comply with the requirements of subparagraphs VI.A., B. and C., above, including establishing and disseminating applicable policies and procedures to all employees no later than 30 (thirty) days after the Order becomes final.
- E. Valero shall provide written notification to the staff of the Commission at least 30 (thirty) days prior to leasing to VEC the use, on an exclusive basis, of any of the tanks (or any portion thereof) at the Retained San Francisco Bay Terminals that, as of the date Respondents executed the Consent Agreement, was designated for commingled storage of ethanol; *provided, however*, that such notice is not required for tanks leased to VEC at the Selby Terminal so long as at least four hundred thousand (400,000) shell barrels of tankage remains designated for commingled storage of ethanol at the Selby Terminal.
- F. The purpose of this Paragraph VI. is to ensure continued access to the Retained San Francisco Bay Terminals for customers at least at the same level of access that they had at the time of the announcement of the proposed Merger and to remedy the lessening of competition in the Terminaling of bulk ethanol resulting from the proposed Merger, as alleged in the Commission's Complaint.

**VII.**

**IT IS FURTHER ORDERED** that:

- A. For a period commencing on the date this Order becomes final and continuing for ten (10) years, Respondents shall not, without prior written notification to the Commission,

## Decision and Order

acquire, directly or indirectly, the Philadelphia Area Terminals or any portion thereof.

- B. The prior notification required by the Paragraph VII.A. shall be given on the Notification and Report Form set forth in the Appendix to Part 803 of Title 16 of the Code of Federal Regulations as amended (hereinafter referred to as the “Notification”), and shall be prepared and transmitted in accordance with the requirements of that part, except that no filing fee will be required for any such Notification, Notification shall be filed with the Secretary of the Commission, Notification need not be made to the United States Department of Justice, and Notification is required only of Respondents and not of any other party to the transaction. Respondents shall provide the Notification to the Secretary of the Commission at least thirty (30) days prior to consummating any such transaction (hereinafter referred to as the “first waiting period”). If, within the first waiting period, representatives of the Commission make a written request for additional information or documentary material (within the meaning of 16 C.F.R. § 803.20), Respondents shall not consummate the transaction until thirty (30) days after submitting such additional information or documentary material. Early termination of the waiting periods in this Paragraph may be requested and, where appropriate, granted by letter from the Commission’s Bureau of Competition; *provided, however*, that prior notification shall not be required by this Paragraph for a transaction for which notification is required to be made, and has been made, pursuant to Section 7A of the Clayton Act, 15 U.S.C. § 18a.

**VIII.**

**IT IS FURTHER ORDERED** that:

- A. Within thirty (30) days after the initial report is required to be filed pursuant to the Consent Agreement in this matter,

Decision and Order

and every sixty (60) days thereafter until Respondents have fully complied with Paragraphs II., III., IV., or V. of this Order, Respondents shall submit to the Commission a verified written report setting forth in detail the manner and form in which they intend to comply, are complying, and have complied with this Order; *provided, however*, that Respondents may consolidate all required information into one report and submit one consolidated report on behalf of all Respondents. Respondents shall include in the reports, among other things that are required from time to time, a full description of the efforts being made to comply with the relevant Paragraphs of the Order, including a description of all substantive contacts or negotiations related to the divestiture of the relevant assets and the identity of all parties contacted. Respondents shall include in the reports copies of all written communications to and from such parties, all internal memoranda, and all reports and recommendations concerning its obligations under this Order.

- B. One (1) year from the date this Order becomes final, annually for the next nine (9) years on the anniversary of the date this Order becomes final, and at other times as the Commission may require, Respondents shall file a verified written report with the Commission setting forth in detail the manner and form in which they have complied and are complying with this Order.

**IX.**

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

## Decision and Order

**X.**

**IT IS FURTHER ORDERED** that, for the purpose of determining or securing compliance with this Order, and subject to any legally recognized privilege, and upon written request with reasonable notice to any Respondent, Respondents shall permit any duly authorized representative of the Commission:

- A. Access, during office hours of that Respondent and in the presence of counsel, to all facilities and access to inspect and copy all books, ledgers, accounts, correspondence, memoranda, and all other records and documents in the possession or under the control of that Respondent related to compliance with this Order; and
- B. Upon five (5) days' notice to that Respondent and without restraint or interference from that Respondent, to interview officers, directors, or employees of that Respondent, who may have counsel present, regarding such matters.

**XI.**

**IT IS FURTHER ORDERED** that if: (1) within the time period required for divestiture pursuant to Paragraphs II., III., or IV., of this Order, Respondents have submitted a complete application in support of the applicable divestiture (including the acquirer, manner of divestiture, and all other matters subject to Commission approval) as required by such paragraphs; and (2) the Commission has approved the applicable divestiture and has not withdrawn its acceptance; but (3) Respondents have certified to the Commission prior to the expiration of the applicable time period that (a) notwithstanding timely and complete application for approval by Respondents to the State of California under an applicable consent decree to which the State of California and Respondents are parties, the State of California has failed to approve the divestiture that is also required under this Order, or (b) the State of California has filed a timely motion in court seeking to enjoin the proposed divestiture or other relief under an

Decision and Order

applicable consent decree to which the State of California and Respondents are parties, then, (4) with respect to the particular divestiture that remains unconsummated, the time in which the divestiture is required under this Order to be complete shall be extended (a) for ninety (90) days or (b) until the disposition of the motion filed by the State of California pertaining to the proposed divestiture, whichever is later. During such period of extension, Respondents shall exercise utmost good faith and best efforts to resolve the concerns of the State of California.

**XII.**

**IT IS FURTHER ORDERED** that this Order shall terminate ten (10) years from the date this Order becomes final.

By the Commission.

Analysis

**Analysis of Proposed Consent Order To Aid Public Comment****I. Introduction**

The Federal Trade Commission (“Commission” or “FTC”) has issued a complaint (“Complaint”) alleging that Valero L.P.’s proposed acquisition of Kaneb Services LLC and Kaneb Pipe Line Partners, L.P. (collectively “Kaneb”) would violate Section 7 of the Clayton Act, as amended, 15 U.S.C. § 18, and Section 5 of the Federal Trade Commission Act, as amended, 15 U.S.C. § 45, and has entered into an agreement containing consent orders (“Agreement Containing Consent Orders”) pursuant to which Valero L.P., Valero Energy, and Kaneb (collectively “Respondents”) agree to be bound by a proposed consent order that requires divestiture of certain assets (“Proposed Consent Order”) and a hold separate order that requires Respondents to hold separate and maintain certain assets pending divestiture (“Hold Separate Order”). The Proposed Consent Order remedies the likely anticompetitive effects arising from the proposed acquisition, as alleged in the Complaint. The Hold Separate Order preserves competition pending divestiture.

**II. Description of the Parties and the Transaction**

Valero L.P. is a publicly traded master limited partnership based in San Antonio, Texas. Valero L.P. shares its headquarters with Valero Energy, which owns 46% of Valero L.P.’s common units. Valero L.P. is engaged in the transportation and storage of crude oil and refined petroleum products and currently derives 98% of its total revenues from services provided to Valero Energy. The remaining 2% of revenue is generated from third parties who pay fees to use Valero L.P.’s pipelines and terminals. Valero L.P. reported 2004 net income of \$78.4 million on total revenue of \$221 million.

Respondent Valero Energy Corporation is an independent domestic refining company, headquartered in San Antonio, Texas. It is engaged in national refining, transportation, and marketing of



Analysis

petroleum products and related petrochemical products. Valero Energy reported 2004 net income of \$1.8 billion on revenues of nearly \$55 billion.

Kaneb is a single company represented by two publicly traded entities: Kaneb Pipe Line Partners, L.P. (“KPP”) and Kaneb Services LLC (“KSL”). Kaneb owns and operates refined petroleum product pipelines and petroleum and specialty liquids storage and terminaling facilities. KPP is a master limited partnership that owns Kaneb’s pipeline and terminaling assets. KSL owns the general partnership in KPP and five million of KPP’s limited partnership units. KSL’s wholly owned subsidiary, Kaneb Pipeline Company LLC, manages and operates KPP’s pipeline and terminaling assets. KSL reported 2004 consolidated net income of \$24 million on total revenue of approximately \$1 billion.

Pursuant to the terms of the Agreements and Plans of Merger between Valero L.P. and the Kaneb entities, (1) Valero L.P. will pay \$525 million in cash for the entirety of KSL’s partnership units, and (2) Valero L.P. will exchange \$1.7 billion in Valero L.P. partnership units for all outstanding KPP partnership units. As a result of the transactions, both KSL and KPP will be wholly owned subsidiaries of Valero L.P., and Valero Energy’s equity ownership in Valero L.P. would be reduced to 23%.

### **III. The Investigation and the Complaint**

The Complaint alleges that the merger of Valero L.P. and Kaneb would violate Section 7 of the Clayton Act, as amended, 15 U.S.C. § 18, and Section 5 of the Federal Trade Commission Act, as amended, 15 U.S.C. § 45, by substantially lessening competition in each of the following markets: (1) terminaling services for bulk suppliers of light petroleum products in the Greater Philadelphia Area; (2) pipeline transportation and terminaling services for bulk suppliers of light petroleum products in the Colorado Front Range; (3) terminaling services for bulk suppliers of refining components, blending components, and light

## Analysis

petroleum products in Northern California; and (4) terminaling for bulk ethanol in Northern California.

To remedy the anticompetitive effects of the merger, the Proposed Consent Order requires Respondents to divest the following assets: (1) in the Greater Philadelphia Area, Kaneb's Paulsboro, New Jersey, Philadelphia North, and Philadelphia South terminals; (2) in the Colorado Front Range, Kaneb's West Pipeline system, which originates in Casper, Wyoming, and terminates in Rapid City, South Dakota, and Colorado Springs, Colorado, and includes Kaneb's terminals in Rapid City, South Dakota, Cheyenne, Wyoming, Denver, Colorado, and Colorado Springs, Colorado; and (3) in Northern California, Kaneb's Martinez and Richmond terminals. Finally, the Order also requires Valero L.P. not to discriminate in favor of or otherwise prefer Valero Energy in bulk ethanol terminaling services and to maintain customer information confidentiality at the Selby and Stockton terminals.

The Commission's decision to issue the Complaint and enter into the Agreement Containing Consent Orders was made after an extensive investigation in which the Commission examined competition and the likely effects of the merger in the markets alleged in the Complaint and in other markets.<sup>1</sup> The Commission has concluded that the merger is unlikely to reduce competition significantly in markets other than those alleged in the Complaint.

The Complaint alleges that the merger would violate the antitrust laws in four product and geographic markets, each of which is discussed below. The analysis applied in each market

---

<sup>1</sup> The Commission conducted the investigation leading to the Complaint in collaboration with the Attorney General of the State of California. As part of this joint effort, Respondents have entered into a State Decree with California settling charges that aspects of the transaction affecting California consumers would violate both state and federal antitrust laws.

Analysis

requiring structural relief follows the analysis set forth in the FTC and U.S. Department of Justice *Horizontal Merger Guidelines* (1997) (“*Merger Guidelines*”). The relief obtained in the bulk ethanol terminaling market is consistent with the Commission’s past remedies in similarly-structured mergers.

In addition, the Commission focused on the identity and corporate control of the merging parties. Valero Energy owns the general partner of Valero L.P. The general partner is presumed to exercise all operational rights afforded by the partnership agreements and applicable state corporation law. In light of this relationship, and for purposes of competitive analysis, the Commission attributes Valero Energy’s assets and incentives to Valero L.P. The Commission further determined that Valero Energy may have incentives to operate the Valero L.P. assets less competitively than would Kaneb, by maximizing product prices rather than terminal or pipeline revenues. Given the trend toward master limited partnerships holding midstream petroleum transportation and terminaling assets, Commission staff will continue to scrutinize the ownership and control of limited partnerships in its evaluation of midstream asset transactions. Where it appears an operator’s interests may be more closely aligned with downstream output reductions than increased transportation and terminaling throughput, the Commission will apply the analysis conducted during this investigation.

**Count I    Terminaling Services for Bulk Suppliers of Light Petroleum Products in the Greater Philadelphia Area**

The Complaint charges that the proposed merger would likely reduce competition in the market for terminaling services for bulk suppliers of light petroleum products in the Greater Philadelphia Area, thereby increasing the price for terminaling services and bulk supply of transportation fuels, by (1) eliminating direct competition between Valero L.P. and Kaneb; and (2) increasing the ability and likelihood of coordinated interaction between the combined company and its competitors in the Greater

## Analysis

Philadelphia Area. The proposed merger reduces the number of suppliers of terminaling services for transportation fuels and eliminates Kaneb as a source of imported transportation fuel, thereby increasing the likelihood of coordination.

Valero L.P. and Kaneb compete in the supply of terminaling services for bulk suppliers of light petroleum products in the Greater Philadelphia Area, a relevant antitrust market. Terminaling customers such as refiner-marketers, independent marketers, and traders rely on terminals to supply transportation fuel to the area. There are no substitutes for terminals in supplying and distributing transportation fuels in the Greater Philadelphia Area.

The Greater Philadelphia Area includes the city of Philadelphia, the Philadelphia suburbs, and portions of southern New Jersey and northern Delaware. Terminals outside the Greater Philadelphia Area are not economic substitutes for terminals within the area because of additional costs of transporting product by truck from more distant terminals. Post-merger, the remaining terminal operators could profitably impose a small but significant and nontransitory price increase in terminaling services for transportation fuels because no additional terminals can serve the Greater Philadelphia Area without significantly raising the cost of distributing fuel.

Seven firms currently provide terminaling services for transportation fuels in the Philadelphia area: Valero L.P., Kaneb, Sunoco, ConocoPhillips, Hess, Premcor, and ExxonMobil. Each of these firms owns or has contractual rights to one or more terminals in the Greater Philadelphia Area. The proposed merger would significantly increase market concentration, and post-merger the market would be highly concentrated. The change in market concentration understates the competitive significance of the merger because Kaneb is the only terminal system in the Greater Philadelphia Area capable of facilitating imports into the market.

Analysis

Valero L.P.'s purchase of Kaneb's terminals in the Greater Philadelphia Area would allow the remaining terminaling owners to profitably impose a small but significant and nontransitory price increase in the price of terminaling services. Eliminating Kaneb as an independent terminaling service competitor would have additional anticompetitive effects in the sale of bulk supplies of transportation fuels. Kaneb does not own or market any of the product in its terminals and earns its revenue solely from providing terminaling services to third parties. The other terminaling services providers, including Valero, also provide bulk supply to the market and sell their own transportation fuels through downstream marketing assets. These terminal owners use their terminal assets primarily for their own marketing needs and often do not provide terminaling services to third parties.

Because Kaneb does not earn any revenue from the sale of product, it has no economic interest in the price of the product. Kaneb's incentive is strictly to obtain as much third party terminaling business as it can. Thus, third party marketers can reliably use the Kaneb terminals to receive and throughput bulk supplies imported by pipeline and by water from outside the Greater Philadelphia Area. These imports are critical in maintaining a competitive market and to keeping prices low for transportation fuels in the Greater Philadelphia Area. The proprietary terminal operators have different incentives from Kaneb. As downstream marketers, higher product prices increase their profitability from their marketing operations, which typically accounts for a much larger portion of their business than terminaling. Post-merger, Valero would control the Kaneb terminals and could restrict access by third parties to these terminals. Without open access to the Kaneb terminals, it would be much more difficult for third party marketers to import product into the Greater Philadelphia Area. The elimination of imports would reduce competitive pressure on the local bulk suppliers, including Valero, thereby allowing them to maintain higher prices for bulk supplies of transportation fuel in the Greater Philadelphia Area.

## Analysis

Entry into the terminaling market is difficult and would not be timely, likely, or sufficient to preclude anticompetitive effects resulting from the proposed merger. Building a new terminal requires significant sunk costs and would be a very long process, in part due to lengthy permitting requirements. Converting a non-transportation fuel terminal is also expensive and time consuming, and would not be likely in the Greater Philadelphia Area.

The efficiencies proposed by the Respondent, to the extent they relate to this market, are not cognizable under the *Merger Guidelines*, and are small compared to the extent of the potential anticompetitive harm. Even if the proposed efficiencies were achieved, they would not be sufficient to reverse the merger's potential to raise the price of bulk supply and terminal services.

**Count II Pipeline Transportation and Terminaling Services for Bulk Suppliers of Light Petroleum Products in the Colorado Front Range**

The Complaint charges that the proposed acquisition would likely substantially reduce competition in pipeline transportation and terminaling services for bulk suppliers of light petroleum products in Denver and Colorado Springs by (1) eliminating direct competition between Valero L.P. and Kaneb, (2) increasing the ability and likelihood of coordinated interaction between the combined company and its competitors in the Denver area, and (3) eliminating all competition in Colorado Springs, making Valero L.P. a monopolist in pipeline transportation and terminaling services. While the relevant market is pipeline transportation and terminaling services, any purchaser of light petroleum products would have to pay for the product to get to the market through pipeline transportation and/or terminals. Therefore, a price increase in these relevant markets would also cause an increase in light petroleum products prices.

Valero L.P. and Kaneb compete in the pipeline transportation and terminaling services for bulk suppliers of light petroleum products in both Denver and Colorado Springs. While light

Analysis

petroleum products can be trucked to Denver and Colorado Springs, pipeline transportation is the only economic means to ship bulk supplies of light petroleum products to either Denver or Colorado Springs. There is no economically feasible substitute to pipeline transportation to reach these geographic areas.

Light petroleum products reach Denver and Colorado Springs through terminals that can receive product from either pipelines or refineries. Tank trucks pick up the light petroleum products from these local terminals and deliver them short haul distances to retail outlets and other customers. Terminals outside of Denver and Colorado Springs cannot economically supply those areas due to the costs of shipping light petroleum products by truck. Therefore, terminaling services provided by those terminals in the Denver and Colorado Springs areas is a relevant market.

Following the merger, the combined firm would control a significant share of bulk supply and terminaling services for light petroleum products in the Colorado Front Range. The proposed transaction would significantly increase market concentration, and post-merger the market would be highly concentrated. Moreover, the proposed transaction would result in the combined firm having a monopoly in the Colorado Springs area. The change in market concentration underestimates the likely competitive harm because it does not take into account how Valero L.P.'s incentives differ from Kaneb's current incentives in operating the Kaneb West Pipeline system.

Entry is difficult and would not be timely, likely, or sufficient to prevent anticompetitive effects arising from the proposed acquisition. Pipeline entry in Denver or Colorado Springs is very unlikely because of the high expense of constructing a new pipeline to these geographically isolated areas. It is highly improbable, if not impossible, that a new pipeline originating in a distant market could be both approved and constructed within the two-year period required by the *Merger Guidelines*.

## Analysis

Terminal entry in Denver or Colorado Springs is also very unlikely. Each refinery in and each pipeline to the Denver and Colorado Springs markets is accommodated by an existing terminal. Given the sufficient terminal capacity for the existing refinery and pipeline infrastructure, it is highly unlikely that a potential entrant could find a financial incentive to make a major investment, involving high sunk costs, in the construction of a new terminal.

The efficiency claims of the Respondents, to the extent they relate to these markets, are not cognizable under the *Merger Guidelines*, are small as compared to the magnitude of the potential harm, and would not be sufficient to reverse the merger's potential to raise the price of bulk supply and terminal services.

The proposed acquisition would create a highly concentrated market in Denver and Colorado Springs and create a presumption that the acquisition "will create or enhance market power or facilitate its exercise. . ." *Merger Guidelines* § 1.5(c). These anticompetitive effects could result from the coordinated interaction between Valero L.P. and the remaining firms with enough excess capacity to defeat a price increase in Denver, and from a unilateral reduction in supply or price increase instituted by Valero L.P. in Colorado Springs.

**Count III Terminaling Services for Bulk Suppliers of Refining Components, Blending Components, and Light Petroleum Products in Northern California**

The Complaint charges that the proposed acquisition would likely substantially reduce competition in terminaling services for bulk suppliers of refining components, blending components, and light petroleum products in Northern California by (1) eliminating direct competition between the firms in the provision of terminaling services for bulk suppliers of refining components, blending components, and light petroleum products, and (2) increasing the ability and likelihood of coordinated interaction between the combined company and its competitors in Northern



Analysis

California. Downstream effects will likely result in increased prices for light petroleum products.

Valero L.P. and Kaneb compete in providing terminaling services for bulk suppliers of refining components, blending components, and light petroleum products in Northern California. Refiner-marketers, independent marketers, and traders use Kaneb's three marine-accessible Northern California terminals to receive and store imported products and to distribute light petroleum products via pipeline to other Northern California terminals. In addition, refiners use the Kaneb terminals to store refining components, blending components, and light petroleum products that are needed to optimize production from their refineries. There are no substitutes for terminaling services for these products.

Northern California is a relevant geographic market. Due to trucking costs, firms need access to the Kinder Morgan intrastate pipeline to distribute bulk volumes of California gasoline and other light petroleum products throughout the state, and Southern California terminals are not connected to Kinder Morgan's Northern California pipeline network. In addition, constraints in Southern California terminal infrastructure make it unlikely that Southern California terminals could handle excess volume in the event of a Northern California terminal services price increase.

The market for terminaling services for bulk suppliers of refining components, blending components, and light petroleum products in Northern California will be highly concentrated following the proposed acquisition. Participants in the market include Kaneb and the five San Francisco Bay Area refiners (Valero Energy, Chevron Corp., ConocoPhillips, Shell, and Tesoro). Other terminals lack sufficient capacity into the Kinder Morgan pipeline system to transport excess product in the event of a price increase. The proposed acquisition would significantly increase market concentration, and post-merger the market would be highly concentrated.

## Analysis

Post-acquisition, Valero L.P. would have an incentive to increase light petroleum prices by restricting products moving into and through the three marine-accessible Kaneb terminals in Northern California. Valero L.P. could limit the amount of product reaching that market by (1) limiting out-of-state marine shipments of California-grade gasoline and other products into Northern California; (2) limiting the volume of product entering the Kinder Morgan pipeline system in Northern California; and (3) limiting the ability of other Bay Area refiners to produce California-grade gasoline by restricting their storage for refining components, blending components, and other products needed to optimize refinery output.

The acquisition increases the likelihood of coordinated interaction among the remaining market participants by eliminating the terminal services provider with different incentives. Kaneb is the only market participant that does not also own or market light petroleum products in Northern California. Because after the merger all market participants will benefit from higher prices for light petroleum products, Valero L.P.'s restriction of terminaling services would likely not trigger an offsetting response from its terminaling competitors.

Entry into the market for Northern California terminaling services for these products would not be likely or timely, for the reasons discussed in other terminal markets. Indeed, if anything, entry is even more difficult in California, given that the state imposes an extensive and costly permitting process that would prolong any attempt to secure and develop new terminal space.

The efficiency claims of the Respondents, to the extent they relate to any of these three markets with horizontal overlaps, are not cognizable under the *Merger Guidelines*, are small as compared to the magnitude of the potential harm, and would not be sufficient to reverse the merger's potential to raise the price of bulk supply and terminal services.

Analysis

**Count IV Terminating for Bulk Ethanol in Northern California**

The Complaint charges that the proposed acquisition would likely substantially reduce competition in terminaling services for bulk ethanol in Northern California by changing the owner of Kaneb's Selby and Stockton terminals. Ethanol is a necessary input in producing California-grade "CARB" gasoline. This is the Commission's first opportunity to examine a merger's competitive effects on ethanol since California adopted it as the preferred oxygenate.

In Northern California, Kaneb's Selby, Stockton, and Richmond terminals are the only terminals capable of receiving and storing bulk quantities of ethanol. From these terminals, ethanol is offloaded from large rail or marine shipments, placed into storage tanks, and loaded onto trucks for delivery to other nearby terminals. Once the ethanol reaches these other terminals, ethanol is blended at the truck rack to produce CARB gasoline.

Terminal services for bulk ethanol is the relevant product market. There are no substitutes for these services; large quantities of ethanol received from producers must be broken into smaller volumes for distribution to remote gasoline terminals. Because remote terminals must receive ethanol supplies by truck, the geographic market is limited to Northern California. It is simply not feasible to supply Northern California terminals with ethanol trucked from Southern California terminals. Similarly, customers currently using Kaneb's Stockton terminal would face additional trucking costs if forced to use either of Kaneb's Selby or Richmond terminals.

The proposed acquisition raises vertical issues relating to ethanol terminaling services with likely effects in finished gasoline sales. Valero Energy and the other Northern California refiners do not offer ethanol terminaling services that compete with Kaneb and would not likely be able to do so in the event of a price increase. Post-acquisition, Valero L.P.'s ownership of the

## Analysis

Kaneb terminals would give it control over an input necessary to finish gasoline for portions of Northern California. Valero Energy refines and markets CARB gasoline. By virtue of the merger, Valero L.P. could use control over bulk ethanol terminaling to limit access to ethanol storage by refusing to renew storage agreements with terminaling customers, by canceling contracts at some terminals to force competitors to truck longer distances, or by simply raising prices or abusing confidential information for ethanol terminaling. Because a percentage of ethanol must be added to CARB gasoline where oxygenation is required, any of these actions could increase the price of finished gasoline in Northern California. Because Kaneb does not market CARB gasoline, Kaneb currently has no incentive to manipulate ethanol access in these ways.

New entry into the market for Northern California bulk ethanol terminaling services would not be likely or timely, for the same reasons that entry would not be timely or likely for terminaling services for refining components, blending components, and light petroleum products in Northern California.

#### **IV. The Proposed Consent Order**

The Commission has provisionally accepted the Agreement Containing Consent Orders executed by Valero L.P., Valero Energy, and Kaneb in the settlement of the Complaint. The Agreement Containing Consent Orders contemplates that the Commission would issue the Complaint and enter the Proposed Order and the Hold Separate Order for the divestiture of certain assets described below. Under the terms of the Proposed Order, the merged firm must: (1) divest Kaneb's Paulsboro, New Jersey, Philadelphia North, and Philadelphia South terminals; (2) divest the Kaneb West Pipeline System; (3) divest Kaneb's Martinez and Richmond terminals; (4) ensure that customers and prospective customers have non-discriminatory access to commingled terminaling of ethanol at its retained San Francisco Bay terminals, on terms and conditions no less advantageous to those given to Valero Energy; and (5) create firewalls that prevent the transfer of

Analysis

competitively sensitive information between the merged firm and Valero Energy. The Commission will appoint James F. Smith as the hold separate trustee.

**A. Kaneb's Paulsboro, Philadelphia North, and Philadelphia South Terminals**

To remedy the lessening of competition in the supply of terminaling services for bulk suppliers of light petroleum products in the Greater Philadelphia Area alleged in Count I of the Complaint, Paragraph III of the Proposed Order requires Respondents to divest Kaneb's Paulsboro, New Jersey, Philadelphia North, and Philadelphia South terminals. The assets to be divested include the three terminals, and all assets located at or used in connection with these terminals, including truck racks, local connector pipelines, storage tanks, real estate, inventory, customer contracts, and real estate.

The divestiture is designed to ensure that, post-merger, the same number of players will compete in supplying terminaling services as at present. In addition, divesting the Philadelphia area package to an independent terminal operator that does not benefit from higher product prices will complicate the ability of the integrated terminal owners in the Greater Philadelphia Area to coordinate their bulk supply decisions and will maintain the pre-merger competition in this market.

These terminal assets must be divested within six months of the date the merger is effectuated to a buyer that receives that prior approval of the Commission. In a separate Order to Hold Separate and Maintain Assets, Respondents are required to hold all assets to be divested separate and to maintain the viability and marketability of the assets until they are divested.

**B. Kaneb West Pipeline System**

To remedy the lessening of competition in pipeline transportation and terminaling services for bulk suppliers of light

## Analysis

petroleum products in the Colorado Front Range alleged in Count II of the Complaint, Paragraph II of the Proposed Order requires Respondents to divest the Kaneb West Pipeline System. The assets to be divested include: (1) a refined products pipeline originating near Casper, Wyoming, and terminating in Rapid City, South Dakota, and Colorado Springs, Colorado; (2) refined products terminals in Rapid City, South Dakota; Cheyenne, Wyoming; Dupont, Colorado; and Fountain, Colorado. The assets to be divested also include all assets located at, or used in connection, with these pipelines and terminals, including truck racks, local connector pipelines, storage tanks, real estate, inventory, customer contracts, and real estate.

This divestiture is designed to maintain the likelihood that the new owner of the Kaneb West Pipeline System will not restrict Montana and Wyoming refiners' ability to send product to Denver and Colorado Springs. The divestiture will eliminate the ability of the combined company to raise light petroleum product prices in Denver and Colorado Springs by restricting access to the West Pipeline System. It also ensures that the current competition for pipeline transportation to and terminaling services in Denver and Colorado Springs will be maintained, with the same number of competitors post-acquisition as pre-acquisition. The divestiture of the West Pipeline System will also complicate the ability of the terminal and pipeline owners in these markets to coordinate in raising their pipeline transportation or terminaling service fees. Finally, the divestiture prevents Valero L.P. from controlling light petroleum product pipeline transportation to and terminaling in Colorado Springs. It effectively maintains the pre-merger competition in this market.

These pipeline and terminal assets must be divested within six months of the date the merger is effectuated to a buyer that receives the prior approval of the Commission. In a separate Order to Hold Separate and Maintain Assets, Respondents are required to hold all assets to be divested separate and to maintain the viability and marketability of the assets until they are divested.

Analysis

### **C. Kaneb's Martinez and Richmond Terminals**

To remedy the lessening of competition in terminaling services for bulk suppliers of refining components, blending components, and light petroleum products in Northern California as alleged in Count III of the Complaint, Paragraph IV of the Proposed Order requires Respondents to divest Kaneb's Martinez and Richmond terminals to a Commission-approved buyer. The assets to be divested include both terminals, and all assets located at or used in connection with these terminals, including truck racks, local connector pipelines, storage tanks, real estate, inventory, customer contracts, and real estate.

The divestiture is ordered to maintain the likelihood that the new owner of these terminals does not restrict access to these terminals or otherwise limit imports into the Northern California market. The divestiture also complicates the ability of the remaining terminal owners in the market to coordinate to raise the prices of terminaling services. Although Valero L.P. will acquire Kaneb's Selby terminal, the presence of an independent operator of Martinez and Richmond will check Valero L.P.'s incentive and ability to restrict access at that terminal.

These terminal assets must be divested within six months of the date the Merger is effectuated to a buyer that receives the prior approval of the Commission. In a separate Order to Hold Separate and Maintain Assets, Respondents are required to hold all assets to be divested separate and to maintain the viability and marketability of the assets until they are divested.

In considering an application to divest any of these three asset packages, to one or more buyers, the Commission will consider factors such as the acquirer's ability and incentive to invest and compete in the businesses in which Kaneb was engaged in the relevant geographic markets alleged in the Complaint. The Commission will consider whether the acquirer has the business experience, technical judgment, and available capital to continue

## Analysis

to invest in the terminals in order to maintain current levels of competition.

**D. Terminaling Services for Bulk Ethanol in Northern California**

To remedy the lessening of competition in terminaling services for bulk ethanol in Northern California alleged in Count IV of the Complaint, Paragraph VI of the Proposed Order requires Respondents to maintain an information firewall. The Paragraph also requires that the Respondents not discriminate in offering access to commingled terminaling of ethanol at its retained Northern California terminals in Stockton and Selby, and offer access to third parties on terms and conditions no less advantageous to those given to Valero Energy. This remedy is ordered to ensure that the Respondents do not use confidential business information or limit access to ethanol storage to maintain competition in the terminaling of ethanol and the sale of finished gasoline in Northern California.

**E. Other Terms**

Paragraph VII requires the Respondents to provide written notification prior to acquiring the Paulsboro, New Jersey, Philadelphia North, or Philadelphia South terminals, or any portion thereof. It further requires Respondents to provide reports to the Commission regarding compliance with the Proposed Order. Paragraph IX requires the Respondents to provide written notification prior to any proposed dissolution, acquisition, merger, or consolidation, or any other change that may affect compliance obligations arising out of the Proposed Order. Paragraph X requires the Respondents to provide the Commission with access to their facilities and employees for purposes of determining or securing compliance with the Proposed Order. Paragraph XI provides for an extension of time to complete divestitures required under the Proposed Order if the particular divestiture has been challenged by a State.



Analysis

## **V. Opportunity for Public Comment**

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

Complaint

IN THE MATTER OF

**CHEVRON CORPORATION, ET. AL.**CONSENT ORDER, ETC., IN REGARD TO ALLEGED VIOLATIONS OF  
SEC. 7 OF THE CLAYTON ACT AND SEC. 5 OF THE FEDERAL TRADE  
COMMISSION ACT*Docket C-4144; File No. 0510125  
Complaint, July 27, 2005--Decision, July 27, 2005*

This consent order addresses the merger of Respondent Chevron Corporation -- a major international energy firm engaged in exploring for, developing and producing crude oil and natural gas; refining crude oil into finished petroleum products; marketing crude oil, natural gas, and other finished products derived from petroleum; and transporting crude oil, natural gas, and finished petroleum products by pipeline, marine vessels, and other means -- and Respondent Unocal Corporation, another major international energy firm engaged primarily in oil and gas exploration, development and production. The order, among other things, requires the respondents to cease and desist from any and all efforts to assert or enforce any of Unocal's relevant U.S. patents -- including in particular patents covering technology that refiners must use to produce California Air Resources Board compliant reformulated gasoline, the only type of gasoline that can be sold in California -- against any person to recover any damages or costs for alleged infringements of any of these patents, or to collect any fees, royalties or other payments, in cash or in kind, for the practice of any of these patents. The consent order also requires the respondents, within thirty days, to file with the United States Patent and Trademark Office the necessary documents to disclaim or dedicate to the public the remaining term of the patents. In addition, the consent order requires the respondents, within thirty days, to dismiss with prejudice all pending legal actions relating to the alleged infringement of any of the patents.

*Participants*

For the Commission: *Dennis F. Johnson, Chong S. Park, Frank Lipson, Geary A. Gessler, Phillip Broyles, Geoffrey D. Oliver, Daniel P. Ducore, Jeffrey H. Fischer and Mark Frankena.*

For the Respondent: *Martin R. Lueck and David W. Beehler, Robins, Kaplan, Miller & Ciresi, David S. Neill, Wachtell, Lipton, Rosen & Katz, and Joe Sims, Jones Day.*

Complaint

## COMPLAINT

Pursuant to the provisions of the Federal Trade Commission Act and the Clayton Act, and by virtue of the authority vested in it by said Acts, the Federal Trade Commission (“FTC” or “Commission”), having reason to believe that Respondent Chevron Corporation (“Chevron”) and Respondent Unocal Corporation (“Unocal”) have entered into an agreement and plan of merger whereby Chevron proposes to acquire all of the outstanding common stock of Unocal, that such agreement and plan of merger violates 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, and it appearing to the Commission that a proceeding in respect thereof would be in the public interest, hereby issues its complaint, stating its charges as follows:

### I. RESPONDENTS

#### *Chevron Corporation*

1. Respondent Chevron, formerly ChevronTexaco Corporation, is a corporation organized, existing and doing business under and by virtue of the laws of the state of Delaware, with its office and principal place of business located at 6001 Bollinger Canyon Road, San Ramon, California 94583.
2. Respondent Chevron is, and at all times relevant herein has been, a diversified energy firm engaged, either directly or through affiliates, in the exploration for, and production of, petroleum products; the pipeline transportation of crude oil and natural gas; the refining of crude oil into refined products, including gasoline and other light petroleum products; the transportation, terminaling, and marketing of gasoline, diesel fuel, and aviation fuel; and other related energy businesses.
3. Respondent Chevron is, and at all times relevant herein has been, engaged in commerce as “commerce” is defined in

## Complaint

Section 1 of the Clayton Act, as amended, 15 U.S.C. § 12, and is a corporation whose business is in or affecting commerce as “commerce” is defined in Section 4 of the Federal Trade Commission Act, as amended, 15 U.S.C. § 44.

***Unocal Corporation***

4. Respondent Unocal is a corporation organized, existing and doing business under and by virtue of the laws of the state of Delaware, with its office and principal place of business located at 2141 Rosecrans Avenue, Suite 4000, El Segundo, California 90245.
5. Respondent Unocal is, and at all times relevant herein has been, an energy firm engaged, either directly or through affiliates, in the exploration for, and production of, petroleum products; the pipeline transportation of crude oil, natural gas and other petroleum products; and other related energy businesses.
6. Respondent Unocal is, and at all times relevant herein has been, engaged in commerce as “commerce” is defined in Section 1 of the Clayton Act, as amended, 15 U.S.C. § 12, and is a corporation whose business is in or affecting commerce as “commerce” is defined in Section 4 of the Federal Trade Commission Act, as amended, 15 U.S.C. § 44.

**II. THE PROPOSED MERGER**

7. Pursuant to an agreement and plan of merger dated April 4, 2005, Chevron intends to acquire all of the outstanding common stock of Unocal in exchange for cash and common stock of Chevron. At the time of the agreement, the value of the transaction was approximately \$18 billion.

Complaint

### III. TRADE AND COMMERCE

8. Gasoline is a motor fuel that is used in automobiles and other vehicles. It is refined from crude oil at refineries in the United States and throughout the world. Gasoline is produced in various grades and formulations, including conventional unleaded gasoline, low emissions reformulated gasoline (“RFG”), California Air Resources Board (“CARB”) compliant reformulated gasoline, and others. There is no substitute for gasoline as a fuel for automobiles and other vehicles that are designed to use gasoline.
9. CARB compliant reformulated gasoline (“CARB RFG”) is a motor fuel that meets the specifications of the California Air Resources Board. CARB RFG is cleaner burning and causes less air pollution than conventional unleaded gasoline. The sale of any gasoline other than CARB RFG is prohibited in California. There is no substitute for CARB RFG as a fuel for automobiles and other vehicles that use gasoline purchased in California.
10. CARB RFG is produced primarily in California and at a few other locations on the West Coast. Chevron is a leading refiner and marketer of CARB RFG. Unocal is not engaged in the refining or marketing of CARB RFG.
11. Through its wholly-owned subsidiary, Union Oil Company of California, Unocal owns a portfolio of five U.S. patents relating to reformulated gasoline. Unocal’s RFG patents cover the production and supply of CARB RFG, particularly in the warmer weather months. Refiners must use the technology covered by the Unocal RFG patents for producing a substantial portion of CARB RFG during warmer weather months – *i.e.*, CARB “summertime” gasoline.
12. Unocal licenses its RFG patents to others in exchange for payments ranging from 1.2 to 3.4 cents per gallon. In

## Complaint

addition, Unocal has won a patent infringement suit against major refiners of CARB RFG and obtained a court judgment awarding Unocal royalties of 5.75 cents per infringing gallon produced in California.

***Relevant Product Market***

13. Relevant lines of commerce in which to analyze the effects of the proposed merger are the marketing and refining of CARB RFG.

***Relevant Geographic Market***

14. Relevant sections of the country in which to analyze the proposed merger are the State of California and smaller areas contained therein.

***Market Structure***

15. The relevant markets for the refining and marketing of CARB RFG are either highly concentrated or moderately concentrated.

***Entry Conditions***

16. Entry into the relevant lines of commerce in the relevant sections of the country is difficult and would not be timely, likely or sufficient to prevent anticompetitive effects resulting from the proposed merger.

**IV. VIOLATION CHARGED**

17. Because of factors such as Unocal's perception of possible actions by the California Air Resources Board or other governmental authorities, Unocal is likely to be constrained in charging the full monopoly level price to licensees of the Unocal patents. Unocal has no operations at downstream levels of the industry through which it could attempt to

Complaint

recoup any additional profits. Because of its significant operations at the refining and marketing levels, Chevron will have a greater ability than Unocal to obtain additional profits by coordinating with its competitors at the downstream refining and marketing levels.

18. As part of Unocal's license agreements, Unocal regularly collects detailed reports from licensees about their production of CARB RFG and other refinery operations. Such information is not otherwise available to members of the industry, and could be used to facilitate coordination among refiners and marketers of CARB RFG.
19. The effect of the proposed merger, if consummated, may be substantially to lessen competition in the marketing and refining of CARB RFG in the relevant sections of the country, in violation of Section 7 of the Clayton Act, as amended, 15 U.S.C. § 18, and Section 5 of the Federal Trade Commission Act, as amended, 15 U.S.C. § 45, in the following ways, among others:
  - a. By increasing the likelihood of, or facilitating, collusion or coordinated interaction between Chevron and its competitors in the refining of CARB RFG in the relevant sections of the country,
  - b. By increasing the likelihood of, or facilitating, collusion or coordinated interaction between Chevron and its competitors in the marketing of CARB RFG in the relevant sections of the country,

each of which increases the likelihood of anticompetitive price increases for CARB RFG in the relevant sections of the country.

20. The proposed merger between Chevron and Unocal violates Section 5 of the Federal Trade Commission Act, as amended, 15 U.S.C. § 45, and would, if consummated,

## Complaint

violate Section 7 of the Clayton Act, as amended, 15 U.S.C. § 18, and Section 5 of the Federal Trade Commission Act, as amended, 15 U.S.C. § 45.

WHEREFORE, THE PREMISES CONSIDERED, the Federal Trade Commission on this 27<sup>th</sup> day of July, 2005, issues its complaint against said Respondents.



Decision and Order

## **DECISION AND ORDER**

The Federal Trade Commission (“Commission”), having initiated an investigation of the proposed merger between Respondent Chevron Corporation (“Chevron”) and Respondent Unocal Corporation (“Unocal”) (collectively “Respondents”), and Respondents having been furnished thereafter with a copy of a draft of Complaint that the Bureau of Competition proposed to present to the Commission for its consideration and which, if issued by the Commission, would charge Respondents with violations of Section 7 of the Clayton Act, as amended, 15 U.S.C. § 18, and Section 5 of the Federal Trade Commission Act, as amended, 15 U.S.C. § 45; and

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

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

## Decision and Order

1. Respondent Chevron Corporation is a corporation organized, existing, and doing business under and by virtue of the laws of the state of Delaware, with its office and principal place of business located at 6001 Bollinger Canyon Road, San Ramon, California 94583.

2. Respondent Unocal Corporation is a corporation organized, existing and doing business under and by virtue of the laws of the state of Delaware, with its office and principal place of business located at 2141 Rosecrans Avenue, Suite 4000, El Segundo, California 90245.

3. The Federal Trade Commission has jurisdiction of the subject matter of this proceeding and of Respondents, and the proceeding is in the public interest.

**ORDER****I.**

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

- A. "Chevron" means Chevron Corporation (formerly ChevronTexaco Corporation), its directors, officers, employees, agents, representatives, successors, and assigns; and its joint ventures, subsidiaries, divisions, groups and affiliates controlled by Chevron Corporation, and the respective directors, officers, employees, agents, representatives, successors, and assigns of each.
- B. "Unocal" means Unocal Corporation, its directors, officers, employees, agents, representatives, successors, and assigns; and its joint ventures, subsidiaries (including but not limited to Union Oil Company of California), divisions, groups and affiliates controlled by Unocal Corporation, and the respective directors, officers, employees, agents, representatives, successors, and assigns of each.

Decision and Order

- C. "Respondents" means Chevron and Unocal.
- D. "Commission" means the Federal Trade Commission.
- E. "Action" means any lawsuit or other action, whether legal, equitable, or administrative, as well as any arbitration, mediation, or any other form of private dispute resolution, in the United States or anywhere else in the world.
- F. "License Agreement" means any contract, agreement, arrangement or other understanding between Unocal and any other party or parties that requires, calls for, or otherwise contemplates, payment of fees, royalties or other monies, in cash or in kind, to practice under the Relevant U.S. Patents.
- G. "Merger" means the proposed merger between Chevron and Unocal, as contemplated by the Agreement and Plan of Merger dated as of April 4, 2005 among Unocal Corporation, ChevronTexaco Corporation, and Blue Merger Sub Inc.
- H. "Merger Effective Date" means the earlier of the following dates:
1. the date that the certificate of merger for the Merger is filed with the Secretary of State of Delaware or such later time as specified in such certificate of merger, or
  2. the date that Chevron acquires control of Unocal Corporation, as "control" is defined by 16 C.F.R. § 801.1(b).
- I. "Person" means both natural persons and artificial persons, including, but not limited to, corporations, unincorporated entities, and governments.

## Decision and Order

- J. “Relevant U.S. Patents” means United States Patent Numbers 5,288,393, 5,593,567, 5,653,866, 5,837,126, 6,030,521, and any other patents presently in existence or to be issued in the future that claim priority to United States Patent Application Number 07/628,488, filed December 13, 1990.

**II.**

IT IS FURTHER ORDERED that, immediately upon the Merger Effective Date, Respondents shall cease and desist from any and all efforts, and shall not undertake any new efforts, by any means, directly or indirectly, in or affecting commerce as “commerce” is defined in Section 4 of the Federal Trade Commission Act, 15 U.S.C. § 44, to assert or enforce any of the Relevant U.S. Patents against any Person, to recover any damages or costs for alleged infringements of any of the Relevant U.S. Patents, or to collect any fees, royalties or other payments, in cash or in kind, for the practice of any of the Relevant U.S. Patents, including but not limited to fees, royalties, or other payments, in cash or in kind, to be collected pursuant to any License Agreement, provided, however, that nothing in this Order obligates or requires Respondents to refund any fees, royalties or other payments collected in connection with any of the Relevant U.S. Patents prior to the Merger Effective date.

**III.**

IT IS FURTHER ORDERED that:

- A. Within thirty (30) days following the Merger Effective Date, Respondents shall file, or cause to be filed, with the United States Patent and Trademark Office, the necessary documents pursuant to 35 U.S.C. § 253, 37 C.F.R. § 1.321, and the Manual of Patent Examining Procedure to disclaim or dedicate to the public the remaining term of the Relevant U.S. Patents, provided, however, that such disclaimer or dedication to the public shall not constitute an admission or

Decision and Order

representation by Respondents with respect to the validity or patentability of the claims of the Relevant U.S. Patents.

- B. Respondents shall correct as necessary, and shall not withdraw or seek to nullify, any disclaimers, or dedications filed pursuant to Paragraph III. A.

**IV.**

IT IS FURTHER ORDERED that, within thirty (30) days following the Merger Effective Date, Respondents shall move to dismiss, with prejudice, all Actions relating to the alleged infringement of any Relevant U.S. Patents, including but not limited to the following actions pending in the United States District Court for the Central District of California: *Union Oil Company of California v. Atlantic Richfield Company, et al.*, Case No. CV-95-2379-CAS and *Union Oil Company of California v. Valero Energy Corporation*, CV-02- 00593 SVW.

**V.**

IT IS FURTHER ORDERED that:

- A. Within thirty (30) days after the date this Order becomes final, Respondents shall distribute a copy of this Order and the complaint in this matter to:
1. any Person that either Respondent has contacted regarding possible infringement of any of the Relevant U.S. Patents,
  2. any Person against which either Respondent is, or was, in any Action regarding possible infringement of any of the Relevant U.S. Patents,
  3. any licensee or other Person from which either Respondent has collected any fees, royalties or other

## Decision and Order

payments, in cash or in kind, for the practice of the Relevant U.S. Patents, and

4. any Person that either Respondent has contacted with regard to the possible collection of any fees, royalties or other payments, in cash or in kind, for the practice of the Relevant U.S. Patents.
- B. Within thirty (30) days after the date this Order becomes final, Respondents shall distribute a copy of this Order and the complaint in this matter to every officer and director of Respondents having responsibility for any of Respondents' obligations under this Order, and to every employee or agent having managerial responsibility for any of Respondents' obligations under this Order.
- C. For a period of five (5) years after the date this Order becomes final, Respondents shall furnish a copy of this Order and the complaint in this matter to each new officer and director of Respondents who will have responsibility for any of Respondents' obligations under this Order, and to each new employee or agent of Respondents who will have managerial responsibility for any of Respondents' obligations under the Order. Such copies shall be furnished within thirty (30) days after each such person assumes his or her position as officer, director, employee, or agent. For purposes of this Paragraph V.C., "new employee or agent" shall include, without limitation, Respondents' employees and agents whose duties change during their employment or agency relationship to include managerial responsibility for any of Respondents' obligations under this Order.

**VI.**

IT IS FURTHER ORDERED that:

- A. Respondents shall, within sixty (60) days after the date this Order becomes final, submit to the Commission a verified

Decision and Order

written report setting forth in detail the manner and form in which each Respondent intends to comply, is complying, and has complied with this Order.

- B. Respondents shall, one year from the date this Order becomes final and annually thereafter for five (5) years, submit a verified written report to the Commission setting forth in detail the manner and form in which each Respondent has complied and is complying with the Order.

**VII.**

IT IS FURTHER ORDERED that, for the purpose of determining or securing compliance with this Order, and subject to any legally recognized privilege, and upon written request with reasonable notice to Respondents, Respondents shall permit any duly authorized representative of the Commission:

- A. Access, during office hours of Respondents and in the presence of counsel, to all facilities and access to inspect and copy all books, ledgers, accounts, correspondence, memoranda, and all other records and documents in the possession or under the control of Respondents related to compliance with this Order; and
- B. Upon five (5) days' notice to Respondents and without restraint or interference from Respondents, to interview officers, directors, or employees of Respondents, who may have counsel present, regarding such matters.

**VIII.**

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

## Decision and Order

dissolution of subsidiaries, or any other change in either Respondent.

**IX.**

IT IS FURTHER ORDERED that this Order will terminate twenty (20) years after the date it becomes final.



Analysis

**Analysis of Proposed Consent Order to Aid Public Comment**

**I. Introduction**

The Federal Trade Commission (“Commission” or “FTC”) has issued a complaint (“Complaint”) alleging that the proposed merger of Chevron Corporation (“Chevron,” formerly ChevronTexaco Corporation) and Unocal Corporation (“Unocal”) (collectively “Respondents”) would violate Section 7 of the Clayton Act, as amended, 15 U.S.C. § 18, and Section 5 of the Federal Trade Commission Act, as amended, 15 U.S.C. § 45, and has entered into an agreement containing consent order (“Agreement Containing Consent Order”) pursuant to which Respondents agree to be bound by a proposed consent order (“Proposed Consent Order”). The Proposed Consent Order remedies the likely anticompetitive effects arising from Respondents’ proposed merger, as alleged in the Complaint.

**II. Description of the Parties and the Transaction**

**A. Chevron**

Chevron is a major international energy firm with operations in North America and about 180 foreign countries in Europe, Africa, South America, Central America, Indonesia, and the Asia-Pacific region. Its petroleum operations consist of exploring for, developing and producing crude oil and natural gas; refining crude oil into finished petroleum products; marketing crude oil, natural gas, and various finished products derived from petroleum; and transporting crude oil, natural gas, and finished petroleum products by pipeline, marine vessels, and other means. The company operates light petroleum refineries for products such as gasoline, jet fuel, kerosene and fuel oil at Pascagoula, Mississippi; El Segundo, California; Richmond, California; Salt Lake City, Utah; and Kapolei, Hawaii. Chevron is a major refiner and marketer of gasoline that meets the requirements of the California Air Resources Board (“CARB”). Chevron also has operations for the manufacture and marketing of commodity petrochemicals for

## Analysis

industrial uses and additives for fuels and lubricants. For 2004, the company had total revenues of approximately \$155.3 billion and total assets of approximately \$93.2 billion.

**B. Unocal**

Unocal is also a major international energy firm with operations in North America, Asia, and other locations around the world. Its primary activities are oil and gas exploration, development and production. It has oil and gas operations located in various countries, including Thailand, Myanmar, Indonesia, Azerbaijan, Bangladesh, and Vietnam. Unocal sold most of its downstream operations in the United States to another company in the mid-1990's. As a result, Unocal has no downstream operations in refining or gasoline retailing, and with a few exceptions almost all of Unocal's operations are in the upstream segment of the industry, *i.e.*, exploration and production. The company had total revenues for 2004 of approximately \$8.2 billion and total assets of approximately \$13.1 billion.

**III. The Transaction**

Pursuant to an Agreement and Plan of Merger dated April 4, 2005, Chevron plans to acquire 100% of the voting securities of Unocal. Unocal will merge into a direct wholly-owned subsidiary of Chevron, with the subsidiary continuing as the surviving entity and a wholly-owned subsidiary of Chevron. Under the terms of the agreement, Unocal shareholders may elect to receive 1.03 shares of Chevron stock, \$65 in cash, or the combination of \$16.25 in cash and 0.7725 of a share of Chevron common stock. The election is subject to the limitation that 75% of the outstanding shares of Unocal common stock will be exchanged for Chevron common stock and 25% will be exchanged for cash, with prorationing in the event the cash election is oversubscribed or undersubscribed. The total value of the transaction is estimated at approximately \$18 billion, which includes approximately \$1.6 billion in assumed debt.

Analysis

The transaction is subject to various closing conditions, including the approval of Unocal shareholders and the expiration or early termination of the waiting period under the Hart-Scott-Rodino Act, 15 U.S.C. § 18A. The parties expect to close the transaction as soon as practicable after the last of the conditions to closing have been satisfied.

#### **IV. The Complaint**

The Complaint alleges that the merger of Chevron and Unocal would violate Section 7 of the Clayton Act, as amended, 15 U.S.C. § 18, and Section 5 of the Federal Trade Commission Act, as amended, 15 U.S.C. § 45, by substantially lessening competition in the refining and marketing of reformulated gasoline that has been approved by the California Air Resources Board (“CARB”) for sale in California. Through its wholly-owned subsidiary, Union Oil Company of California (“Union Oil”), Unocal owns a portfolio of five U.S. patents relating to reformulated gasoline (“RFG”). These patents (the “Relevant U.S. Patents”) cover the production and supply of CARB RFG, particularly in warmer weather months. To remedy the alleged anticompetitive effects of the merger, the Proposed Consent Order requires Respondents to take certain actions, including (1) to cease and desist from any efforts to assert or enforce any of the Relevant U.S. Patents against any person, to recover any damages or costs for alleged infringements of any of the Relevant U.S. Patents, or to collect any fees, royalties or other payments for the practice of the Relevant U.S. Patents; and (2) to take the necessary actions to dedicate to the public the remaining terms of the patents.

According to the Complaint, gasoline is a motor fuel used in automobiles and other vehicles. It is produced in various grades and formulations, including conventional unleaded gasoline, low emissions reformulated gasoline (“RFG”), California Air Resources Board (“CARB”) compliant reformulated gasoline, and others. CARB compliant reformulated gasoline (“CARB RFG”) is a type of gasoline that meets the specifications of the California

## Analysis

Air Resources Board. CARB RFG is cleaner burning and causes less air pollution than conventional unleaded gasoline. The sale of any gasoline other than CARB RFG is prohibited in California, and there is no substitute for CARB RFG as a fuel for automobiles and other vehicles that use gasoline purchased in California. As a result, CARB RFG is a relevant line of commerce in which to analyze the potential effects of the merger.

CARB RFG is produced primarily in California and at a few other locations on the West Coast. The Complaint alleges that the state of California, and smaller areas contained therein, are relevant sections of the country in which to analyze the potential effects of the merger.

Chevron is a leading refiner and marketer of CARB RFG. Unocal does not refine or market CARB RFG. However, through its wholly-owned subsidiary, Union Oil, Unocal owns Relevant U.S. Patents relating to CARB RFG. Refiners must use the technology covered by the Unocal Relevant U.S. Patents for producing CARB RFG during warmer weather months – *i.e.*, CARB “summertime” gasoline. Thus, Unocal controls an important input used by CARB refiners to produce CARB gasoline.

Unocal licenses its RFG patents to others in exchange for payments ranging from 1.2 to 3.4 cents per gallon. In addition, Unocal has won a patent infringement suit against major refiners of CARB RFG and obtained a court judgment awarding Unocal royalties of 5.75 cents per infringing gallon produced in California.

There are relatively few producers of CARB RFG. As a result, the relevant markets for the refining and marketing of CARB RFG are either highly concentrated or moderately concentrated. The Complaint further alleges that entry into the relevant lines of commerce in the relevant sections of the country is difficult and would not be timely, likely or sufficient to prevent anticompetitive effects resulting from the proposed merger.

Analysis

The Complaint states that, because of factors such as Unocal's perception of possible actions by the California Air Resources Board or other governmental authorities, Unocal is likely to be constrained in charging the full monopoly level price to licensees of the Unocal patents. Moreover, Unocal has no operations at downstream levels of the industry through which it could attempt to recoup any additional profits.

Because of its significant operations at the refining and marketing levels, Chevron will have a greater ability than Unocal to obtain additional profits by coordinating with its competitors at the downstream refining and marketing levels. As part of Unocal's license agreements, Unocal regularly collects detailed reports from licensees about their production of CARB RFG and other refinery operations. By obtaining the Unocal patents, Chevron would receive additional information about the production of competitors and other information not otherwise available to members of the industry. Chevron could facilitate coordination among refiners and marketers of CARB RFG by using this information to monitor a collusive agreement and thus detect cheating on a collusive agreement. The anticompetitive effects from such coordination would be likely to outweigh any efficiencies that would be obtained by the integrated firm.

As a result, the Complaint charges that the effect of the proposed merger, if consummated, may be substantially to lessen competition in the marketing and refining of CARB RFG in the relevant sections of the country, in violation of Section 7 of the Clayton Act, as amended, 15 U.S.C. § 18, and Section 5 of the Federal Trade Commission Act, as amended, 15 U.S.C. § 45.

## **V. Resolution of the Competitive Concerns**

The Commission has provisionally entered into an Agreement Containing Consent Order with Chevron and Unocal in settlement of the Complaint. The Agreement Containing Consent Orders

## Analysis

contemplates that the Commission would issue the Complaint and enter the Proposed Consent Order requiring the relief described below.

In order to remedy the anticompetitive effects that have been identified, Chevron and Unocal have agreed to take several actions. First, they will cease and desist from any and all efforts, and will not undertake any new efforts, to assert or enforce any of Unocal's Relevant U.S. Patents against any person, to recover any damages or costs for alleged infringements of any of the Relevant U.S. Patents, or to collect any fees, royalties or other payments, in cash or in kind, for the practice of any of the Relevant U.S. Patents, including but not limited to fees, royalties, or other payments, in cash or in kind, to be collected pursuant to any License Agreement. These obligations become effective as of the "Merger Effective Date," which is defined as the earlier of (1) the date that the certificate of merger for the Merger is filed with the Secretary of State of Delaware or such later time as specified in such certificate of merger, or (2) the date that Chevron acquires control of Unocal Corporation, as "control" is defined by 16 C.F.R. § 801.1(b).

Second, the Proposed Consent Order requires that, within thirty (30) days following the Merger Effective Date, Respondents shall file, or cause to be filed, with the United States Patent and Trademark Office, the necessary documents pursuant to 35 U.S.C. § 253, 37 C.F.R. § 1.321, and the Manual of Patent Examining Procedure to disclaim or dedicate to the public the remaining term of the Relevant U.S. Patents. The Proposed Consent Order further requires that Respondents shall correct as necessary, and shall not withdraw or seek to nullify, any disclaimers or dedications filed pursuant to the order.

Third, the order requires that, within thirty (30) days following the Merger Effective Date, Respondents shall move to dismiss, with prejudice, all pending legal actions relating to the alleged infringement of any Relevant U.S. Patents, including but not limited to the following actions pending in the United States

Analysis

District Court for the Central District of California: *Union Oil Company of California v. Atlantic Richfield Company, et al.*, Case No. CV-95-2379-CAS and *Union Oil Company of California v. Valero Energy Corporation*, Case No. CV-02- 00593 SVW.

Paragraph V of the Proposed Consent Order requires Respondents to distribute a copy of the Order and the Complaint in this matter to certain interested parties, including (1) any person that either Respondent has contacted regarding possible infringement of any of the Relevant U.S. Patents, (2) any person against which either Respondent is, or was, involved in any legal action regarding possible infringement of any of the Relevant U.S. Patents, (3) any licensee or other person from which either Respondent has collected any fees, royalties or other payments, in cash or in kind, for the practice of the Relevant U.S. Patents, and (4) any person that either Respondent has contacted with regard to the possible collection of any fees, royalties or other payments, in cash or in kind, for the practice of the Relevant U.S. Patents.

Paragraph V also requires Respondents to distribute a copy of the Order and the Complaint to present and future officers and directors of Respondents having responsibility for any of Respondents' obligations under the Order, and to employees and agents having managerial responsibility for any of Respondents' obligations under the Order.

Paragraphs VI, VII and VIII of the Proposed Consent Order contain standard reporting, access, and notification provisions designed to allow the Commission to monitor compliance with the order. Paragraph IX provides that the Order shall terminate twenty (20) years after the date it becomes final.

## **VI. Opportunity for Public Comment**

The Proposed Consent Order has been placed on the public record for thirty (30) days for receipt of comments by interested persons. Comments received during this thirty day comment period will become part of the public record. After

## Analysis

thirty (30) days, the Commission will again review the Proposed Order and the comments received and will decide whether it should withdraw from the Proposed Order or make final the agreement's Proposed Order.

By accepting the Proposed Order subject to final approval, the Commission anticipates that the competitive problems alleged in the Complaint will be resolved. The purpose of this analysis is to invite public comment on the Proposed Order, and to aid the Commission in its determination of whether it should make final the Proposed Order contained in the agreement. This analysis is not intended to constitute an official interpretation of the Proposed Order, nor is it intended to modify the terms of the Proposed Order in any way.



Complaint

**IN THE MATTER OF**

**UNION OIL COMPANY OF CALIFORNIA**

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

*Docket D-9305; File No. 0110214*

*Complaint, March 4, 2003--Decision, July 27, 2005*

This consent order addresses a series of actions taken by Respondent Union Oil Company of California, an international energy firm, with respect to proceedings conducted by the California Air Resources Board (“CARB”) to set regulations and standards governing the composition of low emissions, reformulated gasoline (“RFG”), in an effort to reduce California air pollution levels. The order, among other things, requires the respondent to cease and desist from any and all efforts to assert or enforce any of its relevant U.S. patents – including in particular patents covering technology that refiners must use to produce CARB-compliant reformulated gasoline, the only type of gasoline that can be sold in California – against any person to recover any damages or costs for alleged infringements of any of these patents, or to collect any fees, royalties or other payments, in cash or in kind, for the practice of any of these patents. The consent order also requires the respondent, within thirty days, to file with the United States Patent and Trademark Office the necessary documents to disclaim or dedicate to the public the remaining term of the patents. In addition, the consent order requires the respondent, within thirty days, to dismiss with prejudice all pending legal actions relating to the alleged infringement of any of the patents.

*Participants*

For the Commission: *J. Robert Robertson, Chong S. Park, David F. Conn, Peggy Bayer Femenella, John Roberti, Lisa Fialco, Suzanne Michel, Sean P. Gates, Lore Unt, Thomas Krattenmaker, Dean C. Graybill, John S. Martin, Richard B. Dagen, Geoffrey D. Oliver, Daniel P. Ducore, Terri Martin, Robert A. Walters, Elizabeth J. Grimm, Paige E. Pidano, Jessica Picone, Diana Cowen, Guru Raj, Kathleen Jones, Yasmine Carson, Mark D. Williams, Jeffrey H. Fischer, and Mark Frankena.*

## Complaint

For the Respondent: *Martin R. Lueck and David W. Beehler, Robins, Kaplan, Miller & Ciresi, and Joseph Kattan and Chris Wood, Gibson, Dunn & Crutcher.*

**COMPLAINT**

Pursuant to the provisions of the Federal Trade Commission Act, and by virtue of the authority vested in it by said Act, the Federal Trade Commission (“Commission”), having reason to believe that Union Oil Company of California (hereinafter, “Unocal” or “Respondent”) has violated Section 5 of the Federal Trade Commission (“FTC”) Act, as amended, 15 U.S.C. § 45, and it appearing to the Commission that a proceeding in respect thereof would be in the public interest, hereby issues its complaint, stating its charges as follows:

**Nature of the Case**

1. This case involves Unocal’s subversion of state regulatory standard-setting proceedings relating to low emissions gasoline standards. To address California’s serious air pollution problems, the California Air Resources Board (“CARB”) initiated rulemaking proceedings in the late 1980s to determine “cost-effective” regulations and standards governing the composition of low emissions, reformulated gasoline (“RFG”). Unocal actively participated in the CARB RFG rulemaking proceedings and engaged in a pattern of bad-faith, deceptive conduct, exclusionary in nature, that enabled it to undermine competition and harm consumers. Through a pattern of anticompetitive acts and practices that continues even today, Unocal has illegally monopolized, attempted to monopolize, and otherwise engaged in unfair methods of competition in both the technology market for the production and supply of CARB-compliant “summer-time” RFG and the downstream CARB “summer-time” RFG product market.

Complaint

2. During the RFG rulemaking proceedings in 1990-1994, Unocal made materially false and misleading statements including, but not limited to, the following:
  - a. Representing to CARB and other participants that its emissions research results showing, *inter alia*, the directional relationships between certain gasoline properties (most notably the midpoint distillation temperature of gasoline or "T50") on automobile emissions were "nonproprietary," were in "the public domain," or otherwise were available to CARB, industry members, and the general public, without disclosing that Unocal intended to assert its proprietary interests (as manifested in pending patent claims) in these research results;
  - b. Representing to CARB that a "predictive model" -- *i.e.*, a mathematical model that predicts whether the resulting emissions from varying certain gasoline properties (including T50) in a fuel are equivalent to the emissions resulting from a specified and fixed fuel formulation -- would be "cost-effective" and "flexible," without disclosing that Unocal's assertion of its proprietary interests would undermine the cost-effectiveness and flexibility of such a model;
  - c. Making statements and comments to CARB and other industry participants relating to the cost-effectiveness and flexibility of the regulations that further reinforced the materially false and misleading impression that Unocal had relinquished or would not enforce any proprietary interests in its emissions research results.
3. Through its knowing and willful misrepresentations and other bad faith, deceptive conduct, Unocal created and maintained the materially false and misleading impression that it did not possess, or would not enforce, any relevant intellectual property rights that could undermine the cost-effectiveness and flexibility of the CARB RFG regulations.

## Complaint

4. Although Unocal knew by July 1992 that most of the pending patent claims based on its emissions research had been allowed by the United States Patent and Trademark Office, Unocal concealed this material information from CARB and other participants in the CARB RFG proceedings. Until Unocal's public announcement of its RFG patent rights on January 31, 1995, Unocal continued to perpetuate the false and misleading impression that it did not possess, or would not enforce, any proprietary interests relating to RFG.
5. But for Unocal's fraud, CARB would not have adopted RFG regulations that substantially overlapped with Unocal's concealed patent claims; the terms on which Unocal was later able to enforce its proprietary interests would have been substantially different; or both. Unocal's misrepresentations, on which CARB and other participants in the rulemaking process reasonably and detrimentally relied, have harmed competition and led directly to the acquisition of monopoly power for the technology to produce and supply California "summer-time" reformulated gasoline (mandated for up to eight months of the year, from approximately March through October). Unocal's "patent ambush" also has permitted it to undermine competition and harm consumers in the downstream product market for "summer-time" reformulated gasoline in California.
6. Unocal did not announce the existence of its proprietary interests and patent rights relating to RFG until shortly before CARB's Phase 2 regulations were to go into effect. By that time, the refining industry had spent billions of dollars in capital expenditures to modify their refineries to comply with the CARB Phase 2 RFG regulations. After CARB and the refiners had become locked into the Phase 2 regulations, however, Unocal commenced its patent enforcement efforts by publicly announcing its RFG patent rights and its intention to collect royalty payments and fees. Since Unocal's public announcement of the issuance of its first RFG patent on January 31, 1995, Unocal has obtained four additional patents

Complaint

and vigorously enforced its RFG patent rights through litigation and licensing activities.

7. The anticompetitive conduct by Unocal that is at issue in this action has materially caused or threatened to cause substantial harm to competition, and will in the future materially cause or threaten to cause further substantial injury to competition and to consumers.
8. The threatened or actual anticompetitive effects of Unocal's conduct include but are not limited to the following:
  - a. increased royalties (or other payments) associated with the use of technology to refine, produce, and supply low emissions, reformulated gasoline for the California market;
  - b. increases in the price of low emissions, reformulated gasoline in California;
  - c. reductions in the manufacture, output, and supply of low emissions, reformulated gasoline for the California market; and
  - d. decreased incentives, on the part of refiners, blenders, and importers, to produce and supply low emissions, reformulated gasoline to the California market.
9. Unocal's enforcement of its patent rights has resulted, *inter alia*, in a jury determination of a 5.75 cents per gallon royalty on gasoline produced by ARCO, Shell, Exxon, Mobil, Chevron, and Texaco that infringed the first of Unocal's five RFG patents – United States Patent No. 5,288,393 (the “393 patent”). These major refiners are still embroiled with Unocal in a pending accounting action to determine the total amount of infringement damages owed to Unocal for the period August 1996 through December 2000. Unocal also has sued Valero Energy Company (“Valero”) seeking the imposition of a 5.75 cents per gallon royalty (and treble damages) on gasoline

## Complaint

produced by Valero that infringes the '393 patent and the fourth of Unocal's five RFG patents – United States Patent No. 5,837,126 (the "'126 patent"). Taken together, the major refiners and Valero comprise approximately 90 percent of the current refining capacity of CARB-compliant RFG in the California market. Unocal has publicly announced that its "uniform" RFG licenses, with fees ranging from 1.2 to 3.4 cents per gallon, are available to "non-litigating" refiners.

10. Were Unocal to receive a 5.75 cents per gallon royalty on all gallons of "summer-time" CARB RFG produced annually for the California market, this would result in an estimated annual cost of more than \$500 million (assuming approximately 14.8 billion gallons per year California consumption, with up to 8 months of CARB summer-time gasoline requirements). Unocal's own economic expert has testified under oath that 90 percent of any royalty would be passed through to consumers in the form of higher retail gasoline prices.

**Respondent**

11. Union Oil Company of California is a public corporation organized, existing, and doing business under, and by virtue of, the laws of California. Its office and principal place of business is located at 2141 Rosecrans Avenue, Suite 4000, El Segundo, California 90245. Since 1985, Union Oil Company of California has done business under the name "Unocal." Unocal is a wholly-owned, operating subsidiary of Unocal Corporation, a holding company incorporated in Delaware.
12. Unocal is, and at all relevant times has been, a corporation as "corporation" is defined by Section 4 of the Federal Trade Commission Act, 15 U.S.C. § 44; and at all times relevant herein, Unocal has been, and is now, engaged in commerce as "commerce" is defined in the same provision.

Complaint

13. Prior to 1997, Unocal owned and operated refineries in California as a vertically integrated producer, refiner, and marketer of petroleum products. In March 1997, Unocal completed the sale of its west coast refining, marketing, and transportation assets to Tosco Corporation. Currently, Unocal's primary business activities involve oil and gas exploration and production, as well as production of geothermal energy, ownership in proprietary and common carrier pipelines, natural gas storage facilities, and the marketing and trading of hydrocarbon commodities.
14. In its annual report for the year 2001 filed with the United States Securities and Exchange Commission, Form 10-K, Unocal lists as another of its key business activities: "[p]ursuing and negotiating licensing agreements for reformulated gasoline patents with refiners, blenders and importers." Unocal has publicly announced that it expects to reap up to \$150 million in revenues a year from licensing its RFG patents.
15. Unocal is the owner, by assignment, of the following patents relating to low emissions, reformulated gasoline: United States Patent No. 5,288,393 (issued February 22, 1994); United States Patent No. 5,593,567 (issued January 14, 1997); United States Patent No. 5,653,866 (issued August 5, 1997); United States Patent No. 5,837,126 (issued November 17, 1998); United States Patent No. 6,030,521 (issued February 29, 2000). These patents all arise from the same scientific discovery and are related in that they all claim priority based on patent application No. 07/628,488, filed on December 13, 1990. These patents share the identical specification.

**California Air Resources Board (CARB)**

16. The California Air Resources Board is a department of the California Environmental Protection Agency. Established in 1967, CARB's mission is to protect the health, welfare,

## Complaint

and ecological resources of California through the effective and efficient reduction of air pollutants, while recognizing and considering the effects of its actions on the California economy. CARB fulfills this mandate by, among other things, setting and enforcing standards for low emissions, reformulated gasoline.

17. California's Administrative Procedures Act governs CARB's rulemaking proceedings and requires, *inter alia*, notice of any proposed regulations, the development of an evidentiary basis for any proposed regulations, the solicitation of public comments, and the conduct of hearings. Given the scientific and technical nature of the issues involved, CARB relies on the accuracy of the data and information presented to it in the course of rulemaking proceedings.
18. All CARB regulations are subject to review by California's Office of Administrative Law to ensure that such regulations meet statutory standards of necessity, authority, clarity, consistency, reference and nonduplication. CARB's regulations are subject to judicial review to determine whether the agency acted within its delegated authority, whether the agency employed fair procedures, and whether the agency's action was arbitrary, capricious, or lacking in evidentiary support.

**Reformulated Gasoline in California**

19. CARB's RFG regulations had their genesis in an effort by California to study the viability of alternative fuels for motor vehicles, such as methanol. In 1987, the California legislature passed AB 234, which resulted in the formation of a panel to study the environmental impact of alternative fuels and to develop a proposal to reduce emissions. This panel included representatives from the refining industry,



Complaint

including Roger Beach, a high level Unocal executive who later became the Chief Executive Officer and Chairman of the Board of Unocal.

20. Based in substantial part on the representations of oil industry executives that the oil industry could, and would, develop gasoline that would be cleaner-burning and cheaper than methanol, the AB 234 study panel eventually recommended exploring reformulated gasoline as an alternative to methanol.
21. In late 1988, the California legislature amended the California Clean Air Act to require CARB to take actions to reduce harmful car emissions, and directed CARB to achieve this goal through the adoption of new standards for automobile fuels and low-emission vehicles. CARB's authority in conducting its Phase 2 RFG rulemaking proceedings was circumscribed by an express and limited delegation of authority by the legislature. CARB's specific legislative mandate, set forth in California Health and Safety Code Section 43018, provided, *inter alia*, that CARB undertake the following actions:
  - a. Take "necessary, cost-effective, and technologically feasible" actions to achieve "reduction in the actual emissions of reactive, organic gases of at least 55 percent, a reduction in emissions of oxides of nitrogen of at least 15 percent from motor vehicles" no later than December 31, 2000;
  - b. Take actions "to achieve the maximum feasible reduction in particulates, carbon monoxide, and toxic air contaminants from vehicular sources";
  - c. Adopt standards and regulations that would result in "the most cost-effective combination of control measures on all classes or motor vehicles and motor vehicle fuels"

## Complaint

including the “specification of vehicular fuel composition.”

22. Following the 1988 California Clean Air Act amendments, CARB embarked on two rulemaking proceedings relating to low emissions, reformulated gasoline. In these rulemaking proceedings – Phase 1 and Phase 2, respectively – CARB prescribed limits on specific gasoline properties.
23. The Phase 1 RFG proceedings resulted in the adoption of regulations in 1990 mandating a reduction in Reid Vapor Pressure (“RVP”), the elimination of leaded gasoline, and a requirement that deposit control additives be included in gasoline. The Phase 1 regulations did not require refiners to make large capital investments.
24. CARB’s Phase 2 RFG proceedings represented an effort by CARB to develop stringent standards for low emissions, reformulated gasoline. Participants to the Phase 2 RFG proceedings understood that the CARB Phase 2 RFG regulations would require refiners to make substantial capital investments to reconfigure their refineries to produce compliant gasoline.
25. In its Phase 2 RFG proceedings, CARB did not conduct any independent studies of its own, but relied on industry to provide the needed research and resulting knowledge.
26. CARB’s Phase 2 RFG proceedings were quasi-adjudicative in nature. In the course of these proceedings, CARB adhered to the procedures set forth in the California Administrative Procedures Act. CARB provided notice of proposed regulations; provided the language of these proposed regulations and a statement of reasons; solicited and accepted written comments from the public; and conducted lengthy hearings at which oral testimony was received. CARB also issued written findings on the results of its rulemaking proceedings. Following adoption of the

Complaint

regulations, several parties sought judicial review of the CARB Phase 2 RFG regulations that provided small refiners with a two-year exemption for compliance with the regulations.

27. Unocal management and employees understood that information and data relating to the potential costs of complying with, or relating to the cost-effectiveness of, the Phase 2 regulations were material to CARB's RFG rulemaking proceedings.

**Unocal's RFG Research**

28. By 1989, Unocal management knew that CARB intended to achieve significant emissions reductions by regulating the chemical and physical properties of gasoline sold in California. Unocal scientists from the company's Science and Technology Division began to design experiments to determine how controlling various properties of gasoline affected automobile emissions. In January 1990, Unocal scientists conducted in-house emissions testing of various gasoline fuels in a single car to determine which gasoline properties had the greatest emissions impact.
29. On May 14, 1990, Unocal scientists Michael Croudace and Peter Jessup presented the preliminary results of the emissions research program to the highest levels of Unocal's management to obtain approval and funding for additional, confirmatory research. These research results were presented to the members of Unocal's Executive Committee, including Richard Stegemeier, the Chief Executive Officer and Chairman of the Board of Unocal. Unocal management approved funding for additional emissions testing, and this project became known as the "5/14 Project."
30. Unocal management approved the filing of a patent application covering the invention and discovery that sprang

## Complaint

from the “5/14 Project,” specifically the Unocal scientists’ purportedly novel discovery of the directional relationships between eight fuel properties – RVP, T10 (the temperature at which 10 percent of a fuel evaporates), T50 (the temperature at which 50 percent of a fuel evaporates), T90 (the temperature at which 90 percent of a fuel evaporates), olefin content, aromatic content, paraffin content, and octane – and three types of tailpipe emissions – *i.e.*, incompletely burned or unburned hydrocarbons (“HC”), carbon monoxide (“CO”), and nitrogen oxides (“NOx”).

31. Unocal management made prosecution of the patent application a high priority. Unocal’s chief patent counsel, Gregory Wirzbicki, personally undertook the task of prosecuting the patent application.
32. On December 13, 1990, Unocal filed with the United States Patent and Trademark Office a patent application, No. 07/628,488. This application presented Unocal’s emissions research results, including the regression equations and underlying data; detailed the directional relationships between the fuel properties and emissions studied in the “5/14 Project;” and set forth composition and method claims relating to low emissions, reformulated gasoline. All five Unocal RFG patents referred to in paragraph 15 are the progeny of the ‘488 application.

**Unocal’s Conduct Before CARB**

33. Prior to and after the filing of the patent application on December 13, 1990, Unocal employees and management discussed and considered the potential competitive advantage and corporate profit that could be extracted through effectuating an overlap between the CARB regulations and Unocal’s patent claims.
34. During the same time that Unocal participated in the CARB RFG rulemaking proceedings, specific discussions took

Complaint

place within the company concerning how to induce the regulators to use information supplied by Unocal so that Unocal could realize the huge licensing income potential of its pending patent claims.

35. Beginning in 1990, and continuing throughout the CARB Phase 2 RFG rulemaking process, Unocal provided information to CARB for the purpose of obtaining competitive advantage. Unocal gave CARB this information in private meetings with CARB, through participation in CARB's public workshops and hearings, as well as by participating in industry groups that also were providing input into the CARB regulations. This information was materially misleading in light of Unocal's suppression of facts relating to its proprietary interests in its emissions research results and Unocal's active prosecution of patents based on these research results.
36. On June 11, 1991, CARB held a public workshop regarding the Phase 2 RFG regulations. This workshop included discussions of CARB staff's proposed gasoline specifications – *i.e.*, the levels at which certain gasoline properties should be set – to reduce the emissions from gasoline-fueled vehicles. The set of specifications proposed by CARB for discussion at this public workshop did not include a T50 specification.
37. On June 20, 1991, Unocal presented to CARB staff the results of its "5/14 Project" to show CARB that "cost-effective" regulations could be achieved through adoption of a "predictive model" and to convince CARB of the importance of T50. Unocal's pending patent application contained numerous claims that included T50 as a critical limitation, in addition to other fuel properties that CARB proposed to regulate.

## Complaint

38. Prior to the presentation to CARB, Unocal management decided not to disclose Unocal's pending '393 patent application to CARB staff.
39. On July 1, 1991, Unocal provided CARB with the actual emissions prediction equations developed in the "5/14 Project." Unocal requested that CARB "hold these equations confidential, as we feel that they may represent a competitive advantage in the production of gasoline." But Unocal went on to state:

If CARB pursues a meaningful dialogue on a predictive model approach to Phase 2 gasoline, Unocal will consider making the equations and underlying data public as required to assist in the development of a predictive model.
40. Following CARB's agreement to develop a predictive model, Unocal made its emissions research results, including the test data and equations underlying its "5/14 Project," publicly available.
41. On August 27, 1991, Unocal unequivocally stated in a letter to CARB that its emissions research data were "nonproprietary." Specifically, Unocal stated:

Please be advised that Unocal now considers this data to be non-proprietary and available to CARB, environmental interest groups, other members of the petroleum industry, and the general public upon request.
42. At the time Unocal submitted its August 27, 1991 letter to CARB, it did not disclose to CARB its proprietary interests in the "5/14 Project" data and equations, its prosecution of a patent application, or its intent to enforce its proprietary interests to obtain licensing income. Read separately or in

Complaint

conjunction with Unocal's July 1, 1991 letter, the August 27, 1991 letter created the materially false and misleading impression that Unocal agreed to give up any "competitive advantage" it may have had relating to its purported invention and arising from its emissions research results.

43. In reasonable reliance on Unocal's representation that the information was no longer proprietary, CARB used Unocal's equations in setting a T50 specification. Subsequently, in October 1991, CARB published Unocal's equations in public documents supporting the proposed Phase 2 RFG regulations.
44. On November 22, 1991, the CARB Board adopted Phase 2 RFG regulations that set particular standards for the composition of low emissions, reformulated gasoline. These regulations specified limits for eight gasoline properties: RVP, benzene, sulfur, aromatics, olefins, oxygen, T50, and T90. Unocal's pending patent claims recited limits for five of the eight properties specified by the regulations: T50, T90, olefins, aromatics, and RVP.
45. Unocal's misrepresentations and materially false and misleading statements caused CARB to adopt Phase 2 RFG regulations that substantially overlapped with Unocal's concealed patent claims. Specifically, for example, CARB included a specification for T50 in its Phase 2 RFG regulations and eventually adopted a "predictive model" that included T50 as one of the parameters.
46. Prior to the final approval of the CARB Phase 2 RFG regulations in November 1992, Unocal submitted comments and presented testimony to CARB opposing CARB's proposal to grant small refiners a two-year exemption for complying with the regulations. Unocal vigorously opposed this proposed exemption on the grounds that it would increase the costs of compliance and undermine the cost-effectiveness of the CARB Phase 2 RFG

## Complaint

regulations. In making these statements, Unocal again failed to disclose that it had proprietary rights that would materially increase the cost and reduce the cost-effectiveness and flexibility of the regulations that CARB had adopted in reasonable reliance on Unocal's representations.

47. CARB amended the Phase 2 regulations in June 1994 to include a predictive model as an alternative method of complying with the regulations that was intended to provide refiners with additional flexibility. At the urging of numerous companies, including Unocal, this "predictive model" permits a refiner to comply with the RFG regulations by producing fuel that is predicted – based on its composition and the levels of the eight properties – to have equivalent emissions to a fuel that meets the strict gasoline property limits set forth in the regulations.
48. During the development of the predictive model, Unocal continued to meet with CARB, providing testimony and information. Unocal submitted comments to CARB touting the predictive model as offering "flexibility" and furthering CARB's mandate of "cost-effective" regulations. These statements were materially false and misleading because Unocal suppressed the material fact that assertion of its proprietary rights would materially increase the cost and reduce the flexibility of the proposed regulations.
49. On February 22, 1994, the United States Patent Office issued the '393 patent. CARB first became aware of Unocal's '393 patent shortly after Unocal's issuance of a press release on January 31, 1995.

**Unocal's Participation in Industry Groups**

50. During the CARB RFG rulemaking, Unocal actively participated in the Auto/Oil Air Quality Improvement Research Program ("Auto/Oil" or the "Program"), a



Complaint

cooperative, joint research program between the automobile and oil industries. By agreement dated October 14, 1989, the big three domestic automobile manufacturers – General Motors, Ford, and Chrysler – and representatives from fourteen oil companies, including Unocal, entered into a joint research agreement in accordance with the National Cooperative Research Act of 1984 (“Auto/Oil Agreement”).

51. The stated objective of the Auto/Oil joint research venture was to plan and carry out research and tests designed to measure and evaluate automobile emissions and the potential improvements in air quality achievable through the use of reformulated gasolines, methanol, and other alternative fuels, and to evaluate the relative cost-effectiveness of these various improvements.
52. The Auto/Oil Agreement provided that “[t]he results of research and testing of the Program will be disclosed to government agencies, the Congress and the public, and otherwise placed in the public domain.” This agreement specifically provided for the following dedication of any and all intellectual property rights to the public:

No proprietary rights will be sought nor patent applications prosecuted on the basis of the work of the Program unless required for the purpose of ensuring that the results of the research by the Program will be freely available, without royalty, in the public domain.
53. While the Auto/Oil Agreement permitted participating companies to conduct independent research, and further permitted them to withhold the fruits of such independent research from the Auto/Oil Group, once data and information were in fact presented to the Auto/Oil Group, they became the “work of the Program.”

## Complaint

54. Unocal viewed its participation in industry groups, such as Auto/Oil, as an integral part of its strategy of deception for the purpose of obtaining a competitive advantage therefrom. On September 26, 1991, Unocal presented to Auto/Oil the results of Unocal's emissions research, including the test data, equations, and corresponding directional relationships between fuel properties and emissions derived from the "5/14 Project." Unocal management authorized this presentation, which was substantially similar to that made to CARB on June 20, 1991. Unocal informed Auto/Oil participants that the data had been made available to CARB and were in the public domain. Unocal also represented that the data would be made available to Auto/Oil participants. Unocal's 5/14 work thus became part of the "work" of the Auto/Oil Program.
55. Unocal's 5/14 work also became part of the Auto/Oil Program through the subsequent testing – as part of the Program – of the 5/14 fuel property relationships.
56. During the CARB Phase 2 RFG rulemaking proceedings, Unocal also actively participated in the Western States Petroleum Association ("WSPA"), an oil industry trade association that represents companies accounting for the bulk of petroleum exploration, production, refining, transportation and marketing in the western United States. WSPA, as a group, actively participated in the CARB RFG rulemaking process. WSPA commissioned, and submitted to CARB, three cost studies in connection with the CARB Phase 2 RFG rulemaking.
57. One cost study commissioned by WSPA incorporated information relating to process royalty rates associated with non-Unocal patents and was used by CARB to determine the cost-effectiveness of the proposed CARB Phase 2 RFG standards. This WSPA cost study estimated the costs of the proposed regulations on a cents-per-gallon basis and estimated the incremental costs associated with regulating

Complaint

specific gasoline properties. This WSPA study could have incorporated costs associated with potential royalties flowing from Unocal's pending patent rights.

58. On September 10, 1991, Unocal presented its "5/14 Project" emissions research results to WSPA. Unocal management authorized the presentation of the research results to WSPA. This Unocal presentation created the materially false and misleading impression that Unocal's emissions research results, including the data and equations, were nonproprietary and could be used by WSPA or its individual members without concern for the existence or enforcement of any intellectual property rights.
59. None of the participants in the WSPA or Auto/Oil groups knew of the existence of Unocal's proprietary interests and/or pending patent rights at any time prior to the issuance of the '393 patent in February 1994, by which time most, if not all, of the oil company participants to these groups had made substantial progress in their capital investment and refinery modification plans for compliance with the CARB Phase 2 RFG regulations.

**Unocal's Patent Prosecution and Enforcement**

60. Following the November 1991 adoption of CARB Phase 2 RFG specifications, Unocal amended its patent claims in March 1992 to ensure that the patent claims more closely matched the regulations. In some cases, Unocal's patent claims were narrowed to resemble the regulations.
61. On or about July 1, 1992, Unocal received an office action from the U.S. Patent and Trademark Office indicating that most of Unocal's pending patent claims had been allowed. Unocal did not disclose this information to CARB or other participants to the CARB Phase 2 RFG rulemaking.

## Complaint

62. Subsequently, after the submission of additional amendments, Unocal received a notice of allowance from the U.S. Patent and Trademark Office for all of its pending claims in February 1993. Unocal did not disclose this information to CARB or other participants to the CARB Phase 2 RFG rulemaking.
63. In June 1993, Unocal filed a divisional application (No. 08/77,243) of its original patent application that allowed Unocal to pursue additional patents based on the discoveries of the “5/14 Project.”
64. The U.S. Patent and Trademark Office issued the ’393 patent to Unocal on February 22, 1994. Unocal waited until January 31, 1995, to issue a press release announcing issuance of the ’393 patent. The Unocal press release stated that the ’393 patent “covers many of the possible fuel compositions that refiners would find practical to manufacture and still comply with the strict California Air Resources Board (CARB) Phase 2 requirements.”
65. In March 1995, Unocal met separately with California Governor Pete Wilson and CARB and made assurances that Unocal would not enjoin or otherwise impair the ability of refiners to produce and supply to the California market gasoline that complied with the CARB Phase 2 RFG regulations. In or about the same time period, CARB expressed its own concern to Unocal about the coverage of the patent and even sought and received from Unocal a license to use the ’393 patent in making and using test fuels.
66. On March 22, 1995, five days after meeting with CARB staff, Unocal filed a continuation patent application (No. 08/409,074) claiming priority to the original December 1990 application. Unocal did not inform CARB or Governor Wilson that it intended to obtain additional RFG patents.

Complaint

67. Unocal subsequently filed additional continuation patent applications on June 5, 1995 (No. 08/464,544), August 1, 1997 (No. 08/904,594), and November 13, 1998 (No. 08/191,924), all claiming priority based on Unocal's original December 13, 1990 patent application.
68. On April 13, 1995, ARCO, Exxon, Mobil, Chevron, Texaco, and Shell filed suit in the United States District Court for the Central District of California seeking to invalidate Unocal's '393 patent. Unocal filed a counterclaim for patent infringement of the '393 patent. The jury in this private litigation determined that Unocal's '393 patent was valid and infringed, and found that the refiners must pay a royalty rate of 5.75 cents per gallon for the period from March through July 1996 for sales of infringing gasoline in California.
69. The United States Court of Appeals for the Federal Circuit subsequently affirmed the trial court's judgment. The United States Supreme Court denied the refiner-defendants' petition for a writ of certiorari. The refiner-defendants have made payments totaling \$91 million to Unocal for damages, costs, and attorneys' fees.
70. An accounting action is still ongoing in the United States District Court for the Central District of California to determine damages for infringement of the '393 patent by the refiners for the period from August 1, 1996, through December 31, 2000. The court ruled in August 2002 that the 5.75 cents per gallon royalty fee awarded by the jury would apply to all infringing gasoline produced and/or supplied in California.
71. On January 23, 2002, Unocal sued Valero Energy Company in the Central District of California for willful infringement of both the '393 patent and the '126 patent (see Paragraph

## Complaint

9). In its complaint, Unocal seeks damages at the rate of 5.75 cents per gallon for all infringing gallons, and treble damages for willful infringement.

72. Unocal also has enforced its patent claims through licensing activities. To date, Unocal has entered into license agreements with eight refiners, blenders and/or importers covering the use of all five RFG patents. The terms of these license agreements are confidential. Unocal has announced that these license agreements feature a “uniform” licensing schedule that specifies a range from 1.2 to 3.4 cents per gallon depending on the volume of gasoline falling within the scope of the patents. As a licensee practices under the license more frequently, the licensing fee per gallon is reduced.

**Relevant Product and Geographic Markets**

73. Unocal has obtained and exercised market power and/or monopoly power in two relevant product markets.
74. One relevant product market consists of the technology claimed in patent application No. 07/628,488 (filed on December 13, 1990) and Unocal’s issued RFG patents, and any alternative technologies that enable firms to refine, produce, and supply CARB-compliant “summer-time” RFG for sale in California at comparable or lower cost, and comparable or higher effectiveness, without practicing the Unocal technology. The relevant geographic market for such technology is worldwide.
75. Another relevant market consists of CARB-compliant “summer-time” RFG produced and supplied for sale in California. The relevant geographic market is California.

Complaint

**Unocal's Materially False and Misleading Statements  
During CARB's RFG Proceedings Led to its Market Power**

76. By engaging in fraudulent conduct in connection with the CARB rulemaking proceedings, Unocal unlawfully obtained market power. Unocal obtained unlawful market power through affirmative misrepresentations, materially false and misleading statements, and other bad-faith, deceptive conduct that caused CARB to enact regulations that overlapped almost entirely with Unocal's pending patent rights.
77. Unocal, through its management and authorized employees, made knowing and willful misrepresentations to CARB by making materially false and misleading statements and/or by suppressing facts while giving information of other facts that were likely to mislead for want of communication of the suppressed facts. Unocal's statements were materially false and misleading in that they failed to disclose Unocal's proprietary interests in its emissions research data, and/or Unocal's intention and efforts to obtain competitive advantage and corporate profit through enforcement of its intellectual property rights.
78. Unocal's knowing and willful misrepresentations to CARB include, but are not limited to, the following:
  - a. Unocal presented its emissions research results to CARB on June 20, 1991, for the purpose, *inter alia*, of showing CARB the relationship between T50 and automobile exhaust emissions; and it represented that a predictive model that included T50 would be "cost effective" and flexible without disclosing that the assertion of its proprietary rights would materially increase the cost and reduce the flexibility of such a model. Unocal represented that these data and equations were confidential to Unocal, and "may represent a competitive advantage" to Unocal.

## Complaint

- b. Having previously asserted that its equations might provide it with a competitive advantage, Unocal informed CARB by letter, dated August 27, 1991, that its emissions research data thereafter would be “nonproprietary” and available to CARB, industry members, and the general public. By this representation, Unocal created the materially false and misleading impression that Unocal had relinquished or would not enforce any proprietary interests in its emissions research results.
  - c. On numerous occasions after August 27, 1991, Unocal made statements and comments to CARB relating to the “cost effectiveness” of CARB Phase 2 regulations, and the “flexibility” offered by the implementation of a predictive model to reduce refiner compliance costs. These statements and comments include, but are not limited to, both written and/or oral statements made to CARB on the following dates: October 29, 1991, November 21, 1991, November 22, 1991, March 16, 1992, June 19, 1992, August 14, 1992, September 4, 1992, June 3, 1994, and June 9, 1994. Under the circumstances, these statements further reinforced the materially false and misleading impression that Unocal had no proprietary interests in its emissions research results and/or that Unocal had disclaimed any and all such proprietary rights and would not seek to enforce these rights.
79. Throughout its communications and interactions with CARB prior to January 31, 1995, Unocal failed to disclose that it had pending patent rights, that its patent claims overlapped with the proposed RFG regulations, and that Unocal intended to charge royalties. Unocal hence failed to disclose material information that would have impacted CARB’s analysis of the cost-effectiveness of the Phase 2



Complaint

RFG regulations. Unocal instead perpetuated false and misleading impressions concerning the nature of its proprietary interests in its “5/14 Project” research results.

80. CARB reasonably relied on Unocal’s misrepresentations and materially false and misleading statements in developing the Phase 2 RFG regulations. But for Unocal’s fraud, CARB would not have adopted RFG regulations that substantially overlapped with Unocal’s concealed patent claims; the terms on which Unocal was later able to enforce its proprietary interests would have been substantially different; or both.
81. Unocal, through its management and authorized employees, made knowing and willful misrepresentations to participants in the Auto/Oil joint venture by making materially false and misleading statements and/or by suppressing facts while giving information of other facts which were likely to mislead for want of communication of the suppressed facts.
82. Unocal made a presentation to Auto/Oil on September 26, 1991, at which Unocal shared its research results with the group. Unocal informed Auto/Oil that CARB also had been provided with Unocal’s data and equations, and that these data and equations were in the public domain. Unocal represented that it would supply its data to the Auto/Oil Group and its members. Unocal’s statements were materially false and misleading in that they failed to disclose Unocal’s proprietary interests in its emissions research results and Unocal’s intention and efforts to obtain competitive advantage through enforcement of its intellectual property rights.
83. Throughout all of its communications and interactions with Auto/Oil prior to January 31, 1995, Unocal failed to disclose that it had pending patent rights, that its patent claims overlapped with the proposed RFG regulations, and that Unocal intended to charge royalties.

## Complaint

84. By deceptive conduct that included, but was not limited to, false and misleading statements concerning its proprietary interests in the results of its emissions research results, Unocal violated the letter and spirit of the Auto/Oil Agreement and breached its fiduciary duties to the other members of the Auto/Oil joint venture. Such deceptive conduct violated the integrity of the Auto/Oil joint venture's procedures and subverted Auto/Oil's process of providing accurate and nonproprietary research data and information to CARB.
85. Unocal, through its management and authorized employees, made knowing and willful misrepresentations to members of WSPA by making materially false and misleading statements and/or by suppressing facts while giving information of other facts which were likely to mislead for want of communication of the suppressed facts. Unocal's statements were materially false and misleading in that they failed to disclose Unocal's proprietary interests in its emissions research results and/or Unocal's intention and efforts to obtain competitive advantage through enforcement of its intellectual property rights.
86. Unocal made a presentation to WSPA on September 10, 1991, relating to its emissions research. At, or shortly following this presentation, Unocal provided to WSPA members the data and equations derived from this emissions research. In its interactions with WSPA, Unocal created the materially false and misleading impression that Unocal did not have any proprietary interests or intellectual property rights associated with its emissions research results.
87. Unocal actively participated in WSPA committees that discussed the potential cost implications of the CARB Phase 2 RFG regulations. Unocal knew that royalties were considered in a cost study commissioned by WSPA for submission to CARB.

Complaint

88. Throughout all of its communications and interactions with WSPA prior to January 31, 1995, Unocal failed to disclose that it had pending patent rights, that its patent claims overlapped with the proposed RFG regulations, and that Unocal intended to charge royalties.
89. By deceptive conduct that included, but was not limited to, false and misleading statements concerning its proprietary interests in the results of its emissions research results, Unocal breached its fiduciary duties to the other members of WSPA. Such deceptive conduct violated the integrity of the WSPA's procedures and subverted WSPA's process of providing accurate data and information to CARB.
90. Participants in Auto/Oil and WSPA reasonably relied on Unocal's misrepresentations and material omissions. But for Unocal's fraud, these participants in the rulemaking process would have taken actions including, but not limited to, (a) advocating that CARB adopt regulations that minimized or avoided infringement on Unocal's patent claims; (b) advocating that CARB negotiate license terms substantially different from those that Unocal was later able to obtain; and/or (c) incorporating knowledge of Unocal's pending patent rights in their capital investment and refinery reconfiguration decisions to avoid and/or minimize potential infringement. As a result, if other participants in WSPA or Auto/Oil had known the truth, the harm to competition and consumers, as described in this Complaint, would have been avoided.
91. Unocal's fraudulent conduct has resulted in Unocal's acquisition of market power in the following markets: the technology market for the production and supply of CARB-compliant "summer-time" gasoline in California, and the downstream product market for CARB-compliant "summer-time" gasoline in California.

## Complaint

92. The extensive overlap between the CARB RFG regulations and the Unocal patent claims makes avoidance of the Unocal patent claims technically and/or economically infeasible.
93. Refiners in California invested billions of dollars in sunk capital investments without knowledge of Unocal's patent claims to reconfigure their refineries in order to comply with the CARB Phase 2 RFG regulations. These refiners cannot produce significant volumes of non-infringing CARB-compliant gasoline without incurring substantial additional costs.
94. CARB cannot now change its RFG regulations sufficiently to provide flexibility for refiners and others to avoid Unocal's patent claims. Had Unocal disclosed its proprietary interests and pending patent rights to CARB earlier, CARB would have been able to consider the potential costs of the Unocal patents in establishing its regulations, and the harm to competition and to consumers, as described in this Complaint, would have been avoided.
95. Unocal has exercised, and continues to exercise, its market power through business conduct by enforcing its patents through litigation and licensing activities. Through its litigation and licensing related to its RFG patents, Unocal has enforced, or threatened to enforce, its patents against those refiners that control in excess of 95 percent of the capacity for the manufacture and/or sale of CARB-compliant gasoline in California. Unocal's enforcement of its patent rights is the proximate cause of substantial competitive harm and consumer injury.
96. Unocal is not shielded from antitrust liability pursuant to the Noerr-Pennington doctrine for numerous reasons as a matter of law and as a matter of fact including, but not limited to, the following: (i) Unocal's misrepresentations were made in the course of quasi-adjudicative rulemaking proceedings;

Complaint

(ii) Unocal's conduct did not constitute petitioning behavior; and (iii) Unocal's misrepresentations and materially false and misleading statements to Auto/Oil and WSPA, two non-governmental industry groups, were not covered by any petitioning privilege.

**Anticompetitive Effects of Unocal's Conduct**

97. The foregoing conduct by Unocal has materially caused or threatened to cause substantial harm to competition and will, in the future, materially cause or threaten to cause further substantial injury to competition and consumers, absent the issuance of appropriate relief in the manner set forth below. The threatened or actual anticompetitive effects of Unocal's conduct include, but are not limited to, those set forth in Paragraph 8 above.
98. Unocal's enforcement of its patent portfolio has caused, and will cause, substantial consumer injury. Unocal's own economic expert has testified under oath that 90 percent of any royalty costs associated with the patents will be passed through to consumers in the form of higher retail gasoline prices.

**First Violation Alleged**

99. As described in Paragraphs 1-98 above, which are incorporated herein by reference, Unocal has willfully engaged in anticompetitive and exclusionary acts and practices, undertaken since the early 1990s, and continuing even today, whereby it has wrongfully obtained monopoly power in the technology market for the production and supply of CARB-compliant "summer-time" gasoline to be sold in California, which acts and practices constitute unfair methods of competition in violation of Section 5 of the FTC Act.

Complaint

---

**Second Violation Alleged**

100. As described in Paragraphs 1-98 above, which are incorporated herein by reference, Unocal has willfully engaged in anticompetitive and exclusionary acts and practices, undertaken since the early 1990s, and continuing even today, with a specific intent to monopolize the technology market for the production and supply of CARB-compliant “summer-time” gasoline to be sold in California, resulting, at a minimum, in a dangerous probability of monopolization in the aforementioned market, which acts and practices constitute unfair methods of competition in violation of Section 5 of the FTC Act.

---

**Third Violation Alleged**

101. As described in Paragraphs 1-98 above, which are incorporated herein by reference, Unocal has willfully engaged in anticompetitive and exclusionary acts and practices, undertaken since the early 1990s, and continuing even today, with a specific intent to monopolize the downstream goods market for CARB-compliant “summer-time” gasoline to be sold in California, resulting, at a minimum, in a dangerous probability of monopolization in the aforementioned market, which acts and practices constitute unfair methods of competition in violation of Section 5 of the FTC Act.

---

**Fourth Violation Alleged**

102. As described in Paragraphs 1-98 above, which are incorporated herein by reference, Unocal has willfully engaged in anticompetitive and exclusionary acts and practices, undertaken since the early 1990s, and continuing even today, whereby it has unreasonably restrained trade in the technology market for the production and supply of CARB-compliant “summer-time” gasoline to be sold in California, which acts and practices constitute unfair

Complaint

methods of competition that harm consumers in violation of Section 5 of the FTC Act.

---

**Fifth Violation Alleged**

103. As described in Paragraphs 1-98 above, which are incorporated herein by reference, Unocal has willfully engaged in anticompetitive and exclusionary acts and practices, undertaken since the early 1990s, and continuing even today, whereby it has unreasonably restrained trade in the downstream goods market for CARB-compliant “summer-time” gasoline to be sold in California, which acts and practices constitute unfair methods of competition that harm consumers in violation of Section 5 of the FTC Act.

**Notice**

Notice is hereby given to the Respondent that the fourth day of June, 2003, at 10 a.m., or such later date as determined by an Administrative Law Judge of the Federal Trade Commission, is hereby fixed as the time and Federal Trade Commission offices, 600 Pennsylvania Avenue, N.W., Washington, D.C. 20580, as the place when and where a hearing will be had before an Administrative Law Judge of the Federal Trade Commission, on the charges set forth in this complaint, at which time and place you will have the right under the FTC Act to appear and show cause why an order should not be entered requiring you to cease and desist from the violations of law charged in the complaint.

You are notified that the opportunity is afforded to you to file with the Commission an answer to this complaint on or before the twentieth (20<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.

## Complaint

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 Administrative Law Judge shall file an initial decision containing appropriate findings and conclusions and an appropriate order disposing of the proceeding. In such answer, you may, however, reserve the right to submit proposed findings and conclusions under § 3.46 of the Commission's Rules of Practice for Adjudicative Proceedings and the right to appeal the initial decision to the Commission under § 3.52 of said Rules.

Failure to answer within the time above provided shall be deemed to constitute a waiver of your right to appear and contest the allegations of the complaint and shall authorize the Administrative Law Judge, without further notice to you, to find the facts to be as alleged in the complaint and to enter an initial decision containing such findings, appropriate conclusions, and order.

The ALJ will schedule an initial prehearing scheduling conference to be held not later than 14 days after the last answer is filed by any party named as a Respondent in the complaint. Unless otherwise directed by the ALJ, 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 prehearing scheduling conference, and Rule 3.31(b) obligates counsel for each party, within 5 days of receiving a respondent's answer, to make certain initial disclosures without awaiting a formal discovery request.

**Notice of Contemplated Relief**

Should the Commission conclude from the record developed in any adjudicative proceedings in this matter that Respondent's



Complaint

conduct violated Section 5 of the Federal Trade Commission Act as alleged in the complaint, the Commission may order such relief as is supported by the record and is necessary and appropriate, including but not limited to:

1. Requiring Respondent to cease and desist all efforts it has undertaken by any means, including without limitation the threat, prosecution, or defense of any suits or other actions, whether legal, equitable, or administrative, as well as any arbitration, mediation, or any other form of private dispute resolution, through or in which Respondent has asserted that any person or entity, by manufacturing, selling, distributing, or otherwise using motor gasoline to be sold in California infringes any of Respondent's current or future United States patents that claim priority back to U.S. Patent Application Number No. 07/628,488 filed December 13, 1990 or any other Patent Application filed before January 31, 1995.
2. Requiring Respondent not to undertake any new efforts by any means, including without limitation the threat, prosecution, or defense of any suits or other actions, whether legal, equitable, or administrative, as well as any arbitration, mediation, or any other form of private dispute resolution, through or in which Respondent has asserted that any person or entity, by manufacturing, selling, distributing, or otherwise using motor gasoline to be sold in California infringes any of Respondent's current or future United States patents that claim priority back to U.S. Patent Application Number No. 07/628,488 filed December 13, 1990 or any other Patent Application filed before January 31, 1995.
3. Requiring Respondent to cease and desist all efforts it has undertaken by any means, including without limitation the threat, prosecution, or defense of any suits or other actions, whether legal, equitable, or administrative, as well as any arbitration, mediation, or any other form of private dispute resolution, through or in which Respondent has asserted that any person or entity, by manufacturing, selling, distributing, or

## Complaint

otherwise using motor gasoline, for import or export to or from the state of California, infringes any of Respondent's current or future United States patents that claim priority back to U.S. Patent Application No. 07/628,488 filed December 13, 1990 or any other Patent Application filed before January 31, 1995.

4. Requiring Respondent to employ, at Respondent's cost, a Commission-approved compliance officer who will be the sole representative of Respondent for the purpose of communicating Respondent's patent rights relating to any standard or regulations under consideration by (a) any standard-setting organization of which Respondent is a member; and/or (b) any state or federal governmental entity that conducts rulemaking proceedings in which Respondent participates.
5. Such other or additional relief as is necessary to correct or remedy the violations alleged in the complaint.

WHEREFORE, THE PREMISES CONSIDERED, the Federal Trade Commission on this fourth day of March, 2003, issues its complaint against said Respondent.

Decision and Order

## **DECISION AND ORDER**

The Federal Trade Commission (“Commission”), having heretofore issued its complaint charging Respondent Union Oil Company of California with violations of Section 5 of the Federal Trade Commission Act, as amended, and Respondent Union Oil Company of California having been served a copy of that complaint, together with a notice of contemplated relief, and Respondent Union Oil Company of California having answered the complaint denying said charges and asserting affirmative defenses but admitting the jurisdictional allegations set forth herein; and the matter having proceeded through the completion of an adjudicative hearing; and

The Respondent, its attorneys, and counsel for the Commission having thereafter executed an Agreement Containing Consent Order, an admission by the Respondent of all the jurisdictional facts set forth in the complaint, a statement that the signing of said agreement is for settlement purposes only, is entered into by Respondent contingent upon the Agreement Containing Consent Order in the Matter of Chevron Corporation and Unocal Corporation, File No. 051-1225 (the “Merger Consent”) and does not constitute an admission by Respondent that the law has been violated as alleged in such complaint, or that the facts as alleged in such complaint, other than jurisdictional facts, are true and waivers and other provisions as required by the Commission’s Rules, which admission and statement are contingent upon the consummation of the Merger and are effective only upon the Merger Effective Date; and

The Secretary of the Commission having thereafter withdrawn this matter from adjudication in accordance with § 3.25(c) of its Rules; and

The Commission having thereafter considered the matter and having thereupon accepted the executed consent agreement and placed such agreement on the public record for a period of thirty (30) days, and having duly considered the comments received

## Decision and Order

from interested parties pursuant to § 2.34 of its Rules, now in further conformity with the procedure prescribed in § 3.25(f) of its Rules, the Commission hereby makes the following jurisdictional findings and enters the following Order:

1. Respondent Union Oil Company of California is a corporation organized, existing under and by virtue of the laws of the state of California, with its office and principal place of business located at 2141 Rosecrans Avenue, Suite 4000, El Segundo, California 90245. Respondent Union Oil Company of California is a wholly owned operating subsidiary of Unocal Corporation, a corporation organized, existing and doing business under and by virtue of the laws of the state of Delaware.

2. The Federal Trade Commission has jurisdiction of the subject matter of this proceeding and of Respondent, and the proceeding is in the public interest.

**ORDER****I.**

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

- A. "Chevron" means Chevron Corporation (formerly ChevronTexaco Corporation), its directors, officers, employees, agents, representatives, successors, and assigns; and its joint ventures, subsidiaries, divisions, groups and affiliates controlled by Chevron Corporation, and the respective directors, officers, employees, agents, representatives, successors, and assigns of each.
- B. "Union Oil" means Union Oil Company of California, its directors, officers, employees, agents, representatives, successors, and assigns; its joint ventures, subsidiaries, divisions, groups and affiliates controlled by Union Oil Company of California, and the respective directors, officers,

Decision and Order

employees, agents, representatives, successors, and assigns of each.

- C. “Unocal” means Unocal Corporation, its directors, officers, employees, agents, representatives, successors, and assigns; and its joint ventures, subsidiaries (including but not limited to Union Oil Company of California), divisions, groups and affiliates controlled by Unocal Corporation, and the respective directors, officers, employees, agents, representatives, successors, and assigns of each.
- D. “Respondent” means Union Oil.
- E. “Commission” means the Federal Trade Commission.
- F. “Action” means any lawsuit or other action, whether legal, equitable, or administrative, as well as any arbitration, mediation, or any other form of private dispute resolution, in the United States or anywhere else in the world.
- G. “License Agreement” means any contract, agreement, arrangement or other understanding between Unocal and any other party or parties that requires, calls for, or otherwise contemplates, payment of fees, royalties or other monies, in cash or in kind, to practice under the Relevant U.S. Patents.
- H. “Merger” means the proposed merger between Chevron and Unocal, as contemplated by the Agreement and Plan of Merger dated as of April 4, 2005 among Unocal Corporation, ChevronTexaco Corporation, and Blue Merger Sub Inc.
- I. “Merger Effective Date” means the earlier of the following dates:
  - 1. the date that the certificate of merger for the Merger is filed with the Secretary of State of Delaware or such later time as specified in such certificate of merger, or

## Decision and Order

2. the date that Chevron acquires control of Unocal Corporation, as "control" is defined by 16 C.F.R. § 801.1(b).
- J. "Person" means both natural persons and artificial persons, including, but not limited to, corporations, unincorporated entities, and governments.
- K. "Relevant U.S. Patents" means United States Patent Numbers 5,288,393, 5,593,567, 5,653,866, 5,837,126, 6,030,521, and any other patents presently in existence or to be issued in the future that claim priority to United States Patent Application Number 07/628,488, filed December 13, 1990.

**II.**

IT IS FURTHER ORDERED that, immediately upon the Merger Effective Date, Respondent shall cease and desist from any and all efforts, and shall not undertake any new efforts, by any means, directly or indirectly, in or affecting commerce as "commerce" is defined in Section 4 of the Federal Trade Commission Act, 15 U.S.C. § 44, to assert or enforce any of the Relevant U.S. Patents against any Person, to recover any damages or costs for alleged infringements of any of the Relevant U.S. Patents, or to collect any fees, royalties or other payments, in cash or in kind, for the practice of any of the Relevant U.S. Patents, including but not limited to fees, royalties, or other payments, in cash or in kind, to be collected pursuant to any License Agreement, provided, however, that nothing in this Order obligates or requires Respondent to refund any fees, royalties or other payments collected in connection with any of the Relevant U.S. Patents prior to the Merger Effective date.

Decision and Order

**III.**

IT IS FURTHER ORDERED that:

- A. Within thirty (30) days following the Merger Effective Date, Respondent shall file, or cause to be filed, with the United States Patent and Trademark Office, the necessary documents pursuant to 35 U.S.C. § 253, 37 C.F.R. § 1.321, and the Manual of Patent Examining Procedure to disclaim or dedicate to the public the remaining term of the Relevant U.S. Patents, provided, however, that such disclaimer or dedication to the public shall not constitute an admission or representation by Respondent with respect to the validity or patentability of the claims of the Relevant U.S. Patents.
- B. Respondent shall correct as necessary, and shall not withdraw or seek to nullify, any disclaimers, or dedications filed pursuant to Paragraph III. A.

**IV.**

IT IS FURTHER ORDERED that, within thirty (30) days following the Merger Effective Date, Respondent shall move to dismiss, with prejudice, all Actions relating to the alleged infringement of any Relevant U.S. Patents, including but not limited to the following actions pending in the United States District Court for the Central District of California: *Union Oil Company of California v. Atlantic Richfield Company, et al.*, Case No. CV-95-2379-CAS and *Union Oil Company of California v. Valero Energy Corporation*, Case No. CV-02-00593-SVW.

**V.**

IT IS FURTHER ORDERED that:

- A. Within thirty (30) days after the date this Order becomes final, Respondent shall distribute a copy of this Order and the complaint in this matter to:

## Decision and Order

1. any Person that Respondent has contacted regarding possible infringement of any of the Relevant U.S. Patents,
  2. any Person against which Respondent is, or was, in any Action regarding possible infringement of any of the Relevant U.S. Patents,
  3. any licensee or other Person from which Respondent has collected any fees, royalties or other payments, in cash or in kind, for the practice of the Relevant U.S. Patents, and
  4. any Person that Respondent has contacted with regard to the possible collection of any fees, royalties or other payments, in cash or in kind, for the practice of the Relevant U.S. Patents.
- B. Within thirty (30) days after the date this Order becomes final, Respondent shall distribute a copy of this Order and the complaint in this matter to every officer and director of Respondent having responsibility for any of Respondent's obligations under this Order, and to every employee or agent having managerial responsibility for any of Respondent's obligations under this Order.
- C. For a period of five (5) years after the date this Order becomes final, Respondent shall furnish a copy of this Order and the complaint in this matter to each new officer and director of Respondent who will have responsibility for any of Respondent's obligations under this Order, and to each new employee or agent of Respondent who will have managerial responsibility for any of Respondent's obligations under the Order. Such copies shall be furnished within thirty (30) days after each such person assumes his or her position as officer, director, employee, or agent. For purposes of this Paragraph V.C., "new employee or agent" shall include, without limitation, Respondent's employees and agents whose duties change during their employment or agency relationship to



Decision and Order

include managerial responsibility for any of Respondent's obligations under this Order.

**VI.**

IT IS FURTHER ORDERED that:

- A. Respondent shall, within sixty (60) days after the date this Order becomes final, submit to the Commission a verified written report setting forth in detail the manner and form in which Respondent intends to comply, is complying, and has complied with this Order.
- B. Respondent shall, one year from the date this Order becomes final and annually thereafter for five (5) years, submit a verified written report to the Commission setting forth in detail the manner and form in which Respondent has complied and is complying with the Order.

**VII.**

IT IS FURTHER ORDERED that, for the purpose of determining or securing compliance with this Order, and subject to any legally recognized privilege, and upon written request with reasonable notice to Respondent, Respondent shall permit any duly authorized representative of the Commission:

- A. Access, during office hours of Respondent and in the presence of counsel, to all facilities and access to inspect and copy all books, ledgers, accounts, correspondence, memoranda, and all other records and documents in the possession or under the control of Respondent related to compliance with this Order; and
- B. Upon five (5) days' notice to Respondent and without restraint or interference from Respondent, to interview officers, directors, or employees of Respondent, who may have counsel present, regarding such matters.

Decision and Order

**VIII.**

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

**IX.**

IT IS FURTHER ORDERED that this Order will terminate twenty (20) years after the date it becomes final.

Analysis

**Analysis of Proposed Consent Order to Aid Public Comment**

The Federal Trade Commission has accepted for public comment an Agreement Containing Consent Order (“Agreement”) with Union Oil Company of California (“Union Oil”) to resolve matters charged in an Administrative Complaint issued by the Commission on March 4, 2003 (“Complaint”). Pursuant to the Agreement, Union Oil provisionally has agreed to be bound by a proposed consent order (“Proposed Consent Order”).

The Agreement has been placed on the public record for thirty (30) days for receipt of comments from interested members of the public. The Agreement is for settlement purposes only and does not constitute an admission by Union Oil that the law has been violated as alleged in the Complaint or that the facts alleged in the Complaint, other than jurisdictional facts, are true. The Proposed Consent Order remedies alleged anticompetitive effects arising from Union Oil’s conduct, as alleged in the Complaint.

**I. The Commission’s Complaint**

The Complaint alleges that Respondent Union Oil engaged in a series of acts to subvert state regulatory standard-setting procedures relating to low emissions gasoline. To address California’s serious air pollution problems, the California Air Resources Board (“CARB”) initiated proceedings in the late 1980s to set regulations and standards governing the composition of low emissions, reformulated gasoline (“RFG”). The Complaint alleges that Union Oil actively participated in CARB RFG rulemaking proceedings and engaged in a pattern of bad-faith, deceptive conduct, exclusionary in nature, that enabled it to undermine competition and harm consumers. The Complaint states that Union Oil also engaged in deceptive and exclusionary conduct through its participation in two private industry groups – the Auto/Oil Air Quality Improvement Program (“Auto/Oil”) and the Western States Petroleum Association (“WSPA”). According to the Complaint, Union Oil thereby illegally monopolized, attempted to monopolize, and otherwise engaged in unfair

## Analysis

methods of competition in violation of Section 5 of the FTC Act in both the technology market for the production and supply of CARB-compliant “summer-time” gasoline, and the downstream “summer-time” gasoline product market.

Union Oil is a public corporation, organized in, and doing business under, the laws of California. Union Oil is a wholly-owned operating subsidiary of Unocal Corporation, a holding company incorporated in Delaware. Prior to 1997, Union Oil owned and operated refineries in California as a vertically-integrated producer, refiner, and marketer of petroleum products. In 1997, Union Oil sold its west coast refining, marketing, and transportation assets. Currently, Union Oil’s primary business activities involve oil and gas exploration and production.

The Complaint alleges that during the CARB “Phase 2” RFG rulemaking proceedings in 1990-1994, Union Oil made a series of materially false and misleading statements. According to the allegations in the Complaint, Union Oil willfully and intentionally:

- a. Represented to CARB and other participants that Union Oil’s emissions research results showing, *inter alia*, the relationships between certain gasoline properties and automobile emissions, were “nonproprietary,” in “the public domain,” or otherwise were available to CARB, industry members, and the general public – without disclosing that Union Oil intended to assert its proprietary interests (as manifested in pending patent claims) in the results of this research;
- b. Represented to CARB that a “predictive model” – *i.e.*, a mathematical model that predicts whether the emissions that would result from varying certain gasoline properties in a fuel are equivalent to the emissions resulting from a specified and fixed fuel formulation – would be “cost-effective” and “flexible,” without disclosing that Union

Analysis

Oil's assertion of its proprietary interests would undermine the cost-effectiveness and flexibility of such a model; and

- c. Made statements and comments to CARB and other industry participants relating to the cost-effectiveness and flexibility of the regulations that further reinforced the materially false and misleading impression that Union Oil had relinquished or would not enforce any proprietary interests in its emissions research results.

According to the Complaint, Union Oil continued to conceal its intention to obtain a competitive advantage through the enforcement of its proprietary interests relating to RFG even after Union Oil received notice that the pending patent claims were allowed and issued. The Complaint alleges that Union Oil thereby led CARB and two private industry groups – Auto/Oil and WSPA (and their respective industry members) – to believe that Union Oil did not have, or would not enforce, any proprietary interests or intellectual property rights associated with its emissions research results.

The Complaint alleges that Union Oil's conduct caused CARB to adopt Phase 2 "summer-time" RFG regulations that substantially overlapped with Union Oil's concealed pending patent claims. But for Union Oil's deception, according to the Complaint, CARB would not have adopted RFG regulations substantially incorporating Union Oil's proprietary interests; the terms on which Union Oil was later able to enforce its proprietary interests would have been substantially different; or both.

The Complaint alleges that but for Union Oil's deceptive conduct, industry participants in Auto/Oil and WSPA would have taken actions including, but not limited to, (a) advocating that CARB adopt regulations that minimized or avoided infringement of Union Oil's patent claims; (b) advocating that CARB negotiate license terms substantially different from those that Union Oil was later able to obtain; and/or (c) incorporating knowledge of Union Oil's pending patent rights in their capital investment and refinery

## Analysis

reconfiguration decisions to avoid and/or minimize potential infringement.

According to the Complaint, Union Oil did not announce the existence of its proprietary interests and patent rights relating to RFG until January 1995 – shortly before the relevant CARB Phase 2 RFG regulations were to go into effect. The Complaint alleges that, by that time, the refining industry had spent billions of dollars in capital expenditures to modify their refineries to comply with the CARB Phase 2 RFG regulations, in reliance on Union Oil’s representations that its research results were in “the public domain.” The Complaint states that once CARB and the refiners had become locked into the Phase 2 regulations, Union Oil commenced vigorous enforcement of its patent rights through litigation and licensing, and obtained four additional patents based on the same RFG research results.

Union Oil’s misrepresentations, according to the Complaint, have harmed competition and led directly to the acquisition of monopoly power for the technology to produce and supply California “summer-time” reformulated gasoline (mandated for up to eight months of the year, from approximately March through October). The Complaint alleges that Union Oil’s conduct also permitted it to undermine competition and harm consumers in the downstream product market for “summer-time” reformulated gasoline in California. The Complaint alleges that without recourse, Union Oil’s conduct would continue materially to cause or threaten to cause further substantial injury to competition and to consumers.

According to the Complaint, Union Oil’s enforcement of its RFG patents has resulted, *inter alia*, in a jury determination of a 5.75 cents per gallon royalty on gasoline produced by major California refiners comprising approximately 90 percent of the current refining capacity of CARB-compliant RFG in the California market. The Complaint alleges that Union Oil also has

Analysis

publicly announced that it will license its RFG patent portfolio, with fees ranging from 1.2 to 3.4 cents per gallon, to “non-litigating” refiners.

The Complaint alleges that Unocal’s conduct could result in an estimated annual cost of more than \$500 million to the refining industry. According to the Complaint, Union Oil’s own economic expert has testified under oath that 90 percent of any royalty would be passed through to consumers in the form of higher gasoline prices.

## **II. Terms of the Proposed Consent Order**

The Commission has provisionally entered into an Agreement with Union Oil in settlement of the Complaint. As discussed below, the provisions of the Agreement are conditioned upon the completion of certain steps in Chevron Corporation’s merger with Unocal Corporation, as contemplated by the Agreement and Plan of Merger dated as of April 4, 2005, among Unocal Corporation, ChevronTexaco Corporation, and Blue Merger Sub Inc.

In order to remedy the alleged anticompetitive effects, Union Oil has agreed to take several actions. First, it will cease and desist from any and all efforts, and will not undertake any new efforts to: (a) assert or enforce any of Union Oil’s Relevant U.S. Patents against any person; (b) recover any damages or costs for alleged infringements of any of the Relevant U.S. Patents; or (c) collect any fees, royalties or other payments, in cash or in kind, for the practice of any of the Relevant U.S. Patents, including but not limited to fees, royalties, or other payments, in cash or in kind, to be collected pursuant to any License Agreement. These obligations become effective as of the “Merger Effective Date,” which is defined as the earlier of (1) the date that the certificate of merger for the Merger is filed with the Secretary of State of Delaware or such later time as specified in such certificate of merger, or (2) the date that Chevron Corporation acquires control of Unocal Corporation, as “control” is defined by 16 C.F.R. § 801.1(b).

## Analysis

Second, the Proposed Consent Order requires that, within thirty (30) days following the Merger Effective Date, Union Oil shall file, or cause to be filed, with the United States Patent and Trademark Office, the necessary documents pursuant to 35 U.S.C. § 253, 37 C.F.R. § 1.321, and the Manual of Patent Examining Procedure to disclaim or dedicate to the public the remaining term of the Relevant U.S. Patents. The Proposed Consent Order further requires that Union Oil shall correct as necessary, and shall not withdraw or seek to nullify, any disclaimers or dedications filed pursuant to the Proposed Consent Order.

Third, the Proposed Consent Order requires that, within thirty (30) days following the Merger Effective Date, Union Oil shall move to dismiss, with prejudice, all pending legal actions relating to the alleged infringement of any Relevant U.S. Patents, including but not limited to the following actions pending in the United States District Court for the Central District of California: *Union Oil Company of California v. Atlantic Richfield Company, et al.*, Case No. CV-95-2379-CAS and *Union Oil Company of California v. Valero Energy Corporation*, Case No. CV-02-00593 SVW.

Paragraph V of the Proposed Consent Order requires Union Oil to distribute a copy of the Proposed Consent Order and the Complaint in this matter to certain interested parties, including (1) any person that Union Oil has contacted regarding possible infringement of any of the Relevant U.S. Patents, (2) any person against which Union Oil is, or was, involved in any legal action regarding possible infringement of any of the Relevant U.S. Patents, (3) any licensee or other Person from which Union Oil has collected any fees, royalties or other payments, in cash or in kind, for the practice of the Relevant U.S. Patents, and (4) any person that Union Oil has contacted with regard to the possible collection of any fees, royalties or other payments, in cash or in kind, for the practice of the Relevant U.S. Patents.

Paragraph V also requires Union Oil to distribute a copy of the Proposed Consent Order and the Complaint to Union Oil's present



Analysis

and future officers and directors having responsibility for any of its obligations under the Proposed Consent Order, and to employees and agents having managerial responsibility for any of its obligations under the Proposed Consent Order.

Paragraphs VI, VII and VIII of the Proposed Consent Order contain standard reporting, access, and notification provisions designed to allow the Commission to monitor compliance with the order. Paragraph IX provides that the Proposed Consent Order shall terminate twenty (20) years after the date it becomes final.

### **III. Opportunity for Public Comment**

The Proposed Consent Order has been placed on the public record for thirty (30) days for receipt of comments by interested persons. Comments received during this thirty-day comment period will become part of the public record. After thirty (30) days, the Commission will again review the Proposed Consent Order and the comments received and will decide whether it should withdraw from the Proposed Consent Order or make final the Agreement's Proposed Consent Order.

By accepting the Proposed Consent Order subject to final approval, the Commission anticipates that the competitive problems alleged in the Complaint will be resolved. The purpose of this analysis is to invite public comment on the Proposed Consent Order, and to aid the Commission in its determination of whether it should make final the Proposed Consent Order contained in the Agreement. This analysis is not intended to constitute an official interpretation of the Proposed Consent Order, nor is it intended to modify the terms of the Proposed Consent Order in any way.

Statement

**STATEMENT OF THE COMMISSION****Concerning****UNION OIL COMPANY OF CALIFORNIA AND  
CHEVRON/UNOCAL**

The Federal Trade Commission has voted unanimously (4-0-1, with Chairman Majoras recused) to accept two linked consent agreements that resolve both the Commission's monopolization case against Unocal Corporation's subsidiary Union Oil Company of California and any antitrust concerns arising from Chevron Corporation's pending acquisition of Unocal. The key element in the settlements, which will become effective when the acquisition is completed, is Chevron's agreement not to enforce certain Union Oil patents that potentially could have increased gasoline prices in California by over \$500 million a year (or almost six cents per gallon). This agreement provides the full relief that the Commission sought in its administrative litigation with Union Oil and also addresses the only possible objection to the Chevron/Unocal acquisition.

On April 4, 2005, Chevron agreed to acquire Unocal in a transaction valued at approximately \$18 billion. Chevron and Unocal both have extensive oil and gas operations. However, nearly all of Unocal's operations are in the so-called "upstream" segment of the business – namely, the exploration and production of crude oil and natural gas. Unocal has no refineries or gasoline stations in the United States or anywhere else in the world, and has few other "downstream" operations. As a result, virtually all of the competitive overlaps between the two firms are in unconcentrated upstream markets, and the merger thus creates no competitive risk. For example, Chevron and Unocal combined have only 2.7 percent of world crude oil production, 0.77 percent of world crude oil reserves, 11.3 percent of U.S. crude oil

Statement

production, and 11.4 percent of U.S. crude oil reserves.<sup>1</sup> *We want to emphasize that the merger will have no impact whatsoever on concentration at the retail or refinery levels.* It is clear from all we have seen that Chevron's primary motivation is to gain access to Unocal's upstream oil reserves.

The only potential competitive concern with Chevron's proposed acquisition of Unocal involved patents held by Union Oil – the same group of patents involved in the Commission's monopolization case against Union Oil. In order to explain why this is so, it is necessary first to discuss the issues in this monopolization case.

The Commission's administrative complaint against Union Oil charged that the firm had illegally acquired monopoly power in the technology market for producing certain low-emission gasoline mandated by the California Air Resources Board (CARB) for sale and use in California for up to eight months of the year. According to the complaint, Union Oil misrepresented to CARB that certain gasoline research was non-proprietary and in the public domain, while at the same time it pursued a patent that would enable it to charge substantial royalties if the research results were used by CARB in the development of regulations. The complaint further asserted that Union Oil similarly misled its fellow members of private industry groups, which were also participating in the CARB rulemaking process. As a result, if Union Oil were permitted to enforce its patent rights, companies

---

<sup>1</sup> Sources for the underlying data include the Energy Information Administration, U.S. Department of Energy, U.S. Crude Oil, Natural Gas, and Liquids Table 2003 Annual Report, Table B5, available at <<http://www.eia.doe.gov>>, the FTC Bureau of Economics Staff Study, "The Petroleum Industry: Mergers, Structural Change, and Antitrust Enforcement," August 2004, Table 5-3, available at <<http://www.ftc.gov/os/2004/08/040813/mergersinpetrolberpt.pdf>>, and the Oil and Gas Journal.

## Statement

producing this low-emission CARB gasoline would be required to pay royalties to Union Oil, the bulk of which would be passed on to California consumers in the form of higher gasoline prices. The Commission estimated that Union Oil's enforcement of these patents could potentially result in over \$500 million of additional consumer costs each year. The complaint sought an order requiring Union Oil to cease and desist from all efforts to assert these patents against those manufacturing, selling, distributing, or otherwise using motor gasoline to be sold in California. In the settlement announced today, Unocal and Chevron have agreed to all of this requested relief.

The consent orders also resolve any possible antitrust objections to the merger. Although Unocal does not engage in any refining or retailing itself, it had claimed the right to collect patent royalties from companies that did so (including Chevron). If Chevron had unconditionally inherited these patents by acquisition, it would have been in a position to obtain sensitive information and to claim royalties from its own horizontal downstream competitors. We have reason to believe that this scenario would likely have an adverse effect on competition and, in any event, would inevitably have required an extensive inquiry and possible litigation.

For example, Union Oil regularly collects detailed reports from licensees about their production of CARB gasoline and other refinery operations. If Chevron had continued these license agreements after inheriting Union Oil's patents, it would have received information not otherwise available to members of the industry. Chevron could have used this information to facilitate coordinated interaction and detect any deviations. Chevron might also have been able to use the patents to discourage maverick behavior. Our present knowledge suggests that the likely competitive harm from this potential coordination and discipline would outweigh any likely efficiency gains from the vertical integration of a merged Chevron-Unocal. Now, a further inquiry into that belief is not necessary.

Statement

The settlement of these two matters is thus a double victory for California consumers. The Commission's monopolization case against Unocal was complex and, with possible appeals, could have taken years to resolve. The stakes were high, and substantial royalties could have been paid in the meantime – with an immediate impact on consumers. If the Commission lost the case, the dollar costs to consumers ultimately would have been immense. At the same time, a challenge against the acquisition of Unocal by Chevron would itself be a complex case, with high stakes and an uncertain outcome. The settlement provides the full relief sought in the monopolization case and resolves the only competitive issue with the proposed merger. With the settlement, consumers will benefit immediately from the elimination of royalty payments on the Union Oil patents, and potential merger efficiencies could result in additional savings at the pump.

Complaint

IN THE MATTER OF

**TROPICANA PRODUCTS, INC.**CONSENT ORDER, ETC., IN REGARD TO ALLEGED VIOLATIONS OF  
SEC. 5 AND 12 OF THE FEDERAL TRADE COMMISSION ACT*Docket C-4145; File No. 0423154*  
*Complaint, August 19, 2005--Decision, August 19, 2005*

This consent order, among other things, requires Respondent Tropicana Products, Inc., to possess competent and reliable scientific evidence before representing that (1) drinking three glasses of “Healthy Heart” orange juice a day for one month will raise good cholesterol by twenty-one percent and improve the ratio of good to bad cholesterol by sixteen percent; (2) drinking twenty ounces of “Healthy Heart” a day for one month will increase blood folate levels by forty-five percent and decrease homocysteine levels by eleven percent; and (3) drinking two glasses of orange juice a day for eight weeks will lower blood pressure an average of ten points. The consent order also requires the respondent to possess competent and reliable scientific evidence before making certain representations that any food will affect any biological marker or health-related endpoint by any specific amount; blood cholesterol levels, blood folate levels, blood homocysteine levels, or blood pressure; or the risk of developing heart disease, stroke, or cancer. In addition, the consent order prohibits the respondent from misrepresenting the existence, contents, validity, results, conclusions, or interpretations of any test or study.

*Participants*

For the Commission: *Karen M. Muoio, Michelle K. Rusk, Mary K. Engle and Margaret A. Patterson.*

For the Respondent: *Steven B. Steinborn, Hogan & Hartson and Anne V. Maher, Kleinfeld Kaplan & Becker*

**COMPLAINT**

The Federal Trade Commission, having reason to believe that Tropicana Products, Inc., a corporation, (“respondent”), has violated the provisions of the Federal Trade Commission Act, and it appearing to the Commission that this proceeding is in the public interest, alleges:

Complaint

1. Respondent is a Delaware corporation with its principal office or place of business at 555 Monroe Street, Chicago, Illinois 60661.
2. Respondent has advertised, labeled, offered for sale, sold, and distributed food products to the public, including orange juice sold under the “Tropicana” name.
3. Orange juice is a “food” within the meaning of Sections 12 and 15 of the Federal Trade Commission Act.
4. The acts and practices of respondent alleged in this complaint have been in or affecting commerce, as “commerce” is defined in Section 4 of the Federal Trade Commission Act.
5. Respondent has disseminated or has caused to be disseminated national advertising and promotional materials for its orange juice, including but not limited to the television and print advertisements attached as Exhibits A-C. The advertisements contain the following statements and depictions:
  - A. VISUAL: Carton of Tropicana orange juice with blood pressure gauge attached.  
  
TEXT: Lowering your blood pressure never tasted so good.  
  
VISUAL: Two small glasses of orange juice.  
  
TEXT: A new clinical study shows enjoying two glasses of Tropicana Pure Premium every day can lower your blood pressure an average of ten points.  
  
FINE PRINT: Two 8-oz. glasses daily over 6 weeks resulted in an average reduction of 10 pts. Consult your physician. Results may vary.

## Complaint

Full page, color print advertisement, *New York Times*, March 20, 2002 (Exhibit A)

- B. ON SCREEN: Older man sings and dances around doctor's examining room while drinking Tropicana orange juice. Camera shots alternate between man and various pieces of medical equipment, including blood pressure monitor.
- MUSIC: Everybody's smiling. Sunshine day.
- VOICEOVER: A new study finds that 2 glasses of great tasting Tropicana Pure Premium every day can significantly lower your blood pressure.
- SUPERSCRIPT: Two 8 oz glasses daily over 6 weeks resulted in an average of 10 pt. reduction. Results may vary. Consult your physician on how a healthy diet can help lower your blood pressure.
- ON SCREEN: Carton of Tropicana orange juice.
- ON SCREEN: Arm on dial of blood pressure gauge lowers from 140 points to below 128 points.
- ON SCREEN: Man dances out of doctor's office.

## Television advertisement (Exhibit B)

- C. TEXT: Over the past few years, researchers have tied America's favorite breakfast beverage to a bonanza of health perks. Besides being fat-, sodium- and cholesterol-free, orange juice has been shown to improve heart health. And there's growing evidence it may have other benefits, including helping to stave off cancer. . . .



Complaint

TEXT: Most research on o.j. links a juice habit to healthier hearts. For instance, researchers recently showed that drinking three glasses of Tropicana orange juice a day for four weeks raised HDL, the “good” cholesterol, by 21 percent and improved the ratio of good cholesterol to bad (LDL) cholesterol by 16 percent. . . .

TEXT: Hearts also benefit from folic acid (folate), which lowers levels of a harmful substance called homocysteine. High amounts of this amino acid are associated with increased risk of cardiovascular problems, but drinking orange juice may counter its ill effects. A study from the Medical College of Wisconsin found that drinking 20 ounces of orange juice a day increased blood levels of folate by almost 45 percent and decreased homocysteine by 11 percent. . . .

TEXT: Orange juice also appears to lower blood pressure and stroke risk, which appears to be at least partly due to its high potassium levels. When researchers at the Cleveland Clinic Heart Center asked 24 people to drink two glasses of Tropicana each day for eight weeks, study participants experienced a significant lowering of blood pressure: Systolic blood pressure (the upper number) dropped an average of 10 points.

VISUAL: Orange with wrist heart monitor strapped around it and straw sticking out of it.

Multi-page print advertisement, *Newsweek*,  
February 9, 2004 (Exhibit C)

6. Through the means described in Paragraph 5, respondent has represented, expressly or by implication, that

## Complaint

- A. Drinking three cups of Tropicana orange juice a day for four weeks will raise HDL cholesterol by 21 percent and improve the ratio of HDL to LDL cholesterol by 16 percent;
  - B. Drinking 20 ounces of Tropicana orange juice a day will increase blood levels of folate by almost 45 percent and decrease homocysteine by 11 percent; and
  - C. Drinking two cups of Tropicana orange juice a day for six or eight weeks will lower systolic blood pressure an average of 10 points.
7. Through the means described in Paragraph 5, respondent has represented, expressly or by implication, that it possessed and relied upon a reasonable basis that substantiated the representations set forth in Paragraph 6, at the time the representations were made.
8. In truth and in fact, respondent did not possess and rely upon a reasonable basis that substantiated the representations set forth in Paragraph 6, at the time the representations were made. Therefore, the representation set forth in Paragraph 7 was, and is, false or misleading.
9. Through the means described in Paragraph 5, respondent has represented, expressly or by implication, that:
- A. A clinical study shows that drinking Tropicana orange juice will reduce the risk of heart disease by substantially raising HDL (good) cholesterol levels and substantially improving the ratio of HDL cholesterol to LDL (bad) cholesterol, including specifically that drinking three cups of Tropicana orange juice a day for four weeks will raise HDL by 21 percent and improve the ratio of HDL to LDL cholesterol by 16 percent;

Complaint

- B. A clinical study shows that drinking Tropicana orange juice will reduce the risk of heart disease by substantially increasing the levels of folate in the blood and substantially decreasing the levels of homocysteine in the blood, including specifically that drinking 20 ounces of Tropicana orange juice a day will increase blood levels of folate by almost 45 percent and decrease homocysteine by 11 percent; and
  - C. A clinical study shows that drinking Tropicana orange juice will reduce the risk of stroke by substantially lowering blood pressure, including specifically that drinking two cups of Tropicana orange juice a day for six or eight weeks will lower systolic blood pressure an average of 10 points.
10. In truth and in fact:
- A. A clinical study does not show that drinking Tropicana orange juice will reduce the risk of heart disease by substantially raising HDL (good) cholesterol levels and substantially improving the ratio of HDL cholesterol to LDL (bad) cholesterol, including specifically that drinking three cups of Tropicana orange juice a day for four weeks will raise HDL by 21 percent and improve the ratio of HDL to LDL cholesterol by 16 percent;
  - B. A clinical study does not show that drinking Tropicana orange juice will reduce the risk of heart disease by substantially increasing the levels of folate in the blood and substantially decreasing the levels of homocysteine in the blood, including specifically that drinking 20 ounces of Tropicana orange juice a day will increase blood levels of folate by almost 45 percent and decrease homocysteine by 11 percent; and
  - C. A clinical study does not show that drinking Tropicana orange juice will reduce the risk of stroke by substantially lowering blood pressure, including specifically that drinking

## Complaint

two cups of Tropicana orange juice a day for six or eight weeks will lower systolic blood pressure an average of 10 points.

Therefore, the making of the representations set forth in Paragraph 9 was, and is, false or misleading.

11. The acts and practices of respondent as alleged in this complaint constitute unfair or deceptive acts or practices, and the making of false advertisements, in or affecting commerce in violation of Sections 5(a) and 12 of the Federal Trade Commission Act.

IN WITNESS WHEREOF, the Federal Trade Commission has caused its complaint to be signed by its Secretary and its official seal to be hereto affixed at Washington, D.C. this 19<sup>th</sup> day of August, 2005.

Decision and Order

## **DECISION AND ORDER**

The Federal Trade Commission having initiated an investigation of certain acts and practices of the respondent named in the caption hereof, and the respondent having been furnished thereafter with a copy of a draft of complaint which the Bureau of Consumer Protection proposed to present to the Commission for its consideration and which, if issued by the Commission, would charge respondent with violation of the Federal Trade Commission Act; and

The respondent, its attorneys, and counsel for Federal Trade Commission having thereafter executed an agreement containing a consent order, an admission by the respondent of all the jurisdictional facts set forth in the aforesaid draft of complaint, a statement that the signing of said agreement is for settlement purposes only and does not constitute an admission by respondent that the law has been violated as alleged in such complaint, or that the facts as alleged in such complaint, other than jurisdictional facts, are true and waivers and other provisions as required by the Commission's Rules; and

The Commission having thereafter considered the matter and having determined that it had reason to believe that the respondent has violated the said Act, and that complaint should issue stating its charges in that respect, and having thereupon accepted the executed consent agreement and placed such agreement on the public record for a period of thirty (30) days, and having duly considered the comments filed thereafter by interested persons pursuant to § 2.34 of its Rules, now in further conformity with the procedure prescribed in § 2.34 of its Rules, the Commission hereby issues its complaint, makes the following jurisdictional findings and enters the following order:

1. Proposed respondent is a Delaware corporation with its principal office or place of business at 555 Monroe Street, Chicago, Illinois 60661.

## Decision and Order

2. The Federal Trade Commission has jurisdiction of the subject matter of this proceeding and of the respondents, and the proceeding is in the public interest.

**ORDER****DEFINITIONS**

For purposes of this order, the following definitions shall apply:

1. Unless otherwise specified, “respondent” shall mean Tropicana Products, Inc., its successors and assigns, and its officers, agents, representatives, and employees.
2. “Commerce” shall mean as defined in Section 4 of the Federal Trade Commission Act, 15 U.S.C. § 44.
3. “Competent and reliable scientific evidence” shall mean tests, analyses, research, studies, or other evidence based on the expertise of professionals in the relevant area, that has been conducted and evaluated in an objective manner by persons qualified to do so, using procedures generally accepted in the profession to yield accurate and reliable results.
4. “Endorsement” shall mean as defined in 16 C.F.R. § 255.0.
5. “Food” shall mean as defined in Section 15 of the Federal Trade Commission Act, 15 U.S.C. § 55.

**I.**

IT IS ORDERED that respondent, directly or through any corporation, subsidiary, division, or other device, in connection with the labeling, advertising, promotion, offering for sale, sale, or distribution of orange juice, in or affecting commerce, shall not make any representation, in any manner, expressly or by

Decision and Order

implication, including through the use of endorsements or the product name that:

- A. Drinking three cups of Tropicana orange juice a day for four weeks will raise HDL cholesterol by 21 percent and improve the ratio of HDL to LDL cholesterol by 16 percent;
- B. Drinking 20 ounces of Tropicana orange juice a day will increase blood levels of folate by almost 45 percent and decrease homocysteine by 11 percent; or
- C. Drinking two cups of Tropicana orange juice a day for six or eight weeks will lower systolic blood pressure an average of 10 points;

unless, at the time it is made, respondent possesses and relies upon competent and reliable scientific evidence that substantiates the representation.

**II.**

IT IS FURTHER ORDERED that respondent, directly or through any corporation, subsidiary, division, or other device, in connection with the labeling, advertising, promotion, offering for sale, sale, or distribution of any food, in or affecting commerce, shall not make any representation, in any manner, expressly or by implication, including through the use of endorsements or the product name, that drinking such food will affect any biological marker or health-related endpoint by any specific amount; will affect blood cholesterol levels, blood folate levels, blood homocysteine levels, or blood pressure; or will otherwise affect the risk of developing heart disease, stroke, or cancer; unless, at the time it is made, respondent possesses and relies upon competent and reliable scientific evidence that substantiates the representation. Provided, however, that a statement that such product contains a particular nutrient shall not, by itself, be considered a claim for purposes of this Part.

Decision and Order

**III.**

IT IS FURTHER ORDERED that respondent, directly or through any corporation, subsidiary, division, or other device, in connection with the labeling, advertising, promotion, offering for sale, sale, or distribution of any food, in or affecting commerce, shall not misrepresent, in any manner, expressly or by implication, including through the use of endorsements or the product name, the existence, contents, validity, results, conclusions, or interpretations of any test or study.

**IV.**

Nothing in this order shall prohibit respondent from making any representation for any product that is specifically permitted in labeling for such product by regulations promulgated by the Food and Drug Administration pursuant to the Nutrition Labeling and Education Act of 1990.

**V.**

IT IS FURTHER ORDERED that respondent shall, for five (5) years after the last date of dissemination of any representation covered by this order, maintain and upon request make available to the Federal Trade Commission for inspection and copying:

- A. All advertisements and promotional materials containing the representation including videotape recordings of all such broadcast advertisements;
- B. All materials that were relied upon in disseminating the representation; and
- C. All tests, reports, studies, surveys, demonstrations or other evidence in their possession or control that contradict, qualify, or call into question the representation, or the basis relied upon for the representation, including complaints and



Decision and Order

other communications with consumers or with governmental or consumer protection organizations.

**VI.**

IT IS FURTHER ORDERED that respondent shall deliver a copy of this order to all current and future principals, officers, directors, and managers, and to all current and future employees, agents, and representatives having managerial responsibilities with respect to the subject matter of this order, and shall secure from each such person a signed and dated statement acknowledging receipt of the order. Respondent shall deliver this order to current personnel within thirty (30) days after the date of service of this order, and to future personnel within thirty (30) days after the person assumes such position or responsibilities.

**VII.**

IT IS FURTHER ORDERED that respondent shall notify the Commission at least thirty (30) days prior to any proposed change in its corporate structure that may affect compliance obligations arising under this order, including but not limited to a dissolution, assignment, sale, merger, or other action that would result in the emergence of a successor corporation; the creation or dissolution of a subsidiary, parent, or affiliate that engages in any acts or practices subject to this order; the proposed filing of a bankruptcy petition; or a change in the corporate name or address. *Provided, however,* that, with respect to any proposed change in the corporation about which respondent learn less than thirty (30) days prior to the date such action is to take place, respondent shall notify the Commission as soon as is practicable after obtaining such knowledge. All notices required by this Part shall be sent by certified mail to the Associate Director, Division of Enforcement, Bureau of Consumer Protection, Federal Trade Commission, 600 Pennsylvania Avenue, NW, Washington, D.C. 20580.

Decision and Order

**VIII.**

IT IS FURTHER ORDERED that respondent shall, within sixty (60) days from the date of service of this order, and at such other times as the Federal Trade Commission may require, file with the Commission a report, in writing, setting forth in detail the manner and form in which it has complied with this order.

**IX.**

This order will terminate twenty (20) years from the date of its issuance, or twenty (20) years from the most recent date that the United States or the Federal Trade Commission files a complaint (with or without an accompanying consent decree) in federal court alleging any violation of the order, whichever comes later; *provided, however*, that the filing of such a complaint will not affect the duration of:

- A. Any Part in this order that terminates in less than twenty (20) years;
- B. This order's application to any respondent that is not named as a defendant in such complaint; and
- C. This order if such complaint is filed after the order has terminated pursuant to this Part.

*Provided further*, that if such complaint is dismissed or a federal court rules that the respondent did not violate any provision of the order, and the dismissal or ruling is either not appealed or upheld on appeal, then the order will terminate according to this Part as though the complaint had never been filed, except that the order will not terminate between the date such complaint is filed and the later of the deadline for appealing such dismissal or ruling and the date such dismissal or ruling is upheld on appeal.

Analysis

**Analysis of Proposed Consent Order to Aid Public Comment**

The Federal Trade Commission has accepted, subject to final approval, an agreement containing a consent order from Tropicana Products, Inc.

The proposed consent order has been placed on the public record for thirty (30) days for receipt of comments by interested persons. Comments received during this period will become part of the public record. After thirty (30) days, the Commission will again review the agreement and the comments received, and will decide whether it should withdraw from the agreement or make final the agreement's proposed order.

This matter involves the advertising and promotion of Tropicana's "Healthy Heart" orange juice. According to the FTC complaint, Tropicana represented that (1) drinking three glasses of "Healthy Heart" a day for one month will raise good cholesterol by twenty-one percent and improve the ratio of good to bad cholesterol by sixteen percent; (2) drinking twenty ounces of "Healthy Heart" a day for one month will increase blood folate levels by forty-five percent and decrease homocysteine levels by eleven percent; and (3) drinking two glasses of orange juice a day for eight weeks will lower blood pressure an average of ten points. The complaint alleges that these claims are unsubstantiated. Tropicana also represented that the above three claims were clinically proven. The complaint alleges that this claim is false. Although Tropicana refers to three studies in its advertising, the studies are limited and do not support the claims made.

The proposed consent order contains provisions designed to prevent Tropicana from engaging in similar acts and practices in the future.

Part I of the order requires Tropicana to possess competent and reliable scientific evidence before making the three challenged efficacy claims.

## Analysis

Part II requires Tropicana to possess competent and reliable scientific evidence before making certain representations that any food will affect: any biological marker or health-related endpoint by any specific amount; blood cholesterol levels, blood folate levels, blood homocysteine levels, or blood pressure; or the risk of developing heart disease, stroke, or cancer. Furthermore, Part II provides that a mere statement that a product contains a particular nutrient will not, by itself, be considered to be a health benefit claim covered by Part II.

Part III of the proposed order prohibits Tropicana from misrepresenting the existence, contents, validity, results, conclusions, or interpretations of any test or study.

Part IV permits any representation for any product that is permitted in labeling for such product pursuant to regulations promulgated by FDA pursuant to the Nutrition Labeling and Education Act of 1990.

Parts V through VIII of the order require Tropicana to keep copies of relevant advertisements and materials substantiating claims made in the advertisements; to provide copies of the order to certain of its current and future personnel for three years; to notify the Commission of changes in corporate structure; and to file compliance reports with the Commission. Part IX provides that the order will terminate after twenty (20) years under certain circumstances.

The purpose of this analysis is to facilitate public comment on the proposed order, and it is not intended to constitute an official interpretation of the agreement and proposed order or to modify in any way their terms.

Complaint

IN THE MATTER OF

**CYTODYNE, LLC, EVERGOOD PRODUCTS CORP., AND  
MELVIN L. RICH**

CONSENT ORDER, ETC., IN REGARD TO ALLEGED VIOLATIONS OF  
SEC. 5 AND 12 OF THE FEDERAL TRADE COMMISSION ACT

*Docket C-4146; File No. 0323144  
Complaint, August 23, 2005--Decision, August 23, 2005*

This consent order, among other things, prohibits Respondents Cytodyne, LLC, Evergood Products Corp., and Melvin Rich, from representing that Xenadrine EFX – a dietary supplement marketed for weight loss – or any other product containing green tea extract, bitter orange, or caffeine causes rapid and substantial weight loss or fat loss, and from representing that any weight loss product causes rapid or substantial weight loss without the need to diet or increase exercise. The consent order also prohibits the respondents from representing that any weight loss product, dietary supplement, food, drug, or device causes weight or fat loss, causes permanent or long-term weight loss – or enables users to lose weight or fat without the need to diet or increase exercise – unless the claim is true and respondents possess competent and reliable scientific evidence that substantiates the claim. In addition, the consent order prohibits the respondents from making any other claims about the health benefits, performance, efficacy, safety, or side effects of any such product unless the claim is true and respondents possess competent and reliable scientific evidence that substantiates the claim. The consent order also prohibits the respondents from misrepresenting the existence, contents, validity, results, conclusions, or interpretations of any test or study – in connection with the marketing or sale of any weight loss product, dietary supplement, food, drug, or device – and from misrepresenting that the experience described in any user testimonial for any weight loss product, dietary supplement, food, drug, or device represents the actual experience of the endorser as a result of using the product under the circumstances depicted in the endorsement. In addition, the consent order requires the respondents to pay \$100,000 to the Commission.

*Participants*

For the Commission: *Rona Kelner, Peter B. Miller, Michael F. Ostheimer, Heather Hipsley, Mary K. Engle, and Susan P. Braman.*

For the Respondent: *Jay Geller*

Complaint

**COMPLAINT**

The Federal Trade Commission, having reason to believe that Cytodyne, LLC, a limited liability company, Evergood Products Corp., a corporation, and Melvin Rich, individually and as a manager of Cytodyne, LLC and an officer of Evergood Products Corp. (“respondents”), have violated the provisions of the Federal Trade Commission Act, and it appearing to the Commission that this proceeding is in the public interest, alleges:

1. Respondent Cytodyne, LLC is a New York limited liability company with its principal office or place of business at 200 Adams Boulevard, Farmingdale, NY 11735. Its previous corporate name was Everrich, LLC.
2. Respondent Evergood Products Corp. (“Evergood”) is a Delaware corporation with its principal office or place of business at 200 Adams Boulevard, Farmingdale, NY 11735. Evergood is a holding company and has an eighty-seven and one-half percent ownership interest in Cytodyne, LLC. Evergood has controlled the acts and practices of Cytodyne, LLC with respect to the advertising, marketing, distribution, offering for sale, and sale of Xenadrine EFX.
3. Respondent Melvin L. Rich is a manager of Cytodyne, LLC. He is also President of Evergood and has a forty-five percent ownership interest in the company. Individually or in concert with others, he formulates, directs, or controls the policies, acts, or practices of Cytodyne, LLC and Evergood, including the acts or practices alleged in this complaint. His principal office or place of business is the same as that of Cytodyne, LLC and Evergood.
4. Since May 2003, respondents have advertised, labeled, offered for sale, sold, and distributed the dietary supplement Xenadrine EFX. Xenadrine EFX is a tablet containing, among other ingredients, green tea extract, yerba mate, and bitter orange. A 120-tablet bottle of Xenadrine EFX – a one-month supply – retails

Complaint

for approximately \$40. From June 2003 through mid-August 2004, sales of Xenadrine EFX exceeded \$61 million.

5. Xenadrine EFX is a “food” or “drug” within the meaning of Sections 12 and 15 of the Federal Trade Commission Act.

6. The acts and practices of respondents alleged in this complaint have been in or affecting commerce, as “commerce” is defined in Section 4 of the Federal Trade Commission Act.

7. Respondents have disseminated or have caused to be disseminated advertisements for Xenadrine EFX, including but not limited to the attached Exhibits A through F. These advertisements contain the following statements and depictions:

- a. *Misty Lee Lost 25 Pounds Faster And Easier Than She Ever Dreamed Possible With Xenadrine-EFX!*

*John Murphy lost 37 Pounds in just weeks!*

*Kelly Kinney lost 101 Pounds!*

*Holli Whitacre lost over 100 Pounds!*

**All of these people just discovered the most incredible weight loss product in the world...and it shows!**

There’s safety in numbers. That’s why it’s nice to know that there are millions of people around the world happily counting the pounds they’ve lost with revolutionary new Xenadrine-EFX.

What makes us different than all the rest? Xenadrine-EFX really works! It’s been clinically proven to help you burn fat safely and effectively, without ephedrine. Our incredibly advanced thermogenic formula literally “revs up” your body’s metabolism for rapid reductions in body-fat and an incredible boost to your energy levels.

## Complaint

Amazingly, Xenadrine-EFX's unique formula of advanced thermogenic compounds actually triggers unprecedented results without the use of ephedrine. In fact, it's the only product of its kind proven *more effective* than ephedrine-based fat burners in head-to-head clinical testing. Best of all, you'll start to see and feel the difference almost overnight and even without strict dieting or exercise! It's about time you discovered the most incredible weight loss product in the world. Clinically proven Xenadrine-EFX. The Guaranteed Easiest and Fastest Way to Take Off the Weight!

## Exhibit A (two-page magazine advertisement)

- b. **Video:** Claudette Garza with a photograph labeled "*Before* Claudette Garza lost **22 Pounds!**"
- Announcer 1:** "Xenadrine EFX, the world's number one diet supplement presents swimsuit season."
- Video:** Joey Anderson with a photograph labeled "*Before* Joey Anderson lost **55 Pounds!**"
- Announcer 2:** "Slip into something sleek and sexy, and start strutting your stuff."
- Video:** Hazel Nelson with a photograph labeled "*Before* Hazel Nelson lost **25 Pounds!**"
- Announcer 1:** "Xenadrine EFX can help make it happen, fast and easy."
- Video:** Dan Tedtman with a photograph labeled "*Before* Dan Tedtman lost **35 pounds!**"
- Announcer 2:** "These real people are living proof of Xenadrine EFX's unsurpassed thermogenic power."
- Video:** Alexis Graham with a photograph labeled "*Before* Alexis Graham lost **113 pounds!**"
- Announcer 2:** "Increase your metabolism and get dramatic results without ephedra."
- Video:** Bottle of Xenadrine EFX with "CLINICALLY TESTED" on its label and



Complaint

superscript “**FAST! EASY! EPHEDRA-FREE!**”

**Announcer 1:** “So come on, start turning some heads with Xenadrine EFX. Number one in the world because it really works.”

**Video:** Robert Hale with a photograph labeled “*Before* Robert Hale lost **85 pounds!**”

Exhibit B (thirty-second television advertisement)

c. **The Shape Of Things To Come  
...With Xenadrine-EFX.**

**Melissa lost 45 Pounds! Patrick lost 64 Pounds! Kelly Lost 110 Pounds! Jennifer Lost 52 Pounds!**

**Melissa, Patrick, Kelly and Jennifer are happier than ever before –because they all lost incredible amounts of weight, and kept it off, with Xenadrine-EFX.**

“If it wasn’t for Xenadrine-EFX, I wouldn’t have lost my weight as quickly and as easily as I did.” says Melissa. And Patrick agrees. “I’ve used plenty of products in the past to help with weight loss and improve my energy levels, and Xenadrine-EFX has far surpassed anything I’ve ever used. I’m a new person thanks to Xenadrine-EFX.”

These are just a few of the thousands of people who have achieved real weight loss success with Xenadrine-EFX. Its thermogenic, ephedra-free formula increases metabolism and reduces calories which helped them achieve significant decreases in body fat levels. In fact, the Xenadrine-EFX formula was clinically tested against two leading ephedra-based thermogenic supplements and outperformed them both for the boosting of metabolism and resulting caloric expenditure.

...

**Xenadrine-EFX**

***Real People. Real Science. Real Success.***

Complaint

Exhibit C (magazine advertisement)

d. **Losing Weight  
Was The Best Thing  
I Ever Did For Myself!**

**Jennifer Lost An Incredible 52 Pounds  
And Kept It Off With Xenadrine-EFX!**

“One day, standing in front of my open closet, I started to cry. None of my clothes fit anymore.” That’s when Jennifer made up her mind to do something about it. She started using Xenadrine-EFX, lost 52 pounds, and has kept off the weight.

“Sure, I’d tried other diets, but with Xenadrine-EFX, it was like the pounds just started disappearing,” she says. “And it didn’t make me feel jittery like the stuff I’d used in the past.”

What makes Xenadrine-EFX so different from other diet supplements is the thermogenic, ephedra-free formula that increases your metabolism and helps control your appetite, which helped Jennifer achieve significant decreases in body fat levels. In fact, the Xenadrine-EFX formula was clinically tested against two leading ephedra-based thermogenic supplements and outperformed them both in boosting metabolism and resulting caloric expenditures.

. . .

**Xenadrine-EFX*****Real People.******Real Science.******Real Success.***

Exhibit D (magazine advertisement)

e. **“I lost 100 pounds and I owe it all to Xenadrine-EFX.  
If I can do it, you can too!”**

– Holli Whitacre

Complaint

“I look in the mirror and I still can’t believe that it’s me!” Holli says today. “I’m 100 pounds lighter and I feel 100% healthier! I love what Xenadrine-EFX has done for me.”

Xenadrine-EFX worked for Holli and it will work for you. This amazing weight loss technology attacks body fat by increasing your metabolism better than any other product on the market today. Its unique formula combines a new generation of advanced thermogenic components that work together to stimulate significant increases to your metabolism and subsequently burn calories. Simply stated, Xenadrine-EFX helps you to burn fat more quickly.

And here's more good news. Xenadrine-EFX doesn't contain ephedra. In fact, it is the only thermogenic diet product that has been proven in head to head clinical studies to be more effective than ephedra-based fat burners. Scientifically designed to burn fat and maintain muscle, this revolutionary formula has quickly become the #1 diet supplement in America.

Xenadrine-EFX is the fastest and easiest way to dramatic and long term weight loss. Put Xenadrine-EFX to work for you and discover the unprecedented fat burning power of the next generation in weight-loss technology!

*Xenadrine . . . The #1 Diet Supplement Worldwide . . .  
because it works!*

Exhibit E (magazine advertisement translated from the original Spanish to English)

- f. “It was marvelous **to lose 20 lbs.** It’s even better **not to gain them back** with Xenadrine-EFX.”

Over a year ago, Claudette lost more than 20 pounds thanks to Xenadrine-EFX, and she feels happier than ever. As she, herself, says: “In a few weeks, I went down four clothing sizes. It’s a fact: Xenadrine-EFX changed my life forever!”

## Complaint

But what really makes Claudette's story so incredible is that she has managed to keep the weight off for more than a year... with the help of Xenadrine-EFX, a sensible diet, and regular exercise.

What makes Xenadrine-EFX so effective is its exclusive ephedra-free thermogenic formula, which helps to speed up your metabolism and control your appetite. In fact, the Xenadrine-EFX formula has been clinically proven in comparison with two thermogenic ephedra-based supplements, and in both cases, it had better results in stimulating the metabolism and burning calories.

Xenadrine-EFX: The most popular diet supplement worldwide, because it works!

**Xenadrine-EFX**

*Real People. Real Science. Real Success.*

Exhibit F (magazine advertisement translated from the original Spanish to English)

8. Through the means described in Paragraph 7, respondents have represented, expressly or by implication, that:
  - a. Xenadrine EFX causes rapid and substantial weight loss;
  - b. Xenadrine EFX causes rapid and substantial fat loss;
  - c. Xenadrine EFX causes rapid and substantial weight loss without the need to reduce caloric intake or increase physical activity; and
  - d. Xenadrine EFX causes permanent or long-term weight loss.
  
9. In truth and in fact,

Complaint

- a. Xenadrine EFX does not cause rapid and substantial weight loss;
- b. Xenadrine EFX does not cause rapid and substantial fat loss;
- c. Xenadrine EFX does not cause rapid and substantial weight loss without the need to reduce caloric intake or increase physical activity; and
- d. Xenadrine EFX does not cause permanent or long-term weight loss.

Therefore, the representations set forth in Paragraph 8 were, and are, false or misleading.

10. Through the means described in Paragraph 7, respondents have represented, expressly or by implication, that they possessed and relied upon a reasonable basis that substantiated the representations set forth in Paragraph 8, at the time the representations were made.

11. In truth and in fact, respondents did not possess and rely upon a reasonable basis that substantiated the representations set forth in Paragraph 8, at the time the representations were made. Therefore, the representation set forth in Paragraph 10 was, and is, false or misleading.

12. Through the means described in Paragraph 7, respondents have represented, expressly or by implication, that:

- a. Xenadrine EFX is clinically proven to cause rapid and substantial weight loss; and
- b. Xenadrine EFX is clinically proven to be more effective than leading ephedrine-based diet products.

13. In truth and in fact,

## Complaint

- a. Xenadrine EFX is not clinically proven to cause rapid and substantial weight loss; and
- b. Xenadrine EFX is not clinically proven to be more effective than leading ephedrine-based diet products.

Therefore, the representations set forth in Paragraph 12 were, and are, false or misleading.

14. Through the means described in Paragraph 7, respondents have represented, expressly or by implication, that persons who appeared in Xenadrine EFX advertisements achieved the weight loss reported in those ads solely through the use of Xenadrine EFX.

15. In truth and in fact, persons who appeared in Xenadrine EFX advertisements did not achieve the weight loss reported in those ads solely through the use of Xenadrine EFX. Persons who appeared in the Xenadrine EFX advertisements engaged in rigorous diet and/or exercise programs in order to lose weight, and some were provided with a personal trainer. Therefore, the representation set forth in Paragraph 14 was, and is, false or misleading.

16. Through the means described in Paragraph 7, respondents have presented testimonials for Xenadrine EFX by consumer endorsers who purportedly lost weight in the ordinary course of using the product. Respondents have failed to disclose that the endorsers were paid from \$1,000 to \$20,000 in connection with their endorsing Xenadrine EFX. This fact would be material to consumers in their purchase or use decisions regarding Xenadrine EFX. The failure to disclose this fact, in light of the representation made, was, and is, a deceptive practice.

17. The acts and practices of respondents as alleged in this complaint constitute unfair or deceptive acts or practices, and the making of false advertisements, in or affecting commerce in

Complaint

violation of Sections 5(a) and 12 of the Federal Trade  
Commission Act.

IN WITNESS WHEREOF, the Federal Trade Commission has  
caused its complaint to be signed by its Secretary and its official  
seal to be hereto affixed at Washington, D.C. this 23<sup>rd</sup> day of  
August, 2005.

Decision and Order

**DECISION AND ORDER**

The Federal Trade Commission having initiated an investigation of certain acts and practices of the respondents named in the caption hereof, and the respondents having been furnished thereafter with a copy of a draft complaint which the Bureau of Consumer Protection proposed to present to the Commission for its consideration and which, if issued by the Commission, would charge the respondents with violation of the Federal Trade Commission Act; and

The respondents, their attorneys, and counsel for the Commission having thereafter executed an agreement containing a consent order, an admission by the respondents of all the jurisdictional facts set forth in the aforesaid draft complaint, a statement that the signing of the agreement is for settlement purposes only and does not constitute an admission by the respondents that the law has been violated as alleged in such complaint, or that the facts as alleged in such complaint, other than jurisdictional facts, are true, and waivers and other provisions as required by the Commission's Rules; and

The Commission having thereafter considered the matter and having determined that it had reason to believe that the respondents have violated the Act, and that complaint should issue stating its charges in that respect, and having thereupon accepted the executed consent agreement and placed such agreement on the public record for a period of thirty (30) days, now in further conformity with the procedure prescribed in § 2.34 of its Rules, the Commission hereby issues its complaint, makes the following jurisdictional findings, and enters the following order:

1. Respondent Cytodyne, LLC is a New York limited liability company with its principal office or place of business at 200 Adams Boulevard, Farmingdale, NY 11735.



Decision and Order

Respondent Evergood Products Corp. (“Evergood”) is a Delaware corporation with its principal office or place of business at 200 Adams Boulevard, Farmingdale, NY 11735.

Respondent Melvin L. Rich (“Melvin Rich”) is a manager of respondent Cytodyne, LLC and an officer and director of respondent Evergood. Individually or in concert with others, he formulates, directs, or controls the policies, acts, or practices of Cytodyne, LLC and Evergood, including the acts or practices alleged in this complaint. His principal office or place of business is the same as that of Cytodyne, LLC and Evergood.

2. The Federal Trade Commission has jurisdiction of the subject matter of this proceeding and of the respondents, and the proceeding is in the public interest.

**ORDER**

**DEFINITIONS**

For purposes of this order, the following definitions shall apply:

1. Unless otherwise specified, “respondents” shall mean Cytodyne, LLC, a limited liability company, Evergood Products Corp., a corporation, their successors and assigns, and their officers, members, and managers, and Melvin L. Rich, and each of the above’s agents, representatives, and employees.
2. “Competent and reliable scientific evidence” shall mean tests, analyses, research, studies, or other evidence based on the expertise of professionals in the relevant area, that has been conducted and evaluated in an objective manner by persons qualified to do so, using procedures generally accepted in the profession to yield accurate and reliable results.
3. “Xenadrine EFX” shall mean the Xenadrine EFX dietary supplement.

## Decision and Order

4. “Substantially similar product” shall mean any product containing one or more of the following ingredients: caffeine, citrus aurantium (bitter orange), or green tea extract.
5. “Weight loss product” shall mean any product, program, or service designed, used, or purported to produce weight loss, reduction or elimination of fat, slimming, or caloric deficit in a user of the product, program, or service.
6. “Food,” “drug,” and “device” shall mean as “food,” “drug,” and “device” are defined in Section 15 of the Federal Trade Commission Act, 15 U.S.C. § 55.
7. “Covered product” shall mean any weight loss product, dietary supplement, food, drug, or device.
8. “Commerce” shall mean as defined in Section 4 of the Federal Trade Commission Act, 15 U.S.C. § 44.
9. “Endorsement” shall mean as defined in 16 C.F.R. § 255.0(b).
10. “Clear(ly) and prominent(ly)” shall mean as follows:
  - a. In an advertisement communicated through an electronic medium (such as television, video, radio, and interactive media such as the Internet, online services and software), the disclosure shall be presented simultaneously in both the audio and visual portions of the advertisement. *Provided, however,* that in any advertisement presented solely through visual or audio means, the disclosure may be made through the same means in which the ad is presented. The audio disclosure shall be delivered in a volume and cadence sufficient for an ordinary consumer to hear and comprehend it. The visual disclosure shall be of a size and shade, with a degree of contrast to the background against which it appears, and shall appear on the screen for a duration and in a location, sufficiently noticeable for an ordinary consumer to read and comprehend it.

Decision and Order

- b. In a print advertisement, promotional material, or instructional manual, the disclosure shall be in a type size and location sufficiently noticeable for an ordinary consumer to read and comprehend it, in print that contrasts with the background against which it appears.

**I.**

IT IS ORDERED that the respondents, directly or through any corporation, subsidiary, division, trade name, or other device, in connection with the manufacturing, labeling, advertising, promotion, offering for sale, sale, or distribution of Xenadrine EFX or any other weight loss product, in or affecting commerce, shall not represent, in any manner, expressly or by implication, including through the use of a trade name or endorsement, that:

- A. Such product causes rapid or substantial weight loss without the need to reduce caloric intake or increase physical activity;
- B. Xenadrine EFX or any substantially similar product causes rapid and substantial weight loss; or
- C. Xenadrine EFX or any substantially similar product causes rapid and substantial fat loss.

**II.**

IT IS FURTHER ORDERED that respondents, directly or through any corporation, subsidiary, division, trade name, or other device, in connection with the manufacturing, labeling, advertising, promotion, offering for sale, sale, or distribution of any covered product, in or affecting commerce, shall not make any representation, in any manner, expressly or by implication, including through the use of a trade name or endorsement:

- A. That such product causes weight loss or fat loss;

## Decision and Order

- B. That such product enables users to lose weight or fat without the need to increase exercise or reduce caloric intake;
- C. That such product causes permanent or long-term weight loss; or
- D. About the health benefits, performance, efficacy, safety or side effects, of such product;

unless the representation is true and, at the time it is made, respondents possess and rely upon competent and reliable scientific evidence that substantiates the representation.

**III.**

IT IS FURTHER ORDERED that respondents, directly or through any corporation, subsidiary, division, trade name, or other device, in connection with the labeling, advertising, promotion, offering for sale, sale, or distribution of Xenadrine EFX or any other covered product, in or affecting commerce, shall not misrepresent, in any manner, expressly or by implication the existence, contents, validity, results, conclusions, or interpretations of any test or study.

**IV.**

IT IS FURTHER ORDERED that respondents, directly or through any corporation, subsidiary, division, trade name, or other device, in connection with the manufacturing, labeling, advertising, promotion, offering for sale, sale, or distribution of Xenadrine EFX or any other covered product, in or affecting commerce, shall not misrepresent, in any manner, expressly or by implication, that the experience represented by any user testimonial or endorsement of the product represents the actual experience of the endorser as a result of use of the product under the circumstances depicted in the endorsement.

Decision and Order

**V.**

IT IS FURTHER ORDERED that respondents, directly or through any corporation, subsidiary, division, trade name, or other device, in connection with the manufacturing, labeling, advertising, promotion, offering for sale, sale, or distribution of Xenadrine EFX or any other covered product, in or affecting commerce, shall not make any representation, in any manner, expressly or by implication, about any endorser of such product unless they disclose, clearly and conspicuously, any material connection between such endorser and any respondent or any other individual or entity manufacturing, advertising, promoting, offering for sale, selling, or distributing such product. For purposes of this Paragraph, a “material connection” shall mean any relationship that materially affects the weight or credibility of the endorsement and would not reasonably be expected by consumers, including, but not limited to, monetary payments and the provision of goods, services, or other benefits to any consumer endorser.

**VI.**

Nothing in this order shall prohibit respondents from making any representation for any drug that is permitted in labeling for such drug under any tentative final or final standard promulgated by the Food and Drug Administration, or under any new drug application approved by the Food and Drug Administration.

**VII.**

Nothing in this order shall prohibit respondents from making any representation for any product that is specifically permitted in labeling for such product by regulations promulgated by the Food and Drug Administration pursuant to the Nutrition Labeling and Education Act of 1990.

Decision and Order

**VIII.**

IT IS FURTHER ORDERED that respondents shall pay to the Federal Trade Commission the sum of one hundred thousand dollars (\$100,000). This payment shall be made in the following manner:

- A. The payment shall be made by wire transfer or certified or cashier's check made payable to the Federal Trade Commission, the payment to be made no later than ten (10) days after the date that this order becomes final.
- B. In the event of any default in payment, which default continues for ten (10) days beyond the due date of payment, the amount due, together with interest, as computed pursuant to 28 U.S.C. § 1961 from the date of default to the date of payment, shall immediately become due and payable.
- C. The funds paid by respondents, together with any accrued interest, shall, in the discretion of the Commission, be used by the Commission to provide direct redress to purchasers of Xenadrine EFX in connection with the acts or practices alleged in the complaint, and to pay any attendant costs of administration. If the Commission determines, in its sole discretion, that redress to purchasers of these products is wholly or partially impracticable or is otherwise unwarranted, any funds not so used shall be paid to the United States Treasury. Respondents shall be notified as to how the funds are distributed, but shall have no right to contest the manner of distribution chosen by the Commission. No portion of the payment as herein provided shall be deemed a payment of any fine, penalty or punitive assessment.
- D. Respondents relinquish all dominion, control and title to the funds paid, and all legal and equitable title to the funds vests in the Treasurer of the United States and in the

Decision and Order

designated consumers. Respondents shall make no claim to or demand for return of the funds, directly or indirectly, through counsel or otherwise; and in the event of bankruptcy of any respondent, respondents acknowledge that the funds are not part of the debtor's estate, nor does the estate have any claim or interest therein.

**IX.**

**IT IS FURTHER ORDERED** that respondents must, in connection with this action or any subsequent investigations related to or associated with the transactions or the occurrences that are the subject of the Commission's Complaint, cooperate in good faith with the Commission's reasonable requests for documents and testimony. Respondents or their representatives shall appear at such places and times as the Commission shall reasonably request for interviews, conferences, pretrial discovery, review of documents, and for such other matters, after written notice to respondents and their counsel of record. Respondents or their representatives shall make themselves available for trial consistent with the Federal Rules of Civil Procedure. Respondents also shall produce such documents and information in a manner as may be reasonably requested by the Commission, after written notice to respondents and to their counsel of record.

**X.**

**IT IS FURTHER ORDERED** that respondents Cytodyne, LLC, Evergood, and their successors and assigns, and respondent Melvin Rich shall:

- A. Within thirty (30) days after the date of service of this order, send by first class mail, postage prepaid and return receipt requested, to each purchaser for resale of Xenadrine EFX with which respondents have done business since May 1, 2003 an exact copy of the notice attached hereto as Attachment A. The mailing shall not include any other document, information, or enclosures.

## Decision and Order

- B. In the event that respondents receive information that any of respondents' resellers or distributors are disseminating any advertisement or promotional material that contains any representation prohibited by this order, immediately notify each such reseller or distributor that respondents will stop doing business with that reseller or distributor if it continues to use any advertisement or promotional material that contains any representation prohibited by this order.
- C. Terminate all sales to any reseller or distributor within twenty (20) days if the reseller or distributor has continued to use any advertisement or promotional material that contains any representation prohibited by this order after receipt of the notice required by Subpart B of this Part.

**XI.**

IT IS FURTHER ORDERED that respondents Cytodyne, LLC, Evergood, and their successors and assigns, and respondent Melvin Rich shall, for five (5) years after the last correspondence to which they pertain, maintain and upon request make available to the Federal Trade Commission for inspection and copying:

- A. Copies of all notification letters sent to and return receipts from purchasers for resale pursuant to Subpart A of Part X of this order; and
- B. Copies of all communications with resellers or distributors pursuant to Subpart B and C of Part X of this order.

**XII.**

IT IS FURTHER ORDERED that respondents Cytodyne, LLC, Evergood, and their successors and assigns, and respondent Melvin Rich shall, for five (5) years after the last date of dissemination of any representation covered by this order, maintain and upon request make available to the Federal Trade Commission for inspection and copying:



Decision and Order

- A. All advertisements and promotional materials containing the representation including videotape recordings of all such broadcast advertisements;
- B. All materials that were relied upon in disseminating the representation; and
- C. All tests, reports, studies, surveys, demonstrations or other evidence in their possession or control that contradict, qualify, or call into question the representation, or the basis relied upon for the representation, including complaints and other communications with consumers or with governmental or consumer protection organizations.

**XIII.**

IT IS FURTHER ORDERED that respondents Cytodyne, LLC, Evergood, and their successors and assigns, and respondent Melvin Rich, for a period of ten (10) years after the date of issuance of this order, shall deliver a copy of this order to all current and future principals, officers, directors, and managers, and to all current and future employees, agents, and representatives having responsibilities with respect to the subject matter of this order, and shall secure from each such person a signed and dated statement acknowledging receipt of the order. Respondents shall deliver this order to current personnel within thirty (30) days after the date of service of this order, and to future personnel within thirty (30) days after the person assumes such position or responsibilities.

**XIV.**

IT IS FURTHER ORDERED that respondents Cytodyne, LLC, Evergood, and their successors and assigns, each shall notify the Commission at least thirty (30) days prior to any proposed change in its corporate structure that may affect compliance obligations arising under this order, including but not limited to a dissolution, assignment, sale, merger, or other action that would result in the

## Decision and Order

emergence of a successor corporation; the creation or dissolution of a subsidiary, parent, or affiliate that engages in any acts or practices subject to this order; the proposed filing of a bankruptcy petition; or a change in the corporate name or address. Provided, however, that, with respect to any proposed change in the corporation about which respondent learns less than thirty (30) days prior to the date such action is to take place, respondent shall notify the Commission as soon as is practicable after obtaining such knowledge. All notices required by this Part shall be sent by certified mail to the Associate Director, Division of Enforcement, Bureau of Consumer Protection, Federal Trade Commission, 600 Pennsylvania Avenue, NW, Washington, D.C. 20580.

**XV.**

IT IS FURTHER ORDERED that respondent Melvin Rich shall for a period of five (5) years after the date of issuance of this order, notify the Commission of the discontinuance of his current business or employment, or of his affiliation with any new business or employment that may affect his compliance obligations arising out of this order. The notice shall include respondent's new business address and telephone number and a description of the nature of the business or employment and his duties and responsibilities. All notices required by this Part shall be sent by certified mail to the Associate Director, Division of Enforcement, Bureau of Consumer Protection, Federal Trade Commission, 600 Pennsylvania Avenue, NW, Washington, D.C. 20580.

**XVI.**

IT IS FURTHER ORDERED that respondents Cytodyne, LLC, Evergood, and their successors and assigns, and respondent Melvin Rich shall, within sixty (60) days from the date of service of this order, and at such other times as the Federal Trade Commission may require, file with the Commission a report, in writing, setting forth in detail the manner and form in which they have complied with this order.

Decision and Order

**XVII.**

This order will terminate twenty (20) years from the date of its issuance, or twenty (20) years from the most recent date that the United States or the Federal Trade Commission files a complaint (with or without an accompanying consent decree) in federal court alleging any violation of the order, whichever comes later; provided, however, that the filing of such a complaint will not affect the duration of:

- A. Any Part in this order that terminates in less than twenty (20) years;
- B. This order's application to any respondent that is not named as a defendant in such complaint; and
- C. This order if such complaint is filed after the order has terminated pursuant to this Part.

Provided further, that if such complaint is dismissed or a federal court rules that the respondent did not violate any provision of the order, and the dismissal or ruling is either not appealed or upheld on appeal, then the order will terminate according to this Part as though the complaint had never been filed, except that the order will not terminate between the date such complaint is filed and the later of the deadline for appealing such dismissal or ruling and the date such dismissal or ruling is upheld on appeal.

Decision and Order

**ATTACHMENT A****GOVERNMENT-ORDERED DISCLOSURE  
[on Cytodyne, LLC Letterhead]**

[Insert Date]

Dear Xenadrine EFX Reseller or Distributor,

This letter is to inform you that Cytodyne, LLC recently settled a dispute with the Federal Trade Commission (“FTC”) regarding its advertising for Xenadrine EFX. Among other things, the settlement requires us to instruct resellers and distributors to stop using advertising or promotional materials that make any of the representations prohibited by the settlement. We will terminate all sales to resellers or distributors that make any of these prohibited representations.

The FTC complaint alleges that Cytodyne, LLC engaged in deceptive advertising of Xenadrine EFX, and the FTC order imposes various requirements on us in connection with its past and future advertising of these and other products.

The FTC complaint alleges, among other things, that our advertising materials claimed, expressly or by implication, that Xenadrine EFX causes rapid and substantial weight loss and fat loss; that it does so without the need to reduce caloric intake or increase physical activity; and that it causes permanent or long-term weight loss. The complaint alleges that these claims were false and that the information on which we relied in making these claims was not competent and reliable scientific evidence, as required by law. The FTC order prohibits us from making any claims similar to the challenged claims about any weight loss product unless we have competent and reliable scientific evidence to support them.

In addition, the FTC order provides that we must not make any claim about the health benefits, performance, safety, or efficacy of

Decision and Order

any weight loss product, dietary supplement, food, drug, or device unless we have competent and reliable scientific evidence to support such claims.

The FTC order further provides that we must not misrepresent, in any manner, expressly or by implication, the existence, contents, validity, results, conclusions, or interpretations of any test, study, or scientific research relating to any weight loss product, dietary supplement, food, drug, or device.

The FTC complaint also alleges that our Xenadrine EFX ads represented that the featured consumer endorsers achieved the weight loss reported in those ads solely through the use of Xenadrine EFX, but that endorsers had engaged in rigorous diet and/or exercise programs in order to lose weight. The FTC order prohibits us from making similar misrepresentations in the future.

The FTC order also requires us to monitor resellers' and distributors' advertisements and promotional materials and terminate all sales to resellers and distributors making prohibited claims, whether expressly or by implication, for our products.

Resellers and distributors should visit the Xenadrine website, [www.Xenadrine.com](http://www.Xenadrine.com), for the most up-to-date promotional materials regarding our products.

If you have any questions, please contact [insert name and telephone number of the responsible Cytodyne, LLC Attorney or Officer].

Sincerely,

Melvin Rich, Manager  
Cytodyne, LLC

## Analysis

**Analysis of Proposed Consent Order to Aid Public Comment**

The Federal Trade Commission has accepted, subject to final approval, an agreement containing a consent order from Cytodyne, LLC, Evergood Products Corp., and Melvin Rich, individually and as a manager of Cytodyne, LLC and an officer of Evergood Products Corp. (together, “respondents”).

The proposed consent order has been placed on the public record for thirty (30) days for receipt of comments by interested persons. Comments received during this period will become part of the public record. After thirty (30) days, the Commission will again review the agreement and the comments received, and will decide whether it should withdraw from the agreement or make final the agreement’s proposed order.

This matter involves practices relating to the advertising and promotion of Xenadrine EFX, a dietary supplement marketed for weight loss. According to the FTC complaint, respondents represented that Xenadrine EFX causes rapid and substantial weight and fat loss, causes permanent or long-term weight loss, and causes rapid and substantial weight loss without the need to diet or increase exercise. The complaint alleges that these claims are false and that the company failed to have substantiation for them. It further alleges that respondents falsely represented that scientific studies prove that Xenadrine EFX causes rapid and substantial weight loss and that it is more effective than leading ephedrine-based diet products.

The FTC complaint also alleges that respondents falsely represented that persons appearing in Xenadrine EFX advertisements achieved the weight loss reported in those ads solely through the use of Xenadrine EFX. According to the FTC complaint, persons who appeared in the Xenadrine EFX advertisements engaged in rigorous diet and/or exercise programs in order to lose weight, and some were provided with a personal trainer. Finally, the complaint alleges that, in presenting testimonials for Xenadrine EFX by consumer endorsers who

Analysis

purportedly lost weight in the ordinary course of using Xenadrine EFX, respondents failed to disclose that the endorsers were paid from \$1000 to \$20,000 in connection with their endorsement, a fact that would be material to consumers in their decisions about purchasing or using the product.

The proposed consent order contains provisions designed to prevent the respondents from engaging in similar acts and practices in the future.

Part I of the order prohibits representations that Xenadrine EFX or any other product containing green tea extract, bitter orange, or caffeine causes rapid and substantial weight loss or fat loss. It also prohibits representations that any weight loss product causes rapid or substantial weight loss without the need to diet or increase exercise.

Part II prohibits respondents from representing that any weight loss product, dietary supplement, food, drug, or device causes weight or fat loss, causes permanent or long-term weight loss, or enables users to lose weight or fat without the need to diet or increase exercise unless the claim is true and respondents possess competent and reliable scientific evidence that substantiates the claim. It also prohibits respondents from making any other claims about the health benefits, performance, efficacy, safety, or side effects of any such product unless the claim is true and respondents possess competent and reliable scientific evidence that substantiates the claim.

Part III prohibits any misrepresentation of the existence, contents, validity, results, conclusions, or interpretations of any test or study in connection with the marketing or sale of any weight loss product, dietary supplement, food, drug, or device.

Part IV prohibits any misrepresentation that the experience described in any user testimonial for any weight loss product,

## Analysis

dietary supplement, food, drug, or device represents the actual experience of the endorser as a result of using the product under the circumstances depicted in the endorsement.

Part V prohibits any representation about any endorser of any weight loss product, dietary supplement, food, drug, or device unless the respondents disclose any material connection that exists between the endorser and the respondents or any other person or entity involved in manufacturing, marketing, or selling the product.

Part VI of the proposed order allows the respondents to make any representations for any drug that are permitted in labeling for the drug under any tentative final or final Food and Drug Administration (“FDA”) standard or under any new drug application approved by the FDA.

Part VII of the proposed order allows the respondents to make representations for any product that are specifically permitted in labeling for that product by regulations issued by the FDA under the Nutrition Labeling and Education Act of 1990.

Part VIII provides for the payment of \$100,000 to the Commission.

Part IX requires respondents to cooperate in good faith with the Commission’s reasonable requests for documents and testimony in connection with this action or any investigations related to or associated with the transactions or the occurrences that are the subject of the FTC complaint.

Part X requires respondents to send a letter to purchasers for resale of Xenadrine EFX notifying them of the Commission’s order. It also provides that if respondents learn that any of its resellers or distributors are disseminating any advertisement or promotional material containing prohibited representations, they are required to request that the resellers or distributors stop making such representations and to stop doing business with



Analysis

resellers or distributors that do not comply with this request. Part XI requires respondents to keep copies of the communications required by Part X.

Parts XII through XVI require respondents to keep copies of relevant advertisements and materials substantiating claims made in the advertisements; to provide copies of the order to certain of their personnel; to notify the Commission of changes in corporate structure (for the corporate respondents) and changes in employment (for the individual respondent) that might affect compliance obligations under the order; and to file compliance reports with the Commission. Part XVII provides that the order will terminate after twenty (20) years under certain circumstances.

The purpose of this analysis is to facilitate public comment on the proposed order, and it is not intended to constitute an official interpretation of the agreement and proposed order or to modify in any way their terms.

Complaint

IN THE MATTER OF

**ADVERTISING.COM, INC. DOING BUSINESS AS,  
TEKNOSURF.COM, AND JOHN FERBER**CONSENT ORDER, ETC., IN REGARD TO ALLEGED VIOLATIONS OF  
SEC. 5 OF THE FEDERAL TRADE COMMISSION ACT*Docket C-4147; File No. 0423196**Complaint, September 12, 2005--Decision, September 12, 2005*

This consent order, among other things, prohibits Respondents Advertising.com, Inc., and John Ferber – who advertised and distributed computer software products, including the SpyBlast computer software product, advertised as an Internet security program – from making any representation about the performance, benefits, efficacy, or features of SpyBlast or any of respondents' other executable computer software programs whose principal function is to enhance security or privacy, unless respondents disclose clearly and conspicuously that consumers who install the program will receive advertisements, if that is the case.

*Participants*

For the Commission: *Shira D. Modell, Michael F. Ostheimer, Char Pagar, Thomas B. Pahl, Mary K. Engle and Hajime Hadeishi.*

For the Respondent: *Christine Varney, Hogan & Hartson*

**COMPLAINT**

The Federal Trade Commission, having reason to believe that Advertising.com, Inc., a corporation, also doing business as Teknosurf.com, and John Ferber, individually and as an officer of the corporation (“respondents”), have violated the provisions of the Federal Trade Commission Act, and it appearing to the Commission that this proceeding is in the public interest, alleges:

1. Respondent Advertising.com, Inc., also doing business as Teknosurf.com, is a Maryland corporation with its principal office or place of business at 1020 Hull Street, Baltimore, Maryland 21230.

Complaint

2. Respondent John Ferber is an officer of the corporate respondent. Individually or in concert with others, he formulates, directs, or controls the policies, acts, or practices of the corporation, including the acts or practices alleged in this complaint. His principal office or place of business is the same as that of Advertising.com, Inc.
3. Respondents have developed, advertised, promoted, and distributed to the public computer software products, including the SpyBlast computer software product.
4. The acts and practices of respondents alleged in this complaint have been in or affecting commerce, as “commerce” is defined in Section 4 of the Federal Trade Commission Act.
5. Respondents caused ads for SpyBlast to be served on consumers’ computers (including Exhibit A). These ads represented that because the consumer’s computer was broadcasting an Internet IP address, it was at risk from hackers. Consumers who clicked on this advertisement were shown an ActiveX “security warning” installation box with a hyperlink describing SpyBlast as “Personal Computer Security and Protection Software from unauthorized users” and telling them “once you agree to the License Terms and Privacy Policy – click YES to continue.” (Exhibit B).
6. If a consumer clicked “Yes,” the software was installed, even if the consumer had not clicked on the hyperlink. Only if a consumer clicked on the hyperlink describing SpyBlast as “Personal Computer Security and Protection Software from unauthorized users” before clicking “YES,” did SpyBlast’s End User Licensing Agreement (“EULA”) appear. (Exhibit C). The EULA contained a statement that consumers agreed to receive marketing messages, including pop-up ads, in exchange for getting SpyBlast. It also stated that respondent Advertising.com collected information about SpyBlast users, including “URLs of

## Complaint

visited pages and [the user's] IP address,” and that this information allowed the company “to send [a user] advertisements that might be of interest to [the user].”

7. SpyBlast could also be downloaded directly from the [www.SpyBlast.com](http://www.SpyBlast.com) website. (Exhibit D). At the very bottom of the [www.SpyBlast.com](http://www.SpyBlast.com) home page, below several hyperlinks to download SpyBlast, a small disclosure appeared. This disclosure stated that “In exchange for usage of the SpyBlast software, user agrees to receive . . . offers on behalf of SpyBlast’s marketing partners.”

8. Respondents downloaded bundled adware onto the computers of consumers who installed SpyBlast. The adware collected information about SpyBlast users, including URLs of visited pages and the user’s IP address, and this information allowed respondents to send users advertisements that respondents believed might be of interest to them. Consumers received a substantial number of pop-up advertisements as result of respondents’ installation of this adware onto their computers.

9. Respondents represented to consumers that Spyblast is an Internet security program. Respondents failed to disclose adequately that SpyBlast includes adware that causes consumers to receive pop-up advertisements, as described in Paragraph 8. The installation of such adware would be material to consumers in their decision whether to install the SpyBlast program. The failure to adequately disclose this fact, in light of the representation made, was, and is, a deceptive act or practice.

10. The acts and practices alleged in this complaint constitute unfair or deceptive acts or practices in or affecting commerce in violation of Section 5(a) of the Federal Trade Commission Act.

THEREFORE, the Federal Trade Commission this 12<sup>th</sup> day of September, 2005, has issued this complaint against respondent.



**Advertisement**

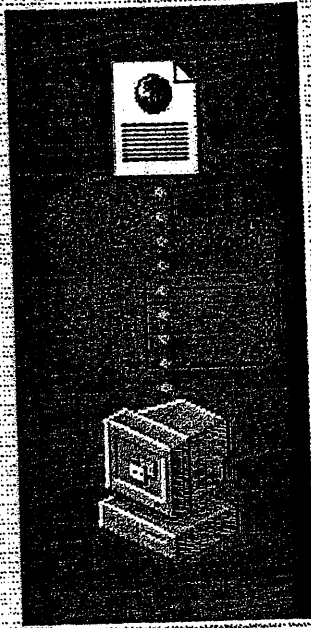


Your Computer Is  
Currently  
Broadcasting An  
Internet IP Address.  
With this Address,  
Someone Can  
Immediately Begin  
Attacking Your  
Computer!

OK



Security Warning



Do you want to install and run "SpyBlast - Personal Computer Security and Protection Software from unauthorized users; once you agree to the License Terms and Privacy Policy - click YES to continue" signed on 8/14/2003 2:02 PM and distributed by:

Teknosurf.com

Publisher authenticity verified by VeriSign Class 3 Code Signing 2001 CA

Caution: Teknosurf.com asserts that this content is safe. You should only install/view this content if you trust Teknosurf.com to make that assertion.

Always trust content from Teknosurf.com

Yes No More Info





**SpyBlast****INTERNET  
SECURITY PROTECTION**

[ CLOSE ]

**IMPORTANT:** PLEASE READ THE FOLLOWING END USER LICENSE AGREEMENT AND REVIEW OUR PRIVACY POLICY CLOSELY BEFORE PROCEEDING WITH THE DOWNLOAD OR USE OF THE SPYBLAST SOFTWARE.

The following End User License Agreement (the "Agreement") between you (referred to herein sometimes as "You" and "End User") and Advertising.com d/b/a Teknosurf.com ("Teknosurf.com" or the "Company") sets out the terms of your use of the SpyBlast software (the "Program"), please read them carefully. By downloading the Program, you are agreeing to be bound by the terms of this Agreement. The Program is offered to you conditioned on your acceptance without modification of the terms, conditions, and notices contained herein and in our Privacy Policy set forth at <http://www.spyblast.com/privacy.html>. If you are unwilling to agree to the terms of this Agreement or our Privacy Policy, you will not be granted access to the Program. The terms of this Agreement comprises the entire agreement between you and Teknosurf.com with respect to the Program and supersede all prior agreements between the parties, regarding the subject matter contained herein.

#### **USE OF THE PROGRAM**

Teknosurf.com is providing you with free proprietary anti-snooping software that alerts you when there is an unauthorized attempt to access your computer. In consideration for the Program, you agree and covenant to receive from Teknosurf.com, from time to time relevant marketing messages based on Your web surfing habits, including pop-up advertisements, which may include opportunities to join and/or participate in services or programs that are offered by other, third-party companies that advertise through Teknosurf.com via the Program. Any dealings with advertisers who market via the Program, or participation in promotions, including the delivery of and the payment for goods and services, and any other terms, conditions, warranties or representations associated with such dealings or promotions, are solely between you and the advertiser or other third party. Teknosurf.com shall not be responsible or liable for any part of any such dealings or promotions. Teknosurf.com collects non-personally identifiable, online behavior statistical information about End Users. Examples of information that we collect include URLs of visited pages and your IP address. Upon termination of an online session, closing of the software application and/or removal of the Program from your computer this information will no longer be collected. We gather this information only to improve the administration of the Program and to provide End Users with a more personally relevant Internet experience. Summaries of such information will be made available to advertisers, so that they can better target their advertising campaigns. The summaries do not include End Users' names, addresses, email addresses, or other personally identifiable information. The gathered information will also allow us to send you advertisements that might be of interest to You. European Union Service users understand and consent to the processing of personal information in the United States. You agree to use the Program in a responsible manner and, should You download the Program to a computer, which is, used in the workplace, in compliance with any of your employer's policies, in addition to complying with any federal, state and local laws. End Users can use the Program on any number of computers as determined by the End User.

To be eligible to use the Program, You must agree to receive from Teknosurf.com, from time to time, marketing messages that are offered by other, third-party companies that advertise through Teknosurf.com via the Program. You may, at any time, opt-out of receiving such marketing messages by closing the Program or removing the Program from Your computer.

#### **REPRESENTATIONS OF END USER**

**EXHIBIT C**

You represent and warrant that you are the owner of this computer and that you have authorized the download and installation of the Program or that the owner of this computer has authorized you to do so. You agree, with respect to all other users of this computer that you have caused the Program to reside, to (i) provide a copy of the SpyBlast Privacy Statement and End User License Agreement; and (ii) to obtain their consent to same before allowing them to use this computer. Alternatively, if you have the legal right to accept this Agreement on behalf of one or more users of this computer that you have caused the Program to reside, then you hereby accept this Agreement on behalf of all such other users. Also, you agree not to use the Program, in a manner prohibited by law, or in violation of any contractual provision by which you are bound. You agree to comply with all applicable laws, rules and regulations in your use of the Program.

You further represent and warrant that you shall not (a) use, or encourage others to use, any robot, spider, other automatic or non-automatic manual device or process intended to interfere or attempt to interfere with the proper working of the Program, or (b) use any means to avoid the display of any third-party marketing messages via the Program while retaining the ability to use the Program, or (c) act against the business interests or reputation of Teknosurf.com or its affiliates or marketing partners.

## TERMINATION

Use of the Program on any computer is completely voluntary. You may terminate this Agreement by removing the Program from Your computer at anytime for any reason.

## SOFTWARE LICENSE

By entering into this Agreement you are receiving A NON-EXCLUSIVE, LIMITED, FREE BETA VERSION ONLY LICENSE TO USE THE PROGRAM which is provided on an "AS IS" basis, for your private personal use only. This Agreement, the SpyBlast Privacy Policy and any other applicable terms of use document available at <http://www.SpyBlast.com> shall apply to any use of the Program. You agree not to extract information from the Program, reverse engineer, decompile, disassemble, alter, duplicate, make copies (other than for backup purposes), create derivative works from, distribute or provide others with the Program. Your license to an existing version of Program may, at Teknosurf.com's discretion, expire when new versions of Program are released. Any and all such modifications or enhancements to the Program by you, Teknosurf.com, or Teknosurf.com's affiliates or partners, remain the sole property of Teknosurf.com. Notwithstanding the foregoing, Teknosurf.com has no obligation to make available to you any subsequent versions of Program.

By accepting the terms of this Agreement you agree that Teknosurf.com is permitted to limit, deny, create different priorities to different users, or cancel some or all of the functionality of the Program at any time, without prior notice. Teknosurf.com makes no warranties or guarantees as to the availability or reliability of the Program to you or to any other user. The Program functionality or any part thereof including without limitation, the availability and functionality of any feature and function of the Program may be changed, limited or terminated at any time, temporarily or permanently, without prior notice, for any reason or no reason by Teknosurf.com in its sole discretion ("Changes in Functionality"). You agree to bear the risks of and hold Teknosurf.com harmless for any and all effects that the Changes of Functionality may have on your ability to use the Program in whole or in part. Additionally,

Teknosurf.com may require the update or automatic distribution of the Program on your computer when a new version of the Program is released to the general public, when new features are available, to display promotional offers, and/or to add new applications to the applications that comprise Program. This update or new download may occur automatically or through other means.

The Program contains features that may link you or provide you with certain reference and functionality to third parties' Web sites, directories, servers or services ("Third Party Services"). These features are provided by Teknosurf.com only as a convenience to You. The Third Party Services are not reviewed, controlled or examined by Teknosurf.com in any way and Teknosurf.com is not responsible for the contents of any such Third Party Services, or any link contained therein. The offering of these features does not imply endorsement of the Third Party Services by Teknosurf.com. It is your sole responsibility to comply with the appropriate terms of services of these Third Party Services you chose to access using these features, as well as with any other obligation under copyright, trade secrets, defamation, decency, privacy, security and export laws and any other applicable laws. In no event shall Teknosurf.com be liable to anyone for any damage arising from or occasioned by the creation or use of the Third Party Services or the information or material accessed through these services. Teknosurf.com reserves the exclusive right and sole discretion to add, change, decline disable or remove, without notice, any feature, access or link to any of the Third Party Services from the Program and/or to introduce different features, access or links to different users. In addition, Teknosurf.com does not endorse any service or product that may be offered by any third party that is advertising through the Program.

Teknosurf.com reserves all rights in the Program not expressly granted to you in this Agreement.

#### **OTHER RESTRICTIONS**

You may not rent, lend, assign, or lease the Program, but you may transfer your rights under this Agreement on a permanent basis provided (i) you transfer all copies of the Program and this Agreement; and (ii) the recipient agrees to be bound to this Agreement. Any transfer must include the most recent product upgrade. Prior to transferring the Program you must remove the Program to be transferred from your machine.

#### **PROPRIETARY RIGHTS**

You agree that the Program is licensed, not sold to you. You agree that the Program belongs to Teknosurf.com, including all intellectual and proprietary rights, unless otherwise specified. Teknosurf.com retains all right, title and interest in and to the Program at all times, and regardless of the form or media in or on which the original or other copies may subsequently exist. Additionally, You acknowledge that content, including but not limited to text, software, music, sound, photographs, video, graphics; or other material contained in either the Program; or electronically distributed, commercially produced information presented to you via the Program, by Teknosurf.com, or Teknosurf.com's third party marketing partners or other content providers; is protected by copyrights, trademarks, service marks, patents or other proprietary rights and laws. You may not modify, copy, reproduce, republish, resell, upload, post, transmit, or distribute in any way the Program or content available through the Program and its associated Web Sites, including code and software. This

Agreement gives you no rights to such content. Finally, any suggestions, ideas or inventions that you voluntarily and optionally disclose to us through any means will be used, or not used, by Teknosurf.com at Teknosurf.com's sole discretion; and, Teknosurf.com will have no obligation to you regarding any ideas or inventions that you disclose through such means.

#### **DISCLAIMERS; LIMITATION OF LIABILITY**

TEKNOSURF.COM AND/OR ITS RESPECTIVE SUPPLIERS MAKE NO REPRESENTATIONS ABOUT THE SUITABILITY, RELIABILITY, AVAILABILITY, TIMELINESS, AND ACCURACY OF THE PROGRAM FOR ANY PURPOSE. THE PROGRAM IS PROVIDED "AS IS" WITHOUT WARRANTY OF ANY KIND. TEKNOSURF.COM AND/OR ITS RESPECTIVE SUPPLIERS HEREBY DISCLAIM ALL WARRANTIES AND CONDITIONS WITH REGARD TO THE PROGRAM, INCLUDING ALL IMPLIED WARRANTIES AND CONDITIONS OF MERCHANTABILITY, FITNESS FOR A PARTICULAR PURPOSE, TITLE AND NON-INFRINGEMENT. TEKNOSURF.COM MAKES NO WARRANTY REGARDING ANY GOODS OR SERVICES PURCHASED OR OBTAINED THROUGH THE PROGRAM OR TRANSACTIONS ENTERED INTO THROUGH THE PROGRAM.

TEKNOSURF.COM DOES NOT WARRANT OR GUARANTEE THAT THE PROGRAM WILL BE UNINTERRUPTED OR ERROR-FREE OR THAT DEFECTS IN THE PROGRAM WILL BE CORRECTED. TEKNOSURF.COM DOES NOT WARRANT OR GUARANTEE THAT THE PROGRAM OR ANY INFORMATION WILL BE FREE FROM INFECTION BY VIRUSES, WORMS, TROJAN-HORSES OR ANYTHING ELSE MANIFESTING CONTAMINATING OR DESTRUCTIVE PROPERTIES.

IN NO EVENT SHALL TEKNOSURF.COM AND/OR ITS SUPPLIERS BE LIABLE FOR ANY DIRECT, INDIRECT, PUNITIVE, INCIDENTAL, SPECIAL, CONSEQUENTIAL DAMAGES OR ANY DAMAGES WHATSOEVER INCLUDING, WITHOUT LIMITATION, DAMAGES FOR LOSS OF USE, DATA OR PROFITS, ARISING OUT OF OR IN ANY WAY CONNECTED WITH THE USE OR PERFORMANCE OF THE PROGRAM OR RELATED WEB SITES, WITH THE DELAY OR INABILITY TO USE THE PROGRAM OR RELATED WEB SITES, THE PROVISION OF OR FAILURE TO PROVIDE SERVICES, OR FOR ANY INFORMATION, SOFTWARE, PRODUCTS, SERVICES AND RELATED GOODS, SERVICES OR GRAPHICS PURCHASED OR OBTAINED OR MESSAGES RECEIVED OR TRANSACTIONS ENTERED INTO THROUGH THE PROGRAM, OR OTHERWISE ARISING OUT OF THE USE OF THE PROGRAM, WHETHER BASED ON CONTRACT, TORT, NEGLIGENCE, STRICT LIABILITY OR OTHERWISE, EVEN IF TEKNOSURF.COM OR ANY OF ITS SUPPLIERS HAS BEEN ADVISED OF THE POSSIBILITY OF DAMAGES. BECAUSE SOME STATES/JURISDICTIONS DO NOT ALLOW THE EXCLUSION OR LIMITATION OF LIABILITY FOR CONSEQUENTIAL OR INCIDENTAL DAMAGES, THE ABOVE LIMITATION MAY NOT APPLY TO YOU. IF YOU ARE DISSATISFIED WITH ANY PORTION OF THE PROGRAM, OR WITH ANY OF THESE TERMS OF USE, YOUR SOLE AND EXCLUSIVE REMEDY IS TO IMMEDIATELY (1) DISCONTINUE USING THE PROGRAM, AND (2) TERMINATE THIS AGREEMENT.

#### **INDEMNIFICATION**

You agree to indemnify and hold Teknosurf.com, its subsidiaries, affiliates, officers and employees, harmless from any claim or demand, including reasonable attorneys fees, made by any third party due to or arising out of your use of the Program, the violation of these terms of this Agreement by you, or the infringement by you, or other user of the Program using your computer, of any intellectual property or other right of any person or entity.

#### **MODIFICATIONS**

Teknosurf.com reserves the right to change any of these terms and conditions at any

time. Upon any change in the terms of this Agreement, Teknosurf.com will notify all members through notice on the SpyBlast.com web site. Your continued use of the Program constitutes an affirmative: (1) acknowledgment by you of the terms of this Agreement and any modifications; and (2) agreement by you to abide and be bound by the terms of this Agreement and modifications. Teknosurf.com reserves the right to modify or discontinue the Program with or without notice. Teknosurf.com shall not be liable to your or any third party should Teknosurf.com exercise its right to modify or discontinue the Program.

## GENERAL

This agreement is governed by the laws of the State of Maryland, and the United States of America and, by accepting the terms of this agreement, You irrevocably consent to the exclusive jurisdiction of the courts of the State of Maryland and the federal courts situated in the State of Maryland in connection with any action arising between you and Teknosurf.com. Use of the Program is unauthorized in any jurisdiction that does not give effect to all provisions of these terms and conditions, including without limitation this paragraph. You agree that no joint venture, partnership, employment, or agency relationship exists between you and Teknosurf.com as a result of this Agreement or use of the Program. Teknosurf.com's performance of this agreement is subject to existing laws and legal process, and nothing contained in this agreement is in derogation of Teknosurf.com's right to comply with governmental, court and law enforcement requests or requirements relating to your use of the Program or information provided to or gathered by Teknosurf.com with respect to such use. If any part of this Agreement is determined to be invalid or unenforceable pursuant to applicable law including, but not limited to, the warranty disclaimers and liability limitations set forth above, then the invalid or unenforceable provision will be deemed superseded by a valid, enforceable provision that most closely matches the intent of the original provision and the remainder of the agreement shall continue in effect. Any waiver (express or implied) or delay by Teknosurf.com of any default or breach of this Agreement shall not constitute a waiver of any other or subsequent default or breach. A printed version of this Agreement and of any notice given in electronic form shall be admissible in judicial or administrative proceedings based upon or relating to this agreement to the same extent and subject to the same conditions as other business documents and records originally generated and maintained in printed form. You and Teknosurf.com agree that any cause of action arising out of or related to this Agreement or the Program must commence within one (1) year after the cause of action arose; otherwise, such cause of action is permanently barred.

Date: 8/14/03

Revision: 3

Copyright © 2003 Teknosurf.com

[Privacy Policy](#) | [Support](#)



# SpyBlast

SpyBlast  
to the  
RESCUE!

INTERNET SECURITY PROTECTION

ABOUT US

FAQ

RESULTS

CONTACT

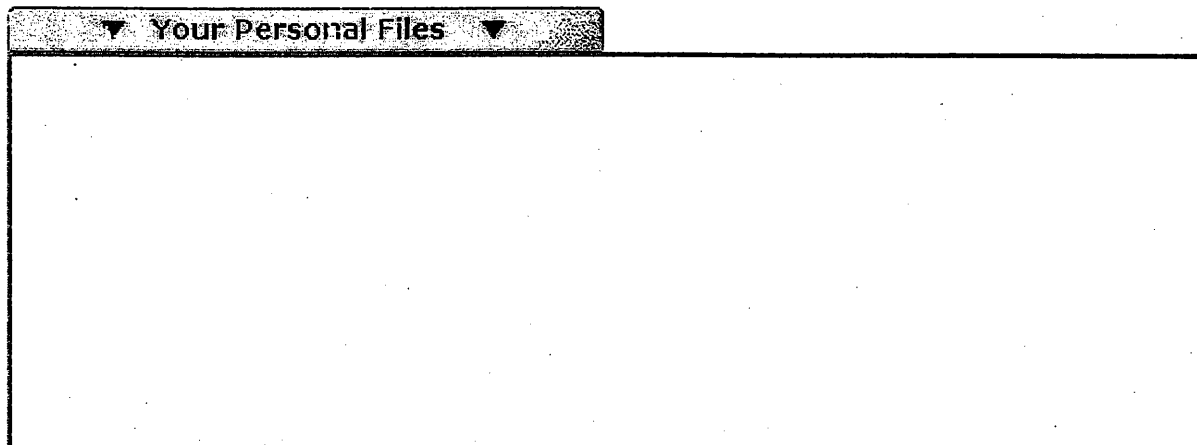
## Detect Internet Intruders with this **FREE** Software!

Someone may be snooping around your computer at this very moment, deleting files, reformatting disks or even worse: stealing your identity.

Below is just some of what an intruder sees on YOUR COMPUTER!



### SpyBlast Security Test Result:



If you can view the results in the box above:  
Hackers may have the ability to view your private files and steal your passwords.

## Rely on **SpyBlast**

If you don't want to share your computer with strangers, SpyBlast can help you detect intruders attempting to hijack your computer. SpyBlast is a TOTALLY FREE\* software that can be downloaded instantly!

If someone tries to gain access to your computer, the SpyBlast icon will FLASH instantly.

EXHIBIT D

---

**SpyBlast** shows you the following information about someone's attempt to invade your privacy:

- **Date and time of the attempted violation**
- **IP address of the violator**
- **Number of attempts the violator has made**

See **SpyBlast Results** [click here!](#)

---

Instead of continuing to be a victim, become aware of who is attempting to access your computer with **SpyBlast**. Its simple, convenient, effective, and it just sits in your system tray.

**[Click here to download your FREE SpyBlast spy software instantly.](#)**

\* In exchange for usage of the SpyBlast software, user agrees to receive, from time to time, special offers on behalf of SpyBlast's marketing partners. Please see the Spyblast Terms & Conditions.

Attention SpyBlast Software Users: The SpyBlast Terms & Conditions have been updated effective August 14, 2003.

[Terms & Conditions](#) | [Privacy Policy](#) | [Support](#)



Decision and Order

## **DECISION AND ORDER**

The Federal Trade Commission having initiated an investigation of certain acts and practices of the respondents named in the caption hereof, and the respondents having been furnished thereafter with a copy of a draft of complaint which the Bureau of Consumer Protection proposed to present to the Commission for its consideration and which, if issued by the Commission, would charge the respondents with violation of the Federal Trade Commission Act; and

The respondents, their attorneys, and counsel for the Commission having thereafter executed an agreement containing a consent order, an admission by the respondents of all the jurisdictional facts set forth in the aforesaid draft complaint, a statement that the signing of the agreement is for settlement purposes only and does not constitute an admission by the respondents that the law has been violated as alleged in such complaint, or that the facts as alleged in such complaint, other than jurisdictional facts, are true, and waivers and other provisions as required by the Commission's Rules; and

The Commission having thereafter considered the matter and having determined that it had reason to believe that the respondents have violated the Act, and that complaint should issue stating its charges in that respect, and having thereupon accepted the executed consent agreement and placed such agreement on the public record for a period of thirty (30) days, now in further conformity with the procedure prescribed in § 2.34 of its Rules, the Commission hereby issues its complaint, makes the following jurisdictional findings, and enters the following order:

1. Respondent Advertising.com, Inc., also doing business as Teknosurf.com, is a Maryland corporation with its principal office or place of business at 1020 Hull Street, Baltimore, Maryland 21230.
2. Respondent John Ferber is an officer of the corporate respondent. Individually or in concert with others, he formulates,

## Decision and Order

directs, or controls the policies, acts, or practices of the corporation. His principal office or place of business is the same as that of Advertising.com, Inc.

3. The Federal Trade Commission has jurisdiction of the subject matter of this proceeding and of the respondent, and the proceeding is in the public interest.

**ORDER****DEFINITIONS**

For purposes of this Order, the following definitions shall apply:

1. Unless otherwise specified, “respondents” shall mean Advertising.com, Inc., also doing business as Teknosurf.com, its successors and assigns, and their officers; John Ferber, individually and as an officer of the corporation; and each of the above’s agents, representatives, and employees.
2. “Commerce” shall mean as defined in Section 4 of the Federal Trade Commission Act, 15 U.S.C. § 44.
3. “Endorsement” shall mean as defined in 16 C.F.R. § 255.0(b).
4. “Clearly and prominently” shall mean as follows:
  - A. In an advertisement communicated through an electronic medium (such as television, video, radio, and interactive media such as the Internet and online services), the disclosure shall be presented simultaneously in both the audio and visual portions of the advertisement. Provided, however, that in any advertisement presented solely through visual or audio means, the disclosure may be made through the same means in which the advertisement is presented. The audio disclosure shall be delivered in a volume and cadence sufficient for an ordinary consumer to hear and comprehend it. The visual disclosure

Decision and Order

shall be of a size and shade, and shall appear on the screen for a duration, sufficient for an ordinary consumer to read and comprehend it. In addition to the foregoing, in interactive media, the disclosure shall also be unavoidable and shall be presented prior to the consumer installing or downloading any software code, program, or content and prior to the consumer incurring any financial obligation.

B. In a print advertisement, promotional material, or instructional manual, the disclosure shall be in a type size and location sufficiently noticeable for an ordinary consumer to read and comprehend it, in print that contrasts with the background against which it appears. In multipage documents, the disclosure shall appear on the cover or first page.

The disclosure shall be in understandable language and syntax. Nothing contrary to, inconsistent with, or in mitigation of the disclosure shall be used in any advertisement.

**I.**

IT IS ORDERED that respondents, directly or through any corporation, subsidiary, division, or other device, in connection with the labeling, advertising, promotion, offering for sale, sale, or distribution, in or affecting commerce, of SpyBlast or any of respondents' other executable computer software programs whose principal function is to enhance security or privacy shall not make any representation, in any manner, expressly or by implication, including through the use of endorsements or the product name, about the performance, benefits, efficacy, or features of such program, unless they disclose, clearly and prominently, that consumers who install the program will receive advertisements, if that is the case.

**II.**

IT IS FURTHER ORDERED that respondent Advertising.com, Inc., its successors and assigns, and respondent John Ferber shall,

## Decision and Order

for five (5) years after the last date of dissemination of any representation covered by this order, maintain and upon request make available to the Federal Trade Commission for inspection and copying:

- A. All advertisements and promotional materials containing the representation;
- B. All materials that were relied upon in disseminating the representation; and
- C. All tests, reports, studies, surveys, demonstrations, or other evidence in their possession or control that contradict, qualify, or call into question the representation, or the basis relied upon for the representation, including complaints and other communications with consumers or with governmental or consumer protection organizations.

**III.**

IT IS FURTHER ORDERED that respondent Advertising.com, Inc., its successors and assigns, and respondent John Ferber shall deliver a copy of this order to all current and future principals, officers, directors, and managers, and to all current and future employees, agents, and representatives having responsibilities with respect to the subject matter of this order. Respondents shall deliver this order to current personnel within thirty (30) days after the date of service of this order, and to future personnel within thirty (30) days after the person assumes such position or responsibilities.

**IV.**

IT IS FURTHER ORDERED that respondent Advertising.com, Inc., and its successors and assigns, shall notify the Commission at least thirty (30) days prior to any change in the corporation that may affect compliance obligations arising under this order, including, but not limited to, a dissolution, assignment, sale,

Decision and Order

merger, or other action that would result in the emergence of a successor corporation; the creation or dissolution of a subsidiary, parent, or affiliate that engages in any acts or practices subject to this order; the proposed filing of a bankruptcy petition; or a change in the corporate name or address. Provided, however, that, with respect to any proposed change in the corporation about which respondent learns less than thirty (30) days prior to the date such action is to take place, respondent shall notify the Commission as soon as is practicable after obtaining such knowledge. All notices required by this Part shall be sent by certified mail to the Associate Director, Division of Enforcement, Bureau of Consumer Protection, Federal Trade Commission, 600 Pennsylvania Avenue, N.W., Washington, D.C. 20580.

**V.**

IT IS FURTHER ORDERED that respondent John Ferber, for a period of ten (10) years after the date of issuance of this order, shall notify the Commission of the discontinuance of his current business or employment, or of his affiliation with any new business or employment. The notice shall include respondent's new business address and telephone number and a description of the nature of the business or employment and his duties and responsibilities. All notices required by this Part shall be sent by certified mail to the Associate Director, Division of Enforcement, Bureau of Consumer Protection, Federal Trade Commission, Washington, D.C. 20580.

**VI.**

IT IS FURTHER ORDERED that respondent Advertising.com, Inc., its successors and assigns, and respondent John Ferber shall, within sixty (60) days after service of this order, and at such other times as the Federal Trade Commission may require, file with the Commission a report, in writing, setting forth in detail the manner and form in which they have complied with this order.

Decision and Order

**VII.**

This order will terminate twenty (20) years from the date of its issuance, or twenty (20) years from the most recent date that the United States or the Federal Trade Commission files a complaint (with or without an accompanying consent decree) in federal court alleging any violation of the order, whichever comes later; provided, however, that the filing of such a complaint will not affect the duration of:

- A. Any Part in this order that terminates in less than twenty (20) years;
- B. This order's application to any respondent that is not named as a defendant in such complaint; and
- C. This order if such complaint is filed after the order has terminated pursuant to this Part.

Provided, further, that if such complaint is dismissed or a federal court rules that the respondent did not violate any provision of the order, and the dismissal or ruling is either not appealed or upheld on appeal, then the order will terminate according to this Part as though the complaint had never been filed, except that the order will not terminate between the date such complaint is filed and the later of the deadline for appealing such dismissal or ruling and the date such dismissal or ruling is upheld on appeal.

Analysis

**Analysis of Proposed Consent Order to Aid Public Comment**

The Federal Trade Commission has accepted, subject to final approval, an agreement containing a consent order from Advertising.com, Inc. and John Ferber, individually and as an officer of Advertising.com (together “respondents”).

The proposed consent order has been placed on the public record for thirty (30) days for receipt of comments by interested persons. Comments received during this period will become part of the public record. After thirty (30) days, the Commission will again review the agreement and the comments received, and will decide whether it should withdraw from the agreement or make final the agreement’s proposed order.

Respondents advertised and distributed computer software products, including the SpyBlast computer software product, which was advertised as an Internet security program. This matter concerns the allegation that respondents failed to disclose adequately that SpyBlast included adware that caused consumers to receive pop-up advertisements.

The Commission’s complaint alleges that respondents disseminated ads for SpyBlast that represented that because a consumer’s computer was broadcasting an Internet IP address, the computer was at risk from hackers. According to the complaint, consumers who clicked on this advertisement were shown an ActiveX “security warning” installation box with a hyperlink describing SpyBlast as “Personal Computer Security and Protection Software from unauthorized users” and telling them “once you agree to the License Terms and Privacy Policy – click YES to continue.” If a consumer clicked “Yes,” the software was installed, even if the consumer had not clicked on the hyperlink. Only if a consumer clicked on the hyperlink describing SpyBlast as “Personal Computer Security and Protection Software from unauthorized users” before clicking “YES,” did SpyBlast’s End

## Analysis

User Licensing Agreement (“EULA”) appear. The EULA contained a statement that consumers agreed to receive marketing messages, including pop-up ads, in exchange for getting SpyBlast.

The complaint further alleges that SpyBlast could also be downloaded directly from the [www.SpyBlast.com](http://www.SpyBlast.com) website. At the very bottom of the [www.SpyBlast.com](http://www.SpyBlast.com) home page, below several hyperlinks to download SpyBlast, a small disclosure stating that “In exchange for usage of the SpyBlast software, user agrees to receive . . . offers on behalf of SpyBlast’s marketing partners” appeared.

According to the Commission’s complaint, respondents downloaded bundled adware onto the computers of consumers who installed SpyBlast. The adware collected information about SpyBlast users, including URLs of visited pages and the user’s IP address, and this information allowed respondents to send users advertisements that they believed might be of interest to them. Consumers received a substantial number of pop-up advertisements as result of respondents’ installation of this adware onto their computers.

The complaint alleges that in representing that SpyBlast is an Internet security program, respondents failed to disclose adequately that SpyBlast included adware that caused consumers to receive pop-up advertisements. The complaint further alleges that the presence of the bundled adware would have been material to consumers in their decision whether to install SpyBlast, and, therefore, that the failure to disclose adequately this material fact was a deceptive practice. This allegation regarding the disclosure of bundled adware applies general Commission law on deception, as enunciated in the *Federal Trade Commission Policy Statement on Deception, appended to Cliffdale Assocs.*, 103 F.T.C. 110, 174-83 (1984). The application of this law in an online context was illustrated in a 2000 FTC Staff Guidance Document, *Dot Com Disclosures: Information about Online Advertising*, which is available at <http://www.ftc.gov/bcp/conline/pubs/buspubs/dotcom/index.pdf>.



Analysis

The proposed consent order contains provisions designed to prevent respondents from engaging in similar acts and practices in the future. The proposed order is designed specifically to address the facts of the case at hand. However, the limitation in the proposed order to respondents' software programs whose principal function is to enhance security or privacy should not be read more broadly to suggest that the requirement for clear and prominent disclosure is necessarily limited to those situations. Moreover, the problem here was not the security software that Advertising.com disseminated with its adware. Instead, it was the respondents' practice of downloading software onto users' computers, without adequate notice and consent, that generated repeated pop-up ads as the computer users surfed the Web.

Part I of the proposed order prohibits respondents from making any representation about the performance, benefits, efficacy, or features of SpyBlast or any of respondents' other executable computer software programs whose principal function is to enhance security or privacy, unless respondents disclose clearly and conspicuously that consumers who install the program will receive advertisements, if that is the case.

Parts II through VI require respondents to keep copies of relevant advertisements and materials substantiating claims made in the advertisements; to provide copies of the order to certain of their personnel; to notify the Commission of changes in corporate structure (for the corporate respondents) and changes in employment (for the individual respondent) that might affect compliance obligations under the order; and to file compliance reports with the Commission. Part VII provides that the order will terminate after twenty (20) years under certain circumstances.

The purpose of this analysis is to facilitate public comment on the proposed order, and it is not intended to constitute an official interpretation of the agreement and proposed order or to modify in any way their terms.

Complaint

IN THE MATTER OF

**PARTNERS HEALTH NETWORK, INC.**CONSENT ORDER, ETC., IN REGARD TO ALLEGED VIOLATIONS OF  
SEC. 5 OF THE FEDERAL TRADE COMMISSION ACT*Docket C-4149; File No. 0410100**Complaint, September 19, 2005--Decision, September 19, 2005*

This consent order addresses practices used by Respondent Partners Health Network, Inc., a physician-hospital organization consisting of approximately 225 physicians; Palmetto Health Baptist Medical Center at Easley; and Cannon Memorial Hospital, in South Carolina. The order, among other things, prohibits the respondent from entering into or facilitating any agreement between or among any physicians (1) to negotiate with payors on behalf of any physician; (2) to deal, not to deal, or threaten not to deal with any payor; (3) on what terms to deal with any payor; or (4) not to deal individually with any payor, or to deal with any payor only through an arrangement involving the respondent. The order also prohibits the respondent from facilitating exchanges of information between physicians concerning whether, or on what terms, to contract with a payor, and from attempting to engage, or inducing anyone to engage in, any action prohibited by the order. In addition, the order requires the respondent to notify the Commission before entering into any arrangement to act as a messenger, or as an agent on behalf of any physicians, with payors regarding contracts, and before participating in contracting with health plans on behalf of a qualified risk-sharing joint arrangement, or a qualified clinically-integrated joint arrangement. The order also requires the respondent, at any payor's request and without penalty, to terminate its current contracts with respect to providing physician services; to distribute payor requests for contract termination to all physicians who participate in Partners Health; and to terminate all current contracts not otherwise terminated no later than one year from the date the order becomes final.

*Participants*

For the Commission: *Karan Singh, Anne R. Schenof, David R. Pender, Daniel P. Ducore, Louis Silvia, and Mark Frankena.*

For the Respondent: *F. Martin Dajani, DLA Piper Rudnick Gray Cary US LLP*

Complaint

## COMPLAINT

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

### Nature of the Case

1. This matter concerns agreements among competing physicians, acting through the Respondent, to fix prices charged to health plans and other third-party payors (“payors”), and to refuse to deal with payors except on collectively agreed upon terms. The Respondent had no legitimate justification for these agreements, which increased consumer health care costs in northwestern South Carolina.

### Respondent

2. Partners Health, a physician-hospital organization (“PHO”), is a for-profit corporation, organized, existing, and doing business under and by virtue of the laws of the State of South Carolina, with its principal address at 215 East 1st Avenue, Easley, South Carolina 29640-3038.

3. Partners Health was formed to increase the members’ negotiating leverage concerning payment terms in health contracts. Partners Health contracts with payors on behalf of its member physicians jointly, as well as on behalf of its two member hospitals separately.

## Complaint

4. Partners Health members include more than 225 physicians licensed to practice allopathic or osteopathic medicine in South Carolina, and two non-profit hospitals. The hospitals, Palmetto Health Baptist Easley and Cannon Memorial Hospital, are the only two hospitals in Pickens County, located in northwestern South Carolina. About 150 of the Partners Health physician members practice in Pickens County, and they account for approximately 75% of the physicians in the county. To be marketable in the Pickens County area, a payor's health plan must contract with a large number of physicians who are members of Partners Health.

5. Partners Health's eight-member Board of Directors consists of four physicians and four hospital administrators. The physicians on the Board are elected by the Partners Health physician members to represent the members' interests in Partners Health's affairs.

6. On health plan contracting issues, the Board of Directors receives advice from its Advisory Board, which consists of ten representatives of the physician members and two hospital member representatives.

**Jurisdiction**

7. At all times relevant to this Complaint, Partners Health has been engaged in the business of contracting with payors, on behalf of Partners Health's physician members, for the provision of physician services.

8. Except to the extent that competition has been restrained as alleged herein, a substantial majority of Partners Health physician members have been, and are now, in competition with each other for the provision of physician services in the Pickens County, South Carolina, area.

Complaint

9. Partners Health, a for-profit entity, is a corporation within the meaning of Section 4 of the Federal Trade Commission Act, as amended, 15 U.S.C. § 44.

10. The general business practices of Partners Health, and of its physician members, including the acts and practices herein alleged, are in or affect “commerce” as defined in the Federal Trade Commission Act, as amended, 15 U.S.C. § 44.

### **Overview of Physician Contracting with Payors**

11. Physicians contract with payors to establish the terms and conditions, including price terms, under which they render physician services to the subscribers to the payors’ health plans (“insureds”). Physicians entering into such contracts often agree to lower compensation to obtain access to additional patients made available by the payors’ relationship with insureds. These contracts may reduce payors’ costs and enable them to lower the price of insurance, and thereby result in lower medical care costs for insureds.

12. Absent agreements among them, otherwise competing physicians unilaterally decide whether to enter into payor contracts to provide services to insureds, and what prices they will accept pursuant to such contracts.

13. The Medicare Resource Based Relative Value Scale (“RBRVS”) is a system used by the Centers for Medicare and Medicaid Services to determine the amount to pay physicians for the services they render to Medicare patients. Generally, payors in South Carolina make contract offers to individual physicians or groups at price levels specified by some percentage of the RBRVS fee for a particular year (e.g., “110% of 2004 RBRVS”).

### **Anticompetitive Conduct**

14. Partners Health, acting as a combination of its physician members, and in conspiracy with its members, has acted to

## Complaint

restrain competition by, among other things, facilitating, entering into, and implementing agreements, express or implied, to fix the prices and other terms at which they would contract with payors; to engage in collective negotiations over terms and conditions of dealing with payors; and to have Partners Health members refrain from negotiating individually with payors or contracting on terms other than those approved by Partners Health.

15. Partners Health physician members have agreed, upon joining Partners Health, to be automatically bound by contracts that Partners Health negotiates on their behalf, unless the member opts out of the contract within 30 days after he or she receives notice of the contract. Physician members also agreed to refer insureds under Partners Health contracts only to other Partners Health physicians, except in medical emergencies.

16. Under the Partners Health contracting system, Partners Health polls its physician members to determine their fee expectations from payor contracts. Partners Health's Executive Director uses the highest of the fees received to formulate a "floor" fee schedule that he presents to payors as Partners Health's "fee expectations." Partners Health then negotiates the fees that the payor will present for the Partners Health members' consideration.

17. Under Partners Health's bylaws, the Board of Directors must approve any fee offer from a payor before the offer may be presented to the Partners Health physician members for their review. In practice, however, the Executive Director consults with the Advisory Board during contract negotiations, and the Board of Directors is merely notified of the offer terms that are to be presented to the physician members.

18. In some cases, a physician member who opts out of a Partners Health contract, or leaves Partners Health, may not individually contract with the payor due to the exclusivity provision Partners Health seeks to include in all of its contracts. Under this contract provision, payors that contract with Partners

Complaint

Health may not contract with individual physicians in Pickens County without the approval of Partners Health.

19. In 2003, after a payor objected to the Partners Health contracting system, Partners Health began referring to its contracting system as a “messenger model.” Competing physicians sometimes use a “messenger” to facilitate their contracting with payors, in ways that do not constitute an unlawful agreement on prices and other competitively significant terms. Messenger arrangements can reduce contracting costs between payors and physicians. A messenger can be an efficient conduit to which a payor submits a contract offer, with the understanding that the messenger will transmit that offer to a group of physicians and inform the payor how many physicians across specialties accept the offer or have a counteroffer. A messenger may not negotiate prices or other competitively significant terms, however, and may not facilitate coordination among physicians on their responses to contract offers.

20. Despite calling its contracting system a messenger model, Partners Health continued to negotiate with payors the price terms to be offered or paid to the Partners Health physician members.

### **Contract Negotiations with Beech Street**

21. Beech Street had both individual physician contracts with Pickens County physicians, and a letter of agreement with Partners Health for physician services dating to 1996. In November 1996, Partners Health informed Beech Street that it wanted to update the letter of agreement, and sent Beech Street its “physician fee expectations” in a fee schedule. Partners Health’s Executive Director told Beech Street that the Partners Health Board of Directors would need to approve the negotiated contract terms before the terms would be presented to the Partners Health physicians for their acceptance. After negotiating price terms, Partners Health entered into a new contract with Beech Street.

## Complaint

22. In 2001, Partners Health approached Beech Street with a request to renegotiate the prices in the contract. Beech Street began negotiations by presenting the standard fee schedule it pays most South Carolina physicians. Partners Health told Beech Street that this offer fell below a “negotiation corridor,” and presented a price list for several hundred procedures that was 18% higher than the Beech Street offer. Partners Health claimed it had developed the list based on its view of what the Partners Health members had considered acceptable in past contract negotiations.

23. Beech Street agreed to the Partners Health fee schedule, with a few modifications. After the parties agreed to the prices and contract language, the final contract was presented to the Partners Health members, who accepted the new contract terms.

**Negotiations with CCN & First Health**

24. In the summer of 2001, the Partners Health Board of Directors ordered the renegotiation of the CCN contract to get higher prices. In July 2001, Partners Health sent CCN a list of higher fees for the existing contract’s fee schedule. In response, CCN offered to pay a percentage of the Partners Health members’ billed charges. Partners Health rejected the offer and countered with rates 5-15% higher than CCN’s offer, still as a percentage of the members’ billed charges, depending on specialty.

25. CCN responded by offering fee terms of a flat percentage of 2001 Medicare RBRVS for all procedures, which Partners Health told CCN was “completely unacceptable.” Partners Health stated that it “can only agree to two different payment methodologies”: either a percentage of members’ billed charges, or a fee schedule that Partners Health sent CCN. Partners Health rejected the CCN offer without submitting it to the Partners Health physician members.

26. Partners Health terminated the CCN contract, effective February 2002, because “CCN will not agree to renegotiate with



Complaint

Partners Health based on Partners Health's historical payment expectations and methodology.”

27. Following the contract termination, Partners Health organized its members' refusal to deal with CCN so as “to strengthen Partners Health Network's position.” In December 2001, Partners Health members were instructed that “[i]f CCN makes any attempt to contact your hospital or office in the next two months then please do what you have previously done - refer them to the [Partners Health] office.” In February 2002, Partners Health's Executive Director told the Partners Health physicians to continue to refuse to deal with CCN, terminate any direct contracts they may have with CCN, and steer CCN to Partners Health.

28. CCN's attempts at direct contracts with Partners Health members during this period resulted in the physicians directing CCN to Partners Health. Meanwhile, CCN merged with First Health and sought to combine the two companies' contracts with Partners Health into a single joint agreement that still distinguished between the two companies' brand names.

29. First Health sent direct contracts to Pickens County physicians in early 2003, but the physicians either referred First Health to Partners Health or sent First Health's contracting offer materials straight to Partners Health.

30. After receiving the forwarded offers for the First Health portion of the contract, Partners Health contacted First Health and demanded that any First Health portion of the combined contract have the same percentage-of-billed-charges arrangement as in the CCN portion of the contract. First Health refused, and offered Partners Health up to four different fee schedules for the First Health portion of the contract. Partners Health rejected each one, insisted on a discount-off-billed-charges arrangement, and never sent the fee schedules to the Partners Health members.

## Complaint

31. In June of 2003, First Health agreed to take the “Partners Fee Schedule” for the First Health portion of the contract. Partners Health then presented the First Health fee offer to the Partners Health members, and they accepted it.

32. Eventually Partners Health reached a joint First Health/CCN agreement in December 2003. The CCN portion of the contract contained payment terms that were 17% higher than the original CCN offer.

**Contract Negotiations with Premier Health Systems**

33. Premier Health Systems ("Premier") has contracted with Partners since 1995. Contract renegotiations began in October 2000, when the Partners Health Executive Director told Premier that “general expectations” for a new contract included Premier’s acceptance of an attached fee schedule. Partners Health negotiated fee terms with Premier over the next ten months, ending when Premier accepted Partners Health’s fee expectations, which were 17% higher than Premier’s initial offer.

34. The Partners Health Executive Director informed the Partners Health members of Premier’s agreement to the fees in August 2001, telling them: "As customary regarding physician payment, PHN has negotiated specialized pricing for over 600 [procedures]."

35. In December 2003, Partners Health polled its members to learn what fees they would accept for a new Premier contract. The individual member practices responded with their fee requests, which varied by practice. However, Partners Health presented Premier with a single fee schedule that listed the highest requested rate among the Partners Health practices.

36. On March 10, 2004, Partners Health sent Premier an email: “Bottom line . . . [the attached fee schedule] represent[s] Partners Health’s expectation,” which averaged 12% higher than the currently contracted rates. Premier countered with a 6%

Complaint

increase over the current rates. Partners Health sent the Premier increase to its members in May 2004, and they accepted the contract.

**Contract Negotiations with United Healthcare**

37. For years, United Healthcare of South Carolina, Inc. (“United”), accessed Partners Health physician members by contracting with third-party administrator Medcost, which had contracts with Partners Health for physician services.

38. United told Partners Health in March 2003 that it wanted to contract with Partners Health directly, instead of accessing the Partners Health physician members through Medcost. United included a fee schedule for 50 procedures. Partners Health responded with a list of “payment expectations for a contract,” including a fee schedule that listed hundreds of procedures with an overall average price almost double United’s proposal. United responded with a more comprehensive counteroffer of fees than it had submitted on March 5, on average 39% higher than its original offer.

39. After receiving United’s offer, Partners Health suspended negotiations. In May 2003, Partners Health sent its members a memo detailing its decision to cease negotiations with United. Partners Health explained that the two deal-breakers were that United only wanted Partners Health to facilitate individual physician contracts, and that United would “only offer a standard/universal fee schedule (no negotiating flexibility) at rates significantly lower than Medcost.” The memo continued by stating that United’s requests “are unacceptable to Partners Health because facilitating individual agreements achieves no future clout and defensive strength . . . and accepting rates so much lower is inappropriate in a climate of increasing overhead costs.”

40. In July 2003, United sent an antitrust article on messenger arrangements to the Partners Health physician practices, and at the same time it asked Partners Health to messenger the United

## Complaint

physician fee schedule to the Partners Health members. In the August 15, 2003, Advisory Board meeting, after discussing the antitrust issues raised by United's article, the Advisory Board decided to send the first United offer to the Partners Health members, and ask them to communicate their fee expectations to the Executive Director, "who will then messenger back [to United] a comprehensive offer" for the entire membership. The Advisory Board agreed that "[i]f a majority of [Partners Health] members do not want to contract with United at all then Partners Health will suspend negotiations again."

41. On September 24, 2003, Partners Health forwarded United's original offer to its members for the first time. Along with the offer, Partners Health "polled" its members by asking them to identify their preferences for contracting with United -- either through Partners Health, another PHO, directly, or not at all. If the members wanted to contract through Partners Health, they were told to return a list of fee counteroffers for United.

42. An October 15, 2003, follow-up memo to the Partners Health members stressed that Partners Health needed 40 out of the 49 practices to choose to contract through Partners Health "to develop a credible contracting position with [United]." The memo stated "[t]he majority of [Partners Health] members . . . will only contract through Partners Health with [United] as verified by the responses already received." The memo concluded by emphasizing that Partners Health "[has] the market completely on our side in terms of access," and that "[e]mployers will drop [United] like a stone come January if there is not a full network in place as a result of severing ties with Medcost without contracting to develop [United's] own [network]."

43. Partners Health then sent its members a memorandum naming the practices that returned the polling form and fee requests, along with a list of practices that chose to contract directly with United. This memorandum bolstered the members' resolve to refuse to deal with United, and targeted the practices

Complaint

choosing to directly contract for peer pressure to conform to the group's wishes to jointly contract.

44. In February 2004, Partners Health told United that it messengered United's offers to the Partners Health members, and included what it called the "members aggregated fee expectations," in the form of a single fee schedule.

45. United has been unable to contract with Partners Health, and is still unable to contract with enough physicians to have a viable network in the Pickens County area. Moreover, Partners Health successfully pressured MedCost, through the threat of network termination, to end United's access to the Partners Health members through MedCost, effective as of July 1, 2004.

### **Contracting with Other Payors**

46. Partners Health, on behalf of its physician members, has orchestrated collective negotiations with other payors who do business, or have attempted to do business, in the Pickens County area, including Aetna, Great-West Healthcare, MedCost, Private Health Care Systems, Southcare, United Payors/United Providers, and USA Managed Care, Inc. Partners Health negotiated with these payors on price, making proposals and counter-proposals, as well as accepting or rejecting offers, without transmitting them to members for their individual acceptance or rejection. Partners Health also facilitated collective refusals to deal and threats of refusals to deal with payors. Partners Health's members collectively accepted or rejected these payor contracts, and refused to deal with these payors individually. Due to Partners Health's dominant position in the Pickens area, these coercive tactics have been successful in raising the prices paid to its physician members.

### **Respondent's Price-fixing Is Not Justified**

47. The physician members of Partners Health have not integrated their practices in any economically significant way, nor

## Complaint

have they created efficiencies sufficient to justify their acts or practices described in paragraphs 14 through 46.

**Respondent's Actions Have Had Substantial Anticompetitive Effects**

48. Respondent's actions described in Paragraphs 14 through 46 of this Complaint have had, or tend to have had, the effect of restraining trade unreasonably and hindering competition in the provision of physician services in the Pickens County area in the following ways, among others:

- a. price and other forms of competition among physician members of Partners Health were unreasonably restrained;
- b. prices for physician services were increased; and
- c. health plans, employers, and individual consumers were deprived of the benefits of competition among physicians.

**Violation of the Federal Trade Commission Act**

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

**WHEREFORE, THE PREMISES CONSIDERED,** the Federal Trade Commission on this 19<sup>th</sup> day of September, 2005, issues its Complaint against Respondent Partners Health.

Decision and Order

## **DECISION AND ORDER**

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

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

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

1. Respondent Partners Health is a for-profit corporation, organized, existing, and doing business under and by virtue of the laws of the State of South Carolina, with its principal

## Decision and Order

address located at 215 East 1st Avenue, Easley, South Carolina 29640-3038.

2. The Federal Trade Commission has jurisdiction of the subject matter of this proceeding and of the Respondent, and the proceeding is in the public interest.

**ORDER****I.**

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

- A. “Respondent Partners Health” means Partners Health Network, Inc., its officers, directors, employees, agents, attorneys, representatives, successors, and assigns; the subsidiaries, divisions, groups, and affiliates controlled by it, and the respective officers, directors, employees, agents, attorneys, representatives, successors, and assigns of each.
- B. “Hospital” means a health care facility licensed by any state as a hospital, including, but not limited to, Cannon Memorial Hospital and Palmetto Health Baptist Medical Center at Easley.
- C. “Medical Group Practice” means a bona fide, integrated firm in which physicians practice together as partners, shareholders, owners, or employees, or in which only one physician practices.
- D. “Participate” in an entity means (1) to be a partner, shareholder, owner, member, or employee of such entity, or (2) to provide services, agree to provide services, or offer to provide services, to a payor through such entity. This definition applies to all tenses and forms of the word “participate,” including, but not limited to, “participating,” “participated,” and “participation.”



Decision and Order

- E. “Payor” means any person that pays, or arranges for payment, for all or any part of any physician services for itself or for any other person. Payor includes any person that develops, leases, or sells access to networks of physicians.
- F. “Person” means both natural persons and artificial persons, including, but not limited to, corporations, unincorporated entities, and governments.
- G. “Physician” means a doctor of allopathic medicine (“M.D.”) or a doctor of osteopathic medicine (“D.O.”).
- H. “Preexisting contract” means a contract for the provision of physician services that was in effect on the date of the receipt by a payor that is a party to such contract of notice sent by Respondent Partners Health, pursuant to Paragraph V.A.3 of this Order, of such payor’s right to terminate such contract.
- I. “Principal address” means either (1) primary business address, if there is a business address, or (2) primary residential address, if there is no business address.
- J. “Qualified clinically-integrated joint arrangement” means an arrangement to provide physician services in which:
  - 1. all physicians that participate in the arrangement participate in active and ongoing programs of the arrangement to evaluate and modify the practice patterns of, and create a high degree of interdependence and cooperation among, the physicians that participate in the arrangement, in order to control costs and ensure the quality of services provided through the arrangement; and
  - 2. any agreement concerning price or other terms or conditions of dealing entered into by or within the arrangement is reasonably necessary to obtain significant efficiencies through the arrangement.

## Decision and Order

- K. “Qualified risk-sharing joint arrangement” means an arrangement to provide physician services in which:
1. all physicians that participate in the arrangement share substantial financial risk through their participation in the arrangement and thereby create incentives for the physicians that participate jointly to control costs and improve quality by managing the provision of physician services, such as risk-sharing involving:
    - a. the provision of physician services to payors at a capitated rate,
    - b. the provision of physician services for a predetermined percentage of premium or revenue from payors,
    - c. the use of significant financial incentives (*e.g.*, substantial withholds) for physicians that participate to achieve, as a group, specified cost-containment goals, or
    - d. the provision of a complex or extended course of treatment that requires the substantial coordination of care by physicians in different specialties offering a complementary mix of services, for a fixed, predetermined price, where the costs of that course of treatment for any individual patient can vary greatly due to the individual patient’s condition, the choice, complexity, or length of treatment, or other factors; and
  2. any agreement concerning price or other terms or conditions of dealing entered into by or within the arrangement is reasonably necessary to obtain significant efficiencies through the arrangement.
- L. “Upstate South Carolina Area” means the area of South Carolina that comprises Pickens, Oconee, Greenville, and Anderson Counties.

Decision and Order

**II.**

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

- A. Entering into, adhering to, participating in, maintaining, organizing, implementing, enforcing, or otherwise facilitating any combination, conspiracy, agreement, or understanding between or among any physicians:
  - 1. to negotiate on behalf of any physician with any payor;
  - 2. to deal, refuse to deal, or threaten to refuse to deal with any payor;
  - 3. regarding any term, condition, or requirement upon which any physician deals, or is willing to deal, with any payor, including, but not limited to, price terms; or
  - 4. not to deal individually with any payor, or not to deal with any payor through any arrangement other than Respondent Partners Health;
- B. Exchanging or facilitating in any manner the exchange or transfer of information between or among physicians concerning any physician’s willingness to deal with a payor, or the terms or conditions, including any price terms, on which the physician is willing to deal with a payor;
- C. Attempting to engage in any action prohibited by Paragraphs II.A or II.B above; and

## Decision and Order

- D. Encouraging, suggesting, advising, pressuring, inducing, or attempting to induce any person to engage in any action that would be prohibited by Paragraphs II.A through II.C above.

**PROVIDED HOWEVER**, that, subject to the requirements of Paragraph IV of this Order, nothing in this Paragraph II shall prohibit any agreement involving, or any conduct that is reasonably necessary to form, participate in, or take any action in furtherance of a qualified risk-sharing joint arrangement or a qualified clinically-integrated joint arrangement that does not restrict the ability, or facilitate the refusal, of physicians who participate in it to deal with payors on an individual basis or through any other arrangement, or that solely involves physicians in the same medical group practice.

**III.**

**IT IS FURTHER ORDERED** that, for three (3) years after the date this Order becomes final, Respondent Partners Health shall notify the Secretary of the Commission in writing (“Paragraph III Notification”) at least sixty (60) days prior to entering into any arrangement with any physicians or any medical group practices under which Respondent Partners Health would act as a messenger, or as an agent on behalf of those physicians or those medical group practices, with payors regarding contracts. The Paragraph III Notification shall include the identity of each proposed physician participant; the proposed geographic area in which the proposed arrangement will operate; a copy of any proposed physician participation agreement; a description of the proposed arrangement’s purpose and function; a description of any resulting efficiencies expected to be obtained through the arrangement; and a description of procedures to be implemented to limit possible anticompetitive effects, such as those prohibited by this Order. Paragraph III Notification is not required for Respondent Partners Health’s subsequent acts as a messenger pursuant to an arrangement for which this Paragraph III Notification has been given. Receipt by the Commission of any Paragraph III Notification, pursuant to Paragraph III of the Order,

Decision and Order

is not to be construed as a determination by the Commission that any action described in such Paragraph III Notification does or does not violate this Order or any law enforced by the Commission.

**IV.**

**IT IS FURTHER ORDERED** that, for three (3) years from the date this Order becomes final, pursuant to each qualified clinically-integrated joint arrangement or qualified risk-sharing joint arrangement (“Arrangement”) in which Respondent Partners Health is a participant, Respondent Partners Health shall notify the Secretary of the Commission in writing (“Paragraph IV Notification”) at least sixty (60) days prior to:

- A. Participating in, organizing, or facilitating any discussion or understanding with or among any physicians or medical group practices in such Arrangement relating to price or other terms or conditions of dealing with any payor; or
- B. Contacting a payor, pursuant to an Arrangement, to negotiate or enter into any agreement relating to price or other terms or conditions of dealing with any payor, on behalf of any physician in such Arrangement.

**PROVIDED, HOWEVER,** that Paragraph IV Notification shall not be required for an Arrangement whenever such Notification has been previously given for that Arrangement.

**PROVIDED FURTHER:**

- 1. that with respect to any Paragraph IV Notification, Respondent Partners Health shall include the following information:

## Decision and Order

- a. the identity of each physician participant, the medical or other physician specialty, group practice, if applicable, and the name of each hospital where the physician has privileges;
  - b. a description of the Arrangement and its purpose, function, and geographic area of operation;
  - c. a description of the nature and extent of the integration and the efficiencies resulting from the Arrangement;
  - d. an explanation of how any agreement on prices, or on contract terms related to price, furthers the integration and achievement of the efficiencies resulting from the Arrangement;
  - e. a description of any procedures proposed to be implemented to limit possible anticompetitive effects resulting from the Arrangement or its activities; and
  - f. all studies, analyses, and reports that were prepared for the purpose of evaluating or analyzing competition for physician services in the Upstate South Carolina Area or in Pickens County, South Carolina, including, but not limited to, the market share of physician services in such market(s); and
2. if, within sixty (60) days from the Commission's receipt of the Paragraph IV Notification, a representative of the Commission makes a written request for additional information to Respondent Partners Health, then Respondent Partners Health shall not engage in any conduct described in Paragraph IV.A or Paragraph IV.B of this Order prior to the expiration of thirty (30) days after substantially complying with such request for additional information, or such shorter waiting period as may be granted in writing from the Bureau of Competition. The expiration of any waiting period described herein without a

Decision and Order

request for additional information or without the initiation of an enforcement proceeding shall not be construed as a determination by the Commission, or its staff, that a violation of the law, or of this Order, may not have occurred. Further, receipt by the Commission from Respondent Partners Health of any Paragraph IV Notification, pursuant to Paragraph IV of this Order, is not to be construed as a determination by the Commission that any such Arrangement does or does not violate this Order or any law enforced by the Commission.

**V.**

**IT IS FURTHER ORDERED** that Respondent Partners Health shall:

- A. Within thirty (30) days after the date on which this Order becomes final, send a copy of this Order and the Complaint by first-class mail:
  1. with delivery confirmation, to each physician and hospital that participates in Respondent Partners Health;
  2. with return receipt requested, to each present officer, director, manager, and employee of Respondent Partners Health; and
  3. with return receipt requested, and with the letter attached as Appendix A to this Order, to the chief executive officer of each payor with whom Respondent Partners Health has a record of being in contact since January 1, 2001, regarding contracting for the provision of physician services; *provided, however*, that a copy of Exhibit A need not be included in the mailings to those payors with whom Respondent Partners Health has not entered into or renewed (including any automatic renewal of) a contract since January 1, 2001.

## Decision and Order

- B. For a period of three (3) years after the date this Order becomes final:
1. Distribute by first-class mail, return receipt requested, a copy of this Order and the Complaint to:
    - a. each physician and hospital that begins participating in Respondent Partners Health, and that did not previously receive a copy of this Order and the Complaint from Respondent Partners Health, within thirty (30) days of the day that such participation begins;
    - b. each payor that contracts with Respondent Partners Health for the provision of physician services, and that did not previously receive a copy of this Order and the Complaint from Respondent Partners Health, within thirty (30) days of the day that such payor enters into such contract; and
    - c. each person who becomes an officer, director, manager, or employee of Respondent Partners Health, and who did not previously receive a copy of this Order and the Complaint from Respondent Partners Health, within thirty (30) days of the day that he or she assumes such responsibility with Respondent Partners Health; and
  2. Annually publish a copy of this Order and the Complaint in an official annual report or newsletter sent to all physicians who participate in Respondent Partners Health, with such prominence as is given to regularly featured articles;
- C. File a verified written report within sixty (60) days after the date on which this Order becomes final, annually thereafter for three (3) years on the anniversary of the date this Order becomes final, and at such other times as the Commission may by written notice require. Each such report shall include:



Decision and Order

1. A detailed description of the manner and form in which Respondent Partners Health has complied and is complying with this Order;
  2. The name, address, and telephone number of each payor with which Respondent Partners Health has had any contact; and
  3. Copies of the delivery confirmations required by Paragraph V.A.1 of this Order, and copies of the signed return receipts required by Paragraphs V.A.2, V.A.3, V.B.1, and V.E of this Order;
- D. Terminate, without penalty or charge, and in compliance with any applicable laws, any preexisting contract with any payor for the provision of physician services, at the earliest of:
1. the termination date specified in a written request from a payor to Respondent Partners Health to terminate such contract;
  2. the earliest termination or renewal date (including any automatic renewal date) of such contract; or
  3. one year from the date this Order becomes final.

**PROVIDED, HOWEVER,** a preexisting contract may extend beyond any such termination or renewal date no later than one (1) year from the date that the Order becomes final if, prior to such termination or renewal date, (a) the payor submits to Respondent Partners Health a written request to extend such contract to a specific date no later than one (1) year from the date that this Order becomes final, and (b) Respondent Partners Health has determined not to exercise any right to terminate;

**PROVIDED FURTHER,** that any payor making such request to extend a contract retains the right, pursuant to part (1) of

## Decision and Order

Paragraph V.D of this Order, to terminate the contract at any time; and

- E. Within ten (10) days of receiving a written request from a payor, pursuant to Paragraph V.D (1) of this Order, distribute, by first-class mail, return receipt requested, a copy of that request to each physician and hospital participating in Respondent Partners Health as of the date Respondent Partners Health receives such request.

**VI.**

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

**VII.**

**IT IS FURTHER ORDERED** that Respondent Partners Health shall notify the Commission of any change in its principal address within twenty (20) days of such change in address.

**VIII.**

**IT IS FURTHER ORDERED** that, for the purpose of determining or securing compliance with this Order, Respondent Partners Health shall permit any duly authorized representative of the Commission:

- A. Access, during office hours and in the presence of counsel, to inspect and copy all books, ledgers, accounts, correspondence, memoranda, calendars, and other records

Decision and Order

and documents in its possession, or under its control,  
relating to any matter contained in this Order; and

- B. Upon five (5) days' notice, and in the presence of counsel, and without restraint or interference from it, to interview officers, directors, or employees of the Respondent.

**IX.**

**IT IS FURTHER ORDERED** that this Order shall terminate twenty (20) years from the date it is issued.

Decision and Order

**Appendix A**

[letterhead of Respondent Partners Health]

[date]

[name and address of payor's CEO]

Dear [CEO]:

Enclosed is a copy of a complaint and a decision and order (“Order”) issued by the Federal Trade Commission against Partners Health Network, Inc. (“Partners Health”).

Pursuant to Paragraph V.D of the Order, Partners Health must allow you to terminate, upon your written request, without any penalty or charge, any contracts with Partners Health for the provision of physician services that are in effect as of the date you receive this letter.

If you do not make such written request to terminate the contract, Paragraph V.D further provides that the contract will terminate on the earlier of:

1. [date], the contract's termination or renewal date; or
2. [date], one year from the date the Order becomes final.

You may, however, ask Partners Health to extend the contract beyond [date], the termination or renewal date, to any date no later than [date], one (1) year after the date the Order becomes final.

If you choose to extend the term of the contract, you may later terminate the contract at any time.

Any request either to terminate or to extend the contract should

Decision and Order

be made in writing, and sent to me at the following address:  
[address].

Sincerely,

[signatory]

[Partners Health to fill in applicable dates]

## Analysis

**Analysis of Agreement Containing Consent Order to Aid  
Public Comment**

The Federal Trade Commission has accepted, subject to final approval, an agreement containing a proposed consent order with Partners Health Network, Inc. The agreement settles charges that Partners Health violated Section 5 of the Federal Trade Commission Act, 15 U.S.C. § 45, by orchestrating and implementing agreements among members of Partners Health to fix prices and other terms on which they would deal with health plans, and to refuse to deal with such purchasers except on collectively-determined terms. The proposed consent order has been placed on the public record for 30 days to receive comments from interested persons. Comments received during this period will become part of the public record. After 30 days, the Commission will review the agreement and the comments received, and will decide whether it should withdraw from the agreement or make the proposed order final.

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

**The Complaint**

The allegations of the complaint are summarized below.

Partners Health is a physician-hospital organization consisting of approximately 225 physicians, Palmetto Health Baptist Medical Center at Easley, and Cannon Memorial Hospital. Partners Health does business in the Pickens, South Carolina, area, which is located in northwestern South Carolina. Partners Health was “created to develop, negotiate, enter into, and administer

Analysis

contracts” for its physician members, and its “primary function” is described as “centralized managed care contracting.”

Partners Health’s physician members account for approximately 75% of the physicians independently practicing (that is, those not employed by area hospitals) in and around the Pickens County area. To be marketable in this area, a health plan must have access to a large number of physicians who are members of Partners Health.

Although Partners Health purports to operate as a “messenger model”<sup>1</sup> – that is, an arrangement that does not facilitate horizontal agreements on price – it orchestrated such price agreements. The Partners Health Executive Director negotiates physician contracts with payors using a physician fee schedule that he created with input from the Partners Health physician members. This contracting process is overseen from start to finish by the Advisory Board and the Board of Directors. The Advisory Board is a 12-member committee that provides consultation to both the Board of Directors and the Executive Director during contract negotiations.

The Executive Director creates the Partners Health fee schedule by first polling the Partners Health physician practices to determine what prices they would like to receive in managed care contracts. The Executive Director then takes the highest prices he receives from among the physicians’ responses for a given medical procedure, and assembles those highest prices into

---

<sup>1</sup> Some arrangements can facilitate contracting between health care providers and payors without fostering an illegal agreement among competing physicians on fees or fee-related terms. One such approach, sometimes referred to as a “messenger model” arrangement, is described in the 1996 Statements of Antitrust Enforcement Policy in Health Care jointly issued by the Federal Trade Commission and U.S. Department of Justice, at 125. See <http://www.ftc.gov/reports/hlth3s.htm#9>.

## Analysis

a single fee schedule. The Executive Director uses this fee schedule to negotiate contract terms with health plans. Whenever a health plan rejects the Partners Health fee schedule, Partners Health's Executive Director negotiates, in consultation with the Advisory Board, a contract with a "comparable" fee schedule. After notifying the Board of Directors, the Executive Director transmits these contract terms to the Partners Health member practices for their review. Physician members are automatically bound by the contract unless they specifically opt out within 30 days of receiving the offer.

When they join Partners Health, the physician members agree to refer the patients they see under Partners Health contracts only to other Partners Health physicians, except in medical emergencies. This requirement stands even if non-Partners Health physicians are in the contracted payor's network.

Partners Health has orchestrated collective agreements on fees and other terms of dealing with health plans, carried out collective negotiations with health plans, fostered refusals to deal, and threatened to refuse to deal with health plans that resisted Partners Health's desired terms. Partners Health succeeded in forcing numerous health plans to raise the fees paid to Partners Health physician members, and thereby raised the cost of medical care in the Pickens County area. Partners Health engaged in no efficiency-enhancing integration sufficient to justify joint negotiation of fees. By the acts set forth in the Complaint, Partners Health violated Section 5 of the FTC Act.

**The Proposed Consent Order**

The proposed order is designed to remedy the illegal conduct charged in the complaint and prevent its recurrence. It is similar to recent consent orders that the Commission has issued to settle charges that physician groups engaged in unlawful agreements to raise fees they receive from health plans.



Analysis

The proposed order's specific provisions are as follows:

Paragraph II.A prohibits Partners Health from entering into or facilitating any agreement between or among any physicians: (1) to negotiate with payors on any physician's behalf; (2) to deal, not to deal, or threaten not to deal with payors; (3) on what terms to deal with any payor; or (4) not to deal individually with any payor, or to deal with any payor only through an arrangement involving Partners Health.

Other parts of Paragraph II reinforce these general prohibitions. Paragraph II.B prohibits Partners Health from facilitating exchanges of information between physicians concerning whether, or on what terms, to contract with a payor. Paragraph II.C bars attempts to engage in any action prohibited by Paragraph II.A or II.B, and Paragraph II.D proscribes Partners Health from inducing anyone to engage in any action prohibited by Paragraphs II.A through II.C.

As in other Commission orders addressing providers' collective bargaining with health care purchasers, certain kinds of agreements are excluded from the general bar on joint negotiations. Partners Health would not be precluded from engaging in conduct that is reasonably necessary to form or participate in legitimate joint contracting arrangements among competing physicians in a "qualified risk-sharing joint arrangement" or a "qualified clinically-integrated joint arrangement." The arrangement, however, must not facilitate the refusal of, or restrict, physicians in contracting with payors outside of the arrangement.

As defined in the proposed order, a "qualified risk-sharing joint arrangement" possesses two key characteristics. First, all physician participants must share substantial financial risk through the arrangement, such that the arrangement creates incentives for the physician participants jointly to control costs and improve quality by managing the provision of services. Second, any agreement concerning reimbursement or other terms or conditions

## Analysis

of dealing must be reasonably necessary to obtain significant efficiencies through the joint arrangement.

A “qualified clinically-integrated joint arrangement,” on the other hand, need not involve any sharing of financial risk. Instead, as defined in the proposed order, physician participants must participate in active and ongoing programs to evaluate and modify their clinical practice patterns in order to control costs and ensure the quality of services provided, and the arrangement must create a high degree of interdependence and cooperation among physicians. As with qualified risk-sharing arrangements, any agreement concerning price or other terms of dealing must be reasonably necessary to achieve the efficiency goals of the joint arrangement.

Paragraph III, for three years, requires Partners Health to notify the Commission before entering into any arrangement to act as a messenger, or as an agent on behalf of any physicians, with payors regarding contracts. Paragraph III also sets out the information necessary to make the notification complete.

Paragraph IV, for three years, requires Partners Health to notify the Commission before participating in contracting with health plans on behalf of a qualified risk-sharing joint arrangement, or a qualified clinically-integrated joint arrangement. The contracting discussions that trigger the notice provision may be either among physicians, or between Partners Health and health plans. Paragraph IV also sets out the information necessary to satisfy the notification requirement.

Paragraph V requires Partners Health to distribute the complaint and order to all physicians who have participated in Partners Health, and to payors that negotiated contracts with Partners Health or indicated an interest in contracting with Partners Health. Paragraph V.D requires Partners Health, at any payor’s request and without penalty, or, at the latest, within one year after the order is made final, to terminate its current contracts with respect to providing physician services. Paragraph V.D. also

Analysis

allows any contract currently in effect to be extended, upon mutual consent of Partners Health and the contracted payor, to any date no later than one year from when the order became final. This extension allows both parties to negotiate a termination date that would equitably enable them to prepare for the impending contract termination. Paragraph V.E requires Partners Health to distribute payor requests for contract termination to all physicians who participate in Partners Health.

Paragraphs VI, VII, and VIII of the proposed order impose various obligations on Partners Health to report or provide access to information to the Commission to facilitate monitoring Partners Health's compliance with the order.

The proposed order will expire in 20 years.

Commission Opinion

## IN THE MATTER OF

**TELEBRANDS CORP., TV SAVINGS, LLC, AND AJIT  
KHUBANI**OPINION OF THE COMMISSION AND FINAL ORDER IN REGARD TO  
ALLEGED VIOLATIONS OF SEC. 5 OF THE  
FEDERAL TRADE COMMISSION ACT*Docket 9313; File No. 0223279**Complaint, Sept. 30, 2003--Opinion and Final Order, Sept. 19, 2005*

In a unanimous Opinion, the Commission addressed advertising practices used by Respondents Telebrands Corporation and TV Savings, L.L.C. – and their principal, Respondent Ajit Khubani – for the Ab Force, a belt-like device that uses electronic stimulation (“EMS”) to cause involuntary contraction of the muscles of the abdominal wall, and determined that certain of these practices violated Section 5 of the Federal Trade Commission Act. The Final Order, among other things, prohibits the respondents – in connection with the manufacturing, labeling, advertising, promotion, offering for sale, sale, or distribution of the Ab Force EMS device or any substantially similar device – from representing (1) that any such device causes or promotes loss of weight, inches, or fat; (2) that any such device causes or promotes well-defined abdominal muscles; (3) that use of any such device for any period of time is an effective alternative to regular exercise; or (4) that any such device makes a material contribution to any system, program, or plan that produces the results described in the first three clauses. The Order also prohibits the respondents from misrepresenting – in connection with the manufacturing or marketing of any EMS device – (1) that any such device causes or promotes loss of weight, inches, or fat; (2) that any such device causes or promotes well-defined abdominal muscles; (3) that use of any such device for any period of time is an effective alternative to regular exercise; or (4) that any such device makes a material contribution to any system, program, or plan that produces the results described in the first three clauses.

*Participants*

For the Commission: *Constance M. Vecellio, Walter C. Gross, III, Joshua S. Millard, Amy M. Lloyd, James Reilly Dolan, Elaine D. Kolish, James A. Kohm, Russell Porter, Susan P. Braman, and Gerard R. Butters.*

For the Respondent: *Edward F. Glynn, Jr. and Theodore W. Atkinson, Venable LLP.*

Commission Opinion

## OPINION OF THE COMMISSION

By LEIBOWITZ, Commissioner, For A Unanimous Commission:

This is a case about firm abs and phony ads. It illustrates how false and unsubstantiated claims can be communicated indirectly but with utter clarity – to the detriment of consumers and in violation of the laws this Commission enforces.

Respondents Telebrands Corporation (“Telebrands”), TV Savings, L.L.C. (“TV Savings”), and their principal, Ajit Khubani, appeal from Administrative Law Judge (“ALJ”) Stephen J. McGuire’s Initial Decision and Order holding them liable for violating Sections 5 and 12<sup>1</sup> of the Federal Trade Commission Act (“FTC Act”), 15 U.S.C. §§ 45 and 52, by using unsubstantiated claims in multiple media to promote the “Ab Force,” a belt-like device that uses electronic stimulation to cause involuntary contraction of muscles in the abdominal wall. Complaint counsel cross-appeal the scope of the order’s coverage. We affirm liability under Sections 5 and 12 and partially modify the ALJ’s Order.

From December 2001 to at least April 2002, respondents marketed the Ab Force belt on television, radio, the Internet, and in print. On September 30, 2003, the Commission issued an administrative complaint charging respondents with making unsubstantiated claims that the Ab Force (1) causes loss of weight,

---

<sup>1</sup> Section 5 of the FTC Act, 15 U.S.C. § 45, prohibits “unfair or deceptive acts or practices.” Section 12 of the FTC Act, 15 U.S.C. § 52, prohibits the dissemination of any false advertisement that is likely to induce the purchase of food, drugs, devices, services, or cosmetics. A “false advertisement” is any advertisement that is “misleading in a material respect.” 15 U.S.C. § 55(a)(1). Under Section 15 of the FTC Act, 15 U.S.C. § 55(d), a “device” includes “an instrument, apparatus, implement, machine, [or] contrivance \*\*\* which is \*\*\* intended to affect the structure or any function of the body of a man.”

## Commission Opinion

inches, or fat; (2) creates well-defined abdominal muscles; and (3) is an effective alternative to regular exercise. According to the complaint, respondents' failure to substantiate such claims constitutes an unfair or deceptive act or practice and the making of false advertisements in violation of Sections 5 and 12 of the FTC Act.

The ALJ found that the product name, visual images, and statements in respondents' advertising create the net impression that the Ab Force electronic muscle stimulation ("EMS") device provides health, fitness, weight loss, or exercise benefits; that those claims were false and misleading; and that the claims were material to consumers' purchasing decisions. ID at 41-43, 60-61.<sup>2</sup> Accordingly, he entered an order prohibiting respondents, *inter alia*, from representing that the Ab Force, or any substantially similar device, causes loss of weight, inches, or fat; promotes well-defined muscles; or is an effective alternative to exercise. Order ¶ II. The order also prohibits respondents from making such misrepresentations, expressly or by implication, about any EMS device. Order ¶ III. Paragraph IV of the ALJ's order further prohibits respondents from making any representation regarding, *inter alia*, the safety, efficacy, or benefits of any EMS device, or any product, service, or program relating to health, weight loss, fitness, and exercise without "competent and

---

<sup>2</sup> References to the record are abbreviated as follows:

IDF Initial Decision Finding

ID Initial Decision

Tr. Transcript of Trial Testimony

CX Complaint Counsel's Exhibit

RX Respondents' Exhibit

JX Joint Exhibit

RAB Respondents' Appeal Brief

CAB Complaint Counsel's Answering and Cross-Appeal Brief

RRB Respondents' Brief in Reply to Complaint Counsel's  
Brief in Opposition to Respondent's Appeal and in  
Opposition to Complaint Counsel's Cross-Appeal

Commission Opinion

reliable scientific evidence” that substantiates the representation. Order ¶ IV.

Respondents’ principal contention on appeal is that the ALJ erred in finding that their advertising for the Ab Force conveyed the challenged claims. Complaint counsel cross-appeal the ALJ’s refusal to order fencing-in relief<sup>3</sup> that would require respondents to substantiate all claims about weight, inch, or fat loss; muscle definition; or the health benefits, safety, or efficacy of any of respondents’ products, services, or programs. Complaint counsel also appeal the ALJ’s refusal to require respondent Khubani to obtain a performance bond of \$1 million to prevent future violations.

Based on our consideration of the entire record in this case and the arguments of counsel, we deny respondents’ appeal and grant in part, and deny in part, complaint counsel’s cross-appeal. We agree with the ALJ’s findings of fact and conclusions of law to the extent they are consistent with those set forth in this opinion and, except as noted herein, adopt them as our own. The Order we issue today supplements the fencing-in relief ordered by the ALJ with a provision prohibiting respondents from making claims about the health benefits, safety, or efficacy of any product, service, or program unless they possess and rely upon substantiation for their claims. With regard to complaint counsel’s request that respondent Khubani be required to post a performance bond, complaint counsel have not made an adequate showing that the \$1 million bond is appropriate in this case. Thus, although we reject respondents’ contention that the

---

<sup>3</sup> “Fencing-in” relief refers to provisions in a final Commission order that are broader in scope than the conduct that is declared unlawful. Fencing-in remedies are designed to prevent future unlawful conduct. *See, e.g., FTC v. Colgate-Palmolive Co.*, 380 U.S. 374, 395 (1965); *Kraft, Inc. v. FTC*, 970 F.2d 311, 326 (7th Cir. 1992).

## Commission Opinion

Commission lacks authority to impose such relief, we decline to order it in this case.

**I. Factual Background and Proceedings Below**

Respondent Telebrands develops, markets, and distributes a wide array of consumer products. IDF 4. It has marketed hundreds of products since 1987, principally through “direct response” advertising. IDF 3, 4, 20, 22; Khubani Tr. 435. Direct response advertising can include program-length infomercials, live TV shopping, or any medium that allows consumers to order products directly from the advertiser. IDF 17-19; Khubani Tr. 431-34.

Telebrands is solely owned by respondent Ajit Khubani, who oversaw the Ab Force promotional campaign and had primary responsibility for developing scripts for radio and TV advertising. IDF 10, 16. As President, CEO, and Chairman of the Board, he sets the general direction of the business and is heavily involved in new product development. IDF 10, 14-16; Khubani, Tr. 247. He tracks trends in the marketplace and in various channels of advertising, using industry publications that collect data and rank direct-response ads on a weekly basis. IDF 126; Khubani Tr. 248-50.

Several times a year, based on Mr. Khubani’s assessment of market trends, Telebrands enters the market by offering a product at a lower price than offered by competitors already in the market for the same or similar products. IDF 25; Khubani Tr. 247-48. Once Telebrands decides to market a particular product, it creates “test” advertising. IDF 26-27; Khubani Tr. 440. The term “test” ad is used throughout these proceedings to refer to ads that accompanied the product’s initial release and were run on a limited basis by respondents so that they could make a prediction as to a product’s likely success before committing to a full-scale national advertising campaign. IDF 27-31. The “test” ads were not simply shown to consumers who participated in focus groups or other types of consumer perception research, but were aired in



Commission Opinion

selected markets for limited periods of time and generated actual sales. IDF 30, 44-45, 49. If consumers respond to the “test” advertising, Telebrands proceeds with a full-scale rollout of the new product promotion. IDF 31; Khubani Tr. 440-42. Respondents purport to conduct a review of the ads “from a claims perspective and a compliance perspective” before mounting a full-fledged national advertising campaign. Khubani Tr. 442; IDF 32-33.

Respondents’ business practices have drawn Commission scrutiny in the past. Since 1990, Mr. Khubani has entered three separate agreements with the Commission – in two cases, relating to Telebrands’ practices – resolving alleged violations of the Commission’s Mail Order Rule. Mr. Khubani and Telebrands also settled a separate action relating to false or unsubstantiated claims for two products, and misrepresentations about the company’s money-back guarantee. Mr. Khubani and Telebrands paid more than \$900,000 in civil penalties to resolve these actions.<sup>4</sup>

Respondents entered the market for EMS abdominal (“ab”) belts in December 2001. IDF 62. Mr. Khubani believed that ab belts – including the AbTronic, Ab Energizer, and Fast Abs – represented “one of the hottest categories to ever hit the industry.”<sup>5</sup> IDF 63 (*quoting* Khubani Tr. 255). Ads for the AbTronic, Ab Energizer, and Fast Abs were among the most frequently aired infomercials in 2001 and early 2002. Indeed, according to a direct response television industry publication, the

---

<sup>4</sup> See n.58, *infra*.

<sup>5</sup> Respondent TV Savings, L.L.C., a Connecticut limited liability company, was created to handle respondents’ promotional campaign for the Ab Force. IDF 7, 9-10.

## Commission Opinion

*J.W. Greensheet*,<sup>6</sup> infomercials for the AbTronic, Ab Energizer, and Fast Abs brands were among the 50 most frequently disseminated infomercials in the United States on numerous occasions between September 2001 and March 2002. IDF 125, 127-34. Ads for two of these products also appeared 34 times in the top 40 direct response spot rankings, as published by the *J.W. Greensheet*, in 2001 and 2002. IDF 131, 133.

The AbTronic, Ab Energizer, and Fast Abs belts are substantially similar in appearance to the Ab Force belt, IDF 119, and advertisements for them contain substantially similar images of well-muscled, bare-chested men and lean, shapely women wearing EMS devices around the waist and experiencing abdominal contractions. *Compare JX 2-5 with JX 7-9*; IDF 73-76, 78, 83, 119-24. They also depict men and women performing conventional abdominal exercises and close-ups of men and women showing off their trim waists and well-defined abdominals. IDF 119-24. The infomercials contain express and strongly implied claims that the ab belts are an effective alternative to exercise, and will cause users to develop tighter abdominals and lose inches, fat, or weight. IDF 120. According to industry monitoring services, more than 5,000 infomercials for the AbTronic, Fast Abs, and Ab Energizer aired from April 2001 to February 2002.<sup>7</sup> CX 126.

---

<sup>6</sup> The *J.W. Greensheet* is published for the direct response television industry on a weekly basis. IDF 125. Each issue contains a top 50 ranking of infomercials, a top 40 ranking of television spot ads, and a top 20 ranking of infomercial products. IDF 127. Its rankings are compiled on the basis of confidential media budgets and its own monitoring of national cable and selected broadcast markets. IDF 128. At the time of trial in this case, respondent Telebrands had subscribed to the *J.W. Greensheet* for about 12 years. IDF 126.

<sup>7</sup> In addition to infomercials, the AB Energizer and Fast Abs belts were advertised in short spot ads. IDF 131, 133.

## Commission Opinion

The Commission, under Section 13(b) of the FTC Act, 15 U.S.C. § 53(b), filed actions for permanent injunctive and equitable monetary relief against marketers of the AbTronic, Ab Energizer, and Fast Abs in May 2002, alleging that their advertisements made false representations that the devices were an effective alternative to exercise and caused users to lose weight, inches, and fat. IDF 135. In July 2003, the Commission settled with marketers of the Fast Abs device for a stipulated permanent injunction and more than \$5 million in equitable monetary relief. *FTC v. United Fitness of America, LLC*, CV-S-02-0648-KJD-LRL (D. Nev. July 24, 2003). In the AbTronic case, the Commission was awarded a permanent injunction and a judgment holding the defendants jointly and severally liable for \$83 million. *FTC v. Hudson Berkley Corp.*, No. CV-S-02-0649-PMP-RJJ (D. Nev. June 30, 2003). In April 2005, the Commission settled with marketers of the AB Energizer for a permanent injunction and more than \$80 million in equitable monetary relief. *FTC v. Electronic Products Distribution, LLC*, No. 02-CV-888-BEN (AJB) (S.D. Cal. April 26, 2005).<sup>8</sup>

Believing that he could sell an EMS ab belt device for significantly less than they were being offered in infomercials, Mr. Khubani contacted an overseas manufacturer and, with that company, began to develop an EMS ab belt based on the same technology. IDF 37, 39; Khubani Tr. 263-64, 534. In fact, the same manufacturer also produced the AbTronic, one of the competing EMS belts. IDF 38. Mr. Khubani settled on the name “Ab Force” for his product because, as he explained at trial, “it was designed to work primarily on the abdominal area” and it was “catchy, sort of like Air Force.” IDF 69 (*quoting* Khubani Tr. 264). In less than four months, respondents sold more than 700,000 Ab Force units and accessories, grossing more than \$19 million. IDF 41-42, 44, 46, 49-51.

---

<sup>8</sup> See also IDF 119-24 (describing the AbTronic, Ab Energizer, and Fast Abs advertisements and the claims communicated in those infomercials).

## Commission Opinion

On September 30, 2003, the Commission issued an administrative complaint pursuant to Section 5(a) of the FTC Act, 15 U.S.C. § 45(a), charging respondents with making false and unsubstantiated claims that the Ab Force (1) causes loss of weight, inches, or fat; (2) creates well-defined abdominal muscles; and (3) is an effective alternative to regular exercise. Respondents stipulated that they had no substantiation for these claims. *See* JX 6 ¶¶ 16-19. They denied, however, that the alleged claims were conveyed by their Ab Force advertising.

After a three-day trial, the ALJ rendered a 72-page initial decision. Based on the interaction between and among various elements in the ads – the product name, visual images, text, and surrounding circumstances – the ALJ concluded that respondents’ ads strongly and clearly conveyed the alleged claims. ID at 41-43. The ALJ explained that the name of the product – “Ab Force” – suggests that the device “applies a force to the abdominal muscles and also implies that use of the device will make the abdominal muscles more forceful.” IDF 70; *see* ID at 41. In addition, the ALJ relied on the visual images in respondents’ TV advertising – *e.g.*, pulsating abdominal muscles; trim and fit male and female models; a male model performing abdominal crunches. IDF 73-76, 83. These visual images, he explained, “are effective in conveying claims and may also be used to determine implied claims.” ID at 41, *citing Kraft, Inc.*, 114 F.T.C. 40, 122-23 (1991), *aff’d*, 970 F.2d 311 (7th Cir. 1992), *cert. denied*, 507 U.S. 909 (1993). Additionally, he noted, some ads contain statements (*e.g.*, “abs into great shape fast – without exercise;” “latest fitness craze;” “powerful and effective;” “powerful technology”) that “strongly and clearly imply” that the Ab Force provides users with health, weight loss, fitness, or exercise benefits. ID at 42; IDF 86-92.

Respondents’ failure to identify any other purpose for their EMS device was another factor the ALJ considered in determining the overall net impression of respondents’ ads. ID at 43. Most of

Commission Opinion

the ads did not expressly state any purpose for the product;<sup>9</sup> two television ads mentioned a massage function briefly – and then only in a video superscript – but the ALJ ruled that the use of the “single, momentary phrase ‘relaxing massage’ [in those ads did] not offset or counter the numerous oral and printed statements, in combination with the name and visual images \* \* \*.” ID at 42-43; see IDF 97, IDF 100-09. The ALJ also observed that the models in respondents’ TV ads did not indicate that wearing the Ab Force device was a relaxing or soothing experience. IDF 108.

In addition, the ALJ considered the surrounding circumstances – most notably, evidence that respondents intended to disseminate the challenged claims. ID at 44-46. He reviewed evidence outside the four corners of the advertisements – *i.e.*, expert testimony and copy tests – and concluded that this evidence supported his conclusions regarding the meaning conveyed by the text and images in respondents’ advertising. The ALJ, however, did not credit the testimony of complaint counsel’s marketing expert, Dr. Michael Mazis, regarding so-called “indirect effects” – *i.e.*, the effects on consumers of previous exposure to ab belts through infomercials, word-of-mouth, or retail packaging for other EMS ab belts. ID at 49-51. While noting that respondents’ ads specifically invite consumers to think of infomercials for competing ab belts and expressly claim comparability to those other products, the ALJ found that it was not possible to conclude with confidence that consumers, upon hearing the reference to “those other ab belt infomercials,” would necessarily infer that the claims made in those other infomercials would apply to the Ab Force. ID at 50-51.

---

<sup>9</sup> IDF 102. While the ads did not expressly state the purpose for the Ab Force, respondents’ ads made statements about the purpose of competitors’ ab belts – in some cases, direct statements – and indicated that the Ab Force was equally effective, allowing consumers to make the obvious logical connection. *See, e.g.*, CX 1 H, JX 2.

## Commission Opinion

At trial, both complaint counsel and respondents addressed the impact of consumers' preexisting beliefs about the Ab Force belts from sources other than the Ab Force ads themselves. Complaint counsel argued that respondents should be held liable for exploiting consumers' preexisting beliefs; respondents countered that the copy test – even as controlled with a control group – was unreliable because it failed to filter out preexisting beliefs completely. The ALJ rejected the argument that respondents should be liable for exploiting preexisting beliefs on the basis that there was not enough evidence of the “existence, extent, or impact of those preexisting beliefs,” but held that the copy test was reasonably reliable and probative. ID at 56-57; *see also* ID at 54-57 (reviewing arguments and case law on liability for preexisting beliefs).

Turning next to the question whether the challenged claims were false or misleading, the ALJ noted that respondents had stipulated that use of the Ab Force does not cause loss of weight, inches, or fat; does not create well-defined abdominals; is not an alternative to exercise; and, furthermore, that they had no substantiation for those claims. ID at 60; IDF 270-73. Given these stipulations, the ALJ held that the alleged claims were false and misleading. ID at 60. Moreover, the ALJ held, the claims related to the purpose and effect of using the product, and the evidence showed that respondents intended to make the implied claims. ID at 61. Accordingly, he reasoned, there was no question that the alleged claims were material to consumers' purchasing decisions. ID at 60-61.

Finally, the ALJ addressed the scope of appropriate relief. The ALJ declined to order respondent Khubani to post a performance bond, given the absence of any case law to support such relief in a litigated FTC adjudicative matter. ID at 63. As to fencing-in relief, the ALJ recognized the seriousness, deliberateness, and transferability of respondents' violations. ID at 64-65. Because respondents' history of prior consent orders did not involve findings of liability, the ALJ did not rely on them; he held, however, that a respondent “need not have a history of prior

Commission Opinion

violations in order for fencing-in relief to be imposed.” ID at 65-66. He ordered fencing-in requiring respondents to “possess and rely upon competent and reliable scientific evidence” to substantiate any representation about weight, inch, or fat loss; muscle definition; exercise benefits; or the health benefits, safety, or efficacy of any products, devices, and services promoting the efficacy of or pertaining to health, weight loss, fitness, or exercise benefits. ID at 66, 70.

On appeal, respondents contend that the ALJ erred in concluding that their Ab Force advertising conveyed the challenged claims.<sup>10</sup> Complaint counsel cross-appeal from the ALJ’s refusal to require respondents to post a performance bond before selling or promoting any “device,” as defined in Section 15 of the FTC Act, 15 U.S.C. § 55. Complaint counsel also contend that the ALJ should have entered a broader order that would have prohibited respondents, in the absence of substantiation, from making any claim for any product, service, or program, instead of covering those products only when respondents made claims promoting their efficacy or pertaining to health, weight loss, fitness, or exercise benefits.

---

<sup>10</sup> Although respondents’ notice of appeal purports to lodge an appeal from the initial decision insofar as it found that their ads were false or misleading, their brief focuses on the question whether the ads in fact conveyed the alleged claims to consumers. They do not argue that there is any substantiation for the alleged claims, or deny that the alleged claims are false, misleading, or material to consumers. Indeed, respondents and complaint counsel stipulated before trial that use of the Ab Force does not cause loss of weight, inches, or fat; does not cause well-defined abdominal muscles; and is not an effective alternative to regular exercise. ID at 60; IDF 270-72. The parties further stipulated that respondents did not have or rely on substantiation that the Ab Force would have those effects. ID at 60; IDF 273.

Commission Opinion

## II. The Challenged Representations

### A. Legal Standard

An advertisement is deceptive if it contains a representation or omission of fact that is likely to mislead a consumer acting reasonably under the circumstances, and that representation or omission is material to a consumer's purchasing decision. *FTC Policy Statement on Deception*, 103 F.T.C. 174, 175 (1984) ("Deception Statement"); *see, e.g., Novartis Corp.*, 127 F.T.C. 580, 679 (1999), *aff'd*, 223 F.3d 783 (D.C. Cir. 2000); *Stouffer Foods Corp.*, 118 F.T.C. 746, 798 (1994); *Kraft*, 114 F.T.C. at 120. In addition, the Commission long has held that making objective claims without a reasonable basis constitutes a deceptive practice in violation of Section 5. *FTC Policy Statement Regarding Advertising Substantiation*, 104 F.T.C. 839 (1984) ("Substantiation Statement"); *see, e.g., Automotive Breakthrough Sciences, Inc.*, 126 F.T.C. 229, 293 & 293 n.20 (1998); *Jay Norris, Inc.*, 91 F.T.C. 751, 854 (1978), *aff'd as modified*, 598 F.2d 1244 (2d Cir. 1979), *cert. denied*, 444 U.S. 980 (1979).

The primary evidence of what representations an advertisement conveys to reasonable consumers is the advertisement itself. *Deception Statement*, 103 F.T.C. at 176; *see, e.g., Novartis*, 127 F.T.C. at 680; *Stouffer*, 118 F.T.C. at 798; *Kraft*, 114 F.T.C. at 121. Thus, to determine whether an advertisement conveys a particular claim, the Commission looks at the interaction between and among the constituent elements of the ad to determine the "net impression" that is conveyed by the ad as a whole. *Deception Statement*, 103 F.T.C. at 178; *see, e.g., Novartis*, 127 F.T.C. at 679; *Kraft*, 114 F.T.C. at 122. The Commission may rely on the ad itself and need not resort to extrinsic evidence if the text or depictions are clear enough that the Commission can "conclude with confidence" that the claim is conveyed to reasonable consumers. *Novartis*, 127 F.T.C. at 680; *see Stouffer*, 118 F.T.C. at 798; *Deception Statement*, 103 F.T.C. at 176. If an alleged claim is not manifest from the text and images in the ad, the Commission will look to "extrinsic evidence." *See Novartis*, 127



Commission Opinion

F.T.C. at 680. Such evidence might include common usage of terms, expert opinion as to how an advertisement might reasonably be interpreted, copy tests, generally accepted principles of consumer behavior, surveys, or “any other reliable evidence of consumer interpretation.” *Cliffdale Associates*, 103 F.T.C. 110, 166 (1984); *see, e.g., Thompson Medical Co.*, 104 F.T.C. 648, 789-90 (1984) (expert testimony; consumer survey), *aff’d*, 791 F.2d 189 (D.C. Cir. 1986), *cert. denied*, 479 U.S. 1086 (1987); *Novartis*, 127 F.T.C. at 611-12, 617-33, 682-84 (expert testimony; copy tests); *Kraft*, 114 F.T.C. at 121-22 (expert testimony; copy tests); *Figgie Internat’l, Inc.*, 107 F.T.C. 313, 337-39, 377 n.10 (1986) (expert testimony), *aff’d*, 994 F.2d 595 (9th Cir. 1993), *cert. denied*, 510 U.S. 1110 (1994).

The Commission has recognized that an ad may be amenable to more than one reasonable interpretation. *See, e.g., Kraft*, 114 F.T.C. at 120-21 n.8; *Thompson Medical*, 104 F.T.C. at 787 n.7. Where an ad conveys more than one meaning, only one of which is misleading, a seller is liable for the misleading interpretation even if nonmisleading interpretations are possible. *See, e.g., Bristol-Myers Co.*, 102 F.T.C. 21, 320 (1983), *aff’d*, 738 F.2d 554 (2d Cir. 1984), *cert. denied*, 469 U.S. 1189 (1985); *National Commission on Egg Nutrition v. FTC*, 570 F.2d 157, 161 n.4 (7th Cir. 1977), *cert. denied*, 439 U.S. 821 (1978). Moreover, an ad need not mislead a majority of reasonable consumers. An ad is misleading if at least a significant minority of reasonable consumers are likely to take away the misleading claim. *See, e.g., Kraft*, 114 F.T.C. at 122; *Deception Statement*, 103 F.T.C. at 177 n.20.

If an ad is targeted at a particular audience, the Commission analyzes ads from the perspective of that audience. *Deception Statement*, 103 F.T.C. at 178-79. Different target audiences come to an ad with different perceptions. Consumers cannot understand an ad – or any communication – without applying their own knowledge, associations, or cultural understandings that are external to the ad itself. For that reason, the purpose of ad interpretation is to determine the claims that consumers –

## Commission Opinion

particularly the target audience – take away from an ad, whether or not an advertiser intended to communicate those claims. On the other hand, ad interpretation focuses on the impact of the particular ad on reasonable consumers in the target group; an advertiser is not liable for an interpretation of an ad that a consumer may have based on an idiosyncratic perspective.

The final step in the analysis is to determine whether the challenged claims are “material,” or likely to affect a consumer’s purchasing decision. The Commission presumes that claims are material if, as in this case, they pertain to the “central characteristics of a product \* \* \* such as those relating to its purpose \* \* \* [or] efficacy” or to safety. *Thompson Medical*, 104 F.T.C. at 816-17.

### **B. Facial Analysis of Respondents’ Ab Force Advertising**

We turn first to an examination of the text and images in respondents’ ads.<sup>11</sup> We agree with the ALJ that the challenged

---

<sup>11</sup> Respondents’ Ab Force promotion included the following ads: (1) a “test” radio ad (CX 1 H); (2) a “roll-out” radio ad (RX 49); (3) a one-minute “test” TV ad (JX 2 (tape); CX 1 B (transcript)); (4) a one-minute “roll-out” TV ad (JX 4 (tape); CX 1 F (transcript)); (5) a two-minute “test” TV ad (JX 3 (tape); CX 1 D (transcript)); (6) a two-minute “roll-out” TV ad (JX 5); (7) a print ad (CX 1 G; RX 48); (8) an Internet ad (RX 52); and (9) two email ads (RX 50-51). Again, all of the ads – including the so-called “test” ads for radio and TV – were disseminated and generated sales. IDF 43-45, 49. Respondents spent more than \$4 million on television advertising. IDF 52. The test ads for TV alone were broadcast nearly 96 times in January 2002; more than 4500 orders were called into the telephone number that appeared in those ads. IDF 44-45. The roll-out versions of respondents’ television spots were broadcast more than 11,000 times from January 19, 2002 through April 7, 2002. IDF 46-47. The telephone numbers that appeared in the TV ads were associated

Commission Opinion

claims are clearly communicated in ads for the Ab Force belt.<sup>12</sup> As shown below, it is not necessary to look beyond the four corners of respondents' ads to reach this conclusion. This is a straightforward case.

## 1. Visual Images and Ad Copy

### a. Radio Advertisements

Respondents opened their promotion in December 2001 with a 60-second radio spot.<sup>13</sup> The ad invites consumers to recall “those

---

with more than 300,000 orders for the Ab Force. IDF 48. The radio advertising was more limited, generating a total of only 1,340 orders. IDF 49. The print ad ran for about one week in 13 newspapers and for another week as a newspaper insert. IDF 50. The print and Internet ads together accounted for less than 3 percent of all orders. IDF 50-51.

<sup>12</sup> Respondents challenged the ALJ's findings of fact as to ad interpretation, arguing that the ALJ based the findings on the messages communicated by the Ab Force ad campaign as a whole rather than the messages communicated by each individual ad. We do not agree that the ALJ erred in analyzing the ads but, in any case, the Commission has examined each ad individually and determined that the ads communicate the challenged claims.

<sup>13</sup> The text of respondents' first radio ad – the opening ad of the campaign – is as follows:

*Have you seen those fantastic Electronic Ab Belt (sic) infomercials on TV? They're amazing . . . promising to get our abs into great shape fast – without exercise! They're the latest fitness craze to sweep the country! But, they're expensive, selling for up to 120 dollars each! But what if you could get a high quality electronic ab belt for just 10 dollars? That's right, just 10 dollars! Why so cheap?*

## Commission Opinion

fantastic Electronic Ab Belt infomercials on TV.” It then declares: “They’re amazing . . . promising to get our abs into great shape fast – without exercise! They’re the latest fitness craze to sweep the country!” CX 1 H. The ad continues by claiming that the Ab Force is “just as powerful and effective” as “the expensive ab belts on TV,” and would send “just the right amount of electronic stimulation to [a user’s] abdominal area.” *Id.*

Respondents made several minor changes in the ad after “final review and legal review” and “discussions with counsel” – that is, after the test radio ad had aired. IDF 90 (*quoting* Khubani Tr. 275, 278), IDF 92.<sup>14</sup> These modifications did not change the fundamental ad messages. Again, the rollout radio ad invites comparison to their competitors’ “fantastic” and “amazing” ab belts, which they claim are “the latest craze to sweep the country.” RX 49. But while the “test” ad claims that the Ab Force is “just as powerful and effective” as “the expensive ab belts on TV” (CX

---

Because intense competition and mass production have forced prices down. We cut a deal with the factory to buy up to 1 million units at a very special price and we are passing the savings on to you. *The Abforce (sic) is just as powerful and effective as the expensive ab belts on TV* – designed to send just the right amount of electronic stimulation to your abdominal area. Best of all, they’re only 10 dollars and have a full money back guarantee. Call now [telephone number omitted]. Don’t miss out. Get the amazing electronic Abforce (sic) belt – the latest fitness craze for just \$10 [phone numbers omitted].

CX 1 H (emphasis added).

<sup>14</sup> Mr. Khubani admitted that he was aware at the time that there was no substantiation for certain claims about Ab Force, for example that a user could get into shape quickly without exercise and could get a flatter stomach without doing sit-ups. IDF 58-60.

Commission Opinion

1 H), the “rollout” ad declares that the Ab Force has the “same powerful technology as those expensive Ab Belts.”<sup>15</sup> IDF 91; RX 49. The revised text does not expressly identify any particular purpose for the Ab Force. It states, however, that it is “[c]apable of directing 10 different intensity levels at [the user’s] abdominal area.” IDF 100; RX 49.<sup>16</sup>

---

<sup>15</sup> The script of the rollout radio ad reads as follows:

*Have you seen those fantastic electronic ab belt infomercials on TV? They’re amazing! They’re the latest craze to sweep the country and everybody wants one! The thing is, they’re expensive, selling for up to 120 dollars each! That’s why we developed the Abforce (sic) that you can buy right now for just 10 dollars. That’s right, just 10 dollars! Why so cheap? Well just like cell phones and VCRs, the price of electronic products keeps coming down. We were able to cut a special deal directly with the factory and are passing the savings on to you. The Abforce (sic) uses the same powerful technology as those expensive Ab Belts (sic). Capable of directing 10 different intensity levels at your abdominal area (sic). Best of all, the Abforce (sic) is just 10 dollars and has a full money back guarantee. Demand is overwhelming. Don’t miss out [on this] tremendous opportunity. Call now [phone numbers omitted].*

RX 49 (emphasis added).

<sup>16</sup> Clearly, the process of reviewing and refining advertising claims to remove potentially misleading claims – before an ad is disseminated, not after – is critical, and we encourage advertisers strongly to review their ads. Respondents, however, merely toned down the most obvious false statements in the initial ads. Even though the radio and television rollout ads were revised, the ad copy (and, in the television ads, the visual images) communicated the same messages just as clearly.

## Commission Opinion

The ALJ concluded that the challenged Ab Force radio advertisements conveyed the claims alleged in the Commission’s complaint. ID at 41-43. We agree. Respondents’ “test” ad for radio expressly reinforces the performance claims that their competitors were disseminating for their own ab belts – *e.g.*, that the belts will get a user’s abs “into great shape fast – without exercise” – and then goes on to claim that the Ab Force is “just as powerful and effective.” CX 1 H. Even consumers who might not have seen ads for competing ab belts or might not remember the ads they had seen would conclude from the text that the Ab Force is as effective as the referenced ab belts in getting their abs “into great shape fast – without exercise.” Respondents later eliminated some of the text that described their competitors’ efficacy claims, focusing instead on the Ab Force’s “powerful technology” and its ability to direct ten different intensity levels at a user’s abdominal muscles. RX-49. Respondents’ slight modifications to the original text did not alter the elements that communicated deceptive claims as to the product’s purpose but only removed claims that would be most likely to attract regulators’ attention. While the rollout ad is less direct, the promise that the product has the same “powerful technology” as the other ab belts is not simply a comparative statement: in context, it clearly implies that the product has *some* power and effect on the body. Combined with the claim that the belt is “[c]apable of directing 10 different intensity levels at [the user’s] abdominal area,” it also clearly implies that the product would exert a “powerful” force and “intensity” at the user’s abdominal area. Given respondents’ failure to offer any other purpose for the product, listeners would reasonably conclude that such “powerful” technology was designed to develop a fitter abdomen and help them slim down and trim down without exercise.

**b. Television Advertisements**

Respondents’ TV spots feature substantially the same kinds of images as those used by competitors in their ab belt infomercials. IDF 73-76, 121. Each of the Ab Force spots displays images of well-muscled, bare-chested men and trim women in tight-fitting

Commission Opinion

exercise apparel wearing Ab Force belts and experiencing abdominal contractions. ID at 41; IDF 73-76. Close-up images highlight the models' trim waists and well-defined abs. JX 2-5. Additionally, the spot ads depict stock images of men without ab belts performing abdominal crunches on an exercise bench (JX 3, 5) and bikini-clad women, also shown without ab belts, showing off their well-toned bodies and trim waistlines in the background. See JX 2-5 (Ab Force TV ads); JX 7-10 (infomercials); ID at 41; IDF 83.<sup>17</sup> It was no accident that the models were not only slender and fit but also had well-muscled abdomens – the commercial casting agents were specifically looking for “great abs.” IDF 79-80. The producer of the commercials admitted that people viewing the television ads were supposed to aspire to become like the bikini-wearing models in the ads. IDF 85 (*citing* JX 6 at 2 (Liantonio Dep. at 70)).

These visual images of well-toned Ab Force users juxtaposed with images of men executing conventional exercises and trim bikini-clad models clearly convey the message that the Ab Force is not only an alternative to exercise, but also that users of the device will achieve the same trim waists and well-developed abdominal muscles as those displayed by respondents' models. The accompanying text reinforces this message. For example, referring to those “fantastic” and “amazing” ab belt infomercials on TV, respondents claim that the Ab Force is “just as powerful and effective” and characterize the impact of those prior ab belts as “the latest fitness craze.” JX 2 (tape); CX 1 B (transcript). For example, one of the early 60-second television advertisements claimed as follows:

[Spokesperson]: I'm sure you've seen those fantastic electronic ab belt infomercials on TV. They're amazing. They're the latest fitness craze to sweep the country and everybody wants one.

---

<sup>17</sup> Other stock images in the ads included dollar signs and falling numbers. IDF 81-82.

## Commission Opinion

The Ab Force is just as powerful and effective as those expensive ab belts sold by others—

ON SCREEN: image of electronic stimulation of abdominal muscles

[Spokesperson]: – designed to send just the right amount of electronic stimulation to your abdominal area.

JX 2 (tape); CX 1 B (transcript). Coupled with visual images of fit, muscled men and fit, trim women wearing the Ab Force belt and experiencing abdominal contractions, the text strongly suggests that consumers can achieve the same results with the Ab Force. Like the radio ad (CX 1 H), the statement that the product was “designed to send just the right amount of electronic stimulation to your abdominal area” implies that the product will send the right amount of stimulation to your abdominal area *to do something*.

In a two-minute television spot, respondents’ spokesperson appears in a business suit.<sup>18</sup> She does not state exactly what the Ab Force is supposed to do, but she does claim that it is “just as powerful and effective” as the infomercial ab belts and that it uses “sophisticated electronic technology” that is “designed to send just the right amount of electronic stimulation to your abdominal area.” JX-3 (tape); CX 1 D (transcript). She also states that the product is so comfortable that “[consumers] can wear it under clothes.” *Id.* Indeed, directing the viewer’s attention to her own abdomen, she indicates that the product “is working while [she is] working.” *Id.*; IDF 77. The obvious message for consumers is that the Ab Force device is an effective and convenient alternative to exercise.

---

<sup>18</sup> This ad, like the other television ads, showed well-muscled men and trim women showing off the ab belt, an image of a woman with trim abs in a bikini, a man preparing to exercise, etc. JX-3 (tape); CX 1 D (transcript).



## Commission Opinion

In some ads the claims are conveyed in more subtle fashion but still are clearly communicated. For example, in one ad, a 60-second television spot, respondents refer to ab belts as the “latest craze,” dropping the word “fitness.” IDF 89; JX 4 (tape); CX 1 F (transcript). Additionally, instead of asserting that the Ab Force is as “powerful and effective” as competing ab belts in infomercials, the female spokesperson states that the device has “10 completely different intensity levels directed at your abdominal area.” IDF 100; JX 4, CX 1 F. JX 5, a 120-second television spot, likewise claims that the Ab Force has “sophisticated computer components” and the “same powerful technology” as other ab belts advertised in infomercials. Furthermore, respondents claim, with “10 completely different intensity levels directed at [a user’s] abdominal area,” the product is “designed for comfort in mind” and is “so comfortable [that consumers] can wear it under [their] clothes.” To illustrate the point, respondents’ spokesperson – again gesturing towards her abdomen – reveals that the device is “working while [she is] working.” This is truly “a high quality, *powerful*, comfortable” product that is in high demand, she declares. JX 5 (emphasis added). A consumer would reasonably believe that a product designed – supposedly – to work out for them would help them lose weight or inches, just as exercising would.

While the intended purpose of an Ab Force device – as opposed to competitors’ ab belts – is not stated explicitly in any of the ads, the product name and references to “sophisticated” and “powerful” technology strongly suggest that it is effective in honing the abdominal muscles to make them more powerful or forceful. The visual images are used by respondents to convey the impression that their device is an alternative to conventional exercise. The juxtaposition of a male model who is executing abdominal crunches on an exercise bench with men and women in fitness clothing who are wearing Ab Force belts and effortlessly experiencing abdominal contractions drives home the message. Respondents’ spokesperson states that her Ab Force belt is “working” while she is “working” in her business suit. Given the spokesperson’s business attire, consumers would reasonably

## Commission Opinion

believe that the device can be used in any setting to give their abdominal muscles the stimulation they need to make them fit.

**c. Print Advertisement**

Respondents' print ad appeared in thirteen newspapers in February 2002 and in a newspaper insert in March 2002. CX 1 G; RX 48. It follows the same basic format as respondents' radio and TV ads – *e.g.* reminding consumers of “the latest craze to sweep the country” and referring to “those fantastic” and “amazing” ab belt infomercials on TV. RX 48. Respondents claim that the Ab Force has the “same powerful technology as those Ab Belts sold by other companies on infomercials” and consumers “can even wear it under [their] clothes.” *Id.* Indeed, the ad continues, it “is capable of directing 10 completely different intensity levels at [a user's] abdominal area \* \* \*.” *Id.* Coupled with a close-up photograph of a well-defined male torso wearing an Ab Force belt, respondents' statements strongly imply that consumers can achieve the same well-developed, toned abs as the model merely by wearing an Ab Force belt under their clothes.

**d. Internet and Email Advertisements**

Respondents' Internet ads (RX 51-52) use the same basic format to remind consumers that the Ab Force is comparable to those “fantastic” and “amazing” electronic ab belt infomercials on TV. The photographic image of a well-defined, sculpted male torso wearing an ab belt and its accompanying label – that “AbForce (sic) uses the same powerful technology as those expensive ab belts sold through infomercials” – strongly imply that (1) by using “those fantastic” and “amazing” electronic ab belts that are advertised on TV, consumers can achieve the same well-defined muscles as those displayed in the accompanying photograph; and (2) because it uses the “same powerful technology,” purchasers can achieve similar results by wearing an Ab Force. The email ad (RX 50) is less compelling, but it too claims that the “AbForce (sic) uses the same powerful technology as those Ab Belts (sic) sold by other companies on infomercials.”

Commission Opinion

## 2. Product Name

As respondents undoubtedly recognized, IDF 69, a product name can help the advertiser convey a claim about the central attributes of a product. *See, e.g., Jacob Siegel Co. v. FTC*, 327 U.S. 608, 609 (1946) (“Alpacuna” suggests that the product contains vicuna); *Thompson Medical*, 104 F.T.C. at 793 (name “Aspercreme” implies the product contains aspirin). The product name “Ab Force” is an artful choice of words that easily suggests that consumers will achieve more forceful or well-developed abdominal muscles. ID at 41; IDF 70. We agree with the ALJ that the product name itself, in combination with the text and visual images in each of the ads, played an obvious role in conveying respondents’ implied claims to consumers. ID at 41.

Based on our own review of the challenged advertising, we conclude that consumers would reasonably interpret respondents’ Ab Force ads to mean that the device (1) causes loss of weight, inches, or fat; (2) creates well-defined abdominal muscles; and (3) is an effective alternative to regular exercise – even if the consumers had not seen ads for competing ab belts. As shown below, our facial analysis is confirmed by the surrounding circumstances and extrinsic evidence, including expert opinion and a copy test of respondents’ most widely disseminated TV ad.

### C. Other Considerations

Our facial analysis of the ads is informed by the market context in which the ads were disseminated and respondents’ intent to take advantage of that context by presenting the AbForce as a substitute for other heavily advertised but more expensive “ab belts.” As discussed above, respondents presented the Ab Force as an “ab belt,” and expressly drew comparisons to other products with which many consumers had been made familiar through prior

## Commission Opinion

advertising<sup>19</sup> and which – as respondents knew<sup>20</sup> – were advertised as improving the physical condition of the user’s abdominal muscles.<sup>21</sup> It may be possible, of course, for a seller to use a particular product description while at the same time making clear through its advertising that it does not claim a particular functionality for the product. The respondents can point to no such efforts, though, in the context of the Ab Force campaign.

We agree with the ALJ that an advertiser’s failure to make a statement about the purpose or core function of its product can play a role in determining which implied claims are conveyed to consumers. ID at 43; *cf. Thompson Medical Co.*, 104 F.T.C. at 793 (noting “absence of any elements giving a contrary impression, such as express disclosures”). Given the absence of any statements in the later TV and radio ads about the purpose of using an Ab Force device (IDF 97) and the express invocation of ads for other ab belts that did communicate the products’ purpose, there is nothing to act as a counterweight to respondents’ conspicuous visual images or the general notion that an “ab belt” is a device that purports to improve the condition of the abdominal muscles and slim down and firm up users. Although the phrase “relaxing massage” flashes briefly on the screen in two of respondents’ TV ads (*see* IDF 100-01; JX 4-5),<sup>22</sup> we agree with

---

<sup>19</sup> *See* IDF 125, 127-34 (advertisement monitoring service rankings showing that infomercials for the competing ab belts were among the 50 most frequently disseminated infomercials and in the top 40 direct response spot rankings in the United States on a number of occasions in 2001 and 2002).

<sup>20</sup> *See, e.g.*, *Khubani Tr.* 273-74, 445, 461, 471-72.

<sup>21</sup> *See* IDF 117-24 (referencing claims made in infomercials for the Fast Abs, AbTronic, and Ab Energizer ads).

<sup>22</sup> We recognize that a few ab belts – including the respondents’ own Ab Pulse – have been advertised as a massage

## Commission Opinion

the ALJ that it is not nearly sufficient to offset the central message that respondents convey repeatedly with the name of the product and the audio and video elements of the ads. ID at 42-43; *see Kraft*, 114 F.T.C. at 123-24; *Removatron Int'l Corp.*, 111 F.T.C. 206, 294 (1988), *aff'd*, 884 F.2d 1489 (1st Cir. 1989); *Thompson Medical*, 104 F.T.C. at 797-98. It is not clear, for example, why an ad for a massage product would include images of men performing ab crunches on exercise equipment, or why an ad for a massage product would reference competing products' claims to "get [one's] abs into great shape fast – without exercise!" Indeed, the visual images of men and women experiencing rapid and intense abdominal contractions through electronic muscle stimulation seem inconsistent with any commonsense notion of a relaxing experience. As noted by the ALJ, the men and women who were shown wearing an Ab Force device in the TV ads gave no indication that wearing the device was a soothing or relaxing experience. IDF 108; JX 4-5. Finally, at oral argument, counsel for respondents repeatedly declined to represent that the product was intended as a massage device. In fact, he repeatedly stated that he did not know what the Ab Force product was supposed to do. *See, e.g.*, Oral Argument Tr. at 7-11. For example:

---

tool. Clearly, however, despite a passing reference to "relaxing massage" – in only two of the Ab Force ads – the product was not intended as a massage tool. *See infra*; *see also* Oral Argument Tr. at 7-11 (colloquy about purpose of Ab Force product in which respondents' counsel claimed he did not know the purpose of the product). The primary focus of the advertising for ab belts as a product category was their supposed efficacy as a health, weight loss, and fitness device. IDF 120-24, 142-46. In fact, respondents' advertising for Ab Pulse, which attempted to position that product as a massage product, tried to distinguish the product from other ab belts on the market. IDF 112; CX 2. Unlike ab belts that were sold for health, weight loss, and fitness, the Ab Pulse product was unsuccessful and quickly pulled from the market. ID at 44; IDF 113; Khubani, Tr. 281.

## Commission Opinion

Commissioner Swindle: \* \* \* What was the purpose of the ab belt, I mean, the Abforce belt?

Counsel: I have no idea, Your Honor. I'm basically saying what I'm taking is the language of the commercial. They have the same technology, but they're a lot cheaper.

In fact, all Mr. Khubani was trying to do was to provide a reference point to other products that were being advertised.

Chairman Majoras: What does the technology do?

Counsel: I don't know what the technology does.

*Id.* at 8-9.

Moreover, there is ample evidence that respondents intended to convey the challenged claims, which provides further support for our facial analysis. ID at 45-46; *see, e.g.*, IDF 65-102. A showing of an intent to make a particular claim is not required to find liability for violating Section 5 of the FTC Act. *See, e.g., Chrysler Corp. v. FTC*, 561 F.2d 357, 363 & n.5 (D.C. Cir. 1977); *Novartis*, 127 F.T.C. at 683; *Kraft*, 114 F.T.C. at 121. However, a showing of intent is powerful evidence that the alleged claim in fact was conveyed to consumers. *See, e.g., Novartis*, 127 F.T.C. at 683; *Thompson Medical*, 104 F.T.C. at 791.

The timing of respondents' decision to enter the market – after reading about the AbTronic and determining that it was a “hot category” – coupled with their decision to invite consumers to recall the (deceptive) advertisements for those products while viewing the Ab Force ads suggests strongly that respondents intended to jump on that bandwagon with the same messages for consumers that had turned ab belts into “one of the hottest categories to hit the market.” IDF 63 (*quoting* Khubani Tr. 255). As demonstrated by the text of the ads, respondents' promotion specifically targeted consumers who were already familiar with ab belt infomercials. *See, e.g.*, CX 1 H (“Have you seen those

Commission Opinion

fantastic Electronic Ab Belt infomercials on TV? They're amazing . . . promising to get our abs into great shape fast – without exercise!"); JX 2 (tape), CX 1 B (transcript) ("I'm sure you've seen those fantastic electronic ab belt infomercials on TV. They're amazing. They're the latest fitness craze to sweep the country and everybody wants one."); RX 49 ("Have you seen those fantastic electronic ab belt infomercials on TV? They're amazing! They're the latest craze to sweep the country and everybody wants one!"). By explicitly referencing the ads for their competitors' "amazing" and "fantastic" ab belts products at the outset of each and every one of their ads (*see* IDF 114), respondents clearly intended to spur consumers' recall of those advertisements' claims<sup>23</sup> and intended consumers to understand that they could accomplish the same fitness goals with the Ab Force that respondents' competitors promised – *i.e.*, tighter abs, loss of inches, weight or fat, and an alternative to conventional exercise. In short, respondents' ads targeted consumers who had seen competitors' ads.

Respondents contend that they merely made express and truthful "compare and save" claims, which they used to create a "bandwagon effect."<sup>24</sup> RAB at 7. They argue that they had to refer to competitors' products to make the price comparison, but suggest that they made no claim about the purpose of the product.

---

<sup>23</sup> Many consumers did see the competitors' ads based upon the rankings – clearly, the respondents assumed that they had and the frequency with which those ads aired bears out that assumption. *See* IDF 125, 127-34. Moreover, because consumers typically watch TV in multiple time slots, a viewer could easily see an infomercial for one or more of respondents' competitors and also see an ad for the Ab Force on a different channel and in a different time slot. Mazis Tr. 184-85.

<sup>24</sup> A "bandwagon effect" refers to the advertiser's effort to generate interest in a product based on the idea that consumers should buy a product because of its popularity. IDF 96.

## Commission Opinion

They contend that consumers would want to purchase the Ab Force simply because it is a popular product that other people are buying, even if they are unaware of the product's function. As noted above, respondents' ads clearly communicated the product's purpose within the four corners of the ad. In any case, the suggestion that consumers were buying a product like the Ab Force – without knowing what the product was for – merely because the ad promised that many other people were buying it is not only not credible but also disingenuous. While a product's perceived popularity may motivate a consumer's purchase of items such as clothing or decorations or novelties – witness the “Pet Rock” fad of the 1970s – it is not plausible that consumers would have purchased an Ab Force belt without any idea as to its purpose or function. The comparability claims – *i.e.*, that the Ab Force has the same “powerful” technology and is “just as effective” as their more expensive competitors – reinforced the message that the Ab Force was effective. The references to competitors' (admittedly deceptive) advertisements make little sense unless respondents expected and knew that significant numbers of consumers would recall the claims that respondents' competitors made in their infomercials and interpret respondents' ads with those in mind.<sup>25</sup>

---

<sup>25</sup> Similarly, in respondents' ad campaign for a later product that was positioned as a massage tool, the respondents also acknowledged that consumers had likely seen the infomercials for the competing ab belts, although respondents attempted to distinguish the Ab Pulse product from those products. Respondents cautioned viewers not to confuse the Ab Pulse “with an electronic ab belt you've seen on infomercials,” emphasizing the point by depicting a red “X” superimposed on the image of a model wearing an ab belt and the on-screen legend, “infomercial ab belts.” CX 2. To be sure, the ALJ erred in finding that respondents brought the Ab Force to market after disappointing sales of the Ab Pulse belt. *Compare* ID at 44-45 with CX 31 & CX 108. Nonetheless, regardless of the time sequence, it is doubtful that respondents would have found it necessary to



Commission Opinion

### **D. Extrinsic Evidence Supplements and Confirms the Commission's Facial Analysis of the Ab Force Ads**

Based on our facial analysis of respondents' Ab Force ads, we conclude that they clearly convey the claims alleged in the Commission's complaint. Although extrinsic evidence is not necessary to reach our decision, consistent with our practice we have examined the extrinsic evidence that the parties have offered about the meaning of the challenged Ab Force ads. *See, e.g., Stouffer*, 118 F.T.C. at 799. This includes (1) Dr. Mazis's expert testimony and report regarding how respondents' TV ads would be perceived by consumers; (2) a copy test that Dr. Mazis designed, based on the most widely disseminated TV ad; and (3) a critique by respondents' expert, Dr. Jacob Jacoby, of the methodology that Dr. Mazis adopted. As discussed below, we conclude that the extrinsic evidence confirms our facial analysis of the Ab Force ads.<sup>26</sup>

#### **1. Expert Testimony**

Dr. Mazis testified that respondents' ads communicated certain core performance claims to consumers as a direct result of the text and images in the ads ("direct effects") and, indirectly, as a result

---

distinguish their Ab Pulse from "infomercial ab belts" in this manner unless they assumed that consumers would associate the images of models wearing an ab belt in the Ab Pulse ads with the express fitness claims made for the "infomercial ab belts."

<sup>26</sup> Although, as respondents note (RAB at 42 n.6), the extrinsic evidence offered by complaint counsel relates to the trial and rollout versions of respondents' TV ads, many of the elements considered by Dr. Mazis also appear in the print, radio, Internet, and email ads.

## Commission Opinion

of their familiarity with infomercials for other ab belts (“indirect effects”).<sup>27</sup>

With regard to the “direct effects” of the ads, Dr. Mazis identified the main visual images in respondents’ ads – trim models with well-developed abdominal muscles, and an Ab Force belt shown causing a model’s abs to pulsate (Mazis Tr. 59-60, 66) – and concluded that together with the name of the product they were likely to convey the message that by using the Ab Force consumers would achieve well-developed abdominal muscles and loss of inches around the waist. Mazis Tr. 59-61, 66-67, 165. “[E]ven if you had never heard of an ab belt before, \* \* \* you

---

<sup>27</sup> Dr. Mazis testified that the ads conveyed four implied claims. According to Dr. Mazis, the two most prominent claims – that users of the Ab Force will achieve well-developed muscles and lose inches around the waist – were conveyed through the visual imagery in respondents’ ads. Mazis Tr. 61. Dr. Mazis also testified that consumers may associate the Ab Force with losing weight and view the product as a substitute for exercise principally because of the association with previous ab belt ads. Mazis Tr. 61-62. Of course, even if one had not seen the prior ads, those claims were neatly incorporated into the Ab Force ads themselves. *See, e.g.*, CX 1 H (Ab Force is “just as powerful and effective as the expensive ab belts on TV” that supposedly would “get our abs into great shape fast – without exercise”); JX-3 (tape), CX 1 D (transcript) (Ab Force is “just as powerful and effective” as the infomercial ab belts, uses “sophisticated electronic technology” that is “designed to send just the right amount of electronic stimulation to your abdominal area,” and “is working” on the abdomen even under business wear); RX 48 (promises that Ab Force has the “same powerful technology as those Ab Belts sold by other companies on infomercials” and “is capable of directing 10 completely different intensity levels at [a user’s] abdominal area \* \* \*” paired with a close-up of a muscled male torso).

Commission Opinion

could see the ad and you could make inferences because there's certain implied claims in the ads." Mazis Tr. 66.<sup>28</sup>

Dr. Mazis also testified as to the "indirect effects" of the ads, which he attributed primarily to respondents' efforts to "exploit" or "free-ride" on a blitz of infomercial advertising for three other EMS ab belts – the AbTronic, Ab Energizer, and Fast Abs. CX 58 ¶ 19-20, 48; IDF 163-66; Mazis Tr. 64-66. Infomercials for the AbTronic, Ab Energizer, and Fast Abs contained "numerous representations about how using the products causes consumers to obtain well-defined abdominal muscles and to lose inches around the waist." CX 58 ¶ 17; *see* IDF 122-24. The infomercials also claimed that the products were an alternative to conventional exercise and that consumers could lose weight by using them.<sup>29</sup> CX 58 ¶ 18; IDF 120-24. These claims and representations were conveyed through statements (*e.g.*, "six-pack abs," "washboard abs," "rock-hard abs"); before-and-after photographs; testimonials; and depictions of models with trim waists and highly defined abs. CX 58 ¶ 17. The infomercials aired from 2001 to early 2002 – *i.e.*, the period of time leading up to, and overlapping with, respondents' own Ab Force promotion. IDF 125, 129-33; CX 58 ¶ 15; CX 96 (AbTronic); CX 98 (Ab Energizer); CX 100 (Fast Abs). Given the timing of the promotional campaigns and the similarity in name, appearance, and function of all four EMS products, Dr. Mazis concluded that the infomercial advertising was likely to have had an impact on consumers' perceptions of

---

<sup>28</sup> Respondents' expert, Dr. Jacoby, was also qualified to testify as an expert witness in consumer behavior, consumer psychology, and consumer comprehension, but did not offer his own views as to the meaning of the ads.

<sup>29</sup> According to Dr. Mazis, "[t]hese are claims that appear in some of the ads for the other EMS ab belts," but they are not as "prominent" as claims that the products cause users to develop well-defined abs and to lose inches around the waist. CX 58 ¶ 21.

## Commission Opinion

respondents' Ab Force ads. CX 58 ¶¶ 16, 19-21, 48; Mazis Tr. 48, 59-67. As described by Dr. Mazis,

There are depictions of well-muscled men and trim women with well-defined abdominal muscles in advertisements for Ab Force and for AbTronic, AB Energizer, and Fast Abs. The models in the Ab Force ads are similar to the models shown in ads for the other EMS ab belts. Also, the brand names are similar – Ab Force, AbTronic, AB Energizer, and Fast Abs use the term “ab” or “abs” to refer to the abdominal muscles.

CX 58 ¶ 19.

Based on the psychological and consumer behavior theory of “categorization,”<sup>30</sup> Dr. Mazis testified that those consumers who had been exposed to infomercials for competing ab belts, word-of-mouth, and retail packaging for ab belts would have developed an “ab belt category of beliefs.” IDF 163, 166, 169. Such general category beliefs would have included an association between ab belts with well-developed abs, loss of weight and inches, and alternatives to regular exercise. IDF 164. According to Dr. Mazis, respondents' Ab Force ads would trigger such beliefs and cause consumers to read them into the Ab Force ads. IDF 167. The fact that respondents' advertising specifically relied on the fact that many viewers would have seen infomercials for other EMS ab belts (*e.g.*, “I’m sure you’ve seen those fantastic ab belt infomercials on TV”) was cited by Dr. Mazis as further support for concluding that respondents were “free-riding” on claims their

---

<sup>30</sup> The consumer behavior theory of “categorization” is premised on evidence that people place objects in categories based on their similarity. ID at 49-50; IDF 169.

Commission Opinion

competitors were making for the other EMS ab belts.<sup>31</sup> See JX 7-10; CX 58 ¶ 19; Mazis Tr. 47-48.

With regard to the “direct effects” of the ads, the ALJ rejected respondents’ contention that Dr. Mazis’s facial analysis was not a proper subject of expert testimony. ID at 48. He explained that while Dr. Mazis’s testimony regarding the claims directly conveyed by the four corners of the ads was “not necessary,” it was “relevant” and “valuable not as an expression of his personal opinion, but rather as expert opinion regarding his knowledge and experience of consumer perceptions and claims that consumers would take away from the four corners of the advertising at issue.” *Id.* Dr. Mazis has taught undergraduate and graduate courses in consumer behavior at American University for more than a decade, and has served as a consultant on advertising issues and

---

<sup>31</sup> Respondents’ ads referred to “those fantastic ab belt infomercials.” As shown in industry monitoring publications, infomercials for the AbTronic, Ab Energizer, and Fast Abs EMS ab belts aired frequently in the period leading up to, and during much of, respondents’ Ab Force promotion. IDF 125. Indeed, they were the only ab belt infomercials among the 50 most frequently aired infomercials during the relevant time period. IDF 134. Although the GymFitness device was advertised in infomercials, it was not widely advertised; it did not achieve a Top 50 infomercial ranking at any point during respondents’ promotion of the Ab Force. IDF 143. While respondents placed on the record promotional materials for other EMS devices (IDF 137-46), three of these – the IGIA Electrosage, the Mini Wireless Massage System, and the Accusage – are not electronic ab belts. IDF 139-141. Advertisements for another four devices – the Smart Toner, ElectroGym, Slim Tron, and SlendertoneFlex – appeared as short spots, not infomercials (IDF 142, 144-46), so they were evidently not the ads that inspired the references in the respondents’ ads. In any case these ads – like those for the AbTronic, Ab Energizer, and Fast Abs – touted the products’ health, fitness, and weight loss benefits. IDF 142, 144-46.

## Commission Opinion

consumer behavior for federal and state governments and for private industry. IDF 148-49. Additionally, he has conducted hundreds of surveys and research studies and published numerous articles in academic journals. IDF 151. Based on his knowledge and experience, he was properly qualified by the ALJ as an expert in the area of consumer perception.

Respondents contend that Dr. Mazis did not attempt to explain how his expertise was relevant to his opinions, or how his opinions were logically related to that expertise. RAB at 44. Accordingly, they claim, under the standards established in *Daubert v. Merrell Dow Pharmaceuticals, Inc.*, 509 U.S. 579 (1993) and *Kumho Tire Co. v. Carmichael*, 526 U.S. 137 (1999), his facial analysis must be set aside. RAB at 43-49.<sup>32</sup> We reject respondents' contention that *Daubert* and *Kumho* require the Commission to reject Dr. Mazis's testimony. In the context of the so-called "soft sciences," federal district courts are allowed discretion to choose which factors are appropriate and relevant, according to the expertise in question and the subject of the proffered expert testimony. *Kumho*, 526 U.S. at 149-50; *see, e.g., Betterbox Communications Ltd. v. BB Technologies, Inc.*, 300 F.3d 325, 329-30 (3d Cir. 2002) (in trademark infringement case district court did not abuse discretion in receiving expert opinion

---

<sup>32</sup> *Daubert* and *Kumho* do not apply directly to administrative agencies' adjudicative proceedings. *See, e.g., Niam v. Ashcroft*, 354 F.3d 652, 660 (7th Cir. 2004); *Peabody Coal Co. v. McCandless*, 255 F.3d 465, 469 (7th Cir. 2001); *cf. FTC v. Cement Institute*, 333 U.S. 683, 705-06 (1948) (FTC adjudicative proceedings are not governed by the "rigid rules of evidence"). The Commission nonetheless is guided by the spirit of *Daubert* and *Kumho* in making a determination as to the admissibility of expert testimony. *See* 16 C.F.R. § 3.43(b)(1) ("[R]elevant, material, and reliable evidence shall be admitted. Irrelevant, immaterial, and unreliable evidence shall be excluded."). *See also Niam*, 354 F.3d at 660; *Libas, Ltd. v. United States*, 193 F.3d 1361, 1366 (Fed. Cir. 1999).

## Commission Opinion

testimony regarding likelihood of confusion that was based on expert's personal knowledge and experience). To the extent Dr. Mazis's testimony merely identifies elements in the ads that communicate the challenged claims, his testimony adds little to a facial analysis. We agree with the ALJ, however, that Dr. Mazis's testimony regarding how consumers tend to perceive ads – e.g., that consumers remember visual images in an ad for a longer period than the ad's text (Mazis Tr. 59) – is relevant and probative “as expert opinion regarding his knowledge and experience of consumer perceptions and claims \* \* \*.” ID at 48; *see, e.g., Kraft*, 114 F.T.C. at 122; *Thompson Medical*, 104 F.T.C. at 790. Considering evidence that shows “how consumers might ordinarily be expected to perceive or understand representations like those contained in the ads we are reviewing” is fully consistent with our past practice. *Thompson Medical*, 104 F.T.C. at 790; *see Kraft*, 114 F.T.C. at 122.

As to the “indirect effects” of the ads, however, the ALJ refused to credit Dr. Mazis's testimony. According to the ALJ, Dr. Mazis's testimony that “many consumers would have been exposed” to infomercials for other ab belts was not credible in the absence of empirical research regarding “exactly how frequently any one advertisement at issue had aired, and no information identifying the stations, days, or times those ads aired \* \* \*.” ID at 50-51.<sup>33</sup> We disagree with the ALJ's conclusion that additional

---

<sup>33</sup> Dr. Mazis relied in part on the psychological and consumer behavior theory of “categorization” to discuss the effects of consumers' prior exposure to ab belts and ab belt advertising on their perception of messages in respondents' ads. ID at 49-50. Respondents' expert did not question the validity of categorization theory. Rather, he questioned whether Dr. Mazis had been able to confirm that consumers were “exposed to or recall (sic) the exemplars that formed the foundation for the categories that they, in his estimation, have developed.” Jacoby Tr. 345. However, as discussed below, given the manner in which respondents *expressly pitched their ads to consumers who were already familiar with*

## Commission Opinion

empirical evidence was required to demonstrate that the wave of infomercial ab belt advertising influenced consumers' perceptions of respondents' Ab Force ads. *See* ID at 51. By crafting an advertising campaign that expressly capitalized on consumers' familiarity with the infomercial EMS ab belts, respondents effectively conceded – and in fact intended – that the content of their competitors' ads would influence how consumers would perceive their Ab Force ads. Surely respondents would not have structured their entire advertising campaign around comparisons to infomercials for other ab belts unless they believed that, when prompted by ads for the Ab Force, a significant number of consumers would recall their competitors' claims. Contrary to respondents' contention (RAB 1), the Commission therefore breaks no new ground in concluding that a significant number of such consumers would respond to respondents' comparability claims by associating competitors' claims with the Ab Force device. While we also find such claims within the four corners of respondents' ads, there is no doubt that those efficacy claims would resonate most strongly with consumers targeted by respondents who had already been exposed to repeated advertisements for other ab belts during the same time period. *See Deception Statement*, 103 F.T.C. at 177-78 (when representations are targeted to a specific audience the Commission will consider the representations from the perspective of the targeted group); *Porter & Dietsch*, 90 F.T.C. 770, 864-65 (1977), *aff'd*, 605 F.2d 294 (7th Cir. 1979) (same), *cert. denied*, 445 U.S. 950 (1980); *Pfizer, Inc.*, 81 F.T.C. 23, 58 (1972) (same).

---

*infomercial advertising for EMS ab belts*, it is not necessary for the Commission to address the question that troubled the ALJ (ID at 50-51) – *i.e.*, what empirical evidence would be necessary to establish that consumers' prior exposure to infomercial advertising influenced their perception of claims in respondents' advertising.



Commission Opinion

## 2. Copy Test

Dr. Mazis designed a copy test of the most widely disseminated Ab Force TV ad to help determine whether it conveyed the claims alleged in the Commission's complaint. IDF 193, 195. Using a questionnaire designed by Dr. Mazis, a contractor conducted a mall intercept study in suburban shopping malls in nine different geographic regions. IDF 197, 199. Interviewers screened consumers to bring into the study those who might have some propensity to buy the product – *i.e.*, those who had bought products or used a service for massage or to lose weight or tone muscle within the last 12 months. IDF 206, 209. The questionnaire was designed to screen out consumers who had not made purchases by responding to direct response TV ads or infomercials as well as anyone with specialized knowledge of fitness, weight loss, massage, and research methodology. IDF 207-08, 210.

Consumers who qualified to participate in the study were then assigned at random to a “test group” or a “control group.” IDF 214; Mazis Tr. 90. The “test group” viewed a version of the most widely aired Ab Force TV ad,<sup>34</sup> while the “control group” viewed a “cleansed” version of one of respondents’ two-minute rollout ads. IDF 214; CX 104, 105. In this case, Dr. Mazis, working with a video editor, created the cleansed “control” ad by eliminating respondents’ references to infomercials for other ab belts, stock images of a woman in a bikini and a man performing an abdominal crunch, and some – but not all – images of models wearing the Ab Force device. IDF 217; Mazis Tr. 83-84. (It was not possible to remove every element without fundamentally redesigning the original ad. Mazis Tr. 83, 108.) Dr. Mazis also

---

<sup>34</sup> The tape that Dr. Mazis used in the copy test was received into evidence as CX 104. It depicts the same ad – the most widely disseminated AB Force TV ad – as the tape that was received as JX 4. The transcript of the ad was received as CX 1 F.

## Commission Opinion

added the statement “Ab Force for a relaxing massage” to suggest a massage purpose. CX 58 ¶ 28.

As Dr. Mazis explained, a control ad is the equivalent of a placebo in medical studies – *i.e.*, it accounts for responses that are attributable to factors other than the ad itself.<sup>35</sup> Mazis Tr. 83-84. A control ad is similar to the challenged or “test” ad but, to the extent possible, it is cleansed by eliminating those elements of the ad that allegedly communicate the challenged claims. IDF 216. Generally, the numbers of consumers who perceive the challenged claim in the control ad are subtracted from the numbers who perceive the challenged claim in the test ad. IDF 258-62. If all the challenged elements have been removed from the control ad, the difference between the two figures (“net takeaway”) represents the percentage of consumers whose perception of the challenged claims is based on the particular elements of the test ad. *See* CX 58 ¶ 28; *Stouffer*, 118 F.T.C. at 762 (Initial Decision).

Survey participants saw the test ad or control ad twice. IDF 227. Eighty-one participants were eliminated from the study after they could not recall the name of the product. IDF 228-30. The remaining participants were asked a series of questions, beginning with an open-ended (*i.e.*, “unguided”) question which asked consumers to state in their own words what they perceived in the ads. IDF 231-32. Consumers were then asked about their perceptions using a progressively narrowing series of open-ended

---

<sup>35</sup> The control group responses represent what is sometimes referred to as “noise” – *i.e.*, preexisting beliefs, confusion, or other factors other than the ad at issue that would account for the participant’s affirmative response. Absent other considerations, a survey generally tests more precisely the influence of the stimulus at issue when this “noise” is deducted from the test group responses. *See, e.g., Novartis*, 127 F.T.C. at 619 (Initial Decision); *Stouffer*, 118 F.T.C. at 806.

Commission Opinion

and closed-ended questions.<sup>36</sup> After eliminating consumers whose responses to a “filtering question” indicated they would be inclined to guess,<sup>37</sup> interviewers instructed participants that they would hear a list of statements (*i.e.*, the “closed-ended questions”) of which some, all, or none may have been implied by or made in the ad.<sup>38</sup> IDF 236. Participants were then presented with eight

---

<sup>36</sup> By asking questions in this order of successively narrowing focus, Dr. Mazis ensured that consumers’ answers would not be biased by knowing the content of the questions in advance. *See, e.g., Kraft*, 114 F.T.C. at 70 (Initial Decision); *Stouffer*, 118 F.T.C. at 804.

<sup>37</sup> The filtering question asked: “Does or Doesn’t (sic) the Ab Force commercial say, show, or imply that Ab Force improves users’ appearance, fitness, or health?” CX 58 ¶ 33. Consumers who answered that the commercial does not say, show, or imply that Ab Force improves users’ appearance, fitness, or health were not asked to respond to the five key closed-ended statements. They were funneled to the next question in the survey because their responses to the more specific questions might not be reliable. *See* CX 58 ¶ 33; Mazis Tr. 95.

<sup>38</sup> Only five of the statements that were read to study participants related to claims alleged in the Commission’s complaint:

“Using Ab Force causes users to lose inches around the waist.”

“Using Ab Force results in well-defined abdominal muscles.”

“Using Ab Force removes fat deposits.”

“Using Ab Force is an effective alternative to regular exercise.”

“Using Ab Force causes users to lose weight.”

IDF 238.

## Commission Opinion

statements, five of which related to the allegations of the Commission's complaint, and provided the opportunity to select one of three possible answers: (1) "YES, it is implied by or made in the Ab Force Commercial;" (2) "NO, it is not implied by or made in the Ab Force commercial;" or (3) "You DON'T KNOW or you have NO OPINION." IDF 237-40. An additional three statements – relating to matters that were not at issue (stomach ulcers, nausea, and blood pressure) – were "masking" or "control" questions that Dr. Mazis used to ensure that participants were paying attention and not merely just saying yes to every question (*i.e.*, "yea-saying"). IDF 239.

The copy test results demonstrate that respondents' most widely disseminated TV ad conveyed each of the claims alleged in the Commission's complaint. In this particular copy test, there are three different ways to look at the copy test results: 1) the responses to the open-ended questions (no controls are necessary for these responses); 2) the responses to the closed-ended questions as controlled by the control group responses; and 3) the responses to the closed-ended questions as controlled by the control or "masking" questions.

a. Open-ended Questions

Open-ended questions allow survey participants themselves to articulate the central claim or claims in the ad – those that first come to mind. Marketing experts have found that credible evidence can be obtained from the responses to open-ended questions. *See, e.g., Stouffer*, 118 F.T.C. at 781 (Initial Decision). We agree with the ALJ that it is appropriate to consider the open-ended responses without netting out any controls. ID 58 (*citing Stouffer*, 118 F.T.C. at 808). In this instance, the open-ended question "What did the commercial say, show, or imply about Ab Force?" was followed by asking, "Anything else?" to elicit additional responses. CX 58 ¶ 32.

The copy test showed that a total of 22.3% of participants who viewed the test ad indicated that the ad conveyed that Ab Force

## Commission Opinion

causes users to achieve leaner or flatter abs, loss of weight or fat, a better physique, or loss of inches around the waist. IDF 256-57; CX 58 ¶ 42. As the ALJ determined, these results show that a significant number of respondents took away those claims. ID at 59. These results, if anything, likely understate the consumer take-away because consumers are unlikely to volunteer all of the messages they glean from an ad. The response rate for open-ended questions is usually “much lower than for closed-ended questions where the respondent need only check off the response.” *Sears Roebuck & Co.*, 95 F.T.C. 406, 451 (1980) (Initial Decision), *aff’d*, 676 F.2d 385 (9th Cir. 1982). *See also Stouffer*, 118 F.T.C. 746 at 805 (citing testimony of an expert for Stouffer that “often a researcher must rely on open-ended responses in the magnitude of 8 percent to 10 percent as being meaningful”); *Thompson Medical*, 104 F.T.C. at 697 (Initial Decision) (“open-ended questions . . . do not draw out a complete or exhaustive list of all the things respondents may have on their minds. Rather, respondents will play back the dominant theme or primary impression and, having done that, will probably stop.”); *American Home Products Corp.*, 98 F.T.C. 136, 416 (1981) (“the open-ended questioning technique used by ASI does not elicit an exhaustive playback from consumers of all the representations that may be perceived in the tested advertising”), *enforced as modified*, 695 F.2d 681 (3d Cir. 1983).

b. Closed-ended Questions as Controlled by the Control Group

Marketing experts also rely upon the results to closed-ended questions as indicative of consumer responses to ads. *See Kraft*, 114 F.T.C. at 108 (Initial Decision). Closed-ended questions, however, have the potential to direct participants to certain aspects of an ad. Consequently, participants may respond to such questions based upon yea-saying, inattention, pre-conceptions, or other “noise.” Thus, closed-ended questions require the use of some type of control mechanism. *See Stouffer*, 118 F.T.C. at 808. An appropriate control can involve the use of a control ad, *Kraft*, 114 F.T.C. at 110 (Initial Decision); *Thompson Medical*, 104

## Commission Opinion

F.T.C. at 805, or a control question, *see Stouffer*, 118 F.T.C. at 809. The use of both is not required.

In this case, Dr. Mazis used both a control ad and control or masking questions. Examining first the closed-ended responses as controlled by the control ad group, the ALJ found that 43% of participants in the test ad group and 28.1% of the participants in the control group perceived the message that using the Ab Force belt results in loss of weight. IDF 258; CX 58 ¶ 47. Taking these results and subtracting the control group responses from the test group responses results in a net difference of 14.9%, indicating that 14.9% of consumers perceived the deceptive weight loss claim from the test ad.<sup>39</sup> To the statement that using the Ab Force causes users to lose inches around the waist, 58.1% of the test group and 42.4% of the control group responded affirmatively, resulting in a net difference of 15.7%. IDF 259; CX 58 ¶ 47. The statement that using the Ab Force results in well-defined abdominal muscles received positive responses from 65.4% of the test group and 48.1% of the control group, leaving a 17.3% net difference. IDF 261; CX 58 ¶ 47. For the statement that the Ab Force is an effective alternative to conventional exercise, there was an affirmative response from 39.1% of the test group and 28.6% from the control group, with a net difference of 10.5%. IDF 262; CX 58 ¶ 47. By contrast, for the statement that the Ab Force removes fat deposits, 22.9% of the test group and 19% of the control group responded in the affirmative, with a net difference of only 3.9% that was not statistically significant,

---

<sup>39</sup> The ALJ's findings report a net difference of 15.7% for the question relating to weight loss. *See* IDF 258. It is apparent, however, that this figure is a typographical error and the ALJ inadvertently used the figures that Dr. Mazis reported for the closed-ended questions relating to loss of inches around the waist. *Compare* IDF 258 *with* IDF 259. The actual net difference reported by Dr. Mazis for the question relating to weight loss was 14.9%. Mazis Tr. 107; CX 58 ¶ 47.

Commission Opinion

indicating that the test ad did not clearly communicate this claim compared to the control ad. IDF 260.<sup>40</sup>

c. Closed-ended Questions as Controlled by Control Questions

Closed-ended responses in copy tests can also be adequately controlled by control or masking questions. *See Stouffer*, 118 F.T.C. at 808-09. These questions typically ask about a product attribute reasonably associated with the advertised product or product category, but not one closely linked to the explicit claims in the ad. *See id.* at 806 & n.24. Responses to the control question or questions – like a control group – measure the number of participants who answered based upon yea-saying, inattention, the halo effect, or other “noise.” *See id.* at 806. To eliminate the effect of such external factors, the responses to the control or masking questions are subtracted from responses to the test questions.<sup>41</sup>

---

<sup>40</sup> All of the results were also reported in terms of statistical significance. IDF 266; CX 58 ¶ 44, 46. The results for the question relating to well-defined abdominal muscles was statistically significant at the .001 level. Mazis Tr. 106. The questions relating to loss of inches around the waist and loss of weight were statistically significant at the .01 level. Mazis Tr. 106-07. The net difference for the question relating to using the Ab Force as an effective alternative to exercise was statistically significant at the .05 level. Mazis Tr. 107. The net difference for the question relating to fat deposits was not statistically significant. *Id.* *See also* CX 58 ¶ 47.

<sup>41</sup> When a copy test uses control or masking questions to control for noise in responding to closed-ended questions, one only needs to examine the results from the test ad group. *See Stouffer*, 118 F.T.C. at 806. Results for the control ad group can be ignored.

## Commission Opinion

In this case, the control or masking questions that Dr. Mazis used asked about stomach ulcers, nausea, and blood pressure. CX 58 ¶ 34. Claims about those conditions were not communicated in the ad, so participants should have responded in the negative to closed-ended questions asking whether the ad made claims about those conditions. The highest percentage of participants who responded affirmatively to one of the three control questions – whether due to inattention, preconceptions about the product, or some other reason – was 5 percent. To be conservative, this “noise” was eliminated by subtracting 5 percent from the percentage of participants who responded affirmatively to each of the five closed-ended questions that related to the claims challenged in the Commission’s complaint. After eliminating this noise level from each of the closed-ended questions, 38% of the survey participants perceived the message that using the Ab Force belt results in loss of weight. To the statement that using the Ab Force causes users to lose inches around the waist, 53.1% of survey participants responded affirmatively. The statement that using Ab Force results in well-defined abs got positive responses from 60.4% of participants. For the statement that the Ab Force is an effective alternative to conventional exercise, there was an affirmative response of 34.1%. Finally, for the statement that the Ab Force removes fat deposits, 17.9% of survey participants responded in the affirmative. IDF 264. These results show that – with the exception of the fat deposit claim – at least one third of survey participants found that the ad communicated the challenged claims, a remarkably high takeaway.

d. Copy Test Analysis

Respondents did not offer a copy test of their own to support their interpretation of the challenged ads. Rather, they contend that methodological flaws in the copy test render the results unreliable. RAB at 50-60. Primarily, respondents allege that the copy test was not probative because they believe that it did not



Commission Opinion

control for preexisting beliefs of the survey participants.<sup>42</sup> RAB at 51. Consequently, they argue, it is not possible to determine with any confidence whether the message that consumers took away from their TV ads is attributable to their claims or to consumers' preexisting beliefs about ab belts. RAB at 54-57. Respondents also allege that Dr. Mazis used an overbroad sampling universe, asked leading open-ended and closed-ended questions, and improperly excluded 81 survey participants. RAB at 51.

We conclude that the copy test was probative and that it confirms our facial analysis of respondents' most widely disseminated TV ad. The standard that the Commission applies in determining whether a copy test is methodologically sound is whether it "draw[s] valid samples from the appropriate population, ask[s] appropriate questions in ways that minimize bias, and analyze[s] results correctly." *Thompson Medical Co.*, 104 F.T.C. at 790. Dr. Mazis's copy test satisfies this standard.

Respondents contend that the control ad was not completely "cleansed" of all the elements that Dr. Mazis indicated were responsible for conveying the challenged claims. Consequently, they argue, it is not possible to identify with precision how many of the control group participants provided affirmative answers to the closed-ended questions solely as a result of their preexisting beliefs or other potential influence on their answers. *See* RAB at 54-57.<sup>43</sup> We agree that the control ad for the copy test was not –

---

<sup>42</sup> As noted by Dr. Mazis, the level of affirmative responses for the control was relatively high, most likely due to the influence of the product name, visual images, and preexisting beliefs about ab belts on the study participants' perceptions of the test Ab Force ad. IDF 266.

<sup>43</sup> Respondents' reliance on our decision in *Kraft* for the proposition that a copy test invariably must control for preexisting beliefs is misplaced. RAB at 53-54. As we observed subsequently in *Stouffer*, there is no basis for arguing that such a

## Commission Opinion

and could not be – cleansed of every element that communicated the challenged claims.<sup>44</sup> ID at 54; IDF 217-220. Dr. Mazis acknowledged this limitation (IDF 221; Mazis Tr. 108),<sup>45</sup> but this purported “flaw” actually worked in respondents’ favor. Regardless of the cause – whether due to preexisting beliefs or ad elements that could not be removed altogether from the control ad – the net difference between the test group and control group responses was, if anything, *reduced* as a result of the relatively high percentage of control group participants who reported affirmative responses to the closed-ended questions. ID at 54. Thus, there is no merit to the contention that respondents were prejudiced by using an incompletely “cleansed” control ad, as any reduction in net takeaway would favor respondents.<sup>46</sup>

---

control is invariably required. *Stouffer*, 118 F.T.C. at 810.

<sup>44</sup> This case illustrates the difficulties inherent in designing a control ad where the product name and visual elements appearing throughout the ad communicate the challenged messages to consumers. On the one hand, it may not be feasible in such cases to excise all of the ad elements without creating something that would not be recognizable as an actual ad. On the other hand, writing a completely new control ad to show consumers is not a viable option because it would introduce new, uncontrolled sources of bias into the copy test.

<sup>45</sup> While the copy test may be flawed for its failure to excise from the control ad all of the elements that communicated the challenged claims, copy tests do not have to be flawless to be reasonably reliable and probative. *See, e.g., Novartis*, 127 F.T.C. at 699 n.24; *Stouffer*, 118 F.T.C. at 807; *Bristol-Myers Co.*, 85 F.T.C. 688, 744 (1975).

<sup>46</sup> Respondents suggest that the random assignment of copy test participants to the test group or the control group is inadequate to control for preexisting beliefs. RAB at 54-57. That is exactly what the control group is for, however. One cannot

Commission Opinion

Regardless of the reduction in the difference between the test group and control group responses, the ALJ held correctly that as a matter of law the net takeaway – which ranged from 10.5% to 17.3% for all claims except the fat deposit claim<sup>47</sup> – was sufficient to conclude that the challenged claims were communicated. ID at 57-58 (setting forth Commission cases and Lanham Act cases where net takeaway of 10% – or even lower – supported finding that the ads communicated the claims at issue); *see, e.g., Firestone Tire & Rubber Co. v. FTC*, 481 F.2d 246, 249 (6th Cir. 1973) (it would be “hard to overturn the deception findings of the Commission if the ad thus misled 15% (or 10%) of the buying public”); *Mutual of Omaha Ins. Co. v. Novak*, 836 F.2d 397, 400 (8th Cir. 1987) (10% net takeaway was enough to support finding that claim was communicated in Lanham Act case); *Goya Foods, Inc. v. Condal Distributions, Inc.*, 732 F. Supp. 453, 456-57 (S.D.N.Y. 1990) (net takeaway of 9% justified finding claim was made).

Furthermore, though respondents argue that consumers’ preexisting beliefs fatally undermine the copy test results, we believe that their intentional invocation of other ab belt infomercials cuts the other way. In an attempt to argue that the copy test is unreliable, respondents claim that, among other things, “the existence of other, heavily disseminated advertising

---

possibly account for all of the differences between people – whether based on education level, income, ethnicity, or any other factor – that could possibly affect consumers’ perception of an ad. Randomization is the proper technique to control for these possible differences. Mazis Tr. 153. Statistically significant results for comparisons of the test group and control group responses – here, for all but the fat deposit claim – belie the suggestion that the results could be due to chance assignment between the two groups.

<sup>47</sup> For this claim, the 3.9% net difference is not statistically significant. Thus, this result indicates nothing about consumer perception of this particular claim.

## Commission Opinion

may have contributed to consumers' exposure to previous claims, thus influencing their results." RAB at 53-54. Yet respondents' strategy in promoting the Ab Force was to invite consumers to recall the claims in advertising that consumers had previously seen for other ab belts – advertising to which respondents referred in every one of their ads.<sup>48</sup> Indeed, it was exactly that “other, heavily disseminated advertising” that respondents took pains to evoke in their own advertising – including claims that respondents knew were unsubstantiated. *See, e.g.,* Khubani Tr. 273-74, 490; ID at 45; IDF 58-60; CX 1 H.<sup>49</sup> Where, as here, an advertiser exploits preexisting beliefs deliberately by inviting consumers to recall the claims in other ads to help convey a message, it makes little sense to remove the influence of those other ads. *See Simeon Management Corp. v. FTC*, 579 F.2d 1137, 1146 (9th Cir. 1978) (the fact that a false belief “is attributable to factors other than the advertisement itself does not preclude the advertisement from being deceptive”). Accordingly, we believe that the copy test results as controlled by the control group – which serves to filter out the effects of preexisting beliefs – likely understate the extent to which the challenged claims were communicated.

---

<sup>48</sup> IDF 114. *See, e.g.,* CX 1-H (“Have you seen those fantastic Electronic Ab Belt infomercials on TV? They’re amazing . . . promising to get our abs in great shape fast – without exercise!”); JX 2 (tape), CX 1 B (transcript) (“I’m sure you’ve seen those fantastic electronic ab belt infomercials on TV. They’re amazing. They’re the latest fitness craze to sweep the country and everybody wants one.”); RX 49 (“Have you seen those fantastic electronic ab belt infomercials on TV? They’re amazing! They’re the latest craze to sweep the country and everybody wants one!”).

<sup>49</sup> This is not a case where an advertiser selling an item for one purpose is simply aware of a consumer misperception that the product is effective for another use. Respondents’ campaign was built around the existence of and exploited that misperception.

Commission Opinion

In this instance, because of respondents' consistent, overt references to competitors' advertising claims, it is clear that respondents specially targeted consumers who had preexisting misperceptions based on those ads. We recognize, however, that many cases may not be so simple. In some cases, for example, an advertiser might not be liable for misperceptions that consumers hold – even if the advertiser is aware of them – if an ad does not exploit that misperception. In other cases, however, an advertiser might be liable if the ad leads reasonable consumers to take away a misleading message, even if the ad does not invoke other ads and even if there is no evidence that the advertiser intended to communicate a misleading message. Our holding, therefore, is limited to these facts: here, it is unnecessary to control for preexisting beliefs that are due in part to the extensive prior advertising that respondents' ads invoke.

We turn next to respondents' contentions that Dr. Mazis improperly excluded 81 survey participants, used an overbroad sampling universe, and asked leading open-ended and closed-ended questions. RAB at 51. We agree with the ALJ (ID at 57) that Dr. Mazis's exclusion of inattentive participants was consistent with the goal of a copy test – *i.e.* to identify a universe of potential purchasers of the product and determine what messages they perceive in an ad. Given that persons who cannot recall the name of a product would not be likely to purchase it (*see* Mazis Tr. 94), it was reasonable for Dr. Mazis to exclude such inattentive participants from the survey universe and, in fact, it is commonly done. Mazis Tr. 102; *see, e.g., Kraft*, 114 F.T.C. at 70 n.2 (excluding participants who could not remember brand name or responded “don't know” to a question asking them to restate the points in the ad).

Respondents' remaining objections to the copy test similarly lack merit. With regard to the sampling universe, the ALJ rejected respondents' contention that the survey population – *i.e.*, those who in the last 12 months had purchased a product or service for weight loss, toning, or massage and also purchased any product by responding to a direct response TV ad – was

## Commission Opinion

overbroad. ID at 52-53. Respondents would have limited the survey to those who had purchased a product for weight loss, toning, or massage from a direct response ad. Jacoby Tr. 355-56; *see* RAB at 51. The ALJ held that Dr. Mazis's definition of the survey universe was "reasonably reliable and probative." ID at 53. We agree. The goal of the study was to determine whether potential purchasers of the Ab Force – *i.e.*, those consumers that respondents intended to persuade – perceived the misrepresentations that were alleged in the Commission's complaint. CX 58 ¶ 22. There is no basis for assuming that only consumers who had purchased weight loss, toning, or massage products from direct response TV, rather than by some other means, would be potential Ab Force purchasers. As they had already purchased other products through that venue and demonstrated an interest in this type of product, it is not unreasonable to include them as potential Ab Force purchasers.

With regard to the allegation that the closed-ended questions were leading (RAB at 51), we conclude that the copy test instructions (CX 58 ¶ 34 & Exh. D) were adequate to ensure that participants would give equal weight to all possible responses. *See* ID at 53. In addition, using two different versions of the questionnaire, Dr. Mazis changed the order of the questions. CX 58 ¶ 29; Mazis Tr. 92, 96. The rotation in the order in which the questions were posed supplemented other controls. ID at 53-54; Mazis Tr. 96.

Turning to respondents' allegation (RAB at 51) that the wording of the closed-ended questions invited "yea-saying," we agree with the ALJ that Dr. Mazis used appropriate techniques to ensure that the copy test results would not be compromised by the yea-saying phenomenon or other factors. ID at 53. These techniques included using a filter question to eliminate guessing; rotating the order of questions; and reading the three possible answers to each question before asking any survey question. *Id.* Dr. Mazis also used control or "masking" questions – *i.e.*, questions about attributes that are not closely linked to the alleged claims in the ads – to identify participants whose affirmative

Commission Opinion

answers to closed-ended questions about the test ad could be attributed to yea-saying, inattention, or other factors. *Id.* at 53-54.

To summarize, we conclude that, although extrinsic evidence was not required to find liability, the copy test and other extrinsic evidence helped confirm our own determination that respondents' ads communicated the challenged claims to significant numbers of reasonable consumers.

### III. First Amendment Claims

Respondents' contention that the First Amendment limits the Commission's ability to conduct a facial analysis of ads to "a narrow category of cases" in essence rearticulates their previous objections to the ALJ's interpretation of their ads. RAB at 64. Simply put, respondents' First Amendment argument is equally without merit: they cannot manufacture a constitutional issue out of a straightforward deceptive advertising case. The First Amendment does not protect deceptive commercial speech. *See Dun & Bradstreet, Inc. v. Greenmoss Builders, Inc.*, 472 U.S. 749, 762 (1985); *Virginia State Bd. of Pharmacy v. Virginia Citizens Consumer Council*, 425 U.S. 748, 771-72 (1976).

Respondents concede, as they must, the Commission's authority "to engage in facial analysis and to find, in an appropriate case, the existence of implied claims without reliance on extrinsic evidence \* \* \*." RAB at 63. Respondents contend, however, that there is no basis for the ALJ's facial analysis and "no reliable extrinsic evidence that consumers actually took such claims away from the advertisements." RAB at 61. According to respondents, "substantial constitutional problems" concerning regulation of commercial speech would be raised if the alleged implied claims "have to be teased and constructed out of background elements." RAB at 64.

This plainly is not a case in which implied claims "have to be teased and constructed out of background elements." *Id.* The challenged claims are clearly communicated. Moreover, the

## Commission Opinion

Commission's facial analysis of the implied claims is buttressed by extrinsic evidence, including expert testimony and a copy test.

Moreover, contrary to respondents' claim (RAB at 67), nothing in *In re R.M.J.*, 455 U.S. 191, 202 (1982), or its progeny suggests that facial analysis runs an "inherent risk" (RAB at 68) of restricting protected commercial speech. Indeed, in *Zauderer v. Office of Disciplinary Counsel*, 471 U.S. 626, 652-53 (1985), the Supreme Court squarely rejected that proposition, ruling that no consumer survey was required to prove that the public would be misled by a law firm's ad that claimed "if there is no recovery, no legal fees are owed by our clients." Although at issue was the public perception of the distinction between such technical terms as "fees" and "costs," the Court relied on commonsense assumptions as to how consumers would interpret the language to find that the possibility of deception was so "self-evident" that it would not require state disciplinary authorities to "conduct a survey of the public before it [may] determine that the [advertisement] had a tendency to mislead." *Id.* at 653 (*quoting Colgate-Palmolive Co.*, 380 U.S. at 391-92). In *R.M.J.*, the Supreme Court considered a different issue – whether a state regulatory scheme that broadly prohibited attorney advertising without regard to whether the solicitations were false or misleading was constitutional. Because such blanket prohibitions risk snaring truthful expression along with fraudulent and deceptive speech, the Court concluded that to justify a prophylactic rule the government must demonstrate that the prohibited conduct is either inherently likely to deceive, or provide record evidence that a particular method of advertising in fact has been deceptive. *R.M.J.*, 455 U.S. at 202. Such prophylactic rules are not at issue here. Rather, this case involves an adjudicative finding that the particular ads challenged in this case are false and misleading.

Thus, respondents' cited decisions provide absolutely no support for the proposition that the First Amendment requires that the government provide extrinsic "evidence that a particular form or method of advertising has in fact been deceptive." RAB at 67.



Commission Opinion

*See American Home Products Corp. v. FTC*, 695 F.2d 681, 687 n.10 (3d Cir. 1982) (argument that the First Amendment requires an order to be based on empirical evidence that the public was misled is “distortion” of *R.M.J.*). When implied claims are self-evident, as they are in this case, there is no constitutional mandate for the government to survey consumers before it can find that an ad is misleading. *Zauderer*, 471 U.S. at 652-53; *see Kraft*, 970 F.2d at 320; *FTC v. Brown & Williamson Tobacco Corp.*, 778 F.2d 35, 41 (D.C. Cir. 1985).<sup>50</sup> *See also Zauderer*, 471 U.S. at 652-53 (when the alleged deception rises to a “commonplace,” a court may itself find the deception to be “self-evident”).<sup>51</sup>

In the present case, the Commission has considered carefully all the extrinsic evidence and, notwithstanding respondents’ allegations of methodological flaws, we conclude that it

---

<sup>50</sup> Even if facial analysis might, in rare cases, raise the sorts of concerns that respondents have raised about an “inherent risk of restricting protected speech” (RAB at 68), that problem would not arise with respect to an order that, as here, simply prohibits false and deceptive claims and requires advertisers to have substantiation for any claims they might make in the future.

<sup>51</sup> Respondents also contend that a facial analysis is necessarily a “subjective measure that looks into the minds of the Commissioners.” RAB at 62. According to respondents, such an analysis effectively denies a respondent “meaningful appellate review” of the Commission’s decision except in “the most extreme cases” because a reviewing court may not inquire into the minds of agency decision makers. RAB at 65. Given that a reviewing court can conduct an independent review of the ads, there is no foundation for the argument that a facial analysis of the ads would deny respondents effective review of an adverse Commission decision. Moreover, this contention would logically apply to any exercise of the Commission’s authority to determine implied claims; yet respondents admit that, except in unusual cases, the Commission has authority to determine implied claims.

## Commission Opinion

corroborates the Commission's own interpretation of the ads. Thus, respondents' concern about an "inherent risk of restricting protected speech" (RAB at 68) is inapposite. The challenged claims are obvious from the face of the ads. *See Kraft*, 970 F.2d at 320-21.

In its amicus brief, the National Association of Chain Drug Stores ("NACDS") raises concerns about chilling commercial speech, specifically comparative advertising. NACDS asks the Commission to clarify when the sponsor of a "compare and save" advertisement may be deemed "derivatively liable" for misleading implied claims in an advertisement that is part of the "target universe" for the sponsor's "compare and save" advertisement. Amicus at 13. To be sure, truthful comparative advertising, including "compare and save" advertising, is generally valuable for consumers and competition. *See Federal Trade Commission Statement of Policy Regarding Comparative Advertising*, 16 C.F.R. § 14.15(b) (1979). Head-to-head product comparisons can demonstrate a product's superiority over a competitor or highlight a price differential. As noted above, however, this case does not stand for the proposition that compare and save advertisers are derivatively liable for all advertising claims made by a competitor by virtue of a comparison. Putting aside the fact that respondents' ads communicated the challenged claims within the four corners of the ads, the comparisons in this case are readily distinguishable from the prototypical "compare and save" advertising where an advertiser places a terse, "Compare to \_\_\_" message on a product package or "shelf talker" that names a competing brand's product. Respondents' ads expressly referred consumers to advertisements for the comparison products – not just to the products themselves – and then proceeded to repeat and incorporate claims from those ads. Moreover, as respondents knew,<sup>52</sup> ab belts as a product class were consistently positioned as products that would improve a user's health or fitness or cause weight loss, but the competing ab

---

<sup>52</sup> *See, e.g.,* Khubani Tr. 273-74, 445, 461, 471-72.

Commission Opinion

belts – and the Ab Force, as respondents again knew<sup>53</sup> – had no actual value for those purposes. This case does not present the question, and the Commission does not address, what implied claims are communicated when an advertiser merely claims that it is comparable to a competitor’s product without conveying additional information.

As for the possible “chilling effect” on the dissemination of truthful “compare and save” advertising, we reject the proposition that implied claims are inherently unpredictable. *Kraft*, 970 F.2d at 320-21 (rejecting First Amendment challenge “when the alleged deception although implied, is conspicuous”). Indeed, this case provides a good example of implied claims that are so conspicuous and self-evident from the face of an ad that extrinsic evidence is simply not required to determine what messages the ad likely conveys to a reasonable consumer. We recognize, of course, that the role of consumer perception creates an inevitable continuum of meaning in ad interpretation.<sup>54</sup> It does not follow, however, that finding liability based in part on respondents’ parroting of competitors’ ad claims will have a “chilling effect” on the dissemination of legitimate “compare and save” advertising. *See, e.g., 44 Liquormart, Inc. v. Rhode Island*, 517 U.S. 484, 523 n.4 (1996) (Thomas, J., concurring) (commercial speech, the “offspring of economic self-interest,” is a “hardy breed of expression”) (*quoting Central Hudson Gas & Elec. Corp. v. Public Service Comm’n*, 447 U.S. 557, 564 n.6 (1980) (internal quotation marks omitted)).

A respondent who believes that an advertisement does not communicate an implied claim may, of course, choose to conduct a copy test or submit other evidence demonstrating that consumers

---

<sup>53</sup> *See* ID at 45; IDF 58-60; Khubani, Tr. 490; JX 6 ¶¶ 16-19.

<sup>54</sup> Indeed, even where extrinsic evidence has been introduced, differences of opinion can emerge as to which claims are conveyed to consumers.

## Commission Opinion

do not take away such a claim. These respondents did not. The Commission will consider carefully all the extrinsic evidence, including consumer surveys, that the parties may introduce as to the meaning of challenged ads. *See Stouffer*, 118 F.T.C. at 799; *Kraft*, 114 F.T.C. at 121-22; *Thompson Medical*, 104 F.T.C. at 789-90.

**IV. Remedy**

In considering the breadth of appropriate fencing-in, the ALJ acknowledged respondents' substantial resources, their experience and sophistication in marketing a broad array of products, and the deliberate nature of their violations. ID at 64-65. He nonetheless limited fencing-in relief to any product, service, or program "promoting the efficacy of or pertaining to health, weight loss, fitness, or exercise benefits." ID at 66. Complaint counsel contend that more comprehensive fencing-in relief is necessary, including a performance bond and a requirement that respondents have substantiation prior to advertising the "Ab Force, any other EMS device, or any food, drug, dietary supplement, device, or any other product, service, or program" for any representation "about weight, inch, or fat loss, muscle definition, or the health benefits, safety, or efficacy" of the product. CAB at 67. We conclude that more comprehensive fencing-in relief is warranted but are not persuaded that the record supports a performance bond requirement.

Courts have long recognized that the Commission has considerable discretion in fashioning an appropriate remedial order, subject to the constraint that it must bear a reasonable relationship to the unlawful practices. *See, e.g., Colgate-Palmolive Co.*, 380 U.S. at 394-95; *FTC v. Ruberoid Co.*, 343 U.S. 470, 473 (1952); *Jacob Siegel Co.*, 327 U.S. at 612-13. In determining the appropriate scope of relief, the Commission considers three factors: (1) the seriousness and deliberateness of the violation; (2) the ease with which the violation may be transferred to other products; and (3) whether the respondent has a history of prior violations. *See Stouffer*, 118 F.T.C. at 811;

Commission Opinion

*Thompson Medical*, 104 F.T.C. at 833. All three elements need not be present to warrant fencing-in. See *Sears, Roebuck & Co. v. FTC*, 676 F.2d 385, 392 (9th Cir. 1982); *Porter & Dietsch*, 605 F.2d at 306.

As the ALJ found, the first two elements weigh in favor of broad fencing-in. ID at 64-65. We agree. First, as discussed above, the alleged violations were serious and deliberate.<sup>55</sup> This is not a case where the product advertised was essentially fit for the intended purpose but the advertising oversold the product's qualities in some way. Rather, respondents promised that Ab Force users would get health, fitness, and weight loss benefits, but without substantiation that the device provided any such benefits to those who purchased it. Indeed, Mr. Khubani admitted that he knew before the ad campaign started that he lacked substantiation for the claims that users "could get into shape fast without exercise" and could get "a flatter tummy without painful sit-ups." ID at 45; IDF 58-60; Khubani, Tr. 490. Yet the day after he removed those direct claims from a proposed television script, a radio ad he had authored hit the air waves; the ad proclaimed that the Ab Force "is just as powerful and effective" as other ab belts that "promis[ed] to get [one's] abs into great shape fast – without exercise." Khubani, Tr. 484-86; CX 1 H.

Respondents contend that the evolution of the advertising campaign demonstrates that they took their compliance obligations seriously. Although the respondents slightly modified

---

<sup>55</sup> The ALJ seems to have treated a portion of Mr. Khubani's trial testimony as an admission that express claims in the so-called "test" ads were still communicated implicitly in respondents' "rollout" ads. IDF 87-89. In our view, the cited testimony is inconclusive on this point. Compare Khubani Tr. 492 ("[A]ll these scripts were the same message.") with Khubani Tr. 496 ("There were some minor changes made in the wording. In my opinion, the message was – was still the same, compare and save."). Accordingly, we do not rely on it.

## Commission Opinion

their claims in the ads that were disseminated most widely, we have no doubt that the respondents deliberately intended to communicate the implied claims even in the later ads, as the ALJ determined. ID at 64-65.<sup>56</sup> It is not plausible that the respondents expected to sell the Ab Force as a mere phenomenon. The record demonstrates that respondents carefully and deliberately timed their launch of the Ab Force promotion to coincide with an ongoing infomercial promotion of EMS ab belts by respondents' competitors – a situation that respondents quickly put to their advantage with their repeated comparisons between the Ab Force and “those ‘fantastic electronic Ab belt infomercials on TV’” or “ab belts sold by other companies.” IDF 114. Respondents were well aware of the express claims in those infomercials – claims that respondents concede were not only unsubstantiated, but false. *See* ID at 60; IDF 270-73; JX 6 ¶¶ 16-19. As the ALJ concluded, while Mr. Khubani did not want to make those claims expressly, “the evidence shows that Khubani intended to imply those same claims. Merely removing false express claims will not protect an advertisement where the same claims are implied.” ID at 45

---

<sup>56</sup> For example, after legal review, the phrase “relaxing massage” was added as a briefly flashing superscript in two roll-out television ads. IDF 100-01. Neither that phrase nor the word “massage” were used in any other ads or in any of Mr. Khubani's radio and television scripts, however. IDF 106. The user manual – which consumers received only after the purchase – stated that the product was “intended to provide a relaxing massage. Ab Force is not intended for medical use, for the treatment of any medical condition, or for any permanent physical changes.” RX 45-46; IDF 104-05. This disclaimer must have been mystifying to consumers who purchased the product – for example, consumers who purchased the Ab Force after responding to the ad that opened respondents' promotional campaign. That ad compared the Ab Force to other ab belts that “promis[ed] to get our abs into great shape fast – without exercise” and said ab belts were “the latest fitness craze to sweep the country,” but said nothing about massage. IDF 86, 93, 104-08; CX 1 H.

Commission Opinion

(citing *Thompson Medical*, 104 FTC at 792). Furthermore, the nationwide dissemination in multiple media, cost of the campaign, and risk that purchasers of the Ab Force would view the product as a substitute for regular exercise all demonstrate that the violations were serious.

Second, as for the ease with which the claims may be transferred to other products, respondents market a broad range of products and services. ID at 65; IDF 4. Respondents' marketing strategy is potentially applicable to almost any kind of product or service, including the many products it already markets. They already employ the same strategy with other products – in fact, it is one of the company's standard techniques. *Khubani Tr.* 247-49.<sup>57</sup> Given that the violations were serious and deliberate and easily transferable to other products, we conclude that comprehensive fencing-in relief is necessary to ensure that respondents will not be able to use the same or similar strategies to mislead consumers in the future.

These two factors – the serious and deliberate nature of respondents' violations and the ease with which they can be transferred to any one of the myriad of services and products offered by respondents – are sufficient, without more, to justify comprehensive coverage in our final order. Nevertheless, respondents' history of entering into multiple consent orders with

---

<sup>57</sup> Indeed, as described by respondent *Khubani*, a strategy that *Telebrands* has used on a number of occasions (one or two times a year on average) is to identify existing popular products and then enter the market as a competitor at a lower price. *Khubani Tr.* 439. To be clear, there is nothing wrong with this approach, but the fact that respondents' deceptive practice here is easily transferable to the other products that it markets in this manner is relevant to the remedy.

## Commission Opinion

the FTC<sup>58</sup> – the third element that we consider – provides additional support for more stringent fencing-in. Thus, we disagree with the ALJ’s conclusion that Mr. Khubani’s previous consent agreements “cannot be utilized to form the basis for

---

<sup>58</sup> In the past 15 years, Mr. Khubani has entered into three separate consent agreements with the Commission resolving alleged law violations – some addressing multiple counts – and agreed to a modification of one consent agreement; Mr. Khubani and Telebrands paid more than \$900,000 in civil penalties. In 1990, respondent Khubani and a mail order company he operated, Direct Marketing of Virginia, settled allegations they were violating the Commission’s Mail Order Rule by paying a \$30,000 civil penalty. *United States v. Azad Int’l, Inc.*, No. 90-CV-2412-PLN (S.D.N.Y. April 12, 1990). Subsequently, in September 1996, Mr. Khubani and Telebrands paid a \$95,000 civil penalty to settle charges that they failed to ship their products in a timely manner in violation of the Mail Order Rule. *United States v. Telebrands Corp.*, Civ. No. 96-0827-R (W.D. Va. Sept. 18, 1996). Also in 1996, Mr. Khubani and Telebrands settled charges that they had made unsubstantiated performance and efficacy claims for two products, the WhisperXL hearing aid and Sweda Power Antenna, and misrepresented the terms of a money-back guarantee. They stipulated to entry of an administrative cease and desist order that prohibited them from making unsubstantiated or false performance claims with respect to the Sweda Power Antenna and any hearing aid. *In re Telebrands Corp.*, 122 F.T.C. 512 (1996). Finally, in 1999, respondents Telebrands and Mr. Khubani stipulated to a modification of the 1996 Mail Order Rule civil penalty order providing that those respondents pay \$800,000 in civil penalties and requiring, as an additional remedy, that they fund an independent monitor with expertise in mail or telephone order fulfillment. *United States v. Telebrands Corp.*, Civ. No. 96-0827-R (W.D. Va. Sept. 1, 1999).



Commission Opinion

imposing a broad fencing in order in this case.”<sup>59</sup> ID at 65. We

---

<sup>59</sup> The ALJ held that broad fencing-in relief was warranted based on the deliberateness and seriousness of the violations and the ease with which respondents’ unlawful conduct could be transferred to other products. ID at 66. With regard to complaint counsel’s contention that respondents’ history of prior consent orders should also be considered, the ALJ ruled that the consent orders were not in evidence and did not involve any findings of liability. ID at 65. Accordingly, he declined to consider them in determining the appropriate scope of fencing-in relief.

We agree with the ALJ that the deliberateness, seriousness, and transferability of respondents’ violations are sufficient, without more, to warrant broad fencing-in relief. However, we do not agree with the ALJ that complaint counsel’s failure to offer the prior consent orders into evidence precludes the Commission from considering them in fashioning its order. The Commission may take official notice of them to the extent they are on the public record. *See, e.g., Chicago Bridge & Iron Co.*, 2005 FTC LEXIS 70 at \*39 n.82 (2005) (taking official notice of SEC K-1 filing); *South Carolina State Board of Dentistry*, FTC Docket No. 9311, slip op. at 11-12 (July 30, 2004) (matters of official notice include those contained in public records, such as judicial decisions, statutes, regulations, and reports and records of administrative agencies); *Avnet Inc.*, 82 F.T.C. 391, 464 n.31 (1973) (taking official notice of U.S. Census report), *aff’d*, 511 F.2d 70 (7th Cir. 1975), *cert. denied*, 423 U.S. 833 (1975). Furthermore, while complaint counsel could have filed a formal motion before the ALJ to take judicial notice of the consent orders earlier in the proceedings, respondents have no claim of prejudice; indeed, the existence of the consent orders is undisputed. As for complaint counsel’s alleged “failure to follow the formalities” (RRB at 63), the Commission’s adjudicative rules specifically anticipate the possibility that in rendering a decision on the merits the Commission *sua sponte* will take official notice of a material fact. *See* 16 C.F.R. 3.43(d) (“When any decision of an [ALJ] or of the

## Commission Opinion

recognize that litigants may settle matters for a variety of reasons; indeed, whether in federal court or at the Commission, most litigation is settled. Settlement is often an efficient way of resolving legal disputes. Holding a prior consent agreement against a party in a subsequent action may affect that party's decision to settle. Having said that, if every consent agreement were inadmissible, the Commission could never fashion relief appropriate to address a pattern of conduct by someone who repeatedly violates the law but invariably settles. Moreover, we are well aware that a majority of the Commissioners must have "reason to believe" that the law has been violated before issuing a proposed complaint, 15 U.S.C. § 45, including any proposed complaint accompanied by a proposed consent agreement.

Thus, we hold that it is appropriate to consider a pattern of consent agreements. The fact that a party has entered into one prior consent agreement with the Commission may say little about the appropriate scope of relief in a future case. *See Thompson Medical*, 104 F.T.C. at 833 n.78 ("Because consent orders do not constitute a legal admission of wrongdoing, we will not use a single consent order as a basis for concluding that Thompson has a history of past violations."). The Commission, however, may properly take into account a respondent's pattern and practice of alleged law violations that result in a succession of narrowly tailored injunctive orders in determining whether more comprehensive relief is called for. *See Sterling Drug Inc.*, 102

---

Commission rests, in whole or in part, upon the taking of official notice of a material fact not appearing in evidence of record, opportunity to disprove such noticed fact shall be granted any party making timely motion therefor."). Thus, the Commission's ability to take official notice of a fact does not turn on whether any of the parties has filed a formal motion before the ALJ, as respondents seem to suggest. *Cf. Dobrota v. INS*, 195 F.3d 970, 973 (7th Cir. 1999) (taking *sua sponte* judicial notice of updated country conditions in light of parties' failure to introduce such information).

Commission Opinion

F.T.C. 395, 793 n.54 (1983) (five outstanding advertising orders, one litigated and four by consent), *aff'd*, 741 F.2d 1146 (9th Cir. 1984), *cert. denied*, 470 U.S. 1084 (1985); *Jay Norris Corp.*, 91 F.T.C. at 856 n.33 (three consent orders in 15 years); *see also FTC v. SlimAmerica, Inc.*, 77 F. Supp. 2d 1263, 1270-72 (S.D. Fla. 1999) (seven prior court and administrative orders entered by consent). Respondents' previous consent order with the Commission relating to allegedly unsubstantiated advertising claims for a hearing aid and an antenna – leaving aside the troubling misrepresentation relating to the company's money-back guarantee – demonstrates that respondents were well aware of the Commission's advertising substantiation requirements, including requirements for "devices" such as the Ab Force. Moreover, the alleged violations that resulted in a succession of consent orders relating to Mail Order Rule violations – culminating in an order that required the company to hire a third party monitor to oversee compliance – suggests a troubling inability to comply with the consumer protection laws enforced by the Commission.

Accordingly, we modify the fencing-in provisions in the ALJ's order to take into account the demonstrated need to protect the public from future unfair or deceptive acts or practices by respondents. Our Order requires respondents to substantiate all claims about weight, inch, or fat loss; muscle definition; or the health benefits, safety, or efficacy of any product, service, or program. This broader product coverage is warranted in light of the seriousness of this violation; the ease of transferability of these deceptive practices to products of all types; and the pattern of alleged illegal activity that resulted in the previous consent orders.

All product coverage is reasonably related to the Commission's goal of protecting the public. As the Supreme Court stated in *Colgate-Palmolive*, "We think it reasonable for the Commission to frame its order broadly enough to prevent respondents from engaging in similarly illegal practices in future advertisements." 380 U.S. at 395; *id.* at 394-95 (upholding order prohibiting deceptive mock-ups in advertisements for "any product" and noting that "courts will not interfere except where the remedy

## Commission Opinion

selected has no reasonable relation to the unlawful practices found to exist”). *See also Jay Norris Corp.*, 598 F.2d 1244 (2d Cir. 1979), *cert. denied*, 444 U.S. 980 (1979) (affirming Commission order fencing-in claims for all products). We recognize that this order will impose some additional burden on respondents to substantiate claims for products that the ALJ’s order would not cover, but Commission law requires such substantiation for any advertiser in any case. *See, e.g., Substantiation Statement*, 104 F.T.C. at 839. In limiting these provisions to a prohibition on deceptive and unsubstantiated claims, the Commission’s order leaves respondents free to advertise in any way they choose, except deceptively. Moreover, respondents market a wide range of products; efficacy claims for most of these products would not be covered by the ALJ’s order as they do not relate to health, weight loss, fitness, or exercise benefits.<sup>60</sup> In fact, one of the respondents’ previous consent orders<sup>61</sup> relates to unsubstantiated performance and efficacy claims for an antenna – the type of deception that would violate Section 5 of the FTC Act but not the ALJ’s order. As the Commission held in *Litton Industries, Inc.*, 97 F.T.C. 1 (1981), *aff’d as modified*, 676 F.2d 364 (9th Cir. 1982):

---

<sup>60</sup> Products respondents have marketed in the past include Ambervision Sunglasses, the Magic Hanger, Dental White Tooth Whitening System, the Safety Can Opener, the Audobon Singing Bird Clock, the Better Pasta Pot, and the Roll-a-Hose Flat Hose. IDF 22. Another recent Telebrands product was the Cyclone Diet, a blended powder that would supposedly cause users to “lose ten pounds in two days,” a seemingly impossible claim. Khubani Tr. 251-52. *Cf.* Federal Trade Commission, *Red Flag: Bogus Weight Loss Claims*, available at <[www.ftc.gov/bcp/online/edcams/redflag/beyond.html](http://www.ftc.gov/bcp/online/edcams/redflag/beyond.html)> (setting forth claims for weight loss products that are false on their face because they are not scientifically feasible).

<sup>61</sup> *See In re Telebrands Corp.*, 122 F.T.C. 512 (1996).

Commission Opinion

The rationale for entry of a multi-product order based upon violations in the advertising of only one or a few products is that many kinds of deceptive advertising are readily transferrable to a variety of products, and it would serve the public poorly to halt the use of a deceptive tactic in the advertising of one product if the respondent remained free to repeat the deceptive practice in another guise, with no threat of sanction save for another order to cease and desist.

*Id.* at 78-79 (citations omitted).

We turn then to complaint counsel's request that the Commission order respondent Khubani to obtain a performance bond of \$1 million before engaging in or assisting others in engaging in any manufacturing, sale, or promotion of any "device," as that term is defined in Section 15(d) of the FTC Act, 15 U.S.C. § 55(d).<sup>62</sup> As the ALJ observed, although the Commission has accepted numerous consent agreements that require respondents to obtain performance bonds, it has not required a performance bond in a litigated administrative case. *ID* at 63. However, this is not a proper basis for declining to impose such relief.<sup>63</sup> Courts have recognized that the Commission has

---

<sup>62</sup> While Mr. Khubani challenges the application of a bond requirement to himself as an individual rather than to the corporation, it is not only appropriate but sometimes preferable to make the principal of a corporation subject to fencing-in so that the individual cannot circumvent the order by establishing a new company with a different name.

<sup>63</sup> Respondents' reliance on *Heater v. FTC*, 503 F.2d 321 (9th Cir. 1974) for the proposition that such relief is beyond the Commission's remedial authority is misplaced. RRB at 65-67. In *Heater*, the Ninth Circuit specifically recognized the Commission's authority to order affirmative relief, but treated restitution as a private, retroactive remedy – tantamount to an award of damages – that was beyond the Commission's authority

## Commission Opinion

broad discretion in its choice of remedies and is authorized to impose fencing-in provisions to prevent a recurrence of the same or similar violations and “to close all roads to the prohibited goal” so the respondent cannot simply circumvent the order. *Ruberoid*, 343 U.S. at 473. The Commission has employed a wide variety of fencing-in remedies to achieve effective relief. *See, e.g., FTC v. Dean Foods Co.*, 384 U.S. 597, 606 (1966) (divestiture order); *Warner-Lambert Co. v. FTC*, 562 F.2d 749 (D.C. Cir. 1977) (corrective advertising), *cert. denied*, 435 U.S. 950 (1978); *American Cyanamid Co. v. FTC*, 363 F.2d 757 (6th Cir. 1966) (compulsory licensing of intellectual property), *appeal after remand, Pfizer Co. v. FTC*, 401 F.2d 574 (6th Cir. 1968), *cert. denied*, 394 U.S. 920 (1969); *Chicago Bridge & Iron Co. N.V.*, 2004 FTC LEXIS 250 (Dec. 21, 2004) (appointment of monitor trustee); *Brake Guard Products, Inc.*, 1998 FTC LEXIS 184 (Jan. 23, 1998) (brand name excision). Such fencing-in relief may include a performance bond requirement that, together with the prospect of monetary penalties for violating an order, is likely to spur a respondent to take appropriate measures to ensure compliance and, failing that, provide some measure of relief for consumers who were harmed by the illegal conduct.

In determining whether a performance bond is warranted as fencing-in, we apply the same standard enunciated in *Ruberoid*. We consider the likelihood of a respondent’s future violations, the deliberateness and egregiousness of any past violations, and the

---

in an administrative proceeding. Even assuming, *arguendo*, that the *Heater* court correctly treated an administrative award of restitution as a private remedy, a performance bond operates *prospectively* by ensuring that a fund will be available for consumers should respondent Khubani violate the order in the future, and increasing his incentives to comply. *See FTC v. U.S. Sales Corp.*, 785 F. Supp. 737, 753 (N.D. Ill. 1992), *modified by*, 1992 U.S. Dist. LEXIS 6152 (N.D. Ill. May 6, 1992), *aff’d sub nom. FTC v. Vlahos*, 1995 U.S. App. LEXIS 6092 (7th Cir. Mar. 6, 1995).

Commission Opinion

transferability of the unlawful practices to other products or situations. As discussed above, after consideration of those factors, we believe that broad injunctive relief is warranted here.

The Commission, of course, also considers other factors to decide whether a performance bond is reasonably necessary to supplement other forms of fencing-in. In this instance, we decline to order Mr. Khubani to obtain a performance bond because complaint counsel has presented insufficient evidence as to the amount of the performance bond that would likely be necessary to prevent future law violations. The Commission must determine whether a performance bond is reasonably necessary to secure Mr. Khubani's compliance with the order yet there is no evidence in the record as to his financial resources. Such information would assist the Commission in determining whether a bond requirement is appropriate – and, if so, at what amount – to ensure his compliance and in assessing the financial burden that a bond might impose on him. The amount may have to be more than the \$1 million requested or less than that amount, but the Commission does not have enough information to weigh the reasonableness of the request. Although Mr. Khubani's compliance with the order will not be secured by the performance bond, we believe that the order's requirement that respondents substantiate objective claims for all of their products – while not a substitute for the bond – will help protect consumers in the future.

## **V. Conclusion**

Contrary to respondents' claim, this case does not involve a novel theory of liability. It involves false and unsubstantiated claims that are communicated with such utter clarity that, even without any consideration of extrinsic evidence, we are able to conclude with confidence that the claims were made. Undoubtedly, as a result of respondents' calculated efforts to capitalize on their competitors' ongoing infomercial promotions, respondents' claims for the Ab Force resonated more strongly with those who had viewed those infomercials or were familiar with the competing ab belts. But respondents' ads are not subtle:

## Commission Opinion

even putting aside the claims used in the so-called “test” phase of their Ab Force promotion – which generated sales, like the rollout ads – the images and text in the other ads clearly conveyed each of the claims alleged in the Commission’s complaint. The copy test amply confirms this conclusion. We emphasize, moreover, that this is not a case in which the product was merely “oversold.” Respondents’ advertising left no doubt that the Ab Force was an amazing tool that would work wonders on the body, but they had no evidence that the product did any such thing. The product is useless for the health, weight loss, and fitness purposes for which it was advertised, as respondents were well aware. The idea that consumers were purchasing the Ab Force simply to share in the excitement of buying a popular product is not credible.

For all the foregoing reasons, we affirm the ALJ’s finding as to liability and conclude that a broad cease and desist order applicable to all products is appropriate here. As discussed above, however, we decline to require respondent Khubani to obtain a performance bond.



Final Order

## **FINAL ORDER**

This matter having been heard by the Commission upon the appeal of Respondents and the cross-appeal of Complaint Counsel, and upon briefs and oral argument in support thereof and opposition thereto, and the Commission, for the reasons stated in the accompanying Opinion, having determined to sustain the Initial Decision with certain modifications:

**IT IS ORDERED THAT** the Initial Decision of the administrative law judge be, and it hereby is, adopted as the Findings of Fact and Conclusions of Law of the Commission, to the extent it is not inconsistent with the findings of fact and conclusions of law contained in the accompanying Opinion.

Other findings of fact and conclusions of law of the Commission are contained in the accompanying Opinion.

**IT IS FURTHER ORDERED THAT** the following Order to cease and desist be, and it hereby is, entered:

## **ORDER**

### **DEFINITIONS**

For purposes of this order, the following definitions shall apply.

1. "Commerce" shall mean as defined in Section 4 of the Federal Trade Commission Act, 15 U.S.C. § 44.
2. "Competent and reliable scientific evidence" shall mean tests, analyses, research, studies, or other evidence based on the expertise of professionals in the relevant area, that has been conducted and evaluated in an objective manner by persons qualified to do so, using procedures generally accepted in the profession to yield accurate and reliable results.

## Final Order

3. “EMS device” shall mean any appliance or machine, or any accessories thereof, used to stimulate the muscles of the human body with electricity.
4. “Food,” “drug,” “device,” and “cosmetic” shall mean as “food,” “drug,” “device,” and “cosmetic” are defined in Section 15 of the Federal Trade Commission Act, 15 U.S.C. § 55.
5. Unless otherwise specified, “respondents” shall mean Telebrands (a corporation), TV Savings (a limited liability company), their successors and assigns and their officers; Ajit Khubani, individually and as president of Telebrands and sole member of TV Savings; and each of the above’s agents, representatives, and employees.

**I.**

**IT IS ORDERED** that respondents, directly or through any corporation, subsidiary, division, or other entity, in connection with the manufacturing, labeling, advertising, promotion, offering for sale, sale, or distribution of the Ab Force EMS device or any substantially similar device in or affecting commerce, shall not represent, in any manner, including through the use of pictures, demonstrations, testimonials or endorsements, expressly or by implication, that:

- A. any such device causes or promotes loss of weight, inches, or fat;
- B. any such device causes or promotes well-defined abdominal muscles, including through the use of terms such as “rock hard abs,” “washboard abs,” “chiseled abs,” “cut abs,” “well-developed abs,” and/or any other terms with substantially similar meaning;

Final Order

- C. use of any such device for any period of time is an effective alternative to regular exercise, including but not limited to sit-ups, crunches, or any substantially similar exercises; or
- D. any such device makes a material contribution to any system, program, or plan that produces the results referenced in Subparts A-C of this Part.

**II.**

**IT IS FURTHER ORDERED** that respondents, directly or through any corporation, subsidiary, division, or other entity, in connection with the manufacturing, labeling, advertising, promotion, offering for sale, sale, or distribution of any EMS device, shall not make any misrepresentation, in any manner, including through the use of pictures, demonstrations, testimonials or endorsements, expressly or by implication, that:

- A. any such device causes or promotes loss of weight, inches, or fat;
- B. any such device causes or promotes well-defined abdominal muscles, including through the use of terms such as “rock hard abs,” “washboard abs,” “chiseled abs,” “cut abs,” “well-developed abs,” and/or any other terms with substantially similar meaning;
- C. use of any such device for any period of time is an effective alternative to regular exercise, including but not limited to sit-ups, crunches, or any substantially similar exercises; or
- D. any such device makes a material contribution to any system, program, or plan that produces the results referenced in Subparts A-C of this Part.

Final Order

**III.**

**IT IS FURTHER ORDERED** that respondents, directly or through any corporation, subsidiary, division, or other entity, in connection with the manufacturing, labeling, advertising, promotion, offering for sale, sale, or distribution of Ab Force, any other EMS device, or any food, drug, dietary supplement, device, or any other product, service, or program, shall not make any representation, in any manner, expressly or by implication, about weight, inch, or fat loss, muscle definition, or the health benefits, safety, performance, or efficacy of any product, service, or program, unless, at the time the representation is made, respondents possess and rely upon competent and reliable evidence, which when appropriate must be competent and reliable scientific evidence, that substantiates the representation.

**IV.**

Nothing in this Order shall prohibit respondents from making any representation for any device that is specifically permitted in labeling for that device under any premarket approval application or premarket notification approved or cleared by the Food and Drug Administration.

**V.**

**IT IS FURTHER ORDERED** that respondents Telebrands and TV Savings, and their successors and assigns, and respondent Khubani shall, for five (5) years after the last date of dissemination of any representation covered by this order, maintain and upon request make available to the Federal Trade Commission for inspection and copying:

- A. all advertisements and promotional materials containing the representation;
- B. all materials that were relied upon in disseminating the representation; and

Final Order

- C. all tests, reports, studies, surveys, demonstrations, or other evidence in their possession or control that contradict, qualify, or call into question the representation, or the basis relied upon for the representation, including complaints and other communications with consumers or with governmental or consumer protection organizations.

**VI.**

**IT IS FURTHER ORDERED** that respondents Telebrands and TV Savings, and their successors and assigns, and respondent Khubani shall deliver a copy of this order to all current and future principals, officers, directors, and managers, and to all current and future employees, agents, and representatives having responsibilities with respect to the subject matter of this order, and shall secure from each such person a signed and dated statement acknowledging receipt of the order. Respondents shall deliver this order to current personnel within thirty (30) days after the date of service of this order, and to future personnel within thirty (30) days after the person assumes such position or responsibilities.

**VII.**

**IT IS FURTHER ORDERED** that respondents Telebrands and TV Savings and their successors and assigns shall notify the Commission at least thirty (30) days prior to any change in the corporation or limited liability company that may affect compliance obligations arising under this order, including but not limited to a dissolution, assignment, sale, merger, or other action that would result in the emergence of a successor corporation; the creation or dissolution of a subsidiary, parent, or affiliate that engages in any acts or practices subject to this order; the proposed filing of a bankruptcy petition; or a change in the corporate name or address. *Provided, however,* that, with respect to any proposed change in the corporation about which respondents learn less than thirty (30) days prior to the date such action is to take place, respondents shall notify the Commission as soon as is practicable after obtaining such knowledge. All notices required by this Part

Final Order

shall be sent by certified mail to the Associate Director, Division of Enforcement, Bureau of Consumer Protection, Federal Trade Commission, Washington, D.C. 20580.

### VIII.

**IT IS FURTHER ORDERED** that respondent Khubani, for a period of ten (10) years after the date of issuance of this order, shall notify the Commission of the discontinuance of his current business or employment, or of his affiliation with any new business or employment. The notice shall include respondent's new business address and phone number and a description of the nature of the business or employment and his duties and responsibilities. All notices required by this Part shall be sent by certified mail to the Associate Director, Division of Enforcement, Bureau of Consumer Protection, Federal Trade Commission, Washington, D.C. 20580.

### IX.

**IT IS FURTHER ORDERED** that respondents Telebrands and TV Savings, and their successors and assigns, and respondent Khubani shall, within sixty (60) days after the date of service of this order, and at such other times as the Federal Trade Commission may require, file with the Commission a report, in writing, setting forth in detail the manner and form in which they have complied with this order.

### X.

This order will terminate twenty (20) years from the date of its issuance, or twenty (20) years from the most recent date that the United States or the Federal Trade Commission files a complaint (with or without an accompanying consent decree) in federal court alleging any violation of the order, whichever comes later; *provided however*, that the filing of such a complaint will not affect the duration of:

Final Order

- A. Any Part in this order that terminates in less than twenty (20) years;
- B. This Order's application to any respondent that is not named as a defendant in such complaint; and
- C. This Order if such complaint is filed after the order has terminated under this Part.

*Provided, further,* that if such complaint is dismissed or a federal court rules that the respondent did not violate any provision of the order, and the dismissal or ruling is either not appealed or upheld on appeal, then the order will terminate according to this Part as though the complaint had never been filed, except that the order will not terminate between the date such complaint is filed and the later of the deadline for appealing such dismissal or ruling and the date such dismissal or ruling is upheld on appeal.

Complaint

**COMPLAINT**

The Federal Trade Commission (“FTC” or “Commission”), having reason to believe that Telebrands Corp. (“Telebrands”), TV Savings, LLC (“TV Savings”), and Ajit Khubani (“Khubani”), individually and as president of Telebrands and sole member of TV Savings (collectively “respondents”), have violated the provisions of the Federal Trade Commission Act, and it appearing to the Commission that this proceeding is in the public interest, alleges:

1. Respondent Telebrands is a New Jersey corporation with its principal office or place of business at 79 Two Bridges Road, Fairfield, NJ 07004.
2. Respondent TV Savings is a Connecticut limited liability company with its principal office or place of business at 79 Two Bridges Road, Fairfield, NJ 07004.
3. Respondent Khubani is president of Telebrands and sole member of TV Savings. Individually or in concert with others, he formulates, directs, or controls the policies, acts, or practices of these two business entities, including the acts and practices alleged in this complaint. His principal office or place of business is the same as those of Telebrands and TV Savings.
4. The foregoing respondents have operated as a common enterprise to label, advertise, offer for sale, sell, and distribute the Ab Force, an electronic muscle stimulation (“EMS”) device, which is a “device” within the meaning of Sections 12 and 15 of the FTC Act.
5. The acts and practices of respondents alleged in this complaint have been in or affecting commerce, as “commerce” is defined in Section 4 of the Federal Trade Commission Act.



Complaint

**The Ab Force EMS Device**

6. The Ab Force EMS device is comprised of: (1) a black elasticized belt; (2) a thin black pad measuring approximately 8 inches by 4 inches; and (3) a small control unit, powered by a coin-sized battery, which attaches to the pad and, in some models, enables the user to control the intensity of electronic stimulation. These three components assemble to form a belt with the pad and unit in the middle. According to respondents' instructions, the user should apply a water-based gel to the pad and place this pad against the abdomen, bicep, or thigh to send the electrical current generated by the control unit to the body.

**Advertising and Promotion of the Ab Force EMS Device**

7. From December 2001 to May 2002, respondents disseminated, or caused to be disseminated, advertisements and promotional materials for the Ab Force, including but not necessarily limited to 60 and 120 second television commercials, Internet advertisements, radio advertisements, and print advertisements. Respondents offered the Ab Force for the price of \$10. Gross sales of the Ab Force, including accessories like batteries and gels, exceeded \$19 million.
8. Respondents spent more than four million dollars to televise commercials for the Ab Force. These commercials appeared more than 10,000 times on cable, satellite, and broadcast television outlets, and were among the most frequently aired commercials on cable television during the weeks and months in which they appeared, according to an industry monitoring service.
9. Through advertisements for the Ab Force, respondents represented that the Ab Force used the same technology and was just as powerful and effective as other more expensive EMS devices that were advertised on program-length television commercials ("infomercials") during or shortly before the time period in which the Ab Force commercials appeared.

## Complaint

10. The Ab Force advertisements, including but not limited to the attached Exhibits A through H, contained the following statements or depictions, among others:
- a. PAT MURPHY: I'm sure you've seen those fantastic electronic ab belt infomercials on TV. They're amazing. They're the latest fitness craze to sweep the country and everybody wants one.
- ON SCREEN: UP TO \$120 EACH!**
- PAT MURPHY: The problem is, they're expensive, selling for up to \$120 each.
- ON SCREEN:**  
\*\*\*\*
- AB FORCE**
- PAT MURPHY: Well, that's why we developed the Ab Force that you can buy right now for just \$10.
- ON SCREEN: JUST \$10!**
- PAT MURPHY: That's right, just \$10.
- ...
- PAT MURPHY: . . . The Ab Force is just as powerful and effective as those expensive ab belts sold by others - -
- ON SCREEN: ELECTRONIC STIMULATION**
- PAT MURPHY: - - designed to send just the right amount of electronic stimulation to your abdominal area!
- Exhibit A (videotape of television commercial); Exhibit B (Certified transcript of 60-second television commercial).

These statements are accompanied by the following images, among others:

- (1) over a dozen depictions of well-muscled, bare-chested men and lean, shapely women wearing Ab Force belts and experiencing abdominal muscle contractions; and (2) two close-up images of a bikini-clad woman showing off her trim waist and well-defined abdominal muscles.

Complaint

- b. PAT MURPHY: I'm sure you've seen those fantastic electronic ab belt infomercials on TV. They're amazing. They're the latest fitness craze to sweep the country and everybody wants one.

**ON SCREEN: UP TO \$120 EACH!**

PAT MURPHY: But the problem is they're expensive, selling for up to \$120 each.

**ON SCREEN:**

\*\*\*\*

**AB FORCE**

PAT MURPHY: Well, that's why we developed the Ab Force that you can buy right now for just \$10.

**ON SCREEN: JUST \$10!**

PAT MURPHY: That's right, just \$10.

**ON SCREEN:**

\*\*\*\*

**AB FORCE**

PAT MURPHY: But don't be fooled by the price. The Ab Force is just as powerful and effective as those ab belts sold by other companies on infomercials.

**ON SCREEN: HIGH QUALITY**

PAT MURPHY: The Ab Force is truly a high quality product.

**ON SCREEN: SOPHISTICATED COMPUTER COMPONENTS**

**ELECTRONIC STIMULATION**

PAT MURPHY: Using sophisticated electronic technology, the Ab Force is designed to send just the right amount of electronic stimulation to your abdominal area.

. . .

PAT MURPHY: . . . It is so comfortable that you can even wear it under your clothes. In fact, I'm wearing one right now and it's working while I'm working.

**ON SCREEN:**

\*\*\*\*

**AB FORCE**

**High Quality**

**Powerful**

## Complaint

**Comfortable**

PAT MURPHY: The Ab Force is high quality, powerful, comfortable - -

**ON SCREEN:**

\*\*\*\*

**AB FORCE****JUST \$10**

PAT MURPHY: - - and best of all it's just \$10

**ON SCREEN: 30 DAY****SATISFACTION GUARANTEE!**

PAT MURPHY: . . demand for the ab force is overwhelming and - -

**ON SCREEN: NOT AVAILABLE IN STORES**

PAT MURPHY: - - it's not available in stores anywhere. So, don't miss out on this incredible opportunity. Call to reserve your electronic Ab Force now.

—Exhibit C (videotape of television commercial); Exhibit D (Certified transcript of 120-second test television commercial).

These statements are accompanied by the following images, among others:

(1) over a dozen depictions of well-muscled, bare-chested men and lean, shapely women wearing Ab Force belts and experiencing abdominal muscle contractions; (2) two close-up images of a bikini-clad woman showing off her trim waist and well-defined abdominal muscles; and (3) one close-up image of a well-muscled, bare-chested man performing a crunch on an exercise bench.

c. **ON SCREEN: Consult Your Physician Before Using the Ab Force**

PAT MURPHY-STARK: Hi, Pat Murphy-Stark here.

**ON SCREEN:**

\*\*\*\*

**AB FORCE**

**Do not use if you have a pacemaker, a heart or medical condition, or are pregnant.**

Complaint

PAT MURPHY-STARK: I'm sure you've seen those fantastic electronic ab belt infomercials on TV. They're amazing. They're the latest craze to sweep the country and everybody wants one.

**ON SCREEN: Up to \$120 Each**

PAT MURPHY-STARK: But the thing is, they're expensive, selling for up to \$120 each.

**ON SCREEN:**

\*\*\*\*

**AB FORCE**

PAT MURPHY-STARK: Well, that's why we developed the Ab Force that you can buy right now for just \$20.

. . .

PAT MURPHY-STARK: The Ab Force uses the same powerful technology as those expensive ab belts - -

**ON SCREEN: RELAXING MASSAGE**

**10 INTENSITY LEVELS**

PAT MURPHY-STARK: - - Capable of directing 10 different intensity levels at your abdominal area.

**ON SCREEN: HERE'S AN EVEN BETTER DEAL!**

PAT MURPHY-STARK: And here's an even better deal

**ON SCREEN: 1-800-322-4343**

PAT MURPHY-STARK: Call right now and we'll double your order.

**ON SCREEN: 2 for \$20**

**1-800-322-4343**

PAT MURPHY-STARK: That's two electronic Ab Force belts for just \$20. Don't miss out on this incredible opportunity. Call Now.

—Exhibit E (videotape of television commercial); Exhibit F (Certified transcript of 60-second television commercial).

These statements are accompanied by the following images, among others:(1) over a dozen depictions of well-muscled, bare-chested men and lean, shapely women wearing Ab Force belts and experiencing abdominal muscle contractions; and (2) two close-up images of a

## Complaint

bikini-clad woman showing off her trim waist and well-defined abdominal muscles.

- d. “I’m sure you’ve seen those fantastic electronic ab belt infomercials on TV. They’re amazing! They’re the latest craze to sweep the country and everybody wants one. The thing is they’re expensive selling for up to \$120 each. That’s why we developed the Abforce that you can buy right now for just \$10.

...

**Don’t Be Fooled By the Price!**

The Abforce uses the same powerful technology as those Ab Belts sold by other companies on infomercials.

...

Using sophisticated computer components, the Abforce is capable of directing 10 completely different intensity levels at your abdominal area. .

...

So why would you want to buy a more expensive ab belt from the competition when the Abforce is as low as just \$10?”  
—Exhibit G (print advertisement).

Adjacent to these statements is an image of a well-muscled man wearing an Ab Force belt. Superimposed on this image is a red-and-white, square-shaped “AS SEEN ON TV” logo, and the statement, “Ab Force uses the same powerful technology as those expensive Ab Belts on infomercials.”

- e. “Have you seen those fantastic Electronic Ab Belt infomercials on TV? They’re amazing...promising to get our abs into great shape fast—without exercise! They’re the latest fitness craze to sweep the country. But, they’re expensive, selling for up to 120 dollars each! But what if you could get a high quality electronic ab belt for just 10 dollars? That’s right, just 10 dollars! . . . . The Ab Force is just as powerful and effective as the expensive ab belts on TV—designed to send just the right amount of

Complaint

electronic stimulation to your abdominal area. . . . Don't miss out. Get the amazing electronic Ab [F]orce belt—the latest fitness craze for just \$10.”  
—Exhibit H (radio advertisement).

**Advertising and Promotion of Other EMS Devices on Infomercials**

11. From April 2001 through May 2002, during or shortly before the time period in which the Ab Force commercials appeared, several other EMS devices were offered for sale, sold, and distributed throughout the United States. Three of these EMS devices, the “AbTronic,” “AB Energizer,” and “Fast Abs,” were substantially similar in appearance to the Ab Force, were comprised of components substantially similar to those identified in Paragraph 6, and were widely advertised through television infomercials. All three EMS devices were more expensive than the Ab Force.
12. The AbTronic EMS device was offered for the price of \$120. According to an industry monitoring service, AbTronic infomercials appeared more than 2,000 times on cable television stations from April 2001 through March 2002, at an estimated cost of more than \$18 million. AbTronic infomercials were among the most frequently-aired infomercials on cable television during the weeks and months in which they appeared. Gross sales of the AbTronic EMS device, including accessories like batteries and gels, exceeded \$106 million dollars.
13. The AB Energizer EMS device was offered for the price of \$59.95. According to an industry monitoring service, AB Energizer infomercials appeared more than 1,600 times on cable television stations from October 2001 through February 2002, at an estimated cost of more than \$11 million. AB Energizer infomercials were among the most frequently-aired infomercials on cable television during the weeks and months in which they appeared. Gross sales of

## Complaint

the AB Energizer EMS device, including accessories like batteries and gels, exceeded two million units, that is, approximately \$120 million.

14. The Fast Abs EMS device was offered for the price of \$39.95. According to an industry monitoring service, Fast Abs infomercials appeared more than 1,200 times on cable television stations between November 2001 and February 2002, at an estimated cost of more than \$12 million. Fast Abs infomercials were among the most frequently-aired infomercials on cable television during the weeks and months in which they appeared. Gross sales of the Fast Abs EMS device, including accessories like batteries and gels, exceeded 660,000 units, that is, more than \$26 million dollars.
15. Infomercials for the AbTronic, AB Energizer, and Fast Abs devices contained the following depictions, among others: (1) well-muscled, bare-chested men and lean, shapely women wearing EMS devices around the waist and experiencing abdominal muscle contractions; (2) men and women performing conventional abdominal exercises such as sit-ups or crunches; and (3) close-up images of men and women in revealing clothes showing off their trim waists and well-defined abdominal muscles.
16. Infomercials for the AbTronic, AB Energizer, and Fast Abs devices contained the following representations, among others, that the advertised device causes the loss of weight, inches, or fat:
  - a. **ON SCREEN: K.T. Roberge**  
**Homemaker**  
**Results based on use and muscle response**  
TESTIMONIALIST K.T. ROBERGE: When I first started using the AbTronic System, I was skeptical at first, thinking it's just too easy, strapping it on, nothing to plug



Complaint

in, and it just contracts your muscles. But for three weeks, I have used it now and I've lost two inches in my waist.

—*Federal Trade Commission v. Hudson Berkley, Corporation, et al.*, CV-S-02-0649-PMP, (May 7, 2002), Complaint Exhibit 2 at 19.

**b. ON SCREEN: Kathy Horn  
Tanning Salon Owner**

TESTIMONIALIST KATHY HORN: After using the AbTronic System, I've lost three inches on my waist in the matter of two weeks and my abdominals look so much better.

—*Federal Trade Commission v. Hudson Berkley, Corporation, et al.*, CV-S-02-0649-PMP, (May 7, 2002), Complaint Exhibit 2 at 32-33.

**c. ON SCREEN: Before and After photographs**

UNIDENTIFIED MALE: The Ab Energizer System I've used for five weeks and I've gotten incredible results.

**ON SCREEN: Lost 40 lbs.  
Size 37 to 34**

**Results not typical. Individuals results may vary.**

UNIDENTIFIED MALE: I've lost 40 pounds. I've gone from a waist 37 to a waist 34. The Ab Energizer and the Ab Energizer System has changed my life and it's really given my life back to me.

—*Federal Trade Commission v. Electronic Products Distribution, LLC, et al.*, 02CV0888 H(AJB), (May 7, 2002), Complaint Exhibit 2 at 30-31

**d. SPOKESWOMAN KITA PELLY: The AB Energizer System is absolutely incredible for people who want tighter abs and want to lose inches around the midsection.**

—*Federal Trade Commission v. Electronic Products Distribution, LLC, et al.*, 02CV0888 H(AJB), (May 7, 2002), Complaint Exhibit 2 at 29-30.

## Complaint

- e. MALE ANNOUNCER: People everywhere are sitting back and relaxing while they firm up, slim down, and shed inches quickly.

—*Federal Trade Commission v. United Fitness of America, LLC, et al.*, CV-S-02-0648-KJD-LRL, (May 7, 2002), Complaint Exhibit B at 4, 23, 54; Complaint Exhibit D at 4, 23-24, 45, 57.

- f. MALE ANNOUNCER: You'll drop four inches in the first 30 days. We guarantee it.

—*Federal Trade Commission v. United Fitness of America, LLC, et al.*, CV-S-02-0648-KJD-LRL, (May 7, 2002), Complaint Exhibit B at 31, 59; Complaint Exhibit D at 32, 63.

17. Infomercials for the AbTronic, AB Energizer, and Fast Abs devices contained the following representations, among others, that the advertised device causes well-defined abdominal muscles:

- a. MALE ANNOUNCER: AbTronic is the electronic dream machine that will show you immediate improvement without strenuous time-consuming workouts. You'll develop that six-pack you've always wanted in the easiest way imaginable.

—*Federal Trade Commission v. Hudson Berkley, Corporation, et al.*, CV-S-02-0649-PMP, (May 7, 2002), Complaint Exhibit 2 at 13, 27, 38.

- b. MALE ANNOUNCER: Now, with one touch of a button, you can get that six-pack you always wanted, guaranteed.

—*Federal Trade Commission v. Hudson Berkley, Corporation, et al.*, CV-S-02-0649-PMP, (May 7, 2002), Complaint Exhibit 4 at 3.

- c. MAIL ANNOUNCER: Now, with a touch of a button, you can go from flab to rock-hard abs.

Complaint

—*Federal Trade Commission v. Electronic Products Distribution, LLC, et al.*, 02CV0888 H(AJB), (May 7, 2002), Complaint Exhibit 2 at 22, 39, 50, 62.

- d. MALE ANNOUNCER: Do you want rock-hard abs without sweating in a gym for hours? Do you want to have toned muscles all over your body without lifting heavy weights? Well, now, you can. Introducing Fast Abs— the no-sweat, full body workout.

—*Federal Trade Commission v. United Fitness of America, LLC, et al.*, CV-S-02-0648-KJD-LRL, (May 7, 2001), Complaint Exhibit B at 3-4, 22.

- e. SPOKESWOMAN KATHY DERRY: “The simple, fast, easy, effective tool to help tool and reshape your body and help(s) get those washboard lean sexy abs is finally here. With Fast Abs, we’ll guarantee fast results with no sweat.”

—*Federal Trade Commission v. United Fitness of America, LLC, et al.*, CV-S-02-0648-KJD-LRL, (May 7, 2002), Complaint Exhibit B at 52; Complaint Exhibit D at 54.

18. Infomercials for the AbTronic, AB Energizer, and Fast Abs devices contained the following representations, among others, that use of the advertised device is equivalent to or more effective than regular exercise:

- a. MALE ANNOUNCER: You’ll see how the AbTronic System gives you the results of 600 sit-ups in just 10 minutes without any effort.

—*Federal Trade Commission v. Hudson Berkley, Corporation, et al.*, CV-S-02-0649-PMP, (May 7, 2002), Complaint Exhibit 2 at 3-4.

- b. **ON SCREEN: Idrise Ward-El  
Professional Bodybuilder**

IDRISE WARD-EL: When I first used the AbTronic System, it looked small and I didn’t have any idea what it

## Complaint

would feel like. When I did use it, I had a very strong contraction, a lot stronger than doing sit-ups. Even after 100 sit-ups, you don't get the kind of contraction you get here, because normally, when doing sit-ups you get tired first. Then it starts to work. Doing the first AbTronic systems, the first contraction feels like you've done already 100, 150 sit-ups.

—*Federal Trade Commission v. Hudson Berkley, Corporation, et al.*, CV-S-02-0649-PMP, (May 7, 2002), Complaint Exhibit 2 at 20.

- c. MALE ANNOUNCER: [W]atch as your ab muscles contract as if you're doing a sit-up. . . . Ten minutes on the AbTronic is the equivalent of 600 sit-ups. That's why we guarantee you'll lose two inches off your midsection in less than a month or your money back.

—*Federal Trade Commission v. Hudson Berkley, Corporation, et al.*, CV-S-02-0649-PMP, (May 7, 2002), Complaint Exhibit 2 at 14, 27, 39; Complaint Exhibit 4 at 3.

- d. MALE ANNOUNCER: The secret is Ab Energizer's electronic impulses that stimulate your abs so they contract and relax as if you're doing a sit-up.

**ON SCREEN: Up to 700 Muscle Contractions  
10 Minutes!**

MALE ANNOUNCER: Now you can get up to 700 muscle contractions in just 10 minutes and get the tone and definition you've always wanted.

—*Federal Trade Commission v. Electronic Products Distribution, LLC, et al.*, 02CV0888 H(AJB), (May 7, 2002), Complaint Exhibit 2 at 62,63.

- e. DR. DONALD FURNIVAL [introduced as a chiropractor specializing in "natural healthcare"]: There are several studies that have been done that show that electrical muscle stimulation is more effective and more efficient than regular working out or going to the gym.

Complaint

—*Federal Trade Commission v. United Fitness of America, LLC, et al., CV-S-02-0648-KJD-LRL*, (May 7, 2002), Complaint Exhibit B at 15.

- f. MALE ANNOUNCER: The secret is EMS, electronic muscle stimulation. This tiny transformer sends out safe, gentle impulses that trigger your motor nerves and activate deep muscle contractions. Tests have proven that this unique isometric action can be—

**ON SCREEN: 30% More Effective!**

MALE ANNOUNCER: —30 percent more effective than anything you can do on your own with normal exercise.

—*Federal Trade Commission v. United Fitness of America, LLC, et al., CV-S-02-0648-KJD-LRL*, (May 7, 2002), Complaint Exhibit B at 24.

- g. SPOKESWOMAN KATHY DERRY: In fact, just 10 minutes of Fast Abs is like doing 600 sit-ups. Imagine that. 600 sit-ups.

**ON SCREEN: 10 minutes = 600 sit ups.**

—*Federal Trade Commission v. United Fitness of America, LLC, et al., CV-S-02-0648-KJD-LRL*, (May 7, 2002), Complaint Exhibit B at 11; see also Fast Abs Ex. B at 5, 23, 35, 43, 50, 54-55

**Violations of Sections 5 and 12 of the FTC Act**

19. Through the means described in Paragraphs 9 and 10, respondents represented, expressly or by implication, including, but not limited to, references to products and infomercials with representations such as those described in Paragraphs 11 through 18, that:
- a. Ab Force causes loss of weight, inches, or fat;
  - b. Ab Force causes well-defined abdominal muscles; and

## Complaint

c. Use of Ab Force is an effective alternative to regular exercise.

20. In truth and in fact:

a. Ab Force does not cause loss of weight, inches, or fat;

b. Ab Force does not cause well-defined abdominal muscles; and

c. Use of Ab Force is not an effective alternative to regular exercise.

Therefore the representations set forth in Paragraph 19 were, and are, false and misleading.

21. Through the means described in Paragraphs 9 and 10, respondents represented, expressly or by implication, including, but not limited to, references to products and infomercials with representations such as those described in Paragraphs 11 through 18, that they possessed and relied upon a reasonable basis that substantiated the representations set forth in Paragraph 19, at the time the representations were made.

22. In truth and fact, respondents did not possess and rely upon a reasonable basis that substantiated the representations set forth in Paragraph 10, at the time the representations were made. Therefore, the representation set forth in Paragraph 21 was deceptive.

23. The acts and practices of respondents as alleged in this complaint constitute unfair or deceptive acts or practices and the making of false advertisements in or affecting commerce in violation of Sections 5(a) and 12 of the Federal Trade Commission Act.

Complaint

**NOTICE**

Proceedings on the charges asserted against you in this complaint will be held before an Administrative Law Judge (ALJ) of the Federal Trade Commission, under Part 3 of the Commission's Rules of Practice, 16 C.F.R. Part 3. A copy of Part 3 of the Rules is enclosed with this complaint.

You may file an answer to this complaint. Any such answer must be filed within 20 days after service of the complaint on you. If you contest the complaint's allegations of fact, your answer must concisely state the facts constituting each ground of defense, and must specifically admit, deny, explain, or disclaim knowledge of each fact alleged in the complaint. You will be deemed to have admitted any allegations of the complaint that you do not so answer.

If you elect not to contest the allegations of fact set forth in the complaint, your answer shall state that you admit all of the material allegations to be true. Such an answer will 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 ALJ will file an initial decision containing appropriate findings and conclusions and an appropriate order disposing of the proceeding. Such an answer may, however, reserve the right to submit proposed findings and conclusions and the right to appeal the initial decision to the Commission under Section 3.52 of the Commission's Rules of Practice.

If you do not answer within the specified time, you waive your right to appear and contest the allegations of the complaint. The ALJ is then authorized, without further notice to you, to find that the facts are as alleged in the complaint and to enter an initial decision and a cease and desist order.

The ALJ will schedule an initial prehearing scheduling conference to be held not later than 14 days after the last answer is filed by any party named as a respondent in the complaint. Unless

## Complaint

otherwise directed by the ALJ, the scheduling conference and further proceedings will take place at the Federal Trade Commission, 600 Pennsylvania Avenue, N.W., Washington, D.C. 20580. Rule 3.21(a) requires a meeting of the parties' counsel as early as practicable before the prehearing scheduling conference, and Rule 3.31(b) obligates counsel for each party, within 5 days of receiving a respondent's answer, to make certain initial disclosures without awaiting a formal discovery request.

A hearing on the complaint will begin on February 2, 2004, at 10:00 A.M. in Room 532, or such other date as determined by the ALJ. At the hearing, you will have the right to contest the allegations of the complaint and to show cause why a cease and desist order should not be entered against you.

The following is the form of order which the Commission has reason to believe should issue if the facts are found to be as alleged in the complaint. If, however, the Commission should conclude from the record facts developed in any adjudicative proceedings in this matter that the proposed order provisions as to Telebrands Corp., TV Savings, LLC, and Ajit Khubani, individually and as president of Telebrands and sole member of TV Savings, might be inadequate to fully protect the consuming public, the Commission may order such other relief as it finds necessary or appropriate, including corrective advertising or other affirmative disclosure.

Moreover, the Commission has reason to believe that, if the facts are found as alleged in the complaint, it may be necessary and appropriate for the Commission to seek relief to redress injury to consumers, or other persons, partnerships or corporations, in the form of restitution and refunds for past, present, and future consumers and such other types of relief as are set forth in Section 19(b) of the Federal Trade Commission Act. The Commission will determine whether to apply to a court for such relief on the basis of the adjudicative proceedings in this matter and such other factors as are relevant to consider the necessity and appropriateness of such action.



Complaint

**ORDER**

DEFINITIONS

For purposes of this order, the following definitions shall apply:

1. “Commerce” shall mean as defined in Section 4 of the Federal Trade Commission Act, 15 U.S.C. § 44.
2. “Competent and reliable scientific evidence” shall mean tests, analyses, research, studies, or other evidence based on the expertise of professionals in the relevant area, that has been conducted and evaluated in an objective manner by persons qualified to do so, using procedures generally accepted in the profession to yield accurate and reliable results.
3. “EMS device” shall mean any appliance or machine, or any accessories thereof, used to stimulate the muscles of the human body with electricity.
4. “Food,” “drug,” “device,” and “cosmetic” shall mean as “food,” “drug,” “device,” and “cosmetic” are defined in Section 15 of the Federal Trade Commission Act, 15 U.S.C. § 55.
5. Unless otherwise specified, “respondents” shall mean Telebrands (a corporation), TV Savings (a limited liability company), their successors and assigns and their officers; Ajit Khubani, individually and as president of Telebrands and sole member of TV Savings; and each of the above’s agents, representatives, and employees.

**I.**

**IT IS ORDERED** that respondents, directly or through any corporation, subsidiary, division, or other entity, in connection with the manufacturing, labeling, advertising, promotion, offering

## Complaint

for sale, sale, or distribution of the Ab Force EMS device or any substantially similar device in or affecting commerce, shall not represent, in any manner, including through the use of pictures, demonstrations, testimonials or endorsements, expressly or by implication, that:

- A. any such device causes or promotes loss of weight, inches, or fat;
- B. any such device causes or promotes well-defined abdominal muscles, including through the use of terms such as “rock hard abs,” “washboard abs,” “chiseled abs,” “cut abs,” “well-developed abs,” and/or any other terms with substantially similar meaning;
- C. use of any such device for any period of time is an effective alternative to regular exercise, including but not limited to sit-ups, crunches, or any substantially similar exercises;
- D. any such device makes a material contribution to any system, program, or plan that produces the results referenced in Subparts A-C of this Part.

**II.**

**IT IS FURTHER ORDERED** that respondents, directly or through any corporation, subsidiary, division, or other entity, in connection with the manufacturing, labeling, advertising, promotion, offering for sale, sale, or distribution of any EMS device, shall not make any misrepresentation, in any manner, including through the use of pictures, demonstrations, testimonials or endorsements, expressly or by implication, that:

- A. any such device causes or promotes loss of weight, inches, or fat;
- B. any such device causes or promotes well-defined abdominal muscles, including through the use of terms such as “rock

Complaint

hard abs,” “washboard abs,” “chiseled abs,” “cut abs,” “well-developed abs,” and/or any other terms with substantially similar meaning;

- C. use of any such device for any period of time is an effective alternative to regular exercise, including but not limited to sit-ups, crunches, or any substantially similar exercises;
- D. any such device makes a material contribution to any system, program, or plan that produces the results referenced in Subparts A-C of this Part.

**III.**

**IT IS FURTHER ORDERED** that respondents, directly or through any corporation, subsidiary, division, or other entity, in connection with the manufacturing, labeling, advertising, promotion, offering for sale, sale, or distribution of Ab Force, any other EMS device, or any food, drug, dietary supplement, device, or any other product, service, or program, shall not make any representation, in any manner, expressly or by implication, about weight, inch, or fat loss, muscle definition, or the health benefits, safety, or efficacy of any such product, service, or program, unless, at the time the representation is made, respondents possess and rely upon competent and reliable scientific evidence that substantiates the representation.

**IV.**

Nothing in this Order shall prohibit respondents from making any representation for any device that is specifically permitted in labeling for that device under any premarket approval application or premarket notification approved or cleared by the Food and Drug Administration.

Complaint

**V.**

**IT IS FURTHER ORDERED** that respondent Khubani, directly or through any corporation, subsidiary, division, or other entity, shall not engage in or assist others in engaging in any manufacturing, labeling, advertising, promotion, offering for sale, sale or distribution of any device, as that term is defined in Section 15(d) of the FTC Act, 15 U.S.C. § 52, unless, prior to engaging in that activity, respondent Khubani first obtains a performance bond (“the bond”) in the principal sum of \$1,000,000. The terms and conditions of the bond requirement are as follows:

- A. The bond shall be conditioned upon compliance with Sections 5(a) and 12 of the FTC Act, 15 U.S.C. §§ 45(a) and 52, and Parts I through III of this Order. The bond shall be deemed continuous and remain in full force and effect as long as defendant is engaging in any manufacturing, labeling, advertising, promotion, offering for sale, sale or distribution of any device. Respondent Khubani shall maintain the bond for a period of three years after he provides notice to the Commission that he has ceased engaging in any manufacturing, labeling, advertising, promotion, offering for sale, sale or distribution of any device. The bond shall cite this Order as the subject matter of the bond, and shall provide surety thereunder against financial loss resulting from whole or partial failure of performance due, in whole or in part, to any violation of Sections 5(a) and 12 of the FTC Act, or Parts I through III of this Order.
- B. The bond shall be an insurance agreement providing surety for financial loss issued by a surety company that is admitted to do business in each state in which respondent Khubani, or any entity directly or indirectly under his control, is doing business and that holds a Federal Certificate of Authority As Acceptable Surety On Federal Bond and Reinsuring. The bond shall be in favor of the

Complaint

Federal Trade Commission for the benefit of any consumer injured as a result of any activities that required obtaining the bond.

- C. The bond required pursuant to this Paragraph is in addition to, and not in lieu of, any other bonds required by federal, state or local law.
- D. At least 10 days before commencing any activity that requires obtaining the bond, respondent Khubani shall provide notice to the Commission describing in reasonable detail the activities and include in the notice a copy of the bond obtained.
- E. Respondent Khubani, directly or through any business entity, shall not disclose the existence of the bond to any consumer, or other purchaser or prospective purchaser in connection with advertising, promoting, marketing, offering for sale, or sale of any product, service, or program. *Provided, however,* that this provision does not apply to the handling of consumer complaints and cancellation and refund requests so long as respondent Khubani, directly or through any business entity, also discloses, at the same time, that the bond is “required by Order of the Federal Trade Commission to resolve an action charging that Ajit Khubani engaged in deceptive practices as alleged in *In the Matter of Telebrands Corp., et al.*, Docket No. 9313.” The disclosure shall be stated or set forth in a clear and prominent manner. If in print, the disclosure shall be separated from all other text, in 100 percent black ink against a light background, in print at least as large as the main text of the sales material or document, and enclosed in a box containing only the required disclosure.

**VI.**

**IT IS FURTHER ORDERED** that respondents Telebrands and TV Savings, and their successors and assigns, and respondent

## Complaint

Khubani shall, for five (5) years after the last date of dissemination of any representation covered by this order, maintain and upon request make available to the Federal Trade Commission for inspection and copying:

- A. all advertisements and promotional materials containing the representation;
- B. all materials that were relied upon in disseminating the representation; and
- C. all tests, reports, studies, surveys, demonstrations, or other evidence in their possession or control that contradict, qualify, or call into question the representation, or the basis relied upon for the representation, including complaints and other communications with consumers or with governmental or consumer protection organizations.

**VII.**

**IT IS FURTHER ORDERED** that respondents Telebrands and TV Savings, and their successors and assigns, and respondent Khubani shall deliver a copy of this order to all current and future principals, officers, directors, and managers, and to all current and future employees, agents, and representatives having responsibilities with respect to the subject matter of this order, and shall secure from each such person a signed and dated statement acknowledging receipt of the order. Respondents shall deliver this order to current personnel within thirty (30) days after the date of service of this order, and to future personnel within thirty (30) days after the person assumes such position or responsibilities.

**VIII.**

**IT IS FURTHER ORDERED** that respondents Telebrands and TV Savings and their successors and assigns shall notify the Commission at least thirty (30) days prior to any change in the corporation or limited liability company that may affect

Complaint

compliance obligations arising under this order, including but not limited to a dissolution, assignment, sale, merger, or other action that would result in the emergence of a successor corporation; the creation or dissolution of a subsidiary, parent, or affiliate that engages in any acts or practices subject to this order; the proposed filing of a bankruptcy petition; or a change in the corporate name or address. *Provided, however*, that, with respect to any proposed change in the corporation about which respondents learn less than thirty (30) days prior to the date such action is to take place, respondents shall notify the Commission as soon as is practicable after obtaining such knowledge. All notices required by this Part shall be sent by certified mail to the Associate Director, Division of Enforcement, Bureau of Consumer Protection, Federal Trade Commission, Washington, D.C. 20580.

**IX.**

**IT IS FURTHER ORDERED** that respondent Khubani, for a period of ten (10) years after the date of issuance of this order, shall notify the Commission of the discontinuance of his current business or employment, or of his affiliation with any new business or employment. The notice shall include respondent's new business address and phone number and a description of the nature of the business or employment and his duties and responsibilities. All notices required by this Part shall be sent by certified mail to the Associate Director, Division of Enforcement, Bureau of Consumer Protection, Federal Trade Commission, Washington, D.C. 20580.

**X.**

**IT IS FURTHER ORDERED** that respondents Telebrands and TV Savings, and their successors and assigns, and respondent Khubani shall, within sixty (60) days after the date of service of this order, and at such other times as the Federal Trade Commission may require, file with the Commission a report, in writing, setting forth in detail the manner and form in which they have complied with this order.

## Complaint

**XI.**

This order will terminate twenty (20) years from the date of its issuance, or twenty (20) years from the most recent date that the United States or the Federal Trade Commission files a complaint (with or without an accompanying consent decree) in federal court alleging any violation of the order, whichever comes later; *provided, however*, that the filing of such a complaint will not affect the duration of:

- A. Any Part in this order that terminates in less than twenty (20) years;
- B. This Order's application to any respondent that is not named as a defendant in such complaint; and
- C. This Order if such complaint is filed after the order has terminated under this Part.

*Provided, further*, that if such complaint is dismissed or a federal court rules that the respondent did not violate any provision of the order, and the dismissal or ruling is either not appealed or upheld on appeal, then the order will terminate according to this Part as though the complaint had never been filed, except that the order will not terminate between the date such complaint is filed and the later of the deadline for appealing such dismissal or ruling and the date such dismissal or ruling is upheld on appeal.

THEREFORE, the Federal Trade Commission this thirtieth day of September, 2003, has issued this complaint against respondents.



Initial Decision

## INITIAL DECISION

By Stephen J. McGuire, Chief Administrative Law Judge

### I. INTRODUCTION

#### A. Overview and Summary of Decision

This case addresses the advertising campaign for the Ab Force, an electronic muscle stimulation ("EMS") ab belt device. Telebrands Corporation ("Telebrands"), TV Savings, L.L.C. ("TV Savings"), and Ajit Khubani ("Khubani") (collectively "Respondents") marketed the Ab Force through spot television, print, radio, internet, and email advertisements. Complaint Counsel alleges: (1) that Respondents' advertising campaign for the Ab Force makes claims that the use of the Ab Force causes loss of weight, inches, or fat; causes well-defined abdominal muscles; and is an effective alternative to regular exercise; (2) that these claims are false or misleading; and (3) that these claims are material to consumers. Respondents' primary argument is that the Ab Force advertisements did not contain the challenged claims.

The parties focus on the issue of whether Respondents should be held liable for dissemination of ads that capitalize on preexisting consumer beliefs regarding the effects of using ab belts. As discussed more fully in Section III(B)(1), *infra*, this theory of liability is neither central nor determinative of the case. Rather, the central issue is whether the advertisements are likely to mislead consumers, acting reasonably under the circumstances, in a material respect. This matter is resolved utilizing traditional case law analysis.

As set forth in this Initial Decision, the record indicates that the advertisements at issue made false and misleading claims that use of the Ab Force causes loss of weight, inches, or fat; causes well-defined abdominal muscles; and is an effective alternative to regular exercise. These claims, relating to health, weight loss, fitness, or exercise benefits, are clearly made based upon a facial analysis of the advertisements. Extrinsic evidence, although not

## Initial Decision

necessary to the determination of these issues, further supports the ultimate conclusion that the advertising was likely to mislead consumers, acting reasonably under the circumstances, in a material respect. The remedy imposed is an appropriate cease and desist Order.

**B. Summary of Complaint and Answer**

The Federal Trade Commission ("FTC") issued its Complaint in this matter on September 30, 2003. The Complaint charges that Telebrands, TV Savings, and Khubani, individually and as president of Telebrands and sole member of TV Savings, violated Sections 5 and 12 of the Federal Trade Commission Act, as amended ("FTC Act"). Complaint, PP 1-4. The Complaint charges Respondents with making false and misleading claims that the Ab Force causes loss of weight, inches, or fat; causes well-defined abdominal muscles; and is an effective alternative to regular exercise. Complaint, PP 19-20.

In its Answer filed on October 23, 2003, Respondents denied the material allegations of the Complaint and asserted that the evidence would show that the alleged claims were not made in the Ab Force advertising. Answer, PP 19-23.

**C. Procedural Background**

Complaint Counsel filed a Motion for Summary Decision on March 23, 2004. Respondents filed a Motion for Summary Decision on March 24, 2004. Both motions were denied on April 13, 2004 on the basis that whether the advertisements conveyed the alleged claims raised genuine issues of material facts requiring a trial on the merits.

The final prehearing conference was held on April 30, 2004. Trial in this proceeding commenced on May 4, 2004. The last day on which testimony was received was May 6, 2004. The parties subsequently filed post hearing briefs, proposed findings of fact and conclusions of law, and replies thereto. Closing arguments were heard on June 17, 2004.

Initial Decision

The hearing record was closed pursuant to Commission Rule 3.44(c) by Order dated June 18, 2004. This Initial Decision is filed within one year of the issuance of the Complaint and within ninety days of the close of the record, pursuant to Commission Rule 3.51(a).

**D. Evidence**

The Initial Decision is based on the transcript of the testimony, the exhibits properly admitted in evidence, and the briefs, proposed findings of fact and conclusions of law, and replies thereto filed by the parties. Citations to specific numbered Findings of Fact in this Initial Decision are designated by "F." n1

n1 References to the record are abbreviated as follows:

CX -- Complaint Counsel Exhibit  
RX -- Respondents Exhibit  
JX -- Joint Exhibit  
Tr. -- Transcript of Testimony before the Administrative Law Judge  
Dep. -- Transcript of Deposition  
CCPFF -- Complaint Counsel's Proposed Findings of Fact  
CCRPFF -- Complaint Counsel's Response to Respondents' Proposed Findings of Fact  
CCB -- Complaint Counsel's Post Hearing Brief  
CCRB -- Complaint Counsel's Post Hearing Reply Brief  
RPF -- Respondents' Proposed Findings of Fact  
RRPF -- Respondents' Response to Complaint Counsel's Proposed Findings of Fact  
RB -- Respondents' Post Hearing Brief  
RRB -- Respondents' Post Hearing Reply Brief

This Initial Decision addresses only material issues of fact and law. Proposed findings of fact not included in this Initial Decision were rejected, either because they were not supported by the evidence or because they were not dispositive or material to the determination of the allegations of the Complaint or the defenses

## Initial Decision

thereto. The Commission has held that Administrative Law Judges are not required to discuss the testimony of each witness or all exhibits that are presented during the administrative adjudication. *In re Amrep Corp.*, 102 F.T.C 1362, 1670 (1983). Further, administrative adjudicators are "not required to make subordinate findings on every collateral contention advanced, but only upon those issues of fact, law, or discretion which are 'material.'" *Minneapolis & St. Louis Ry. Co. v. United States*, 361 U.S. 173, 193-94 (1959).

**II. FINDINGS OF FACT****A. Factual Background****1. Respondents**

1. Respondents Telebrands Corporation, TV Savings, L.L.C., and Ajit Khubani worked together on the marketing and distribution of the Ab Force product. (JX 1, P 6).

**a. Telebrands Corporation**

2. Respondent Telebrands Corporation ("Telebrands") is a New Jersey Corporation with its principal place of business at 79 Two Bridges Road, Fairfield, New Jersey 07004. (JX 1, P 2).

3. Telebrands was formed in 1987 as the successor to Direct Connection, which Ajit Khubani formed in 1983. (Khubani, Tr. 430).

4. Telebrands is in the business of developing, marketing, and distributing a wide variety of consumer products through direct response advertising. (Khubani, Tr. 431).

5. Telebrands either develops its own products or licenses the right to market products from inventors. (Khubani, Tr. 438).

6. Telebrands provided the financing necessary to perform media management services, credit card processing, customer response services, customs clearance, accounting, and bookkeeping services and acted as importer of record for TV Savings with respect to the Ab Force, as required under the

Initial Decision

Service Agreement between Telebrands and TV Savings. (JX 1, P 14).

**b. TV Savings, L.L.C.**

7. Respondent TV Savings, L.L.C. ("TV Savings"), a Connecticut limited liability company, was organized on January 22, 2002. (JX 1, PP 4, 5).

8. TV Savings has offices at 81 Two Bridges Road, Fairfield, New Jersey 07004. (JX 1, P 3). TV Savings shares office space with Telebrands. (Khubani, Tr. 282).

9. TV Savings was created to handle the Ab Force campaign. (Khubani, Tr. 282-83).

**c. Ajit Khubani**

10. Respondent Ajit Khubani ("Khubani") is the president, chief executive officer, chairman of the board, and sole owner of Telebrands. (JX 1, P 7). Khubani is also the sole member of TV Savings. (JX 1, P 8).

11. Khubani's office is located at 79 Two Bridges Road, Fairfield, New Jersey 07004. (Answer, P 3).

12. Khubani has been involved in direct response television ("DRTV") since 1987 and has been involved with the direct response advertising industry since 1983. (Khubani, Tr. 434).

13. Khubani is a guest lecturer at Princeton University and belongs to the Electronic Retailing Association, where he served on the Board of Directors from 1999 to 2002. (Khubani, Tr. 430-31).

14. Individually or in concert with his officers and employees, Khubani formulates, directs, or controls the policies, acts, and practices of Telebrands and TV Savings. (JX 1, P 9).

15. Khubani was appointed by Telebrands as the "Program Manager" pursuant to the Service Agreement dated January 22, 2002 between Telebrands and TV Savings. (JX 1, P 13). He was also TV Savings' representative under the Service Agreement. (JX 1, P 13). As the Program Manager appointed by Telebrands and

## Initial Decision

as TV Savings' representative under the Service Agreement, Khubani represents both entities with regard to the responsibilities and duties of each under the Service Agreement. (JX 1, P 13).

16. Khubani was ultimately responsible for overseeing the marketing and creative design of the Ab Force advertising and promotional campaign and was primarily responsible for the creation and development of the scripts for the Ab Force television and radio advertising of the Ab Force product. (JX 1, P 11; Khubani, Tr. 271-72). Khubani also set the pricing strategy for the Ab Force and decided when the Ab Force would no longer be marketed or sold. (JX 1, P 12).

## **2. The Direct Response Advertising Industry**

17. Direct response advertising typically describes a product and offers the consumer a vehicle to order the product directly by telephone, by internet, or through a mailing address. (Khubani, Tr. 431-32). Unlike most traditional advertising, direct response advertising allows a consumer to order the product directly from the advertiser. (Khubani, Tr. 432).

18. The direct response industry is significant in scope and includes every form of advertisement to which a customer responds by ordering the product directly, including the internet, catalogues, direct mail, credit card inserts, print media, radio, and television. (Khubani, Tr. 434, 441).

19. DRTV advertising generally takes three forms. One is long form commercials, also called "infomercials." (Khubani, Tr. 432). These are usually program length commercials, typically 28 minutes, 30 seconds in length. (Khubani, Tr. 432). The second form is short form spot DRTV, which are commercials that are typically 30 seconds, 60 seconds, 90 seconds or 120 seconds in length. (Khubani, Tr. 432). The third form is live shows, many of which are broadcast twenty four hours per day, seven days a week. These include QVC, Home Shopping Network, and Shop NBC. (Khubani, Tr. 432-33).

Initial Decision

### **3. Telebrands' Marketing Practices and Techniques**

20. Telebrands sells a variety of products directly to consumers through direct response channels (telephone numbers and addresses contained in the advertising for the product) and through retail stores. (Khubani, Tr. 245-46; JX 1, P 2).

21. Telebrands has employed all three types of DRTV -- infomercials, short form, and live television -- but relies primarily on short form commercials. (Khubani, Tr. 433). Khubani testified that short form commercials are most effectively used to advertise simple products typically sold for twenty dollars or less. (Khubani, Tr. 433).

22. Telebrands has marketed hundreds of products throughout its history and has had a number of successful products that have sold three to fifteen million units each. (Khubani, Tr. 435) (successful products include: Ambervision Sunglasses, the Magic Hanger, Dental White Tooth Whitening System, the Safety Can Opener, the Audubon Singing Bird Clock, the Better Pasta Pot, and the Roll-a-Hose Flat Hose).

23. Telebrands uses a variety of strategies in determining whether to market a product. (Khubani, Tr. 438-43).

24. Khubani typically will observe trends in the marketplace and in various channels of advertising and distribution and will evaluate what products would be appropriate for advertising on television. (Khubani, Tr. 438). This includes assessing what stage the product has reached in its life cycle and evaluating what steps competitors are taking in the marketplace. (Khubani, Tr. 438).

25. If Telebrands believes it has a competitive advantage and/or strategy for competing, Telebrands will compete with products already in the market. (Khubani, Tr. 439). Several times per year, Telebrands identifies existing popular products in the marketplace and enters the market as a competitor by offering a similar product at a lower price. (Khubani, Tr. 439-40).

26. Once Telebrands decides to market a product, it undertakes several steps to bring that product to the marketplace. (Khubani, Tr. 440-43).

## Initial Decision

27. Telebrands first creates test advertising, which involves creating an actual advertisement that is disseminated in a number of markets on a limited basis, and with a limited advertising budget. (Khubani, Tr. 440).

28. Telebrands typically runs test ads for thirty to forty products per year; about ten percent of which it expects will be successful. (Khubani, Tr. 442-43).

29. This test advertising may take the form of print, radio, television, or direct mail advertising. (Khubani, Tr. 441).

30. Test advertisements are disseminated to the public for a limited period of time. (Khubani, Tr. 440).

31. If the response to that test advertising is deemed positive, Telebrands will enter the second phase, called the "rollout" phase. (Khubani, Tr. 440).

32. Before a full-fledged, expensive nationwide campaign is rolled out, Telebrands undertakes a thorough review of its advertising and its acquisition plans so as to minimize risks of loss and ensure compliance with applicable regulations. (Khubani, Tr. 442). This includes a review of intellectual property, production plans, and a compliance review of any rollout advertising. (Khubani, Tr. 442).

33. The final legal review includes "final review of the TV commercial from a claims perspective and a compliance perspective" because "you don't want there to be any issues from any government agencies." (Khubani, Tr. 442). The substantiation for any claims that are made in the advertisements is also reviewed. (Khubani, Tr. 441).

#### **4. The Ab Force Ab Belt**

##### **a. The Product**

34. The Ab Force ab belt is comprised of a black elasticized belt; a thin, diamond-shaped pad measuring approximately nine by five inches that is purple on one side and silver/gray on the other; a warning and instruction label attached to the silver/gray



Initial Decision

side of the pad that divides the silver/gray side of the pad into two areas; and a small, battery powered control unit attached to the purple side of the pad. (Answer, P 6).

35. The Ab Force ab belt is an electronic muscle stimulation ("EMS") device which uses electronic stimulation intended to cause stimulation of the muscles. (JX 1, P 15). Electronic muscle stimulation makes one's muscles contract involuntarily. (Khubani, Tr. 455, 505).

36. The Ab Force is designed so that some amount of electricity goes into the body. (Khubani, Tr. 506).

37. Khubani contacted an overseas manufacturer and, with that manufacturer, began to develop the ab belt product to be sold by Telebrands. (JX 1, P 19).

38. The manufacturer of the Telebrands ab belt product informed Khubani that it was also the manufacturer of the AbTronic ab belt, another EMS device. (Khubani, Tr. 264; JX 1, P 20).

39. The manufacturer informed Khubani that the Telebrands ab belt product would have the same power output as two other advertised ab belt products, the AbTronic and the Fast Abs belts. (Khubani, Tr. 266; CX 18). Khubani believed that he could sell products with the same technology and same or similar power output to consumers for a significantly lower cost than that offered by other ab belt advertisers. (JX 1, P 20).

40. Khubani posed the question of technical comparability to the manufacturer because he wanted to make sure that his advertisements were truthful in saying that the Ab Force used the same technology as ab belts which sold "for as much as \$ 120." (Khubani, Tr. 266-67). The AbTronic sold for \$ 120 and was the ab belt to which Khubani was referring. (Khubani, Tr. 267).

**b. Sales**

41. Gross sales for the Ab Force, including accessories such as batteries and gels, exceeded nineteen million dollars. (JX 1, P 36).

## Initial Decision

42. Respondents sold approximately 747,000 units of the Ab Force and consumers placed a total of 330,510 orders for the Ab Force. (JX 1, PP 25-26).

43. Each of the ads disseminated by Respondents for the Ab Force generated orders from consumers. (JX 1, PP 25-26).

44. The 60 second and 120 second test television commercials (AB-B-60 and AB-B-120, respectively) ran in January of 2002 and were cleared for broadcast nearly ninety-six times. (JX 1, P 24; RX 60).

45. Consumers placed 2,392 orders for the Ab Force by using the telephone number found in the 60 second test commercial. (JX 1, P 27). Consumers also placed 2,238 orders for the Ab Force by using the telephone number found in the 120 second test commercial. (JX 1, P 28; RX 61).

46. The final versions of the 60 second and 120 second television commercials for the Ab Force (AB-E-60 and AB-E-120, respectively) ran from January 19, 2002 until April 7, 2002. (JX 1, P 29).

47. The AB-E-60 and AB-E-120 versions of the television spots were cleared for broadcast 11,508 times. (JX 1, P 30). The Ab Force spots ran during all media day parts and appeared on cable, satellite, and broadcast television outlets in major national markets. (Khubani, Tr. 513; Answer, P 8).

48. Consumers placed 74,566 orders for the Ab Force using the telephone number displayed in the 120 second spot (AB-E-120) and 240,440 orders using the telephone number listed in the 60 second spot (AB-E-60). (JX 1, P 31; RX 61). This constitutes approximately ninety five percent of all orders placed. (JX 1, P 31; RX 61).

49. The radio advertisement ran from December 23, 2001 through January 23, 2002. (RX 61; Khubani, Tr. 272-73). The radio advertisement generated a total of 1,340 orders, 211 for the test spot, and 1,129 for the final radio spot. (Khubani Tr. 493-94; JX 1, P 32; RX 61).

Initial Decision

50. The print advertisement was not run in any publication until February 14, 2002. (JX 1, P 34). At that time, it ran approximately one week in thirteen newspapers, and again as a newspaper insert from March 10, 2002 to March 17, 2002. (JX 1, P 34). The print advertisement generated a total of 6,871 orders, or approximately two percent of all Ab Force orders placed. (JX 1, P 34; RX 61).

51. The internet advertising ran from February 26, 2002 through April 6, 2002 and generated 2,663 orders in response, totaling less than one percent of all orders placed. (RX 61).

52. Respondents spent over four million dollars to televise commercials for the Ab Force. (Complaint, P 8; Answer, P 8).

53. Khubani set the pricing strategy for the Ab Force and decided when the Ab Force would no longer be marketed or sold. (JX 1, P 12).

**c. Advertisements**

54. Khubani wrote the scripts for the radio and print ads on December 18, 2001. (Khubani, Tr. 480-81, 488-89).

55. Khubani testified that he provided those two scripts to Collette Liantonio, the producer of the television advertisements, "so she would have a basis for writing her TV commercials." (Khubani, Tr. 482).

56. Liantonio has a regular working relationship with Telebrands. (RX 81 (Liantonio, Dep. at 26)). Her firm has produced more than a dozen television commercials for Telebrands. (RX 81 (Liantonio, Dep. at 26)).

57. Liantonio testified, however, that no one at Telebrands told her what the Ab Force was designed to do. (RX 81 (Liantonio, Dep. at 53)). She stated that she had no product, no literature, and no written information from Telebrands regarding Ab Force before the day that the television commercial was originally recorded. (RX 81 (Liantonio, Dep. at 30, 32-33)).

58. On December 22, 2001, the day the commercials were shot, Liantonio provided Khubani with a script which began with

## Initial Decision

the statement: "do you wish you could get into shape fast without exercise? Wouldn't you love to have a flatter tummy without painful sit-ups?" (Khubani, Tr. 490).

59. Khubani rewrote Liantonio's scripts, creating two new scripts (AB-B-60 and AB-B-120) that were used to shoot the test ads. (Khubani, Tr. 490, 492-93). It was Khubani's regular practice to rewrite Liantonio's scripts. (RX 81 (Liantonio, Dep. at 36)).

60. Khubani testified that he did not want to make the express claims in Liantonio's scripts "because we didn't possess substantiation to make those claims." (Khubani, Tr. 490).

61. In addition to television, radio, and print advertising, Telebrands also created internet and email advertising. (JX 1, P 33).

62. The Ab Force advertisements ran from December 2001 through April 2002. (Answer, P 7; JX 1, PP 21-22).

63. Khubani believed the product category that included the AbTronic, Ab Energizer, and Fast Abs ab belts was "one of the hottest categories to ever hit the industry." (Khubani, Tr. 255; CX 61).

64. Khubani testified that he felt safe saying in the Ab Force ads that the Ab Force was "just as powerful and effective as those expensive ab belts sold on infomercials on TV," because he asked the factory how the Ab Force compared to those ab belts and was told by the factory that the Ab Force had the same output as the AbTronic and the Fast Abs belts. (Khubani, Tr. 266, 540-41).

## **B. Claims Made in the Ab Force Advertising**

### **1. Facial Analysis**

65. The Ab Force advertisements expressly claim that the Ab Force is technologically comparable to other ab belts and that the Ab Force is significantly less expensive than those other ab belts. (JX 2; JX 3; JX 4; JX 5; CX 1 G; CX 1 H; RX 50; RX 51; RX 52).

Initial Decision

66. The alleged claims that use of the Ab Force causes loss of weight, inches, or fat; causes well-defined abdominal muscles; and is an effective alternative to regular exercise are not expressly made in the Ab Force advertisements. (JX 2; JX 3; JX 4; JX 5; CX 1 G; CX 1 H; RX 50; RX 51; RX 52).

67. Khubani's intention regarding the advertising did not change from one draft to the other. (Khubani, Tr. 492, 498). For example, Khubani testified that "all these scripts were the same message" and that the "message was . . . still the same" even after changes were made to the scripts. (Khubani, Tr. 492, 496, 497, 498).

68. Each television commercial refers to the product name, includes visual images of primary models and stock footage, and includes oral and written statements. (JX 2; JX 3; JX 4; JX 5).

**a. Product Name**

69. Khubani testified that he selected the name Ab Force because "it was designed to work primarily on the abdominal area" and he thought it "was catchy, sort of like Air Force." (Khubani, Tr. 264).

70. The name Ab Force implies that the device applies a force to the abdominal muscles and also implies that use of the device will make the abdominal muscles more forceful. (See JX 2; JX 3; JX 4; JX 5; CX 1 G; CX 1 H; RX 50; RX 51; RX 52).

71. In the short test ad, AB-B-60, the name Ab Force is mentioned three times and in the long test ad, AB-B-120, the name Ab Force is mentioned nine times. (JX 2; JX 3). Moreover, in both test ads, the name Ab Force appears on the screen in a large font size at least four times, not including the order screen. (JX 2; JX 3).

72. In the short rollout ad, AB-E-60, the name Ab Force is mentioned four times and in the long rollout ad, AB-E-120, the name Ab Force is mentioned ten times. (JX 4; JX 5). Moreover, in both rollout ads the name Ab Force appears on the screen in a large font size at least four times, not including the order screen. (JX 4; JX 5).

Initial Decision

**b. Visual Images****i. Primary Models**

73. The television advertisements all feature a female spokesperson, two female models, and a male model. (JX 2; JX 3; JX 4; JX 5).

74. The spokesperson is wearing a business suit; the male model is bare chested with exercise shorts or pants and both female models are wearing sports bras and exercise shorts or pants. (JX 2; JX 3; JX 4; JX 5).

75. Each model has abdomens that are bare except for the Ab Force. (JX 2; JX 3; JX 4; JX 5). Each model is thin with well-defined abs. (JX 2; JX 3; JX 4; JX 5).

76. There are over a dozen depictions of the models wearing the Ab Force and experiencing abdominal muscle contractions. (JX 2; JX 3; JX 4; JX 5).

77. In the longer test and rollout ads, the spokesperson indicates that she is wearing the Ab Force under her business suit, although it is not visible in the ads. (JX 3; JX 5) ("I'm wearing one right now, and it's working while I'm working.").

78. Khubani testified that he used models in the Ab Force ads with slim physiques showing bare parts of their bodies, such as their abs, partly because he felt "this was a product that forced the muscles to involuntarily contract, and the only way you could see what this product was doing and demonstrate what this product does was to show people that were slim enough to show that happening." (Khubani, Tr. 518).

79. Liantonio and her employees at Concepts TV made handwritten notes in the course of creating television commercials for Ab Force. These notes indicate that Ab Force television models were required to wear sportswear and have great abdominal muscles. (CX 4; CX 5; CX 6).

80. A Concepts TV talent confirmation sheet for Ab Force states: "seeing your abs is important." (CX 6). A production job

Initial Decision

card for the Ab Force states: "girl with great abs." (CX 4). Another talent confirmation sheet for Ab Force states: "please have Abs looking their best!" (CX 5). For wardrobe, this talent confirmation sheet calls for a "selection of fitness outfits, a sports bra and bike shorts type look." (CX 5).

**ii. Stock Footage**

81. Khubani asked Liantonio to insert some stock visual images into the advertising as background for the spokesperson. (Khubani, Tr. 541-42, 553-54).

82. The stock footage selected for the commercials included dollar signs, falling numbers, and wheels of technology, which reinforced the message of lower price. (JX 2; JX 3; JX 4; JX 5). There is also stock footage of a spinning globe and an American flag. (JX 2; JX 3; JX 4; JX 5).

83. The stock footage also includes close-up images of a bikini-clad woman showing off her thin waist and well-defined abdominal muscles. (JX 2 (twice); JX 3 (twice); JX 4 (once); JX 5 (once)). The longer ads include a close-up image of a bare-chested, thin, well-muscled man performing a crunch. (JX 3; JX 5). In these stock images, the models are not wearing the Ab Force or any exercise belt. (JX 2; JX 3; JX 4; JX 5).

84. Liantonio testified that Ab Force television commercials contained these stock images of bikini-clad models because "it's a beautiful body," conveying "beauty, the ideal." (RX 81 (Liantonio, Dep. at 69)).

85. When asked whether images of bikini-clad models appeared in Ab Force commercials because this was the image that the viewer was supposed to aspire to, Liantonio responded, "yes." (RX 81 (Liantonio, Dep. at 70)).

**c. Statements**

**i. Oral Statements**

86. The test radio ad contains the statement: "have you seen those fantastic Electronic Ab Belt infomercials on TV? They're

## Initial Decision

amazing . . . promising to get our abs into great shape fast -- without exercise!" (CX 1 H). Khubani testified that this language was included in the test radio script while he was determining "what sounds the best." (Khubani, Tr. 489).

87. The "abs into great shape fast without exercise" language was eliminated from the rollout radio ad and was not included in any of the other ads, although Khubani stated that he felt the print ad and television commercials had the same message as the radio ad. (Khubani, Tr. 488-89, 492, 496, 498).

88. Khubani was asked "there's a reference in the radio ad to no exercise, and the subsequent radio ad did not have that reference. Do you recall that change?" to which he answered, "yes." (Khubani, Tr. 498). The next question asked "did you intend to change the meaning from one ad to the next?" to which Khubani answered, "no, I didn't." (Khubani, Tr. 498).

89. The test ads refer to the "latest fitness craze" while the rollout ads refer to the "latest craze." (JX 2; JX 3; JX 4; JX 5). However, Khubani testified that the message was still the same. (See Khubani, Tr. 495-96).

90. Khubani took out the word "fitness" during a "final review and legal review" and "based on discussions with counsel." (Khubani, Tr. 275, 278).

91. The rollout ads refer to the "same powerful technology as those expensive ab belts" and "same powerful technology as those ab belts sold by other companies," while the test ads state that the Ab Force is "just as powerful and effective" as other ab belts. (JX 2; JX 3; JX 4; JX 5).

92. The sentence "Ab Force is just as powerful and effective" was changed to "Ab Force uses the same powerful technology" during the legal and final review process, although according to Khubani "quite frankly, not that I thought that the other copy was inaccurate." (Khubani, Tr. 276).

93. The opening to the test commercials contain the statements: "I'm sure you've seen those fantastic electronic ab belt infomercials on TV. They're amazing. They're the latest fitness craze to sweep the country, and everybody wants one. The



Initial Decision

problem is they're expensive, selling for up to \$ 120 each." (JX 2; JX 3; CX 1 B; Khubani Tr. 491).

94. Khubani testified that this language was included to serve as a point of reference for his price saving claims. (Khubani, Tr. 486-89).

95. Khubani also testified that this language was included to create excitement as part of an "everyone wants one" bandwagon effect. (Khubani, Tr. 491-92).

96. A "bandwagon effect" is a frequently observed phenomenon in advertising used to generate interest in a product based on the idea that the product is popular and that consumers should buy it to join in the popularity. (Jacoby, Tr. 373).

97. There are no oral statements in the television or radio advertisements about the purpose or effects of using the Ab Force. (JX 2; JX 3; JX 4; JX 5; CX 1 H).

**ii. Written Statements**

98. The words on the screen in the rollout ads include the name Ab Force, the price, and ordering information. (JX 4; JX 5).

99. While the announcer is discussing the price savings, the words that appear reinforce that message by stating: "Price of Electronics Comes Down; Mass Production; Factory Deal; Pass Savings On To You!" (JX 2; JX 3; JX 4; JX 5).

100. In the 60 second rollout ad, the phrase "RELAXING MASSAGE" flashes for a brief moment while the spokesperson says "capable of directing." The words then change to "10 INTENSITY LEVELS" while the announcer says "ten different intensity levels at your abdominal area." (JX 4; Khubani, Tr. 279).

101. In the 120 second rollout ad, the phrase "RELAXING MASSAGE" appears briefly while the spokesperson says "it is so comfortable that you can even wear it under . . ." (JX 5). As the words disappear, she finishes the sentence, saying ". . . your clothes." (JX 5).

## Initial Decision

102. There are no other written statements in the advertisements about the purpose or effect of using the Ab Force. (JX 2; JX 3; JX 4; JX 5; CX 1 G; CX 1 H; RX 50; RX 51; RX 52).

**d. No Massage Claims Made**

103. Telebrands prepared two User's Manuals to accompany the two different models of the Ab Force product. (Khubani, Tr. 499; RX 45; RX 46).

104. The first lines of both User's Manuals state: "Ab Force is intended to provide a relaxing massage. Ab Force is not intended for medical use, for the treatment of any medical condition, or for any permanent physical changes." (RX 45; RX 46) (emphasis omitted).

105. Consumers did not receive the Ab Force User's Manual until after they received the Ab Force ab belt. (Khubani, Tr. 551).

106. The television and radio scripts written by Khubani do not use the word "massage." (Khubani, Tr. 538; CX 1 H). The print, internet, and email ads Khubani wrote also do not use the word "massage." (CX 1 G; RX 50; RX 51; RX 52).

107. Operations Manager of CCT Marketing, Mark Golden, who worked on the Ab Force campaign, was never told that Ab Force was a massager. (Golden, Tr. 223).

108. In the Ab Force television commercials, the models who were depicted using the Ab Force did not indicate, through gestures or utterances, that they were being soothed or felt more relaxed. (JX 2; JX 3; JX 4; JX 5).

109. None of the Ab Force advertisements used the term electrical muscle stimulation or "EMS." (JX 2; JX 3; JX 4; JX 5; CX 1 G; CX 1 H; RX 50; RX 51; RX 52).

Initial Decision

## **e. Surrounding Circumstances**

### **i. The Ab Pulse Campaign**

110. Ab Pulse was another ab belt marketed by Telebrands. (Golden, Tr. 191). Ab Pulse was similar in appearance to the Ab Force. (CX 2). The Ab Pulse was expressly described in the television advertisement as a "massaging ab belt." (Golden, Tr. 218; CX 2).

111. Elements of the television advertisements for the Ab Pulse were strikingly similar to elements in the television advertisements for the Ab Force. Both advertisements contained: identical oral statements regarding a cost savings from mass production and special deals with the factory; identical oral statements that "I'm wearing one right now and it's working while I'm working;" the identical written statement "Price of Electronics Comes Down; Mass Production; Factory Deal; Pass Savings On To You!"; the same stock images of falling numbers, wheels of technology, and the American flag; the same spokeswoman; and male and female models in sports clothing with abdominal area bare except for the ab belt. (CX 2; JX 2, JX 3; JX 4; JX 5).

112. The primary difference from the Ab Force advertisements was that the Ab Pulse ad affirmatively stated that Ab Pulse was unlike electronic ab belts sold through infomercials by: describing the product as "the most innovative massaging ab belt to hit the market," stating, "don't confuse the Ab Pulse with an electronic ab belt that you've seen on infomercials," and by showing a graphic of a red X superimposed on an ab belt displayed alongside the on-screen legend "infomercial ab belts." (Golden, Tr. 218-19; CX 2). In addition, there are express claims in the Ab Pulse ads that the belt is soothing and comfortable and the product is distinguished from other ab belts which "some people find uncomfortable." (CX 2).

113. Based on sales results, Khubani considered the Ab Pulse campaign a failure. (Khubani, Tr. 281). Ab Pulse was offered for about a month and did not receive high call volume. (Golden, Tr. 222).

Initial Decision

**ii. Other Companies' Ab Belt Infomercials**

114. Unlike the Ab Pulse advertising campaign, the four Ab Force televisions ads, the radio, print, and internet ads, and one of the email ads expressly referred to those "fantastic electronic Ab belt infomercials on TV." (JX 2; JX 3; JX 4; JX 5; CX 1 G; CX 1 H; RX 49; RX 51; RX 52). The other Ab Force email ad expressly referred to "Ab belts sold by other companies on infomercials." (RX 50).

115. When Respondent Khubani wrote the script for the Ab Force radio, print, and television ads, and the text for the internet and email ads, he testified that he was attempting to create a "compare and save" advertisement and to establish a point of reference. (JX 1, P 11; Khubani, Tr. 486-87, 489-90).

116. Khubani testified that in "compare and save" advertising, there must be a point of reference for comparison; otherwise the consumer doesn't know "what you're comparing to." (Khubani, Tr. 487).

117. The AbTronic, Ab Energizer, and Fast Abs infomercials were among the ab belt infomercials to which Khubani was referring. (Khubani, Tr. 273-74).

118. AbTronic, Ab Energizer, and Fast Abs were EMS ab belts that were advertised by television infomercials in the United States prior to and during the time period when the Ab Force commercials appeared. (JX 1, P 37).

119. AbTronic, Ab Energizer, and Fast Abs were substantially similar in appearance to the Ab Force, and were comprised of components substantially similar to those used by the Ab Force. (JX 2; JX 3; JX 4; JX 5; JX 7; JX 8; JX 9; JX 10; Mazis, Tr. 60). The Fast Abs and the AbTronic resemble the Ab Force in the button configuration on the belts. (Khubani, Tr. 271).

120. The advertising for the AbTronic, Ab Energizer, and Fast Abs ab belts made express and strongly implied claims that consumers using these devices would lose weight, fat, and inches; gain well-defined abdominal muscles; and achieve such results without the need for exercise. (JX 7; JX 8; JX 9; JX 10; Mazis, Tr. 47-48).

Initial Decision

121. The television advertising for the AbTronic, Ab Energizer, and Fast Abs ab belts contained extensive footage of thin male and female models with well-defined abs wearing the belts over their abdominal areas. (JX 7; JX 8; JX 9; JX 10). These images were displayed on the screen while the infomercial hosts repeatedly represented that the devices caused weight, inch, or fat loss; caused well-developed abs; and were an effective alternative to regular exercise. (JX 7; JX 8; JX 9; JX 10).

122. The AbTronic infomercials stated: "well, you can lose all the weight in the world that you want, but unless you have good muscle tone underneath, you're not going to have a washboard abdomen;" "with systems like the AbTronic where we can stimulate these muscles and you do both things, both the system of losing some weight, losing those inches, and then firming and toning the muscles underneath, that muscle definition will, therefore, show through much better and give you better cosmetic improvement;" and "watch as your ab muscles contract as if you're doing a sit-up . . . Ten minutes on the AbTronic is the equivalent of 600 sit-ups. That's why we guarantee you'll lose two inches off your midsection in less than a month or your money back." (JX 7; CX 96, Ex. 2 at 10-11, 14, 27, 39).

123. The Ab Energizer infomercial contains statements: that the Ab Energizer was "absolutely incredible for people who want tighter abs and want to lose inches around the midsection" and that "with a touch of a button, you can go from flab to rock-hard abs." (JX 8; CX 98, Ex. 2 at 3, 10, 11). The 60 second television spot for the Ab Energizer ab belt contains the following statements: "the secret is Ab Energizer's electronic impulses that stimulate your abs so they contract and relax as if you were doing a sit-up;" "now you can get up to 700 muscle contractions in just 10 minutes and get the tone and definition you've always wanted;" "I've gone from a waist 37 to a waist 34;" and "if you don't lose at least two inches off your waist in the first 30 days, return it for a full refund." (CX 98, Ex. 4 at 3, 4, 5).

124. The Fast Abs infomercial contained the following statements: "you'll drop four inches in the first 30 days. We guarantee it;" "in fact, just 10 minutes of Fast Abs is like doing

## Initial Decision

600 sit-ups;" and "I guarantee you'll firm the saggy midriff, tone those flabby love handles and lose that belly that's been embarrassing you for years. Reshape all your problem areas or simply return Fast Abs, no questions asked. You deserve to have the body you've always imagined and now you don't have to spend all day at the gym to get it." (JX 9; CX 100, Ex. B at 11, 31, 53, 59; CX 100, Ex. D at 32, 63).

125. Infomercials for the AbTronic, Ab Energizer, and Fast Abs ab belts were aired frequently before and during much of the Ab Force campaign, according to the J.W. Greensheet. (CX 126; JX 1, P 37). The J.W. Greensheet is a DRTV industry publication published weekly by Jordan Whitney, Inc. (Khubani, Tr. 248-49).

126. Telebrands has subscribed to the J.W. Greensheet for about twelve years. (JX 1, P 18; Khubani, Tr. 249, 525). The J.W. Greensheet costs approximately \$ 250 per week. (Khubani, Tr. 249).

127. Each issue of the J.W. Greensheet contains a Top 50 ranking of television infomercials, a Top 40 ranking of television spots, and a Top 20 ranking of infomercial products. (Towers, Tr. 286).

128. The J.W. Greensheet states that it compiles its rankings based on confidential media budgets supplied by direct response marketers as well as its own monitoring of national cable and selected broadcast television markets. (Towers, Tr. 288).

129. The AbTronic electronic ab belt appeared twenty four times in the Top 50 infomercial rankings published in the J.W. Greensheet reports between September 3, 2001 and March 4, 2002. (Towers, Tr. 296-97; CX 72 at T011047; CX 73 at T011036; CX 74 at T011025; CX 75 at T011014; CX 76 at T011001; CX 77 at T011160; CX 78 at T011145; CX 79 at T011129; CX 80 at T011112; CX 62 at T011098; CX 82 at T011084; CX 83 at T011071; CX 84 at T011060; CX 85 at T011337; CX 86 at T011325; CX 87 at T011313; CX 88 at T011299; CX 89 at T011285; CX 90 at T011406; CX 91 at T011393; CX 92 at T011379; CX 93 at T011364; CX 94 at T011349; CX 95 at T011503).

Initial Decision

130. The Ab Energizer infomercial appeared nineteen times in the Top 50 infomercial rankings published in the J.W. Greensheet reports between October 15, 2001 and March 4, 2002. (Towers, Tr. 297; CX 77 at T011161; CX 78 at T011145; CX 79 at T011129; CX 80 at T011112; CX 62 at T011098; CX 82 at T011084; CX 83 at T011071; CX 84 at T011060; CX 85 at T011337; CX 86 at T011325; CX 87 at T011313; CX 88 at T011299; CX 89 at T011285; CX 90 at T011407; CX 91 at T011393; CX 92 at T011379; CX 93 at T011364; CX 94 at T011350; CX 95 at T011504).

131. The Ab Energizer television spot appeared nineteen times in the Top 40 direct response spots rankings published in the J.W. Greensheet reports between October 15, 2001 and March 4, 2002. (CX 77 at T011163; CX 78 at T011147; CX 79 at T011131; CX 80 at T011114; CX 62 at T011100; CX 82 at T011086; CX 83 at T011073; CX 84 at T011062; CX 85 at T011339; CX 86 at T011327; CX 87 at T011315; CX 88 at T011301; CX 89 at T011287; CX 90 at T011409; CX 91 at T011395; CX 92 at T011381; CX 93 at T011366; CX 94 at T011351; CX 95 at T011505).

132. Fast Abs infomercials appeared fifteen times in the Top 50 infomercial rankings published in the J.W. Greensheet reports between November 19, 2001 and March 4, 2002. (Towers, Tr. 298; CX 62 at T011099; CX 82 at T011084; CX 83 at T011071; CX 84 at T011060; CX 85 at T011337; CX 86 at T011325; CX 87 at T011313; CX 88 at T011299; CX 89 at T011285; CX 90 at T011406; CX 91 at T011393; CX 92 at T011379; CX 93 at T011364; CX 94 at T011349; CX 95 at T011503).

133. The Fast Abs television spot appeared fifteen times in the Top 40 direct response spots rankings published in the J.W. Greensheet reports between November 19, 2001 and March 4, 2002. (CX 62 at T011101; CX 82 at T011086; CX 83 at T011073; CX 84 at T011062; CX 85 at T011340; CX 86 at T011328; CX 87 at T011315; CX 88 at T011301; CX 89 at T011287; CX 90 at T011410; CX 91 at T011395; CX 92 at T011381; CX 93 at T011366; CX 94 at T011352; CX 95 at T011506).

## Initial Decision

134. AbTronic, Ab Energizer, and Fast Abs were the only ab belts that appeared in the J.W. Greensheet Top 50 infomercials rankings between early September 2001 and mid-April 2002. (Towers, Tr. 305).

135. The Federal Trade Commission issued complaints against the advertisers of the Ab Energizer, Fast Abs, and AbTronic on May 7, 2002. (JX 1, P 46).

136. Television advertisements for Ab Force were ranked five times in the Top 40 television spot rankings published in the J.W. Greensheet between February 4, 2002 and March 4, 2002. (CX 91 at T011395; CX 92 at T011381; CX 93 at T011366; CX 94 at T011351; CX 95 at T011505).

**iii. Other EMS Device Advertisements**

137. Respondents placed on the record promotional materials for eight EMS devices: (1) IGIA Electrosage (RX 72); (2) Mini Wireless Massage System (RX 73); (3) Accusage (RX 74); (4) Smart Toner (RX 75); (5) GymFitness (RX 76); (6) ElectroGym (RX 77); (7) Slim Tron (RX 78); and (8) Slendertone Flex (RX 79).

138. Khubani admitted that the EMS ab products being marketed at the time made a variety of statements, from weight loss and rock hard abs to relaxing massage, toning, and strengthening claims. (Khubani, Tr. 471-72).

139. The IGIA Electrosage is not an electronic ab belt and was advertised in spot advertising, not infomercials. (RX 72; Towers, Tr. 304). The IGIA Electrosage was advertised to provide a massage that would leave users "feeling refreshed, relaxed, and reenergized." (RX 72). From September 2001 through February 2002, the short spot for the IGIA Electrosage appeared approximately twenty times in the J.W. Greensheet Top 40 direct response spot rankings. (Towers, Tr. 304; CX 73 at T011038; CX 74 at T011027; CX 75 at T011016; CX 76 at T011003; CX 77 at T011162; CX 78 at T011147; CX 79 at T011131; CX 80 at T011114; CX 81 at T011100; CX 82 at T011086; CX 83 at T011073; CX 84 at T011062; CX 85 at T011339; CX 86 at



Initial Decision

T011327; CX 87 at T011315; CX 88 at T011301; CX 90 at T011409; CX 91 at T011395; CX 92 at T011381; CX 93 at T011367).

140. The Mini Wireless Massage System product is not an electronic ab belt and was advertised in spot advertising, not infomercials. (RX 73; Towers, Tr. 301, 304). The television commercial for the Mini Wireless Massage System promises a "soothing and relaxing massage" and promises to "relieve muscle pain, soreness, and stiffness." (RX 73; Khubani, Tr. 459). The television spot for the Mini Wireless Massage System did not appear in the Top 40 commercial spot rankings published in the J.W. Greensheet from September 2001 through February 2002. (CX 62; CX 72-CX 95).

141. The Accusage product is not an electronic ab belt. (RX 74; Towers, Tr. 301-02). The Accusage promises a "relaxing muscle massage." (RX 74). The Accusage was listed once in the Top 40 Direct Response Spots in the J.W. Greensheet for the weeks of December 24, 2001 (CX 86 at T011328) and January 14, 2002 (CX 88 at T011309).

142. The television spot for the Smart Toner ab belt states that the product is "the fast, easy, sexy way to have the slim, sexy body you've always wanted" and "in fact, we'll guarantee you'll lose two inches from your waist in just two weeks, or your money back." (RX 75). Product testimonials in the Smart Toner ab belt commercial assert the loss of fifteen pounds, "a big reduction in body fat," and "over two inches lost in the waistline." (RX 75). The Smart Toner advertisement provided by Respondents was a short spot, not an infomercial. (RX 75). The television spot for the Smart Toner ab belt did not appear in the Top 40 commercial spot rankings published in the J.W. Greensheet from September 2001 through February 2002. (Towers, Tr. 302; see also CX 62; CX 72-CX 95).

143. The GymFitness advertisement mentions both massage and fitness, promising to "condition your muscles without working out;" offering "a relaxing massage;" promising to "work [] your abs and condition your muscles, toning them perfectly;" and repeatedly states that it is for use "when you can't get to the

## Initial Decision

gym." (RX 76). The infomercial for the GymFitness ab belt did not appear in the Top 50 infomercial rankings or the Top 40 commercial spot rankings in the J.W. Greensheet from September 2001 through February 2002. (Towers, Tr. 302-03; see also CX 62; CX 72-CX 95).

144. The ElectroGym advertisement provided by Respondents was a short spot, not an infomercial. (RX 77). The ElectroGym product briefly appeared in an infomercial for the IGIA Electrosage. (RX 72). In this infomercial, the ElectroGym ab belt was offered as a "free gift" in connection with the sale of the IGIA Electrosage. (RX 72; Khubani, Tr. 451). This infomercial contains a statement that the ElectroGym ab belt offers "a great workout." (RX 72; Khubani, Tr. 451). The television spot for the ElectroGym appeared approximately eight times in the Top 40 commercial spot rankings in the J.W. Greensheet from September 2001 through February 2002. (Towers, Tr. 303).

145. The Slim Tron advertisements indicates that the product will "tone your muscles and [you will] get a great looking body," and indicates that users will lose three inches off their waist. (RX 78). The television spot for the Slim Tron ab belt appeared approximately three times in the Top 40 commercial spot rankings in the J.W. Greensheet from September 2001 through February 2002. (Towers, Tr. 303; see also CX 62; CX 72-CX 95).

146. The Slendertone Flex advertisement provided by Respondents was a short spot, not an infomercial. (RX 79). Slendertone Flex is an electronic ab belt. (RX 79). Direct response television spots for Slendertone Flex have very recently appeared on television. (Khubani, Tr. 447). Respondent Khubani stated that the presentation for Slendertone Flex on QVC was "very similar" to the recorded Slendertone Flex television spot, which is dated November 10, 2003. (Khubani, Tr. 447; RX 79). The recorded Slendertone Flex television spot states: "You mean I don't have to do sit-ups anymore?" and "9 in 10 users reported firmer, tighter abs." (Khubani, Tr. 447 (playing exhibit); RX 79). Television advertising for the Slendertone Flex ab belt did not appear in the Top 50 infomercial rankings or the Top 40 commercial spot rankings in the J.W. Greensheet from September

Initial Decision

2001 through February 2002. (See Towers, Tr. 305; CX 62; CX 72-CX 95).

## **2. Extrinsic Evidence**

147. Complaint Counsel offered the expert opinion of Michael Mazis, Ph.D. to provide extrinsic evidence of the claims conveyed by the Ab Force ads. (Mazis, Tr. 35 et seq.; CX 58).

148. Mazis is Professor of Marketing at the Kogod School of Business, American University. (CX 58, P 2; Mazis, Tr. 37). He has been a faculty member at American University for over twenty years, serving ten years as chair of the Department of Marketing. (CX 58, P 2; Mazis, Tr. 37). For over a decade, he has taught undergraduate and graduate courses in marketing research and consumer behavior. (CX 58, P 2; Mazis, Tr. 37-38).

149. Mazis served as a consultant on advertising issues and consumer behavior for the FTC, Food and Drug Administration, Consumer Product Safety Commission, Department of Justice, U. S. Mint, Bureau of Alcohol, Tobacco, and Firearms, the State of California, and Warner-Lambert Pharmaceutical Company. (CX 58, PP 4-5).

150. Mazis is a member of the American Marketing Association and a member and former director of the Association for Consumer Research. (CX 58, P 6). He was editor of the Journal of Public Policy & Marketing from 1992 to 1995 and Associate Editor of The Journal of Consumer Affairs from 1998 to 2001. (CX 58, P 6; Mazis, Tr. 38).

151. Mazis has conducted hundreds of surveys and research studies. (Mazis, Tr. 38). Mazis has published over sixty articles in academic journals including the Journal of Marketing, Journal of Consumer Research, Journal of Marketing Research, Journal of Public Policy & Marketing, The Journal of Consumer Affairs, Journal of Personality and Social Psychology, Journal of Experimental Social Psychology, and Journal of the American Medical Association. (CX 58, P 7; Mazis, Tr. 38).

## Initial Decision

152. Respondents offered the expert opinion of Jacob Jacoby, Ph.D who severely criticized Mazis's analysis and conclusions. (Jacoby, Tr. 335 et. seq).

153. Jacoby holds an endowed chair at the Stern School of Business at New York University where he teaches research methodology and consumer behavior courses. (Jacoby, Tr. 336-37).

154. Jacoby served as a peer reviewer on the chapter on survey research evidence in the Reference Manual on Scientific Evidence published by the Federal Judicial Center and wrote the chapter on consumer psychology in the International Encyclopedia of the Social and Behavioral Sciences. (Jacoby, Tr. 337-39).

155. Jacoby served as president of the Association for Consumer Research and the Society for Consumer Psychology and is a fellow of both institutions and has received awards from the Association for Consumer Research and from the Society for Consumer Psychology for research excellence. (Jacoby, Tr. 339-40).

156. Jacoby received several major grants from the National Science Foundation and from the American Association of Advertising Agencies to study the comprehension and miscomprehension of advertising. (Jacoby, Tr. 339).

**a. Mazis's Facial Analysis of the Ab Force Ads**

157. Mazis opines that consumers took away from the Ab Force ads certain core performance claims that were either the result of familiarity with ads for other ab belts or implied by images and words within the four corners of the Ab Force ads. (Mazis, Tr. 61-62).

**i. Direct Effects Within the Four Corners of the Ab Force Ads**

158. Direct effects within the four corners of the ad cause consumers to make inferences about Ab Force and take away implied claims. (Mazis, Tr. 66-67).

Initial Decision

159. "Even if you had never heard of an ab belt before, even if you didn't have any category beliefs about ab belts, you could see the ad and you could make inferences because there's certain implied claims in the ads." (Mazis, Tr. 66).

160. "Visual images are really more important than the verbal messages, because they really remain in people's memories." (Mazis, Tr. 59).

161. Direct effects in the challenged ads include the appearance of fit, trim models and the depiction of the Ab Force belt, itself, shown visibly pulsating the abdominal muscles of the models. (Mazis, Tr. 66-67).

162. Another direct effect is the name Ab Force which could have a double effect on consumers: "on the one hand, it applies force to your abs because of this stimulation, and you can also say it makes your abs a force. In other words, it makes your abs noticeable, that they . . . are really well developed." (Mazis, Tr. 60).

**ii. Indirect Effects of the Ab Force Ads**

163. Mazis refers to the effects generated on consumers because of previous exposure to ab belts through either the infomercials for AbTronic, Ab Energizer, or Fast Abs, word-of-mouth about ab belts, and retail packaging for ab belts as "indirect effects" which cause consumers to develop an ab belt category of beliefs. (Mazis, Tr. 48, 65-66).

164. Mazis testified that these beliefs would cause consumers to associate ab belts with well-developed abs, losing inches, losing weight, and effective alternatives to exercise. (Mazis, Tr. 48). As a result of these indirect effects, Mazis opines that the Ab Force television spots contain implied claims that using Ab Force will result in well-developed abs and loss of inches around the waist. (Mazis, Tr. 61).

165. In identifying indirect effects that could shape and influence a consumer's category beliefs, Mazis reviewed and considered the Complaint and exhibits in this matter; transcripts and videotapes of the infomercials for AbTronic, Ab Energizer,

## Initial Decision

and Fast Abs; and infomercial ranking reports for the AbTronic, Ab Energizer, and Fast Abs products. (Mazis, Tr. 120-21; CX 58, P 9).

166. Mazis testified that the ab belt category beliefs may be effected by word-of-mouth communication generated by viewers of the infomercials, or by people who have purchased an ab belt and communicated their impressions to others who did not see the ads, or by seeing the packaging for them on display in retail outlets. (Mazis, Tr. 64-65, 169-70). According to Mazis, people could be exposed to claims that appear on the retail packaging for ab belt products that appear on the shelves of retail outlets and they could use such information to form their own category beliefs. (Mazis, Tr. 139-40, 170-71).

167. According to Mazis, people exposed to infomercials for other ab belts do not necessarily remember the specifics of the ads they saw, rather, the ab belt infomercials produce general category beliefs about ab belts that would be triggered by the Ab Force ads. (Mazis, Tr. 156-57).

168. Mazis provided no empirical evidence that Ab Force advertisement viewers who happened to see the ads for AbTronic, Ab Energizer, or Fast Abs would remember or take away that information. (Mazis, Tr. 184).

169. Mazis's opinion is grounded in the psychological/consumer behavior theory of "categorization." (Mazis, Tr. 49, 156-57). He testified that according to the categorization theory, people take objects such as products and group them together in categories based on their similarity. (Mazis, Tr. 49, 156-57).

170. The categorization theory is generally accepted in the field of consumer behavior. (Mazis, Tr. 49). A leading proponent of the theory, Mita Sujan, published a well-known peer-reviewed article on the subject in the Journal of Consumer Research about fifteen years ago. (Mazis, Tr. 49).

171. According to Sujan, the "basic premise [of the categorization approach] is that people naturally divide the world of objects around them into categories enabling an efficient

Initial Decision

understanding and processing of the environment. . . . If a new stimulus can be categorized as an example of a previously defined category, then the affect associated with the category can be quickly retrieved and applied to the stimulus." (CX 57 at 31).

172. Sujan investigated if and how novice and expert consumers processed information regarding one category of cameras in relation to another. (CX 57). In reaching a conclusion, Sujan designed an experiment whereby two descriptions were given in simulated print ads and were used to match or mismatch conditions to eliminate the confound between the manipulation of information match/mismatch and the actual content of the information. (CX 57 at 35). Test participants were asked to recall the type of camera about which they had received information in order to ensure that they had the relevant category available in memory. (CX 57 at 38).

173. While Respondents' marketing expert, Jacoby, testified that he was familiar with the theory and with Sujan's article, he did not agree with application of the theory to this case. (Jacoby, Tr. 344-45).

174. Jacoby testified that according to categorization theory consumers will form an understanding of categories and will place objects into categories, and thus will interpret and infer things about those objects. (Jacoby, Tr. 344).

175. Jacoby objected to the application of categorization theory to this case because, as presented by Sujan, categorization theory relies on the participants having a preexisting category of beliefs and there is no evidence that consumers have a preexisting ab belt category of beliefs. (Jacoby, Tr. 344-45).

176. A communication to consumers does not necessarily mean that the communication was sufficient to have an impact on consumers' beliefs and behaviors. (Jacoby, Tr. 369). Simply because a source conveys information does not necessarily mean it has an impact on the receiver exposed to it, or that the communication has an impact to a significant degree. (Jacoby, Tr. 369). In other words, a mere reference to "other ab belts" or the physical appearance of the product or other elements may not be

## Initial Decision

sufficient to trigger any category beliefs that consumers may have. (Jacoby, Tr. 367).

177. Jacoby indicated that in order to determine whether there was an impact on consumers, further research needs to be conducted. (Jacoby, Tr. 370-72).

178. Mazis, however, testified that four key elements in the Ab Force commercials would cause consumers to categorize the Ab Force with the AbTronic, Ab Energizer, and Fast Abs ab belts. (Mazis, Tr. 59-60). These four elements are: references in Ab Force ads to the other ab belts on television, the visual images of models with well-developed abs and slim bodies, the physical appearance of the Ab Force product which is similar to the other ab belts, and the similarity of the name Ab Force to the names of the other ab belts. (Mazis, Tr. 59-60).

179. When asked at trial whether he should have considered other EMS ab products in reaching his opinions, Mazis testified that while consumers would form a category belief based on seeing EMS ab belts, they would not include in that category other EMS ab products unless they were "relatively similar" in appearance. (Mazis, Tr. 135-36).

180. When asked whether products with a number of patches as opposed to one patch, and which made similar claims, could be considered in the category, Mazis admitted that he would need to examine the product and the ads before he could reach any opinion: "It would be one of those things where I would have to see the product and look at the -- look at the advertisements. I just -- answering it hypothetically is basically impossible." (Mazis, Tr. 136).

181. Mazis indicated that there "might be a different category" established for products that looked different (for example, products that had wires) and that made some different claims. (Mazis, Tr. 136).



Initial Decision

182. Mazis admitted that his opinion that the only ab belts in the ab belt category would be ones that looked the same and made the same claims "is a theory, this is a model" and that he had conducted no quantitative testing of this theory. (Mazis, Tr. 136-37).

183. Mazis was never provided with advertisements or products, nor did he review advertisements or retail packaging, for any other EMS ab product. (Mazis, Tr. 123-24, 134).

184. Mazis testified that he did not know how many consumers would have been exposed to the ads for AbTronic, Ab Energizer, or Fast Abs. (Mazis, Tr. 128, 182-83). Indeed, Mazis had no opinion about the likelihood that somebody who saw the Ab Force commercials would also have seen one of the ads for AbTronic, Ab Energizer, or Fast Abs, because he had "no information on that." (Mazis, Tr. 172).

185. Mazis testified that, through the process of selective attention, people who have an interest in certain product categories such as those relating to losing weight or exercise, e.g., the target audience, will pay attention to commercials for such products. (Mazis, Tr. 172-73). Thus, based on his knowledge of consumer behavior and how people watch television, if there is a propensity for people to watch one ab belt infomercial, there is a propensity for those same people to selectively attend to other such advertising. (Mazis, Tr. 173).

186. Mazis relied on his "assumption that there's a lot of exposure to a lot of these different products," because these infomercials ran "on weekends, late nights and so on, when there aren't a lot of programming choices out there." (Mazis, Tr. 172-73). This assumption, however, ignores his own testimony that spot advertising may not necessarily run at the same time or on the same stations to which infomercials are limited. (Mazis, Tr. 131-32).

187. Even if there was significant overlap between the Ab Force ad viewership and the viewership for AbTronic, Ab Energizer, and Fast Abs infomercials, Mazis admitted that it was not certain that the viewers who were exposed to the ads would

## Initial Decision

have necessarily retained or even comprehended the ads. (Mazis, Tr. 172). He testified that retention would depend on "a lot of factors that go into that," none of which he described or demonstrated applied in this case. (Mazis, Tr. 172).

188. Mazis admitted that he had seen no empirical data about the ability of viewers to remember what they saw in the infomercials for AbTronic, Ab Energizer, and Fast Abs. (Mazis, Tr. 184). He conceded that his opinions "about the take-away from those ads are just based on my facial analysis of those ads." (Mazis, Tr. 184).

189. Mazis did not know what messages were being conveyed by advertisements or packaging for other EMS ab products. (Mazis, Tr. 167-71). Mazis did not know what messages were being conveyed by word-of-mouth communication. (Mazis, Tr. 169-70). Mazis did not know what other print or radio advertisements were being disseminated. (Mazis, Tr. 181-82). Indeed, Mazis admitted that when he referred to category beliefs, he was referring only to "ab belt category beliefs relative to those three products and only those three products [AbTronic, Ab Energizer, and Fast Abs]." (Mazis, Tr. 171-72).

190. Despite having no reliable information regarding how frequently any one advertisement at issue had aired, and no information identifying the stations, days, or times those ads aired, Mazis stood by his belief that "many consumers would have been exposed to these ads." (Mazis, Tr. 166).

191. Because Mazis failed to test the theory that consumers necessarily formed or retained categorization beliefs about EMS ab products prior to viewing the Ab Force ads, or whether they even saw any of the ads for AbTronic, Ab Energizer, or Fast Abs prior to seeing the Ab Force ads, Mazis's opinion that there was categorization by consumers is merely speculation, not evidence of the association. (Jacoby, Tr. 347-51).

192. Mazis's assumption that consumers who saw the Ab Force ad also likely saw the ads for AbTronic, Ab Energizer, and Fast Abs is mere speculation that was untested in this matter. (Jacoby, Tr. 367). Mazis's opinion that consumers actually

Initial Decision

developed categorization beliefs is mere untested speculation. (Jacoby, Tr. 347-51).

**b. The Copy Test**

193. Mazis conducted a consumer survey in which he designed a copy test of an Ab Force television spot. (Mazis, Tr. 67).

194. A copy test is an in-person survey in which people are shown an advertisement, and asked a number of questions in terms of their perceptions of the advertisement, which is sometimes referred to as the "take-away" from the advertisement. (Mazis, Tr. 67).

195. The purpose of the copy test was to assess whether a 60 second advertisement for Ab Force communicates to consumers that using Ab Force results in well-developed abdominal muscles; causes users to lose inches around the waist; causes users to lose weight; is an effective alternative to exercise; and removes fat deposits. (CX 58, P 22).

196. Copy testing the Ab Force ad was preferable to surveying past purchasers of Ab Force ab belts because people are not likely to remember why they bought a product a year or more ago or exactly what claims the ads made, and they might make up answers. (Mazis, Tr. 151-52). Showing consumers the ad and getting their immediate response is the more valid means of measuring the way consumers perceive the ad. (Mazis, Tr. 151-52).

197. Mazis designed the study, and the contractor for the study, U.S. Research, collected the data. (Mazis, Tr. 67).

198. U.S. Research is reliable to execute such copy tests. (Mazis, Tr. 67).

Initial Decision

**i. The Universe for the Copy Test Was Properly Defined**

199. The copy test was conducted in nine shopping malls located in Albuquerque, NM; Austin, TX; Colorado Springs, CO; Orlando, FL; Poughkeepsie, NY; St. Louis, MO; Schenectady, NY; Seattle, WA; and Toledo, OH. (Mazis, Tr. 67-68; CX 58, P 24).

200. The choice of the mall locations assured geographic diversity throughout the country and facilitated achieving an approximately equal number of interviews in the four Census regions. (Mazis, Tr. 71).

201. Copy test interviews were conducted in December, 2003 and January, 2004. (CX 58, P 25).

202. Interviewers from U.S. Research approached shoppers in the selected malls and asked them if they would answer a few brief questions. (Mazis, Tr. 72).

203. Interviewers used a screening questionnaire ("screener") designed by Mazis to determine whether potential respondents were qualified to participate in the study. (Mazis, Tr. 68; CX 58, P 26; CX 58, Ex. C).

204. Age and sex quotas for copy test survey participants were based upon the results of a 1996 survey of consumers who were trying to lose weight and which was published in the October 13, 1999 issue of the Journal of the American Medical Association. (Mazis, Tr. 71-72; CX 58, P 23).

205. The survey called for a survey universe of sixty percent females, forty percent males with twenty percent 18-29 years of age, forty five percent 30-49 years of age, and thirty five percent 50 years of age and older. (Mazis, Tr. 71-72; CX 58, P 23).

206. The screener asked both "inclusion" questions and "exclusion" questions. (Mazis, Tr. 73-76; see CX 58, P 26). These questions were designed to bring into the study people who might have some propensity to buy the product and eliminate people who wouldn't be typical consumers. (Mazis, Tr. 68).

207. The questionnaire screened out people who worked for an advertising agency, a public relations firm, or a marketing

Initial Decision

research firm because they would have specialized knowledge of research technique. (Mazis, Tr. 75; CX 58, Ex. E).

208. Likewise, the questionnaire screened out people who worked for a store or company that sells exercise, fitness, weight loss products or programs, or products to massage the body because such people would have specialized knowledge about fitness, exercise, weight loss, or massage and consequently would not be typical consumers who would have a propensity to purchase the Ab Force. (Mazis, Tr. 75; CX 58, Ex. E).

209. In order to qualify for the study, potential survey participants had to have purchased in the past twelve months a product or used a service to help them lose weight, tone muscles, or massage the body. (CX 58 at 26; Mazis, Tr. 73-74). Consumers who had bought products or used a service to lose weight, tone their muscles, or massage their body were in a class of likely purchasers of the Ab Force ab belt. (Mazis, Tr. 73). Jacoby opined that this particular question was appropriate. (Jacoby, Tr. 353-54).

210. In addition, potential respondents, in the past twelve months, had to have purchased a product by calling a toll-free number that was included in a television ad, program, or infomercial. (CX 58, P 26; Mazis, Tr. 74-75). Consumers who never bought products by calling toll free numbers in response to television ads, programs, or infomercials would be unlikely purchasers of the Ab Force. (Mazis, Tr. 75).

211. The screening questionnaire did not ask about prior purchases of ab belts. (Mazis, Tr. 152).

212. The screening questionnaire did not ask about whether people had been exposed to advertising for ab belts. (Mazis, Tr. 153-54).

213. The screening questionnaire also included "masking" questions regarding working for companies that sell personal computers or prescription drugs that served to disguise the true intent of the study and prevent people from assuming that the study was for a fitness or massage product. (Mazis, Tr. 74; CX 58, Ex. E).

Initial Decision

**ii. The Control Advertisement**

214. Survey respondents who qualified to participate in the study were randomly assigned to either a test group or a control group. (CX 58, PP 12, 27). The test group (consisting of 182 survey respondents) watched a version of the Ab Force ad (CX 104) that Respondents aired most often (AB-E-60). (Mazis, Tr. 79; CX 58, PP 12, 27). The control group (consisting of 220 survey respondents) saw an advertisement created by Mazis (CX 105) that was a "cleansed" (60 second) version of one of the 120 second rollout commercials for Ab Force. (Mazis, Tr. 83; CX 58, P 28).

215. "Use of a control group is an attempt to essentially remove preexisting beliefs as a possible cause of the results we see." (Mazis, Tr. 157).

216. A "cleansed" or control ad may have allegedly misleading elements removed and/or a statement correcting the alleged deception. (CX 58, P 28).

217. In the control ad, the mention of ads for other electronic abdominal belts advertised on television was removed, the stock images of a woman in a bikini and a man performing a crunch were removed, and some, but not all, images of models wearing the Ab Force were removed. (CX 105).

218. The control ad did not eliminate the elements which Mazis indicated were direct effects that convey the claims that use of the Ab Force causes loss of weight, inches, or fat; causes well-defined abdominal muscles; and is an effective alternative to regular exercise. (See F. 158-62).

219. The control ad includes three images of the female and male model with well-defined abs, wearing the Ab Force and sports clothing, and experiencing muscle contractions. (CX 105).

220. In the control ad, the name Ab Force is stated verbally six times. (CX 105).

221. The results for the control ad "are relatively high numbers for a control ad" which Mazis attributes to preexisting beliefs about ab belts. (Mazis, Tr. 108).

Initial Decision

### **iii. The Questions Were Unbiased and Appropriate**

222. The control ad included the following statement at the end of the commercial: "Ab Force for a relaxing massage" which appeared on the screen and was read by an announcer. (Mazis, Tr. 88-89; CX 58, P 28).

223. Survey respondents who qualified for the study were escorted to the interviewing facility maintained by the research organization and were administered one of the two versions of the "main" questionnaire. (Mazis, Tr. 77-78).

224. Approximately one half of the survey respondents were administered questionnaire version Version 1A and the other half Version 1B. (Mazis, Tr. 92). Each version contained exactly the same questions, but the order was changed to control for bias resulting from question ordering. (Mazis, Tr. 92; CX 58, P 29).

225. In addition, each version of the questionnaire was color coded blue or green to correspond to either the "blue dot" test ad or the "green dot" control ad. (Mazis, Tr. 91-92). Respondents were initially asked to identify the color of the dot on the tape cassette they were about to view. (Mazis, Tr. 91-92). This was done to assure that respondents viewed the correct commercial. (Mazis, Tr. 91; CX 58, P 30).

226. Survey participants were assigned to the test group or the control group at random. (Mazis, Tr. 90).

227. Each survey participant saw the test ad or the control ad twice before the questionnaire was administered. (CX 58, P 31; Mazis, Tr. 92).

228. Survey participants were asked to identify the brand name of the product that was advertised in the commercial they had just seen. (CX 58, P 31). The eighty one survey participants who were unable to identify the sponsor were not asked any of the subsequent questions and were eliminated from the study. (Mazis, Tr. 93, 147-48; CX 58, P 31).

229. Mazis testified that the failure of eighty one participants to recall the name of the product indicated to him that those

## Initial Decision

participants were not paying attention to the ad, which he considered a good reason not to include them in the final result. (Mazis, Tr. 147).

230. Eliminating inattentive participants from the survey, although not required, was not unreasonable because inattentive survey respondents may have been unlikely to give meaningful responses to the ensuing questions. (See Mazis, Tr. 94).

231. The remaining participants were then asked an open-ended question: "what did the commercial say, show, or imply about Ab Force?" (CX 58, P 32).

232. Open-ended questions are questions in which there are no defined answer categories. (Mazis, Tr. 95) ("People just give the answer in their own words, and the interviewer records that response verbatim.")

233. Question 4 asked respondents whether the commercial said, showed, or implied that Ab Force improves users' appearance, fitness, or health. (CX 58, P 33). Participants were shown a card with only three possible answers: "yes, it does," "no, it doesn't," or "don't know or no opinion," and asked to provide one of those three answers. (CX 58, P 33). This is a "filter" question designed to reduce guessing to subsequent questions. (CX 58, P 33).

234. Only participants who answered question 4 in the affirmative were asked the ensuing close-ended questions. (CX 58, P 33; Mazis, Tr. 95).

235. The purpose of the filtering question was to eliminate participants who might be prone to guess in answering subsequent closed-ended questions. (Mazis, Tr. 95; CX 58, P 33). If participants did not see a fitness, health, or appearance claim in the commercial, their answers to the more specific questions would not be very reliable. (Mazis, Tr. 95).

236. Question 5 began with participants being informed that they would be read a list of statements, of which, some, all, or none, may have been implied by or made in the Ab Force commercial. (Mazis, Tr. 95-96).



Initial Decision

237. This instruction was followed by a series of eight statements with the order rotated throughout the questionnaires so that there was no order bias. (CX 58, P 34; Mazis, Tr. 96).

238. Five of the eight statements were at issue in the case:

"Using Ab Force causes users to lose inches around the waist."

"Using Ab Force results in well-defined abdominal muscles."

"Using Ab Force removes fat deposits."

"Using Ab Force is an effective alternative to regular exercise."

"Using Ab Force causes users to lose weight."

(CX 34; Mazis, Tr. 97-98).

239. The three other statements (regarding stomach ulcers, nausea, and blood pressure) were included to mask the intent of the study. (CX 58, P 34). Mazis explained that these were included to assure that participants were paying attention and not just saying yes to every question. (Mazis, Tr. 97).

240. After each statement was read to participants, they had the opportunity to select one of three possible answers: "YES, it is implied by or made in the Ab Force Commercial," "NO, it is not implied by or made in the Ab Force commercial," or, "You DON'T KNOW or you have NO OPINION." (Mazis, Tr. 96; CX 58, P 34).

241. Question 6 asks "does or doesn't the Ab Force commercial say, show, or imply that the Ab Force gives users a massage?" (Mazis, Tr. 98). Mazis explained that this question was included in anticipation of Respondents' claim that their ads conveyed a massage claim. (Mazis, Tr. 98).

242. This massage question was asked before question 4 (the appearance, fitness, health question) in half of the questionnaires to control for order bias. (Mazis, Tr. 98-99).

## Initial Decision

243. Question 7 asks whether, in the last thirty days, respondents had seen, read, or heard a news story or stories featuring an abdominal device. (Mazis, Tr. 100).

244. Question 7 was added just before the study was about to go into the field and was prompted by recent news accounts on television discussing an FTC action regarding companies making weight loss claims with depictions of ab belts. (Mazis, Tr. 99).

245. Those who answered affirmatively were asked "as best you can remember, what did the news story or stories say about abdominal belt ab belts?" (CX 58, P 36).

246. Forty-one persons gave responses indicating that the news stories said that the ab belts were ineffective, didn't cause weight loss, were dangerous, or were a false advertising scam. (CX 58, P 41; Mazis, Tr. 100).

247. These survey participants were removed out of prudence to avoid potential bias due to the recent news stories. (Mazis, Tr. 154-56).

248. At the completion of the survey, completed questionnaires from the nine shopping malls were sent to U.S. Research where they were reviewed to confirm that they had been filled out properly and for possible mistakes in the way the interview was administered. (Mazis, Tr. 101).

249. The names and telephone numbers of all survey respondents who provided them were then sent to Park Research, an interviewing service not affiliated with U.S. Research, to conduct telephone validation. (CX 58, P 40).

250. The purpose of validation is to confirm that the survey respondents did, in fact, participate in the interview and that they met the criteria for being included in the study. (Mazis, Tr. 101; CX 58, PP 40-41).

251. As a result of the validation process, 171 survey respondents were eliminated from the database. (CX 58, P 41). Most of the people were removed because they said that they hadn't purchased a product from an 800 number. (Mazis, Tr. 101).

Initial Decision

252. After validation, Mazis removed the questionnaires of the forty one people who, in response to question 7, indicated either that ab belts were ineffective, didn't cause weight loss, were dangerous, or were a false advertising scam. (CX 58, P 41; Mazis, Tr. 100, 154-56).

253. Mazis also did not include the eighty one partially completed questionnaires of survey respondents who were inattentive and unable to identify Ab Force as the sponsor of the advertisement. (Mazis, Tr. 102; CX 58, P 41).

254. Therefore, 389 questionnaires were included in the data tabulations. (CX 58, P 41).

**iv. Results**

255. Copy test results were reported in total percentages, and then in terms of statistical significance. (CX 58).

256. Under Mazis's supervision, U.S. Research developed a coding framework for the open-ended question: "what did the commercial say, show, or imply about Ab Force?" (CX 58, P 38; CX 58, Ex. F; Mazis, Tr. 104). Two independent coders, who were unaware of the study's purpose, coded the responses to the open-ended question. (Mazis, Tr. 102).

257. The responses to this open-ended question reveal that 22.3% of survey respondents in the test ad group and 11.9% of the survey respondents in the control group indicated that the advertisement communicated that using Ab Force results in well-defined abdominal muscles, in loss of weight or inches around the waist, or in an improved physique. (CX 58, P 42; Mazis, Tr. 104-05).

258. For the statement that using Ab Force causes users to lose weight, 43% of the test group and 28.1% of the control group responded affirmatively. (Mazis, Tr. 107). The net difference between the test group and the control group for the lose inches around the waist statement was 15.7%. (Mazis, Tr. 106). That result was statistically significant at the .01 level. (Mazis, Tr. 107).

## Initial Decision

259. To the statement that using Ab Force causes users to lose inches around the waist, 58.1% of the test group and 42.4% of the control group responded affirmatively. (Mazis, Tr. 106). The net difference between the test group and the control group for the lose inches around the waist statement was 15.7%. (Mazis, Tr. 106). That result was statistically significant at the .01 level. (Mazis, Tr. 106).

260. For the statement that using Ab Force removes fat deposits, 22.9% of the test group and 19.0% of the control group responded affirmatively. (Mazis, Tr. 107). The net difference between the test group and the control group of 3.9% was not statistically significant. (Mazis, Tr. 107).

261. To the statement that using Ab Force results in well-defined abdominal muscles, 65.4% of the test group and 48.1% of the control group responded affirmatively. (Mazis, Tr. 106). The net difference between the test group and the control group for the well-defined muscles statement was 17.3%. (Mazis, Tr. 106). That result was significant to the .001 level. (Mazis, Tr. 106).

262. For the statement that using Ab Force was an effective alternative to exercise, 39.1% of the test group and 28.6% of the control group responded positively. (Mazis, Tr. 107). The net difference between the test group and the control group for the lose inches around the waist statement was 10.5%. (Mazis, Tr. 107). That result was statistically significant at the .05 level. (Mazis, Tr. 107).

263. The following chart summarizes the affirmative responses to each of the five key closed-ended statements posed in Question 5:

Initial Decision

Using Ab Force . . .	TEST AD	CONTROL AD
Results in well-defined abdominal muscles	117 (65.4%)	101 (48.1%)
Causes users to lose inches around the waist	104 (58.1%)	89 (42.4%)
Causes users to lose weight	77 (43.0%)	59 (28.1%)
Is an effective alternative to exercise	70 (39.1%)	60 (28.6%)
Removes fat deposits	41 (22.9%)	40 (19.0%)
Lowers blood pressure	9 (5.0%)	6 (2.9%)
Relieves nausea	2 (1.1%)	4 (1.9%)
Relieves pain from stomach ulcers	0 (0%)	9 (4.3%)

(CX 58, P 47).

264. If the maximum percent of participants who responded affirmatively to the control questions is subtracted from the percent responding affirmatively to the tested ad, then the claims at issue were found by 60.4% (well-defined abdominal muscles); 53.1% (lose inches around the waist); 38% (lose weight); 34.1% (alternative to exercise) and 17.9% (removes fat deposits). (See F. 258-63, 267-69).

265. The level of affirmative responses for the control ad was relatively high, particularly for the well-defined abdominal muscles response (48.1%) and the inches around the waist response (42.4%). (Mazis, Tr. 107-08; CX 58, P 45).

266. Mazis attributed the high level of response to survey respondents' prior knowledge of ab belts and the presence in the control ad of the name Ab Force and the visual image of an ab belt around the waist. (Mazis, Tr. 108; CX 58, P 45).

267. None of the test group and only 4.3% of the control group answered yes to the statement about stomach ulcers. (CX 58, Ex. H at 12).

268. To the statement about relieving nausea, only 1.1% of the test ad participants and 1.9% of the control ad participants answered yes. (CX 58, Ex. H at 15).

269. Only 5.0% of the test group and 2.9% of the control group said yes to the statement that Ab Force lowers blood pressure. (CX 58, Ex. H at 17).

Initial Decision

**C. The Ab Force Does Not Cause Loss of Weight, Inches, or Fat; Does Not Cause Well-Defined Abdominal Muscles; and Is Not an Effective Alternative to Regular Exercise**

270. Use of the Ab Force does not cause loss of weight, inches, or fat. (JX 6, P 16)

271. Use of the Ab Force does not cause well-defined abdominal muscles. (JX 6, P 17)

272. Use of the Ab Force is not an effective alternative to regular exercise. (JX 6, P 18)

273. Respondents did not possess and rely upon substantiation for the alleged claims that use of the Ab Force causes loss of weight, inches, or fat; causes well-defined abdominal muscles; and is an effective alternative to regular exercise. (JX 6, P 19)

**D. Claims That Use of the Ab Force Causes Loss of Weight, Inches, or Fat; Causes Well-Defined Abdominal Muscles; and Is an Effective Alternative to Regular Exercise Are Material to Consumers**

274. Claims that use of the Ab Force causes loss of weight, inches, or fat; causes well-defined abdominal muscles; and is an effective alternative to regular exercise relate to the central purpose of the Ab Force and are material to consumers. (See F. 97, 102-109).

275. Claims that use of the Ab Force causes loss of weight, inches, or fat; causes well-defined abdominal muscles; and is an effective alternative to regular exercise involve appearance, fitness, or health claims and are material to consumers. (See CX 58).

**III. ANALYSIS AND CONCLUSIONS OF LAW****A. Preliminary Issues****1. Jurisdiction**

The Complaint charges Respondents with violating Sections 5 and 12 of the FTC Act. 15 U.S.C. § 45, 52. Section 5(a)(2) of

## Initial Decision

the FTC Act gives the Commission jurisdiction "to prevent persons, partnerships, or corporations . . . from using . . . unfair or deceptive acts or practices in or affecting commerce." 15 U.S.C. § 45(a)(2); *FTC v. Pantron I Corp.*, 33 F.3d 1088, 1095 (9th Cir. 1994); *American Fin. Services Assoc. v. FTC*, 767 F.2d 957, 966 (D.C. Cir. 1985); *Koch v. FTC*, 206 F.2d 311, 315 (6th Cir. 1953)). The Ab Force ab belt, an EMS device which uses electronic stimulation of the muscles, is a device within the meaning of Section 15 of the FTC Act which defines "device" as including "an instrument, apparatus, implement, machine, [or] contrivance . . . which is . . . intended to affect the structure or any function of the body of man." 15 U.S.C. § 55(d). Respondents engaged in a nationwide advertising campaign to offer for sale and sell the Ab Force. F. 41-53. Respondents were engaged in and affected commerce, as "commerce" is defined in Section 4 of the FTC Act. 15 U.S.C. § 44. Respondents do not dispute that the acts and practices of Respondents challenged in the Complaint have been and are now in or affecting commerce, as "commerce" is defined in the FTC Act, or that the Federal Trade Commission has jurisdiction in this proceeding. RRPF at 157, 159. Accordingly, the Commission has jurisdiction over Respondents and the subject matter of this proceeding.

**2. Burden of Proof**

Under Commission Rule of Practice 3.51(c)(1), "an initial decision shall be based on a consideration of the whole record relevant to the issues decided, and shall be supported by reliable and probative evidence." 16 C.F.R. § 3.51(c)(1). The Commission made amendments to its Rules of Practice, effective May 18, 2001. FTC Rules of Practice, Interim rules with request for comments, 66 Fed. Reg. 17,622 (April 3, 2001). Through these amendments, the Commission removed the requirement of Rule 3.51(c)(3) that the initial decision of an Administrative Law Judge ("ALJ") be supported by "substantial" evidence. 66 Fed. Reg. at 17,626. The Administrative Procedure Act, however, requires that an ALJ may not issue an order "except on consideration of the whole record or those parts thereof cited by a party and supported by and in accordance with the reliable,

## Initial Decision

probative, and substantial evidence." Administrative Procedure Act ("APA") 5 U.S.C. § 556(d). According to Black's Law Dictionary, "probative evidence" means having the effect of proof; tending to prove, or actually proving an issue. "Substantial evidence" is defined in Black's Law Dictionary as such evidence that a reasonable mind might accept as adequate to support a conclusion. At the adjudicative level of these proceedings, any difference between "probative" evidence and "substantial" evidence is not dispositive under these standards. Therefore, all findings and conclusions in this Initial Decision are supported by reliable, probative, and substantial evidence.

The parties' burdens of proof are governed by Commission Rule 3.43(a), Section 556(d) of the APA, and case law. FTC Rules of Practice, Interim rules with request for comments, 66 Fed. Reg. 17,622, 17626 (April 3, 2001). Pursuant to Commission Rule 3.43(a), "counsel representing the Commission . . . shall have the burden of proof, but the proponent of any factual proposition shall be required to sustain the burden of proof with respect thereto." 16 C.F.R. § 3.43(a). Under the APA, "except as otherwise provided by statute, the proponent of a rule or order has the burden of proof." 5 U.S.C. § 556(d). See also *Steadman v. SEC*, 450 U.S. 91, 102 (1981) (APA establishes preponderance of the evidence standard of proof for formal administrative adjudicatory proceedings). The preponderance of the evidence standard has been used in false advertising cases. See, e.g., *In re Peacock Buick, Inc.*, 86 F.T.C. 1532; 1975 FTC LEXIS 4, \*46-48 (1975).

For these reasons, Complaint Counsel's case in this proceeding shall be adjudicated under the preponderance of evidence standard.

**B. Analytical Framework**

The FTC Act makes it unlawful to engage in unfair or deceptive practices or to induce consumers to purchase certain products through advertising that is misleading in a material respect. 15 U.S.C. §§ 45, 52, 55. An "advertisement is deceptive under the Act if it is likely to mislead consumers, acting



Initial Decision

reasonably under the circumstances, in a material respect." *Kraft, Inc. v. FTC*, 970 F.2d 311, 314 (7th Cir. 1992); see also *Pantron*, 33 F.3d at 1095; *In re Thompson Medical*, 104 F.T.C 648, 788 (1984), *aff'd*, 791 F.2d 189 (D.C. Cir. 1986). "In implementing this standard, the Commission examines the overall net impression of an ad and engages in a three-part inquiry: (1) what claims are conveyed in the ad; (2) are those claims false or misleading; and (3) are those claims material to prospective consumers." *Novartis Corp. v. FTC*, 223 F.3d 783, 786 (D.C. Cir. 2000); accord *Kraft*, 970 F.2d at 314.

The Complaint alleges that the Ab Force advertisements made the claims that use of the Ab Force causes loss of weight, inches, or fat; causes well-defined abdominal muscles; and is an effective alternative to regular exercise; that these claims are false and misleading; and that these claims are material to consumers. Complaint PP 19-23.

### **1. Whether the Claims at Issue Are Conveyed in the Ad**

To prove its case, Complaint Counsel must establish that consumers, acting reasonably under the circumstances, would likely interpret the message of the advertisement to have conveyed the alleged claims. See *In re Novartis Corp.*, 127 F.T.C. 580, 679 (1999), *aff'd*, 223 F.3d 783 (D.C. Cir. 2000). Claims may be either express claims or implied claims. *In re Kraft, Inc.*, 114 F.T.C. 40, 120 (1991), *aff'd*, 970 F.2d 311 (7th Cir. 1992); *Thompson Medical*, 104 F.T.C. at 788.

An advertisement may convey numerous representations, and the same advertising elements may be amenable to more than one reasonable interpretation. *Kraft*, 114 F.T.C. at 120 n.8; *Thompson Medical*, 104 F.T.C. at 789 n.7. Thus, the representation(s) alleged in the Complaint need not be the only reasonable interpretation(s) of the challenged advertising; an advertisement that reasonably can be interpreted in a misleading way is deceptive, even though other, non-misleading interpretations may be equally possible. *Kraft*, 114 F.T.C. at 120 n.8; *Thompson Medical*, 104 F.T.C. at 789 n.7, 818; *In re Bristol-Myers Co.*, 102 F.T.C. 21, 320 (1983), *aff'd*, 738 F.2d 554 (2d Cir. 1984).

## Initial Decision

Moreover, evidence that consumers have actually been misled is not necessary; the likelihood of deception is the standard by which the advertising is judged. *American Home Prods. Corp. v. FTC*, 695 F.2d 681, 687, 687 n.9 (3d Cir. 1982); *In re Cliffdale Assocs., Inc.*, 103 F.T.C. 110, 165 (1984).

In determining whether the asserted claims were made, the advertising, itself, is reviewed in a facial analysis. If it can be determined with confidence from the facial analysis that the claims appear in the advertising, then resort to extrinsic evidence of those claims is unnecessary. *Novartis*, 127 F.T.C. at 680; *In re Stouffer Foods Corp.*, 118 F.T.C. 746, 798 (1994); *Kraft*, 114 F.T.C. at 121; *Thompson Medical*, 104 F.T.C. at 789. If, however, the claims are not self-evident or reasonably apparent on the face of the advertising, then extrinsic evidence that the advertising made the asserted claims will be considered. *Novartis*, 127 F.T.C. at 680; *Stouffer*, 118 F.T.C. at 798-99; *Kraft*, 114 F.T.C. at 121; *Thompson Medical*, 104 F.T.C. at 789; *Bristol-Myers*, 102 F.T.C. at 319.

**a. Facial Analysis****i. Express Claims**

Express claims directly state the representation at issue. *Kraft*, 114 F.T.C. at 120; *Thompson Medical*, 104 F.T.C. at 788. In this case, the Ab Force advertisements expressly claim that the Ab Force is technologically comparable to other ab belts and that the Ab Force is significantly less expensive than other ab belts. F. 65. These price savings and comparable technology claims were made by oral and written statements that were reinforced by visual images in the advertisements. F. 82, 99. The alleged claims that use of the Ab Force causes loss of weight, inches, or fat; causes well-defined abdominal muscles; and is an effective alternative to regular exercise are not, however, expressly made in the Ab Force advertisements. F. 66. Indeed, the purpose of the Ab Force is never expressly identified in any of the advertisements. F. 97, 102. Therefore, to determine whether the claims alleged in the Complaint were made in the advertisements, an analysis of whether the alleged claims are implied must be undertaken.

Initial Decision

## **ii. Implied Claims -- from Four Corners**

Implied claims are any claims that are not express. Kraft, 114 F.T.C. at 120. Implied claims range on a continuum from claims that would be "virtually synonymous with an express claim through language that literally says one thing but strongly suggests another to language which relatively few consumers would interpret as making a particular representation." *Id.* (quoting Thompson Medical, 104 F.T.C. at 789); accord Novartis, 127 F.T.C. at 680. Implied claims will only be found where it may be determined with confidence, after examining all of the constituent elements of the advertising, that the challenged implied claims are conspicuous, self-evident, or reasonably clear on the face of the ad. Kraft, 970 F.2d at 318-20; Thompson Medical, 104 F.T.C. at 320.

An advertisement will only be found to contain implied claims where the "language or depictions are clear enough to permit us to conclude with confidence, after examining the interaction of all of the constituent elements, that they convey a particular implied claim to consumers acting reasonably under the circumstances." Kraft, 114 F.T.C. at 121; Thompson Medical, 104 F.T.C. at 789. However, "if, based on [an] initial review of the evidence from the advertisement itself, we cannot conclude with confidence that an advertisement can reasonably be read to contain a particular implied message, we will not find the ad to have made the claim unless extrinsic evidence allows us to conclude that such a reading of the ad is reasonable." Kraft, 114 F.T.C. at 121 (citing Thompson Medical, 104 F.T.C. at 789; Bristol-Myers, 102 F.T.C. at 319).

Such facial interpretation must be based upon the overall net impression of the advertisement, taken as a whole. Kraft, 970 F.2d at 314, 319. The determination must be made based on the "net impression created by the interaction of different elements in a given ad, not [based on] the elements by themselves." Thompson Medical, 104 F.T.C. at 793 n.17. A facial analysis does not involve the effect of individual words, phrases, or visual images. See Thompson Medical, 104 F.T.C. at 793, n.17. In this

## Initial Decision

case, the product name, visual images, and statements all contribute to the overall net impression of the advertisements, taken as a whole.

A product name may play a role in implying a claim. E.g., *Jacob Siegel Co. v. FTC*, 327 U.S. 608, 609 (1946) (addressing order where name "Alpacuna" implied that the product contained vicuna); *Thompson Medical*, 104 F.T.C. at 793 (name "Aspercreme" implied that product contains aspirin). Upon a facial review of the challenged Ab Force advertisements, the Court determines that the name Ab Force conveys the impression that the device works on the abdominal muscles -- either because it applies force to the abs or because it makes the abs more forceful. See F. 162. As Khubani admitted, the name Ab Force was selected because "the product was designed to work primarily on the abdominal area." F. 69. That Khubani also claims he chose the name because of the play on "Air Force" does not preclude other interpretations. See *Kraft*, 114 F.T.C. at 120; *Thompson Medical*, 104 F.T.C. at 789. While the name Ab Force, alone, would not be sufficient to imply a claim, in combination with the visual images and words used, it contributes to the overall net impression that use of the Ab Force confers health, weight loss, exercise, or fitness benefits.

Visual images are effective in conveying claims and may also be used to determine implied claims. See, e.g., *Kraft*, 114 F.T.C. at 322; see also F. 160. The visual images in the Ab Force television commercials consist of shots of the spokesperson, over a dozen shots of three models, and stock footage. F. 73-85. The three models are wearing exercise clothing and each model is thin, with well-defined abs. F. 74-75. Each model has an abdomen that is bare, except for wearing the Ab Force. F. 75. During the ads, each model can be seen experiencing abdominal muscle contractions. F. 76. Stock footage includes, inter alia, a close-up image of a bikini-clad woman showing off her thin waist and well-defined abdominal muscles. F. 83. The longer ads also include a close-up of a bare-chested, thin, well-muscled man performing a crunch on an exercise bench. F. 83. In this stock footage, the models are not wearing the Ab Force. F. 83. These visual images strongly convey the impression that the Ab Force is

Initial Decision

designed to provide health, weight loss, fitness, or exercise benefits.

Statements contained in advertisements may also be used to determine implied claims. See, e.g., Kraft, 114 F.T.C. at 322. The statements in the challenged Ab Force advertisements are both oral and written on the screen. F. 86-102. The test radio ad opened by referring to other ab belt infomercials, stating that they "promise to get our abs into great shape fast -- without exercise." F. 86. When asked whether he intended to change the meaning in the rollout radio ad (which did not include the "no exercise" language), Khubani said that he did not. F. 87-88. The test television and radio ads make statements that refer to the "latest fitness craze." F. 89. Although the rollout television ads only refer to the "latest craze," Khubani testified that the message was still the same. F. 89. Khubani testified that the word "fitness" was taken out during a "final review and legal review." F. 90. In addition, the phrases "powerful technology" and "just as powerful and effective" conspicuously imply that the Ab Force does something "powerful" and "effective" to the abdominal muscles. See F. 91-92. These phrases -- "abs into great shape fast -- without exercise," "latest fitness craze," "latest craze," "powerful technology," and "powerful and effective" -- strongly and clearly imply that the Ab Force is, inter alia, a fitness or exercise device, and convey the impression that the Ab Force is designed to provide health, weight loss, fitness, or exercise benefits.

Respondents seemingly argue that the Ab Force advertisements made massage claims as well as price savings and comparable technology claims. See RPF at 24-25. Although the phrase "relaxing massage" is briefly flashed on the screen, it is too brief and non-specific to put consumers on notice that the device is intended merely or exclusively for massage. The "relaxing massage" phrase is displayed in connection with a discussion of the ten intensity levels in the short rollout ad and in the context of the belt's comfort in the long rollout ad. F. 100-01. If the consumer noticed the phrase, it would be reasonable to conclude that "relaxing massage" was but one of the ten available power settings of the device or that the Ab Force included a relaxing, comfortable setting. Indeed, other EMS devices

## Initial Decision

explicitly advertise that some available settings provide a massage, while other EMS device ads combine claims of massage with claims of weight loss, fitness, or muscle development. F. 137-46. Thus, the single, momentary phrase "relaxing massage" does not offset or counter the numerous oral and printed statements, in combination with the name and visual images, which contribute to the overall net impression that use of the Ab Force causes loss of inches, weight and fat; causes well-defined abs; and is an effective alternative to regular exercise.

If there is an intended purpose or effect of using the Ab Force other than losing inches, weight, and fat; building well-defined abs; or being an effective alternative to regular exercise, that purpose or effect was never identified in any of the Ab Force advertisements. See F. 97, 102. Indeed, the only evidence of the purpose for which the Ab Force is intended is the statements in the instruction manual that consumers received after purchasing the product. F. 103-09. In this case there are no words, phrases, or visual images that effectively counter the implication that use of the Ab Force causes loss of inches, weight, and fat; causes well-defined abs; and is an effective alternative to regular exercise. See F. 65-109. Such an absence of any identified purpose may be considered in determining an ad's claims. *Thompson Medical*, 104 F.T.C. at 648 (noting "the absence of any elements giving a contrary impression, such as express disclosures").

The overall net impression of the product name, visual images, and statements in the four corners of the challenged Ab Force advertisements is conspicuous, self-evident, and reasonably clear so that the Court may conclude with confidence that the advertisements convey the claims that use of the Ab Force causes loss of inches, weight, and fat; causes well-defined abs; and is an effective alternative to regular exercise. This conclusion is based solely upon an assessment of the interaction of all of the constituent elements, or the net impression created by the advertisements, without reference to ads for other ab belts or the need for extrinsic evidence. An analysis of the surrounding circumstances behind the development of the challenged ads contributes to this facial analysis.

Initial Decision

### **iii. Implied Claims -- from Surrounding Circumstances**

The "circumstances surrounding" advertising, including the advertiser's intent, may be considered in false advertising cases. Thompson Medical, 104 F.T.C. at 789; Novartis, 127 F.T.C. at 683. "While a respondent need not intend to make a claim in order to be held liable, evidence of intent to make a claim may support a finding that the claims were indeed made." Novartis, 127 F.T.C. at 683. In this case, Respondents' intent to make the alleged claims is demonstrated from an examination of Respondents' prior experience marketing another ab belt, the Ab Pulse, and from the process of drafting the Ab Force advertisements. In addition, although the existence of advertising for other ab belts is appropriate to consider as part of the surrounding circumstances, the impact on consumers of the advertising for other ab belts is not clear and cannot be determined on a facial analysis.

The record shows that Khubani decided to enter the ab belt market after noticing a mention of the AbTronic in industry market reports and after determining that ab belts, including AbTronic, Ab Energizer, and Fast Abs, were "one of the hottest categories to ever hit the industry." F. 63. The Ab Pulse was a "massaging ab belt" marketed by Telebrands. F. 110. The Ab Pulse was similar in appearance to the Ab Force and the advertisements for the Ab Pulse were strikingly similar to the advertisements for the Ab Force in making claims of cost savings. F. 111. The Ab Pulse television commercial differed from the Ab Force commercials by distinguishing it from other ab belts by: stating "don't confuse the Ab Pulse with an electronic ab belt that you've seen on infomercials;" by showing a graphic of a red X superimposed on an ab belt displayed alongside the on-screen legend "infomercial ab belts;" and by making a soothing or comfort claim. F. 112. The Ab Pulse was offered for sale for about a month, did not receive high call volume, and, based on sales results, was considered by Khubani to be a marketing failure. F. 113. Thus, Respondents' first attempt to enter the market by selling a "massaging ab belt" and differentiating it from other electronic ab belts proved unsuccessful. The Ab Pulse campaign, however, provided Respondents with valuable

## Initial Decision

experience in the ab belt market and affected the development of its subsequent advertising.

Khubani wrote the scripts for the radio and print ads for the Ab Force on December 18, 2001. F. 54. The radio ad included an express statement that other ab belts "promise to get our abs into great shape fast without exercise." F. 86. On December 22, 2001, the day the commercials were shot, Liantonio provided Khubani with a script which began with the statements: "do you wish you could get into shape fast without exercise? Wouldn't you love to have a flatter tummy without painful sit-ups?" F. 58. Khubani rewrote Liantonio's scripts, deleting these express claims, and creating two new scripts (AB-B-60 and AB-B-120) that were used to shoot the test ads. F. 59. Parts of the Ab Force scripts are identical to parts of the Ab Pulse scripts. F. 111. Khubani testified that he did not want to make the express claims in Liantonio's scripts because "we didn't possess substantiation to make those claims." F. 60. While Khubani clearly did not want to make health, weight loss, fitness, and exercise claims expressly, given his desire to enter "one of the hottest categories to ever hit the industry" and his inability to successfully market a "massaging ab belt," the evidence shows that Khubani intended to imply those same claims. Merely removing false express claims will not protect an advertisement where the same claims are implied. *Thompson Medical*, 104 F.T.C. at 792 ("We note to begin with that none of the Aspercreme ads includes an express representation that Aspercreme contains aspirin. On the contrary, like much advertising we find deceptive, the ads are drafted with an artful choice of words to make what Thompson thought were literally correct statements.").

The record here demonstrates Khubani's desire to enter the ab belt market and recounts his initial failure to successfully market the Ab Pulse, a product whose only stated purpose was as a "massaging ab belt." F. 110. Given the commercial success of the "infomercial ab belts" and despite knowing that he did not have substantiation to expressly make the type of health, weight loss, fitness, and exercise claims contained in those ads, Khubani nevertheless created commercials for the Ab Force which relied on the name, visual images, and statements to implicitly make



Initial Decision

those very same false and misleading claims. F. 60, 65-102, 114-36. The absence of an expressly identified purpose of using the Ab Force required consumers to rely on these implied claims. Thus, Khubani's intent seems clear. While Khubani may have removed the express health, weight loss, fitness, and exercise claims, perhaps in an effort to avoid liability, he clearly intended to make those same claims by implication.

Complaint Counsel argues that in this case, the Ab Force advertisements invite scrutiny of the surrounding circumstances by explicitly referring to other Ab Belt infomercials. CCB at 28. Each of the Ab Force commercials made some comparison of the Ab Force's power and effectiveness to the other ab belts advertised on television. F. 91. Complaint Counsel asserts that the express references in the Ab Force ads to infomercials for competing ab belts, along with the claims of comparability to those products, invite consumers to think of those infomercials while viewing the Ab Force ads. CCB at 28. While such express references to other ab belt infomercials must be considered in the analysis of the surrounding circumstances, it is not clear from such an analysis what effect this inclusion has on consumer beliefs.

Respondents assert that the reference to other ab belts infomercials was part of a compare and save marketing strategy and was meant only to serve as a point of reference for the comparison. RB at 22-23. Khubani testified that there were a number of other products in this category and that his marketing strategy was to offer the same technology at a cost savings. F. 39, 65, 93. In addition, Khubani testified that the language is designed as hype to build excitement about the product. F. 94-96. While there clearly are express price saving and comparable technology messages in the advertisements, this, by itself, does not insulate Respondents from liability. See *Kraft*, 114 F.T.C. at 120 n.8; *Thompson Medical*, 104 F.T.C. at 789 n.7. Respondents will be liable for deceptive advertising even if other, non-false, messages are conveyed. See *Kraft*, 114 F.T.C. at 120 n.8; *Thompson Medical*, 104 F.T.C. at 789 n.7.

## Initial Decision

The impact on consumers of the express reference in Ab Force ads to other ab belt infomercials is inconclusive. Complaint Counsel has not met its burden of demonstrating whether references to other ab belt infomercials effected the claims conveyed by the ads. Thus, the Court cannot conclude with confidence that references to other ab belt infomercials would lead consumers to take away the alleged claims. Where the impact of a statement is not conspicuous, self-evident, or reasonably clear on the face of the ad, and cannot be determined with confidence from the face of the ad, extrinsic evidence is required to determine the impact of that statement. See *Kraft*, 970 F.2d at 318; *Thompson Medical*, 104 F.T.C. at 320. However, as explained in Section II(B)(2)(1)(ii), *supra*, the extrinsic evidence also does not support the theory that claims are implied in the Ab Force ads merely by the reference to other ab belt infomercials.

Despite this conclusion, it is clear from the other evidence of the surrounding circumstances, including the Ab Pulse campaign and the development of the Ab Force campaign, when combined with the product name, visual images, and statements, that the ads make the claims that use of the Ab Force causes loss of inches, weight, and fat; causes well-defined abs; and is an effective alternative to regular exercise. Although an examination of the extrinsic evidence is not necessary for disposition of this case, that evidence likewise supports the Court's conclusions.

**b. Extrinsic Evidence**

When extrinsic evidence is used to determine the meaning of an ad, the evidence may consist of expert opinion, consumer testimony, copy tests, surveys, or any other reliable evidence of consumer interpretation. *Cliffdale*, 103 F.T.C. at 166; see also *Thompson Medical*, 104 F.T.C. at 790. The opinions of expert witnesses in the proceeding as to how an advertisement might reasonably be interpreted may be considered "if such opinions are adequately supported." *Kraft*, 114 F.T.C. at 122. However, where the opinions voiced by experts are not adequately supported, those opinions will be given little weight. *Thompson Medical*, 104 F.T.C. at 790. "To be adequately supported [those] opinions that describe empirical research or analyses [must be] based on

Initial Decision

generally recognized marketing principles or other objective manifestations of professional expertise. Opinions not so supported may easily be contradicted by the contrary opinions of opposing experts and thus may be of little value in resolving the issue." *Id.* at 790 n.11.

Complaint Counsel's expert, Dr. Michael Mazis, is qualified in this matter to testify as an expert witness in consumer response to advertising, including a facial analysis of advertising, advertising effectiveness, consumer behavior, marketing research, including the design and implementation of surveys and analysis of surveys. F. 147-51. Mazis testified that in this case the implied claims are established through direct effects from the four corners of the advertisements; through indirect effects of prior exposure to ab belts through other advertising, word-of-mouth, or retail packaging; and as evidenced by a copy test which he conducted. F. 157-69. Respondents' expert, Dr. Jacob Jacoby, is qualified in this matter to testify as an expert witness in consumer behavior and consumer psychology, as well as consumer comprehension and miscomprehension of advertising. F. 152-56. Jacoby severely criticized Mazis's conclusions and methods. F. 152. After a review of the expert testimony, the Court concludes that Mazis's conclusions are entitled to varying degrees of weight, as explained below.

**i. Direct Effects**

A type of evidence that will be considered, if offered, is the opinion of expert witnesses as to how an advertisement might reasonably be interpreted. *Thompson Medical*, 104 F.T.C. at 790; *Kraft*, 114 F.T.C. at 122. Respondents argue that Mazis's analysis of the direct and indirect effects is no more than his own personal opinion and is not the proper subject of expert testimony. RB at 49. It is clear, however, that experts may testify based on their experience in their given field, including their knowledge of consumer perceptions, to claims that consumers might take away. See *Thompson Medical*, 104 F.T.C. at 790; see generally *Fed. R. Evid.* 702. Thus, Mazis's testimony regarding direct effects is valuable not as an expression of his personal opinion, but rather as expert opinion regarding his knowledge and experience of

## Initial Decision

consumer perceptions and claims that consumers would take away from the four corners of the advertising at issue.

Mazis testified that there are direct effects within the four corners of the ad that cause consumers to make inferences about the Ab Force and to take away from its ads certain implied claims. F. 158-62. Mazis stated "that even if you had never heard of an ab belt before, . . . you could see the ad and you could make inferences because there's certain implied claims in the ads." F. 158-59. Mazis identified as direct effects the appearance of trim, fit models and the depiction of the Ab Force belt itself shown visibly pulsating the abdominal muscles of the models. F. 161. According to Mazis, another influence that is within the four corners of the Ab Force ads is the name Ab Force. F. 162. Mazis testified that the name could have a double effect on consumers: "on the one hand, it applies force to your abs because of this stimulation, and you can also say it makes your abs a force. In other words it makes your abs noticeable, that they are -- really well developed." F. 162.

Mazis's testimony regarding consumer perceptions of the challenged advertising is relevant in determining the claims directly conveyed by the four corners of the ads. Mazis's expert testimony regarding consumer perceptions thus supports the conclusion that the Ab Force advertising made the claims that use of the Ab Force causes loss of inches, weight, and fat; causes well-defined abs; and is an effective alternative to regular exercise. However, as noted earlier, Mazis's opinion is not necessary to reach that determination.

**ii. Indirect Effects**

Mazis uses the term "indirect effects" to refer to the effects on consumers of previous exposure to ab belts through either infomercials, word-of-mouth, or retail packaging for other ab belts. F. 163. Mazis opines that it is through these indirect effects that the Ab Force television spots make implied claims that using Ab Force will result in well-defined abs and loss of inches around the waist. F. 164. Mazis also opined that consumers may perceive claims that use of the Ab Force results in weight loss and that the

Initial Decision

Ab Force is an effective substitute for regular exercise because consumers associate them with ab belt category beliefs. F. 164, 167.

Mazis's opinion is based on the psychological and consumer behavior theory of "categorization." F. 169. Categorization theory is generally accepted in the field of consumer behavior. F. 170. A leading proponent of the theory, Mita Sujon, asserted in a well-known peer-reviewed article that the "basic premise [of the categorization approach] is that people naturally divide the world of objects around them into categories enabling an efficient understanding and processing of the environment. . . . If a new stimulus can be categorized as an example of a previously defined category, then the effect associated with the category can be quickly retrieved and applied to the stimulus." F. 171.

Complaint Counsel argues that consumers, upon hearing the reference in the Ab Force commercials to "those other ab belt infomercials" would infer that the claims made in those other infomercials would apply to the Ab Force. CCB at 7-12. Mazis testified that four key elements in the Ab Force commercials would have an impact on consumers that would cause them to categorize the Ab Force specifically with the AbTronic, Ab Energizer, and Fast Abs products. F. 178. These four elements are: (1) references in Ab Force ads to the other ab belts, (2) the visual images of models with well-defined abs and slim bodies, (3) the physical appearance of the Ab Force product which is similar to the other ab belts, and (4) the similarity of the name Ab Force to the names of the other ab belts. F. 178.

Mazis considered only a limited number of materials and conducted no empirical research to support his opinions regarding the indirect effects of the Ab Force advertisements. F. 165, 168, 183, 188-92. Mazis's conclusions regarding indirect effects must be viewed in light of his limited analysis. Mazis reviewed and considered the Complaint and exhibits in this matter; transcripts and videotapes of the infomercials for AbTronic, Ab Energizer, and Fast Abs; and infomercial ranking reports for the AbTronic, Ab Energizer, and Fast Abs products. F. 165. Mazis did not know and could not determine what messages were being conveyed by

## Initial Decision

advertisements or packaging for other EMS ab products, by word-of-mouth communication, or what other print or radio advertisements were being disseminated. F. 166, 189. Indeed, Mazis admitted that when he referred to category beliefs, he was referring only to "ab belt category beliefs relative to those three products and only those three products [AbTronic, Ab Energizer, and Fast Abs]." F. 189. Mazis provided no evidence that those Ab Force ad viewers who happened to see the ads for AbTronic, Ab Energizer, and Fast Abs would retain or even comprehend that information. F. 184-88. Despite having no reliable information regarding exactly how frequently any one advertisement at issue had aired, and no information identifying the stations, days, or times those ads aired, Mazis stood by his belief that "many consumers would have been exposed to these ads." F. 166. This is not credible testimony supported by reliable evidence.

Respondents' marketing expert, Jacoby, testified that he was familiar with the categorization theory and with Sujjan's article. F. 173. Jacoby, however, did not agree with Mazis's application of the theory to this case. F. 173. In particular, Jacoby argued that categorization theory, as presented by Sujjan, relies on consumers having a preexisting category of beliefs. F. 175. Respondents argue that consumers might not have an ab belt category of beliefs and that even if they have such a category, it might be formed based upon devices other than the AbTronic, Ab Energizer, or Fast Abs. RB at 31-48.

Upon review of the record, there is no empirical evidence to determine what beliefs consumers would include in an ab belt category. Indeed, there is no reliable, demonstrated showing regarding whether consumers have an ab belt category of beliefs and, if so, what products would fall into the category. This would likely depend on a number of factors: when, what channels, and how often advertisements for other ab belts or EMS devices aired; whether the consumers had seen advertisements for other ab belts or EMS devices; whether the consumers remembered the claims from the other advertising; how similar the products were in appearance; and how similar the advertisements were in terms of claims, visual images, and statements. These indirect effects, if any, cannot be determined without more evidence than was

Initial Decision

provided by Complaint Counsel in this case. Thus, to the extent that Mazis relied upon categorization theory to support his conclusions, such analysis fails as a matter of proof.

**iii. Copy Test -- Methodology**

The reliability of the copy test designed and introduced by Mazis in this proceeding is examined next. In doing so, the Court notes that courts are not limited only to looking at a survey of prior purchasers asking why they purchased a product. See *FTC v. Figgie Int'l, Inc.*, 994 F. 2d 595, 605 (9th Cir. 1993); *FTC v. Security Rare Coin & Bullion Corp.*, 931 F. 2d 1312, 1316 (8th Cir. 1991). "The most convincing extrinsic evidence is a survey 'of what consumers thought upon reading the advertisement in questions,' but the Commission also relies on other forms of extrinsic evidence including consumer testimony, expert opinion, and copy tests of ads." *Kraft*, 970 F.2d at 318 (quoting *Thompson Medical*, 104 F.T.C. at 788-89). To constitute reliable and probative evidence, copy tests must be methodologically sound. *Stouffer*, 118 F.T.C. at 799; *Thompson Medical*, 104 F.T.C. at 790. The standard used to determine whether copy tests are methodologically sound is whether they "draw valid samples from the appropriate population, ask appropriate questions in ways that minimize bias, and analyze results correctly." *Thompson Medical*, 104 F.T.C. at 790; accord *Stouffer*, 118 F.T.C. at 799. In evaluating survey evidence, the Commission does not require that surveys be perfect methodologically, but that they be "reasonably reliable and probative." *Stouffer*, 118 F.T.C. at 799.

A copy test is an in-person survey in which people are shown an advertisement, and asked a number of questions in terms of their perceptions of the advertisement, which is sometimes referred to as the "take-away" from the advertisement. F. 194. The copy test designed by Mazis and implemented by U.S. Research, although flawed in certain respects, confirms that the Ab Force television commercials made the claims that use of the Ab Force causes loss of weight, inches, or fat; causes well-defined abdominal muscles; and is an effective alternative to regular exercise. As explained below, (1) the universe of participants was reasonably reliable and probative; (2) appropriate questions were

## Initial Decision

asked; (3) the control ad, although flawed, does not adversely impact the copy test results; and (4) the failure to control for preexisting beliefs was not critical.

First, the universe for participants in the copy test was limited to people who, in the last twelve months, had purchased a product or used a service for weight loss, muscle toning, or massage, and also in the last twelve months had purchased a product by responding to a direct response television ad. F. 209-10. Age and sex quotas were based upon a survey report in the *Journal of the American Medical Association* of persons trying to lose weight. F. 204. Respondents object to the survey population, arguing that it is overly broad because the purchase of any item via response to a direct response television ad was not sufficiently tailored to limit the universe to potential purchasers of the Ab Force. RB at 53-54. Respondents argue that "appropriate criteria should have excluded those respondents who had not purchased a product to help them lose weight, tone muscles, or massage their bodies from a toll-free number." RB at 55. Respondents do not, apparently, object to the age and sex quotas or exclusion of people who had not purchased a product or used a service for weight loss, muscle toning, or massage. See RB at 53. Complaint Counsel argues that for a claim take away survey, the universe of participants should be relatively broad and it would have been unnecessarily narrow to have excluded from the universe those people who had demonstrated an interest in weight loss, muscle toning, or massage and who had made purchases via direct response television of products other than in those three categories. CCRB at 29-30. While the universe for participants in the copy test could have been more narrowly tailored, as designed it is nevertheless reasonably reliable and probative. See *Stouffer*, 118 F.T.C. at 799.

Second, appropriate, unbiased questions were asked in the copy test. F. 231-54. The evidence shows that the copy test questionnaire proceeded from general, open-ended questions to more narrow, close-ended questions; used a filter question to ensure that responses to follow-up, close-ended questions would not be based upon random guessing; that such a tunneling approach is the best way to ask questions on a copy test; that the



Initial Decision

close-ended questions rotated the order in which the questions were read, thereby controlling for order bias, or yea-saying; and that all three possible answers to each question were read and shown to the participants before each question was asked. F. 231-54. As designed and implemented, Complaint Counsel has demonstrated that appropriate questions were asked in a manner that was proper, minimized bias, and produced reliable results. See Stouffer, 118 F.T.C. at 804-06.

Third, although a control of some kind is necessary for close-ended questions, the control may take the form of a control ad or a control question. *Thompson Medical*, 118 F.T.C. at 808-09. Moreover, "there is nothing in Commission precedent that requires the use of a control ad for open-ended questions." *Id.* at 808. The record shows that Mazis utilized both methods, a control ad and three control questions, in his copy test. F. 214-30, 239. The parties focused on the impact of the control ad.

The copy test utilized a control ad to compare to the test ad. F. 214-30. The test ad was a 60 second Ab Force spot that was the most frequently aired of the four commercials produced for Respondents. F. 214. The control ad was created by Mazis and consisted of a 120 second Ab Force ad that he pared down to 60 seconds by eliminating all references to other ab belts and ab belt infomercials, eliminating the stock images and eliminating some, but not all, images of models wearing the Ab Force. F. 214, 217. The control ad, however, was ineffective because it did not eliminate the very elements which Mazis, himself, indicated were direct effects that convey the health, weight loss, fitness, and exercise benefits of using the Ab Force. F. 218. Specifically, the control ad includes three images of the female and male model with well-defined abs, wearing the Ab Force, and experiencing muscle contractions. F. 219. In addition, in the control ad, the name Ab Force is stated six times. F. 220. Study participants who saw the control advertisement took away the same claims as those who saw the test advertisement, albeit in smaller numbers. F. 255-69. Mazis admits that the results for the control ad "are relatively high numbers for a control ad" and attributes these numbers to preexisting beliefs about ab belts. F. 221. The higher numbers, however, could also result from the direct effects which remained

## Initial Decision

in the control ad. Regardless of the cause, the flaws in the control ad inflate the control ad numbers thereby reducing the net take away results. See F. 266-69.

Fourth, a central issue in this case has been the impact of consumers' preexisting beliefs. Respondents argue that the copy test failed to adequately control for the influence of any preexisting beliefs held by study participants; that a reliable survey must control for background "noise," including preexisting beliefs; that Mazis admitted his controls were ineffective, but improperly dismissed the failure to control as not relevant; that Mazis nevertheless decided to control for one source of preexisting beliefs while not controlling for others; and that the "relatively high" number of control participants who detected misleading claims confirms that the effect of background noise on the results was substantial. RB at 57-65. Complaint Counsel responds that Mazis properly controlled for preexisting beliefs of the survey participants. CCRB at 32-36.

The extent of advertisers' liability under the FTC Act for preexisting beliefs has been discussed in case law only in the context of whether copy tests should control for preexisting beliefs. E.g., *Stouffer*, 118 F.T.C. at 809-11; *Kraft*, 114 F.T.C. at 131. For example, in *Kraft*, the Commission rejected as unreliable a copy test which failed "to correct for preexisting or inherent survey bias" where there was a suggestion that the response rate may have been attributable to consumers' prior exposure to other *Kraft* ads. *Kraft*, 114 F.T.C. at 131 n.19. Discussing this section of *Kraft*, the Commission in *Stouffer* stated that "the [*Kraft*] case does not hold that consumer surveys must invariably control for preexisting beliefs. Instead, *Kraft* teaches that the failure of a consumer survey to control for preexisting beliefs about the alleged advertising claim introduces a potential for bias, and indeed that this may be a critical defect." *Stouffer*, 118 F.T.C. at 810 (emphasis in original). The footnote to this section of *Stouffer* states: "indeed, it is established that respondents may be held liable for dissemination of ads that capitalize on preexisting consumer beliefs." *Id.* at 810 n.31 (citing *Simeon Mgmt. Corp. v. FTC*, 579 F.2d 1137, 1146 (9th Cir. 1978)). The Commission in *Stouffer*, based on this analysis of *Kraft*, refused to reject a copy

Initial Decision

test which failed to control for preexisting beliefs that the sodium content of Lean Cuisine entrees was low where the evidence indicated that, to the extent consumers had a preexisting belief regarding the entrees, it was that the sodium content was high, not low. *Id.* at 810-11 ("there must be evidence of preexisting bias to find that failure to control for such bias is a critical defect.").

Complaint Counsel relies heavily on the above-quoted footnote 31 in *Stouffer* which cites the *Simeon* case. In *Simeon*, the Ninth Circuit stated "that the belief [that injections have been determined by a proper government agency to be safe and effective] is attributable in part to factors other than the advertisement itself does not preclude the advertisement from being deceptive." *Simeon*, 579 F.2d at 1146 (citing *cf. Brite Mfg. Co. v. FTC*, 347 F.2d 477 (D.C. Cir. 1965)). In *Brite*, the D.C. Circuit held that the Commission properly took official notice of specific consumer preferences where the respondents made no attempt to rebut those perceptions during the hearing, stating that the FTC was "entitled to rely on established general facts within the area of its expertise, subject, of course, to [respondent's] right to rebut." *Brite*, 347 F.2d at 478. Neither of these cases supports the assertion in *Stouffer* that "respondents may be held liable for dissemination of ads that capitalize on preexisting consumer beliefs." *Stouffer*, 118 F.T.C. at 810 n.31.

While *Kraft* stands for the proposition that a copy test may be rejected for failure to control for preexisting beliefs (even where those beliefs were created by the respondent itself) and *Stouffer* stands for the proposition that a copy test will not be rejected for failure to control for a preexisting belief where there is no evidence that such a belief effected the results, neither case stands for the legal theory that advertisers may be found liable for capitalizing on preexisting consumer beliefs. This issue was addressed in the Lanham Act case of *Johnson & Johnson \* Merck Consumer Pharmaceuticals Co. v. Smithkline Beecham Corp.*, 960 F.2d 294 (2d Cir. 1992). In *J&J\*Merck*, the Second Circuit states that "*J&J\*Merck* argues that [the advertisement] purposefully taps into a preexisting body of public misinformation [that the ingestion of aluminum causes Alzheimer's disease] in order to communicate the false and

## Initial Decision

misleading message that aluminum-based antacids are harmful. The gravamen of J&J\*Merck's claim is that advertisers may be liable for the knowing exploitation of public misperception." *Id.* at 297. The Second Circuit did not "reject nor embrace" this "novel theory of Lanham Act liability." *Id.* In this case, in addition to the weak legal support, there is no factual support for imposition of liability based upon capitalizing on preexisting consumer beliefs.

The factual record in this case does not support imposing liability on Respondents based upon the preexisting beliefs of consumers because there is insufficient empirical evidence of the existence, extent, or impact of those preexisting beliefs. See F. 157-269. However, the case law does not require rejecting the entirety of the conclusions reached in the copy test merely for failure to account for preexisting beliefs. The copy test is valid even though, as explained above, the control advertisement was flawed. Therefore, despite flaws in Mazis's control ad, the copy test is sufficiently methodologically sound as to be reasonably reliable and probative of the issues before the Court.

**iv. Copy Test -- Results**

Mazis's copy test results were reported in total percentages, and then in terms of statistical significance. F. 255. Respondents assert that the net difference between the numbers of test and control group participants who perceived misleading claims is the appropriate measure to be examined; and that Mazis's improper decision to drop eighty one study participants substantially affects the results reported. RB at 65-69. Complaint Counsel argues that Mazis properly excluded from the survey analysis eighty one respondents who could not remember the name of the product after viewing the ab force spots twice. CCRB at 36-39. Because a primary goal of copy testing is to define a universe of likely purchasers of the tested product, it is not unreasonable to conclude that people who could not recall the product name should not be a part of the survey universe. Unlike other screening criteria that were a part of a separate screening questionnaire, it was not possible to screen these people out until they had actually viewed the commercial. In addition, even when

Initial Decision

the results of the copy test are viewed in terms of net difference, as Respondents prefer, the results support the conclusion that the ads, in fact, made the claims that use of the Ab Force causes loss of weight, inches, or fat; causes well-defined abdominal muscles; and is an effective alternative to regular exercise.

In so holding, the Court notes that there is no absolute minimum number of copy test respondents who must report taking away a specific message from an advertisement before that message is deemed communicated. The Commission's opinion in Thompson Medical provides a level of close-ended responses deemed sufficient to show that a claim was communicated by an advertisement. There, the Commission relied on percentages, after the control question responses had been deducted, of sixteen to eighteen percent of the respondents answering that they took the claim to conclude that the tested ad "did, in fact, cause average viewers to believe the [claim]." Thompson Medical, 104 F.T.C. at 805-06 (22.2% minus 6.3% or 4.8%). Other FTC cases suggest that the Commission would be justified in considering levels of ten percent net take away sufficient. For example, in Firestone, where Firestone's own consumer survey revealed that 15.3% perceived "Safe Tire" to mean every tire was "absolutely safe" or "absolutely free from defects," the court stated that it was "hard to overturn the deception findings of the Commission if the ad thus misled 15% (or 10%) of the buying public." Firestone Tire & Rubber Co. v. FTC, 481 F.2d 246, 249 (6th Cir. 1973); see also Stouffer, 118 F.T.C. at 805 (where the Commission noted that one of Stouffer's own experts "testified that often a researcher must rely on open-ended responses in the magnitude of 8 percent to 10 percent as being meaningful").

Moreover, numerous decisions in Lanham Act cases support the proposition that a result of between ten percent and fifteen percent is sufficient to support an allegation of trademark infringement. E.g., Mutual of Omaha Ins. Co. v. Novak, 836 F.2d 397, 400 (8th Cir. 1987) (10%); Humble Oil & Refining Co. v. American Oil Co., 405 F.2d 803, 817 (8th Cir. 1969) (11%); James Burrough Ltd. v. Sign of the Beefeater, Inc., 540 F.2d 266, 279 n.23 (7th Cir. 1976) (referring to prior case showing 11%); Goya Foods, Inc. v. Condal Distributions, Inc., 732 F. Supp. 453, 456-

## Initial Decision

57 (S.D.N.Y. 1990) (9%); compare *Sara Lee Corp. v. Kayser-Roth Corp.*, 81 F.3d 455, 467 n.15 (4th Cir. 1996) ("We may infer from case law that survey evidence clearly favors the defendant when it demonstrates a level of confusion much below ten percent.").

The copy test results, despite the previously noted flaws, support the conclusion that the Ab Force ads conveyed the claims that use of the Ab Force causes loss of weight, inches, or fat; causes well-defined abdominal muscles; and is an effective alternative to regular exercise. To the open-ended question, "what does the Ab Force commercial say, show, or imply about Ab Force?" over twenty two percent (22.3%) of the test ad respondents and nearly twelve percent (11.9%) of the control ad respondents said that the advertisement claimed that using the Ab Force results in well-defined abdominal muscles, in loss of weight, or inches, or in an improved physique. F. 257. As discussed above, results of open-ended questions may be reliable without subtracting the results from a control ad or control question. *Stouffer*, 118 F.T.C. at 808.

As to a claim about weight loss, 43.0% of the test ad respondents and 28.1% of the control ad respondents agreed that the ad they saw communicated that the Ab Force "causes users to lose weight." F. 258, 263. Over half (58.1%) of the test ad respondents and over two-fifths (42.4%) of the control ad respondents perceived a claim that the Ab Force "causes users to lose inches around the waist" F. 259, 263. As to whether "using Ab Force removes fat deposits," approximately one-fifth of each group of respondents (22.9% test, 19.0% control) agreed that the commercial they saw made the claim. F. 260, 263. As to claims about fitness and exercise, nearly two-thirds (65.4%) of the test ad respondents and almost half (48.1%) of the control ad respondents agreed that the ad they saw communicated that "using the Ab Force results in well-defined abdominal muscles." F. 261, 263. Nearly forty percent (39.1%) of the test ad respondents and more than a quarter (28.6%) of the control ad respondents agreed with the claim that "using Ab Force is an effective alternative to regular exercise." F. 262, 263.

Initial Decision

The copy test also included close-ended control questions regarding whether the ads conveyed claims regarding stomach ulcers, nausea, or lower blood pressure. F. 239. The results of these control questions showed a maximum result of five percent. F. 263, 267-69. When using a control question, the percentage of participants who responded affirmatively to the control question is deducted from the percentage of participants who responded affirmatively to the tested claim. *Stouffer*, 118 F.T.C. at 806. Here, if the maximum percent of participants who responded affirmatively to the control questions is subtracted from the percent responding affirmatively to the tested ad, then the claims at issue were found by 60.4% (well-defined abdominal muscles); 53.1% (lose inches around the waist); 38% (lose weight); 34.1% (alternative to exercise) and 17.9% (removes fat deposits). F. 264.

Thus, both the open-ended and close-ended questions contained in the copy test demonstrate that a significant number of participants took away from the test ad the claims that use of the Ab Force causes loss of weight, inches, or fat; causes well-defined abdominal muscles; and is an effective alternative to regular exercise.

## **2. Whether the Claims at Issue Are False or Misleading**

Section 12 of the FTC Act prohibits the dissemination of any false advertisement that is likely to induce the purchase of food, drugs, devices, or cosmetics. 15 U.S.C. § 52. A "false advertisement" is any advertisement that is "misleading in a material respect." 15 U.S.C. § 55; see also *Pantron*, 33 F.3d at 1095. There are "two theories on which the government can . . . rely in section 12 cases involving objective product claims:" (1) the "falsity" theory under which the government must "'carry the burden of proving that the express or implied message conveyed by the ad is false'" or (2) the "so-called 'reasonable basis' theory" under which "the government must 'show that the advertiser lacked a reasonable basis for asserting that the message was true.'" *Id.* at 1096 (quoting *Thompson Medical*, 104 F.T.C. at 818-19).

## Initial Decision

Under either the falsity theory or the reasonable basis theory, Complaint Counsel has established that the alleged claims are false or misleading. The parties stipulated that use of the Ab Force does not cause loss of weight, inches, or fat; does not cause well-defined abdominal muscles; and is not an effective alternative to regular exercise. F. 270-72; RRPFF at 154. The parties further stipulated that Respondents did not possess and rely upon substantiation for the alleged claims that use of the Ab Force causes loss of weight, inches, or fat; causes well-defined abdominal muscles; and is an effective alternative to regular exercise. F. 273; RRPFF at 154. Therefore, any claims that the use of the Ab Force causes consumers to lose weight, fat, and inches; causes well-defined abdominal muscles; and is a substitute for regular exercise are patently false and misleading.

**3. Whether the Claims at Issue Are Material to Consumers**

A "material claim is one that 'involves information that is important to consumers and, hence, likely to affect their choice of, or conduct regarding, a product.'" *Novartis Corp.*, 223 F.3d at 786 (quoting *Cliffdale Assocs.*, 103 F.T.C. at 165); see *Kraft*, 970 F.2d at 322. The Commission may apply a presumption of materiality to three types of claims: (1) express claims; (2) implied claims where there is evidence that the seller intended to make the claim; and (3) claims that significantly involve health, safety, or other areas with which reasonable consumers would be concerned. *Novartis*, 223 F.3d at 786; *Kraft*, 970 F.2d at 322-23; *Thompson Medical*, 104 F.T.C. at 816-17. In *Novartis*, the D.C. Circuit affirmed the Commission's application of a presumption of materiality based on its finding that the implied claim was intentional and involved both a health matter and the product's purpose and efficacy. *Novartis*, 223 F.3d at 786-87.

The claims implied by the Ab Force advertising were material. Claims that use of the Ab Force causes loss of weight, inches, or fat; causes well-defined abdominal muscles; and is an effective alternative to regular exercise directly involve the purpose and effects of using the product. F. 274-75. Such claims involve information that is important to consumers and, hence, likely to affect their choice of, or conduct regarding, a product. If



Initial Decision

unsubstantiated or false, these claims would likely mislead reasonable consumers considering such a purchase. Moreover, there is evidence that Respondent intended to make the implied health, weight loss, fitness, and exercise claims which further supports the finding of materiality. See Section II(B)(1)(e), *supra*. Therefore, based on the record as developed at trial, the claims that use of the Ab Force causes loss of weight, inches, or fat; causes well-defined abdominal muscles; and is an effective alternative to regular exercise are found to be material to consumers.

### **C. Remedy**

#### **1. Joint and Individual Liability**

Corporate respondents acting in concert to further a common enterprise are each liable for the acts and practices of the others in furtherance of the enterprise. See *Sunshine Art Studios, Inc. v. FTC*, 481 F.2d 1171, 1175 (1st Cir. 1973) (treating all defendants as single economic entity where there was common control); *Waltham Precision Instrument Co. v. FTC*, 327 F.2d 427, 431 (7th Cir. 1964) (treating all defendants as single economic entity where there was common control); *Delaware Watch Co. v. FTC*, 332 F.2d 745, 746 (2d Cir. 1964) (common enterprise found where individuals were transacting an integrated business through a maze of interrelated companies); *Zale Corp. and Corrigan-Republic, Inc. v. FTC*, 473 F.2d 1317, 1320 (5th Cir. 1973) (sharing office space and offices). Respondent Ajit Khubani is the president, chief executive officer, chairman of the board, and sole owner of Telebrands. F. 10. Khubani is also the sole member of TV Savings. F. 10. Telebrands and TV Savings share office space. F. 8. Individually or in concert with his officers and employees, Khubani formulates, directs, or controls the policies, acts, or practices of Telebrands and TV Savings. F. 14. Khubani was appointed by Telebrands as the "Program Manager" pursuant to the Service Agreement dated January 22, 2002 between Telebrands and TV Savings and was also TV Savings' representative under the Service Agreement. F. 15. Together, Respondents have operated as a common enterprise to label,

## Initial Decision

advertise, offer for sale, sell, and distribute the Ab Force device. Thus, the evidence establishes that Respondents Telebrands, TV Savings, and Khubani were acting in concert to further a common enterprise and that they jointly and collectively violated Sections 5 and 12 of the FTC Act.

To obtain a cease and desist order against an individual, Complaint Counsel must prove violations of the FTC Act by the corporation and that the individual either directly participated in the acts at issue or had some measure of control over those acts. *FTC v. Standard Educ. Soc'y*, 302 U.S. 112, 119-20 (1937); *National Housewares, Inc.*, 90 F.T.C. 572, 598 (1977). As stated above, the evidence shows that individually or in concert with his officers and employees, Respondent Khubani had authority to and did control the policies, acts, or practices of Respondents Telebrands and TV Savings. F. 14. As the program manager appointed by Telebrands and as TV Savings' representative under the Service Agreement, Khubani represents both entities with regard to the responsibilities and duties of each under the Service Agreement. F. 15. Khubani was ultimately responsible for overseeing the marketing and creative design of the challenged Ab Force advertising and promotional campaign; was primarily responsible for the creation and development of the scripts for the Ab Force television and radio advertising and the text for the internet and email advertising of the Ab Force product; set the pricing strategy for the Ab Force and decided when the Ab Force would no longer be marketed or sold. F. 16. Therefore, Respondent Khubani is found to be individually and jointly liable with TV Savings and Telebrands for violations of Sections 5 and 12 of the FTC Act. Having addressed the issue of liability, the Court next considers the appropriateness of the relief proposed in the Complaint.

## **2. Fencing In Provisions**

Included in the relief sought in the Complaint is a request to impose broad "fencing in" relief including, among other provisions, a performance bond and substantiation prior to advertising "any other EMS device, or any food, drug, dietary supplement, device, or any other product, service, or program."

Initial Decision

Complaint at 16-17 (proposed order); CCPFF at 118. As explained below, portions of the relief contemplated by the proposed remedy are overly broad and unsupported by law. For instance, Complaint Counsel seeks the imposition of a performance bond as part of the proposed remedy. Complaint at 16-17 (proposed Order). However, Complaint Counsel has not cited, nor has the Court found, any case law which would support the imposition of such a bond as a remedy in a litigated Part III matter. The fact that the Commission has previously accepted consent orders with a performance bond in Part III matters does not provide sufficient legal foundation to impose such a bond in this case. "The circumstances surrounding . . . negotiated [consent agreements] are so different that they cannot be persuasively cited in a litigation context." *United States v. E.I. du Pont de Nemours & Co.*, 366 U.S. 316, 331 n.12 (1961). Accordingly, no performance bond will be ordered.

Rather, the Order entered by the Court restricts Respondents from making any representations regarding the production, promotion, sale, and distribution of Ab Force and any other EMS device, or any device, product, service, or program pertaining to the efficacy of or pertaining to health, weight loss, fitness, and exercise, unless Respondents can substantiate such representations by competent and scientific evidence. Order, Section IV, *infra*.

In so ordering, the Court notes that "the Commission is not limited to prohibiting the illegal practice in the precise form in which it is found to have existed in the past.' Having been caught violating the Act, respondents 'must expect some fencing in.'" *FTC v. Colgate-Palmolive Co.*, 380 U.S. 374, 395 (1965) (quoting *FTC v. Ruberoid Co.*, 343 U.S. 470, 473 (1952) and *FTC v. Nat'l Lead Co.*, 352 U.S. 419, 431 (1957)); see also *Jacob Siegel*, 327 U.S. at 611-12. The Supreme Court held in *Jacob Siegel* that the remedy selected must have a "reasonable relation to the unlawful practices found to exist." *Jacob Siegel*, 327 U.S. at 613; see also *Colgate-Palmolive*, 380 U.S. at 394. The Supreme Court has cautioned, however, that an order must be sufficiently clear and precise to be understood by the violator and "as specific as the circumstances will permit." *Colgate-Palmolive*, 380 U.S. at 392-

## Initial Decision

93; see also *American Home*, 695 F.2d at 705. Moreover, the "propriety of a broad order depends upon the specific circumstances of the case." *Colgate-Palmolive*, 380 U.S. at 394.

In determining whether a broad fencing in order bears a "reasonable relationship" to a violation of the Act, factors to be considered include: the deliberateness and seriousness of the violation; the degree of transferability of the violation to other products; and any history of prior violations. *Kraft*, 970 F.2d at 326; *Sears, Roebuck and Co. v. FTC*, 676 F.2d 385, 392 (9th Cir. 1982); *American Home*, 695 F.2d at 706. "The weight given a particular factor or element will vary. The more egregious the facts with respect to a particular element, the less important it is that another negative factor be present. In the final analysis, we look to the circumstances as a whole and not to the presence or absence of any single factor." *Sears*, 676 F.2d at 392; see also *Kraft*, 970 F.2d at 327.

A violation is serious and deliberate where it involves "an expensive, nationwide campaign with highly effective results." *Kraft*, 970 F.2d at 326. The Ab Force advertising campaign constitutes a serious violation because the deceptive claims were disseminated in numerous ads and through multiple media (television, print, radio, internet, and email). F. 47, 49-51, 61. Respondents spent over four million dollars to disseminate the challenged ads nationwide. F. 52. The Ab Force television spots appeared more than ten thousand times on cable, satellite, and broadcast television outlets in major national markets. F. 44-51. Respondents sold approximately 747,000 units of the Ab Force and gross sales, including accessories, exceeded nineteen million dollars. F. 41-42. The duration, number of executions, and multi-million dollar cost of the campaign, as well as the total sales and revenues, all constitute significant evidence of the effectiveness of the advertisements and, thus, the seriousness of the violations. Moreover, the evidence regarding Respondents' intent (see Section III(B)(1)(a)(iii), *supra*) as well as the fact that Khubani is a sophisticated and experienced marketer (see F. 12-13, 22) establish that the claims were made deliberately and purposefully.

Initial Decision

A violation is transferrable where other products could be sold utilizing similar techniques. *Colgate-Palmolive Co.*, 380 U.S. at 394-95; *Sears*, 676 F.2d at 392. The Ab Force advertisements failed to expressly identify the purpose or effects of using the Ab Force but rather strongly implied that use of the Ab Force product would confer health, weight loss, fitness, or exercise benefits. See F. 65-146. The health, weight loss, fitness, or exercise benefits of using a device, product, service, or program cannot readily be determined by consumers from an advertisement and therefore consumers must rely on the representations of the advertiser. Implying these unseen benefits is an advertising practice that is readily transferrable to advertising for other devices, products, services, or programs. Moreover, the fact that Respondents have the ability to provide the financing necessary to perform media management services, credit card processing, customer response services, customs clearance, accounting, and bookkeeping, and act as an importer of record (F. 6); the fact that Respondents have the financial means to spend millions of dollars on effective, nationwide advertising (F. 41-52); and the fact that Respondents have promoted and sold hundreds of products (F. 22) is sufficient for the Court to determine, under the Kraft rationale, that Respondents' advertising techniques and practices are readily transferrable to other products.

Complaint Counsel argues that Respondents have a history of prior violations based on "four previous actions" taken by the FTC against Telebrands. CCRB at 46. This argument is based upon three consent agreements between Telebrands and the FTC and an additional modification of one of the consent agreements. CCRB at 46. Complaint Counsel failed to enter any of these consent agreements into evidence. See RRPFF at 155-56. Moreover, it is the Court's understanding that none of the consent agreements involved any finding of liability on the part of any of the respondents (see RRB at 46) and therefore they cannot be utilized to form the basis for imposing a broad fencing in order in this case. However, a defendant need not have a history of prior violations in order for a broad fencing in order to be imposed. See, e.g., *Kraft*, 970 F.2d at 327.

## Initial Decision

Here, a broad fencing in order is appropriate under the standards in Kraft and Sears given the deliberateness and seriousness of the violations and the ease with which the unlawful conduct can be transferred to other products. Therefore, the fencing in relief in Section IV of the Order extends the prohibitions of the Order beyond the Ab Force device and other EMS devices to any device, product, service, or program promoting the efficacy of, or pertaining to health, weight loss, fitness, or exercise benefits. Courts have repeatedly approved orders that cover multiple products, despite the fact that the violations found involved only a single product. Sears, 676 F.2d at 392; see also Bristol-Myers Co. v. FTC, 738 F.2d 554, 563-64 (2d Cir. 1984); American Home, 695 F.2d at 704-05. Indeed, the Supreme Court has enforced a Commission order which applied to all products produced by the respondents. Colgate-Palmolive, 380 U.S. at 394.

The Court, looking to the circumstances as a whole, has determined that a fencing in order is required and bears a reasonable relationship to Respondents' violations of the Act found to exist. As such, it is necessary to "close all roads to the prohibited goal, so that (the FTC's) order may not be by-passed with impunity." Litton Industries, Inc. v. FTC, 676 F.2d 364, 370 (9th Cir. 1982) (quoting Ruberoid, 347 U.S. at 473). The accompanying Order is narrowly tailored and reasonably related to the violation of law found to exist.

**IV. SUMMARY OF CONCLUSIONS OF LAW**

1. Pursuant to Section 5 and 12 of the FTC Act, 15 U.S.C. § § 45, 52, the Commission has jurisdiction over the subject matter of this proceeding and over Respondents Telebrands Corporation, TV Savings, L.L.C., and Ajit Khubani.
2. Individually or in concert with his officers and employees, Khubani formulates, directs, or controls the policies, acts, and practices of Telebrands and TV Savings.
3. The Ab Force ab belt, an EMS device which uses electronic stimulation of the muscles, is a device within the meaning of Section 15 of the FTC Act which defines "device" as including

Initial Decision

"an instrument, apparatus, implement, machine, [or] contrivance . . . which is . . . intended to affect the structure or any function of the body of man." 15 U.S.C. § 55(d).

4. By engaging in a nationwide advertising campaign to offer for sale and sell the Ab Force device, Respondents were engaged in and affected commerce, as "commerce" is defined in Section 4 of the FTC Act. 15 U.S.C. § 44.

5. Pursuant to Rule 3.51(c)(3) and 5 U.S.C. § 556(d), the findings of fact and conclusions of law in this Initial Decision are supported by reliable, probative, and substantial evidence.

6. The issues in this case are adjudicated under the preponderance of evidence standard.

7. Employing a facial analysis of the Ab Force advertising, there are no express statements which support the claims that using the Ab Force causes loss of weight, inches, or fat; causes well-defined abdominal muscles; and is an effective alternative to regular exercise.

8. The overall net impression of the product name, visual images, and statements in the four corners of the Ab Force advertising in addition to the surrounding circumstances, is conspicuous, self-evident, and reasonably clear so that the Court can conclude with confidence that the advertisements convey the claims that the use of the Ab Force by consumers causes loss of weight, inches, and fat; causes well-defined abs; and is an effective alternative to regular exercise.

9. Mazis's expert testimony regarding consumer perceptions supports the conclusion that the Ab Force advertising made the claims that use of the Ab Force causes loss of inches, weight, and fat; causes well-defined abs; and is an effective alternative to regular exercise.

10. There is no empirical evidence to support what beliefs consumers would include in an ab belt category. Thus, to the extent Complaint Counsel relies upon categorization theory or indirect effects to support the allegations, such analysis fails as a matter of proof.

## Initial Decision

11. Despite flaws in the control ad methodology, the copy test conducted by Complaint Counsel's expert is otherwise valid and is sufficiently sound so as to be reasonably reliable and probative of the issues before the Court.

12. The copy test results support the conclusion that the Ab Force ads convey the claims that use of the Ab Force causes loss of weight, inches, or fat; causes well-defined abdominal muscles; and is an effective alternative to regular exercise.

13. The claims asserting that use of the Ab Force causes consumers to lose weight, fat, and inches; causes well-defined abdominal muscles; and is an effective alternative to regular exercise are false or misleading pursuant to Section 12 of the FTC Act. 15 U.S.C. § 52.

14. The claims asserting that use of the Ab Force causes loss of weight, inches, or fat; causes well-defined abdominal muscles; and is an effective alternative to regular exercise are material to consumers.

15. Corporate respondents acting in concert to further a common enterprise are each liable for the acts and practices of the others in furtherance of the enterprise.

16. Respondents Telebrands Corporation, TV Savings, L.L.C., and Ajit Khubani have operated as a common enterprise to label, advertise, offer for sale, sell, and distribute the Ab Force device. As such, they jointly and collectively violated Sections 5 and 12 of the FTC Act.

17. Respondent Ajit Khubani is individually liable for violations of Sections 5 and 12 of the FTC Act.

18. Complaint Counsel has met its burden of proof in establishing Respondents' liability for the violations of the FTC Act charged in the Complaint.

19. "Fencing in" relief is appropriate where, after examining circumstances of the case as a whole, it bears a "reasonable relationship" to a violation of the FTC Act.



Initial Decision

20. Complaint Counsel has not demonstrated that imposition of a performance bond is an appropriate fencing in remedy in a litigated Part III matter.

21. Previous consent agreements entered into with named respondents to a proceeding do not constitute a "history of prior violations" and thus cannot form the basis for imposing broad fencing in relief, particularly where there is no evidence that any of the consent agreements involved a finding of liability against Respondents.

22. Relief designed to remedy Respondents' unlawful activities and to require Respondents to cease and desist from certain activities is appropriate.

23. The Order entered is necessary and appropriate to remedy the violations of law found to exist.

**ORDER:**

**ORDER**

**I.**

**IT IS ORDERED** that, for purposes of this Order, the following definitions shall apply:

A. "Commerce" shall mean commerce as defined in Section 4 of the Federal Trade Commission Act, 15 U.S.C. § 44.

B. "Competent and reliable scientific evidence" shall mean tests, analyses, research, studies, or other evidence based on the expertise of professionals in the relevant area, that have been conducted and evaluated in an objective manner by persons qualified to do so, using procedures generally accepted in the profession to yield accurate and reliable results.

C. "Electronic muscle stimulation device" or "EMS device" shall mean any appliance or machine, or any

## Initial Decision

accessories thereof, used to stimulate the muscles of the human body with electricity.

D. "Device" shall mean any "device" as that term is defined in Section 15 of the Federal Trade Commission Act, 15 U.S.C. § 55.

E. Unless otherwise specified, "Respondents" shall mean Telebrands (a corporation); TV Savings (a limited liability company), their successors and assigns and their officers; Ajit Khubani, individually and as president of Telebrands and sole member of TV Savings; and each of the above's agents, representatives, and employees.

**II.**

**IT IS FURTHER ORDERED** that Respondents, directly or through any corporation, subsidiary, division, or other entity, in connection with the manufacturing, labeling, advertising, promotion, offering for sale, sale, or distribution of the Ab Force device or any substantially similar device in or affecting commerce, shall not represent, in any manner, including through the use of pictures, demonstrations, testimonials, or endorsements, expressly or by implication, that:

A. any such device causes or promotes loss of weight, inches, or fat;

B. any such device causes or promotes well-defined abdominal muscles;

C. use of any such device for any period of time is an effective alternative to regular exercise; or

D. any such device makes a material contribution to any system, program, or plan that produces the results referenced in Subparts A-C of this Part.

Initial Decision

**III.**

**IT IS FURTHER ORDERED** that Respondents, directly or through any corporation, subsidiary, division, or other entity, in connection with the manufacturing, labeling, advertising, promotion, offering for sale, sale, or distribution of any EMS device, shall not make any misrepresentation, in any manner, including through the use of pictures, demonstrations, testimonials, or endorsements, expressly or by implication, that:

- A. any such device causes or promotes loss of weight, inches, or fat;
- B. any such device causes or promotes well-defined abdominal muscles;
- C. use of any such device for any period of time is an effective alternative to regular exercise; or
- D. any such device makes a material contribution to any system, program, or plan that produces the results referenced in Subparts A-C of this Part.

**IV.**

**IT IS FURTHER ORDERED** that Respondents, directly or through any corporation, subsidiary, division, or other entity, in connection with the manufacturing, labeling, advertising, promotion, offering for sale, sale, or distribution of Ab Force, any other EMS device, or any device, product, service, or program promoting the efficacy of or pertaining to health, weight loss, fitness, or exercise benefits shall not make any representation, in any manner, expressly or by implication, about weight, inch, or fat loss; muscle definition; exercise benefits; or the health benefits, safety, or efficacy of any such product, service, or program, unless, at the time the representation is made, Respondents possess and rely upon competent and reliable scientific evidence that substantiates the representation.

Initial Decision

**V.**

Nothing in this Order shall prohibit Respondents from making any representation for any device that is specifically permitted in labeling for that device under any premarket approval application or premarket notification approved or cleared by the Food and Drug Administration.

**VI.**

**IT IS FURTHER ORDERED** that Respondents Telebrands and TV Savings, and their successors and assigns, and Respondent Khubani shall, for five years after the last date of dissemination of any representation covered by this Order, maintain and upon request make available to the Federal Trade Commission for inspection and copying:

A. all advertisements and promotional materials containing the representation;

B. all materials that were relied upon in disseminating the representation; and

C. all tests, reports, studies, surveys, demonstrations, or other evidence in their possession or control that contradict, qualify, or call into question the representation, or the basis relied upon for the representation, including complaints and other communications with consumers or with governmental or consumer protection organizations.

**VII.**

**IT IS FURTHER ORDERED** that Respondents Telebrands and TV Savings, and their successors and assigns, and Respondent Khubani shall deliver a copy of this Order to all current and future principals, officers, directors, and managers, and to all current and future employees, agents, and representatives having responsibilities with respect to the subject matter of this Order, and shall secure from each such person a signed and dated

Initial Decision

statement acknowledging receipt of the Order. Respondents shall deliver this Order to current personnel within thirty days after the date of service of this Order, and to future personnel within thirty days after the person assumes such position or responsibilities.

**VIII.**

**IT IS FURTHER ORDERED** that Respondents Telebrands and TV Savings and their successors and assigns shall notify the Commission at least thirty days prior to any change in the corporation or limited liability company that may affect compliance obligations arising under this Order, including but not limited to a dissolution, assignment, sale, merger, or other action that would result in the emergence of a successor corporation; the creation or dissolution of a subsidiary, parent, or affiliate that engages in any acts or practices subject to this Order; the proposed filing of a bankruptcy petition; or a change in the corporate name or address. Provided, however, that, with respect to any proposed change in the corporation about which Respondents learn less than thirty days prior to the date such action is to take place, Respondents shall notify the Commission as soon as is practicable after obtaining such knowledge. All notices required by this Part shall be sent by certified mail to the Associate Director, Division of Enforcement, Bureau of Consumer Protection, Federal Trade Commission, Washington, D.C. 20580.

**IX.**

**IT IS FURTHER ORDERED** that Respondent Khubani shall notify the Commission of the discontinuance of his current business or employment or of his affiliation with any new business or employment. The notice shall include Respondent Khubani's new business address and phone number and a description of the nature of the business or employment and his duties and responsibilities. All notices required by this Part shall be sent by certified mail to the Associate Director, Division of Enforcement, Bureau of Consumer Protection, Federal Trade Commission, Washington, D.C. 20580.

Initial Decision

**X.**

**IT IS FURTHER ORDERED** that Respondents Telebrands and TV Savings, and their successors and assigns, and Respondent Khubani shall, within sixty days after the date of service of this Order, and at such other times as the Federal Trade Commission may require, file with the Commission a report, in writing, setting forth in detail the manner and form in which they have complied with this Order.

**XI.**

**IT IS FURTHER ORDERED** that this Order will terminate twenty years from the date of its issuance, or twenty years from the most recent date that the United States or the Federal Trade Commission files a complaint (with or without an accompanying consent decree) in federal court alleging any violation of the Order, whichever comes later; provided, however, that the filing of such a complaint will not affect the duration of:

- A. any Part in this Order that terminates in less than twenty years;
- B. this Order's application to any Respondent that is not named as a defendant in such complaint; and
- C. this Order if such complaint is filed after the Order has terminated under this Part.

Provided, further, that if such complaint is dismissed or a federal court rules that the Respondent did not violate any provision of the Order, and the dismissal or ruling is either not appealed or not upheld on appeal, then the Order will terminate according to this Part as though the complaint had never been filed, except that the Order will not terminate between the date such complaint is filed and the later of the deadline for appealing such dismissal or ruling and the date such dismissal or ruling is upheld on appeal.

Complaint

IN THE MATTER OF

**BJ'S WHOLESALE CLUB, INC.**

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

*Docket C-4148; File No. 0423160*

*Complaint, September 20, 2005--Decision, September 20, 2005*

This consent order, among other things, requires Respondent BJ's Wholesale Club, Inc. -- a membership club with approximately 8 million current members that operates approximately 150 warehouse stores in 16 Eastern states -- to establish and maintain a comprehensive information security program that is reasonably designed to protect the security, confidentiality, and integrity of personal information it collects from or about consumers. The consent order also requires the respondent, for twenty years, to secure biennial assessments and reports to ensure that its security program provides protections that meet or exceed the protections required by the order, and is sufficiently effective to provide reasonable assurance that the security, confidentiality, and integrity of personal information is protected.

*Participants*

For the Commission: *Alain Sheer, Jessica L. Rich, Joel Winston and Louis Silversin.*

For the Respondent: *David Medine and James W. Pendergast, Wilmer Cutler Pickering Hale and Dorr LLP*

**COMPLAINT**

The Federal Trade Commission, having reason to believe that BJ's Wholesale Club, Inc. ("respondent") has violated the provisions of the Federal Trade Commission Act, and it appearing to the Commission that this proceeding is in the public interest, alleges:

1. Respondent BJ's Wholesale Club, Inc. is a Delaware corporation with its principal office or place of business at One Mercer Road, Natick, Massachusetts 01760.

## Complaint

2. The acts and practices of respondent as alleged in this complaint have been in or affecting commerce, as “commerce” is defined in Section 4 of the Federal Trade Commission Act.
3. Respondent operates approximately 150 warehouse clubs (“stores”) in 16 eastern states. Generally, only consumers who have purchased memberships from respondent may make purchases at its stores. Approximately 8 million consumers currently have valid memberships. At its stores, respondent sells memberships as well as approximately 7,500 brand-name food and general merchandise items, including office supplies and equipment, consumer electronics, prerecorded media, small appliances, auto accessories and tires, jewelry, health and beauty aids, household needs, computer software, books, greeting cards, apparel, toys, tools, and seasonal items. Members often pay for such purchases with credit cards and debit cards.
4. Respondent uses computer networks to request and obtain authorization from the bank that issued the card (“issuing bank”) for credit card and debit card purchases at its stores. To obtain authorization, respondent collects information from the customer, including customer name, card number and expiration date, and certain other information (collectively, “personal information”).
5. For a purchase at a store, respondent typically collects the information from the magnetic stripe of the credit or debit card and compiles it into an authorization request on the computer network located in the store (“in-store computer network”). Respondent then transmits the information from the in-store computer network to its central datacenter and from there through outside computer networks to the issuing bank. Respondent receives the issuing bank’s response through the same computer networks used to make the request.
6. Respondent also uses its in-store computer networks to manage inventory. Using wireless inventory scanners (“scanners”),



Complaint

respondent collects inventory information at its stores. Respondent operates wireless access points on its in-store computer networks through which scanners connect and transmit inventory information to in-store computer networks.

7. From at least November 1, 2003, until February, 2004, respondent did not employ reasonable and appropriate measures to secure personal information collected at its stores. Among other things, respondent (1) did not encrypt the information while in transit or when stored on the in-store computer networks; (2) stored the information in files that could be accessed anonymously -- that is, using a commonly known default user id and password; (3) did not use readily available security measures to limit access to its computer networks through wireless access points on the networks; (4) failed to employ sufficient measures to detect unauthorized access or conduct security investigations; and (5) created unnecessary risks to the information by storing it for up to 30 days when it no longer had a business need to keep the information, and in violation of bank rules. As a result, a hacker could have used the wireless access points on an in-store computer network to connect to the network and, without authorization, access personal information on the network.
8. Beginning in late 2003 and early 2004, banks began discovering fraudulent purchases that were made using counterfeit copies of credit and debit cards the banks had issued to customers. The customers had used their cards at respondent's stores before the fraudulent purchases were made, and personal information respondent obtained from their cards was stored on respondent's computer networks. This same information was contained on counterfeit copies of cards that were used to make several million dollars in fraudulent purchases. In response, banks and their customers cancelled and re-issued thousands of credit and debit cards that had been used at respondent's stores, and customers holding these cards were unable to use their cards to access credit and their own bank accounts.

## Complaint

9. As described in Paragraphs 7 and 8 above, respondent's failure to employ reasonable and appropriate security measures to protect personal information and files caused or is likely to cause substantial injury to consumers that is not offset by countervailing benefits to consumers or competition and is not reasonably avoidable by consumers. This practice was an unfair act or practice.
  
10. The acts and practices of respondent as alleged in this complaint constitute unfair acts or practices in or affecting commerce in violation of Section 5(a) of the Federal Trade Commission Act, 15 U.S.C. § 45(a).

THEREFORE, the Federal Trade Commission this 20<sup>th</sup> day of September, 2005, has issued this complaint against respondent.

Decision and Order

## **DECISION AND ORDER**

The Federal Trade Commission having initiated an investigation of certain acts and practices of the Respondent named in the caption hereof, and the Respondent having been furnished thereafter with a copy of a draft Complaint that the Bureau of Consumer Protection proposed to present to the Commission for its consideration and which, if issued by the Commission, would charge the Respondent with violation of the Federal Trade Commission Act, 15 U.S.C. § 45 et seq;

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

The Commission having thereafter considered the matter and having determined that it has reason to believe that the Respondent has violated the said Act, and that a Complaint should issue stating its charges in that respect, and having thereupon accepted the executed Consent Agreement and placed such Consent Agreement on the public record for a period of thirty (30) days, and having duly considered the comments filed thereafter by interested persons pursuant to Section 2.34 of its Rules, now in further conformity with the procedure described in Section 2.34 of its Rules, the Commission hereby issues its Complaint, makes the following jurisdictional findings and enters the following Order:

1. Proposed respondent BJ’s Wholesale Club, Inc. is a Delaware corporation with its principal office or place of business at One Mercer Road, Natick, Massachusetts 01760.

## Decision and Order

2. The Federal Trade Commission has jurisdiction of the subject matter of this proceeding and of the Respondent, and the proceeding is in the public interest.

**ORDER****DEFINITIONS**

For purposes of this order, the following definitions shall apply:

1. "Personal information" shall mean individually identifiable information from or about an individual consumer including, but not limited to: (a) a first and last name; (b) a home or other physical address, including street name and name of city or town; (c) an email address or other online contact information, such as an instant messaging user identifier or a screen name that reveals an individual's email address; (d) a telephone number; (e) a Social Security number; (f) credit and/or debit card information, including credit and/or debit card number, expiration date, and data stored on the magnetic stripe of a credit or debit card; (g) a persistent identifier, such as a customer number held in a "cookie" or processor serial number, that is combined with other available data that identifies an individual consumer; or (h) any other information from or about an individual consumer that is combined with (a) through (g) above.

2. Unless otherwise specified, "respondent" shall mean BJ's Wholesale Club, Inc. and its successors and assigns, officers, agents, representatives, and employees.

3. "Commerce" shall mean as defined in Section 4 of the Federal Trade Commission Act, 15 U.S.C. § 44.

**I.**

**IT IS ORDERED** that respondent, directly or through any corporation, subsidiary, division, or other device, in connection

Decision and Order

with the advertising, marketing, promotion, offering for sale, or sale of any product or service, in or affecting commerce, shall, no later than the date of service of this order, establish and implement, and thereafter maintain, a comprehensive information security program that is reasonably designed to protect the security, confidentiality, and integrity of personal information collected from or about consumers. Such program, the content and implementation of which must be fully documented in writing, shall contain administrative, technical, and physical safeguards appropriate to respondent's size and complexity, the nature and scope of respondent's activities, and the sensitivity of the personal information collected from or about consumers, including:

- A. the designation of an employee or employees to coordinate and be accountable for the information security program.
- B. the identification of material internal and external risks to the security, confidentiality, and integrity of personal information that could result in the unauthorized disclosure, misuse, loss, alteration, destruction, or other compromise of such information, and assessment of the sufficiency of any safeguards in place to control these risks. At a minimum, this risk assessment should include consideration of risks in each area of relevant operation, including, but not limited to: (1) employee training and management; (2) information systems, including network and software design, information processing, storage, transmission, and disposal; and (3) prevention, detection, and response to attacks, intrusions, or other systems failures.
- C. the design and implementation of reasonable safeguards to control the risks identified through risk assessment, and regular testing or monitoring of the effectiveness of the safeguards' key controls, systems, and procedures.

## Decision and Order

D. the evaluation and adjustment of respondent's information security program in light of the results of the testing and monitoring required by subparagraph C, any material changes to respondent's operations or business arrangements, or any other circumstances that respondent knows or has reason to know may have a material impact on the effectiveness of its information security program.

**II.**

**IT IS FURTHER ORDERED** that respondent obtain an assessment and report (an "Assessment") from a qualified, objective, independent third-party professional, using procedures and standards generally accepted in the profession, within one hundred and eighty (180) days after service of the order, and biennially thereafter for twenty (20) years after service of the order that:

- A. sets forth the specific administrative, technical, and physical safeguards that respondent has implemented and maintained during the reporting period;
- B. explains how such safeguards are appropriate to respondent's size and complexity, the nature and scope of respondent's activities, and the sensitivity of the personal information collected from or about consumers;
- C. explains how the safeguards that have been implemented meet or exceed the protections required by Paragraph I of this order; and
- D. certifies that respondent's security program is operating with sufficient effectiveness to provide reasonable assurance that the security, confidentiality, and integrity of personal information is protected and, for biennial reports, has so operated throughout the reporting period.

Each Assessment shall be prepared by a person qualified as a

Decision and Order

Certified Information System Security Professional (CISSP) or as a Certified Information Systems Auditor (CISA); a person holding Global Information Assurance Certification (GIAC) from the SysAdmin, Audit, Network, Security (SANS) Institute; or a similarly qualified person or organization approved by the Associate Director for Enforcement, Bureau of Consumer Protection, Federal Trade Commission, Washington, D.C. 20580. Respondent shall provide the first Assessment, as well as all: plans, reports, studies, reviews, audits, audit trails, policies, training materials, and assessments, whether prepared by or on behalf of respondent, relied upon to prepare such Assessment to the Associate Director for Enforcement, Bureau of Consumer Protection, Federal Trade Commission, Washington, D.C. 20580, within ten (10) days after the Assessment has been prepared. All subsequent biennial Assessments shall be retained by respondent until the order is terminated and provided to the Associate Director of Enforcement within ten (10) days of request.

**III.**

**IT IS FURTHER ORDERED** that respondent shall maintain, and upon request make available to the Federal Trade Commission for inspection and copying, a print or electronic copy of each document relating to compliance, including but not limited to:

A. for a period of five (5) years: any documents, whether prepared by or on behalf of respondent, that contradict, qualify, or call into question respondent's compliance with this order; and

B. for a period of three (3) years after the date of preparation of each biennial Assessment required under Paragraph II of this order: all plans, reports, studies, reviews, audits, audit trails, policies, training materials, and assessments, whether prepared by or on behalf of respondent, relating to

## Decision and Order

respondent's compliance with Paragraphs I and II of this order for the compliance period covered by such biennial Assessment.

**IV.**

**IT IS FURTHER ORDERED** that respondent shall deliver a copy of this order to all current and future principals, officers, directors, and managers, and to all current and future employees, agents, and representatives having managerial responsibilities relating to the subject matter of this order. Respondent shall deliver this order to such current personnel within thirty (30) days after service of this order, and to such future personnel within thirty (30) days after the person assumes such position or responsibilities.

**V.**

**IT IS FURTHER ORDERED** that respondent shall notify the Commission at least thirty (30) days prior to any change in the corporation that may affect compliance obligations arising under this order, including, but not limited to, a dissolution, assignment, sale, merger, or other action that would result in the emergence of a successor corporation; the creation or dissolution of a subsidiary, parent, or affiliate that engages in any acts or practices subject to this order; the proposed filing of a bankruptcy petition; or a change in either corporate name or address. *Provided, however,* that, with respect to any proposed change in the corporation about which respondent learns less than thirty (30) days prior to the date such action is to take place, respondent shall notify the Commission as soon as is practicable after obtaining such knowledge. All notices required by this Paragraph shall be sent by certified mail to the Associate Director, Division of Enforcement, Bureau of Consumer Protection, Federal Trade Commission, Washington, D.C. 20580.



Decision and Order

**VI.**

**IT IS FURTHER ORDERED** that respondent shall, within one hundred and eighty (180) days after service of this order, and at such other times as the Commission may require, file with the Commission an initial report, in writing, setting forth in detail the manner and form in which it has complied with this order.

**VII.**

This order will terminate twenty (20) years from the date of its issuance, or twenty (20) years from the most recent date that the United States or the Federal Trade Commission files a complaint (with or without an accompanying consent decree) in federal court alleging any violation of the order, whichever comes later; *provided, however*, that the filing of such a complaint will not affect the duration of:

A. any Paragraph in this order that terminates in less than twenty (20) years;

B. this order's application to any respondent that is not named as a defendant in such complaint; and

C. this order if such complaint is filed after the order has terminated pursuant to this Paragraph.

*Provided, further*, that if such complaint is dismissed or a federal court rules that respondent did not violate any provision of the order, and the dismissal or ruling is either not appealed or upheld on appeal, then the order will terminate according to this Paragraph as though the complaint had never been filed, except that the order will not terminate between the date such complaint is filed and the later of the deadline for appealing such dismissal or ruling and the date such dismissal or ruling is upheld on appeal.

## Analysis

**Analysis of Proposed Consent Order to Aid Public Comment**

The Federal Trade Commission has accepted, subject to final approval, a consent agreement from BJ's Wholesale Club, Inc. ("BJ's").

The consent agreement has been placed on the public record for thirty (30) days for receipt of comments by interested persons. Comments received during this period will become part of the public record. After thirty (30) days, the Commission will again review the agreement and the comments received, and will decide whether it should withdraw from the agreement and take appropriate action or make final the agreement's proposed order.

BJ's operates about 150 warehouse clubs ("stores") in 16 eastern states. BJ's is a membership club with about 8 million current members. Members often use credit and debit cards to pay for their purchases at BJ's. In the course of seeking approval for these credit and debit card purchases, BJ's collected members' personal information, including card number and expiration date and other information, from magnetic stripes on the cards.

The Commission's proposed complaint alleges that BJ's stored members' personal information on computers at its stores and failed to employ reasonable and appropriate security measures to protect the information. The complaint alleges that this failure was an unfair practice because it caused or was likely to cause substantial consumer injury that was not reasonably avoidable and was not outweighed by countervailing benefits to consumers or competition. In particular, the complaint alleges that BJ's engaged in a number of practices which, taken together, did not provide reasonable security for sensitive personal information, including: (1) failing to encrypt information collected in its stores while the information was in transit or stored on BJ's computer networks; (2) storing the information in files that could be accessed anonymously, that is, using a commonly known default user id and password; (3) failing to use readily available security measures to limit access to its networks through wireless access

Analysis

points on the networks; (4) failing to employ measures sufficient to detect unauthorized access to the networks or conduct security investigations; and (5) storing information for up to 30 days when BJ's no longer had a business need to keep the information, in violation of bank security rules.

The complaint further alleges that several million dollars in fraudulent purchases were made using counterfeit copies of credit and debit cards members had used at BJ's stores. The counterfeit cards contained the same personal information BJ's had collected from the magnetic stripes of members' credit and debit cards and then stored on its computer networks. After discovering the fraudulent purchases, banks cancelled and re-issued thousands of credit and debit cards members had used at BJ's stores, and members holding these cards were unable to use them to access credit and their own bank accounts.

The proposed order applies to personal information from or about consumers BJ's collects in connection with its business. It contains provisions designed to prevent BJ's from engaging in the future in practices similar to those alleged in the complaint.

Specifically, Part I of the proposed order requires BJ's to establish and maintain a comprehensive information security program in writing that is reasonably designed to protect the security, confidentiality, and integrity of personal information it collects from or about consumers. The security program must contain administrative, technical, and physical safeguards appropriate to BJ's size and complexity, the nature and scope of its activities, and the sensitivity of the personal information collected.

Specifically, the order requires BJ's to:

- Designate an employee or employees to coordinate and be accountable for the information security program.
- Identify material internal and external risks to the security, confidentiality, and integrity of consumer information that could result in unauthorized disclosure, misuse, loss,

## Analysis

alteration, destruction, or other compromise of such information, and assess the sufficiency of any safeguards in place to control these risks.

- Design and implement reasonable safeguards to control the risks identified through risk assessment, and regularly test or monitor the effectiveness of the safeguards' key controls, systems, and procedures.
- Evaluate and adjust its information security program in light of the results of testing and monitoring, any material changes to its operations or business arrangements, or any other circumstances that BJ's knows or has to reason to know may have a material impact on the effectiveness of its information security program.

Part II of the proposed order requires that BJ's obtain within 180 days, and on a biennial basis thereafter, an assessment and report from a qualified, objective, independent third-party professional, certifying, among other things, that: (1) BJ's has in place a security program that provides protections that meet or exceed the protections required by Part I of the proposed order, and (2) BJ's security program is operating with sufficient effectiveness to provide reasonable assurance that the security, confidentiality, and integrity of consumers' personal information has been protected.

Parts III through VII of the proposed order are reporting and compliance provisions. Part III requires BJ's to retain documents relating to its compliance with the order. Part IV requires dissemination of the order now and in the future to persons with responsibilities relating to the subject matter of the order. Part V requires BJ's to notify the Commission of changes in BJ's corporate status. Part VI mandates that BJ's submit compliance reports to the FTC. Part VII is a provision "sunsetting" the order after twenty (20 ) years, with certain exceptions.

Analysis

The purpose of this analysis is to facilitate public comment on the proposed order. It is not intended to constitute an official interpretation of the proposed order to modify its terms in any way.

Complaint

**IN THE MATTER OF****NOVARTIS AG**

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

*Docket C-4150; File No. 0510106*

*Complaint, September 21, 2005--Decision, September 21, 2005*

This consent order addresses the acquisition by Respondent Novartis AG of Eon Labs, Inc., from Santo Holding AG. The order, among other things, requires the respondent -- through Sandoz, Inc., its generic pharmaceuticals division -- to divest to Amide Pharmaceutical, Inc. the Eon assets necessary to manufacture and market generic desipramine hydrochloride tablets (a tricyclic antidepressant), and the Sandoz assets necessary to manufacture and market orphenadrine citrate ER tablets (a muscle relaxant) and rifampin oral capsules (one of several drugs used in a multi-drug approach to treating tuberculosis) in the United States. The order also requires Novartis, through Sandoz, to enter into a supply agreement with Amide to enable Amide to market these products until Amide obtains Food and Drug Administration ("FDA") approval to manufacture the products itself, and to provide technology transfer assistance to enable Amide to obtain all necessary FDA approvals as quickly as possible.

*Participants*

For the Commission: *Elizabeth A. Jex, David L. Inglefield, Richard A. Levy, Jeanna L. Composti, Clare E. Jones, Michael R. Moiseyev and Mark Hertzendorf.*

For the Respondent: *Kenneth S. Prince, Shearman & Sterling LLP*

**COMPLAINT**

Pursuant to the Federal Trade Commission Act and the Clayton Act, and by virtue of the authority vested in it by said Acts, the Federal Trade Commission ("Commission"), having reason to believe that Respondent Novartis AG ("Novartis"), a corporation subject to the jurisdiction of the Commission, has offered to acquire 67% of the outstanding shares of Eon Labs, Inc., a corporation subject to the jurisdiction of the Commission, from

Complaint

Santo AG (“Santo”), a corporation subject to the jurisdiction of the Commission, in violation of Section 7 of the Clayton Act, as amended, 15 U.S.C. § 18, and Section 5 of the Federal Trade Commission Act, as amended, 15 U.S.C. § 45, and it appearing to the Commission that a proceeding in respect thereof would be in the public interest, hereby issues its Complaint, stating its charges as follows:

**I. RESPONDENT**

1. Respondent Novartis is a corporation organized, existing and doing business under and by virtue of the laws of Switzerland, with its office and principal place of business located at Lichtstrasse 35, CH-4002 Basel, Switzerland. Respondent Novartis owns a variety of subsidiaries, including Sandoz Inc. which is engaged in the research, development, manufacture and sale of human generic pharmaceutical products in the United States.

2. Novartis is, and at all times relevant herein has been, engaged in commerce, as “commerce” is defined in Section 1 of the Clayton Act as amended, 15 U.S.C. § 12, and is a corporation whose business is in or affects commerce, as “commerce” is defined in Section 4 of the Federal Trade Commission Act, as amended, 15 U.S.C. § 44.

**II. THE ACQUIRED COMPANY**

3. Santo Holding AG (“Santo”) is a corporation organized, existing, and doing business under and by virtue of the laws of Switzerland, with its office and principal place of business located at Alte Landstrasse 106, CH-8702 Zollikon/Zurich.

4. Santo owns 67% of the outstanding stock of Eon Labs, Inc. (“Eon”). Eon is a corporation organized, existing and doing business under and by virtue of the laws of the state of Delaware, with its principal place of business located at 1999 Marcus Avenue, Lake Success, New York 11042. Santo, among other

## Complaint

things, is engaged in the research, development, manufacture, and sale of human pharmaceutical products in the United States through Eon.

**II. THE PROPOSED ACQUISITION**

5. On February 20, 2005, Novartis and Santo entered into a Purchase Agreement and Sale of Stock whereby Novartis agreed to purchase 60 million shares of Eon from Santo for approximately \$1.72 billion in cash (“the Acquisition”). These shares represent approximately 67% of the outstanding stock of Eon. Further, Novartis has made a definitive agreement, approved by the Eon Board of Directors, to offer to acquire the remaining 31.9 million fully diluted shares of Eon for \$31.00 per share cash. With the closing of these transactions, Novartis would become the global leader in generic pharmaceuticals with combined pro forma 2004 sales of \$5.1 billion, and a portfolio of over 600 generic pharmaceutical products.

**III. THE RELEVANT MARKETS**

6. One of the relevant lines of commerce in which to analyze the effects of the Acquisition is the manufacture and sale of generic desipramine hydrochloride tablets. Desipramine hydrochloride is a tricyclic antidepressant. The branded desipramine product, Norpramin, does not offer any significant price pressure in the generic desipramine market other than setting a price ceiling that is currently many times higher than the generic pricing level. The brand price is essentially irrelevant with respect to the pricing of generic desipramine tablets. In contrast, the competition between producers of generic desipramine tablets has a direct and substantial effect on generic desipramine pricing.

7. A second relevant line of commerce in which to analyze the effects of the Acquisition is the manufacture and sale of generic orphenadrine citrate ER tablets. Orphenadrine citrate is a muscle relaxant. The branded orphenadrine citrate product, Norflex, does not impact the pricing of generic orphenadrine citrate other than



Complaint

setting a price ceiling that is currently many times higher than the generic pricing level. In contrast, the competition between producers of generic orphenadrine citrate tablets has a direct and substantial effect on generic orphenadrine citrate pricing.

8. The third relevant line of commerce in which to analyze the effects of the Acquisition is the manufacture and sale of generic rifampin oral capsules. Rifampin is indicated for the treatment of tuberculosis. The branded rifampin product, Rifadin, does not offer any significant price pressure in the generic rifampin oral capsule market other than setting a price ceiling that is currently many times higher than the generic pricing level. In contrast, the competition between producers of generic rifampin capsules has a direct and substantial effect on generic rifampin pricing.

9. For the purposes of this Complaint, the United States is the relevant geographic area in which to analyze the effects of the Acquisition in each of the relevant lines of commerce.

#### **IV. THE STRUCTURE OF THE MARKETS**

10. The market for the manufacture and sale of generic desipramine hydrochloride tablets is highly concentrated. Only Novartis and Eon market all six strengths of generic desipramine hydrochloride tablets in the United States, and the only other firm marketing generic desipramine hydrochloride tablets is Watson Pharmaceuticals, Inc., which markets three of the six strengths.

11. The market for the manufacture and sale of generic orphenadrine citrate ER tablets is highly concentrated. Only Eon, Novartis and Impax Laboratories, Inc. (through its generics division, Global Pharmaceuticals) manufacture and market generic orphenadrine citrate ER tablets in the United States.

12. The market for the manufacture and sale of generic rifampin oral capsules is highly concentrated. Only Eon, Novartis and VersaPharm, Incorporated market generic rifampin oral capsules in the United States.

Complaint

**V. ENTRY CONDITIONS**

13. Entry into each of the relevant product markets would not be timely, likely, or sufficient in its magnitude, character, and scope to deter or counteract the anticompetitive effects of the Acquisition. Developing and obtaining United States Food and Drug Administration approval for the manufacture and sale of generic desipramine hydrochloride tablets, generic orphenadrine citrate ER tablets and generic rifampin oral capsules takes at least two years due to substantial regulatory, technological, and intellectual property barriers.

**VI. EFFECTS OF THE ACQUISITION**

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

- a. by eliminating actual, direct, and substantial competition between Novartis and Eon;
- b. by increasing the likelihood that Novartis will be able to unilaterally exercise market power;
- c. by increasing the likelihood and degree of coordinated interaction between or among competitors; and
- d. by increasing the likelihood that consumers will pay higher prices.

**VII. VIOLATIONS CHARGED**

15. The Purchase Agreement described in Paragraph 4 constitutes a violation of Section 5 of the FTC Act, as amended, 15 U.S.C. § 45.

Complaint

16. The Acquisition described in Paragraph 4, if consummated, would constitute a violation of Section 7 of the Clayton Act, as amended, 15 U.S.C. § 18, and Section 5 of the FTC Act, as amended, 15 U.S.C. § 45.

WHEREFORE, THE PREMISES CONSIDERED, the Federal Trade Commission on this twenty-first day of September, 2005, issues its Complaint against said Respondent.

Decision and Order

**DECISION AND ORDER**

The Federal Trade Commission (“Commission”) having initiated an investigation of the proposed acquisition by Respondent NOVARTIS AG (hereinafter “NOVARTIS,” “Respondent,” or “Respondent NOVARTIS”) of the interest in Eon Labs, Inc. held by Santo Holding AG (“SANTO”) and Respondent having been furnished thereafter with a copy of a draft of Complaint that the Bureau of Competition proposed to present to the Commission for its consideration and which, if issued by the Commission, would charge Respondent with violations of Section 7 of the Clayton Act, as amended, 15 U.S.C. § 18, and Section 5 of the Federal Trade Commission Act, as amended, 15 U.S.C. § 45; and

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

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

Decision and Order

1. Respondent NOVARTIS is a corporation organized, existing and doing business under and by virtue of the laws of Switzerland, with its offices and principal place of business located at Lichtstrasse 35, CH-4002 Basel, Switzerland.

2. The Federal Trade Commission has jurisdiction over the subject matter of this proceeding and of Respondent, and the proceeding is in the public interest.

**ORDER**

**I.**

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

A. “NOVARTIS” means NOVARTIS AG, its directors, officers, employees, agents, representatives, predecessors, successors, and assigns; its joint ventures, subsidiaries (including, but not limited to, Sandoz Inc.), divisions, groups and affiliates controlled by NOVARTIS AG, and the respective directors, officers, employees, agents, representatives, successors, and assigns of each. After the Acquisition Date, the term “NOVARTIS” shall include Eon.

B. “SANTO” means Santo Holding AG, a corporation organized, existing, and doing business under and by virtue of the laws of Switzerland, with its registered office located at Alte Landstrasse 106, CH-8702 Zollikon/Zurich, Switzerland; and all joint ventures, subsidiaries, divisions, groups, and affiliates controlled by SANTO, including, but not limited to, Eon.

C. “Eon” means Eon Labs, Inc., a corporation organized, existing, and doing business under and by virtue of the laws of Delaware, with its principal place of business located at 1999 Marcus Avenue, Lake Success, New York 11042; and all joint ventures, subsidiaries, divisions, groups, and affiliates controlled by Eon.

D. “Respondent” means NOVARTIS.

## Decision and Order

E. “Commission” means the Federal Trade Commission.

F. “Acquisition” means the acquisition contemplated by the “Agreement for Purchase and Sale of Stock” dated as of February 20, 2005, by and between NOVARTIS and SANTO, whereby NOVARTIS agreed to acquire 60,000,000 shares of Eon from SANTO for approximately Euro 1.3 billion in cash.

G. “Acquisition Date” means the date the Acquisition is consummated.

H. “Agency(ies)” means any governmental regulatory authority or authorities in the United States responsible for granting approval(s), clearance(s), qualification(s), license(s) or permit(s) for any aspect of the research, Development, manufacture, marketing, distribution or sale of a Product. The term “Agency” includes, but is not limited to, the United States Food and Drug Administration (“FDA”).

I. “AMIDE” means AMIDE PHARMACEUTICAL, INC., a corporation organized, existing, and doing business under and by virtue of the laws of the State of New Jersey, with its principal place of business located at 101 East Main Street, Little Falls, New Jersey 07424.

J. “AMIDE Divestiture Agreement” means the Asset Purchase Agreement, the Supply Agreement and the Quality Agreement between NOVARTIS’ subsidiary, Sandoz Inc., and AMIDE, dated June 13, 2005, if such agreement has not been rejected by the Commission pursuant to Paragraph II.A., III.A. or IV.A. of this Order, and all related amendments, exhibits, attachments, agreements, and schedules, by and between Respondent NOVARTIS and AMIDE. The AMIDE Divestiture Agreement is attached to this Order as non-public Appendix I.

K. “Application,” “New Drug Application” (“NDA”), “Abbreviated New Drug Application” (“ANDA”), “Supplemental New Drug Application” (“SNDA”), “Supplemental Abbreviated New Drug Application” (“SANDA”) or “Marketing Authorization

Decision and Order

Application” (“MAA”) mean the applications for a Product filed or to be filed with the FDA pursuant to 21 C.F.R. Part 314, and all supplements, amendments, and revisions thereto, any data necessary for the preparation thereof, and all correspondence between Respondent NOVARTIS or SANTO and the FDA or other Agency relative thereto.

L. “Closing Date” means, with respect to each of the divestitures required by Paragraphs II.A., III.A. and IV.A. of this Order, the date on which Respondent NOVARTIS or a Divestiture Trustee and a Commission-approved Acquirer consummate a transaction to divest relevant assets pursuant to this Order. (Pursuant to Paragraphs II.A., III.A. and IV.A. of this Order, the Closing Date is required to occur not later than ten (10) Days after the Acquisition Date.)

M. “Commission-approved Acquirer” means the following:

1. AMIDE, provided AMIDE has not been rejected by the Commission pursuant to Paragraph II.A., III.A. or IV.A. of this Order; or
2. an entity approved by the Commission to acquire assets that Respondent NOVARTIS is required to divest, grant, license, deliver or otherwise convey pursuant to this Order.

N. “Confidential Business Information” means all information owned by, or in the possession or control of, Respondent NOVARTIS that is not in the public domain.

O. “Contract Manufacture” means the manufacture of a Product to be supplied by Respondent NOVARTIS (or a Designee specifically identified in this Order) to the Commission-approved Acquirer.

P. “Day(s)” means the period of time prescribed under this Order as computed pursuant to 16 C.F.R. § 4.3 (a).

Q. “Designee” means any Person other than Respondent NOVARTIS designated by the Commission-approved Acquirer.

## Decision and Order

R. “Desipramine” means the chemical substance known by the international non-proprietary name desipramine and/or all pharmaceutically active derivatives thereof including, without limitation, esters, salts, hydrates, solvates, polymorphs, prodrugs, metabolites and isomers thereof and all hydrates, solvates, polymorphs, prodrugs and isomers of such salts, as manufactured, marketed and sold by SANTO under ANDA numbers 74-430, 71-601, 71-588, 71-602, and 71-766 at any time during the six months preceding the Acquisition Date.

S. “Desipramine Assets” means all of Respondent NOVARTIS’ rights, title and interest in and to all assets, tangible and intangible, acquired from SANTO pursuant to the Acquisition, related to SANTO’s Desipramine business in the United States to the extent legally transferable, including the research, Development, manufacture, distribution, marketing or sale of Desipramine, including, without limitation, the following:

1. all Product Intellectual Property;
2. all Product Registrations;
3. all Product Scientific and Regulatory Material;
4. all Product Manufacturing Technology;
5. all Confidential Business Information relating to Desipramine;
6. all Rights of Reference or Use to: (a) the Drug Master Files related to SANTO’s Desipramine business in the United States, including, but not limited to, the pharmacology and toxicology data contained in all Applications, NDAs, ANDAs, SNDAs, SANDAs and MAAs; and (b) information similar to such Drug Master Files submitted to any Agency other than the FDA, if such rights exist;
7. all Respondent NOVARTIS’ books, records and files related to the foregoing, including, but not limited to, the following specified documents:



Decision and Order

- a. the Product Registrations;
  - b. all pharmacology and toxicology data contained in or related to all Applications, Drug Master Files, NDAs, ANDAs, SNDAs, SANDAs and MAAs; all data submitted to and all correspondence with the FDA and other Agencies; all validation documents and data; including, without limitation, clinical data, and quality control histories pertaining to the Product owned by, or in the possession or control of, NOVARTIS, or to which NOVARTIS has a right of access;
  - c. all customer lists, vendor lists, catalogs, sales promotion literature, advertising materials, research materials, technical information, dedicated management information systems, specifications, designs, drawings, processes and quality control data, all in a form and to an extent deemed satisfactory by the Commission-approved Acquirer;
  - d. all customer purchase orders, customer product specifications and requirements, records of historical customer purchases, customer correspondence, customer information, invoices, payment records, customer records, and customer files, all in a form and to an extent deemed satisfactory by the Commission-approved Acquirer;
8. all unfilled customer orders relating to Desipramine as of the Closing Date (a list of such orders is to be provided to the Commission-approved Acquirer within two (2) Days after the Closing Date); and,
9. at the Commission-approved Acquirer's option, and subject to the approval of the Commission:
- a. any Product Contracts; and,
  - b. all Desipramine inventories, stores, and supplies held by, or under the control of, NOVARTIS, including, but not limited to, the active pharmaceutical ingredient, goods in process, finished goods, and specific packaging and labels.

## Decision and Order

*Provided, however,* that “Desipramine Assets” does not include: (i) any real property; (ii) any personal property; (iii) any plant or other facility; (iv) any equipment; or (v) any asset or business owned by NOVARTIS prior to the Acquisition Date.

T. “Development” means all preclinical and clinical drug development activities, including test method development and stability testing, toxicology, bioequivalency, formulation, process development, manufacturing scale-up, development-stage manufacturing, quality assurance/quality control development, statistical analysis and report writing, conducting clinical trials for the purpose of obtaining any and all approvals, licenses, registrations or authorizations from any Agency necessary for the manufacture, use, storage, import, export, transport, promotion, marketing and sale of a Product, Product approval and registration, and regulatory affairs related to the foregoing. “Develop” means to engage in Development.

U. “Direct Cost” means the cost of direct labor, direct material used and direct out-of-pocket costs incurred to provide the relevant assistance or service.

V. “Divested Assets” means the Desipramine Assets, Orphenadrine Citrate ER Assets, and Rifampin Assets.

W. “Divestiture Trustee” means a trustee appointed by the Commission pursuant to the relevant provisions of this Order.

X. “Drug Master Files” means the information submitted to the FDA as described in 21 C.F.R. Part 314.420 related to a Product.

Y. “Final Finished Form” means a Product packaged in final form and ready for sale by the Commission-approved Acquirer to the Commission-approved Acquirer’s ultimate customer (other than for the addition of the Commission-approved Acquirer’s specific packaging and/or labeling).

Decision and Order

Z. “Governmental Entity” means any Federal, state or local government or any court, legislature, governmental agency or governmental commission or any judicial or regulatory authority in the United States.

AA. “Interim Monitor” means a monitor appointed by the Commission pursuant to Paragraph V. of this Order.

BB. “Orphenadrine Citrate ER” means the chemical substance known by the international non-proprietary name orphenadrine citrate and/or all pharmaceutically active derivatives thereof including, without limitation, esters, salts, hydrates, solvates, polymorphs, prodrugs, metabolites and isomers thereof and all hydrates, solvates, polymorphs, prodrugs and isomers of such salts; and includes extended release formulations of orphenadrine citrate, as manufactured, marketed and sold by NOVARTIS under ANDA number 40-284 at any time during the six months preceding the Acquisition Date.

CC. “Orphenadrine Citrate ER Assets” means all of Respondent NOVARTIS’ rights, title and interest in and to all assets, tangible and intangible, in existence on the day preceding the Acquisition Date, related to NOVARTIS’ Orphenadrine Citrate ER business in the United States to the extent legally transferable, including the research, Development, manufacture, distribution, marketing or sale of Orphenadrine Citrate ER, including, without limitation, the following:

1. all Product Intellectual Property;
2. all Product Registrations;
3. all Product Scientific and Regulatory Material;
4. all Product Manufacturing Technology;
5. all Confidential Business Information relating to Orphenadrine Citrate ER;

## Decision and Order

6. all Rights of Reference or Use to: (a) the Drug Master Files related to NOVARTIS' Orphenadrine Citrate ER business in the United States, including, but not limited to, the pharmacology and toxicology data contained in all Applications, NDAs, ANDAs, SNDAs, SANDAs and MAAs; and (b) information similar to such Drug Master Files submitted to any Agency other than the FDA, if such rights exist;
7. all Respondent NOVARTIS' books, records and files related to the foregoing, including, but not limited to, the following specified documents:
  - a. the Product Registrations;
  - b. all pharmacology and toxicology data contained in or related to all Applications, Drug Master Files, NDAs, ANDAs, SNDAs, SANDAs and MAAs; all data submitted to and all correspondence with the FDA and other Agencies; all validation documents and data; including, without limitation, clinical data, and quality control histories pertaining to the Product owned by, or in the possession or control of, NOVARTIS, or to which NOVARTIS has a right of access;
  - c. all customer lists, vendor lists, catalogs, sales promotion literature, advertising materials, research materials, technical information, dedicated management information systems, specifications, designs, drawings, processes and quality control data, all in a form and to an extent deemed satisfactory by the Commission-approved Acquirer;
  - d. all customer purchase orders, customer product specifications and requirements, records of historical customer purchases, customer correspondence, customer information, invoices, payment records, customer records, and customer files, all in a form and to an extent deemed satisfactory by the Commission-approved Acquirer;
8. all unfilled customer orders relating to Orphenadrine Citrate ER as of the Closing Date (a list of such orders is to be provided

Decision and Order

to the Commission-approved Acquirer within two (2) Days after the Closing Date); and,

9. at the Commission-approved Acquirer's option, and subject to the approval of the Commission:

a. any Product Contracts; and,

b. all Orphenadrine Citrate ER inventories, stores, and supplies held by, or under the control of, NOVARTIS, including, but not limited to, the active pharmaceutical ingredient, goods in process, finished goods, and specific packaging and labels.

*Provided, however,* that "Orphenadrine Citrate ER Assets" does not include: (i) any real property; (ii) any personal property; (iii) any plant or other facility; (iv) any equipment; or (v) any asset or business owned by SANTO prior to the Acquisition Date.

DD. "Patents" means all United States patents and patent applications, in each case existing on the Closing Date, and includes all reissues, divisions, continuations, continuations-in-part, substitutions, reexaminations, restorations, and/or patent term extensions thereof, all inventions disclosed therein, all rights therein provided by international treaties and conventions, and all rights to obtain and file for patents and registrations thereto in the United States, related to a Product of or owned by Respondent on the Closing Date.

EE. "Person" means any company, natural person, incorporated or unincorporated entity, partnership, association, joint venture, government entity, non-profit organization, university, trust or other entity, except for NOVARTIS.

FF. "Product" means each of Desipramine, Orphenadrine Citrate ER and Rifampin.

GG. "Product Contracts" means all contracts and agreements solely relating to a Product between Respondent and any Person.

## Decision and Order

HH. “Product Intellectual Property” means all of the following related to the Product(s):

1. Patents;
2. Product Copyrights;
3. Product Software, other than Product Intellectual Property;
4. Product Trademarks;
5. Product trade secrets, know-how, techniques, data, inventions, practices, methods and other confidential or proprietary technical, business, research, Development and other information;
6. Rights to obtain and file for Patents and registrations thereof; and
7. Rights to sue and recover damages or obtain injunctive relief for infringement, dilution, misappropriation, violation, or breach of any of the foregoing;

*provided, however*, “Product Intellectual Property” does not include the names “Sandoz,” “NOVARTIS,” “Geneva,” “Eon” or the names of any other corporations or companies owned by Respondent NOVARTIS or related logos to the extent used on other of SANTO’s or Respondent NOVARTIS’ products; however, the right to use the name Rimactane in the United States shall be included in Product Intellectual Property related to Rifampin.

II. “Product Manufacturing Technology” means all technology, trade secrets, know-how, and proprietary information (whether patented, patentable or otherwise) related to the manufacture, validation, packaging, release testing, stability and shelf life of the Product, including all product formulations, product specifications, processes, product designs, plans, trade secrets, ideas, concepts, manufacturing, engineering and other manuals and drawings, standard operating procedures, flow diagrams, chemical, pharmacological, toxicological, pharmaceutical,

Decision and Order

physical and analytical, safety, efficacy, bioequivalency, quality assurance, quality control and clinical data, research records, compositions, annual product reviews, process validation reports, analytical method validation reports, specifications for stability trending and process controls, testing and reference standards for impurities in and degradation of products, technical data packages, chemical and physical characterizations, dissolution test methods and results, formulations for administration, clinical trial reports, regulatory communications and labeling and all other information related to the manufacturing process, and supplier lists, in each case with respect to a Product and as in existence and in the possession of Respondent NOVARTIS or SANTO on the Closing Date.

JJ. “Product Registrations” means all United States registrations, permits, licenses, consents, authorizations and other approvals, and pending applications and requests therefore, required by applicable Agencies related to the research, Development, manufacture, finishing, packaging, distribution, marketing or sale of any Product, including all NDAs and ANDAs. “Product Registrations” includes all underlying information, data, filings, reports, correspondence or other materials used to obtain or apply for any of the foregoing, including, without limitation, all data submitted to and all correspondence with the FDA and other Agencies.

KK. “Product Scientific and Regulatory Material” means all technological, scientific, chemical, biological, pharmacological, toxicological, regulatory and clinical trial materials and information related to the Product, and full rights to use such materials, in the United States.

LL. “Product Trademark(s)” means all United States trademarks related to the Product, including, but not limited to any trademark or trade dress covering:

1. the size, shape and color of a single dose entity of any generic version of the Product; and

## Decision and Order

2. the appearance, structure, textual or graphical content and/or color scheme of any labeling, dosing information, product inserts, storage containers and/or other materials, to the extent that the FDA or any other Agency requires the Commission-approved Acquirer to duplicate such appearance, structure, textual or graphical content and/or color scheme of any labeling, dosing information, product inserts, storage containers and/or other materials.

MM. “Proposed Acquirer” means AMIDE or an entity proposed by Respondent NOVARTIS (or a Divestiture Trustee) to the Commission and submitted for the approval of the Commission as the acquirer for particular assets required to be divested, granted, licensed, delivered or otherwise conveyed by Respondent NOVARTIS pursuant to this Order.

NN. “Remedial Agreement” means the following: (1) any agreement between Respondent and a Commission-approved Acquirer (including, but not limited to, the AMIDE Divestiture Agreement) that is specifically referenced and attached to this Order, including all amendments, exhibits, attachments, agreements, and schedules thereto, related to the relevant assets to be assigned, granted, licensed, divested, transferred, delivered, or otherwise conveyed, and that has been approved by the Commission to accomplish the requirements of the Order in connection with the Commission’s determination to make this Order final; and/or (2) any agreement between the Respondent and a Commission-approved Acquirer (or between a Divestiture Trustee and a Commission-approved Acquirer) that has been approved by the Commission to accomplish the requirements of this Order, including all amendments, exhibits, attachments, agreements, and schedules thereto, related to the relevant assets to be assigned, granted, licensed, divested, transferred, delivered, or otherwise conveyed, and that has been approved by the Commission to accomplish the requirements of this Order.

OO. “Rifampin” means the chemical substance known by the international non-proprietary name rifampin and/or all pharmaceutically active derivatives thereof including, without



Decision and Order

limitation, esters, salts, hydrates, solvates, polymorphs, prodrugs, metabolites and isomers thereof and all hydrates, solvates, polymorphs, prodrugs and isomers of such salts, as marketed and sold by NOVARTIS under NDA number 50-429 at any time during the six months preceding the Acquisition Date.

PP. “Rifampin Agreement” means the Manufacture and Supply Agreement, dated July 7, 1999, entered into by and between NOVARTIS and AMIDE.

QQ. “Rifampin Assets” means all of Respondent NOVARTIS’ rights, title and interest in and to all assets, tangible and intangible, in existence on the day preceding the Acquisition Date, related to NOVARTIS’ Rifampin business in the United States to the extent legally transferable, including the research, Development, manufacture, distribution, marketing or sale of Rifampin, including, without limitation, the following:

1. all Product Intellectual Property;
2. all Product Registrations;
3. all Product Scientific and Regulatory Material;
4. all Product Manufacturing Technology;
5. all Confidential Business Information relating to Rifampin;
6. all Rights of Reference or Use to: (a) the Drug Master Files related to NOVARTIS’ Rifampin business in the United States, including, but not limited to, the pharmacology and toxicology data contained in all Applications, NDAs, ANDAs, SNDAs, SANDAs and MAAs; and (b) information similar to such Drug Master Files submitted to any Agency other than the FDA, if such rights exist;
7. all Respondent NOVARTIS’ books, records and files related to the foregoing, including, but not limited to, the following specified documents:

## Decision and Order

- a. the Product Registrations;
  - b. all pharmacology and toxicology data contained in or related to all Applications, Drug Master Files, NDAs, ANDAs, SNDAs, SANDAs and MAAs; all data submitted to and all correspondence with the FDA and other Agencies; all validation documents and data; including, without limitation, clinical data, and quality control histories pertaining to the Product owned by, or in the possession or control of, NOVARTIS, or to which NOVARTIS has a right of access;
  - c. all customer lists, vendor lists, catalogs, sales promotion literature, advertising materials, research materials, technical information, dedicated management information systems, specifications, designs, drawings, processes and quality control data, all in a form and to an extent deemed satisfactory by the Commission-approved Acquirer;
  - d. all customer purchase orders, customer product specifications and requirements, records of historical customer purchases, customer correspondence, customer information, invoices, payment records, customer records, and customer files, all in a form and to an extent deemed satisfactory by the Commission-approved Acquirer;
8. all unfilled customer orders relating to Rifampin as of the Closing Date (a list of such orders is to be provided to the Commission-approved Acquirer within two (2) Days after the Closing Date); and,
9. at the Commission-approved Acquirer's option, and subject to the approval of the Commission:
- a. any Product Contracts (including, but not limited to, the Rifampin Agreement); and,
  - b. all Rifampin inventories, stores, and supplies held by, or under the control of, NOVARTIS, including, but not limited to, the active pharmaceutical ingredient, goods in process, finished goods, and specific packaging and labels.

Decision and Order

*Provided, however,* that “Rifampin Assets” does not include: (i) any real property; (ii) any personal property; (iii) any plant or other facility; (iv) any equipment; or (v) any asset or business owned by SANTO prior to the Acquisition Date.

RR. “Right of Reference or Use” means the authority to rely upon, and otherwise use, an investigation for the purpose of obtaining approval of an Application, including the ability to make available the underlying raw data from the investigation for FDA audit.

SS. “Supply Cost” means the manufacturer’s standard per SKU cost of manufacturing and packaging the Product including those costs associated with quality control and assurance, stability, testing and warehousing; the Supply Cost for Desipramine and Orphenadrine Citrate ER is set forth in non-public Appendix II. “Supply Cost” shall expressly exclude any intracompany business transfer profit.

**II.**

**IT IS FURTHER ORDERED** that:

A. Not later than ten (10) Days after the Acquisition Date, Respondent NOVARTIS shall divest the Desipramine Assets, absolutely and in good faith, to AMIDE pursuant to and in accordance with the AMIDE Divestiture Agreement. The AMIDE Divestiture Agreement shall not vary or contradict, or be construed to vary or contradict, the terms of this Order, it being understood that nothing in this Order shall be construed to reduce any rights or benefits of AMIDE or to reduce any obligations of Respondent NOVARTIS under such agreement.

*provided, however,* that, if Respondent NOVARTIS has divested the Desipramine Assets to AMIDE prior to the date this Order becomes final, and if, at the time the Commission determines to make this Order final, the Commission notifies Respondent NOVARTIS that:

## Decision and Order

1. AMIDE is not an acceptable purchaser of the Desipramine Assets, then Respondent shall immediately rescind the transaction with AMIDE and, within six (6) months from the date the Order becomes final, shall divest the Desipramine Assets to a Commission-approved Acquirer absolutely and in good faith, at no minimum price, and only in a manner that receives the prior approval of the Commission; or
  2. the manner in which the divestiture was accomplished is not acceptable, the Commission may direct Respondent NOVARTIS, or appoint a Divestiture Trustee, pursuant to Paragraph VI. of this Order, to effect such modifications (including, but not limited to, entering into additional agreements or arrangements) as may be necessary to satisfy the requirements of this Order.
- B. Any Remedial Agreement that has been approved by the Commission between Respondent NOVARTIS (or a Divestiture Trustee) and a Commission-approved Acquirer of the Desipramine Assets shall be deemed incorporated into this Order, and any failure by Respondent NOVARTIS to comply with any term of such Remedial Agreement shall constitute a failure to comply with this Order.
- C. Respondent NOVARTIS shall not enforce any agreement against any Person to the extent that such agreement may limit or otherwise impair the ability of the Commission-approved Acquirer to operate the Desipramine Assets as such assets were engaged at the time of the announcement of the Acquisition. Such agreements include, but are not limited to, agreements with respect to the disclosure of Confidential Business Information relating to Desipramine.
- D. Respondent NOVARTIS shall secure, prior to the Closing Date, all consents and waivers from all Persons that are necessary for the divestiture of the Desipramine Assets to the Commission-approved Acquirer, or for the continued research, Development, manufacture, use, import, sale, marketing or distribution of Desipramine in the United States by the Commission-approved Acquirer.

Decision and Order

E. Respondent NOVARTIS shall maintain manufacturing facilities for the Desipramine finished drug product that are validated, qualified and approved by the FDA, and fully capable of producing Desipramine finished drug product and shall Contract Manufacture and supply such finished drug product to the Commission-approved Acquirer until the earlier of (i) the Commission-approved Acquirer (or the Designee of the Commission-approved Acquirer) obtains all FDA approvals necessary to manufacture and sell Desipramine independently of Respondent NOVARTIS; or (ii) four (4) years from the Closing Date for the Desipramine Assets;

*provided, however,* the Commission may eliminate, or further limit the duration of, the Respondent's obligation under this provision should the Commission determine that the Commission-approved Acquirer is not using commercially reasonable best efforts to obtain all FDA approvals necessary to manufacture and sell Desipramine independently of Respondent NOVARTIS.

F. Upon reasonable notice and request from the Commission-approved Acquirer to the Respondent NOVARTIS, Respondent NOVARTIS shall provide (in a timely manner and at no greater than Direct Cost) to the Commission-approved Acquirer consultation with, assistance, training, and advice from, knowledgeable employees of Respondent NOVARTIS with respect to the Development and manufacture of Desipramine that the Commission-approved Acquirer might reasonably need in order to receive and use the Desipramine Assets in a manner consistent with this Order, and shall continue providing such consultation, assistance, training and advice, at the request of the Commission-approved Acquirer, until the Commission-approved Acquirer (or the Designee of the Commission-approved Acquirer) obtains all FDA approvals necessary to manufacture and sell Desipramine independently of Respondent NOVARTIS; *provided, however,* Respondent NOVARTIS' obligation to provide such assistance as required by this paragraph shall not exceed four (4) years from the last Closing Date relating to Desipramine.

## Decision and Order

G. Upon request of the Commission-approved Acquirer and subject to the approval of the Commission, Respondent NOVARTIS shall include in any Remedial Agreement the following provisions:

1. Respondent NOVARTIS shall Contract Manufacture and deliver to the Commission-approved Acquirer, in a timely manner and under reasonable terms and conditions, a supply of Desipramine in Final Finished Form, at Respondent NOVARTIS' Supply Cost, EXW (Incoterms 2000) the manufacturing facility, for a period of time sufficient to allow the Commission-approved Acquirer (or the Designee of the Commission-approved Acquirer) to obtain all FDA approvals necessary to manufacture and sell Desipramine independently of Respondent NOVARTIS; *provided, however*, Respondent NOVARTIS' obligation to Contract Manufacture shall not exceed four (4) years from the last Closing Date relating to Desipramine; *provided further, however*, that commencing nineteen (19) months after the last Closing Date relating to Desipramine, Respondent NOVARTIS' supply of Desipramine to the Commission-approved Acquirer may be at a price that is increased by ten (10) percent per year above Respondent NOVARTIS' Supply Cost.
2. For the term of the Contract Manufacture related to Desipramine, Respondent NOVARTIS will make inventory of Desipramine available for sale or resale only to the Commission-approved Acquirer (not for use in Respondent NOVARTIS' own business after the Acquisition Date); *provided, however*, nothing in this Order shall prohibit Respondent NOVARTIS from researching, developing, manufacturing, using, importing, selling, marketing or distributing products that compete with Desipramine.
3. Respondent NOVARTIS' obligation to supply Desipramine to the Commission-approved Acquirer pursuant to the terms of the Remedial Agreement shall take priority over the manufacture and supply of any product for Respondent NOVARTIS' own use or sale.

Decision and Order

4. Respondent NOVARTIS shall make representations and warranties to the Commission-approved Acquirer that the Desipramine supplied through Contract Manufacture pursuant to the Remedial Agreement meets current good manufacturing practices of the FDA, as set forth in 21 C.F.R. Parts 210 and 211. Respondent NOVARTIS shall agree to indemnify, defend and hold the Commission-approved Acquirer harmless from any and all suits, claims, actions, demands, liabilities, expenses or losses alleged to result from the failure of the Desipramine supplied to the Commission-approved Acquirer pursuant to the Remedial Agreement by Respondent NOVARTIS to meet such specifications. This obligation shall be contingent upon the Commission-approved Acquirer giving Respondent NOVARTIS prompt, adequate notice of such claim and cooperating fully in the defense of such claim. The Remedial Agreement shall be consistent with the obligations assumed by Respondent NOVARTIS under this Order;

*provided, however,* Respondent NOVARTIS may reserve the right to control the defense of any such litigation, including the right to settle the litigation, so long as such settlement is consistent with Respondent NOVARTIS' responsibilities to supply Desipramine in the manner required by this Order;

*provided further, however,* this obligation shall not require Respondent NOVARTIS to be liable for any act or omission or misconduct whether willful or negligent of the Commission-approved Acquirer nor for any representations and warranties, express or implied, made by the Commission-approved Acquirer that exceed the representations and warranties made by Respondent NOVARTIS to the Commission-approved Acquirer.

5. Respondent NOVARTIS shall make representations and warranties to the Commission-approved Acquirer that Respondent NOVARTIS will hold harmless and indemnify the Commission-approved Acquirer for any liabilities including, but not limited to, indirect damages, special damages, consequential damages, lost profits, legal fees and costs resulting from the failure by Respondent NOVARTIS to deliver Desipramine in a timely

## Decision and Order

manner as required by the Remedial Agreement unless Respondent NOVARTIS can demonstrate that its failure was entirely beyond the control of the Respondent NOVARTIS and in no part the result of negligence or willful misconduct by Respondent NOVARTIS.

6. During the term of the Contract Manufacture between Respondent NOVARTIS and the Commission-approved Acquirer, upon request of the Commission-approved Acquirer or Interim Monitor (if applicable), Respondent NOVARTIS shall make available to the Commission-approved Acquirer or the Interim Monitor (if applicable) all records that relate to the Contract Manufacture of Desipramine that are generated or created after the Closing Date.

7. Upon reasonable notice and request from the Commission-approved Acquirer to the Respondent NOVARTIS, Respondent NOVARTIS shall provide in a timely manner at no greater than Direct Cost the following:

a. assistance and advice to enable the Commission-approved Acquirer (or the Designee of the Commission-approved Acquirer) to obtain all necessary permits and approvals from any Agency or Governmental Entity to manufacture and sell Desipramine;

b. assistance to the Commission-approved Acquirer (or the Designee of the Commission-approved Acquirer) to manufacture Desipramine in substantially the same manner and quality employed or achieved by Respondent NOVARTIS; and

c. consultation with knowledgeable employees of Respondent NOVARTIS and training, at the request of the Commission-approved Acquirer and at a facility chosen by the Commission-approved Acquirer, until the Commission-approved Acquirer (or the Designee of the Commission-approved Acquirer) obtains all FDA approvals necessary to manufacture and sell Desipramine independently of Respondent NOVARTIS and sufficient to



Decision and Order

satisfy management of the Commission-approved Acquirer that its personnel (or the Designee's personnel) are adequately trained in the manufacture of Desipramine.

H. Respondent NOVARTIS shall delete Desipramine from any customer contracts in effect as of the Closing Date that are not divested to the Commission-approved Acquirer.

I. Not later than ten (10) Days after the Closing Date, Respondent NOVARTIS shall begin to deliver to the Commission-approved Acquirer, at Respondent NOVARTIS' expense, copies of all Confidential Business Information relating to Desipramine. Not later than one hundred eighty (180) Days after the Closing Date, Respondent NOVARTIS shall complete delivery of all such Confidential Business Information relating to Desipramine to the Commission-approved Acquirer and certify to the Commission that such delivery has occurred in accordance with this Order. Respondent NOVARTIS shall deliver such Confidential Business Information relating to Desipramine as follows: (1) in good faith; (2) as soon as practicable, avoiding any delays in transmission of such information; and (3) in a manner that insures its completeness and accuracy and that fully preserves its usefulness. Pending complete delivery of all such Confidential Business Information relating to Desipramine to the Commission-approved Acquirer, Respondent NOVARTIS shall provide the Interim Monitor (if any has been appointed) with reasonable access to all such Confidential Business Information relating to Desipramine and employees who possess or are able to locate such information for the purposes of identifying the books, records, and files related to the Desipramine Assets that contain such Confidential Business Information relating to Desipramine and facilitating the delivery in a manner consistent with this Order.

J. Respondent NOVARTIS shall take all necessary steps to maintain the confidentiality of the Confidential Business Information relating to Desipramine. *Provided, further, that:*

## Decision and Order

1. Except as permitted under the Remedial Agreement or this Order, Respondent NOVARTIS shall not (i) provide, disclose, or otherwise make available any Confidential Business Information relating to Desipramine to any Person or (ii) use any Confidential Business Information relating to Desipramine for any reason or purpose;

2. Nothing in this Order prohibits Respondent NOVARTIS from disclosing Confidential Business Information relating to Desipramine if required by United States federal or state law, regulation, court order, or subpoena; *provided, however*, that Respondent NOVARTIS shall use its reasonable best efforts to protect the confidentiality of such information, including, but not limited to, obtaining a protective order during an adjudication; and

3. If disclosure of any Confidential Business Information relating to Desipramine is permitted under this Order, Respondent NOVARTIS shall provide, disclose, or otherwise make available such information (i) only to those Persons who require such information for the permitted purposes, (ii) only to the extent that such Confidential Business Information is required, and (iii) only to those Persons who agree in writing or otherwise are required to maintain the confidentiality of such information.

K. Pending the divestiture of the Desipramine Assets, Respondent NOVARTIS shall take such actions as are necessary to maintain the full economic viability, marketability and competitiveness of the business associated with the Desipramine Assets, to minimize any risk of loss of competitive potential for the business associated with the Desipramine Assets, and to prevent the destruction, removal, wasting, deterioration, or impairment of any of the Desipramine Assets except for ordinary wear and tear.

L. The purpose of the divestiture of the Desipramine Assets to a Commission-approved Acquirer is to create an independent, viable and effective competitor in the relevant markets in which the Desipramine Assets were engaged at the time of the announcement of the Acquisition, and to remedy the lessening of

Decision and Order

competition resulting from the Acquisition as alleged in the Commission's Complaint.

**III.**

**IT IS FURTHER ORDERED** that:

A. Not later than ten (10) Days after the Acquisition Date, Respondent NOVARTIS shall divest the Orphenadrine Citrate ER Assets, absolutely and in good faith, to AMIDE pursuant to and in accordance with the AMIDE Divestiture Agreement. The AMIDE Divestiture Agreement shall not vary or contradict, or be construed to vary or contradict, the terms of this Order, it being understood that nothing in this Order shall be construed to reduce any rights or benefits of AMIDE or to reduce any obligations of Respondent NOVARTIS under such agreement.

*provided, however,* that, if Respondent NOVARTIS has divested the Orphenadrine Citrate ER Assets to AMIDE prior to the date this Order becomes final, and if, at the time the Commission determines to make this Order final, the Commission notifies Respondent NOVARTIS that:

1. AMIDE is not an acceptable purchaser of the Orphenadrine Citrate ER Assets, then Respondent shall immediately rescind the transaction with AMIDE and, within six (6) months from the date the Order becomes final, shall divest the Orphenadrine Citrate ER Assets to a Commission-approved Acquirer absolutely and in good faith, at no minimum price, and only in a manner that receives the prior approval of the Commission; or
2. the manner in which the divestiture was accomplished is not acceptable, the Commission may direct Respondent NOVARTIS, or appoint a Divestiture Trustee, pursuant to Paragraph VI. of this Order, to effect such modifications (including, but not limited to, entering into additional agreements or arrangements) as may be necessary to satisfy the requirements of this Order.

B. Any Remedial Agreement that has been approved by the

## Decision and Order

Commission between Respondent NOVARTIS (or a Divestiture Trustee) and a Commission-approved Acquirer of the Orphenadrine Citrate ER Assets shall be deemed incorporated into this Order, and any failure by Respondent NOVARTIS to comply with any term of such Remedial Agreement shall constitute a failure to comply with this Order.

C. Respondent NOVARTIS shall not enforce any agreement against any Person to the extent that such agreement may limit or otherwise impair the ability of the Commission-approved Acquirer to operate the Orphenadrine Citrate ER Assets as such assets were engaged at the time of the announcement of the Acquisition. Such agreements include, but are not limited to, agreements with respect to the disclosure of Confidential Business Information relating to Orphenadrine Citrate ER.

D. Respondent NOVARTIS shall secure, prior to the Closing Date, all consents and waivers from all Persons that are necessary for the divestiture of the Orphenadrine Citrate ER Assets to the Commission-approved Acquirer, or for the continued research, Development, manufacture, use, import, sale, marketing or distribution of Orphenadrine Citrate ER in the United States by the Commission-approved Acquirer.

E. Respondent NOVARTIS shall maintain manufacturing facilities for the Orphenadrine Citrate ER finished drug product that are validated, qualified and approved by the FDA, and fully capable of producing Orphenadrine Citrate ER finished drug product and shall Contract Manufacture and supply such finished drug product to the Commission-approved Acquirer until the earlier of (i) the Commission-approved Acquirer (or the Designee of the Commission-approved Acquirer) obtains all FDA approvals necessary to manufacture and sell Orphenadrine Citrate ER independently of Respondent NOVARTIS; or (ii) six (6) years from the last Closing Date for the Orphenadrine Citrate ER Assets;

*provided, however*, the Commission may eliminate, or further limit the duration of, the Respondent's obligation under this

Decision and Order

provision should the Commission determine that the Commission-approved Acquirer is not using commercially reasonable best efforts to obtain all FDA approvals necessary to manufacture and sell Orphenadrine Citrate ER independently of Respondent NOVARTIS.

F. Upon reasonable notice and request from the Commission-approved Acquirer to the Respondent NOVARTIS, Respondent NOVARTIS shall provide (in a timely manner and at no greater than Direct Cost) to the Commission-approved Acquirer consultation with, assistance, training, and advice from, knowledgeable employees of Respondent NOVARTIS with respect to the Development and manufacture of Orphenadrine Citrate ER that the Commission-approved Acquirer might reasonably need in order to receive and use the Orphenadrine Citrate ER Assets in a manner consistent with this Order, and shall continue providing such consultation, assistance, training and advice, at the request of the Commission-approved Acquirer, until the Commission-approved Acquirer (or the Designee of the Commission-approved Acquirer) obtains all FDA approvals necessary to manufacture and sell Orphenadrine Citrate ER independently of Respondent NOVARTIS; *provided, however*, Respondent NOVARTIS' obligation to provide such assistance as required by this paragraph shall not exceed six (6) years from the last Closing Date relating to Orphenadrine Citrate ER;

G. Upon request of the Commission-approved Acquirer and subject to the approval of the Commission, Respondent NOVARTIS shall include in any Remedial Agreement the following provisions:

1. Respondent NOVARTIS shall Contract Manufacture and deliver to the Commission-approved Acquirer, in a timely manner and under reasonable terms and conditions, a supply of Orphenadrine Citrate ER in Final Finished Form, at Respondent NOVARTIS' Supply Cost, EXW (Incoterms 2000) the manufacturing facility, for a period of time sufficient to allow the Commission-approved Acquirer (or the Designee of the Commission-approved Acquirer) to obtain all FDA approvals

## Decision and Order

necessary to manufacture and sell Orphenadrine Citrate ER independently of Respondent NOVARTIS; *provided, however*, Respondent NOVARTIS' obligation to Contract Manufacture shall not exceed six (6) years from the last Closing Date relating to Orphenadrine Citrate ER; *provided further, however*, that commencing twenty-nine (29) months after the last Closing Date relating to Orphenadrine Citrate ER, Respondent NOVARTIS' supply of Orphenadrine Citrate ER to the Commission-approved Acquirer may be at a price that is increased by ten (10) percent per year above Respondent NOVARTIS' Supply Cost.

2. For the term of the Contract Manufacture related to Orphenadrine Citrate ER, Respondent NOVARTIS will make inventory of Orphenadrine Citrate ER available for sale or resale only to the Commission-approved Acquirer (not for use in Respondent NOVARTIS' own business after the Acquisition Date); *provided, however*, nothing in this Order shall prohibit Respondent NOVARTIS from researching, developing, manufacturing, using, importing, selling, marketing or distributing products that compete with Orphenadrine Citrate ER.

3. Respondent NOVARTIS' obligation to supply Orphenadrine Citrate ER to the Commission-approved Acquirer pursuant to the terms of the Remedial Agreement shall take priority over the manufacture and supply of any product for Respondent NOVARTIS' own use or sale.

4. Respondent NOVARTIS shall make representations and warranties to the Commission-approved Acquirer that the Orphenadrine Citrate ER supplied through Contract Manufacture pursuant to the Remedial Agreement meets current good manufacturing practices of the FDA, as set forth in 21 C.F.R. Parts 210 and 211. Respondent NOVARTIS shall agree to indemnify, defend and hold the Commission-approved Acquirer harmless from any and all suits, claims, actions, demands, liabilities, expenses or losses alleged to result from the failure of the Orphenadrine Citrate ER supplied to the Commission-approved Acquirer pursuant to the Remedial Agreement by Respondent NOVARTIS to meet such specifications. This

Decision and Order

obligation shall be contingent upon the Commission-approved Acquirer giving Respondent NOVARTIS prompt, adequate notice of such claim and cooperating fully in the defense of such claim. The Remedial Agreement shall be consistent with the obligations assumed by Respondent NOVARTIS under this Order;

*provided, however,* Respondent NOVARTIS may reserve the right to control the defense of any such litigation, including the right to settle the litigation, so long as such settlement is consistent with Respondent NOVARTIS' responsibilities to supply Orphenadrine Citrate ER in the manner required by this Order;

*provided further, however,* this obligation shall not require Respondent NOVARTIS to be liable for any act or omission or misconduct whether willful or negligent of the Commission-approved Acquirer nor for any representations and warranties, express or implied, made by the Commission-approved Acquirer that exceed the representations and warranties made by Respondent NOVARTIS to the Commission-approved Acquirer.

5. Respondent NOVARTIS shall make representations and warranties to the Commission-approved Acquirer that Respondent NOVARTIS will hold harmless and indemnify the Commission-approved Acquirer for any liabilities including, but not limited to, indirect damages, special damages, consequential damages, lost profits, legal fees and costs resulting from the failure by Respondent NOVARTIS to deliver Orphenadrine Citrate ER in a timely manner as required by the Remedial Agreement unless Respondent NOVARTIS can demonstrate that its failure was entirely beyond the control of the Respondent NOVARTIS and in no part the result of negligence or willful misconduct by Respondent NOVARTIS.

6. During the term of the Contract Manufacture between Respondent NOVARTIS and the Commission-approved Acquirer, upon request of the Commission-approved Acquirer or Interim Monitor (if applicable), Respondent NOVARTIS shall make available to the Commission-approved Acquirer or the Interim

## Decision and Order

Monitor (if applicable) all records that relate to the Contract Manufacture of Orphenadrine Citrate ER that are generated or created after the Closing Date.

7. Upon reasonable notice and request from the Commission-approved Acquirer to the Respondent NOVARTIS, Respondent NOVARTIS shall provide in a timely manner at no greater than Direct Cost the following:

a. assistance and advice to enable the Commission-approved Acquirer (or the Designee of the Commission-approved Acquirer) to obtain all necessary permits and approvals from any Agency or Governmental Entity to manufacture and sell Orphenadrine Citrate ER;

b. assistance to the Commission-approved Acquirer (or the Designee of the Commission-approved Acquirer) to manufacture Orphenadrine Citrate ER in substantially the same manner and quality employed or achieved by Respondent NOVARTIS; and

c. consultation with knowledgeable employees of Respondent NOVARTIS and training, at the request of the Commission-approved Acquirer and at a facility chosen by the Commission-approved Acquirer, until the Commission-approved Acquirer (or the Designee of the Commission-approved Acquirer) obtains all FDA approvals necessary to manufacture and sell Orphenadrine Citrate ER independently of Respondent NOVARTIS and sufficient to satisfy management of the Commission-approved Acquirer that its personnel (or the Designee's personnel) are adequately trained in the manufacture of Orphenadrine Citrate ER.

H. Respondent NOVARTIS shall delete Orphenadrine Citrate ER from any customer contracts in effect as of the Closing Date that are not divested to the Commission-approved Acquirer.

I. Not later than ten (10) Days after the Closing Date, Respondent NOVARTIS shall begin to deliver to the Commission-approved Acquirer, at Respondent NOVARTIS'



Decision and Order

expense, copies of all Confidential Business Information relating to Orphenadrine Citrate ER. Not later than one hundred eighty (180) Days after the Closing Date, Respondent NOVARTIS shall complete delivery of all such Confidential Business Information relating to Orphenadrine Citrate ER to the Commission-approved Acquirer and certify to the Commission that such delivery has occurred in accordance with this Order. Respondent NOVARTIS shall deliver such Confidential Business Information relating to Orphenadrine Citrate ER as follows: (1) in good faith; (2) as soon as practicable, avoiding any delays in transmission of such information; and (3) in a manner that insures its completeness and accuracy and that fully preserves its usefulness. Pending complete delivery of all such Confidential Business Information relating to Orphenadrine Citrate ER to the Commission-approved Acquirer, Respondent NOVARTIS shall provide the Interim Monitor (if any has been appointed) with reasonable access to all such Confidential Business Information relating to Orphenadrine Citrate ER and employees who possess or are able to locate such information for the purposes of identifying the books, records, and files related to the Orphenadrine Citrate ER Assets that contain such Confidential Business Information and facilitating the delivery in a manner consistent with this Order.

J. Respondent NOVARTIS shall take all necessary steps to maintain the confidentiality of the Confidential Business Information relating to Orphenadrine Citrate ER. *Provided, further,* that:

1. Except as permitted under the Remedial Agreement or this Order, Respondent NOVARTIS shall not (i) provide, disclose, or otherwise make available any Confidential Business Information relating to Orphenadrine Citrate ER to any Person or (ii) use any Confidential Business Information relating to Orphenadrine Citrate ER for any reason or purpose;
2. Nothing in this Order prohibits Respondent NOVARTIS from disclosing Confidential Business Information relating to Orphenadrine Citrate ER if required by United States federal or state law, regulation, court order, or subpoena; *provided, however,*

## Decision and Order

that Respondent NOVARTIS shall use its reasonable best efforts to protect the confidentiality of such information, including, but not limited to, obtaining a protective order during an adjudication; and

3. If disclosure of any Confidential Business Information relating to Orphenadrine Citrate ER is permitted under this Order, Respondent NOVARTIS shall provide, disclose, or otherwise make available such information (i) only to those Persons who require such information for the permitted purposes, (ii) only to the extent that such Confidential Business Information is required, and (iii) only to those Persons who agree in writing or otherwise are required to maintain the confidentiality of such information.

K. Pending the divestiture of the Orphenadrine Citrate ER Assets, Respondent NOVARTIS shall take such actions as are necessary to maintain the full economic viability, marketability and competitiveness of the business associated with the Orphenadrine Citrate ER Assets, to minimize any risk of loss of competitive potential for the business associated with the Orphenadrine Citrate ER Assets, and to prevent the destruction, removal, wasting, deterioration, or impairment of any of the Orphenadrine Citrate ER Assets except for ordinary wear and tear.

L. The purpose of the divestiture of the Orphenadrine Citrate ER Assets to a Commission-approved Acquirer is to create an independent, viable and effective competitor in the relevant markets in which the Orphenadrine Citrate ER Assets were engaged at the time of the announcement of the Acquisition, and to remedy the lessening of competition resulting from the Acquisition as alleged in the Commission's Complaint.

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

A. Not later than ten (10) Days after the Acquisition Date, Respondent NOVARTIS shall divest the Rifampin Assets,

Decision and Order

absolutely and in good faith, to AMIDE pursuant to and in accordance with the AMIDE Divestiture Agreement. The AMIDE Divestiture Agreement shall not vary or contradict, or be construed to vary or contradict, the terms of this Order, it being understood that nothing in this Order shall be construed to reduce any rights or benefits of AMIDE or to reduce any obligations of Respondent NOVARTIS under such agreement.

*provided, however,* that, if Respondent NOVARTIS has divested the Rifampin Assets to AMIDE prior to the date this Order becomes final, and if, at the time the Commission determines to make this Order final, the Commission notifies Respondent NOVARTIS that:

1. AMIDE is not an acceptable purchaser of the Rifampin Assets, then Respondent shall immediately rescind the transaction with AMIDE and, within six (6) months from the date the Order becomes final, shall divest the Rifampin Assets to a Commission-approved Acquirer absolutely and in good faith, at no minimum price, and only in a manner that receives the prior approval of the Commission; or

2. the manner in which the divestiture was accomplished is not acceptable, the Commission may direct Respondent NOVARTIS, or appoint a Divestiture Trustee, pursuant to Paragraph VI. of this Order, to effect such modifications (including, but not limited to, entering into additional agreements or arrangements) as may be necessary to satisfy the requirements of this Order.

B. Any Remedial Agreement that has been approved by the Commission between Respondent NOVARTIS (or a Divestiture Trustee) and a Commission-approved Acquirer of the Rifampin Assets shall be deemed incorporated into this Order, and any failure by Respondent NOVARTIS to comply with any term of such Remedial Agreement shall constitute a failure to comply with this Order.

C. Respondent NOVARTIS shall not enforce any agreement against any Person to the extent that such agreement may limit or

## Decision and Order

otherwise impair the ability of the Commission-approved Acquirer to operate the Rifampin Assets as such assets were engaged at the time of the announcement of the Acquisition. Such agreements include, but are not limited to, agreements with respect to the disclosure of Confidential Business Information relating to Rifampin.

D. Respondent NOVARTIS shall secure, prior to the Closing Date, all consents and waivers from all Persons that are necessary for the divestiture of the Rifampin Assets to the Commission-approved Acquirer, or for the continued research, Development, manufacture, use, import, sale, marketing or distribution of Rifampin in the United States by the Commission-approved Acquirer. If Respondent NOVARTIS assigns the Rifampin Agreement, its obligations under this Paragraph IV.D. include, but are not limited to, obtaining all consents and waivers from all Persons necessary to effect the assignment of the Rifampin Agreement in a manner that provides the Commission-approved Acquirer with all of the economic and competitive benefits of the Rifampin Agreement.

E. Respondent NOVARTIS shall assign the Rifampin Agreement to the Commission-approved Acquirer (or the Designee of the Commission-approved Acquirer);

F. Respondent NOVARTIS shall delete Rifampin from any customer contracts in effect as of the Closing Date that are not divested to the Commission-approved Acquirer.

G. Not later than ten (10) Days after the Closing Date, Respondent NOVARTIS shall begin to deliver to the Commission-approved Acquirer, at Respondent NOVARTIS' expense, copies of all Confidential Business Information relating to Rifampin. Not later than one hundred eighty (180) Days after the Closing Date, Respondent NOVARTIS shall complete delivery of all such Confidential Business Information relating to Rifampin to the Commission-approved Acquirer and certify to the Commission that such delivery has occurred in accordance with this Order. Respondent NOVARTIS shall deliver such

Decision and Order

Confidential Business Information relating to Rifampin as follows: (1) in good faith; (2) as soon as practicable, avoiding any delays in transmission of such information; and (3) in a manner that insures its completeness and accuracy and that fully preserves its usefulness. Pending complete delivery of all such Confidential Business Information relating to Rifampin to the Commission-approved Acquirer, Respondent NOVARTIS shall provide the Interim Monitor (if any has been appointed) with reasonable access to all such Confidential Business Information relating to Rifampin and employees who possess or are able to locate such information for the purposes of identifying the books, records, and files related to the Rifampin Assets that contain such Confidential Business Information relating to Rifampin and facilitating the delivery in a manner consistent with this Order.

H. Respondent NOVARTIS shall take all necessary steps to maintain the confidentiality of the Confidential Business Information relating to Rifampin. *Provided, further,* that:

1. Except as permitted under the Remedial Agreement or this Order, Respondent NOVARTIS shall not (i) provide, disclose, or otherwise make available any Confidential Business Information relating to Rifampin to any Person or (ii) use any Confidential Business Information relating to Rifampin for any reason or purpose;
2. Nothing in this Order prohibits Respondent NOVARTIS from disclosing Confidential Business Information relating to Rifampin if required by United States federal or state law, regulation, court order, or subpoena; *provided, however,* that Respondent NOVARTIS shall use its reasonable best efforts to protect the confidentiality of such information, including, but not limited to, obtaining a protective order during an adjudication; and
3. If disclosure of any Confidential Business Information relating to Rifampin is permitted under this Order, Respondent NOVARTIS shall provide, disclose, or otherwise make available such information (i) only to those Persons who require such information for the permitted purposes, (ii) only to the extent that

## Decision and Order

such Confidential Business Information is required, and (iii) only to those Persons who agree in writing or otherwise are required to maintain the confidentiality of such information.

I. Pending the divestiture of the Rifampin Assets, Respondent NOVARTIS shall take such actions as are necessary to maintain the full economic viability, marketability and competitiveness of the business associated with the Rifampin Assets, to minimize any risk of loss of competitive potential for the business associated with the Rifampin Assets, and to prevent the destruction, removal, wasting, deterioration, or impairment of any of the Rifampin Assets except for ordinary wear and tear.

J. The purpose of the divestiture of the Rifampin Assets to a Commission-approved Acquirer is to create an independent, viable and effective competitor in the relevant markets in which the Rifampin Assets were engaged at the time of the announcement of the Acquisition, and to remedy the lessening of competition resulting from the Acquisition as alleged in the Commission's Complaint.

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

A. At any time after Respondent NOVARTIS signs the Consent Agreement in this matter, the Commission may appoint a monitor ("Interim Monitor") to assure that Respondent NOVARTIS expeditiously complies with all of its obligations and performs all of its responsibilities as required by this Order and the Remedial Agreements.

B. The Commission shall select the Interim Monitor, subject to the consent of Respondent NOVARTIS, which consent shall not be unreasonably withheld. If Respondent NOVARTIS has not opposed, in writing, including the reasons for opposing, the selection of a proposed Interim Monitor within ten (10) Days after notice by the staff of the Commission to Respondent NOVARTIS

Decision and Order

of the identity of any proposed Interim Monitor, Respondent NOVARTIS shall be deemed to have consented to the selection of the proposed Interim Monitor.

C. Not later than ten (10) Days after the appointment of the Interim Monitor, Respondent NOVARTIS shall execute an agreement that, subject to the prior approval of the Commission, confers on the Interim Monitor all the rights and powers necessary to permit the Interim Monitor to monitor Respondent NOVARTIS' compliance with the relevant requirements of the Order in a manner consistent with the purposes of the Order.

D. If an Interim Monitor is appointed, Respondent NOVARTIS shall consent to the following terms and conditions regarding the powers, duties, authorities, and responsibilities of the Interim Monitor:

1. The Interim Monitor shall have the power and authority to monitor Respondent NOVARTIS' compliance with the divestiture and related requirements of the Order, and shall exercise such power and authority and carry out the duties and responsibilities of the Interim Monitor in a manner consistent with the purposes of the Order and in consultation with the Commission.
2. The Interim Monitor shall act in a fiduciary capacity for the benefit of the Commission.
3. The Interim Monitor shall serve until the earlier of:
  - a. the completion by Respondent NOVARTIS of the divestiture of all relevant assets required to be granted, licensed, delivered, or otherwise conveyed pursuant to this Order in a manner that fully satisfies the requirements of the Order and notification by the Commission-approved Acquirer to the Interim Monitor, or a determination by the Interim Monitor, that the Commission-approved Acquirer is fully capable of producing each Product acquired pursuant to a Remedial Agreement independently of Respondent NOVARTIS; or

## Decision and Order

b. the expiration of the last to expire of the Remedial Agreements;

*provided, however,* that the Commission may extend or modify this period as may be necessary or appropriate to accomplish the purposes of the Order.

4. Subject to any demonstrated legally recognized privilege, the Interim Monitor shall have full and complete access to Respondent NOVARTIS' personnel, books, documents, records kept in the normal course of business, facilities and technical information, and such other relevant information as the Interim Monitor may reasonably request, related to Respondent NOVARTIS' compliance with its obligations under the Order, including, but not limited to, its obligations related to the relevant Product assets. Respondent NOVARTIS shall cooperate with any reasonable request of the Interim Monitor and shall take no action to interfere with or impede the Interim Monitor's ability to monitor Respondent NOVARTIS' compliance with the Order.
5. The Interim Monitor shall serve, without bond or other security, at the expense of Respondent NOVARTIS on such reasonable and customary terms and conditions as the Commission may set. The Interim Monitor shall have authority to employ, at the expense of the Respondent NOVARTIS, such consultants, accountants, attorneys and other representatives and assistants as are reasonably necessary to carry out the Interim Monitor's duties and responsibilities. The Interim Monitor shall provide an accounting, at least on a quarterly basis, to Respondent NOVARTIS for all expenses incurred, including fees for his or her services, subject to the approval of the Commission.
6. Respondent NOVARTIS shall indemnify the Interim Monitor and hold the Interim Monitor harmless against any losses, claims, damages, liabilities, or expenses arising out of, or in connection with, the performance of the Interim Monitor's duties, including all reasonable fees of counsel and other reasonable expenses incurred in connection with the preparations for, or defense of, any claim, whether or not resulting in any liability, except to the



Decision and Order

extent that such losses, claims, damages, liabilities, or expenses result from misfeasance, gross negligence, willful or wanton acts, or bad faith by the Interim Monitor.

7. Respondent NOVARTIS shall provide copies of reports to the Interim Monitor in accordance with the requirements of this Order and/or as otherwise provided in any agreement approved by the Commission. The Interim Monitor shall evaluate the reports submitted by Respondent NOVARTIS, and any reports submitted by the Commission-approved Acquirer with respect to the performance of Respondent NOVARTIS' obligations under the Order or the Remedial Agreement. Within thirty (30) Days from the date the Interim Monitor receives these reports, the Interim Monitor shall report in writing to the Commission concerning performance by Respondent NOVARTIS of its obligations under the Order.

8. Respondent NOVARTIS may require the Interim Monitor and each of the Interim Monitor's consultants, accountants, attorneys and other representatives and assistants to sign a customary confidentiality agreement; *provided, however*, that such agreement shall not restrict the Interim Monitor from providing any information to the Commission.

E. The Commission may, among other things, require the Interim Monitor and each of the Interim Monitor's consultants, accountants, attorneys and other representatives and assistants to sign an appropriate confidentiality agreement related to Commission materials and information received in connection with the performance of the Interim Monitor's duties.

F. If the Commission determines that the Interim Monitor has ceased to act or failed to act diligently, the Commission may appoint a substitute Interim Monitor in the same manner as provided in this Paragraph.

## Decision and Order

G. The Commission may on its own initiative, or at the request of the Interim Monitor, issue such additional orders or directions as may be necessary or appropriate to assure compliance with the requirements of the Order.

H. The Interim Monitor appointed pursuant to this Order may be the same person appointed as a Divestiture Trustee pursuant to the relevant provisions of this Order.

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

A. If Respondent NOVARTIS has not fully complied with the obligations to divest assets as required by this Order (including the obligation to divest to AMIDE within ten (10) days), the Commission may appoint a trustee (“Divestiture Trustee”) to divest the assets required to be divested pursuant to each of the relevant Paragraphs in a manner that satisfies the requirements of each such Paragraph. In the event that the Commission or the Attorney General brings an action pursuant to § 5(l) of the Federal Trade Commission Act, 15 U.S.C. § 45(l), or any other statute enforced by the Commission, Respondent NOVARTIS shall consent to the appointment of a Divestiture Trustee in such action to divest the relevant assets. Neither the appointment of a Divestiture Trustee nor a decision not to appoint a Divestiture Trustee under this Paragraph shall preclude the Commission or the Attorney General from seeking civil penalties or any other relief available to it, including a court-appointed Divestiture Trustee, pursuant to § 5(l) of the Federal Trade Commission Act, or any other statute enforced by the Commission, for any failure by Respondent NOVARTIS to comply with this Order.

B. The Commission shall select the Divestiture Trustee, subject to the consent of Respondent NOVARTIS, which consent shall not be unreasonably withheld. The Divestiture Trustee shall be a person with experience and expertise in acquisitions and divestitures. If Respondent NOVARTIS has not opposed, in

Decision and Order

writing, including the reasons for opposing, the selection of any proposed Divestiture Trustee within ten (10) Days after notice by the staff of the Commission to Respondent NOVARTIS of the identity of any proposed Divestiture Trustee, Respondent NOVARTIS shall be deemed to have consented to the selection of the proposed Divestiture Trustee.

C. Not later than ten (10) Days after the appointment of a Divestiture Trustee, Respondent NOVARTIS shall execute a trust agreement that, subject to the prior approval of the Commission, transfers to the Divestiture Trustee all rights and powers necessary to permit the Divestiture Trustee to effect the divestiture required by the Order.

D. If a Divestiture Trustee is appointed by the Commission or a court pursuant to this Paragraph, Respondent NOVARTIS shall consent to the following terms and conditions regarding the Divestiture Trustee's powers, duties, authority, and responsibilities:

1. Subject to the prior approval of the Commission, the Divestiture Trustee shall have the exclusive power and authority to divest the assets that are required by this Order to be divested.
2. The Divestiture Trustee shall have one (1) year after the date the Commission approves the trust agreement described herein to accomplish the divestiture, which shall be subject to the prior approval of the Commission. If, however, at the end of the one (1) year period, the Divestiture Trustee has submitted a plan of divestiture or believes that the divestiture can be achieved within a reasonable time, the divestiture period may be extended by the Commission, or, in the case of a court-appointed Divestiture Trustee, by the court; *provided, however*, the Commission may extend the divestiture period only two (2) times.
3. Subject to any demonstrated legally recognized privilege, the Divestiture Trustee shall have full and complete access to the personnel, books, records and facilities related to the relevant assets that are required to be assigned, granted, licensed, divested,

## Decision and Order

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

4. The Divestiture Trustee shall use commercially reasonable efforts to negotiate the most favorable price and terms available in each contract that is submitted to the Commission, subject to Respondent NOVARTIS' absolute and unconditional obligation to divest expeditiously and at no minimum price. Each divestiture shall be made in the manner and to an acquirer as required by this Order; *provided, however*, if the Divestiture Trustee receives bona fide offers from more than one acquiring entity, and if the Commission determines to approve more than one such acquiring entity, the Divestiture Trustee shall divest to the acquiring entity selected by Respondent NOVARTIS from among those approved by the Commission; *provided further, however*, that Respondent NOVARTIS shall select such entity within five (5) Days after receiving notification of the Commission's approval.

5. The Divestiture Trustee shall serve, without bond or other security, at the cost and expense of Respondent NOVARTIS, on such reasonable and customary terms and conditions as the Commission or a court may set. The Divestiture Trustee shall have the authority to employ, at the cost and expense of Respondent NOVARTIS, such consultants, accountants, attorneys, investment bankers, business brokers, appraisers, and other representatives and assistants as are necessary to carry out the Divestiture Trustee's duties and responsibilities. The Divestiture Trustee shall account for all monies derived from the divestiture and all expenses incurred. After approval by the Commission of the account of the Divestiture Trustee, including

Decision and Order

fees for the Divestiture Trustee's services, all remaining monies shall be paid at the direction of Respondent NOVARTIS, and the Divestiture Trustee's power shall be terminated. The compensation of the Divestiture Trustee shall be based at least in significant part on a commission arrangement contingent on the divestiture of all of the relevant assets that are required to be divested by this Order.

6. Respondent NOVARTIS shall indemnify the Divestiture Trustee and hold the Divestiture Trustee harmless against any losses, claims, damages, liabilities, or expenses arising out of, or in connection with, the performance of the Divestiture Trustee's duties, including all reasonable fees of counsel and other expenses incurred in connection with the preparation for, or defense of, any claim, whether or not resulting in any liability, except to the extent that such losses, claims, damages, liabilities, or expenses result from misfeasance, gross negligence, willful or wanton acts, or bad faith by the Divestiture Trustee.

7. If, at the end of the term provided for in Paragraph VI.D.2. of this Order, the Divestiture Trustee determines that he or she is unable to grant, license, deliver or otherwise convey the relevant assets required to be granted, licensed, delivered or otherwise conveyed in a manner that preserves their marketability, viability and competitiveness and ensures their continued use in the research, Development, manufacture, import, distribution, marketing, promotion, sale, or after-sales support of the relevant Product, the Divestiture Trustee may assign, grant, license, transfer, divest, deliver or otherwise convey such additional relevant Product assets of Respondent NOVARTIS to a Commission-approved Acquirer as necessary to achieve divestitures and to satisfy the purposes and requirements of this Order.

8. The Divestiture Trustee shall have no obligation or authority to operate or maintain the relevant assets required to be granted, licensed, transferred, delivered or otherwise conveyed by this Order.

## Decision and Order

9. The Divestiture Trustee shall report in writing to Respondent NOVARTIS and to the Commission every sixty (60) Days concerning the Divestiture Trustee's efforts to accomplish the divestiture.

10. Respondent NOVARTIS may require the Divestiture Trustee and each of the Divestiture Trustee's consultants, accountants, attorneys and other representatives and assistants to sign a customary confidentiality agreement; *provided, however*, such agreement shall not restrict the Divestiture Trustee from providing any information to the Commission.

E. If the Commission determines that a Divestiture Trustee has ceased to act or failed to act diligently, the Commission may appoint a substitute Divestiture Trustee in the same manner as provided in this Paragraph.

F. The Commission or, in the case of a court-appointed Divestiture Trustee, the court, may on its own initiative or at the request of the Divestiture Trustee issue such additional orders or directions as may be necessary or appropriate to accomplish the divestiture required by this Order.

G. The Divestiture Trustee appointed pursuant to this Paragraph may be the same person appointed as Interim Monitor pursuant to the relevant provisions of this Order.

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

A. Within five (5) Days of the Acquisition Date, Respondent NOVARTIS shall submit to the Commission a letter certifying the date on which the Acquisition occurred.

B. Within thirty (30) Days after the date this Order becomes final, and every sixty (60) Days thereafter until Respondent NOVARTIS has fully complied with Paragraphs II.A. and I., III.A. and I. and IV.A. and G. (*i.e.* has divested all relevant assets

Decision and Order

and delivered all Confidential Business Information to the Commission-approved Acquirer in a manner that fully satisfies the requirements of the Order), Respondent NOVARTIS shall submit to the Commission a verified written report setting forth in detail the manner and form in which it intends to comply, is complying, and has complied with this Order. Respondent NOVARTIS shall submit at the same time a copy of its report concerning compliance with this Order to the Interim Monitor, if any Interim Monitor has been appointed. Respondent NOVARTIS shall include in its reports, among other things that are required from time to time:

1. a full description of the efforts being made to comply with the relevant Paragraphs of the Order;
2. if AMIDE is rejected by the Commission pursuant to Paragraph II.A., III.A. or IV.A. of this Order, a description of all substantive contacts or negotiations related to the divestiture of the Divested Assets and the identity of all parties contacted and copies of all written communications to and from such parties, all internal memoranda, and all reports and recommendations concerning completing its obligations under this Order to divest the Divested Assets;
3. a detailed plan to deliver all Confidential Business Information required to be delivered to the Commission-approved Acquirer pursuant to this Order and agreed upon by the Commission-approved Acquirer, and any updates or changes to such plan;
4. a description of all Confidential Business Information delivered to any Commission-approved Acquirer, including the type of information delivered, method of delivery, and date(s) of delivery;
5. a description of the Confidential Business Information currently remaining to be delivered and a projected date(s) of delivery; and

## Decision and Order

6. a description of all technical assistance provided to any Commission-approved Acquirer during the reporting period.

C. Respondent NOVARTIS shall file annually on the anniversary of the date this Order becomes final a verified written report with the Secretary of the Commission. Each such report shall set forth in detail the manner and form in which Respondent NOVARTIS has complied and is complying with this Order. Respondent NOVARTIS shall include in this report a full description of any claims (whether outstanding or resolved) by any Commission-approved Acquirer that Respondent NOVARTIS has breached or failed to comply fully with this Order or any Remedial Agreement. Respondent NOVARTIS shall include with this report a copy of any written communication (including e-mails) from any Commission-approved Acquirer that includes or relates to a claim that Respondent NOVARTIS has breached or failed to comply fully with this Order or a Remedial Agreement. Respondent NOVARTIS shall file its verified written report:

1. one (1) year after the date this Order becomes final;
2. annually until the earlier of (i) ten (10) years after this Order becomes final, and, (ii) the date Respondent NOVARTIS has fully satisfied all of its obligations under Paragraphs II.A., E. and F.; III.A., E. and F. and IV.A. and E. of this Order and any Remedial Agreement; and,
3. at other times as the Commission may require.

### VIII.

**IT IS FURTHER ORDERED** that Respondent NOVARTIS shall notify the Commission at least thirty (30) Days prior to any (1) proposed dissolution of Novartis AG or Sandoz Inc., (2) proposed acquisition, merger or consolidation of Novartis AG, or (3) any other change in Novartis AG or Sandoz Inc. or other relevant affiliates that may affect compliance obligations arising out of the order, including, but not limited to, assignment, the creation or dissolution of relevant subsidiaries.



Decision and Order

**IX.**

**IT IS FURTHER ORDERED** that, for the purpose of determining or securing compliance with this Order, and subject to any legally recognized privilege, and upon written request with reasonable notice to Respondent NOVARTIS made to its principal United States offices, Respondent NOVARTIS shall permit any duly authorized representative of the Commission:

A. Access, during office hours of Respondent NOVARTIS and in the presence of counsel, to all facilities and access to inspect and copy all books, ledgers, accounts, correspondence, memoranda and all other records and documents in the possession or under the control of Respondent NOVARTIS related to compliance with this Order; and

B. Upon five (5) Days' notice to Respondent NOVARTIS and without restraint or interference from Respondent NOVARTIS, to interview officers, directors, or employees of Respondent NOVARTIS, who may have counsel present, regarding such matters.

**X.**

**IT IS FURTHER ORDERED** that this Order shall terminate upon the earlier of:

A. September 21, 2015; and

B. The date Respondent NOVARTIS has fully satisfied all of its obligations under Paragraphs II.A., E. and F.; III.A., E. and F. and IV.A. and E. of this Order and any Remedial Agreement.

Decision and Order

**APPENDIX I**  
**NON-PUBLIC**  
**AMIDE DIVESTITURE AGREEMENT**  
**[Redacted From the Public Record Version But Incorporated**  
**By Reference]**

Decision and Order

**APPENDIX II**  
**NON-PUBLIC**  
**DESIPRAMINE AND ORPHENADRINE CITRATE ER**  
**SUPPLY COSTS**  
**[Redacted From the Public Record Version But Incorporated**  
**By Reference]**

## Analysis

**Analysis of Proposed Consent Order to Aid Public Comment**

The Federal Trade Commission (“Commission”) has accepted, subject to final approval, an Agreement Containing Consent Order (“Consent Agreement”) from Novartis AG (“Novartis”), which is designed to remedy the anticompetitive effects of the acquisition of Eon Labs, Inc. (“Eon”) by Novartis. Under the terms of the proposed Consent Agreement, Novartis, including its generic pharmaceuticals division Sandoz, Inc. (“Sandoz”), would be required to divest to Amide Pharmaceutical, Inc. (“Amide”) the Eon assets necessary to manufacture and market generic desipramine hydrochloride tablets, and the Sandoz assets necessary to manufacture and market orphenadrine citrate ER tablets and rifampin oral capsules in the United States. Further, Novartis, through Sandoz, has agreed to enter into a supply agreement with Amide to enable Amide to market these products until Amide obtains Food and Drug Administration (“FDA”) approval to manufacture the products itself. Further, Novartis is required to provide technology transfer assistance to enable Amide to obtain all necessary FDA approvals as soon as possible.

The proposed Consent Agreement has been placed on the public record for thirty days for receipt of comments by interested persons. Comments received during this period will become part of the public record. After thirty days, the Commission will again review the proposed Consent Agreement and the comments received, and will decide whether it should withdraw from the proposed Consent Agreement, modify it, or make final the Decision and Order (“Order”).

Pursuant to an Agreement for Purchase and Sale of Stock dated February 20, 2005, Novartis agreed to purchase 60 million shares of Eon from Santo Holding AG (“Santo”) for \$1.72 billion in cash. These shares represent approximately 67% of the outstanding stock of Eon. Further, Novartis has made a definitive agreement, approved by the Eon Board of Directors, to offer to acquire the remaining 31.9 million fully diluted shares of Eon for

Analysis

\$31.00 per share cash. The Commission's Complaint alleges that the proposed acquisition, if consummated, would violate Section 7 of the Clayton Act, as amended, 15 U.S.C. § 18, and Section 5 of the FTC Act, as amended, 15 U.S.C. § 45, in the markets for the manufacture and sale of: (1) generic desipramine hydrochloride tablets, (2) generic orphenadrine citrate ER tablets, and (3) generic rifampin oral capsules. The proposed Consent Agreement will remedy the alleged violations by replacing in each of these markets the lost competition that would result from the acquisition.

Desipramine hydrochloride is a tricyclic antidepressant. The branded desipramine product, Norpramin, does not offer any significant price pressure in the generic desipramine market other than setting a price ceiling that is currently many times higher than the generic pricing level. The brand price is essentially irrelevant with respect to the pricing of generic desipramine tablets. In contrast, the competition between producers of generic desipramine tablets has a direct and substantial effect on generic desipramine pricing. Annual U.S. sales of generic desipramine hydrochloride tablets are reported to be less than \$6 million. The U.S. market for the manufacture and sale of generic desipramine hydrochloride tablets is highly concentrated. Only Novartis and Eon make all six strengths of generic desipramine hydrochloride tablets. Watson Pharmaceuticals, Inc., the only other firm supplying generic desipramine hydrochloride tablets, sells only three of the six strengths. The acquisition of Eon by Novartis would increase significantly the concentration in the generic desipramine hydrochloride market. Post-acquisition, only Novartis would supply the full line, accounting for more than 95% of U.S. generic desipramine hydrochloride sales.

Orphenadrine citrate is a muscle relaxant. The branded orphenadrine citrate product, Norflex, does not impact the pricing of generic orphenadrine citrate other than setting a price ceiling that is currently many times higher than the generic pricing level. In contrast, the competition between producers of generic

## Analysis

orphenadrine citrate tablets has a direct and substantial effect on generic orphenadrine citrate pricing. Annual U.S. sales of generic orphenadrine citrate ER tablets is slightly under \$10 million. The U.S. market for the manufacture and sale of generic orphenadrine citrate ER tablets is highly concentrated. Only Eon, Novartis, and Impax Laboratories, Inc. (through its generic marketing division, Global Pharmaceuticals) manufacture and market generic orphenadrine citrate ER tablets in the United States. The acquisition would result in a duopoly with Novartis accounting for approximately 70% of all prescriptions of generic orphenadrine citrate. The acquisition of Eon by Novartis would increase the concentration in the market significantly.

Rifampin is one of several drugs used in a multi-drug cocktail for the treatment of tuberculosis. Rifampin is indicated for the treatment of tuberculosis. The branded rifampin product, Rifadin, does not offer any significant price pressure in the generic rifampin oral capsule market other than setting a price ceiling that is currently many times higher than the generic pricing level. In contrast, the competition between producers of generic rifampin capsules has a direct and substantial effect on generic rifampin pricing. Annual U.S. sales of generic rifampin oral capsules is about \$14.5 million. The U.S. market for the manufacture and sale of generic rifampin oral capsules is highly concentrated. Only Eon, Novartis, and VersaPharm, Incorporated market generic rifampin oral capsules in the United States. The acquisition would result in a duopoly with Novartis accounting for more than 70% of sales of generic rifampin in the United States. The acquisition of Eon by Novartis would increase the concentration in the market significantly.

Entry into manufacture and sale of: (1) generic desipramine hydrochloride tablets, (2) generic orphenadrine citrate ER tablets, and (3) generic rifampin oral capsules would not be timely, likely, or sufficient in its magnitude, character, and scope to deter or counteract the anticompetitive effects of the acquisition. Developing and obtaining FDA approval for the manufacture and

Analysis

sale of generic desipramine hydrochloride tablets, generic orphenadrine citrate ER tablets, and generic rifampin oral capsules takes at least two years due to substantial regulatory, technological, and intellectual property barriers.

The proposed acquisition would cause significant anticompetitive harm to consumers in the U.S. markets for generic desipramine hydrochloride tablets, generic orphenadrine citrate ER tablets, and generic rifampin oral capsules by eliminating actual, direct, and substantial competition between Novartis and Eon; by increasing the likelihood that Novartis will be able to unilaterally exercise market power; by increasing the likelihood and degree of coordinated interaction between the few remaining competitors; and by increasing the likelihood that consumers will pay higher prices.

The proposed Consent Agreement preserves competition in the generic desipramine hydrochloride tablets, generic orphenadrine citrate ER tablets, and generic rifampin oral capsules markets by requiring that Novartis divest all of the Sandoz orphenadrine citrate ER and rifampin assets and all of Eon's desipramine hydrochloride assets to Amide no later than ten days after the acquisition. Amide, a reputable generic manufacturer, is particularly well-positioned to manufacture and market generic rifampin, because Amide already currently contract manufactures generic rifampin capsules for Novartis. Amide is also well-positioned to obtain FDA approval to manufacture and market generic desipramine hydrochloride and orphenadrine citrate ER in the near future. If the Commission determines that Amide is not an acceptable purchaser, or that the manner of the divestiture is not acceptable, Novartis must rescind the transaction with Amide and divest the assets to a Commission-approved buyer not later than six months from the date the Order becomes final. If Novartis fails to divest within the six months, the Commission may appoint a trustee to divest the desipramine hydrochloride, rifampin, and orphenadrine citrate ER assets.

## Analysis

The proposed remedy contains several provisions designed to ensure the successful divestiture of the desipramine hydrochloride, rifampin, and orphenadrine citrate ER assets to Amide. Novartis must provide various transitional services to enable Amide to compete against Novartis immediately following the divestiture. Novartis is obligated to provide Amide with all inventory of the three divested products and to supply Amide the two products that Amide does not currently manufacture – desipramine hydrochloride and orphenadrine citrate ER – while Amide attempts to obtain FDA approval to manufacture the products for itself in its own facility. Novartis will supply Amide with desipramine hydrochloride for two years, and Amide will have options to extend that supply for two additional one-year periods if Amide is making progress toward approval and needs the additional time to obtain FDA approval. Novartis will supply Amide with orphenadrine citrate ER for four years, and Amide will again have options to extend the supply up to two additional one-year periods as it seeks FDA approval to manufacture orphenadrine citrate for itself. Novartis is also required to provide technology transfer assistance to enable Amide to obtain all necessary FDA approvals to manufacture and sell desipramine hydrochloride, rifampin, and orphenadrine citrate for itself.

The proposed remedy does not provide for a technology transfer or supply obligation for rifampin because Amide is already in possession of the manufacturing technology, having contract manufactured generic rifampin for Novartis for several years.

The proposed remedy also incorporates the use of an Interim Trustee, experienced in obtaining regulatory approval and the manufacture of pharmaceuticals, to oversee the technology transfer and to assist Amide and the Commission in the event of difficulties with supply or delays in obtaining approval. As part of the proposed remedy, Novartis is required to execute an agreement conferring all rights and powers necessary for the Interim Trustee to satisfy his responsibilities under the Order to assure successful



Analysis

divestitures of the desipramine hydrochloride, rifampin, and orphenadrine citrate assets. Novartis has selected Francis J. Civile to be the Interim Monitor and Amide has consented to his selection. The monitor will ensure that the Commission remains informed about the status of the proposed divestitures and asset transfers.

The purpose of this analysis is to facilitate public comment on the proposed Consent Agreement, and it is not intended to constitute an official interpretation of the proposed Consent Agreement or to modify its terms in any way.

Complaint

## IN THE MATTER OF

**PENN NATIONAL GAMING, INC.**CONSENT ORDER, ETC., IN REGARD TO ALLEGED VIOLATIONS OF  
SEC. 7 OF THE CLAYTON ACT AND SEC. 5 OF THE FEDERAL TRADE  
COMMISSION ACT*Docket C-4143; File No. 0510029**Complaint, July 26, 2005--Decision, October 27, 2005*

This consent order addresses the acquisition by Respondent Penn National Gaming, Inc. – which owns and operates a number of casino facilities offering casino gaming services such as slot machines, video poker machines, and table and counter games – of Argosy Gaming Company, another casino operator. The order, among other things, requires the respondent to divest Argosy’s Baton Rouge, Louisiana, casino and associated assets to Columbia Sussex Corporation within four months, or to another acquirer approved by the Commission. An accompanying Order to Hold Separate and Maintain Assets requires the respondent to preserve Argosy’s Baton Rouge casino and associated assets as a viable, competitive, and ongoing operation until the divestiture is achieved.

*Participants*

For the Commission: *Joseph Lipinsky, Steve Mays, Robert J. Schroeder, Charles A. Harwood, Arthur Strong, Michele Cerullo, Daniel P. Ducore, Roy B. Levy, Leslie Farber and Mark Frankena.*

For the Respondent: *Janet L. McDavid, Hogan & Hartson LLP.*

**COMPLAINT**

Pursuant to the Federal Trade Commission Act and the Clayton Act, and by virtue of the authority vested in it by said Acts, the Federal Trade Commission (“Commission”), having reason to believe that Respondent Penn National Gaming, Inc. (“PNG”), a corporation subject to the jurisdiction of the Commission, has agreed to acquire Argosy Gaming Company (“Argosy”), a corporation subject to the jurisdiction of the Commission, in

Complaint

violation of Section 7 of the Clayton Act, as amended, 15 U.S.C. § 18, and Section 5 of the Federal Trade Commission Act (“FTC Act”), as amended, 15 U.S.C. § 45, and it appearing to the Commission that a proceeding in respect thereof would be in the public interest, hereby issues its Complaint, stating its charges as follows:

**I. RESPONDENT**

1. Respondent PNG is a corporation organized, existing and doing business under and by virtue of the laws of the state of Pennsylvania, with its offices and principal place of business located at 825 Berkshire Blvd., Suite 200, Wyomissing, Pennsylvania 19610.
2. Respondent PNG is an owner and operator of casinos, as well as horse racetracks and associated off-track wagering facilities (“OTWs”). The company owns or operates nine casinos located in Colorado, Illinois, Louisiana, Mississippi, West Virginia, and Ontario, Canada. It also owns two racetracks and eleven OTWs in Pennsylvania, owns one racetrack in West Virginia, and, through a joint venture, owns and operates a racetrack in New Jersey.
3. Respondent PNG is, and at all times herein has been, engaged in commerce, as “commerce” is defined in Section 1 of the Clayton Act, as amended, 15 U.S.C. § 12, and is a corporation whose business is in or affects commerce, as “commerce” is defined in Section 4 of the Federal Trade Commission Act, as amended, 15 U.S.C. § 44.

**II. THE ACQUIRED COMPANY**

4. Argosy is a corporation organized, existing and doing business under and by virtue of the laws of the state of Delaware, with its offices and principal place of business located at 219 Piasa Street, Alton, Illinois 62002.

## Complaint

5. Argosy is an owner and operator of six casinos located in Illinois, Missouri, Louisiana, Indiana and Iowa.

**III. THE ACQUISITION**

6. PNG and Argosy entered into a stock Purchase Agreement dated as of November 3, 2004 (the "Purchase Agreement") whereby PNG agreed to acquire Argosy for approximately \$2.2 billion (the "Acquisition").

**IV. THE RELEVANT MARKET**

7. For the purposes of this Complaint, the relevant line of commerce in which to analyze the effects of the Acquisition is casino services. Casino services include a combination of slot machine, video poker machine, and table gaming services, and associated amenities such as parking, food and beverages, and entertainment.
8. For the purposes of this Complaint, the Baton Rouge, Louisiana, metropolitan area is the relevant area in which to analyze the effects of the Acquisition in the relevant line of commerce.

**V. THE STRUCTURE OF THE MARKET**

9. The Baton Rouge, Louisiana, metropolitan area market for casino services is highly concentrated. PNG and Argosy are the only two suppliers of casino services in Baton Rouge, Louisiana.

**VI. ENTRY CONDITIONS**

10. Entry into the relevant market would not be timely, likely, or sufficient to deter or counteract the anticompetitive effects of the Acquisition. The state of Louisiana allows for the licensing of fifteen riverboat casinos across the state, and all fifteen licenses have been awarded. The relocation

Complaint

of an existing Louisiana riverboat casino to the Baton Rouge, Louisiana, metropolitan area to deter or counteract the anticompetitive effects described in paragraph 11 is unlikely to occur in a timely manner because of, among other things, the time and cost associated with acquiring the necessary state, parish, and city approvals.

### **VII. EFFECTS OF THE ACQUISITION**

11. The effects of the Acquisition, if consummated, may be substantially to lessen competition and to tend to create a monopoly in the relevant market in violation of Section 7 of the Clayton Act, as amended, 15 U.S.C. § 18, and Section 5 of the FTC Act, as amended, 15 U.S.C. § 45, by eliminating actual, direct, and substantial competition between PNG and Argosy through a merger to monopoly in the relevant market, thereby: (i) increasing the likelihood that PNG would exercise market power in this market; (ii) reducing existing incentives to improve casino quality or pursue casino improvements; and, (iii) increasing the likelihood that customers would be forced to pay higher prices.

### **VIII. VIOLATIONS CHARGED**

12. The Purchase Agreement described in Paragraph 6 constitutes a violation of Section 5 of the FTC Act, as amended, 15 U.S.C. § 45.
13. The Acquisition described in Paragraph 6, if consummated, would constitute a violation of Section 7 of the Clayton Act, as amended, 15 U.S.C. § 18, and Section 5 of the FTC Act, as amended, 15 U.S.C. § 45.

WHEREFORE, THE PREMISES CONSIDERED, the Federal Trade Commission on this twenty-sixth day of July, 2005, issues its Complaint against said Respondent.

## **Exhibit A**

### **PARCEL IV**

- B. A certain lot or parcel of ground together with all buildings and improvements thereon, situated in that part of the City of Baton Rouge, known as BEAUREGARD TOWN, and being LOT ELEVEN (11) of a resubdivision of SQUARE NINETEEN (19) of said Beauregard Town, made for the heirs of J. S. Cothell by L. Q. Huey, C.E., and of record in the Clerk's office of the Parish of East Baton Rouge in Plan Book One, Folio 38, measuring twenty-five (25') feet frontage on the east side of St. Philip Street by depth at the right angles of One Hundred Twenty-Eight (128') feet.
- C. A certain lot or parcel of ground, together with the buildings and improvements thereon, situated in that subdivision of the City of Baton Rouge, Parish of East Baton Rouge, Louisiana, known as BEAUREGARD TOWN, and designated according to the official plan thereof in the office of the Clerk and Recorder of said Parish as LOT TEN (10) of the resubdivision of Lots Four (4) and Five (5), SQUARE NINETEEN (19), fronting thirty-four (34) feet on Europe Street, by a depth of eighty-one (81') feet between parallel lines.

### **PARCEL VI**

One (1) certain lot or parcel of ground, together with all the buildings and improvements thereon, situated in that part of the City of Baton Rouge, State of Louisiana, known as BEAUREGARD TOWN, and designated on the official map of the City of Baton Rouge as LOT FOUR (4) OF SQUARE EIGHTEEN (18) [or Square Eighteen (18) South] said Beauregard Town, the said lot measuring sixty-four (64) feet front on the south side of Government Street by a depth at right angles and between parallel lines along the west side of St. Louis Street of one hundred six and two-thirds (106 and 2/3rds) feet, running through to the north side of France Street.

### **PARCEL VII**

Three (3) certain fractional lots or parcels of ground, together with all buildings and improvements thereon, situated in that subdivision known as BEAUREGARD TOWN, and all of said fractional lots being situated in SQUARE EIGHTEEN (18) SOUTH of said subdivision; being further described as follows: **FIRST:** The NORTH FORTY-FOUR AND TWO-THIRDS (44 2/3) FEET OF LOT TWO (2), measuring sixty-four (64) feet front on Government Street by a depth between equal and parallel lines of forty-four and 2/3 (44 2/3) feet; **SECOND:** The SOUTHWESTERN PORTION OF LOT TWO (2), measuring thirty-two (32) feet front on the north side of France Street by a depth of sixty-two (62) feet between parallel lines; **THIRD:** The NORTH FIFTY-THREE AND ONE-THIRD (53 1/3) FEET OF LOT THREE (3), measuring sixty-four (64) feet front on Government Street by a depth between parallel lines of fifty-three and 1/3 (53 1/3) feet; and **FOURTH:** The SOUTHWEST ONE-QUARTER (SW 1/4) of LOT

THREE (3), measuring thirty-two (32) feet front on France Street by a depth between equal and parallel lines of fifty-three and 1/3 (53 1/3) feet.

### **PARCEL VIII**

One (1) certain fractional lot or parcel of ground, together with all of the buildings and improvements thereon, situated in that subdivision of the City of Baton Rouge, Parish of East Baton Rouge, Louisiana, known as BEAUREGARD TOWN, and being shown on the official map of the City of Baton Rouge and Beauregard Town as the SOUTHEAST ONE-FOURTH (1/4) OF LOT THREE (3), SQUARE EIGHTEEN (18) SOUTH, BEAUREGARD TOWN, and being further shown on the official map as measuring thirty-two (32) feet front on the north side of France Street by a depth between equal and parallel lines of fifty-three and one-third (53-1/3) feet.

### **PARCEL IX**

- A. LOT FOUR (4), SQUARE NINETEEN (19), BEAUREGARD TOWN, East Baton Rouge Parish, Louisiana, as shown on the official plat of resubdivision of said Square 19, recorded in Book 101, folio 385 (Plan Book 1, folio 38, entry 2) of the Conveyance Records of East Baton Rouge Parish, Louisiana, measuring thirty-nine (39) feet front on the west side of St. Louis Street by a depth between parallel lines of one hundred twelve (112) feet.
- B. LOT FIVE (5), SQUARE NINETEEN (19), BEAUREGARD TOWN, as designated on a plat of resubdivision of Square 19, recorded in Book 101, page 385 (Plan Book 1, folio 38, entry 2) of the aforesaid Conveyance Records, measuring forty-one (41) feet front on St. Louis Street by a depth between parallel lines of ninety-six (96) feet.
- C. LOT SIX (6), SQUARE NINETEEN (19), BEAUREGARD TOWN, as designated on a plat of resubdivision of said Square 19, recorded in Book 101, folio 385 (Plan Book 1, folio 38, entry 2) of the aforesaid Conveyance records, measuring forty (40) feet front along the west side of St. Louis Street by a depth between parallel lines and along the north side of Europe Street of ninety-seven (97) feet.

Decision and Order

**DECISION AND ORDER**

The Federal Trade Commission ("Commission"), having initiated an investigation of the proposed acquisition by Respondent Penn National Gaming, Inc. ("PNG"), hereinafter referred to as "Respondent," of Argosy Gaming Company ("Argosy"), and Respondent having been furnished thereafter with a copy of a draft Complaint that the Bureau of Competition proposed to present to the Commission for its consideration and that, if issued by the Commission, would charge Respondent with violations of Section 7 of the Clayton Act, as amended, 15 U.S.C. § 18, and Section 5 of the Federal Trade Commission Act, as amended, 15 U.S.C. § 45; and

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

The Commission having thereafter considered the matter and having determined that it had reason to believe that Respondent has violated the said Acts, and that a Complaint should issue stating its charges in that respect, and having thereupon issued its Complaint and an Order to Hold Separate and Maintain Assets ("Hold Separate Order" attached to this Decision and Order as Appendix I), and having accepted the executed Consent Agreement and placed such Consent Agreement on the public record for a period of thirty (30) days for the receipt and consideration of public comments, and having modified this Decision and Order in certain respects, now in further conformity



Decision and Order

with the procedure described in Commission Rule 2.34, 16 C.F.R. § 2.34, the Commission hereby makes the following jurisdictional findings and issues the following Decision and Order ("Order"):

1. Respondent PNG is a corporation organized, existing and doing business under and by virtue of the laws of the state of Pennsylvania, with its offices and principal place of business located at 825 Berkshire Blvd., Suite 200, Wyomissing, Pennsylvania 19610.
2. The Commission has jurisdiction of the subject matter of this proceeding and of Respondent, and the proceeding is in the public interest.

**ORDER**

**I.**

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

- A. "PNG" or "Respondent" means Penn National Gaming, Inc., its directors, officers, employees, agents, attorneys, representatives, predecessors, successors, and assigns; and its parents, joint ventures, subsidiaries, divisions, groups and affiliates controlled by Penn National Gaming, Inc., and the respective directors, officers, employees, agents, representatives, predecessors, successors, and assigns of each.
- B. "Argosy" means Argosy Gaming Company a corporation organized, existing and doing business under and by virtue of the laws of the State of Delaware, with its offices and principal place of business located at 219 Piasa Street, Alton, Illinois 62002; and its joint ventures, subsidiaries, divisions, groups, and affiliates controlled by Argosy Gaming Company.

## Decision and Order

- C. "Columbia Sussex" means Columbia Sussex Corporation a corporation organized, existing and doing business under and by virtue of the laws of the State of Kentucky, with its offices and principal place of business located at 206 Grandview Drive, Fort Mitchell, Kentucky 41017; and its joint ventures, subsidiaries, divisions, groups, and affiliates controlled by Columbia Sussex Corporation and/or William J. Yung III
- D. "Commission" means the Federal Trade Commission.
- E. "Acquisition" means the proposed acquisition by merger of Argosy by Respondent pursuant to the "Agreement and Plan of Merger" dated November 3, 2004 (as amended), by and among Argosy, Respondent and a subsidiary of Respondent, whereby Respondent agreed to acquire Argosy.
- F. "Acquisition Date" means the date the Acquisition is consummated.
- G. "Actual Cost" means all direct and indirect costs, including but not limited to, third party costs, labor, materials, and appropriately allocated overhead expenses and depreciation of capital equipment used to provide the relevant assistance or service, but "Actual Cost" does not include general administrative expenses.
- H. "Application" means the forms and schedules, including, but not limited to, any information, disclosure statements, or financial statements prescribed by the LAGC upon which the applicant seeks a license, permit, or renewal or any other approval by the LAGC for the operation of a casino.
- I. "Argosy Baton Rouge Assets" means all of the outstanding shares of capital stock, limited liability company interest, and partnership interests, as the case may be, of any of the ACBR Entities, and all of the real and personal, tangible and

Decision and Order

intangible, assets of the ACBR Entities, and any other assets of Respondent or Argosy, or any of their other subsidiaries used in or related to the Argosy Casino Baton Rouge, Catfish Town, and Centroplex Centre, including, but not limited to:

1. the Argosy Casino Baton Rouge;
2. Catfish Town;
3. Centroplex;
4. all owned or leased parking structures, parking garages, and parking lots used by or related to the Argosy Casino Baton Rouge, Catfish Town, or the Centroplex, including, but not limited to the Leased Properties;
5. all personal property (including, but not limited to, deck barges), fixtures, and improvements owned, placed on, located at, used in connection with the operation of, or related to the ACBR;
6. all studies, surveys, research, audio and video recordings, data (including, but not limited to, the Argosy Casino Baton Rouge Database), information, and documents relating to marketing, advertising, promotion of the ACBR, Catfish Town, and Centroplex;
7. all leases, agreements, and contracts of any kind relating to the ACBR, Catfish Town, and Centroplex, including, but not limited to:
  - a. upon the consent of Sheraton, a license to use the Sheraton name in connection with the operation of the Centroplex; and,
  - b. leases related to the Levee Building/Argosy Landing, Maritime I Building, Beaugard Building, Armour

## Decision and Order

Building, Corner of Europe Street and St. Phillip Street in Baton Rouge, LA, S. Front Street in Baton Rouge, LA, and the dock and walkway in the Maritime Building;

8. all governmental approvals, consents, licenses, waivers, or other authorizations related to the Argosy Casino Baton Rouge;
9. all trademarks, trade names, or copyrights owned or used by the ACBR, Catfish Town, and Centroplex, including, but not limited to irrevocable licenses for the use of all trade names related to Catfish Town and Centroplex; and,
10. all books and records related to the ACBR, Catfish Town, and Centroplex, including but not limited to:
  - a. documents containing information about customers or patrons of the ACBR, Catfish Town, and Centroplex;
  - b. documents containing information about suppliers of any goods or services to the ACBR, Catfish Town, and Centroplex; and,
  - c. documents relating to government approvals required for the construction, maintenance, operation, or licensing (including, but not limited to, regulation by the LAGC) of all or any part of the ACBR (including, but not limited to, the Vessel), Catfish Town, and Centroplex.

*Provided, however,* that the Argosy Baton Rouge Assets do not include:

Decision and Order

1. any intellectual property owned, licensed to, or used by Respondent or Argosy, or their other subsidiaries, other than any and all intellectual property owned exclusively by the ACBR Entities;
  2. any contract or agreement for the service, sale, or lease of gaming machines or equipment used or located at any location other than the ACBR; or,
  3. any of the assets listed under the caption "Other Excluded Assets" in Section 2.5(a) of the Seller Disclosure Letter attached as Annex B to the Agreement to Execute Securities Purchase Agreement.
- J. "Argosy Baton Rouge Employees" means:
1. all of those individuals compensated for at least thirty-five (35) hours a week for at least forty (40) weeks within the twelve (12) month period immediately prior to the Effective Date of Divestiture whose duties related primarily to the Argosy Casino Baton Rouge; and,
  2. all of those individuals employed by Argosy (including, but not limited to, Centroplex Centre Convention Hotel, L.L.C.) within the twelve (12) month period immediately prior to the Effective Date of Divestiture in the positions of Director of Hotel Operations, Rooms Division Manager, Revenue Manager, Sales & Catering Manager, Hotel Controller, or Executive Chef.
- K. "Argosy Baton Rouge Primary Employees" means all Argosy Baton Rouge Employees:
1. who are required to be licensed or to hold a permit from either the State of Louisiana or the United States Coast Guard as a condition of employment with one or more of the ACBR Entities; and,

## Decision and Order

2. compensated at a base hourly rate of \$8.00 or more immediately prior to the Effective Date of Divestiture.
- L. “Argosy Casino Baton Rouge” or “ACBR” means the Land, Vessel, and all other rights related to and required for the operation of the Land and/or Vessel.
- M. “Argosy Casino Baton Rouge Entities” or “ACBR Entities” means Argosy of Louisiana, Inc., Jazz Enterprises, Inc., Centroplex Centre Convention Hotel, L.L.C., and Catfish Queen Partnership in Commendam.
- N. “Argosy Casino Baton Rouge Database” means all customer databases, customer lists, historical records of customers, and any other customer information collected and used by Argosy for marketing, promotional, or any other purposes related to the operation of ACBR, Catfish Town, and Centroplex;
- provided, however, Argosy Casino Baton Rouge Database does not include any customer databases, customer lists, historical records of customers, or any other customer information collected and used by Argosy solely for the marketing or promotion of any assets other than the Argosy Baton Rouge Assets.*
- O. “Argosy License” means Louisiana Riverboat License Number R011700009 issued by the LAGC.
- P. “Catfish Town” means all owned and leased real property and any servitudes appurtenant thereto, structures, fixtures, and personal property constituting, on, or relating to the property commonly know as Catfish Town.

Decision and Order

- Q. “Centroplex” means all owned and leased real property and any servitudes appurtenant thereto, structures, fixtures, and personal property constituting, on, or relating to the property commonly known as the Centroplex Centre Convention Hotel.
- R. "Commission-approved Acquirer" means any Person approved by the Commission to acquire the Argosy Baton Rouge Assets that the Respondent is required to divest pursuant to this Order.
- S. “Condition to Closing” means a condition to the closing of the divestiture specified in the Divestiture Agreement, but not including a condition that requires the delivery of a certificate or other document, or the purchase price, at or immediately prior to the closing.
- T. “Confidential Business Information” means any information relating to the Argosy Baton Rouge Assets (before or after the divestiture required by this Order) that is not in the public domain, including, but not limited to:
1. All contracts, agreements, bids, purchase orders, or other documents or information relating to any acquisitions of goods or services related to the Argosy Baton Rouge Assets;
  2. All marketing studies, marketing plans, data (including, but not limited to, the Argosy Casino Baton Rouge Database), or other documents or information relating to marketing of any of the Argosy Baton Rouge Assets;
  3. All records, applications, data, reports, correspondence, and documents or information relating to any gaming license or other regulation by any political subdivision of the State of Louisiana of the business or operation of the Argosy Baton Rouge Assets; and,

## Decision and Order

4. All records, data, or other information relating to visits, spending, or other activity by any patrons or customers of the Argosy Baton Rouge Assets.

## U. “Divestiture Agreement” means:

1. if Respondent divests the Argosy Casino Baton Rouge Assets to Columbia Sussex, the Agreement to Execute Securities Purchase Agreement (dated as of June 20, 2005) among CP Baton Rouge Casino, L.L.C., Columbia Sussex Corporation, and Penn National Gaming, Inc., and any contract, exhibit, attachment or schedule, or agreement related thereto, including, but not limited to:
  - a. the Securities Purchase Agreement attached as Annex A to the Agreement to Execute Securities Purchase Agreement and all exhibits attached thereto;
  - b. the Seller Disclosure Letter attached as Annex B to the Agreement to Execute Securities Purchase Agreement and all exhibits or schedules attached thereto;
  - c. the Letter Agreement (October 3, 2005) between Columbia Sussex Corporation, CP Baton Rouge Casino, L.L.C., Wimar Tahoe Corporation, Penn National Gaming, Inc., and Argosy Gaming Company; and,
  - d. Any modifications of any such agreement, exhibit, attachment or schedule required by the Commission pursuant to Paragraph II. of this Order; or,
2. if Respondent (or the Divestiture Trustee) divests the Argosy Casino Baton Rouge Assets to any Commission-approved Acquirer other than Columbia Sussex, any agreement that receives the prior approval of the Commission between Respondent and a Commission-approved Acquirer (or between the Divestiture Trustee and a Commission-approved Acquirer) related to the Argosy Baton Rouge Assets required to be divested pursuant to Paragraphs II or IV of this Order and the



Decision and Order

rights or assets to be licensed or otherwise made available to the Commission-approved Acquirer pursuant to Paragraph II of this Order, including, but not limited to, any agreement between the Respondent and the Commission-approved Acquirer required or permitted by or pursuant to Paragraph II. of this Order.

- V. "Divestiture Trustee" means the trustee appointed by the Commission pursuant to Paragraph IV of this Order.
- W. "Effective Date of Divestiture" means the date on which Respondent (or a Divestiture Trustee) divests to a Commission-approved Acquirer the Argosy Baton Rouge Assets completely and as required by Paragraph II or IV of this Order.
- X. "Governmental Entity" means any Federal, state, local or non-U.S. government or any court, legislature, governmental agency or governmental commission or any judicial or regulatory authority of any government.
- Y. "Hold Separate Order" means the Order to Hold Separate and Maintain Assets incorporated into and made a part of the Agreement Containing Consent Orders.
- Z. "Hold Separate Trustee" means the person appointed pursuant to Paragraph II of the Hold Separate Order in this matter.
- AA. "Land" means all real property and/or land parcels related to the operation of the Argosy Baton Rouge Assets, including, but not limited to, all buildings, hotels, parking garages, parking structures, parking lots, Catfish Town, the Sheraton Hotel, Centroplex, and any other buildings or structures located on such land.
- BB. "Leased Properties" means two parking lots on South Front Street, Baton Rouge, LA leased by Catfish through

## Decision and Order

a leasing agreement dated June 27, 2002, and as extended on August 3, 2004, between Phillips Connell Witter, as landlord, and Catfish Queen Partnership In Commendam, as tenant.

- CC. “Louisiana Gaming Control” (“LAGC”) means the Louisiana Gaming Control Board, Louisiana Department of Public Safety - Office of State Police - Gaming Enforcement Section, Louisiana Attorney General’s Office - Gaming Division, Louisiana Riverboat Gaming Commission, or any other judicial or regulatory authority responsible for granting approval(s), qualification(s), license(s), or permit(s) for any aspect of gaming in the state of Louisiana.
- DD. “Person” means any individual, partnership, joint venture, firm, corporation, association, trust, unincorporated organization, joint venture, or other business or governmental entity, and any subsidiaries, divisions, groups or affiliates thereof.
- EE. “Vessel” means the vessel known as Argosy III Riverboat, Official Number 1023758, including, but not limited to: (i) all superstructures currently constructed thereon; (ii) plans and specifications therefor; (iii) existing warranties therefor; and, (iv) all parts, spares, tools, equipment, machinery, gear, implements, broached and unbroached consumable stores, provisions for furniture, fixtures, fuel, pumps, anchors, cables, chains, apparel, rigging, tackle, fittings, accessories, appurtenances, appliances, supplies therefor, inventory parts, ramps, generators and related equipment (including, but not limited to, existing walkways), and all other appurtenances and accessories related to the vessel, whether located onboard the vessel or elsewhere;

*provided, however*, if any plans or specifications are not owned by or in the possession of Argosy, Respondent will

Decision and Order

use best efforts to obtain the consent of the owner or possessor of those plans to transfer such plans to the Commission-approved Acquirer.

**II.**

**IT IS FURTHER ORDERED** that:

- A. Respondent shall divest, absolutely and in good faith and at no minimum price, the Argosy Baton Rouge Assets to Columbia Sussex pursuant to and in accordance with the Divestiture Agreement by the earlier of: (1) three (3) days after the date upon which the LAGC grants the Application to transfer the interest of the licenses held by Catfish Town Partnership in Commendam (doing business as Argosy Casino Baton Rouge), Argosy of Louisiana, and Jazz Enterprises, Inc. to Columbia Sussex or its designee as required by the State of Louisiana to own and operate any of the Argosy Baton Rouge Assets (as determined pursuant to LAC 42:XIII.2501,2503,2505,2507); or, (2) one hundred and twenty (120) days after the date this Order becomes final.
- B. Within ten (10) days after the date Respondent signs the Agreement Containing Consent Orders in this matter, Respondent shall ensure that Columbia Sussex files a completed Application with the LAGC .
- C. Respondent shall cooperate fully and expeditiously with the Commission-Approved Acquirer and the LAGC in obtaining all approvals (including, but not limited to, approval of a transfer of interest in any of the Argosy Baton Rouge Assets) required by the State of Louisiana to own and operate any of the Argosy Baton Rouge Assets, including, but not limited to, providing the Commission-Approved Acquirer and the LAGC with any books, records, and information necessary to complete an Application or obtain a gaming license and any other approvals required by the

## Decision and Order

State of Louisiana to own and operate any of the Argosy Baton Rouge Assets.

*provided, however,* that, if Respondent has divested the Argosy Baton Rouge Assets to Columbia Sussex prior to the date this Order becomes final, and if, at the time the Commission determines to make this Order final, the Commission notifies Respondent that:

1. Columbia Sussex is not an acceptable purchaser of the Argosy Baton Rouge Assets, then Respondent shall immediately rescind the transaction with Columbia Sussex and, within six (6) months from the date the Order becomes final, shall divest the Argosy Baton Rouge Assets to a Commission-approved Acquirer absolutely and in good faith, at no minimum price, and only in a manner that receives the prior approval of the Commission; or,
2. the manner in which the divestiture was accomplished is not acceptable, the Commission may direct Respondent, or appoint a Divestiture Trustee, pursuant to Paragraph IV. of this Order, to effect within sixty (60) days such modifications (including, but not limited to, entering into additional agreements or arrangements) as may be necessary to satisfy the requirements of this Order.

*provided further* that, if the LAGC has failed to issue a decision on Columbia Sussex's Application within one hundred and twenty (120) days after this Order is final, and:

1. Respondent has not violated this Order or the Hold Separate Order;
2. Respondent has not breached the Divestiture Agreement; and,

Decision and Order

3. the sole remaining Condition to Closing (determined as if the closing were to occur one hundred and twenty (120) days after this Order is final) is the failure to obtain one or more approvals, licenses, permits, rulings or decisions by the LAGC,

Respondent shall have until six (6) months from the date this Order is final to divest the Argosy Baton Rouge Assets to Columbia Sussex in a manner that receives the prior approval of the Commission; if Respondent has not divested the Argosy Baton Rouge Assets to Columbia Sussex within six (6) months after this Order is final, the Commission may appoint a Divestiture Trustee.

*provided further* that if the LAGC has disapproved Columbia Sussex's Application less than one hundred and twenty (120) days after the date this Order becomes final, and:

1. Respondent has not violated this Order or the Hold Separate Order;
2. Respondent has not breached the Divestiture Agreement; and,
3. the sole remaining Condition to Closing (determined as if the closing were to occur on the date of such LAGC disapproval) the divestiture is the failure to obtain one or more approvals, licenses, permits, rulings or decisions by the LAGC,

Respondent shall have until six (6) months from the date of such LAGC disapproval to divest the Argosy Baton Rouge Assets to a Commission-approved Acquirer in a manner that receives the prior approval of the Commission; if Respondent has not divested the Argosy Baton Rouge

## Decision and Order

Assets within six (6) months from the date of such LAGC disapproval, the Commission may appoint a Divestiture Trustee.

- D. Subject to the prior approval of the Commission, the Divestiture Agreement shall include the following provisions and terms:
1. The Commission-approved Acquirer shall use best efforts expeditiously to file an application with the LAGC to acquire a gaming license and any other approvals required by the State of Louisiana to own and operate any of the Argosy Baton Rouge Assets;
  2. Respondent shall cooperate fully (including, but not limited to, providing to the Commission-approved Acquirer or the LAGC any books, records, and information, and any required consents) and expeditiously with the Commission-approved Acquirer in obtaining a gaming license and any other approvals required by the State of Louisiana to own and operate any of the Argosy Baton Rouge Assets;
  3. Respondent shall:
    - a. Not provide, disclose, or otherwise make available any Confidential Business Information to any Person; and,
    - b. Not use any Confidential Business Information for any reason other than as required or permitted by this Order;

*Provided, however,* that the Divestiture Agreement shall permit Respondent to use Confidential Business Information only: (i) for the purpose of performing or complying with the Respondent's obligations under this Order, the Hold Separate Order, and the Divestiture

Decision and Order

Agreement; or, (ii) for the purpose of complying with Respondent's financial, tax reporting, health, safety, and environmental obligations or any other disclosure obligations imposed by law, regulation, or judicial order (including, but not limited to, complying with laws of the state of Louisiana or requests by the LAGC).

- E. At the option of the Commission-approved Acquirer, and subject to the prior approval of the Commission, Respondent may retain the real property, together with buildings or improvements thereon, listed on Exhibit A to this Order.
- F. At the option of the Commission-approved Acquirer, and subject to the prior approval of the Commission, the Divestiture Agreement shall include the following provisions, terms, and agreements:
  - 1. A transition services agreement for a term not to exceed six (6) months following the Effective Date of Divestiture pursuant to which Respondent shall provide at its Actual Cost to the Commission-approved Acquirer such administrative, human resource, accounting, and other services as are reasonably necessary to achieve the purposes of this Order;
  - 2. Contracts, licenses, or other agreements sufficient to permit the Commission-approved Acquirer to use, for a period of one (1) year after the Effective Date of Divestiture, any tangible or intangible assets that are not included in the definition of the Argosy Baton Rouge Assets, but that have been used by the Argosy Casino Baton Rouge in some way in the twelve (12) months preceding the date this Order is accepted for public comment;
  - 3. Contracts, licenses, or other agreements sufficient to permit the Commission-approved Acquirer to obtain the

## Decision and Order

equivalent economic and competitive benefit of any rights or obligations of the Argosy Baton Rouge Assets under any existing contract, license, or other agreement that, for any reason, Respondent did not divest to the Commission-approved Acquirer, which contract, license, or other agreement is reasonably necessary to achieve the purposes of this Order; and,

4. A license for no longer than six (6) months for the use of the Argosy name and tradenames.
- G. Until the Effective Date of Divestiture of the Argosy Baton Rouge Assets, Respondent shall take such actions as are necessary to maintain the viability and marketability of the Argosy Baton Rouge Assets and to prevent the destruction, removal, wasting, deterioration, or impairment of the Argosy Baton Rouge Assets, except for ordinary wear and tear (including, but not limited to, regular repair and maintenance efforts, continuation of any planned capital expenditures, and marketing and promotional programs).
- H. Respondent shall:
1. not interfere, directly or indirectly, with the hiring or employing by a Commission-approved Acquirer of the Argosy Baton Rouge Employees, and shall remove any impediments or incentives within the control of Respondent and Argosy that may deter these employees from accepting employment with a Commission-approved Acquirer, including, but not limited to, any non-compete provisions of employment or other contracts with Respondent or Argosy that would affect the ability or incentive of those individuals to be employed by a Commission-approved Acquirer. In addition, Respondent shall not make any counteroffer to



Decision and Order

- a Argosy Baton Rouge Employee who receives a written offer of employment from a Commission-approved Acquirer;
2. provide all the Argosy Baton Rouge Employees with reasonable financial incentives to continue in their positions until the Effective Date of Divestiture. Such incentives shall include, but are not limited to, a continuation of all employee benefits, including regularly scheduled raises and bonuses and a vesting of all pension benefits (as permitted by law and for those Argosy Baton Rouge Employees covered by a pension plan), offered by Respondent until the Effective Date of Divestiture;
  3. not, for a period of eighteen (18) months following the Effective Date of Divestiture, directly or indirectly, employ or enter into a contract for the services of any Argosy Baton Rouge Primary Employees;

*Provided, however,* that this Paragraph II.H. shall not prohibit Respondent from entering into a contract for the services of, making offers of employment to, or employing or contracting with any Argosy Baton Rouge Primary Employees:

- a. when a Commission-approved Acquirer has notified Respondent in writing that the Commission-approved Acquirer:
  - (1) does not intend to make an offer of employment to that employee; or,
  - (2) has terminated that employee without cause; or,
- b. when that employee voluntarily has declined to contract with or continue employment with the Commission-approved Acquirer, and the Commission-approved Acquirer has:
  - (1) not offered to contract with or employ that employee in a position with the same or similar

## Decision and Order

- duties as the position occupied by that employee immediately prior to the Effective Date of Divestiture; or,
- (2) not offered that employee the same or increased monetary compensation and a substantially similar or better package of benefits and other compensation as the employee received immediately prior to the Effective Date of Divestiture;
4. No later than three (3) days after the Acquisition Date:
- a. circulate to all directors and managers of the Held Separate Business, and to Respondent's or Argosy's employees who have responsibilities associated with the Held Separate Business, a copy of the Hold Separate Order and this Order; and,
- b. circulate, in lieu of Exhibit A to the Hold Separate Order, a document in the form of Exhibit B to this Order to all employees of the Held Separate Business.
- I. Prior to the Effective Date of Divestiture, Respondent shall secure all consents and waivers from all Persons that are necessary for the divestiture of the Argosy Baton Rouge Assets to a Commission-approved Acquirer.
- J. Respondent shall comply with all terms of the Divestiture Agreement, and any breach by Respondent of any term of the Divestiture Agreement shall constitute a violation of this Order. If any term of the Divestiture Agreement varies from the terms of this Order ("Order Term"), then to the extent that Respondent cannot fully comply with both terms, the Order Term shall determine Respondent's obligations under this Order. Notwithstanding any paragraph, section, or other provision of the Divestiture Agreement, any failure to meet any condition precedent to closing (whether waived or not) or any modification of the Divestiture Agreement, without the prior approval of the Commission, shall constitute a failure to comply with this Order.

Decision and Order

- K. The purpose of the divestiture of the Argosy Baton Rouge Assets is to ensure the continuing, viable, and competitive operation of the Argosy Baton Rouge Assets in the same manner and in the same business in which the Argosy Baton Rouge Assets were engaged at the time of the announcement of the proposed Acquisition, and to remedy the lessening of competition resulting from the Acquisition as alleged in the Commission's Complaint.

**III.**

**IT IS FURTHER ORDERED** that:

- A. Respondent shall:
1. Not provide, disclose, or otherwise make available any Confidential Business Information to any Person; and,
  2. Not use any Confidential Business Information for any reason or purpose other than as required or permitted by this Order.
- B. Notwithstanding Paragraph III.A. of this Order and subject to the Hold Separate Order, Respondent shall use Confidential Business Information only: (i) for the purpose of performing and complying with Respondent's obligations under this Order, the Hold Separate Order, or the Divestiture Agreement; or, (ii) for the purpose of complying with Respondent's financial, tax reporting, health, safety, and environmental obligations or any other disclosure obligations imposed by law, regulation or judicial order (including, but not limited to, complying with laws of the state of Louisiana or requests by the LAGC).

Decision and Order

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

- A. If Respondent has not fully complied with the obligations to divest the Argosy Baton Rouge Assets as required by Paragraph II of this Order, the Commission may appoint a Divestiture Trustee to divest the Argosy Baton Rouge Assets in a manner that satisfies the requirements of Paragraph II. In the event that the Commission or the Attorney General brings an action pursuant to § 5(l) of the Federal Trade Commission Act, 15 U.S.C. § 45(l), or any other statute enforced by the Commission, Respondent shall consent to the appointment of a Divestiture Trustee in such action to divest the Argosy Baton Rouge Assets. Neither the appointment of a Divestiture Trustee nor a decision not to appoint a Divestiture Trustee under this Paragraph shall preclude the Commission or the Attorney General from seeking civil penalties or any other relief available to it, including a court-appointed Divestiture Trustee, pursuant to § 5(l) of the Federal Trade Commission Act, or any other statute enforced by the Commission, for any failure by Respondent to comply with this Order.
  
- B. The Commission shall select the Divestiture Trustee, subject to the consent of Respondent, which consent shall not be unreasonably withheld. The Divestiture Trustee shall be a person with experience and expertise in acquisitions and divestitures. If Respondent has not opposed, in writing, including the reasons for opposing, the selection of any proposed Divestiture Trustee within ten (10) days after notice by the staff of the Commission to Respondent of the identity of any proposed Divestiture Trustee, Respondent shall be deemed to have consented to the selection of the proposed Divestiture Trustee.

Decision and Order

- C. Not later than ten (10) days after the appointment of a Divestiture Trustee, Respondent shall execute a trust agreement that, subject to the prior approval of the Commission, transfers to the Divestiture Trustee all rights and powers necessary to permit the Divestiture Trustee to effect the divestiture required by this Order.
- D. If a Divestiture Trustee is appointed by the Commission or a court pursuant to this Paragraph IV, Respondent shall consent to the following terms and conditions regarding the Divestiture Trustee's powers, duties, authority, and responsibilities:
1. Subject to the prior approval of the Commission, the Divestiture Trustee shall have the exclusive power and authority to divest the Argosy Baton Rouge Assets.
  2. The Divestiture Trustee shall have one (1) year after the date the Commission approves the trust agreement described herein to accomplish the divestiture, which shall be subject to the prior approval of the Commission. If, however, at the end of the one (1) year period, the Divestiture Trustee has submitted a plan of divestiture or believes that the divestiture can be achieved within a reasonable time, the divestiture period may be extended by the Commission; *provided, however*, the Commission may extend the divestiture period only two (2) times.
  3. Subject to any demonstrated legally recognized privilege, the Divestiture Trustee shall have full and complete access to the personnel, books, records and facilities related to the relevant assets that are required to be divested by this Order and to any other relevant information (including, but not limited to, information related to any regulation of the Argosy Baton Rouge Assets by the LAGC), as the Divestiture Trustee may request. Respondent shall develop such financial or other information as the Divestiture Trustee may request

## Decision and Order

and shall cooperate with the Divestiture Trustee. Respondent shall take no action to interfere with or impede the Divestiture Trustee's accomplishment of the divestiture. Any delays in divestiture caused by Respondent shall extend the time for divestiture under this Paragraph IV in an amount equal to the delay, as determined by the Commission.

4. The Divestiture Trustee shall use commercially reasonable best efforts to negotiate the most favorable price and terms available in each contract that is submitted to the Commission, subject to Respondent's absolute and unconditional obligation to divest expeditiously and at no minimum price. The divestiture shall be made in the manner and to an acquirer as required by this Order; *provided, however*, if the Divestiture Trustee receives bona fide offers from more than one acquiring entity, and if the Commission determines to approve more than one such acquiring entity, the Divestiture Trustee shall divest to the acquiring entity selected by Respondent from among those approved by the Commission; and, *provided further, however*, that Respondent shall select such entity within five (5) days after receiving notification of the Commission's approval.
5. The Divestiture Trustee shall serve, without bond or other security, at the cost and expense of Respondent, on such reasonable and customary terms and conditions as the Commission or a court may set. The Divestiture Trustee shall have the authority to employ, at the cost and expense of Respondent, such consultants, accountants, attorneys, investment bankers, business brokers, appraisers, and other representatives and assistants as are necessary to carry out the Divestiture Trustee's duties and responsibilities. The Divestiture Trustee shall account for all monies derived from the divestiture and all expenses incurred. After the approval

Decision and Order

by the Commission of the account of the Divestiture Trustee, including fees for the Divestiture Trustee's services, all remaining monies shall be paid at the direction of the Respondent, and the Divestiture Trustee's power shall be terminated. The compensation of the Divestiture Trustee shall be based at least in significant part on a commission arrangement contingent on the divestiture of all of the relevant assets that are required to be divested by this Order.

6. Respondent shall indemnify the Divestiture Trustee and hold the Divestiture Trustee harmless against any losses, claims, damages, liabilities, or expenses arising out of, or in connection with, the performance of the Divestiture Trustee's duties, including all reasonable fees of counsel and other expenses incurred in connection with the preparation for, or defense of, any claim, whether or not resulting in any liability, except to the extent that such losses, claims, damages, liabilities, or expenses result from misfeasance, gross negligence, willful or wanton acts, or bad faith by the Divestiture Trustee.
7. The Divestiture Trustee shall have no obligation or authority to operate or maintain the relevant assets required to be divested by this Order; *provided, however,* that the Divestiture Trustee appointed pursuant to Paragraph IV of this Order may be the same Person appointed as Hold Separate Trustee pursuant to the relevant provisions of the Hold Separate Order in this matter.
8. The Divestiture Trustee shall report in writing to Respondent and to the Commission every sixty (60) days concerning the Divestiture Trustee's efforts to accomplish the divestiture.
9. Respondent may require the Divestiture Trustee and each of the Divestiture Trustee's consultants, accountants,

## Decision and Order

attorneys and other representatives and assistants to sign a customary confidentiality agreement; *provided, however,* such agreement shall not restrict the Divestiture Trustee from providing any information to the Commission or to the LAGC.

- E. If the Commission determines that a Divestiture Trustee has ceased to act or failed to act diligently, the Commission may appoint a substitute Divestiture Trustee in the same manner as provided in the Paragraph IV.
- F. The Commission or, in the case of a court-appointed Divestiture Trustee, the court, may on its own initiative or at the request of the Divestiture Trustee issue such additional orders or directions as may be necessary or appropriate to accomplish the divestiture required by this Order.

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

- A. Within five (5) days after the Acquisition, Respondent shall submit to the Commission a letter certifying the date on which the Acquisition occurred.
- B. Within five (5) days after the earlier of the LAGC's approval of a motion to transfer interest in the Argosy License, or the LAGC's issuance of a notice of decision to Respondent or the Commission-approved Acquirer, Respondent shall submit to the Commission a letter certifying the date on which the approval was granted or the notice was issued.
- C. Within thirty (30) days after the date this Order becomes final, and every sixty (60) days thereafter until Respondent has fully complied with Paragraphs II and IV of this Order, Respondent shall submit to the Commission a verified written report setting forth in detail the manner and form in



Decision and Order

which it intends to comply, is complying, and has complied with this Order. Respondent shall submit at the same time a copy of its report concerning compliance with this Order to the Hold Separate Trustee, if any Hold Separate Trustee has been appointed pursuant to the Hold Separate Order in this matter. Respondent shall include in its reports, among other things that are required from time to time, a full description of the efforts being made to comply with the relevant Paragraphs of the Order, including a description of all substantive contacts or negotiations related to the divestiture of the relevant assets and the identity of all Persons (including, but not limited to, the LAGC) contacted. Respondent shall include in its report copies of all written communications to and from such Persons, all internal memoranda, and all reports and recommendations concerning completing the obligations.

- D. One (1) year after the date this Order becomes final, annually until Respondent has complied fully with its obligations under Paragraphs II and IV of this Order, and at other times as the Commission may require, Respondent shall file a verified written report with the Commission setting forth in detail the manner and form in which it has complied and is complying with the Order.

**VI.**

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

Decision and Order

**VII.**

**IT IS FURTHER ORDERED** that, for purposes of determining or securing compliance with this Order, and subject to any legally recognized privilege, and upon written request with reasonable notice, Respondent shall permit any duly authorized representative of the Commission:

- A. access, during business office hours of Respondent, in the presence of counsel, and as permitted by and in accordance with the laws, rules and regulations of the LAGC, to all facilities and access to inspect and copy all books, ledgers, accounts, correspondence, memoranda and all other records and documents in the possession or under the control of Respondent related to compliance with this Order; and
- B. upon five (5) days' notice to Respondent and without restraint or interference from Respondent, to interview officers, directors, or employees of Respondent, who may have counsel present, regarding such matters.

**VIII.**

**IT IS FURTHER ORDERED** that this Order shall terminate on October 27, 2015.

## **Exhibit A**

### **PARCEL IV**

- B. A certain lot or parcel of ground together with all buildings and improvements thereon, situated in that part of the City of Baton Rouge, known as BEAUREGARD TOWN, and being LOT ELEVEN (11) of a resubdivision of SQUARE NINETEEN (19) of said Beauregard Town, made for the heirs of J. S. Cothell by L. Q. Huey, C.E., and of record in the Clerk's office of the Parish of East Baton Rouge in Plan Book One, Folio 38, measuring twenty-five (25') feet frontage on the east side of St. Philip Street by depth at the right angles of One Hundred Twenty-Eight (128') feet.
- C. A certain lot or parcel of ground, together with the buildings and improvements thereon, situated in that subdivision of the City of Baton Rouge, Parish of East Baton Rouge, Louisiana, known as BEAUREGARD TOWN, and designated according to the official plan thereof in the office of the Clerk and Recorder of said Parish as LOT TEN (10) of the resubdivision of Lots Four (4) and Five (5), SQUARE NINETEEN (19), fronting thirty-four (34) feet on Europe Street, by a depth of eighty-one (81') feet between parallel lines.

### **PARCEL VI**

One (1) certain lot or parcel of ground, together with all the buildings and improvements thereon, situated in that part of the City of Baton Rouge, State of Louisiana, known as BEAUREGARD TOWN, and designated on the official map of the City of Baton Rouge as LOT FOUR (4) OF SQUARE EIGHTEEN (18) [or Square Eighteen (18) South] said Beauregard Town, the said lot measuring sixty-four (64) feet front on the south side of Government Street by a depth at right angles and between parallel lines along the west side of St. Louis Street of one hundred six and two-thirds (106 and 2/3rds) feet, running through to the north side of France Street.

### **PARCEL VII**

Three (3) certain fractional lots or parcels of ground, together with all buildings and improvements thereon, situated in that subdivision known as BEAUREGARD TOWN, and all of said fractional lots being situated in SQUARE EIGHTEEN (18) SOUTH of said subdivision; being further described as follows: FIRST: The NORTH FORTY-FOUR AND TWO-THIRDS (44 2/3) FEET OF LOT TWO (2), measuring sixty-four (64) feet front on Government Street by a depth between equal and parallel lines of forty-four and 2/3 (44 2/3) feet; SECOND: The SOUTHWESTERN PORTION OF LOT TWO (2), measuring thirty-two (32) feet front on the north side of France Street by a depth of sixty-two (62) feet between parallel lines; THIRD: The NORTH FIFTY-THREE AND ONE-THIRD (53 1/3) FEET OF LOT THREE (3), measuring sixty-four (64) feet front on Government Street by a depth between parallel lines of fifty-three and 1/3 (53 1/3) feet; and FOURTH: The SOUTHWEST ONE-QUARTER (SW 1/4) of LOT

THREE (3), measuring thirty-two (32) feet front on France Street by a depth between equal and parallel lines of fifty-three and 1/3 (53 1/3) feet.

### **PARCEL VIII**

One (1) certain fractional lot or parcel of ground, together with all of the buildings and improvements thereon, situated in that subdivision of the City of Baton Rouge, Parish of East Baton Rouge, Louisiana, known as BEAUREGARD TOWN, and being shown on the official map of the City of Baton Rouge and Beauregard Town as the SOUTHEAST ONE-FOURTH (1/4) OF LOT THREE (3), SQUARE EIGHTEEN (18) SOUTH, BEAUREGARD TOWN, and being further shown on the official map as measuring thirty-two (32) feet front on the north side of France Street by a depth between equal and parallel lines of fifty-three and one-third (53-1/3) feet.

### **PARCEL IX**

- A. LOT FOUR (4), SQUARE NINETEEN (19), BEAUREGARD TOWN, East Baton Rouge Parish, Louisiana, as shown on the official plat of resubdivision of said Square 19, recorded in Book 101, folio 385 (Plan Book 1, folio 38, entry 2) of the Conveyance Records of East Baton Rouge Parish, Louisiana, measuring thirty-nine (39) feet front on the west side of St. Louis Street by a depth between parallel lines of one hundred twelve (112) feet.
- B. LOT FIVE (5), SQUARE NINETEEN (19), BEAUREGARD TOWN, as designated on a plat of resubdivision of Square 19, recorded in Book 101, page 385 (Plan Book 1, folio 38, entry 2) of the aforesaid Conveyance Records, measuring forty-one (41) feet front on St. Louis Street by a depth between parallel lines of ninety-six (96) feet.
- C. LOT SIX (6), SQUARE NINETEEN (19), BEAUREGARD TOWN, as designated on a plat of resubdivision of said Square 19, recorded in Book 101, folio 385 (Plan Book 1, folio 38, entry 2) of the aforesaid Conveyance records, measuring forty (40) feet front along the west side of St. Louis Street by a depth between parallel lines and along the north side of Europe Street of ninety-seven (97) feet.

**[to be inserted]**, 2005

From: Peter M. Carlino

To: All Argosy Casino-Baton Rouge Employees

Subject: FTC Order to Hold Separate and Maintain Assets

As you may know, on **[to be inserted]**, 2005, Penn National Gaming, Inc. ("Penn") completed its acquisition of Argosy Gaming Company ("Argosy"), and executed an agreement with Columbia Sussex Corporation ("Columbia Sussex") to divest the casino property commonly known as the Argosy Casino-Baton Rouge ("ACBR"). In our press release, we confirmed that Penn elected to divest the ACBR in order to expedite securing Federal Trade Commission ("FTC") and state gaming board approval of the Argosy merger. Penn also announced that the FTC accepted an Agreement Containing Consent Orders (the "Orders"), which incorporates a Decision and Order and an Order to Hold Separate and Maintain Assets. If you have not seen these Orders, you may find them on the FTC's home page at <http://www.ftc.gov/opa/2005/07/pngaming.htm>. Copies are also available at the Human Resources Office, located in Maritime II.

Generally, the Orders require Penn to divest the ACBR, and to hold separate and maintain the casino property from the other Penn properties pending the completion of sale to Columbia Sussex. The Orders also require Penn to appoint a Hold Separate Trustee, who is responsible for managing the business and operation of the ACBR, and for maintaining its independence from Penn prior to the sale to Columbia Sussex. Frank Quigley has agreed to serve as the Hold Separate Trustee of the ACBR during this interim period.

I'm sure that many of you – as well as your families and friends – have questions and concerns about this matter, and I'd like to provide you with some thoughts as you go about the business of serving customers during the course of your day-to-day jobs.

I want to emphasize that during this Hold Separate Period – that is, the time period between Penn’s acquisition of Argosy and its sale of the ACBR to Columbia Sussex – the ACBR should continue to operate as efficiently and as competitively as it has always operated, and should continue to view Penn’s Casino Rouge as a key competitor. In addition, confidential or proprietary information regarding the ACBR, which includes financial results, marketing strategies and customer information, should continue to remain confidential, and should not be discussed or otherwise shared with anyone employed by or associated with Penn.

Penn is very proud of its reputation for and track record of excellence and commitment to upholding the highest ethical standards. We are dedicated to compliance with all applicable antitrust laws in all of our activities and locations.

We understand that you may have additional questions about this matter, and that you may receive questions from customers and others who have read media reports about the Argosy merger and ACBR divestiture. If you have questions about the FTC Orders or their application to your work, please contact Richard Williams at Extension 6043. If you receive any calls from members of the media, please refer the queries to Eric Schippers, Vice President of Public Affairs, at 610-378-8321; [eric.schippers@pngaming.com](mailto:eric.schippers@pngaming.com). If you receive any calls from customers, please refer them to Frank Quigley.

I appreciate your efforts, and want to thank you for continuing to work diligently to service customers to the best of your ability.

Best regards,  
Peter M. Carlino

Order

IN THE MATTER OF

**PENN NATIONAL GAMING, INC.**

**ORDER TO HOLD SEPARATE AND MAINTAIN ASSETS**

The Federal Trade Commission (“Commission”), having initiated an investigation of the proposed acquisition by Respondent Penn National Gaming, Inc. (“PNG”) of Argosy Gaming Company (“Argosy”), and Respondent having been furnished thereafter with a copy of the draft Complaint that the Bureau of Competition proposed to present to the Commission for its consideration and that, if issued by the Commission, would charge Respondent with violations of Section 7 of the Clayton Act, as amended, 15 U.S.C. § 18, and Section 5 of the Federal Trade Commission Act, as amended, 15 U.S.C. § 45; and

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

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

## Order

following jurisdictional findings, and issues this Order to Hold Separate and Maintain Assets (“Hold Separate Order”).

1. Respondent Penn National Gaming, Inc., is a corporation organized, existing, and doing business under and by virtue of the laws of the Commonwealth of Pennsylvania, with its office and principal place of business located at 825 Berkshire Blvd., Suite 200, Wyomissing, Pennsylvania 19610.
2. The Federal Trade Commission has jurisdiction of the subject matter of this proceeding and of Respondent, and the proceeding is in the public interest.

**ORDER****I.**

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

- A. "PNG" or "Respondent" means Penn National Gaming, Inc., its directors, officers, employees, agents, attorneys, representatives, predecessors, successors, and assigns; and its parents, joint ventures, subsidiaries, divisions, groups and affiliates controlled by Penn National Gaming, Inc., and the respective directors, officers, employees, agents, representatives, predecessors, successors, and assigns of each.
- B. "Argosy" means Argosy Gaming Company a corporation organized, existing and doing business under and by virtue of the laws of the State of Delaware, with its offices and principal place of business located at 219 Piasa Street, Alton, Illinois 62002; and its joint ventures, subsidiaries, divisions, groups, and affiliates controlled by Argosy Gaming Company.



Order

- C. “Commission” means the Federal Trade Commission.
- D. “Respondent” means Penn National Gaming, Inc.
- E. "Acquisition" means the proposed acquisition by merger of Argosy by Respondent pursuant to the “Agreement and Plan of Merger” dated November 3, 2004 (as amended), by and among Argosy, Respondent and a subsidiary of Respondent, whereby Respondent agreed to acquire Argosy.
- F. “Acquisition Date” means the date the Acquisition is consummated.
- G. “Argosy Baton Rouge Assets” means all of the outstanding shares of capital stock, limited liability company interest, and partnership interests, as the case may be, of any of the ACBR Entities, and all of the real and personal, tangible and intangible, assets of the ACBR Entities, and any other assets of Respondent or Argosy, or any of their other subsidiaries used in or related to the Argosy Casino Baton Rouge, Catfish Town, and Centroplex Centre, including, but not limited to:
  - 1. the Argosy Casino Baton Rouge;
  - 2. Catfish Town;
  - 3. Centroplex;
  - 4. all owned or leased parking structures, parking garages, and parking lots used by or related to the Argosy Casino Baton Rouge, Catfish Town, or the Centroplex, including, but not limited to the Leased Properties;
  - 5. all personal property (including, but not limited to, deck barges), fixtures, and improvements owned, placed on, located at, used in connection with the operation of, or related to the ACBR;

## Order

6. all studies, surveys, research, audio and video recordings, data (including, but not limited to, the Argosy Casino Baton Rouge Database), information, and documents relating to marketing, advertising, promotion of the ACBR, Catfish Town, and Centrolplex;
7. all leases, agreements, and contracts of any kind relating to the ACBR, Catfish Town, and Centrolplex, including, but not limited to:
  - a. upon the consent of Sheraton, a license to use the Sheraton name in connection with the operation of the Centrolplex; and,
  - b. leases related to the Levee Building/Argosy Landing, Maritime I Building, Beauregard Building, Armour Building, Corner of Europe Street and St. Phillip Street in Baton Rouge, LA, S. Front Street in Baton Rouge, LA, and the dock and walkway in the Maritime Building;
8. all governmental approvals, consents, licenses, waivers, or other authorizations related to the Argosy Casino Baton Rouge;
9. all trademarks, trade names, or copyrights owned or used by the ACBR, Catfish Town, and Centrolplex, including, but not limited to irrevocable licenses for the use of all trade names related to Catfish Town and Centrolplex; and,
10. all books and records related to the ACBR, Catfish Town, and Centrolplex, including but not limited to:
  - a. documents containing information about customers or patrons of the ACBR, Catfish Town, and Centrolplex;
  - b. documents containing information about suppliers of any goods or services to the ACBR, Catfish Town,

Order

and Centroplex; and,

- c. documents relating to government approvals required for the construction, maintenance, operation, or licensing (including, but not limited to, regulation by the LAGC) of all or any part of the ACBR (including, but not limited to, the Vessel), Catfish Town, and Centroplex.

*Provided, however,* that the Argosy Baton Rouge Assets do not include:

1. any intellectual property owned, licensed to, or used by Respondent or Argosy, or their other subsidiaries, other than any and all intellectual property owned exclusively by the ACBR Entities;
2. any contract or agreement for the service, sale, or lease of gaming machines or equipment used or located at any location other than the ACBR; or
3. any of the assets listed under the caption "Other Excluded Assets" in Section 2.5(a) of the Seller Disclosure Letter attached as Annex B to the Agreement to Execute Securities Purchase Agreement.

H. "Argosy Baton Rouge Employees" means:

1. all of those individuals compensated for at least thirty-five (35) hours a week for at least forty (40) weeks within the twelve (12) month period immediately prior to the Effective Date of Divestiture whose duties related primarily to the Argosy Casino Baton Rouge; and,

## Order

2. all of those individuals employed by Argosy (including, but not limited to, Centroplex Centre Convention Hotel, L.L.C.) within the twelve (12) month period immediately prior to the Effective Date of Divestiture in the positions of Director of Hotel Operations, Rooms Division Manager, Revenue Manager, Sales & Catering Manager, Hotel Controller, or Executive Chef.
- I. "Argosy Baton Rouge Primary Employees" means all Argosy Baton Rouge Employees:
    1. Who are required to be licensed or to hold a permit from either the State of Louisiana or the United States Coast Guard as a condition of employment with one or more of the ACBR Entities; and,
    2. Compensated at a base hourly rate of \$8.00 or more immediately prior to the Effective Date of Divestiture.
  - J. "Argosy Casino Baton Rouge" or "ACBR" means the Land, Vessel, and all other rights related to and required for the operation of the Land and/or Vessel.
  - K. "Argosy Casino Baton Rouge Entities" or "ACBR Entities" means Argosy of Louisiana, Inc., Jazz Enterprises, Inc., Centroplex Centre Convention Hotel, L.L.C., and Catfish Queen Partnership in Commendam.
  - L. "Argosy Casino Baton Rouge Database" means all customer databases, customer lists, historical records of customers, and any other customer information collected and used by Argosy for marketing, promotional, or any other purposes related to the operation of ACBR, Catfish Town, and Centroplex;  
  
*provided, however, Argosy Casino Baton Rouge Database does not include any customer databases, customer lists, historical records of customers, or any other customer*

Order

information collected and used by Argosy solely for the marketing or promotion of any assets other than the Argosy Baton Rouge Assets.

- M. “Commission-approved Acquirer” means any Person approved by the Commission to acquire the Argosy Baton Rouge Assets pursuant to Paragraph II of the Decision and Order.
- N. “Confidential Business Information” means any information relating to the Argosy Baton Rouge Assets (before or after the divestiture required by this Order) that is not in the public domain, including, but not limited to:
1. All contracts, agreements, bids, purchase orders, or other documents or information relating to any acquisitions of goods or services related to the Argosy Baton Rouge Assets;
  2. All marketing studies, marketing plans, data (including, but not limited to, the Argosy Casino Baton Rouge Database), or other documents or information relating to marketing of any of the Argosy Baton Rouge Assets;
  3. All records, applications, data, reports, correspondence, and documents or information relating to any gaming license or other regulation by any political subdivision of the State of Louisiana of the business or operation of the Argosy Baton Rouge Assets; and,
  4. All records, data, or other information relating to visits, spending, or other activity by any patrons or customers of the Argosy Baton Rouge Assets.
- O. “Decision and Order” means:
1. until the issuance of a final Decision and Order by the Commission, the proposed Decision and Order

## Order

incorporated into and made a part of the Consent Agreement; or,

2. following the issuance of a final Decision and Order by the Commission, the Decision and Order issued by the Commission.

P. "Divestiture Agreement" means:

1. if Respondent divests the Argosy Casino Baton Rouge Assets to Columbia Sussex, the Agreement to Execute Securities Purchase Agreement (dated as of June 20, 2005) among CP Baton Rouge Casino, L.L.C., Columbia Sussex Corporation, and Penn National Gaming, Inc., and any contract, exhibit, attachment or schedule, or agreement related thereto, including, but not limited to:
  - a. the Securities Purchase Agreement attached as Annex A to the Agreement to Execute Securities Purchase Agreement and all exhibits attached thereto;
  - b. the Seller Disclosure Letter attached as Annex B to the Agreement to Execute Securities Purchase Agreement and all exhibits or schedules attached thereto; and,
  - c. Any modifications of any such agreement, exhibit, attachment or schedule required by the Commission pursuant to Paragraph II of the Decision and Order; or
2. if Respondent (or the Divestiture Trustee) divests the Argosy Casino Baton Rouge Assets to any Commission-approved Acquirer other than Columbia Sussex, any agreement that receives the prior approval of the Commission between Respondent and a Commission-approved Acquirer (or between the Divestiture Trustee and a Commission-approved Acquirer) related to the Argosy Baton Rouge Assets required to be divested pursuant to Paragraphs II or IV of the Decision and Order and the rights or assets to be licensed or otherwise made available to the Commission-approved Acquirer pursuant

Order

to Paragraph II of the Decision and Order, including, but not limited to, any agreement between the Respondent and the Commission-approved Acquirer required or permitted by or pursuant to Paragraph II of the Decision and Order.

- Q. “Divestiture Trustee” means the divestiture trustee(s) appointed pursuant to Paragraph IV of the Decision and Order.
- R. "Effective Date of Divestiture" means the date on which Respondent (or a Divestiture Trustee) divests to a Commission-approved Acquirer the Argosy Baton Rouge Assets completely and as required by Paragraph II or IV of the Decision and Order.
- S. “Held Separate Business” means the Argosy Baton Rouge Assets.
- T. “Hold Separate Period” means the time period during which the Hold Separate Order is in effect, which shall begin on the date that the Acquisition is consummated and terminated pursuant to Paragraph V hereof.
- U. “Hold Separate Trustee” means the trustee appointed pursuant to Paragraph II of this Hold Separate Order.
- V. “Land” means all real property and/or land parcels related to the operation of the Argosy Baton Rouge Assets, including, but not limited to, all buildings, hotels, parking garages, parking structures, parking lots, Catfish Town, the Sheraton Hotel, Centroplex, and any other buildings or structures located on such land.
- W. “Leased Properties” means two parking lots on South Front Street, Baton Rouge, LA, leased by Catfish through a leasing agreement dated June 27, 2002, and as extended on August 3, 2004, between Phillips Connell Witter, as

## Order

landlord, and Catfish Queen Partnership In Commendam, as tenant.

- X. “Louisiana Gaming Control” (“LAGC”) means the Louisiana Gaming Control Board, Louisiana Department of Public Safety - Office of State Police - Gaming Enforcement Section, Louisiana Attorney General’s Office - Gaming Division, Louisiana Riverboat Gaming Commission, or any other judicial or regulatory authority responsible for granting approval(s), qualification(s), license(s), or permit(s) for any aspect of gaming in the state of Louisiana.
- Y. “Person” means any individual, partnership, joint venture, firm, corporation, association, trust, unincorporated organization, joint venture, or other business or governmental entity, and any subsidiaries, divisions, groups or affiliates thereof.
- Z. “Vessel” means the vessel known as Argosy III Riverboat, Official Number 1023758, including, but not limited to: (i) all superstructures currently constructed thereon; (ii) plans and specifications therefor; (iii) existing warranties therefor; and (iv) all parts, spares, tools, equipment, machinery, gear, implements, broached and unbroached consumable stores, provisions for furniture, fixtures, fuel, pumps, anchors, cables, chains, apparel, rigging, tackle, fittings, accessories, appurtenances, appliances, supplies therefor, inventory parts, ramps, generators and related equipment (including, but not limited to, existing walkways), and all other appurtenances and accessories related to the vessel, whether located onboard the vessel or elsewhere;
- provided, however,* if any plans or specifications are not owned by or in the possession of Argosy, Respondent will use best efforts to obtain the consent of the owner or possessor of those plans to transfer such plans to the Commission-approved Acquirer.



Order

**II.**

**IT IS FURTHER ORDERED THAT:**

- A. During the Hold Separate Period, Respondent shall hold the Held Separate Business separate, apart, and independent as required by this Hold Separate Order and shall vest the Held Separate Business with all rights, powers, and authority necessary to conduct its business; Respondent shall not exercise direction or control over, or influence directly or indirectly, the Held Separate Business or any of its operations, or the Hold Separate Trustee, except to the extent that Respondent must exercise direction and control over the Held Separate Business as is necessary to assure compliance with this Hold Separate Order, the Consent Agreement, the Decision and Order, and with all applicable laws (including, but not limited to, compliance with the laws of the state of Louisiana and all requests by the LAGC), including, in consultation with the Hold Separate Trustee, continued oversight of the Held Separate Business's compliance with policies and standards concerning the safety, health, and environmental aspects of its operations and the integrity of its financial controls; and Respondent shall have the right to defend any legal claims, investigations, or enforcement actions threatened or brought against any Held Separate Business.
- B. Until the Effective Date of Divestiture, Respondent shall take such actions as are necessary to maintain the viability and marketability of the Held Separate Business and to prevent the destruction, removal, wasting, deterioration, or impairment of any of the assets, except for ordinary wear and tear.
- C. Until the Effective Date of Divestiture, Respondent shall take such actions as are necessary promptly to comply with any requests of the LAGC (including but not limited to any requests for reports of capital expenditures or financial

## Order

information). Respondent shall provide Commission staff with copies of all correspondence with LAGC, and shall provide Commission staff with copies of all materials provided to the LAGC.

- D. The purposes of this Hold Separate Order are to: (1) preserve the Held Separate Business as a viable, competitive, and ongoing business independent of Respondent until the divestiture required by the Decision and Order is achieved; (2) assure that no Confidential Information is exchanged between Respondent and the Held Separate Business, except in accordance with the provisions of this Hold Separate Order; (3) prevent interim harm to competition pending the relevant divestitures and other relief; and (4) help remedy any anticompetitive effects of the proposed Acquisition.
- E. Respondent shall hold the Held Separate Business separate, apart, and independent on the following terms and conditions:
1. Frank Quigley shall serve as Hold Separate Trustee.
  2. Within five (5) days of the date this Hold Separate Order becomes final, Respondent shall execute an agreement with the Hold Separate Trustee (“Trustee Agreement”) that, subject to the approval of the Commission, confers at least the following rights and obligations upon the Respondent and the Hold Separate Trustee:
    - a. The Trustee Agreement shall require that, no later than one (1) day after the Acquisition Date, Respondent transfer to the Hold Separate Trustee all rights, powers, and authorities necessary to permit the Hold Separate Trustee to perform his/her duties and responsibilities, pursuant to this Hold Separate Order and consistent with the purposes of the Decision and Order.

Order

- b. The Hold Separate Trustee shall have the responsibility, consistent with the terms of this Hold Separate Order and the Decision and Order, for monitoring the organization and operation of the Held Separate Business; for managing the Held Separate Business; for maintaining the independence of the Held Separate Business; and for monitoring Respondent's compliance with its obligations pursuant to this Hold Separate Order and the Decision and Order.
- c. The Hold Separate Trustee shall have full and complete access to all personnel, books, records, documents, the Argosy Casino Baton Rouge Customer Database, and facilities of the Held Separate Business or to any other relevant information as the Hold Separate Trustee may reasonably request including, but not limited to, all documents and records kept by Respondent in the ordinary course of business that relate to the Held Separate Business. Respondent shall develop such financial or other information as the Hold Separate Trustee may request and shall cooperate with the Hold Separate Trustee. Respondent shall take no action to interfere with or impede the Hold Separate Trustee's ability to monitor Respondent's compliance with this Hold Separate Order and the Consent Agreement or otherwise to perform his/her duties and responsibilities consistent with the terms of this Hold Separate.
- d. The Hold Separate Trustee shall have the authority to employ, at the cost and expense of Respondent, such consultants, accountants, attorneys, and other representatives and assistants as are reasonably necessary to carry out the Hold Separate Trustee's duties and responsibilities, *provided, however*, that

## Order

such expenses shall not include any expenses incurred pursuant to Paragraph II.E.5.a. of this Hold Separate Order or in the ordinary course of business.

- e. The Commission may require the Hold Separate Trustee to sign an appropriate confidentiality agreement relating to Commission materials and information received in connection with performance of the Hold Separate Trustee's duties.
- f. Respondent may require the Hold Separate Trustee to sign a confidentiality agreement prohibiting the disclosure of any Confidential Business Information gained as a result of his/her role as Hold Separate Trustee to anyone other than the Commission or the LAGC.
- g. The Hold Separate Trustee shall apply for, obtain, and/or maintain all licenses, findings of suitability, and other approvals required by the LAGC, under the Louisiana gaming laws, to perform his/her obligations under the Decision and Order, at the expense of the Respondent.
- h. Thirty (30) days after the Hold Separate Order becomes final, and every thirty (30) days thereafter until the Hold Separate Order terminates, and as requested by the Commission or staff, the Hold Separate Trustee shall report in writing to the Commission concerning the efforts to accomplish the purposes of this Hold Separate Order. Included within that report shall be the Hold Separate Trustee's assessment of the extent to which the businesses comprising the Held Separate Business are meeting (or exceeding) their projected goals as reflected in operating plans, budgets, projections, or any other regularly prepared financial statements. Upon Respondent's request, the Hold Separate Trustee shall

Order

provide to the Respondent copies of all such reports, *provided, however*, Respondent is not entitled to receive, and the Hold Separate Trustee may redact from copies of any reports provided to the Respondent, all opinions and recommendations of the Hold Separate Trustee.

- i. If the Hold Separate Trustee ceases to act or fails to act diligently and consistent with the purposes of this Hold Separate Order, the Commission may appoint a substitute Hold Separate Trustee consistent with the terms of this paragraph, subject to the consent of Respondent, which consent shall not be unreasonably withheld. If Respondent has not opposed, in writing, including the reasons for opposing, the selection of the substitute Hold Separate Trustee within five (5) days after notice by the staff of the Commission to Respondent of the identity of any substitute Hold Separate Trustee, Respondent shall be deemed to have consented to the selection of the proposed substitute trustee. Respondent and the substitute Hold Separate Trustee shall execute a Trustee Agreement, subject to the approval of the Commission, consistent with Paragraph II.
3. Respondent shall comply with all terms of the Trustee Agreement, and any breach by Respondent of any term of the Trustee Agreement shall constitute a violation of this Hold Separate Order. Notwithstanding any paragraph, section, or other provision of the Trustee Agreement, any modification of the Trustee Agreement, without the prior approval of the Commission, shall constitute a failure to comply with the Decision and Order.
4. The Held Separate Business shall be staffed with sufficient employees to maintain the viability and competitiveness of the Held Separate Business. To the extent that any Argosy Baton Rouge Employees leave or

## Order

have left the Held Separate Business prior to the Effective Date of Divestiture, the Hold Separate Trustee, may replace departing or departed employees with persons who have similar experience and expertise or determine not to replace such departing or departed employees.

5. In connection with support services or products not included within the Held Separate Business, Respondent shall continue to provide, or offer to provide, the same support services to the Held Separate Business as are being provided to such business interest by Respondent or Argosy as of the date the Consent Agreement is signed by Respondent. For any services or products that Respondent may provide to the Held Separate Business, Respondent may charge no more than the lesser of: (i) the same price they charge others (or subsidiaries, divisions, affiliates, or units of Respondent or Argosy) for the same services or products; or (ii) the price charged by Argosy to the Argosy Baton Rouge Assets in the past for the same services or products. Respondent's personnel providing such services or products must retain and maintain all Confidential Business Information of the Held Separate Business on a confidential basis, and, except as is permitted by this Hold Separate Order, such persons shall be prohibited from providing, discussing, exchanging, circulating, or otherwise furnishing any such information to or with any person whose employment involves any of Respondent's or Argosy's businesses, other than the Held Separate Business. Such personnel shall also execute confidentiality agreements prohibiting the disclosure of any Confidential Business Information of the Held Separate Business.
  - a. Respondent shall offer to the Held Separate Business any and all services and products (not purchased or provided directly by the Held Separate Business itself in the ordinary course of business during the twelve

Order

(12) months prior to the date this Hold Separate Order becomes final) that Respondent or Argosy has provided to their other businesses directly or through third party contracts, and that Argosy has provided directly or through third party contracts to the businesses constituting the Held Separate Business, at any time during the twelve (12) months prior to the date this Hold Separate Order becomes final. The Held Separate Business may, with the approval of the Hold Separate Trustee, obtain such services and products from Respondent. The services and products that Respondent or Argosy shall offer the Held Separate Business shall include, but shall not be limited to, the following:

- (1) Human resources and administrative support services, including, but not limited to, payroll processing and employee benefits, including health benefits administration;
- (2) Preparation of tax returns;
- (3) Environmental health and safety services, which are used to develop corporate policies and insure compliance with federal and state regulations and corporate policies;
- (4) Financial accounting and reporting services;
- (5) Legal, licensing, and audit services;
- (6) Federal and state regulatory policy compliance;
- (7) Maintenance and oversight of information technology systems, which includes, but is not limited to, all computer, electronic mail, word processing, software data systems (including all information systems, which constructs, maintains,

## Order

and supports all computer systems), and all items from Exhibit D to the Securities Purchase Agreement;

- (8) Processing of accounts payable and accounts receivable;
  - (9) Procurement of supplies, goods, and services utilized in the ordinary course of business by the Held Separate Business;
  - (10) Public relations and public affairs support services;
  - (11) Construction and development services; and,
  - (12) Procurement and renewal of insurance and related services.
- b. the Held Separate Business shall have, with the approval of the Hold Separate Trustee, the ability to acquire services and products from third parties unaffiliated with Respondent or Argosy.
6. Respondent shall cause the Hold Separate Trustee and each Argosy Baton Rouge Casino Employee having access to Confidential Business Information to submit to the Commission a signed statement that the individual will maintain the confidentiality required by the terms and conditions of this Hold Separate Order. These individuals must retain and maintain all Confidential Business Information relating to the Held Separate Business on a confidential basis and, except as is permitted by this Hold Separate Order, such persons shall be prohibited from providing, discussing, exchanging, circulating, or otherwise furnishing any such information to or with any other person whose employment involves any of Respondent's businesses other than the Held



Order

Separate Business. These persons shall not be involved in any way in the management, production, distribution, sale, marketing, or financial operations of the Penn National Casino Rouge, located in Baton Rouge, Louisiana.

7. No later than two (2) days after the Acquisition Date, Respondent shall establish and obtain approval of the Hold Separate Trustee of written procedures covering the management, maintenance, and independence of the Held Separate Business consistent with the provisions of this Hold Separate Order, including but not limited to: (a) the Argosy Casino Baton Rouge Customer Database; and, (b) all Confidential Business Information.
8. No later than five (5) days after the date this Hold Separate Order becomes final, Respondent shall:
  - a. circulate to all directors and managers of the Held Separate Business, and to Respondent's or Argosy's employees who have responsibilities associated with the Held Separate Business, a copy of this Hold Separate Order and the proposed Decision and Order; and,
  - b. circulate a copy of Exhibit A to this Held Separate Business to all employees of the Held Separate Business.
9. The Hold Separate Trustee shall serve, without bond or other security, at the cost and expense of Respondent, exercising the standard of care and diligence that would be expected of a person in the conduct of the Hold Separate Trustee's duties under the Trustee Agreement and the Orders, and will operate and manage the Held Separate Business in substantially the same manner as previously conducted. The Hold Separate Trustee may not make any decision, take any action, or enter any transaction that is outside the ordinary course of business without the prior approval of the Commission, and

## Order

without providing prior written notice to and an opportunity for consultation with Respondent.

10. Respondent shall indemnify the Hold Separate Trustee and hold him or her harmless against any losses, claims, damages, liabilities, or expenses arising out of, or in connection with, the performance of the Hold Separate Trustee's duties, including all reasonable fees of counsel and other expenses incurred in connection with the preparation for, or defense of any claim, whether or not resulting in any liability, except to the extent that such liabilities, losses, damages, claims, or expenses result from misfeasance, gross negligence, willful or wanton acts, or bad faith by the Hold Separate Trustee.
11. Consistent with the nature and amount of past and planned financial resources furnished and planned to be furnished by Argosy to the ACBR, subject to Paragraph 9 herein, Respondent shall provide the Held Separate Business with sufficient financial resources:
  - a. as are appropriate in the judgment of the Hold Separate Trustee to operate the Held Separate Business as it is currently operated;
  - b. to perform all maintenance to, and replacements of, the assets of the Held Separate Business;
  - c. to carry on existing and planned capital projects and business plans; and
  - d. to maintain the viability, competitive vigor, and marketability of the Held Separate Business.

Such financial resources to be provided to the Held Separate Business shall include, but shall not be limited to, (i) general funds, (ii) capital, (iii) working capital, and (iv)

Order

reimbursement for any operating losses, capital losses, or other losses; *PROVIDED, HOWEVER*, that, consistent with the purposes of the Decision and Order, the Hold Separate Trustee may reduce in scale or pace any capital or research and development project, or substitute any capital or research and development project for another of the same cost.

12. Respondent shall, during the Hold Separate Period:
  - a. not interfere, directly or indirectly, with the hiring or employing by a Commission-approved Acquirer of the Argosy Baton Rouge Employees, and shall remove any impediments or incentives within the control of Respondent and Argosy that may deter these employees from accepting employment with a Commission-approved Acquirer, including, but not limited to, any non-compete provisions of employment or other contracts with Respondent or Argosy that would affect the ability or incentive of those individuals to be employed by a Commission-approved Acquirer. In addition, Respondent shall not make any counteroffer to a Argosy Baton Rouge Employee who receives a written offer of employment from a Commission-approved Acquirer;
  - b. provide all the Argosy Baton Rouge Employees with reasonable financial incentives to continue in their positions until the Effective Date of Divestiture. Such incentives shall include, but are not limited to, a continuation of all employee benefits, including regularly scheduled raises and bonuses and a vesting of all pension benefits (as permitted by law and for those Argosy Baton Rouge Employees covered by a pension plan), offered by Respondent until the Effective Date of Divestiture;

## Order

- c. not, for a period of eighteen (18) months following the Effective Date of Divestiture, directly or indirectly, employ or enter into a contract for the services of any Argosy Baton Rouge Primary Employees;

*Provided, however,* that this Paragraph II.H. shall not prohibit Respondent from entering into a contract for the services of, making offers of employment to, or employing or contracting with any Argosy Baton Rouge Primary Employees:

- (1) when a Commission-approved Acquirer has notified Respondent in writing that the Commission-approved Acquirer:
    - (a) does not intend to make an offer of employment to that employee; or,
    - (b) has terminated that employee without cause; or,
  - (2) when that employee voluntarily has declined to contract with or continue employment with the Commission-approved Acquirer, and the Commission-approved Acquirer has:
    - (a) not offered to contract with or employ that employee in a position with the same or similar duties as the position occupied by that employee immediately prior to the Effective Date of Divestiture; or,
    - (b) not offered that employee the same or increased monetary compensation and a substantially similar or better package of benefits and other compensation as the employee received immediately prior to the Effective Date of Divestiture.
13. If at any time during the Hold Separate Period the Securities Purchase Agreement appended to the Agreement to Execute Purchase Agreement (dated as

Order

of June 20, 2005) is terminated, Respondent shall offer a retention bonus to all Argosy Baton Rouge Primary Employees included in the Held Separate Business who continue their employment with the Held Separate Business until termination of the Hold Separate Period (which shall be in addition to any performance bonus that shall be based solely on the performance of the Held Separate Business, or any severance to which the employees would otherwise be entitled by virtue of their employment by Respondents during the hold separate period if such employee is not hired by the Acquirer); provided, however, that all Argosy Baton Rouge Primary Employees shall receive a retention bonus equal to the greater of: (i) the retention bonus to which such employees were entitled to, but did not receive pursuant to the Securities Purchase Agreement appended to the Agreement to Execute Purchase Agreement (dated as of June 20, 2005); or, (ii) the retention bonus pursuant to this Paragraph II.E.13 of the Hold Separate Order.

14. Except for the Argosy Baton Rouge Employees, and support services employees involved in providing services to the Held Separate Business pursuant to Paragraph II, and except to the extent provided in Paragraph II, Respondent shall not permit any other of its employees, officers, or directors to be involved in the operations of the Held Separate Business.
15. Respondent shall assure that Argosy Baton Rouge Employees receive, during the Hold Separate Period, their salaries, all current and accrued bonuses, pensions and other current and accrued benefits to which those employees would otherwise have been entitled.
16. Respondent's employees (excluding support services employees involved in providing support to the Held

## Order

Separate Business pursuant to this Hold Separate Order) shall not receive, or have access to, or use or continue to use any Confidential Business Information of the Held Separate Business not in the public domain except:

- a. as required by law;
- b. to the extent that necessary information is exchanged in the course of consummating the Acquisition;
- c. in negotiating agreements to divest assets pursuant to the Consent Agreement and engaging in related due diligence;
- d. in complying with this Hold Separate Order or the Consent Agreement;
- e. in complying with any request of the LAGC;
- f. in overseeing compliance with policies and standards concerning the safety, health and environmental aspects of the operations of the Held Separate Business and the integrity of the Held Separate Business's financial controls;
- g. in defending legal claims, investigations or enforcement actions threatened or brought against or related to the Held Separate Business; or
- h. in obtaining legal advice.

Nor shall the Argosy Baton Rouge Employees receive or have access to, or use or continue to use, any Confidential Business Information not in the public domain about Respondent and relating to Respondent's businesses, except such information as is necessary to maintain and operate the Held Separate Business. Respondent may

Order

receive aggregate financial and operational information relating to the Held Separate Business only to the extent necessary to allow Respondent to comply with the requirements and obligations of the laws of the United States, the state of Louisiana, and other states or countries, and to prepare consolidated financial reports, tax returns, reports required by securities laws, and personnel reports. Any such information that is obtained pursuant to this subparagraph shall be used only for the purposes set forth in this subparagraph.

17. Respondent and the Held Separate Business shall jointly implement, and at all times during the Hold Separate Period maintain in operation a system, as approved by the Hold Separate Trustee, of access and data controls to prevent unauthorized access to or dissemination of Confidential Business Information of the Held Separate Business, including, but not limited to, the opportunity by the Hold Separate Trustee, on terms and conditions agreed to with Respondent, to audit Respondent's networks and systems to verify compliance with this Hold Separate Order.

**III.**

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

**IV.**

**IT IS FURTHER ORDERED** that, for the purpose of determining or securing compliance with this Hold Separate Order, and subject to any legally recognized privilege, and upon

## Order

written request with reasonable notice to Respondent made to their principal United States offices, Respondent shall permit any duly authorized representative of the Commission:

- A. Access, during office hours of Respondent, in the presence of counsel, and as permitted by and in accordance with the laws, rules and regulations of the LAGC, to all facilities, and access to inspect and copy all books, ledgers, accounts, correspondence, memoranda and all other records and documents in the possession or under the control of Respondent relating to any matters contained in this Hold Separate Order; and
- B. Upon five (5) days' notice to Respondent and without restraint or interference from Respondent, to interview officers, directors, or employees of Respondent, who may have counsel present, regarding any such matters.

**V.**

**IT IS FURTHER ORDERED** that this Hold Separate Order shall terminate at the earlier of:

- A. three (3) business days after the Commission withdraws its acceptance of the Consent Agreement pursuant to the provisions of Commission Rule 2.34, 16 C.F.R. § 2.34; or
- B. the day after the Effective Date of Divestiture required by the Consent Agreement.



Analysis

## **Analysis of Agreement Containing Consent Orders to Aid Public Comment**

### **I. Introduction**

The Federal Trade Commission ("Commission") has accepted, subject to final approval, an Agreement Containing Consent Orders ("Consent Agreement") from Penn National Gaming, Inc. ("PNG"), which is designed to remedy the likely anticompetitive effects resulting from Penn's acquisition of Argosy Gaming Company ("Argosy"). If the Commission grants final approval, PNG will be required to divest Argosy's Baton Rouge, Louisiana, casino and associated assets to Columbia Sussex Corporation within four (4) months after the Consent Agreement becomes final. The Consent Agreement also includes an Order to Hold Separate and Maintain Assets ("Hold Separate Order") that requires PNG to preserve Argosy's Baton Rouge casino and associated assets as a viable, competitive, and ongoing operation until the divestiture is achieved. The Commission has issued the Hold Separate Order.

The proposed Consent Agreement has been placed on the public record for thirty (30) days to solicit comments from interested persons. Comments received during this period will become part of the public record. After thirty (30) days, the Commission will again review the proposed Consent Agreement and the comments received and will decide whether it should withdraw from the proposed Consent Agreement or make it final.

Pursuant to the November 3, 2004, merger agreement, PNG proposes to acquire Argosy ("Proposed Acquisition"). The total value of the Proposed Acquisition is approximately \$2.2 billion. The Commission's Complaint alleges that the Proposed Acquisition, if consummated, would violate Section 7 of the Clayton Act, as amended, 15 U.S.C. § 18, and Section 5 of the Federal Trade Commission Act, as amended, 15 U.S.C. § 45, by lessening competition in the Baton Rouge, Louisiana, metropolitan area casino services market.

Analysis

## II. The Parties

PNG is a publicly traded company headquartered in Wyomissing, Pennsylvania. The company owns and operates: Casino Rouge in Baton Rouge, Louisiana; Hollywood Casino in Aurora, Illinois; Charles Town Races & Slots in Charles Town, West Virginia; the Bullwhackers casino properties in Black Hawk, Colorado; and three Mississippi casinos: Hollywood Casino in Tunica, Casino Magic in Bay St. Louis, and the Boomtown Biloxi casino in Biloxi. Penn also operates Casino Rama, a gaming facility located approximately 90 miles north of Toronto in Ontario, Canada, pursuant to a management contract.

Argosy is a publicly traded company headquartered in Alton, Illinois. The company owns and operates casinos and related entertainment and hotel facilities in the Midwestern and Southern United States. Argosy owns and operates the Argosy Casino-Baton Rouge in Baton Rouge, Louisiana; the Alton Belle Casino in Alton, Illinois; the Argosy Casino-Riverside in Riverside, Missouri; the Argosy Casino-Sioux City in Sioux City, Iowa; the Argosy Casino-Lawrenceburg in Lawrenceburg, Indiana; and the Empress Casino Joliet in Joliet, Illinois.

## III. Casino Services

The casino services market includes a combination of slot machine, video poker machine, and table gaming services, and associated amenities such as parking, food and beverages, and entertainment.

There are three main categories of casino gaming: slot machines, video poker machines, and table and counter games. Coin or ticket-operated slot machines usually are allocated the largest portion of the gaming floor. These machines are controlled by random-number-generating computer chips that are set to return a percentage of the amount played to the player (“player win”) and to keep a percentage for the casino (“casino win” or “hold”). The machines may be programmed to provide

Analysis

many different game styles or themes, but they all fall into the subcategories of traditional “reel” slot machines or video slot machines.

Video poker machines sometimes are counted among the slot machines, but they actually represent a separate gaming category. While still based on a random-number-generating computer chip, the programming of the video poker rules and pay tables allows an element of player skill to affect the outcome of a game.

Table and counter games represent the third gaming category. Table games include blackjack, craps, poker, and let it ride. Counter games, which are played without cards, include roulette and keno. Casinos have been quick to capitalize on their consumers’ preference for slot machines, as those machines require far less labor, consume fewer square feet of the casino floor, and generate both greater profits and higher profit margins than other types of casino gaming.

Louisiana’s riverboat casinos offer a number of games from each of the three main gaming categories. Each riverboat casino has a similar number of gaming machines and tables, because they are limited by statute to a maximum of 30,000 square feet of aggregated casino floor space. When riverboat casinos differ in gaming minimums, limits, denominations, and hold rates, it is likely in response to highly localized competition. Other differences among riverboat casinos are the colors and layout of the casino’s decks, and the level of amenities provided within the shoreside pavilions alongside of which the riverboats are moored. In December 2004, Louisiana’s riverboat casinos generated nearly \$125 million in gaming revenue.<sup>1</sup>

---

<sup>1</sup>Louisiana State Police, Gaming Revenue Report.

Analysis

#### **IV. The Complaint**

The Commission's Complaint alleges that the Proposed Acquisition would create a monopoly in the Baton Rouge, Louisiana, metropolitan area casino services market. This includes the combination of slot machine, video poker machine, and table gaming, and associated amenities such as parking, food and beverages, and entertainment. The Proposed Acquisition would combine the only two casinos – one owned by PNG, the other by Argosy – in Baton Rouge, Louisiana. Industry participants refer to the Baton Rouge, Louisiana, riverboat casinos as “locals’ casinos” because the vast majority of their revenue comes from consumers who make frequent visits to the casinos and live in the Baton Rouge, Louisiana, metropolitan area.

The Complaint further alleges that new entry into the Baton Rouge, Louisiana, metropolitan area casino services market is not likely to occur in a timely manner, even if prices increased substantially after the Proposed Acquisition, because there are significant impediments to such entry. Louisiana law allows the operation of only 15 riverboat casinos, four racinos, and one non-Native American land-based casino. All those licenses have been granted, and there is no evidence that any of the licensees are planning to relocate.

#### **V. The Consent Agreement**

The Consent Agreement effectively remedies the Proposed Acquisition's likely anticompetitive effects in the Baton Rouge, Louisiana, metropolitan area casino services market by requiring PNG to divest Argosy's Baton Rouge casino and associated assets. Pursuant to the Consent Agreement, PNG is required to divest Argosy's Baton Rouge casino to Columbia Sussex Corporation within four (4) months from the date the consent order is final. This period may be extended for an additional two (2) months to allow the State of Louisiana to determine whether to grant regulatory approvals required to operate the casino. If Columbia Sussex Corporation does not obtain regulatory

Analysis

approvals, the Consent Agreement provides PNG with up to ten (10) months from the date the Consent Agreement becomes final to divest the casino to a buyer approved by the Commission. The Commission's goal in evaluating possible purchasers of divested assets is to ensure that the competitive environment that existed prior to the acquisition is maintained. A proposed acquirer of divested assets must not itself present competitive problems.

Should PNG fail to accomplish the divestiture within the time and in the manner required by the Consent Agreement, the Commission may appoint a trustee to divest these assets. If approved, the trustee would have the exclusive power and authority to accomplish the divestiture within six (6) months of being appointed, subject to any necessary extensions by the Commission. The Consent Agreement requires PNG to provide the trustee with access to information related to Argosy's Baton Rouge casino as necessary to fulfill his or her obligations.

The Commission's Hold Separate Order requires that PNG hold separate and maintain the viability of the Argosy Baton Rouge casino as a competitive operation from the date PNG acquires Argosy until the business is transferred to the Commission-approved acquirer. Furthermore, it contains measures designed to ensure that no material confidential information is exchanged between the PNG and the Argosy Baton Rouge casino (except as otherwise provided in the Consent Agreement), and provisions designed to prevent interim harm to competition in the Baton Rouge, Louisiana, metropolitan area casino services market pending divestiture. The Hold Separate Order names Frank Quigley, the present general manager of the casino, as the Hold Separate Trustee who is charged with the duty of monitoring Penn's compliance with the Consent Agreement and Hold Separate Order until the casino is divested.

In order to ensure that the Commission remains informed about the status of Argosy's Baton Rouge casino's pending divestiture,

## Analysis

and about the efforts being made to accomplish the divestiture, the Consent Agreement requires PNG to file periodic reports with the Commission until the divestiture is completed.

The purpose of this analysis is to facilitate public comment on the Consent Agreement, and is not intended to constitute an official interpretation of the proposed Decision and Order or the Order to Maintain Assets, or to modify their terms in any way.

Complaint

**IN THE MATTER OF**

**DAVITA INC.**

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

*Docket C-4152; File No. 0510051*

*Complaint, October 3, 2005--Decision, November 14, 2005*

This consent order addresses the acquisition by Respondent DaVita Inc. -- the second largest provider in the United States of outpatient dialysis services, which constitute a life-sustaining therapy that replaces the function of the kidneys by removing toxins and excess fluid from the blood -- of the United States dialysis services business of Gambro AB, a publicly-traded Swedish corporation with worldwide operations focused in three business fields: operating dialysis centers, manufacturing dialysis equipment, and providing technology and products to blood centers and hospital blood banks. The order, among other things, requires the respondent to divest 69 dialysis clinics in 35 markets across the United States to Renal Advantage, or to another acquirer approved by the Commission. The order also requires the respondent to terminate two management services agreements, pursuant to which it manages outpatient dialysis clinics on behalf of third-party owners. In addition, the order requires the respondent to provide prior notice to the Commission of its planned acquisitions of dialysis clinics located in the 35 markets addressed by the order.

*Participants*

For the Commission: *David L. Inglefield, Martha H. Oppenheim, Richard H. Cunningham, Richard A. Levy, Michael R. Moiseyev, Eric D. Rohlck, Rendell A. Davis, Jr., Daniel P. Ducore William N. Layher, Leslie Farber and Mark Frankena.*

For the Respondent: *Joseph Schohl, DaVita Inc. and Raymond A. Jacobsen, Jr. and Joel Grossman, McDermott Will & Emery.*

**COMPLAINT**

Pursuant to the Clayton Act and the Federal Trade Commission Act, and by virtue of the authority vested in it by said Acts, the Federal Trade Commission ("Commission"), having reason to

## Complaint

believe that Respondent DaVita Inc. (“DaVita”), a corporation subject to the jurisdiction of the Commission, has agreed to acquire Gambro Healthcare Inc., (“Gambro”), a corporation subject to the jurisdiction of the Commission, in violation of Section 7 of the Clayton Act, as amended, 15 U.S.C. § 18, and Section 5 of the Federal Trade Commission Act (“FTC Act”), as amended, 15 U.S.C. § 45, and it appearing to the Commission that a proceeding in respect thereof would be in the public interest, hereby issues its Complaint, stating its charges as follows:

**I. DEFINITIONS**

1. “Dialysis” means filtering a person’s blood, inside or outside of the body, to replicate the functions of the kidney.
2. “ESRD” means end stage renal disease, a chronic disease characterized by a near total loss of function of the kidneys, which in healthy people remove toxins and excess fluid from the blood.
3. “Outpatient dialysis services” means all procedures and services related to administering chronic dialysis treatment.

**II. RESPONDENT**

4. Respondent DaVita is a corporation organized, existing, and doing business under and by virtue of the laws of the State of Delaware, with its office and principal place of business located at 601 Hawaii Street, El Segundo, CA 90245. Respondent DaVita, among other things, is engaged in the provision and sale of outpatient dialysis services.

5. Respondent DaVita is, and at all times herein has been, engaged in commerce, as “commerce” is defined in Section 1 of the Clayton Act, as amended, 15 U.S.C. § 12, and is a corporation whose business is in or affects commerce, as “commerce” is defined in Section 4 of the Federal Trade Commission Act, as amended, 15 U.S.C. § 44.



Complaint

### **III. THE ACQUIRED COMPANY**

6. Gambro is a corporation organized, existing and doing business under and by virtue of the laws of Tennessee, with its office and principal place of business located at 1627 Cole Boulevard, Lakewood, CO 80401. Gambro is an indirect wholly owned subsidiary of Gambro AB, which is a corporation organized, existing and doing business under and by virtue of the laws of Sweden, with its office and principal place of business located at Jakobsgatan 6, SE-103 91, Stockholm, Sweden. Gambro AB is engaged globally in three business fields: operating dialysis centers, manufacturing dialysis equipment, and providing technology and products to blood centers and hospital blood banks. Gambro is Gambro AB's U.S. dialysis services business and is engaged, among other things, in the provision of outpatient dialysis services.

7. Gambro is, and at all times herein has been, engaged in commerce, as "commerce" is defined in Section 1 of the Clayton Act as amended, 15 U.S.C. §12, and is a corporation whose business is in or affects commerce, as "commerce" is defined in Section 4 of the Federal Trade Commission Act, as amended, 15 U.S.C. § 44.

### **IV. THE PROPOSED ACQUISITION**

8. On December 6, 2004, DaVita entered into an agreement ("Purchase Agreement") with Gambro AB to acquire Gambro, for approximately \$3.1 billion in cash (the "Acquisition").

### **V. THE RELEVANT MARKET**

9. For the purposes of this Complaint, the relevant line of commerce in which to analyze the effects of the Acquisition is the provision of outpatient dialysis services. Most ESRD patients receive dialysis treatments three times per week in sessions lasting between three and five hours. The only alternative to outpatient dialysis treatments for patients suffering from ESRD is a kidney

## Complaint

transplant. However, the wait-time for donor kidneys -- during which ESRD patients must receive dialysis treatments -- can exceed five years. Additionally, many ESRD patients are not viable transplant candidates. As a result, many ESRD patients have no alternative to ongoing dialysis treatments.

10. The relevant geographic market for the provision of dialysis services is defined by the distance ESRD patients are willing and/or able to travel to receive dialysis treatments, and is thus local in nature. Because ESRD patients often suffer from multiple health problems and may require assistance traveling to and from the dialysis clinic, these patients are unwilling and/or unable to travel long distances to receive dialysis treatment. As a general rule, ESRD patients do not travel more than 30 miles or 30 minutes to receive dialysis treatment, although travel times and distances vary depending on geographic barriers, travel patterns, and whether an area is urban, suburban, or rural.

11. The relevant geographic markets within which to assess the competitive effects of the proposed merger are the following metropolitan areas, or, in the case of the larger metropolitan areas, narrower geographic areas contained therein: (1) Chico, California; (2) Fairfield, California; (3) Los Angeles-Orange County, California; (4) Palm Springs-Palm Desert, California; (5) Riverside-Pomona-San Bernardino, California; (6) Sacramento, California; (7) San Diego, California; (8) San Francisco-Oakland-San Jose, California; (9) Stockton, California; (10) Lakeland-Winter Haven, Florida; (11) Fort Pierce-Port St. Lucie, Florida; (12) Punta Gorda, Florida; (13) Tampa-St. Petersburg-Clearwater, Florida; (14) Savannah, Georgia; (15) East St. Louis, Illinois; (16) Springfield, Illinois; (17) Grand Rapids, Michigan; (18) Holland-Zeeland, Michigan; (19) Jackson, Michigan; (20) Muskegon-Grand Haven, Michigan; (21) Omaha, Nebraska; (22) Fremont, Nebraska; (23) Charlotte, North Carolina; (24) Goldsboro, North Carolina; (25) Newport News, Virginia; (26) Norfolk-Chesapeake, Virginia; (27) Richmond, Virginia; and (28) Washington, D.C.

Complaint

## **VI. THE STRUCTURE OF THE MARKET**

12. The market for the provision of outpatient dialysis services is highly concentrated in each of the local areas identified in Paragraph 11, whether measured by the Herfindahl-Hirschman Index (“HHI”) or two or four firm concentration ratios. The combined firm would have a market share that ranges from 47 to 100 percent in each relevant geographic market. The Acquisition would significantly increase concentration in each relevant market, leaving DaVita as the dominant provider of outpatient dialysis services.

13. DaVita and Gambro are actual and substantial competitors in each of the relevant markets.

## **VII. ENTRY CONDITIONS**

14. The most significant barrier to entry into the relevant markets is locating a nephrologist with an established referral base to serve as the clinic’s medical director. By law, each dialysis clinic must have a nephrologist medical director. The medical director is essential to the competitiveness of the clinic because he or she is the clinic’s primary source of referrals. The lack of available nephrologists with an established referral stream is a significant barrier to entry into each of the relevant geographic markets identified in Paragraph 11. Additionally, an area must have certain attributes (such as a rapidly growing ESRD population, a favorable regulatory environment, average or below nursing and labor costs, and a relatively low penetration of managed care) to attract entry. The absence of these attributes is an additional barrier to entry into many of the relevant geographic markets.

15. New entry into the relevant markets sufficient to deter or counteract the anticompetitive effects described in Paragraph 16 is unlikely to occur, and would not occur in a timely manner because it would take over two years to enter and achieve significant market impact.

Complaint

**VIII. EFFECTS OF THE ACQUISITION**

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

- a. eliminating actual, direct, and substantial competition between DaVita and Gambro in the market for the provision of outpatient dialysis services;
- b. increasing the ability of the merged entity unilaterally to raise prices of outpatient dialysis services; and
- c. reducing incentives to improve service or product quality in the relevant markets.

**IX. VIOLATIONS CHARGED**

17. The Purchase Agreement described in Paragraph 8 constitutes a violation of Section 5 of the FTC Act, as amended, 15 U.S.C. § 45.

18. The Acquisition described in Paragraph 8, if consummated, would constitute a violation of Section 7 of the Clayton Act, as amended, 15 U.S.C. § 18, and Section 5 of the FTC Act, as amended, 15 U.S.C. § 45.

WHEREFORE, THE PREMISES CONSIDERED, the Federal Trade Commission on this third day of October, 2005, issues its Complaint against said Respondent.

Decision & Order

## DECISION AND ORDER

The Federal Trade Commission (“Commission”), having initiated an investigation of the proposed acquisition by DaVita Inc. of Gambro Healthcare Inc., a subsidiary of Gambro AB, and DaVita Inc. (hereafter referred to as “Respondent”) having been furnished thereafter with a copy of a draft of Complaint that the Bureau of Competition proposed to present to the Commission for its consideration and which, if issued by the Commission, would charge Respondent with violations of Section 7 of the Clayton Act, as amended, 15 U.S.C. § 18, and Section 5 of the Federal Trade Commission Act, as amended, 15 U.S.C. § 45; and

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

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

1. Respondent DaVita Inc. is a corporation organized, existing and doing business under and by virtue of the laws of the State of Delaware with its office and principal place of

## Decision &amp; Order

business located at 601 Hawaii Street, El Segundo, CA 90245.

2. The Federal Trade Commission has jurisdiction of the subject matter of this proceeding and of Respondent, and the proceeding is in the public interest.

**ORDER****I.**

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

- A. “DaVita” means DaVita Inc., its directors, officers, employees, agents, representatives, successors, and assigns; and its joint ventures, subsidiaries, divisions, groups and affiliates controlled by DaVita Inc. (including, after the Effective Date, Gambro Healthcare Inc.), and the respective directors, officers, employees, agents, representatives, successors, and assigns of each.
- B. “Gambro” means Gambro Healthcare Inc., its directors, officers, employees, agents, representatives, successors, and assigns; and its joint ventures, subsidiaries, divisions, groups and affiliates controlled by Gambro Healthcare Inc., and the respective directors, officers, employees, agents, representatives, successors, and assigns of each.
- C. “Commission” means the Federal Trade Commission.
- D. “Acquirer” and “Acquirers” means Renal Advantage, the Westside Clinic Acquirer, the Colton Partnership, Peninsula Nephrology, and each Person that receives the prior approval of the Commission to acquire any of the Appendix A Clinic Assets or the Owned Real Property pursuant to Paragraphs II or V of this Order.

Decision & Order

- E. “Appendix A Clinics” means Clinics listed in Appendix A to this Order.
- F. “Appendix A Clinic Assets” means the Appendix A Clinics, and all Assets Associated with each of those Clinics, except for the Owned Real Property.
- G. “Assets Associated” means the following assets Relating To the Operation Of A Clinic:
1. all rights under the Clinic’s Physician Contracts;
  2. leases for the Real Property of the Clinic;
  3. consumable or disposable inventory, including, but not limited to, janitorial, office, and medical supplies, and at least ten (10) treatment days of dialysis supplies and pharmaceuticals, including, but not limited to, erythropoietin;
  4. all rights, title and interest of DaVita in any tangible property (except for consumable or disposable inventory) that has been on the premises of the Clinic at any time since July 28, 2005, including, but not limited to, all equipment, furnishings, fixtures, improvements, and appurtenances;
  5. any interest held by DaVita in the Real Property Of The Clinic, PROVIDED, HOWEVER, “Assets Associated” does not mean the Owned Real Property, which is being divested separately pursuant to Paragraph II.A.5. of the Order;
  6. books, records, files, correspondence, manuals, computer printouts, databases, and other documents Relating To the Operation Of The Clinic located on the premises of the Clinic or in the possession of the Regional Manager responsible for such Clinic (or copies thereof where

## Decision &amp; Order

DaVita has a legal obligation to maintain the original document), including, but not limited to:

- a. documents containing information Relating To patients (to the extent transferable under applicable law), including, but not limited to, medical records,
  - b. financial records,
  - c. personnel files,
  - d. Physician lists and other records of the Clinic's dealings with Physicians,
  - e. maintenance records,
  - f. documents Relating To policies and procedures,
  - g. documents Relating To quality control,
  - h. documents Relating To Payors,
  - i. documents Relating To Suppliers,
  - j. documents Relating To Clinics other than the Clinic To Be Divested, *PROVIDED, HOWEVER*, if such documents are located other than on the premises of the Clinic To Be Divested, DaVita may submit a copy of the document with the portions not Relating To the Clinic To Be Divested redacted, and
  - k. copies of contracts with Payors and Suppliers, unless such contracts cannot, according to their terms, be disclosed to third parties even with the permission of DaVita to make such disclosure;
7. DaVita's Medicare and Medicaid provider numbers, to the extent transferable;



Decision & Order

8. all permits and licenses, to the extent transferable;
9. Intangible Property (other than Software) relating exclusively to the Operation Of The Clinic; and a royalty-free perpetual worldwide license for the use, without any limitation, of all other Intangible Property (other than Software) Relating To the Operation Of The Clinic (including the right to transfer or sublicense such Intangible Property, exclusively or nonexclusively, to others by any means); and
10. assets that are used in, or necessary for, the Operation Of The Clinic.

*PROVIDED, HOWEVER*, that “Assets Associated” does not include Excluded Assets.

- H. “Assets To Be Divested” means the Appendix A Clinic Assets, the Westside Clinic Assets, the Colton Clinic Assets, and the Owned Real Property.
- I. “Clinic” means a facility that provides hemodialysis or peritoneal dialysis services to patients suffering from kidney disease.
- J. “Clinic’s Physician Contracts” means all agreements to provide the services of a Physician to a Clinic, regardless of whether any of the agreements are with a Physician or with a medical group, including, but not limited to, agreements for the services of a medical director for the Clinic and “joiner” agreements with Physicians in the same medical practice as a medical director of the Clinic.
- K. “Clinic To Be Divested” and “Clinics To Be Divested” means the Appendix A Clinics, the Westside Clinic, the Colton Clinic, and the South S.F. Clinic.

## Decision &amp; Order

- L. “Colton Clinic” means the Dialysis Center of Colton, located at 1275 W. “C” Street, Colton, CA 92324.
- M. “Colton Clinic Assets” means the Colton Clinic and all Assets Associated with that Clinic that are owned by DaVita, except for twenty-three (23) hemodialysis machines at the Colton Clinic, which shall be leased to the Colton Partnership pursuant to the Colton Clinic Divestiture Agreement.
- N. “Colton Clinic Management Agreement” means collectively:
1. the Management Services Agreement dated August 1, 1997, between Dialysis Center of Colton and Gambro Healthcare Renal Care, Inc., and
  2. any other agreements between the Dialysis Center of Colton and Gambro Relating To the management of the Colton Clinic by Gambro.
- O. “Colton Clinic Divestiture Agreement” means the the Asset Purchase Agreement, Termination of Management Services Agreement, and Transition Services Agreement dated September 9, 2005, by and between Dialysis Center of Colton, Dr. Gerald S. Friedman, Dr. Erlinda Uy-Concepcion, Dr. M. Feroz Alam, Dr. Jin Wang and Gambro Healthcare Renal Care, Inc. (The Colton Clinic Divestiture Agreement is attached as Non-Public Appendix F to this Order.)
- P. “Colton Partnership” means Dialysis Center of Colton, a California general partnership, which has a principal place of business at 1275 W. “C” Street, Colton, CA 92324.
- Q. “Contract Services” means services performed pursuant to any Clinic’s Physician Contract.

Decision & Order

- R. “DaVita Employee Of A Clinic To Be Divested” and “DaVita Employee Of The Clinic To Be Divested” means an Employee Of A Clinic To Be Divested who is employed by DaVita.
- S. “DaVita’s Medical Protocols” means medical protocols promulgated by either DaVita or Gambro, whether in hard copy or embedded in software, that have been in effect at any time since July 28, 2005. *PROVIDED, HOWEVER*, “DaVita’s Medical Protocols” does not mean medical protocols adopted or promulgated, at any time, by any Physician or by any Acquirer, even if such medical protocols are identical, in whole or in part, to medical protocols promulgated by either DaVita or Gambro.
- T. “Divestiture Agreement” and “Divestiture Agreements” mean the Westside Clinic Divestiture Agreement, the Colton Clinic Divestiture Agreement, the South S.F. Clinic Management Termination Agreement, and any agreement pursuant to which DaVita divests any Appendix A Clinic Assets pursuant to this Order and with the prior approval of the Commission.
- U. “Effective Date” means the date on which DaVita acquires Gambro Healthcare Inc.
- V. “Employee Of A Clinic To Be Divested” and “Employee Of The Clinic To Be Divested” mean any individual (including, but not limited to, a clinic director, manager, nurse, technician, clerk, or social worker) who is not a Regional Manager, who is employed by DaVita, by an Acquirer, or by another manager or owner of such Clinic To Be Divested, and who has worked part-time or full-time on the premises of such Clinic To Be Divested at any time since June 1, 2005, regardless of whether the individual has also worked on the premises of any other Clinic.

## Decision &amp; Order

## W. “Excluded Assets” means:

1. all cash, cash equivalents, and short term investments of cash;
2. accounts receivable;
3. income tax refunds and tax deposits due DaVita;
4. unbilled costs and fees, and Medicare bad debt recovery claims, arising before a Clinic is divested to an Acquirer;
5. DaVita’s Medical Protocols (except if requested by an Acquirer pursuant to Paragraph II.B.17.b. of this Order);
6. rights to the names “DaVita” and “Gambro” and any variation of those names, and any names, phrases, marks, trade names, and trademarks to the extent they include the following, “REN,” “Total Renal Care,” “Renal Treatment Centers,” “Vivra,” “At Your Service,” “At Your Service (& Design),” “Dancing Star Logo,” “DaVita At Home,” “DaVita At Home (& Design),” “DaVita Clinical Research,” “DaVita Laboratory Services,” “DaVita Nephrology Partners,” “DaVitaCare,” “DaVita’s Key To Better Health,” “He/She Gives Life,” “K.T. Family Foundation (& Design),” “Kidney Education And You,” “Life-Alysis,” “Maxine,” “Miscellaneous Design (Alligator Design),” “Miscellaneous Design (Bird Design),” “Miscellaneous Design (Star in Square),” “Open Access & Open Access (& Design),” “Our Village Pharmacy,” “Our Village Pharmacy (Design),” “Reggie,” “Renal Connect,” “Rising Star Design,” “RMS,” “RMS & Design,” “Snappy,” “Star Rx,” “Star Rx (& Design),” “Star Rx Reminder,” “Star Rx Reminder (& Design),” “Star/Heart Design,” “Swirling Star Logo,” or “Where Quality of Life Meetings Quality of Care,” “Gambro Connections,” “Gambro Connections (& Design),” “Gambro Healthcare Laboratory Services,” “Gambro

Decision & Order

Healthcare Patient Services,” “Gambro Nephrology Partners,” “Labscope,” “Labscope Online (& Design),” “The Patient’s Benchmark in Renal Replacement Therapy,” “LSO On the Go,” “Servicelink,” “RIMS,” and “AIMS;”

7. insurance policies and all claims thereunder;
8. prepaid items or rebates;
9. minute books (other than governing body minute books of the Clinic To Be Divested), tax returns, and other corporate books and records;
10. any inter-company balances due to or from DaVita or its affiliates;
11. all benefits plans;
12. all writings and other items that are protected by the attorney-client privilege, the attorney work product doctrine or any other cognizable privilege or protection, except to the extent such information is necessary to the Operation Of A Clinic that is divested;
13. telecommunication systems equipment and applications, and information systems equipment including, but not limited to computer hardware, not physically located at a Clinic To Be Divested but shared with the Clinic To Be Divested through local and/or wide area networking systems;
14. e-mail addresses and telephone numbers of DaVita’s employees;
15. Software;

## Decision &amp; Order

16. computer hardware used in the Operation Of The Clinic that is (a) not located at the Clinic, and (b) not otherwise to be divested pursuant to a Divestiture Agreement;
  17. all Supplier or provider numbers issued to DaVita or Gambro by a Supplier or Payor with respect to any Clinic To Be Divested, except for DaVita's Medicare and Medicaid provider numbers for each Clinic To Be Divested;
  18. rights under agreements with Payors and Suppliers that are not assignable even if DaVita and Gambro approve such assignment;
  19. office equipment and furniture that (a) is not, in the Ordinary Course Of Business, physically located at the Clinic To Be Divested, (b) is shared with Clinics other than the Clinic To Be Divested, and (c) is not necessary to the Operation Of The Clinic To Be Divested.
  20. Licensed Intangible Property; and
  21. strategic planning documents that
    - a. relate to the Operation Of The Clinic other than the Clinic To Be Divested, and
    - b. are not located on the premises of the Clinic To Be Divested.
- X. "Governmental Approvals" means any permissions or sanctions issued by any government or governmental organization, including, but not limited to, licenses, permits, accreditations, authorizations, registrations, certifications, certificates of occupancy, and certificates of need.

Decision & Order

- Y. “Government Approvals For Continued Operation” means any Governmental Approvals, other than Government Approvals For Divestiture, that an Acquirer must have to continue to operate a Clinic To Be Divested.
- Z. “Governmental Approvals For Divestiture” means any Governmental Approvals that an Acquirer must have to own, and to initially operate, a Clinic To Be Divested, including, but not limited to, state-issued licenses and state-issued certificates of need.
- AA. “Illinois Governmental Approvals For Divestiture” means any Governmental Approvals For Divestiture issued by the State of Illinois.
- BB. “Illinois Clinic Assets” means:
1. Renal Treatment Centers – Lincolnland, located at 1112 Centre West Drive, Springfield, IL, 62704, and all Assets Associated with that Clinic,
  2. Gambro Breese, located at 160 North Main Street, Breese, IL, 62230, and all Assets Associated with that Clinic, and
  3. Gambro Fairview Heights, located at 821 Lincoln Highway, Fairview Heights, IL, 62208, and all of the Assets Associated with that Clinic.
- CC. “Intangible Property” means intangible property Relating To the Operation Of A Clinic To Be Divested including, but not limited to, intellectual property, software, computer programs, patents, know-how, goodwill, technology, trade secrets, technical information, marketing information, protocols, quality control information, trademarks, trade names, service marks, logos, and the modifications or improvements to such intangible property.

## Decision &amp; Order

DD. “Leases Of The Owned Real Property” means:

1. the Lease Agreement dated September 12, 2005, between Gambro Healthcare, Inc. and RAI Care Centers of Northern California I, LLC for space located at 218 Harding Boulevard, Roseville, California 95678;
2. the Lease Agreement dated September 12, 2005 between Gambro Healthcare, Inc. and RAI Care Centers of Virginia I, LLC for space located at 3204 Churchland Boulevard, Chesapeake, Virginia 23321;
3. the Lease Agreement dated September 12, 2005, between Gambro Healthcare, Inc., and RAI Care Centers of Virginia I, LLC for space located at 311 Goode Way, Portsmouth, Virginia 23704; and
4. the Lease Agreement dated September 12, 2005 between Gambro Healthcare, Inc. and RAI Care Centers of Florida I, LLC for space located at 1124 Lakeview Road, Clearwater, Florida 33756-3524.

(The Leases Of The Owned Real Property are included with the Renal Advantage Divestiture Agreements, which are attached as Non-Public Appendix D to this Order.)

EE. “Licensed Intangible Property” means intangible property licensed to DaVita from a third party Relating To the Operation Of A Clinic To Be Divested including, but not limited to, intellectual property, software, computer programs, patents, know-how, goodwill,, technology, trade secrets, technical information, marketing information, protocols, quality control information, trademarks, trade names, service marks, logos, and the modifications or improvements to such intangible property that are licensed to DaVita. (“Licensed Intangible Property” does not mean modifications and improvements to intangible property that are not licensed to DaVita.)



Decision & Order

- FF. “Management Agreement” and “Management Agreements” mean the South S.F. Clinic Management Agreement and the Colton Clinic Management Agreement.
- GG. “Material Confidential Information” means competitively sensitive, proprietary, and all other information that is not in the public domain owned by or pertaining to a Person or a Person’s business, and includes, but is not limited to, all customer lists, price lists, contracts, cost information, marketing methods, patents, technologies, processes, or other trade secrets.
- HH. “Monitor Agreement” means the Monitor Agreement dated September 12, 2005, between DaVita Inc., and John Strack and Mitch S. Nielson of Focal Point Medical Consulting Group. (The Monitor Agreement is attached as Appendix C to this Order.)
- II. “Operation Of A Clinic” and “Operation Of The Clinic” mean all activities Relating To the business of a Clinic, including, but not limited to:
1. attracting patients to the Clinic for dialysis services, providing dialysis services to patients of the Clinic, and dealing with their Physicians, including, but not limited to, services Relating To hemodialysis and peritoneal dialysis;
  2. providing medical products to patients of the Clinic;
  3. maintaining the equipment on the premises of the Clinic, including, but not limited to, the equipment used in providing dialysis services to patients;
  4. purchasing supplies and equipment for the Clinic;
  5. negotiating leases for the premises of the Clinic;

## Decision &amp; Order

6. providing counseling and support services to patients receiving products or services from the Clinic;
  7. contracting for the services of medical directors for the Clinic;
  8. dealing with Payors that pay for products or services offered by the Clinic, including but not limited to, negotiating contracts with such Payors and submitting claims to such Payors; and
  9. dealing with Governmental Approvals Relating To the Clinic or that otherwise regulate the Clinic.
- JJ. “Ordinary Course Of Business” means actions taken by any Person in the ordinary course of the normal day-to-day Operation Of The Clinic that is consistent with past practices of such Person in the Operation Of The Clinic, including, but not limited to past practice with respect to amount, timing, and frequency.
- KK. “Other Contracts Of Each Clinic To Be Divested” means all contracts Relating To the Operation Of A Clinic, where such Clinic is a Clinic To Be Divested – including, but not limited to, contracts for goods and services provided to the Clinic and contracts with Payors – but does not mean the Clinic’s Physician Contracts and the leases for the Real Property Of The Clinic.
- LL. “Owned Real Property” means the Real Property Of The Clinic at the following Clinics:
1. Roseville Dialysis Center, located at 218 Harding Boulevard, Roseville, CA 95678;
  2. Gambro Healthcare – Churchland, located at 3204 Churchland Boulevard, Chesapeake, VA 2332;

Decision & Order

3. Gambro Healthcare – Portsmouth, located at 311 Goode Way, Portsmouth, VA 23704; and
  4. Gambro Healthcare – Clearwater, located at 1124 Lakeview Road, Suite 1, Clearwater, FL, 33756.
- MM. “Payor” means any Person that purchases, reimburses for, or otherwise pays for medical goods or services for themselves or for any other person, including, but not limited to: health insurance companies; preferred provider organizations; point of service organizations; prepaid hospital, medical, or other health service plans; health maintenance organizations; government health benefits programs; employers or other persons providing or administering self-insured health benefits programs; and patients who purchase medical goods or services for themselves.
- NN. “Peninsula Nephrology” means Peninsula Nephrology, Inc., a California corporation with a principal place of business at 2000 South El Camino Real, San Mateo, CA 94403-1805.
- OO. “Person” means any natural person, partnership, corporation, association, trust, joint venture, government, government agency, or other business or legal entity.
- PP. “Physician” means a doctor of allopathic medicine (“M.D.”) or a doctor of osteopathic medicine (“D.O.”).
- QQ. “Real Property Of The Clinic” means real property on which, or in which, the Clinic is located, including real property used for parking and for other functions Relating To the Operation Of The Clinic.
- RR. “Relating To” means pertaining in any way to, and is not limited to that which pertains exclusively to or primarily to.

## Decision &amp; Order

- SS. “Regional Manager” means any individual who has been employed by DaVita or Gambro with supervisory responsibility for three or more Clinics.
- TT. “Regional Manager Of A Clinic To Be Divested” and “Regional Manager Of The Clinic To Be Divested” mean a Regional Manager who has had direct supervisory responsibility for a Clinic To Be Divested at any time since June 1, 2005.
- UU. “Renal Advantage” means Renal Advantage Inc., a Delaware corporation with a principal place of business at 115 East Park Drive, Suite 300, Brentwood, TN 37027.
- VV. “Renal Advantage Divestiture Agreements” means the following agreements:
1. the Amended and Restated Asset Purchase Agreement dated September 12, 2005, by and among Renal Advantage Inc., Gambro Healthcare, Inc., and DaVita Inc.;
  2. the Transition Services Agreement dated September 12, 2005, between Renal Advantage Inc. and DaVita Inc.;
  3. the letter agreement dated September 23, 2005, by and among Renal Advantage Inc., Gambro Healthcare, Inc., and DaVita Inc. (amending the Amended and Restated Asset Purchase Agreement dated September 12, 2005);
  4. the letter dated September 22, 2005, from Edwin C. Lunsford, III, Vice President and Division Counsel of Gambro Healthcare, Inc., to Larry Dewberry M.D. and Michael Lofti, M.D.; and

Decision & Order

5. the Leases Of The Owned Real Property.

(The Renal Advantage Divestiture Agreements are attached as Non-Public Appendix D to this Order.)

- WW. “Renal Associates of Grand Rapids” means Renal Associates of Grand Rapids, PC and its Physicians.
- XX. “Software” means executable computer code and the documentation for such computer code, but does not mean data processed by such computer code.
- YY. “South S.F. Clinic” means the South San Francisco Dialysis Center located at 205 Kenwood Way, South San Francisco, CA 94080.
- ZZ. “South S.F. Clinic Management Agreement” means collectively:
1. the Amended and Restated Agreement to Provide Management Services to Kidney Dialysis Facilities dated August 31, 1998, between Total Renal Care Holdings, Inc., and Peninsula Nephrology, Inc., and
  2. any other agreements between DaVita and Peninsula Nephrology Relating To the management of the South S.F. Clinic by DaVita.
- AAA. “South S.F. Clinic Management Termination Agreement” means the Termination of Management Services Agreement and Transition Services Agreement, dated September 12, 2005, between Davita Inc. and Peninsula Nephrology, Inc. (The South S.F. Clinic Management Termination Agreement is attached as Non-Public Appendix G to this Order.)

## Decision &amp; Order

- BBB. “Supplier” means any Person that has sold to DaVita or Gambro any goods or services, other than Physician services, for use in a Clinic To Be Divested. *PROVIDED, HOWEVER*, “Supplier” does not mean an employee of DaVita or Gambro.
- CCC. “Time Of Divestiture” means:
1. with respect to the Appendix A Clinics and the Westside Clinic, the date upon which a Clinic is divested to an Acquirer pursuant to this Order, and
  2. with respect to the Colton Clinic and the South S.F. Clinic, the date upon which a Management Agreement for the Clinic is terminated pursuant to this Order.
- DDD. “Westside Clinic” means the Gambro Westside Clinic located at 300 S. Robertson Blvd., Los Angeles, CA 90048.
- EEE. “Westside Clinic Acquirer” means 300 S. Robertson Dialysis, LLC, a California limited liability company with a principal place of business at 1 World Trade Center, Suite 2500, Long Beach, CA 90831.
- FFF. “Westside Clinic Divestiture Agreement” means the Asset Purchase Agreement dated September 10, 2005, by and among Gambro Healthcare, Inc. and 300 S. Robertson Dialysis, LLC, Stuart Friedman, M.D., Donald Nortman, M.D., Franklin Strauss, M.D., Larry Jones, Allen Fulmer, Doris Holmes, R.N., Jerry L. Green, and, with respect to certain sections of the agreement, Innovative Dialysis Systems, Inc. (The Westside Clinic Divestiture Agreement is attached as Non-Public Appendix E to this Order.)
- GGG. “Westside Clinic Assets” means the Westside Clinic and all Assets Associated with that Clinic.

Decision & Order

**II.**

**IT IS FURTHER ORDERED** that:

A. DaVita shall divest the Assets To Be Divested, and shall terminate the Management Agreements, as follows:

1. DaVita shall:

- a. within ten (10) days after the Effective Date, divest to Renal Advantage, absolutely, and in good faith, pursuant to and in accordance with the Renal Advantage Divestiture Agreements, all the Appendix A Clinic Assets, except for the Illinois Clinic Assets, as on-going businesses; and
- b. within sixty (60) days after the Effective Date, divest to Renal Advantage, absolutely, and in good faith, pursuant to and in accordance with the Renal Advantage Divestiture Agreements, the Illinois Clinic Assets, as on-going businesses;

PROVIDED, HOWEVER, if, at the time the Commission makes this Order final, the Commission determines that Renal Advantage is not an acceptable acquirer or that the Renal Advantage Divestiture Agreements are not an acceptable manner of divestiture, and so notifies DaVita, then DaVita shall:

- i. within six (6) months of the date DaVita receives notice of such determination from the Commission, divest the Appendix A Clinic Assets, except for the Illinois Clinic Assets, absolutely and in good faith, at no minimum price, as on-going businesses to an Acquirer or Acquirers that receive the prior approval of the Commission and only in a manner that receives the prior approval of the Commission; and

## Decision &amp; Order

- ii. within eight (8) months of the date DaVita receives notice of such determination from the Commission, divest the Illinois Clinic Assets absolutely and in good faith, at no minimum price, as on-going businesses, to an Acquirer or Acquirers that receive the prior approval of the Commission and only in a manner that receives the prior approval of the Commission.

The Renal Advantage Divestiture Agreements are incorporated by reference into this Order and made a part hereof as Non-Public Appendix D. Any failure by DaVita to comply with the Renal Advantage Divestiture Agreements shall constitute a failure to comply with the Order. The Renal Advantage Divestiture Agreements shall not vary or contradict, or be construed to vary or contradict, the terms of this Order. Nothing in this Order shall reduce, or be construed to reduce, any rights or benefits of Renal Advantage, or any obligations of DaVita, under the Renal Advantage Divestiture Agreements.

If DaVita has divested the Appendix A Clinic Assets to Renal Advantage prior to the date this Order becomes final, and if, at the time the Commission makes this Order final, the Commission determines that Renal Advantage is not an acceptable acquirer or that the Renal Advantage Divestiture Agreements are not an acceptable manner of divestiture, and so notifies DaVita, then DaVita shall within three (3) business days of receiving such notification, rescind the transaction with Renal Advantage and shall divest the Appendix A Clinic Assets in accordance with the proviso to Paragraph II.A.1. of this Order.

2. Within ten (10) days after the Effective Date, DaVita shall divest to the Westside Clinic Acquirer, absolutely, and in good faith, pursuant to and in accordance with the



Decision & Order

Westside Clinic Divestiture Agreement, the Westside Clinic Assets as an on-going business. The Westside Clinic Divestiture Agreement is incorporated by reference into this Order and made a part hereof as Non-Public Appendix E. Any failure by DaVita to comply with the Westside Clinic Divestiture Agreement shall constitute a failure to comply with the Order. The Westside Clinic Divestiture Agreement shall not vary or contradict, or be construed to vary or contradict, the terms of this Order. Nothing in this Order shall reduce, or be construed to reduce, any rights or benefits of the Westside Clinic Acquirer, or any obligations of DaVita, under the Westside Clinic Divestiture Agreement.

3. Within ten (10) days after the Effective Date, pursuant to and in accordance with the Colton Clinic Divestiture Agreement, DaVita shall:
  - a. terminate the Colton Clinic Management Agreement, thereby transferring management of the Colton Clinic to the Colton Partnership, and
  - b. divest to the Colton Partnership, absolutely, and in good faith, the Colton Clinic Assets as an on-going business.

The Colton Clinic Divestiture Agreement is incorporated by reference into this Order and made a part hereof as Non-Public Appendix F. Any failure by DaVita to comply with the Colton Clinic Divestiture Agreement shall constitute a failure to comply with the Order. The Colton Clinic Divestiture Agreement shall not vary or contradict, or be construed to vary or contradict, the terms of this Order. Nothing in this Order shall reduce, or be construed to reduce, any rights or benefits of the Colton Partnership, or any obligations of DaVita, under the Colton Clinic Divestiture Agreement.

## Decision &amp; Order

4. Within ten (10) days after the Effective Date, pursuant to and in accordance with the South S.F. Clinic Management Termination Agreement, DaVita shall terminate the South S.F. Clinic Management Agreement, thereby transferring management of the South S.F. Clinic to Peninsula Nephrology. The South S.F. Clinic Management Termination Agreement is incorporated by reference into this Order and made a part hereof as Non-Public Appendix G. Any failure by DaVita to comply with the South S.F. Clinic Management Termination Agreement shall constitute a failure to comply with the Order. The South S.F. Clinic Management Termination Agreement shall not vary or contradict, or be construed to vary or contradict, the terms of this Order. Nothing in this Order shall reduce, or be construed to reduce, any rights or benefits of Peninsula Nephrology, or any obligations of DaVita, under the South S.F. Clinic Management Termination Agreement.
  5. No later than one hundred twenty (120) days after the date the Agreement Containing Consent Order is accepted for public comment by the Commission, Respondent shall divest absolutely, in good faith, and in a manner that receives the prior approval of the Commission, the Owned Real Property to an Acquirer or Acquirers that receive the prior approval of the Commission. DaVita shall place no restrictions, other than the restrictions imposed by the Leases Of The Owned Real Property, on the use of the Owned Real Property by such Acquirer or Acquirers.
- B. DaVita shall divest the Assets To Be Divested, and terminate the Management Agreements, on the terms set forth in this Paragraph II.B., in addition to other terms that may be required by this Order and by the Divestiture Agreements; and DaVita shall agree with the Acquirers, as part of the Divestiture Agreements, to comply with the terms set forth in this Paragraph II.B.; *PROVIDED*,

Decision & Order

*HOWEVER*, this Paragraph II.B. does not apply to the Owned Real Property or to the Acquirers of the Owned Real Property:

1. DaVita shall place no restrictions on the use by any Acquirer of any of the Assets To Be Divested or any of the Clinics To Be Divested.
2. DaVita shall cooperate with the Acquirer and assist the Acquirer, at no cost to the Acquirer, at the Time Of Divestiture of each Clinic To Be Divested, in obtaining all Government Approvals For Divestiture, and all Government Approvals For Continued Operation, for each Clinic To Be Divested; *PROVIDED, HOWEVER*, this Paragraph II.B.2. does not apply to the South S.F. Clinic, to the Assets Associated with that Clinic, or to the Acquirer of that Clinic.
3. DaVita shall, at the Time Of Divestiture of each Clinic To Be Divested:
  - a. assign to the Acquirer all rights, title, and interest to leases for the Real Property Of The Clinic, and shall obtain all approvals necessary for such assignments; *PROVIDED, HOWEVER*, that (1) if the Acquirer obtains all rights, title, and interest to a lease for Real Property Of A Clinic To Be Divested before the Assets To Be Divested are divested pursuant to Paragraph II.A. of this Order, and (2) the Acquirer certifies its receipt of such lease and attaches it as part of the Divestiture Agreement, then DaVita shall not be required to make the assignments for such Clinic To Be Divested as required by this Paragraph; *PROVIDED, FURTHER, HOWEVER*, this Paragraph II.B.3.a. does not apply to the Colton Clinic and the South S.F. Clinic, to the Assets Associated with those Clinics, or to the Acquirers of those Clinics.; and

## Decision &amp; Order

- b. assign to the Acquirer all of the Clinic's Physician Contracts, and shall obtain all approvals necessary for such assignment; *PROVIDED, HOWEVER*, that (1) if the Acquirer enters into a Clinic's Physician Contract for a Clinic To Be Divested before the Assets To Be Divested are divested pursuant to Paragraph II.A. of this Order, and (2) the Acquirer certifies its receipt of such contract and attaches it as part of the Divestiture Agreement, then DaVita shall not be required to make the assignment for such Clinic To Be Divested as required by this Paragraph; *PROVIDED, FURTHER, HOWEVER*, this Paragraph II.B.3.b. does not apply to the Colton Clinic, the South S.F. Clinic, and the Westside Clinic, to the Assets Associated with those Clinics, or to the Acquirers of those Clinics.
- 4. With respect to all Other Contracts Of Each Clinic To Be Divested, DaVita shall, at the Acquirer's option and at the Time Of Divestiture of each Clinic To Be Divested:
  - a. if such contract can be assigned without third party approval, assign its rights under the contract to the Acquirer; and
  - b. if such contract can be assigned to the Acquirer only with third party approval, assist and cooperate with the Acquirer in obtaining:
    - (1) such third party approval and in assigning the contract to the Acquirer; or
    - (2) a new contract.
- 5. DaVita shall:
  - a. at the Time Of Divestiture of each Clinic To Be Divested, provide to the Acquirer of such Clinic

Decision & Order

contact information about Payors and Suppliers for the Clinic, and

- b. not object to the sharing of Payor and Supplier contract terms Relating To the Clinics To Be Divested: (i) if the Payor or Supplier consents in writing to such disclosure upon a request by the Acquirer, and (ii) if the Acquirer enters into a confidentiality agreement with DaVita not to disclose the information to any third party;

*PROVIDED, HOWEVER*, this Paragraph II.B.5. does not apply to the South S.F. Clinic, to the Assets Associated with that Clinic, or to the Acquirer of that Clinic.

6. Until sixty (60) days after the Time Of Divestiture of each Clinic To Be Divested, DaVita shall:
  - a. facilitate interviews between each DaVita Employee Of A Clinic To Be Divested and the Acquirer of the Clinic, and shall not discourage such employee from participating in such interviews; and
  - b. not interfere in employment negotiations between each DaVita Employee Of A Clinic To Be Divested and the Acquirer of the Clinic;

*PROVIDED, HOWEVER*, this Paragraph II.B.6. does not apply to the South S.F. Clinic, to the Assets Associated with that Clinic, or to the Acquirer of that Clinic.

7. With respect to each DaVita Employee Of A Clinic To Be Divested who receives, within sixty (60) days of the Time Of Divestiture of any Clinic at which he or she is employed, an offer of employment from the Acquirer of that Clinic, DaVita shall do the following:

## Decision &amp; Order

- a. DaVita shall not prevent, prohibit or restrict or threaten to prevent, prohibit or restrict the DaVita Employee Of The Clinic To Be Divested from being employed by the Acquirer of the Clinic, and shall not offer any incentive to the DaVita Employee Of The Clinic To Be Divested to decline employment with the Acquirer of the Clinic;
- b. if the DaVita Employee Of The Clinic To Be Divested accepts such offer of employment from the Acquirer, DaVita shall cooperate with the Acquirer of the Clinic in effecting transfer of the DaVita Employee Of The Clinic To Be Divested to the employ of the Acquirer of the Clinic;
- c. DaVita shall eliminate any contractual provisions or other restrictions that would otherwise prevent the DaVita Employee Of The Clinic To Be Divested from being employed by the Acquirer of the Clinic;
- d. DaVita shall eliminate any confidentiality restrictions that would prevent the DaVita Employee Of The Clinic To Be Divested who accepts employment with the Acquirer of the Clinic from using or transferring to the Acquirer any information Relating To the Operation Of The Clinic;
- e. DaVita shall pay, for the benefit of any DaVita Employee Of The Clinic To Be Divested who accepts employment with the Acquirer of the Clinic, all accrued bonuses, vested pensions and other accrued benefits; and

*PROVIDED, HOWEVER*, this Paragraph II.B.7. does not apply to the South S.F. Clinic, to the Assets Associated with that Clinic, or to the Acquirer of that Clinic.

Decision & Order

8. For a period of two (2) years following the Time Of Divestiture of each Clinic To Be Divested, DaVita shall not, directly or indirectly, solicit, induce, or attempt to solicit or induce any Employee Of A Clinic To Be Divested who is employed by the Acquirer to terminate his or her employment relationship with the Acquirer, unless that employment relationship has already been terminated by the Acquirer; *PROVIDED, HOWEVER*, DaVita may make general advertisements for employees including, but not limited to, in newspapers, trade publications, websites, or other media not targeted specifically at Acquirer's employees; *PROVIDED, FURTHER, HOWEVER*, DaVita may hire employees who apply for employment with DaVita, as long as such employees were not solicited by DaVita in violation of this Paragraph II.B.8.; *PROVIDED, FURTHER, HOWEVER*, DaVita may offer employment to an Employee Of A Clinic To Be Divested who is employed by the Acquirer in only a part-time capacity, if the employment offered by DaVita would not, in any way, interfere with the employee's ability to fulfill his or her employment responsibilities to the Acquirer.
9. For a period of not less than forty-five (45) days, which period may begin prior to the signing of the Consent Agreement and which shall end no earlier than ten (10) days after the Time Of Divestiture of each Clinic To Be Divested ("Forty-Five Day Hiring Period"), DaVita shall:
  - a. facilitate interviews between each Regional Manager Of A Clinic To Be Divested and the Acquirer of the Clinic, and shall not discourage such Regional Manager from participating in such interviews; and
  - b. not interfere in employment negotiations between each Regional Manager Of A Clinic To Be Divested and the Acquirer of the Clinic;

## Decision &amp; Order

*PROVIDED, HOWEVER*, the terms of this Paragraph II.B.9. shall not apply after Acquirers have hired six (6) Regional Managers who were each previously employed by DaVita or Gambro at any time since June 1, 2005; *PROVIDED, FURTHER, HOWEVER*, the terms of this Paragraph II.B.9. shall not apply to the Westside Clinic, the Colton Clinic, and the South S.F. Clinic, to the Assets Associated with those Clinics, or to the Acquirers of those Clinics.

10. With respect to each Regional Manager Of A Clinic To Be Divested who receives, within the Forty-Five Day Hiring Period required by Paragraph II.B.9. of this Order an offer of employment from the Acquirer of that Clinic, DaVita shall do the following:
  - a. DaVita shall not prevent, prohibit or restrict or threaten to prevent, prohibit or restrict the Regional Manager Of The Clinic To Be Divested from being employed by the Acquirer of the Clinic, and shall not offer any incentive to the Regional Manager Of The Clinic To Be Divested to decline employment with the Acquirer of the Clinic;
  - b. if the Regional Manager Of The Clinic To Be Divested accepts such offer of employment from the Acquirer, DaVita shall cooperate with the Acquirer of the Clinic in effecting transfer of the Regional Manager Of The Clinic To Be Divested to the employ of the Acquirer of the Clinic;
  - c. DaVita shall eliminate any contractual provisions or other restrictions that would otherwise prevent the Regional Manager Of The Clinic To Be Divested from being employed by the Acquirer of the Clinic;
  - d. DaVita shall eliminate any confidentiality restrictions that would prevent the Regional Manager Of The Clinic To Be Divested who accepts employment with



Decision & Order

the Acquirer of the Clinic from using or transferring to the Acquirer any information Relating To the Operation Of The Clinic;

- e. DaVita shall pay, for the benefit of any Regional Manager Of The Clinic To Be Divested who accepts employment with the Acquirer of the Clinic, all accrued bonuses, vested pensions and other accrued benefits;
- f. for a period of two (2) years following the Time Of Divestiture of the Clinic To Be Divested, DaVita shall not, directly or indirectly, solicit, induce, or attempt to solicit or induce any Regional Manager of the Acquirer who was previously a Regional Manager of A Clinic To Be Divested to terminate his or her employment relationship with the Acquirer unless the individual has been terminated by the Acquirer; *PROVIDED, HOWEVER*, DaVita may make general advertisements for Regional Managers including, but not limited to, in newspapers, trade publications, websites, or other media not targeted specifically at Acquirer's Regional Managers; *PROVIDED, FURTHER, HOWEVER*, DaVita may hire Regional Managers who apply for employment with DaVita, as long as such Regional Managers were not solicited by DaVita in violation of this Paragraph II.B.10.f.;

*PROVIDED, HOWEVER*, after Acquirers have hired six (6) Regional Managers who were each previously employed by DaVita or Gambro at any time since June 1, 2005, the terms of this Paragraph II.B.10. shall apply only to those six (6) Regional Managers hired by the Acquirers; *PROVIDED, FURTHER, HOWEVER*, the terms of this Paragraph II.B.10. shall not apply to the Westside Clinic, the Colton Clinic, and the South S.F. Clinic, to the Assets Associated with those Clinics, or to the Acquirers of those Clinics.

## Decision &amp; Order

11. With respect to each Physician who has provided services to a Clinic To Be Divested pursuant to any of the Clinic's Physician Contracts in effect at any time during the four (4) months preceding the Time Of Divestiture of the Clinic ("Contract Physician"):
  - a. DaVita shall not offer any incentive to the Contract Physician, the Contract Physician's practice group, or other members of the Contract Physician's practice group to decline to provide services to the Clinic To Be Divested, and shall eliminate any confidentiality restrictions that would prevent the Contract Physician, the Contract Physician's practice group, or other members of the Contract Physician's practice group from using or transferring to the Acquirer of the Clinic To Be Divested any information Relating To the Operation Of The Clinic; *PROVIDED, HOWEVER*, this Paragraph II.B.11.a. does not apply to the South S.F. Clinic, to the Assets Associated with that Clinic, or to the Acquirer of that Clinic; and
  - b. For a period of three (3) years following the Time Of Divestiture of each Clinic To Be Divested, DaVita shall not contract for the services of the Contract Physician, the Contract Physician's practice group, or other members of the Contract Physician's practice group for the provision of Contract Services to be performed in any of the areas listed in Appendix B of this Order that correspond to such Clinic. *PROVIDED, HOWEVER*, if the Contract Physician, or the Contract Physician's practice group, or other members of the Contract Physician's practice group were providing services to a Clinic pursuant to a contract with DaVita or Gambro in effect as of June 1, 2005, then DaVita may contract with such Contract Physicians, or the Contract Physician's practice group, or other members of the Contract Physician's practice group for services to be provided

Decision & Order

to that particular Clinic; *PROVIDED, FURTHER, HOWEVER*, the terms of this Paragraph II.B.11.b. shall not apply to the Westside Clinic, the Colton Clinic, and the South S.F. Clinic, to the Assets Associated with those Clinics, or to the Acquirers of those Clinics; *PROVIDED, FURTHER, HOWEVER*, the terms of this Paragraph II.B.11.b. shall not apply, in Kent County, Michigan, to Renal Associates of Grand Rapids if, prior to the date the Appendix A Clinic Assets are divested pursuant to Paragraph II.A.1., DaVita terminates, in writing, any contractual rights DaVita has with Renal Associates of Grand Rapids that prevent or hinder, in any way, the ability of Renal Associates of Grand Rapids, to contract with, or offer services to, any Person other than DaVita.

12. With respect to Material Confidential Information relating exclusively to any of the Clinics To Be Divested, DaVita shall:
  - a. not disclose such information to any Person other than the Acquirer of such Clinic;
  - b. after the Time Of Divestiture of such Clinic:
    - (1) not use such information for any purpose other than complying with the terms of this Order or with any law; and
    - (2) destroy all records of such information, except to the extent that: (1) DaVita is required by law to retain such information, and (2) DaVita's inside or outside attorneys may keep one copy solely for archival purposes, but may not disclose such copy to the rest of DaVita.

## Decision &amp; Order

13. At the Time Of Divestiture of each Clinic To Be Divested, DaVita shall provide the Acquirer of the Clinic with manuals, instructions, and specifications sufficient for the Acquirer to access and use any information
  - a. divested to the Acquirer pursuant to this Order, or
  - b. in the possession of the Acquirer, and previously used by DaVita or Gambro in the Operation Of The Clinic.
14. For two (2) years following the Time Of Divestiture of each Clinic To Be Divested, DaVita shall not solicit the business of any patients that received any goods or services from such Clinic between May 1, 2005, and the date of such divestiture, *PROVIDED, HOWEVER*, DaVita may (i) make general advertisements for the business of such patients including, but not limited to, in newspapers, trade publications, websites, or other media not targeted specifically at such patients, and (ii) provide advertising and promotions directly to any patient that initiates discussions with, or makes a request to, any DaVita employee.
15. DaVita shall convey to each Acquirer of a Clinic To Be Divested the right to use any Licensed Intangible Property (to the extent permitted by the third-party licensor), if such right is needed for the Operation Of The Clinic by the Acquirer and if the Acquirer is unable, using commercially reasonable efforts, to obtain equivalent rights from other third parties on commercially reasonable terms and conditions.
16. DaVita shall do nothing to prevent or discourage Suppliers that, prior to the Time Of Divestiture of any Clinic To Be Divested, supplied goods and services for use in any Clinic To Be Divested from continuing to supply goods and services for use in such Clinic.

Decision & Order

17. With respect to DaVita's Medical Protocols:

- a. DaVita shall retain a copy of DaVita's Medical Protocols until six (6) months after all of the Assets To Be Divested have been divested, and the Colton Clinic Management Agreement has been terminated, pursuant to this Order;
- b. If any Acquirer of a Clinic To Be Divested requests in writing to DaVita, within six (6) months of the Time Of Divestiture of that Clinic to that Acquirer, that DaVita license a copy of DaVita's Medical Protocols to that Acquirer, DaVita shall within five (5) business days of such request, grant to that Acquirer a royalty-free perpetual worldwide license for the use, without any limitation, of DaVita's Medical Protocols (including the right to transfer or sublicense such protocols, exclusively or nonexclusively, to others by any means); and
- c. DaVita shall create no disincentive for any Acquirer of a Clinic To Be Divested to make such a request for a license for DaVita's Medical Protocols, and shall not enter into any agreement or understanding with any Acquirer that the Acquirer not make such a request.

*PROVIDED, HOWEVER*, this Paragraph II.B.17. does not apply to the South S.F. Clinic, to the Assets Associated with that Clinic, or to the Acquirer of that Clinic.

C. DaVita shall not acquire Gambro Healthcare Inc. until it has obtained for all Clinics To Be Divested:

1. all Governmental Approvals For Divestiture necessary for the Acquirers of such Clinics to be able to own, and initially operate, the Clinics; *PROVIDED, HOWEVER*, DaVita shall not be required to obtain Illinois

## Decision &amp; Order

Governmental Approvals For Divestiture prior to acquiring Gambro Healthcare Inc.;

2. all approvals for assignment of the leases for the Real Property Of The Clinics, as required by to Paragraph II.B.3.a. of this Order; and
3. all approvals for the assignment of the Clinic's Physician Contracts, as required by Paragraph II.B.3.b. of this Order.

Copies of all such approvals shall be incorporated into the Divestiture Agreements as appendices.

- D. The purpose of Paragraph II of this Order is to ensure the continuation of the Clinics To Be Divested as, or as part of, ongoing viable enterprises engaged in the same business in which such assets were engaged at the time of the announcement of the acquisition by DaVita Inc. of Gambro Healthcare Inc., to ensure that the Clinics To Be Divested are operated independently of, and in competition with, DaVita, and to remedy the lessening of competition alleged in the Commission's Complaint.

### III.

**IT IS FURTHER ORDERED** that for a period of five (5) years from the date this Order is issued, DaVita shall not, without providing advance written notification to the Commission in the manner described in this paragraph, directly or indirectly:

- A. acquire any assets of or financial interest in any Clinic located in any of the areas listed in Appendix B of this Order; or
- B. enter into any contract to participate in the management or Operation Of A Clinic located in any of the areas listed in

Decision & Order

Appendix B of this Order, except to the extent that the contract relates exclusively to:

1. off-site lab services or social worker support materials; or
2. billing services, collection services, bookkeeping services, accounting services, supply purchasing and logistics services, or the preparation of financial reports and accounts receivable reports (collectively “Such Services”), where appropriate firewalls and confidentiality agreements are implemented to prevent Material Confidential Information of the Clinic from being disclosed to anyone participating in any way in the operation or management of any Clinic owned by DaVita or any Clinic other than the Clinic to which Such Services are being provided.

Said advance written notification shall contain (i) either a detailed term sheet for the proposed acquisition or the proposed agreement with all attachments, and (ii) documents that would be responsive to Item 4(c) of the Premerger Notification and Report Form under the Hart-Scott-Rodino Premerger Notification Act, Section 7A of the Clayton Act, 15 U.S.C. § 18a, and Rules, 16 C.F.R. § 801-803, Relating To the proposed transaction (hereinafter referred to as “the Notification), *PROVIDED, HOWEVER*, (i) no filing fee will be required for the Notification, (ii) an original and one copy of the Notification shall be filed only with the Secretary of the Commission and need not be submitted to the United States Department of Justice, and (iii) the Notification is required from DaVita and not from any other party to the transaction. DaVita shall provide the Notification to the Commission at least thirty (30) days prior to consummating the transaction (hereinafter referred to as the “first waiting period”). If, within the first waiting period, representatives of the Commission make a written request for additional information or documentary material (within the meaning of 16 C.F.R. § 803.20), DaVita shall not consummate the transaction until thirty days after submitting such

## Decision &amp; Order

additional information or documentary material. Early termination of the waiting periods in this paragraph may be requested and, where appropriate, granted by letter from the Bureau of Competition.

*PROVIDED, HOWEVER*, that prior notification shall not be required by this paragraph for a transaction for which Notification is required to be made, and has been made, pursuant to Section 7A of the Clayton Act, 15 U.S.C. § 18a.

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

- A. John Strack and Mitch S. Nielson, CPA, of Focal Point Medical Consulting Group, shall be appointed Monitors to assure that DaVita expeditiously complies with all of its obligations and performs all of its responsibilities as required by this Order.
- B. No later than one (1) day after this Order is made final, DaVita shall, pursuant to the Monitor Agreement and to this Order, transfer to the Monitors all the rights, powers, and authorities necessary to permit the Monitors to perform their duties and responsibilities in a manner consistent with the purposes of this Order.
- C. In the event a substitute Monitor is required, the Commission shall select the Monitor, subject to the consent of DaVita, which consent shall not be unreasonably withheld. If DaVita has not opposed, in writing, including the reasons for opposing, the selection of a proposed Monitor within ten (10) days after notice by the staff of the Commission to DaVita of the identity of any proposed Monitor, DaVita shall be deemed to have consented to the selection of the proposed Monitor. Not later than ten (10) days after appointment of a substitute Monitor, DaVita shall execute an agreement that, subject to the prior approval of



Decision & Order

the Commission, confers on the Monitor all the rights and powers necessary to permit the Monitors to monitor DaVita's compliance with the terms of this Order, the Order to Maintain Assets, and the Divestiture Agreements in a manner consistent with the purposes of this Order.

- D. DaVita shall consent to the following terms and conditions regarding the powers, duties, authorities, and responsibilities of the Monitors:
1. The Monitors shall have the power and authority to monitor DaVita's compliance with the terms of this Order, the Order to Maintain Assets, and the Divestiture Agreements, and shall exercise such power and authority and carry out the duties and responsibilities of the Monitors in a manner consistent with the purposes of this Order and in consultation with the Commission, including, but not limited to:
    - a. Assuring that DaVita expeditiously complies with all of its obligations and perform all of its responsibilities as required by the this Order, the Order to Maintain Assets, and the Divestiture Agreements;
    - b. Monitoring any transition services agreements;
    - c. Assuring that Material Confidential Information is not received or used by DaVita or the Acquirers, except as allowed in this Order and in the Order to Maintain Assets, in this matter.
  2. The Monitors shall act in a fiduciary capacity for the benefit of the Commission.
  3. The Monitors shall serve for such time as is necessary to monitor DaVita's compliance with the provisions of this

## Decision &amp; Order

Order, the Order to Maintain Assets, and the Divestiture Agreements.

4. Subject to any demonstrated legally recognized privilege, the Monitors shall have full and complete access to DaVita's personnel, books, documents, records kept in the Ordinary Course Of Business, facilities and technical information, and such other relevant information as the Monitors may reasonably request, related to DaVita's compliance with its obligations under this Order, the Order to Maintain Assets, and the Divestiture Agreements. DaVita shall cooperate with any reasonable request of the Monitors and shall take no action to interfere with or impede the Monitors' ability to monitor DaVita's compliance with this Order, the Order to Maintain Assets, and the Divestiture Agreements.
5. The Monitors shall serve, without bond or other security, at the expense of DaVita on such reasonable and customary terms and conditions as the Commission may set. The Monitors shall have authority to employ, at the expense of DaVita, such consultants, accountants, attorneys and other representatives and assistants as are reasonably necessary to carry out the Monitors' duties and responsibilities. The Monitors shall account for all expenses incurred, including fees for services rendered, subject to the approval of the Commission.
6. DaVita shall indemnify the Monitors and hold the Monitors harmless against any losses, claims, damages, liabilities, or expenses arising out of, or in connection with, the performance of the Monitors' duties, including all reasonable fees of counsel and other reasonable expenses incurred in connection with the preparations for, or defense of, any claim, whether or not resulting in any liability, except to the extent that such losses, claims, damages, liabilities, or expenses result from misfeasance,

Decision & Order

gross negligence, willful or wanton acts, or bad faith by the Monitors.

7. DaVita shall report to the Monitors in accordance with the requirements of this Order and/or as otherwise provided in any agreement approved by the Commission. The Monitors shall evaluate the reports submitted to the Monitors by DaVita, and any reports submitted by the Acquirer with respect to the performance of DaVita's obligations under this Order, the Order to Maintain Assets, and the Divestiture Agreements.
  8. Within one (1) month from the date the Monitors are appointed pursuant to this paragraph, every sixty (60) days thereafter, and otherwise as requested by the Commission, the Monitor shall report in writing to the Commission concerning performance by DaVita of its obligations under this Order, the Order to Maintain Assets, and the Divestiture Agreements.
  9. DaVita may require the Monitors and each of the Monitors' consultants, accountants, attorneys, and other representatives and assistants to sign a customary confidentiality agreement; *PROVIDED, HOWEVER*, such agreement shall not restrict the Monitors from providing any information to the Commission.
- E. The Commission may, among other things, require the Monitors and each of the Monitors' consultants, accountants, attorneys, and other representatives and assistants to sign an appropriate confidentiality agreement Relating To Commission materials and information received in connection with the performance of the Monitors' duties.
- F. If the Commission determines that the Monitors have ceased to act or failed to act diligently, the Commission may

## Decision &amp; Order

appoint a substitute Monitor in the same manner as provided in this Paragraph IV.

- G. The Commission may on its own initiative, or at the request of the Monitors, issue such additional orders or directions as may be necessary or appropriate to assure compliance with the requirements of this Order, the Order to Maintain Assets, and the Divestiture Agreements.
- H. A Monitor or Monitors appointed pursuant to this Order may be the same Person appointed as a trustee pursuant to Paragraph V of this Order and may be the same Person or Persons appointed as Monitor or Monitors under the Order to Maintain Assets.

**V.**

**IT IS FURTHER ORDERED** that:

- I. If DaVita has not divested, absolutely and in good faith and with the Commission's prior approval, all of the Assets To Be Divested pursuant to Paragraph II of this Order, the Commission may appoint a trustee to divest any of the Assets To Be Divested that have not been divested pursuant to Paragraph II of this Order in a manner that satisfies the requirements of Paragraph II of this Order. In the event that the Commission or the Attorney General brings an action pursuant to Section 5(l) of the Federal Trade Commission Act, 15 U.S.C. § 45(l), or any other statute enforced by the Commission, DaVita shall consent to the appointment of a trustee in such action to divest the relevant assets in accordance with the terms of this Order. Neither the appointment of a trustee nor a decision not to appoint a trustee under this Paragraph shall preclude the Commission or the Attorney General from seeking civil penalties or any other relief available to it, including a court-appointed trustee, pursuant to § 5(l) of the Federal Trade Commission

Decision & Order

Act, or any other statute enforced by the Commission, for any failure by DaVita to comply with this Order.

- J. The Commission shall select the trustee, subject to the consent of DaVita, which consent shall not be unreasonably withheld. The trustee shall be a Person with experience and expertise in acquisitions and divestitures. If DaVita has not opposed, in writing, including the reasons for opposing, the selection of any proposed trustee within ten (10) days after receipt of notice by the staff of the Commission to DaVita of the identity of any proposed trustee, DaVita shall be deemed to have consented to the selection of the proposed trustee.
- K. Within ten (10) days after appointment of a trustee, DaVita shall execute a trust agreement that, subject to the prior approval of the Commission, transfers to the trustee all rights and powers necessary to permit the trustee to effect the divestitures required by this Order.
- L. If a trustee is appointed by the Commission or a court pursuant to this Order, DaVita shall consent to the following terms and conditions regarding the trustee's powers, duties, authority, and responsibilities:
  - 1. Subject to the prior approval of the Commission, the trustee shall have the exclusive power and authority to divest any of the Assets To Be Divested that have not been divested pursuant to Paragraph II of this Order.
  - 2. The trustee shall have twelve (12) months from the date the Commission approves the trust agreement described herein to accomplish the divestiture, which shall be subject to the prior approval of the Commission. If, however, at the end of the twelve (12) month period, the trustee has submitted a divestiture plan or believes that the divestiture can be achieved within a reasonable time, the divestiture period may be extended by the

## Decision &amp; Order

Commission; *PROVIDED, HOWEVER*, the Commission may extend the divestiture period only two (2) times.

3. Subject to any demonstrated legally recognized privilege, the trustee shall have full and complete access to the personnel, books, records, and facilities related to the relevant assets that are required to be divested by this Order and to any other relevant information, as the trustee may request. DaVita shall develop such financial or other information as the trustee may request and shall cooperate with the trustee. DaVita shall take no action to interfere with or impede the trustee's accomplishment of the divestiture. Any delays in divestiture caused by DaVita shall extend the time for divestiture under this Paragraph V in an amount equal to the delay, as determined by the Commission or, for a court-appointed trustee, by the court.
4. The trustee shall use commercially reasonable best efforts to negotiate the most favorable price and terms available in each contract that is submitted to the Commission, subject to DaVita's absolute and unconditional obligation to divest expeditiously and at no minimum price. The divestiture shall be made in the manner and to an Acquirer or Acquirers as required by this Order; *PROVIDED, HOWEVER*, if the trustee receives bona fide offers for particular assets from more than one acquiring entity, and if the Commission determines to approve more than one such acquiring entity for such assets, the trustee shall divest the assets to the acquiring entity selected by DaVita from among those approved by the Commission; *PROVIDED, FURTHER, HOWEVER*, that DaVita shall select such entity within five (5) days of receiving notification of the Commission's approval.
5. The trustee shall serve, without bond or other security, at the cost and expense of DaVita, on such reasonable and customary terms and conditions as the Commission or a

Decision & Order

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

6. DaVita shall indemnify the trustee and hold the trustee harmless against any losses, claims, damages, liabilities, or expenses arising out of, or in connection with, the performance of the trustee's duties, including all reasonable fees of counsel and other expenses incurred in connection with the preparation for, or defense of, any claim, whether or not resulting in any liability, except to the extent that such losses, claims, damages, liabilities, or expenses result from misfeasance, gross negligence, willful or wanton acts, or bad faith by the trustee.
7. The trustee shall have no obligation or authority to operate or maintain the relevant assets required to be divested by this Order.
8. The trustee shall report in writing to DaVita and to the Commission every sixty (60) days concerning the trustee's efforts to accomplish the divestiture.

## Decision &amp; Order

9. DaVita may require the trustee and each of the trustee's consultants, accountants, attorneys, and other representatives and assistants to sign a customary confidentiality agreement; *PROVIDED, HOWEVER*, such agreement shall not restrict the trustee from providing any information to the Commission.
- M. If the Commission determines that a trustee has ceased to act or failed to act diligently, the Commission may appoint a substitute trustee in the same manner as provided in this Paragraph V.
- N. The Commission or, in the case of a court-appointed trustee, the court, may on its own initiative or at the request of the trustee issue such additional orders or directions as may be necessary or appropriate to accomplish the divestiture required by this Order.
- O. The trustee appointed pursuant to this Paragraph may be the same Person appointed as the Monitor pursuant to the relevant provisions of this Order or the Order to Maintain Assets.

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

- P. the Commission has determined, pursuant to the proviso to Paragraph II.A.1. of this Order, that Renal Advantage is not an acceptable acquirer of the Appendix A Clinic Assets or that the Renal Advantage Divestiture Agreements are not an acceptable manner of divestiture of the Appendix A Clinic Assets,
- Q. the Commission has approved, and has not withdrawn its approval of:



Decision & Order

1. the divestiture of any of the Appendix A Clinic Assets located in California to an acquirer other than Renal Advantage, or
  2. a manner of divestiture of any of the Appendix A Clinic Assets located in California that is different from the manner of divestiture set forth in the Renal Advantage Divestiture Agreement; and
- R. DaVita has certified to the Commission, prior to the expiration of the applicable six (6) month deadline under Paragraph II.A.1. of this Order for completing the divestiture of such assets, that:
1. notwithstanding timely and complete application by DaVita to the State of California for approval of the divestiture pursuant to an applicable consent decree to which the State of California and DaVita are parties, the State of California has failed to approve the divestiture of such assets, or
  2. the State of California has filed a timely motion in court seeking
    - a. to enjoin the proposed divestiture, or
    - b. other relief under such consent decree that, if granted, would prevent the proposed divestiture from occurring or would affect the manner of the proposed divestiture; then the six (6) month deadline for completing the divestiture of such assets shall be extended (i) an additional three (3) months or (ii) if the State of California files the timely motion referenced in Paragraph VI.C.2. of this Order, until the disposition of the motion, whichever is later.

Decision &amp; Order

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

- S. the Commission has determined pursuant to the proviso to Paragraph II.A.1. of this Order, that Renal Advantage is not an acceptable acquirer of the Appendix A Clinic Assets or that the Renal Advantage Divestiture Agreements are not an acceptable manner of divestiture of the Appendix A Clinic Assets;
- T. the Commission has approved, and has not withdrawn its approval of:
  - 1. the divestiture of any of the Appendix A Clinic Assets located in Michigan to an acquirer other than Renal Advantage, or
  - 2. a manner of divestiture of any of the Appendix A Clinic Assets located in Michigan that is different from the manner of divestiture set forth in the Renal Advantage Divestiture Agreement; and
- U. DaVita has certified to the Commission, prior to the expiration of the applicable six (6) month deadline under Paragraph II.A.1. of this Order for completing the divestiture of such assets, that:
  - 1. notwithstanding timely and complete application by DaVita to the State of Michigan for approval of the divestiture pursuant to an applicable consent decree to which the State of Michigan and DaVita are parties, the State of Michigan has failed to approve the divestiture of such assets, or
  - 2. the State of Michigan has filed a timely motion in court seeking

Decision & Order

- a. to enjoin the proposed divestiture, or
- b. other relief under such consent decree that, if granted, would prevent the proposed divestiture from occurring or would affect the manner of the proposed divestiture;

then the six (6) month deadline for completing the divestiture of such assets shall be extended (i) an additional three (3) months or (ii) if the State of Michigan files the timely motion referenced in Paragraph VII.C.2. of this Order, until the disposition of the motion, whichever is later.

**VIII.**

**IT IS FURTHER ORDERED** that:

- V. Beginning thirty (30) days after the date this Order becomes final, and every thirty (30) days thereafter until DaVita has fully complied with Paragraphs II.A., II.B.3., II.B.5.a., II.B.6., II.B.9., II.B.13., and II.B.17. of this Order, DaVita shall submit to the Commission a verified written report setting forth in detail the manner and form in which it intends to comply, is complying, and has complied with the terms of this Order, the Order to Maintain Assets, and the Divestiture Agreements. DaVita shall submit at the same time a copy of these reports to the Monitors, if any Monitors have been appointed.
- W. Beginning twelve (12) months after the date this Order becomes final, and annually thereafter on the anniversary of the date this Order becomes final, for the next four (4) years, DaVita shall submit to the Commission verified written reports setting forth in detail the manner and form in which it is complying and has complied with this Order, the Order to Maintain Assets, and the Divestiture Agreements. DaVita shall submit at the same time a copy

## Decision &amp; Order

of these reports to the Monitors, if any Monitors have been appointed.

**IX.**

**IT IS FURTHER ORDERED** that DaVita shall notify the Commission at least thirty (30) days prior to:

- X. Any proposed dissolution of DaVita,
- Y. Any proposed acquisition, merger or consolidation of DaVita, or
- Z. Any other change in DaVita that may affect compliance obligations arising out of this Order, including but not limited to assignment, the creation or dissolution of subsidiaries, or any other change in DaVita.

**X.**

**IT IS FURTHER ORDERED** that, for the purpose of determining or securing compliance with this Order, and subject to any legally recognized privilege, and upon written request with reasonable notice to DaVita, DaVita shall permit any duly authorized representative of the Commission:

- AA. Access, during office hours of DaVita and in the presence of counsel, to all facilities and access to inspect and copy all books, ledgers, accounts, correspondence, memoranda, and all other records and documents in the possession or under the control of DaVita related to compliance with this Order; and
- BB. Upon five (5) days' notice to DaVita and without restraint or interference from DaVita, to interview officers, directors, or employees of DaVita, who may have counsel present, regarding such matters.

Decision & Order

**XI.**

**IT IS FURTHER ORDERED** that this Order shall terminate ten (10) years from the date the Order is issued.

Decision &amp; Order

**APPENDIX A****APPENDIX A CLINICS**

	<b>Clinic Name</b>	<b>Clinic Address</b>
1	DaVita Chula Vista	1181 Broadway Suite 5 Chula Vista, CA 91911
2	DaVita Community Hemodialysis	1800 Haight Street San Francisco, CA 94117
3	Eastmont Dialysis Center	6955 Foothill Boulevard Oakland, CA 94605
4	Mission Dialysis Center of El Cajon	858 Fletcher Parkway El Cajon, CA 92020
5	Indio Dialysis Center	46767 Monroe Street Suite 101 Indio, CA 92201
6	Irvine Dialysis Center	16255 Laguna Canyon Road Irvine, CA 92618
7	Mission Dialysis Center of Oceanside	2227-B El Camino Real Oceanside, CA 92054
8	DaVita Ocean Garden	1738 Ocean Avenue San Francisco, CA 94112
9	Pacific Coast Dialysis Center	1416 Centinela Avenue Inglewood, CA 90302
10	Palm Desert Dialysis Center	41-501 Corporate Way Palm Desert, CA 92260
11	Peralta Renal Center	2757 Telegraph Avenue Oakland, CA 94612
12	Piedmont Dialysis Center	2710 Telegraph Avenue Suite 200 Oakland, CA 94612

Decision & Order

	<b>Clinic Name</b>	<b>Clinic Address</b>
13	Potrero Hill Dialysis Center	1750 Cesar Chavez Street Suite A San Francisco, CA 94124
14	Rialto Dialysis Center	1850 North Riverside Suite 150 Rialto, CA 92376
15	Mission Dialysis of San Diego	7007 Mission Gorge Road 1 <sup>st</sup> Floor San Diego, CA 92120
16	DaVita San Leandro	198 East 14 <sup>th</sup> Street San Leandro, CA 94577
17	Baker Place Dialysis Center	5084 Ames Avenue Omaha, NE 68104
18	Fremont Dialysis Center	2340 North Clarkson Fremont, NE 68025
19	Renal Treatment Centers – Lincolnland	1112 Centre West Drive Springfield, IL 62704
20	Omaha Dialysis Center	4350 Dewey Avenue 5 <sup>th</sup> Floor Omaha, NE 68105
21	DaVita Roosevelt Park	1080 West Norton Avenue Muskegon, MI 49441
22	DaVita Bay Area	1101 9 <sup>th</sup> Street North St. Petersburg, FL 33701
23	DaVita Garey Dialysis Center	1880 North Garey Avenue Pomona, CA 91767
24	DaVita Haines	110 Patterson Road Haines City, FL 33844
25	DaVita Lake Wales	1348 SR 60 East Lake Wales, FL 33853
26	DaVita Mecklenburg	3515 Latrobe Drive Charlotte, NC 28211

## Decision &amp; Order

	<b>Clinic Name</b>	<b>Clinic Address</b>
27	DaVita University	9030 Glenwater Drive Charlotte, NC 28262
28	DaVita Savannah	1020 Drayton Street Savannah, GA 31401
29	DaVita Warsaw	213 West College Street Warsaw, NC 28398
30	DaVita Wayne County	2403 Wayne Memorial Drive Goldsboro, NC 27534
31	DaVita Winter Haven	400 Security Square Winter Haven, FL 33880
32	Chico Dialysis Center	1030 Village Lane Chico, CA 95926
33	East Olympic Dialysis Center	5714 E. Olympic Boulevard Commerce, CA 90022
34	Elk Grove Dialysis Center	8139 Elk Grove Boulevard Suite 200 Elk Grove, CA 96758
35	Gambro Healthcare – Fountain Valley	17197 Newhope Avenue Suite A, B, C Fountain Valley, CA 92708
36	Garden Grove Dialysis Center	12555 Garden Grove Boulevard Garden Grove, CA 92843
37	Harbor Boulevard Dialysis Center	12761 Harbor Boulevard Garden Grove, CA 92840
38	Los Angeles Dialysis Center	11859 Compton Avenue Los Angeles, CA 90059
39	Placer Dialysis Center	1451 Secret Ravine Parkway Bldg. D Roseville, CA 95661
40	Redlands Dialysis Center	1210 Indiana Court Redlands, CA 92374



Decision & Order

	<b>Clinic Name</b>	<b>Clinic Address</b>
41	Roseville Dialysis Center	218 Harding Boulevard Roseville, CA 95678
42	San Bernardino Dialysis Center	1500 North Waterman Avenue San Bernardino, CA 92404
43	San Joaquin Dialysis Center	3115 West March Lane Stockton, CA 95219
44	Solano Dialysis Center	490 Chadbourne Road Fairfield, CA 94534
45	Stockton Dialysis Center	2350 N. California Street Stockton, CA 95204
46	Tustin Dialysis Center	535 East First Street Tustin, CA 92780-3312
47	Westminster North	290 Hospital Cr. Westminster, CA 92683
48	Gambro Healthcare – Clyde Park	4893 Clyde Park Avenue Southwest Wyoming, MI 49509
49	Gambro Healthcare – Jackson	200 South East Avenue Jackson, MI 49201
50	Gambro Healthcare – Rockford	311 Rockford Park Drive NE Rockford, MI 49341
51	Gambro Healthcare – Zeeland	2 Royal Park Drive Zeeland, MI 49464
52	Gambro Healthcare – Airline Blvd.	2890 Airline Blvd. Portsmouth, VA 23701
53	Gambro Healthcare – Beltsville	10701 Baltimore Avenue Beltsville, MD 20705
54	Gambro Healthcare – Churchland	3204 Churchland Blvd. Chesapeake, VA 23321
55	Gambro Healthcare – Richmond MCV Downtown	800 West Leight Street Richmond, VA 23220

FEDERAL TRADE COMMISSION DECISIONS  
VOLUME 140

Decision & Order

	<b>Clinic Name</b>	<b>Clinic Address</b>
56	Gambro Healthcare – Newport News	739 Thimble Shoals Boulevard #600 Newport News, VA 23606
57	Gambro Healthcare – Oxon Hill	5410 Indian Head Highway Oxon Hill, MD 20745
58	Gambro Healthcare – Portsmouth	311 Goode Way Portsmouth, VA 23704
59	Gambro Healthcare – Richmond MCV	2521 Mechanicsville Turnpike Richmond, VA 23223
60	Gambro Healthcare – Silver Hill	5652 Silver Hill Road Penn Station Shopping Center District Heights, MD 20747
61	Gambro Healthcare – Clearwater	1124 Lakeview Road Suite 1 Clearwater, FL 33756
62	Gambro Healthcare – Fort Pierce	2501 Ohio Avenue Fort Pierce, FL 34947
63	Gambro Healthcare – Palm Harbor	30522 U.S. 19 N. Suite 100 Palm Harbor, FL 34684
64	Gambro Healthcare – Port St. Lucie	1407 SE Gold Tree Drive Port St. Lucie, Fl 34952
65	Gambro Healthcare – Punta Gorda	355 DuPont Street Punta Gorda, FL 33950
66	Gambro Healthcare – Seminole	12505 Starkey Road Suite B Largo, FL 33773
67	Gambro Fairview Heights	821 Lincoln Hwy. Fairview Heights, IL 62208
68	Gambro Breese	160 N. Main St. Breese, IL 62230

Decision & Order

**APPENDIX B**

**AREA DEFINITIONS**

- Five digit numbers refer to zip codes.
- Geographic areas bounded by roads include all properties abutting the referenced road (i.e. properties on both sides of the road).
- Zip codes or other areas fully surrounded by areas included in the area definition shall be considered part of the area definition.
- Area definitions are based on maps submitted to the Commission staff by DaVita.

	<b>Divested Clinics</b>	<b>Corresponding Area Definition</b>
1	Fremont Dialysis Center	The area in and/or near Fremont, Nebraska, consisting of: Dodge County (Nebraska); and 68002, 68015, 68025, 68026, 68044, 68064.
2	DaVita Wayne County, DaVita Warsaw	The area in and/or near Goldsboro, North Carolina, consisting of: Wayne County (North Carolina); and 28325, 28341, 28365, 28393, 28398.
3	Gambro Healthcare – Clyde Park, Gambro Healthcare – Rockford	The area in and/or near Grand Rapids, Michigan, consisting of: Kent County (Michigan).
4	Gambro Healthcare – Zeeland	The area in and/or near Zeeland, Michigan, consisting of: Ottawa County (Michigan) and 49423, 49434.

## Decision &amp; Order

	<b>Divested Clinics</b>	<b>Corresponding Area Definition</b>
5	Gambro Healthcare – Jackson	The area in and/or near Jackson, Michigan, consisting of: Jackson County (Michigan).
6	Gambro Healthcare – Beltsville	The area in and/or near Laurel, Maryland, consisting of: 20704, 20705, 20707, 20708, 20709, 20724, 20725, 20726, 20740, 20741, 20742, 20768, 20770; and the portion of 20723 that lies to the southeast of the line formed by: (1) the section of I-95 between the northern border of 20723 and the intersection of I-95 and State Hwy 216, and (2) the section of State Hwy 216 between the intersection of State Hwy 216 and I-95 and the western border of 20723.
7	DaVita Roosevelt Park	The area in and/or near Muskegon, Michigan, consisting of: Muskegon County (Michigan).
8	Gambro Healthcare – Punta Gorda	The area in and/or near Punta Gorda, Florida, consisting of: Charlotte County (Florida).
9	Solano Dialysis Center	The area in and/or near Fairfield, California, consisting of: 94533, 94534, 94535; and the portion of 94585 that lies to the west of the line formed by: (1) the section of Denverton Rd. between the northern border of 94535 and the intersection of Denverton Rd. and State Hwy. 12, (2) the section of State Hwy. 12 between the intersection of State Hwy. 12 and Denverton Rd. and the intersection of State Hwy. 12 and Shiloh Rd., and (3) the section of Shiloh Rd. between the intersection of Shiloh Rd. and State Hwy. 12 and the southern border of 94535.
10	East Olympic Dialysis Center	The area in and/or near Los Angeles, California, that is circumscribed by the line formed by: (1) the section of N. Lorena St. between the

Decision & Order

	<b>Divested Clinics</b>	<b>Corresponding Area Definition</b>
		<p>intersection of N. Lorena St. and E. Cesar E. Chavez Ave. and the intersection of N. Lorena St. and S. Lorena St.,</p> <p>(2) the section of S. Lorena St. between the intersection of N. Lorena St. and S. Lorena St. and the intersection of S. Lorena St. and S. Grande Vista Ave.,</p> <p>(3) the section of S. Grande Vista Ave. between the intersection of S. Lorena St. and S. Grand Vista Ave. and the intersection of S. Grand Vista Ave. and S. Downey Rd.,</p> <p>(4) the section of S. Downey Rd. between the intersection of S. Grand Vista Ave. and S. Downey Rd. and the intersection of S. Downey Rd. and Bandini Blvd.,</p> <p>(5) the section of Bandini Blvd. between the intersection of S. Downey Rd. and Bandini Blvd. and the intersection of Bandini Blvd. and Garfield Ave.,</p> <p>(6) the section of Garfield Ave. between the intersection of Bandini Blvd. and Garfield Ave. and the intersection of Garfield Ave. and Telegraph Rd.,</p> <p>(7) the section of Telegraph Rd. between the intersection of Garfield Ave. and Telegraph Rd. and the intersection of Telegraph Rd. and S. Greenwood Ave.,</p> <p>(8) the section of Greenwood Ave. between the intersection of S. Greenwood Ave. and Telegraph Rd. and the intersection of S. Greenwood Ave. and Montebello Way,</p> <p>(9) the section of Montebello Way between the intersection of S. Greenwood Ave. and Montebello Way and the intersection of Montebello Way and S. Montebello Blvd.,</p> <p>(10) the section of S. Montebello Blvd. between the intersection of Montebello Way and S. Montebello Blvd. and the intersection of S. Montebello Blvd. and N. Montebello Blvd.,</p> <p>(11) the section of N. Montebello Blvd. between the intersection of S. Montebello Blvd. and N. Montebello Blvd. and the intersection of N. Montebello Blvd. and Paramount Blvd.,</p>

FEDERAL TRADE COMMISSION DECISIONS  
VOLUME 140

Decision & Order

	<b>Divested Clinics</b>	<b>Corresponding Area Definition</b>
		<p>(12) the section of Paramount Blvd. between the intersection of N. Montebello Blvd. and Paramount Blvd. and the intersection of Paramount Blvd. and Arroyo Dr.,</p> <p>(13) the section of Arroyo Dr. between the intersection of Paramount Blvd. and Arroyo Dr. and the intersection of Arroyo Dr. and Ackley St.,</p> <p>(14) the section of Ackley St. between the intersection of Arroyo Dr. and Ackley St. and the intersection of Ackley St. and Fulton Ave.</p> <p>(15) the section of Fulton Ave. between the intersection of Ackley St. and Fulton Ave. and the intersection of Fulton Ave. and Wilcox Ave.,</p> <p>(16) the section of Wilcox Ave. between the intersection of Fulton Ave. and Wilcox Ave. and the intersection of Wilcox Ave. and W. El Repetto Dr.,</p> <p>(17) the section of W. El Repetto Dr. between the intersection of Wilcox Ave. and W. El Repetto Dr. and the intersection of W. El Repetto Dr. and S. Atlantic Blvd.,</p> <p>(18) the section of S. Atlantic Blvd. between the intersection of W. El Repetto Dr. and S. Atlantic Blvd. and the intersection of S. Atlantic Blvd. and Brightwood St.</p> <p>(19) the section of Brightwood St. between the intersection of S. Atlantic Blvd. and Brightwood St. and Brightwood St. and Monterey Pass Rd.</p> <p>(20) the section of Monterey Pass Rd. between the intersection of Brightwood St. and Monterey Pass Rd. and the intersection of Monterey Pass Rd. and E. Cesar E. Chavez Ave., and</p> <p>(21) the section of E. Cesar E. Chavez Ave. between the intersection of S. Monterey Pass Ave. and E. Cesar E. Chavez Ave. and the intersection of E. Cesar E. Chavez Ave. and N. Lorena St.</p>

Decision & Order

	<b>Divested Clinics</b>	<b>Corresponding Area Definition</b>
11	Los Angeles Dialysis Center	The area in and/or near Lynwood, California, that is circumscribed by the line formed by: (1) the section of I-110 between the intersection of I-110 and Route 42 and the intersection of I-110 and Alondra Blvd., (2) the section of Alondra Blvd. between the intersection of I-110 and Alondra Blvd. and the intersection of Alondra Blvd. and I-710, (3) the section of I-710 between the intersection of Alondra Blvd. and I-710 and the intersection of I-710 and Abbott Rd., (4) the section of Abbott Rd. between the intersection of I-710 and Abbott Rd. and the intersection of Abbott Rd. and Wright Rd., (5) the section of Wright Rd. between the intersection of Abbott Rd. and Wright Rd. and the intersection of Wright Rd. and Atlantic Ave., (6) the section of Atlantic Ave. between the intersection of Wright Rd. and Atlantic Ave. and the intersection of Atlantic Ave. and Route 42, and (7) the section of Route 42 between the intersection of I-710 and Route 42 and the intersection of Route 42 and I-110.

FEDERAL TRADE COMMISSION DECISIONS  
VOLUME 140

Decision & Order

	<b>Divested Clinics</b>	<b>Corresponding Area Definition</b>
12	Gambro Fairview Heights, Gambro Breese	<p>The area in and/or near East St. Louis, Illinois, consisting of:</p> <p>62034, 62040, 62059, 62060, 62062, 62071, 62090, 62201, 62202, 62203, 62204, 62205, 62206, 62207, 62208, 62216, 62223, 62225, 62226, 62230, 62232, 62234, 62245, 62254, 62269, 62289, 62293, 62294;</p> <p>the portion of 62218 that lies to the north of the line formed by:</p> <p>(1) the portion of State Hwy 161 between the western border of 62218 and the intersection of State Hwy 161 and County Rd. 1430E,</p> <p>(2) the portion of County Rd. 1430E between the intersection of State Hwy. 161 and County Rd. 1430E and the intersection of County Rd. 1430E and County Rd. 1440E, and</p> <p>(2) the portion of County Rd. 1440E between the intersection of County Rd. 1430E and County Rd. 1440E and the northern border of 62218; and</p> <p>the portion of 62231 that lies to the west of the line formed by:</p> <p>(1) the section of Old State Hwy. between the western border of 62231 and the intersection of Old State Hwy. and County Hwy 13, and</p> <p>(2) the section of County Hwy 13 between the intersection of Old State Hwy. and County Hwy 13 and the southern border of 62231; and</p> <p>the portions of 62221, 62258, and 62265 that lies to the north of the line formed by State Hwy. 161.</p>
13	Renal Treatment Centers – Lincolnland	<p>The area in and/or near Springfield, Illinois, consisting of:</p> <p>Sangamon County (Illinois).</p>



Decision & Order

	<b>Divested Clinics</b>	<b>Corresponding Area Definition</b>
14	Peralta Renal Center, Piedmont Dialysis Center, Eastmont Dialysis Center, DaVita San Leandro	The area in and/or near Oakland, California, consisting of: 94501, 94502, 94546, 94577, 94578, 94579, 94601, 94602, 94603, 94604, 94605, 94606, 94607, 94608, 94609, 94610, 94611, 94612, 94613, 94614, 94618, 94619, 94620, 94621, 94622, 94623, 94624, 94625, 94643, 94649, 94659, 94660, 94661, 94662, 94666, 94702, 94703, 94704, 94705, 94710, 94712, 94720; and the portion of 94580 that lies to the north of the line formed by I-238.
15	San Joaquin Dialysis Center, Stockton Dialysis Center	The area in and/or near Stockton, California, consisting of: 95201, 95202, 95203, 95204, 95205, 95206, 95207, 95208, 95209, 95210, 95211, 95212, 95213, 95215, 95219, 95231, 95234, 95237, 95240, 95241, 95242, 95253, 95258, 95267, 95269, 95296, 95297; and the portion of 95220 that lies to the south of the line formed by: (1) the section of W. Peltier Rd. between the western border of 95220 and the intersection of W. Peltier Rd. and E. Peltier Rd., (2) the section of E. Peltier Rd. between the intersection of W. Peltier Rd. and E. Peltier Rd. and the intersection of N. Tully Rd., (3) the section of N. Tully Rd. between the intersection of E. Peltier Rd. and N. Tully Rd. and the intersection of N. Tully Rd. and E. Jahant Rd. (4) the section of E. Jahant Rd. between the intersection of N. Tully Rd. and E. Jahant Rd. and the intersection of E. Jahant Rd. and N. Mackville Rd., and (6) the section of N. Mackville Rd. between the intersection E. Jahant Rd. and N. Mackville Rd. and the eastern border of 95220.
16	DaVita Haines, DaVita Winter Haven, DaVita Lake Wales	The area in and/or near Lakeland, Florida, consisting of: Polk County (Florida).

## Decision &amp; Order

	<b>Divested Clinics</b>	<b>Corresponding Area Definition</b>
17	Gambro Healthcare – Churchland, Gambro Healthcare – Portsmouth, Gambro Healthcare – Airline Blvd.	The area in and/or near Norfolk, Virginia, that is circumscribed by the line formed by: (1) the section of I-664 between Hampton Roads Bay and the intersection of I-664 and I-64, (2) the section of I-64 between the intersection of I-664 and I-64 and the Hampton Roads Bay, and (3) the Hampton Roads Bay.
18	Gambro Healthcare – Newport News	The area in and/or near Newport News, Virginia, consisting of: 23601, 23602, 23604, 23605, 23606, 23607, 23608, 23609, 23612, 23628, 23630, 23631, 23651, 23653, 23661, 23662, 23663, 23665, 23666, 23667, 23668, 23669, 23670, 23681, 23692, 23693.
19	Chico Dialysis Center	The area in and/or near Chico, California, consisting of: 95926, 95927, 95928, 95929, 95938, 95943, 95951, 95967, 95969, 95973, 95976.
20	Omaha Dialysis Center, Baker Place Dialysis Center	The area in and/or near Omaha, Nebraska, consisting of: 51501, 51502, 51503, 51526; and Douglas County (Nebraska); <i>but excluding</i> 68022, 68064, 68069, 68068, 68007.
21	DaVita Savannah	The area in and/or near Savannah, Georgia, consisting of: the portion of Chatham County (Georgia) that lies to the east of I-95; and the portion of 29927 that lies to the south of the line formed by Route 170.

Decision & Order

	<b>Divested Clinics</b>	<b>Corresponding Area Definition</b>
22	Palm Desert Dialysis Center, Indio Dialysis Center	The area in and/or near Palm Springs, California, consisting of: 92201, 92202, 92203, 92210, 92211, 92234, 92235, 92236, 92247, 92248, 92253, 92260, 92261, 92270, 92276; and the portion of 92262 that lies to the east of the line formed by: (1) the portion of Route 111 between the northern border of 92262 and the intersection of Route 111 and Tramway Rd. and (2) the portion of Tramway Rd. between the intersection of Route 111 and Tramway Rd. and the southern border of 92262.
23	Gambro Healthcare – Fort Pierce, Gambro Healthcare – Port St. Lucie	The area in and/or near Port St. Lucie, Florida, consisting of: St. Lucie County (Florida) and 34945, 34946, 34949, 34951, 34957, 34958, 34990, 34991, 34994, 34995, and 34996.
24	DaVita Mecklenberg, DaVita University	The area in and/or near Charlotte, North Carolina, consisting of: Mecklenburg County (North Carolina).
25	DaVita Garey	The area in and/or near Pomona, California, consisting of: 91701, 91708, 91710, 91711, 91729, 91730, 91743, 91750, 91758, 91761, 91762, 91763, 91764, 91766, 91767, 91768, 91769, 91784, 91785, 91786, 91798; and the portion of 91773 that lies to the southeast of the line formed by: (1) the section of Arrow Hwy. between the eastern border of 91773 and the intersection of Arrow Hwy. and S. Lone Hill Ave., (2) the section of S. Lone Hill Ave. between the intersection of Arrow Hwy. and S. Lone Hill Ave. and the intersection of S. Lone Hill Ave. and Badillo St., and (3) the section of Badillo St. between the intersection of S. Lone Hill Ave. and Badillo St. and the western border of 91773.

FEDERAL TRADE COMMISSION DECISIONS  
VOLUME 140

Decision & Order

	<b>Divested Clinics</b>	<b>Corresponding Area Definition</b>
26	Redlands Dialysis Center, San Bernardino Dialysis Center, Dialysis Center of Colton, Rialto Dialysis Center	The area in and/or near San Bernardino, California, consisting of: 92313, 92316, 92318, 92324, 92334, 92335, 92336, 92346, 92350, 92354, 92357, 92369, 92374, 92375, 92376, 92377, 92401, 92403, 92404, 92405, 92406, 92407, 92408, 92410, 92411, 92412, 92413, 92415, 92418, 92423, 92424, 92427; the portion of 92373 that lies to the west of the line formed by: (1) the section of Alessandro Rd. between the southern border of 92373 and the intersection of Allesandro Rd. and W. Sunset Dr., (2) the section of W. Sunset Drive. between the intersection of Allesandro Rd. and W. Sunset Dr. and the intersection of W. Sunset Dr. and E. Sunset Drive S., (3) the section of E. Sunset Drive S. between the intersection of W. Sunset Dr. and E. Sunset Drive S. and the intersection of E. Sunset Drive S. and Alta Vista Dr., and (4) the section of Alta Vista Dr. between the intersection of E. Sunset Drive S. and Alta Vista Dr. and the northern border of 92373; and the portion of 92359 that lies to the west of the line formed by Crafton Ave.; <i>but excluding</i> 92317, 92321, 92322, 92325, 92352.

Decision & Order

	<b>Divested Clinics</b>	<b>Corresponding Area Definition</b>
27	Gambro Healthcare – Richmond MCV, Gambro Healthcare – Richmond MCV Downtown	The area in and/or near Richmond, Virginia, consisting of: 23075, 23218, 23219, 23220, 23221, 23222, 23223, 23224, 23225, 23226, 23227, 23228, 23230, 23231, 23240, 23241, 23249, 23269, 23272, 23273, 23274, 23279, 23282, 23284, 23285, 23286, 23290, 23291, 23292, 23293, 23295, 23298; and the portions of 23116 and 23111 that lie to the southwest of the line formed by: (1) the section of New Ashcake Rd. between the eastern border of 23116 and the intersection of New Ashcake Rd. and Rural Point Rd., (2) the section of Rural Point Rd. between the intersection of New Ashcake Rd. and Rural Point Rd. and the intersection of Rural Point Rd. and Meadowbridge Rd./Pole Green Rd., (3) the section of Meadowbridge Rd./Pole Green Rd. between the intersection of Rural Point Rd. and Meadowbridge Rd./Pole Green Rd. and the intersection of Meadowbridge Rd./Pole Green Rd. and Lee Davis Rd., (4) the section of Lee Davis Rd. between the intersection of Meadowbridge Rd./Pole Green Rd. and Lee Davis Rd. and Lee Davis Rd. and State Hwy 156, and (5) the section of State Hwy 156 between the intersection of Lee Davis Rd. and State Hwy 156 and the southern border of 23111.

FEDERAL TRADE COMMISSION DECISIONS  
VOLUME 140

Decision & Order

	<b>Divested Clinics</b>	<b>Corresponding Area Definition</b>
28	Gambro Westside	<p>The area in and/or near Hollywood, California, consisting of: 90035, 90036, 90048, 90069, 90211, 90212, 90213; the portion of 90210 to the southeast of the line formed by: (1) the section of Sunset Blvd. between the western border of 90210 and the intersection of Sunset Blvd. and N. Whittier Dr., (2) the section of N. Whittier Dr. between the intersection of Sunset Blvd. and N. Whittier Dr. and the intersection of N. Whittier Dr. and Lexington Rd., (3) the section of Lexington Rd. between the intersection of N. Whittier Dr. and Lexington Rd. and the intersection of Lexington Rd. and N. Beverly Dr., (4) the section of N. Beverly Dr. between the intersection of Lexington Rd. and N. Beverly Dr. and the intersection of N. Beverly Dr. and Coldwater Canyon Dr., (5) the section of Coldwater Canyon Dr. between the intersection of N. Beverly Dr. and Coldwater Canyon Dr. and the intersection of Coldwater Canyon Dr. and Mulholland Dr., (6) the section of Mulholland Dr. between the intersection of Coldwater Canyon Dr. and Mulholland Dr. and the intersection of Mulholland Dr. and the eastern border of 90210; and the portion of 90046 that lies to the south of the line formed by Hollywood Blvd.; and the portion of 90019 that lies to the west of the line formed by S. La Brea Ave.</p>

Decision & Order

	<b>Divested Clinics</b>	<b>Corresponding Area Definition</b>
29	Tustin Dialysis Center, Westminister North, Gambro Healthcare – Fountain Valley, Harbor Boulevard Dialysis Center, Garden Grove Dialysis Center, Irvine Dialysis Center,	The area in and/or near Irvine, California, consisting of: 92602, 92603, 92604, 92605, 92606, 92609, 92612, 92614, 92616, 92617, 92618, 92619, 92620, 92623, 92626, 92628, 92630, 92637, 92647, 92650, 92653, 92654, 92655, 90680, 92683, 92684, 92685, 92697, 92698, 92701, 92702, 92703, 92704, 92705, 92706, 92707, 92708, 92711, 92712, 92725, 92728, 92735, 92780, 92781, 92782, 92799, 92802, 92825, 92840, 92841, 92842, 92843, 92844, 92856, 92859, 92864, 92866, 92867, 92869, 92868, and 92610; <i>but excluding</i> Limestone Canyon Regional Park and Whiting Ranch Regional Park
30	Pacific Coast Dialysis Center	The area in and/or near Inglewood, California, consisting of: 90008, 90043, 90056, 90083, 90189, 90230, 90231, 90233, 90301, 90302, 90303, 90304, 90305, 90308, 90309, 90310, 90313, 90398; and the portion of 90045 that lies to the east of the line formed by Route 1.

## Decision &amp; Order

	<b>Divested Clinics</b>	<b>Corresponding Area Definition</b>
31	Gambro Healthcare – Oxon Hill, Gambro Healthcare – Silver Hill	<p>The area in and/or near Oxon Hill, Maryland, consisting of:</p> <p>20019, 20020, 20026, 20029, 20032, 20233, 20340, 20373, 20375, 20389, 20395, 20409, 20599, 20752, 20731, 20743, 20746, 20747, 20745, 20748, 20750, 20753, 20757, 20791, 20799; and</p> <p>the portion of 20744 that lies to the north of the line formed by:</p> <p>(1) the section of W. Riverview Rd. between the western border of 20744 and the intersection of W. Riverview Rd. and Riverview Rd.,</p> <p>(2) the section of Riverview Rd. between the intersection of W. Riverview Rd. and Riverview Rd. and the intersection of Riverview Rd. and Fort Washington Rd.,</p> <p>(3) the section of Fort Washington Rd. between the intersection of Riverview Rd. and Fort Washington Rd. and the intersection of Fort Washington Rd. and Route 210,</p> <p>(4) the section of Route 210 between the intersection of Fort Washington Rd. and Route 210 and the northern intersection of Route 210 and Old Fort Rd.,</p> <p>(5) the section of Old Fort Rd. between the northern intersection of Route 210 and Old Fort Rd. and the intersection of Old Fort Rd. and Allentown Rd.,</p> <p>(6) the section of Allentown Rd. between the intersection of Old Fort Rd. and Allentown Rd. and the intersection of Allentown Rd. and Steed Rd., and</p> <p>(7) the section of Steed Rd. between the intersection of Allentown Rd. and Steed Rd. and the eastern border of 20744.</p>
32	Elk Grove Dialysis Center, Roseville Dialysis Center, Placer Dialysis Center	<p>The area in and/or near Sacramento, California, consisting of:</p> <p>95650, 95661, 95677, 95678, 95746, 95747, 95765; and Sacramento County (California); <i>but excluding</i> 94571, 95615, 95632, 95638, 95641, 95680, 95683, 95686, 95690, 95693, 95837.</p>



Decision & Order

	<b>Divested Clinics</b>	<b>Corresponding Area Definition</b>
33	Potrero Hill Dialysis Center, DaVita Community Hemodialysis, DaVita Ocean Garden, South San Francisco Dialysis Center	The area in and/or near San Francisco, California, consisting of: San Francisco County (California) and 94005, 94013, 94014, 94015, 94016, 94017, 94030, 94031, 94044, 94045, 94066, 94067, 94080, 94083, 94128, 94167, 94170.
34	Gambro Healthcare – Seminole, Gambro Healthcare – Palm Harbor, Gambro Healthcare – Clearwater, DaVita Bay Area	The area in and/or near St. Petersburg, Florida, consisting of: Pinellas County (Florida).
35	Mission Dialysis Center of Oceanside, Mission Dialysis of San Diego, Mission Dialysis Center of El Cajon, DaVita Chula Vista	The area in and/or near San Diego, California, consisting of: San Diego County (California); <i>but excluding</i> 91901, 91903, 91905, 91906, 91916, 91917, 91931, 91934, 91935, 91948, 91962, 91963, 91980, 91987, 92004, 92028, 92036, 92059, 92060, 92061, 92065, 92066, 92070, 92082, 92086, 92672.

## **APPENDIX C**

### **MONITOR AGREEMENT**

**[PUBLIC RECORD VERSION]**

Decision & Order

## **MONITOR AGREEMENT**

MONITOR AGREEMENT (the "Agreement"), dated as of September 12, 2005, between DaVita Inc ("Respondent"). and John Strack and Mitch Nielson of FocalPoint Medical Consulting Group ("Monitors").

### **PRELIMINARY STATEMENT**

WHEREAS the Federal Trade Commission (the "Commission") is considering for public comment an Agreement Containing Consent Orders with Respondent, which provides, among other things, that Respondent divest a number of dialysis clinics and assets associated with those clinics, Respondent terminate management contracts Respondent has with certain dialysis clinics, enter into agreements -- if necessary --providing the acquirers of the dialysis clinics with transition services, and engage a monitor to monitor Respondent's compliance with its obligations under the Decision and Order and Asset Maintenance Order ("Orders");

WHEREAS, the Commission is expected to issue the Agreement Containing Consent Orders and appoint the Monitors pursuant to the Orders to monitor Respondent's compliance with the terms of the Orders, and the Monitors have consented to such appointment;

WHEREAS, the Orders further provide that Respondent shall execute an agreement, subject to prior approval of the Commission, conferring all the rights and powers necessary to permit the Monitors to carry out their duties and responsibilities pursuant to the Orders;

WHEREAS, this Monitor Agreement, although executed by the Monitors and Respondent, is not effective for any purpose, including but not limited to imposing rights and responsibilities on Respondent or the Monitors under the Orders, until the Asset

## Decision &amp; Order

Maintenance Order has been issued and the Monitor Agreement has been approved by the Commission;

WHEREAS, the parties to this Agreement intend to be legally bound, subject only to the Commission's approval of this Agreement.

## DEFINITIONS

1. “Respondent “DaVita” means DaVita Inc., a corporation organized, existing and doing business under and by virtue of the laws of the State of Delaware, with its office and principal place of business located at El Segundo, CA, its directors, officers, employees, agents, attorneys, representatives, predecessors, successors, and assigns; its joint ventures, divisions, groups and affiliates controlled by DaVita, and the respective directors, officers, employees, agents, attorneys, representatives, predecessors, successors, and assigns of each.
2. “Other Parties” means any Person that receives approval of the Commission to acquire any of the Assets To Be Divested or is a party to the Relevant Agreements pursuant to Paragraph II and V of the Decision and Order.
3. “Acquisition Date” means the date on which the first of the Relevant Agreements pursuant to Paragraph II and V of the Decision and Order goes into effect.
4. “Relevant Agreements” means: all the divestiture agreements, management termination agreements, and transition services agreements entered into pursuant to Paragraphs II and V of the Decision and Order, including but not limited to, the Renal Advantage Divestiture Agreements, the Colton Clinic Management Termination Agreement, the South San Francisco Clinic Management Termination Agreement, and the Transition Services Agreement between Renal Advantage Inc. and DaVita.

Decision & Order

5. All other capitalized words or phrases appearing in this Agreement that are not otherwise defined herein are deemed to have the defined meanings assigned to them in the Orders.

ARTICLE I

Powers of the Monitors. The Monitors shall have the rights, duties, powers and authority conferred upon the Monitor by the Orders that are necessary for the Monitors to monitor Respondent's compliance with the Orders. No later than one day after the Asset Maintenance Order becomes final, Respondent hereby transfers to the Monitors all rights, powers, and authorities necessary to permit the Monitor to perform his duties and responsibilities pursuant to the Asset Maintenance Order and consistent with the purposes of the Decision and Order. Any descriptions thereof contained in this Agreement in no way modify the Monitors' powers and authority or Respondent's obligations under the Orders.

Monitor's Duties. The Monitors shall monitor Respondent's compliance with the Orders, including but not limited to:

- a. Assuring that Respondent expeditiously comply with all of their obligations and perform all of their responsibilities as required by the Orders in this matter;
- b. Monitoring Relevant Agreements;
- c. Assuring that Confidential Business Information is not received or used by Respondent or Other Parties, except as allowed in the Orders in this matter.

Duration of Monitor's Authority. The Monitors shall have all powers and duties described above and consistent with the Orders for the term set forth in the Orders.

## Decision &amp; Order

Confidential and Proprietary Information. The Monitors shall enter into a confidentiality agreement, attached hereto as Confidential Exhibit A, agreeing to be bound by the terms and conditions of the Orders. The Monitors must retain and maintain all Material Confidential Information it receives from either Respondent or Relevant Parties on a confidential basis except as is permitted by the Orders. The Monitors may disclose confidential information only to persons employed by or working with the Monitors under this Agreement, to persons employed at the Commission, and as permitted by Respondent or Relevant Parties with respect to information they provided the Monitor. The Monitors shall require any person retained by the Monitor to assist in carrying out the duties and responsibilities of the Monitors to execute a confidentiality agreement that requires the same standard of care and obligations of confidentiality to which the Monitors must adhere under this Agreement. The Monitors shall maintain the confidentiality, for a period of five (5) years after the termination of this Agreement, of all other aspects of the performance of his duties under this Agreement and shall not disclose any confidential information relating thereto. Monitor reports that are provided to persons employed at the Commission, the State of Michigan, and the State of California may be shared between persons employed at the Commission, the State of Michigan, and the State of California.

Restrictions. The Monitors shall not be involved in any way in the management, production, supply and trading, sales marketing, and financial operations of the competing products of the Respondent.

Reports. Monitors shall report to the Commission pursuant to the terms of the Orders and as otherwise requested by the Commission staff.

Access to records, documents and facilities. Subject to any demonstrated legally recognized privilege, the Monitor shall have full and complete access to Respondent' personnel, books, documents, records kept in the normal course of business,

Decision & Order

facilities and technical information, and such other relevant information as the Monitors may reasonably request, related to Respondent's compliance with their obligations under the Orders in this matter. Respondent shall cooperate with any reasonable request of the Monitors and shall take no action to interfere with or impede the Monitor's ability to monitor Respondent's compliance with the Orders.

ARTICLE II

Retention and payment of Counsel, Consultants, and other Assistants. The Monitors shall have the authority to employ, at the cost and expense of the Respondent, such attorneys, consultants, accountants, and other representatives and assistants as are necessary to carry out the Monitors' duties and responsibilities as allowed pursuant to the Orders.

Compensation. The Monitors shall be compensated by Respondent for his services under this Agreement pursuant to the fee schedule attached as Confidential Exhibit B for time spent in connection with the discharge of his duties under this Agreement and the Orders. In addition, Respondent will pay: (a) out-of-pocket expenses reasonably incurred by the Monitors in the performance of his duties under the Mandate; and (b) fees and disbursements reasonably incurred by any advisor appointed by the Monitors pursuant to the first paragraph in Article II. At its own expense, Respondent may retain an independent auditor to verify such invoices. The Monitors shall provide Respondent with monthly invoices for time and expenses that include details and an explanation of all matters for which the Monitors submit an invoice to Respondent. Respondent shall pay such invoices within thirty (30) days of receipt. When filing the same report with the Commission, the State of Michigan, and the State of California, the Monitor will not charge Respondent additional fees for each report.

Decision &amp; Order

## ARTICLE III

Monitor's liabilities and indemnification. Respondent shall indemnify the Monitors and hold the Monitors harmless against any losses, claims, damages, liabilities, or expenses arising out of, or in connection with, the performance of the Monitors' duties, including all reasonable fees of counsel and other expenses incurred in connection with the preparation for, or defense of any claim, whether or not resulting in any liability, except to the extent that such losses, claims, damages, liabilities, or expenses result from misfeasance, gross negligence, willful or wanton acts, or bad faith by the Monitors.

Monitor's removal. If the Commission determines that Monitors cease to act or fail to act diligently and consistent with the purpose of the Orders, Respondent shall terminate this Agreement and appoint a substitute Monitor, subject to Commission approval and consistent with the Orders.

Approval by the Commission. This Agreement shall have no force or effect until approved by the Commission, other than Respondent obligations under Exhibit A and the confidentiality provisions herein.

Termination: This Agreement shall terminate the earlier of: (a) the date set forth in the Order; (b) Respondent's receipt of written notice from the Commission that the Commission has determined that John Strack and Mitch Nielsen have ceased to act or failed to act diligently, or are unwilling or unable to continue to serve as Monitor; (c) with at least thirty (30) days advance notice to be provided by the Monitor to Respondent and to the Commission, upon resignation of the Monitors; or (d) when DaVita's last obligation under the Orders and the Relevant Agreements that pertains to the Monitors' service has been fully performed, provided, however, that the Commission may require that DaVita extend this Monitor Agreement or enter into an additional agreement with the Monitors as may be necessary or appropriate to accomplish the purposes of the Orders. If this



Decision & Order

Monitor Agreement is terminated for any reason, the confidentiality obligations set forth in this Agreement will remain in force. The termination of the Monitors pursuant to this Monitor Agreement and Orders does not change the status of the Monitor with regard to any other Monitor Agreement entered into by Respondent with the States of Michigan and California. Termination of the Monitors pursuant to the Monitor Agreements entered into by the Respondent with the States of Michigan and California pursuant to those States' orders does not change the status of the Monitors with regard to this Monitor Agreement and Orders.

Conflicts of Interest: If the Monitors become aware during the term of this Agreement that he has or may have a conflict of interest that may affect or could have the appearance of affecting performance by the Monitor of any of his duties under this Agreement, the Monitors shall promptly inform Respondent and the Commission of any such conflict.

IN WITNESS WHEREOF, the parties hereto have caused this Agreement to be executed as of the date first above written.

MONITORS

BY: \_\_\_\_\_ BY: \_\_\_\_\_

NAME: \_\_\_\_\_ NAME: \_\_\_\_\_  
FocalPoint Medical Consulting Group

RESPONDENT

BY: \_\_\_\_\_

NAME: \_\_\_\_\_

TITLE: \_\_\_\_\_

Decision &amp; Order

**[Confidential Exhibit A and Confidential Exhibit B to the Monitor Agreement Have Been Redacted from this Public Version of the Decision and Order, but are incorporated by reference.]**

Decision & Order

**NON-PUBLIC APPENDICES**

**NON-PUBLIC APPENDIX D**

**RENAL ADVANTAGE DIVESTITURE AGREEMENTS**

[REDACTED FROM PUBLIC RECORD VERSION  
BUT INCORPORATED BY REFERENCE]

**NON-PUBLIC APPENDIX E**

**WESTSIDE CLINIC DIVESTITURE AGREEMENT**

[REDACTED FROM PUBLIC RECORD VERSION  
BUT INCORPORATED BY REFERENCE]

**NON-PUBLIC APPENDIX F**

**COLTON CLINIC DIVESTITURE AGREEMENT**

[REDACTED FROM PUBLIC RECORD VERSION  
BUT INCORPORATED BY REFERENCE]

**NON-PUBLIC APPENDIX G**

**SOUTH SAN FRANCISCO MANAGEMENT  
TERMINATION AGREEMENT**

[REDACTED FROM PUBLIC RECORD VERSION  
BUT INCORPORATED BY REFERENCE]

Order

IN THE MATTER OF

DAVITA INC.

**ORDER TO MAINTAIN ASSETS**

The Federal Trade Commission (“Commission”), having initiated an investigation of the proposed acquisition by DaVita Inc. of Gambro Healthcare Inc., a subsidiary of Gambro AB, and DaVita Inc. (hereafter referred to as “Respondent”) having been furnished thereafter with a copy of a draft of Complaint that the Bureau of Competition proposed to present to the Commission for its consideration and which, if issued by the Commission, would charge Respondent with violations of Section 7 of the Clayton Act, as amended, 15 U.S.C. § 18, and Section 5 of the Federal Trade Commission Act, as amended, 15 U.S.C. § 45; and

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

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

Order

following jurisdictional findings, and issues the following Order to Maintain Assets:

1. Respondent DaVita Inc. is a corporation organized, existing and doing business under and by virtue of the laws of the State of Delaware with its office and principal place of business located at 601 Hawaii Street, El Segundo, CA 90245.
2. The Federal Trade Commission has jurisdiction of the subject matter of this proceeding and of Respondent, and the proceeding is in the public interest.

**ORDER**

**I.**

**IT IS ORDERED** that, all capitalized terms used in this Order to Maintain Assets, but not defined herein, shall have the meanings attributed to such terms in the Decision and Order contained in the Consent Agreement.

**II.**

**IT IS FURTHER ORDERED** that:

- A. From the date DaVita signs the Consent Agreement until the Time of Divestiture of each Clinic To Be Divested and until all Assets Associated with each Clinic To Be Divested are divested pursuant to the Consent Agreement, DaVita shall:
  1. Maintain each Clinic To Be Divested and all Assets Associated with it in substantially the same condition (except for normal wear and tear) existing at the time DaVita signs the Consent Agreement;
  2. Take such actions that are consistent with the past practices of DaVita or Gambro, respectively, in

## Order

connection with such Clinic To Be Divested and the Assets Associated with it and that are taken in the Ordinary Course Of Business and in the normal day-to-day operations of DaVita or Gambro;

3. Keep available the services of the current officers, employees, and agents of DaVita; and maintain the relations and good will with Suppliers, Payors, Physicians, landlords, patients, employees, agents, and others having business relations with the Clinic To Be Divested and the Assets Associated with it in the Ordinary Course Of Business; and
  4. Preserve the Clinic To Be Divested and all Assets Associated with it as an ongoing business and not take any affirmative action, or fail to take any action within DaVita's control, as a result of which the viability, competitiveness, and marketability of the Clinic To Be Divested or all Assets Associated with it would be diminished.
- B. From the date DaVita signs the Consent Agreement until DaVita divests the Owned Real Property pursuant to the Consent Agreement, DaVita shall:
1. Maintain the Owned Real Property in substantially the same condition (except for normal wear and tear) existing at the time DaVita signs the Consent Agreement;
  2. Take such actions that are consistent with the past practices of DaVita or Gambro, respectively, in connection with the Owned Real Property and that are taken in the Ordinary Course Of Business and in the normal day-to-day operations of DaVita or Gambro; and
  3. Take no action Relating To the Owned Real Property that would diminish the viability, competitiveness, or

Order

marketability of any Clinic To Be Divested located on or in the Owned Real Property.

- C. From the date DaVita signs the Consent Agreement until the date this Order to Maintain Assets terminates pursuant to Paragraph VII, DaVita shall do the following:
1. Until sixty (60) days after the Time Of Divestiture of each Clinic To Be Divested, DaVita shall not interfere in employment negotiations between each DaVita Employee Of A Clinic To Be Divested and the Acquirer of the Clinic; *PROVIDED, HOWEVER*, this Paragraph II.C.1. does not apply to the South S.F. Clinic, to the Assets Associated with that Clinic, or to the Acquirer of that Clinic.
  2. With respect to each DaVita Employee Of A Clinic To Be Divested who receives, within sixty (60) days of the Time Of Divestiture of any Clinic at which he or she is employed, an offer of employment from the Acquirer of that Clinic, DaVita shall not prevent, prohibit or restrict or threaten to prevent, prohibit or restrict the DaVita Employee Of The Clinic To Be Divested from being employed by the Acquirer of the Clinic, and shall not offer any incentive to the DaVita Employee Of The Clinic To Be Divested to decline employment with the Acquirer of the Clinic; *PROVIDED, HOWEVER*, this Paragraph II.C.2. does not apply to the South S.F. Clinic, to the Assets Associated with that Clinic, or to the Acquirer of that Clinic.
  3. For a period of two (2) years following the Time Of Divestiture of each Clinic To Be Divested, DaVita shall not, directly or indirectly, solicit, induce, or attempt to solicit or induce any Employee Of A Clinic To Be Divested who is employed by the Acquirer to terminate his or her employment relationship with the Acquirer, unless that employment relationship has already been

## Order

terminated by the Acquirer; *PROVIDED, HOWEVER*, DaVita may make general advertisements for employees including, but not limited to, in newspapers, trade publications, websites, or other media not targeted specifically at Acquirer's employees; *PROVIDED, FURTHER, HOWEVER*, DaVita may hire employees who apply for employment with DaVita, as long as such employees were not solicited by DaVita in violation of this Paragraph II.C.3.; *PROVIDED, FURTHER, HOWEVER*, DaVita may offer employment to an Employee Of A Clinic To Be Divested who is employed by the Acquirer in only a part-time capacity, if the employment offered by DaVita would not, in any way, interfere with the employee's ability to fulfill his or her employment responsibilities to the Acquirer.

4. For a period of not less than forty-five (45) days, which period may begin prior to the signing of the Consent Agreement and which shall end no earlier than ten (10) days after the Time Of Divestiture of each Clinic To Be Divested ("Forty-Five Day Hiring Period"), DaVita shall not interfere in employment negotiations between each Regional Manager Of A Clinic To Be Divested and the Acquirer of the Clinic; *PROVIDED, HOWEVER*, the terms of this Paragraph II.C.4. shall not apply after Acquirers have hired six (6) Regional Managers who were each previously employed by DaVita or Gambro at any time since June 1, 2005; *PROVIDED, FURTHER, HOWEVER*, the terms of this Paragraph II.C.4. shall not apply to the Westside Clinic, the Colton Clinic, and the South S.F. Clinic, to the Assets Associated with those Clinics, or to the Acquirers of those Clinics.
5. With respect to each Regional Manager Of A Clinic To Be Divested who receives, within the Forty-Five Day Hiring Period required by Paragraph II.C.4. of this Order to Maintain Assets an offer of employment from the Acquirer of that Clinic, for a period of two (2) years



Order

following the Time Of Divestiture of the Clinic To Be Divested, DaVita shall not, directly or indirectly, solicit, induce, or attempt to solicit or induce any Regional Manager of the Acquirer who was previously a Regional Manager of A Clinic To Be Divested to terminate his or her employment relationship with the Acquirer unless the individual has been terminated by the Acquirer; *PROVIDED, HOWEVER*, DaVita may make general advertisements for Regional Managers including, but not limited to, in newspapers, trade publications, websites, or other media not targeted specifically at Acquirer's Regional Managers; *PROVIDED, FURTHER, HOWEVER*, DaVita may hire Regional Managers who apply for employment with DaVita, as long as such Regional Managers were not solicited by DaVita in violation of this Paragraph II.C.5.; *PROVIDED, HOWEVER*, after Acquirers have hired six (6) Regional Managers who were each previously employed by DaVita or Gambro at any time since June 1, 2005, the terms of this Paragraph II.C.5. shall apply only to those six (6) Regional Managers hired by the Acquirers; *PROVIDED, FURTHER, HOWEVER*, the terms of this Paragraph II.C.5. shall not apply to the Westside Clinic, the Colton Clinic, and the South S.F. Clinic, to the Assets Associated with those Clinics, or to the Acquirers of those Clinics.

6. With respect to each Physician who has provided services to a Clinic To Be Divested pursuant to any of the Clinic's Physician Contracts in effect at any time during the four (4) months preceding the Time Of Divestiture of the Clinic ("Contract Physician"):
  - a. DaVita shall not offer any incentive to the Contract Physician, the Contract Physician's practice group, or other members of the Contract Physician's practice group to decline to provide services to the Clinic To Be Divested, and shall eliminate any confidentiality restrictions that would prevent the Contract

## Order

Physician, the Contract Physician's practice group, or other members of the Contract Physician's practice group from using or transferring to the Acquirer of the Clinic To Be Divested any information Relating To the Operation Of The Clinic; *PROVIDED, HOWEVER*, this Paragraph II.C.6.a. does not apply to the South S.F. Clinic, to the Assets Associated with that Clinic, or to the Acquirer of that Clinic; and

- b. For a period of three (3) years following the Time Of Divestiture of each Clinic To Be Divested, DaVita shall not contract for the services of the Contract Physician, the Contract Physician's practice group, or other members of the Contract Physician's practice group for the provision of Contract Services to be performed in any of the areas that correspond to such Clinic as listed in Appendix B to the Decision and Order contained in the Consent Agreement. *PROVIDED, HOWEVER*, if the Contract Physician, or the Contract Physician's practice group, or other members of the Contract Physician's practice group were providing services to a Clinic pursuant to a contract with DaVita or Gambro in effect as of June 1, 2005, then DaVita may contract with such Contract Physicians, or the Contract Physician's practice group, or other members of the Contract Physician's practice group for services to be provided to that particular Clinic; *PROVIDED, FURTHER, HOWEVER*, the terms of this Paragraph II.C.6.b. shall not apply to the Westside Clinic, the Colton Clinic, and the South S.F. Clinic, to the Assets Associated with those Clinics, or to the Acquirers of those Clinics; *PROVIDED, FURTHER, HOWEVER*, the terms of this Paragraph II.C.6.b. shall not apply, in Kent County, Michigan, to Renal Associates of Grand Rapids if, prior to the date the Appendix A Clinic Assets are divested pursuant to the Consent Agreement, DaVita terminates, in writing, any

Order

contractual rights DaVita has with Renal Associates of Grand Rapids that prevent or hinder, in any way, the ability of Renal Associates of Grand Rapids, to contract with, or offer services to, any Person other than DaVita.

7. With respect to Material Confidential Information relating exclusively to any of the Clinics To Be Divested, DaVita shall:
  - a. not disclose such information to any Person other than the Acquirer of such Clinic;
  - b. after the Time Of Divestiture of such Clinic:
    - (1) not use such information for any purpose other than complying with the terms of the Consent Agreement or with any law; and
    - (2) destroy all records of such information, except to the extent that: (1) DaVita is required by law to retain such information, and (2) DaVita's inside or outside attorneys may keep one copy solely for archival purposes, but may not disclose such copy to the rest of DaVita.
8. For two (2) years following the Time Of Divestiture of each Clinic To Be Divested, DaVita shall not solicit the business of any patients that received any goods or services from such Clinic between May 1, 2005, and the date of such divestiture, *PROVIDED, HOWEVER*, DaVita may (i) make general advertisements for the business of such patients including, but not limited to, in newspapers, trade publications, websites, or other media not targeted specifically at such patients, and (ii) provide advertising and promotions directly to any patient that initiates discussions with, or makes a request to, any DaVita employee.

## Order

9. DaVita shall do nothing to prevent or discourage Suppliers that, prior to the Time Of Divestiture of any Clinic To Be Divested, supplied goods and services for use in any Clinic To Be Divested from continuing to supply goods and services for use in such Clinic.
- D. The purpose of Paragraph II of this Order to Maintain Assets is:
1. to preserve the Clinics To Be Divested and the Assets To Be Divested as viable, competitive, and ongoing businesses, to prevent their destruction, removal, wasting, deterioration, or impairment, and to prevent interim harm to competition, pending the relevant divestitures and other relief;
  2. to preserve the good will of the employees and Regional Managers of the Clinics To Be Divested and of the Physicians, Suppliers, and patients that do business with those Clinics; and
  3. to prevent Material Confidential Information relating exclusively to the Clinics To Be Divested from being exchanged with DaVita's retained dialysis businesses.

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

- A. John Strack and Mitch S. Nielson, CPA, of Focal Point Medical Consulting Group, shall be appointed Monitors to assure that DaVita expeditiously complies with all of its obligations and performs all of its responsibilities as required by the Consent Agreement and by this Order to Maintain Assets.

Order

- B. No later than one (1) day after this Order to Maintain Assets is made final, DaVita shall, pursuant to the Monitor Agreement and to this Order to Maintain Assets, transfer to the Monitors all the rights, powers, and authorities necessary to permit the Monitors to perform their duties and responsibilities in a manner consistent with the purposes of the Consent Agreement and this Order to Maintain Assets.
  
- C. In the event a substitute Monitor is required, the Commission shall select the Monitor, subject to the consent of DaVita, which consent shall not be unreasonably withheld. If DaVita has not opposed, in writing, including the reasons for opposing, the selection of a proposed Monitor within ten (10) days after notice by the staff of the Commission to DaVita of the identity of any proposed Monitor, DaVita shall be deemed to have consented to the selection of the proposed Monitor. Not later than ten (10) days after appointment of a substitute Monitor, DaVita shall execute an agreement that, subject to the prior approval of the Commission, confers on the Monitor all the rights and powers necessary to permit the Monitors to monitor DaVita's compliance with the terms of the Consent Agreement and this Order to Maintain Assets in a manner consistent with the purposes of this Order to Maintain Assets.
  
- D. DaVita shall consent to the following terms and conditions regarding the powers, duties, authorities, and responsibilities of the Monitors:
  - 1. The Monitors shall have the power and authority to monitor DaVita's compliance with the terms of the Consent Agreement and this Order to Maintain Assets, and shall exercise such power and authority and carry out the duties and responsibilities of the Monitors in a manner consistent with the purposes of the Consent Agreement and this Order to Maintain Assets and in consultation with the Commission, including, but not limited to:

## Order

- a. Assuring that DaVita expeditiously complies with all of its obligations and performs all of its responsibilities as required by the Consent Agreement and this Order to Maintain Assets;
  - b. Monitoring any transition services agreements;
  - c. Assuring that Material Confidential Information is not received or used by DaVita or the Acquirers, except as allowed in the Consent Agreement and in this Order to Maintain Assets, in this matter.
2. The Monitors shall act in a fiduciary capacity for the benefit of the Commission.
3. The Monitors shall serve for such time as is necessary to monitor DaVita's compliance with the provisions of the Consent Agreement and this Order to Maintain Assets.
4. Subject to any demonstrated legally recognized privilege, the Monitors shall have full and complete access to DaVita's personnel, books, documents, records kept in the Ordinary Course Of Business, facilities and technical information, and such other relevant information as the Monitors may reasonably request, related to DaVita's compliance with its obligations under the Consent Agreement and this Order to Maintain Assets. DaVita shall cooperate with any reasonable request of the Monitors and shall take no action to interfere with or impede the Monitors' ability to monitor DaVita's compliance with the Consent Agreement and this Order to Maintain Assets.
5. The Monitors shall serve, without bond or other security, at the expense of DaVita on such reasonable and customary terms and conditions as the Commission may set. The Monitors shall have authority to employ, at the expense of DaVita, such consultants, accountants,

Order

attorneys and other representatives and assistants as are reasonably necessary to carry out the Monitors' duties and responsibilities. The Monitors shall account for all expenses incurred, including fees for services rendered, subject to the approval of the Commission.

6. DaVita shall indemnify the Monitors and hold the Monitors harmless against any losses, claims, damages, liabilities, or expenses arising out of, or in connection with, the performance of the Monitors' duties, including all reasonable fees of counsel and other reasonable expenses incurred in connection with the preparations for, or defense of, any claim, whether or not resulting in any liability, except to the extent that such losses, claims, damages, liabilities, or expenses result from misfeasance, gross negligence, willful or wanton acts, or bad faith by the Monitors.
7. DaVita shall report to the Monitors in accordance with the requirements of this Order to Maintain Assets and/or as otherwise provided in any agreement approved by the Commission. The Monitors shall evaluate the reports submitted to the Monitors by DaVita, and any reports submitted by the Acquirer with respect to the performance of DaVita's obligations under the Consent Agreement and this Order to Maintain Assets.
8. Within one (1) month from the date the Monitors are appointed pursuant to this paragraph, every sixty (60) days thereafter, and otherwise as requested by the Commission, the Monitor shall report in writing to the Commission concerning performance by DaVita of its obligations under the Consent Agreement and this Order to Maintain Assets.
9. DaVita may require the Monitors and each of the Monitors' consultants, accountants, attorneys, and other representatives and assistants to sign a customary

## Order

confidentiality agreement; *PROVIDED, HOWEVER*, such agreement shall not restrict the Monitors from providing any information to the Commission.

- E. The Commission may, among other things, require the Monitors and each of the Monitors' consultants, accountants, attorneys, and other representatives and assistants to sign an appropriate confidentiality agreement Relating To Commission materials and information received in connection with the performance of the Monitors' duties.
- F. If the Commission determines that the Monitors have ceased to act or failed to act diligently, the Commission may appoint a substitute Monitor in the same manner as provided in this Paragraph III.
- G. The Commission may on its own initiative, or at the request of the Monitors, issue such additional orders or directions as may be necessary or appropriate to assure compliance with the requirements of the Consent Agreement and this Order to Maintain Assets

**IV.**

**IT IS FURTHER ORDERED** that, beginning fifteen (15) days after the date on which DaVita signs the Consent Agreement and every thirty (30) days thereafter until this Order to Maintain Assets terminates pursuant to Paragraph VII, DaVita shall submit to the Commission a verified written report setting forth in detail the manner and form in which it intends to comply, is complying, and has complied with the terms of this Order to Maintain Assets. DaVita shall submit at the same time a copy of these reports to the Monitors, if any Monitors have been appointed.



Order

**V.**

**IT IS FURTHER ORDERED** that DaVita shall notify the Commission at least thirty (30) days prior to:

- A. Any proposed dissolution of DaVita,
- B. Any proposed acquisition, merger or consolidation of DaVita, or
- C. Any other change in DaVita that may affect compliance obligations arising out of this Order to Maintain Assets, including but not limited to assignment, the creation or dissolution of subsidiaries, or any other change in DaVita.

**VI.**

**IT IS FURTHER ORDERED** that, for the purpose of determining or securing compliance with this Order to Maintain Assets, and subject to any legally recognized privilege, and upon written request with reasonable notice to DaVita, DaVita shall permit any duly authorized representative of the Commission:

- A. Access, during office hours of DaVita and in the presence of counsel, to all facilities and access to inspect and copy all books, ledgers, accounts, correspondence, memoranda, and all other records and documents in the possession or under the control of DaVita related to compliance with this Order to Maintain Assets; and
- B. Upon five (5) days' notice to DaVita and without restraint or interference from DaVita, to interview officers, directors, or employees of DaVita, who may have counsel present, regarding such matters.

Order

**VII.**

**IT IS FURTHER ORDERED** that this Order to Maintain Assets shall terminate at the earlier of:

- A. three (3) business days after the Commission withdraws its acceptance of the Consent Agreement pursuant to the provisions of Commission Rule 2.34, 16 C.F.R. § 2.34; or
- B. such time as (1) all Assets To Be Divested have been divested, and all Management Contracts have been terminated, pursuant to the terms of the Consent Agreement, and (2) the Decision and Order has been made final.

Analysis

## **Analysis of Agreement Containing Consent Orders to Aid Public Comment**

### **I. Introduction**

The Federal Trade Commission (“Commission”) has accepted, subject to final approval, an Agreement Containing Consent Orders (“Consent Agreement”) from DaVita Inc. (“DaVita”). The purpose of the Consent Agreement is to remedy the anticompetitive effects resulting from DaVita’s purchase of Gambro Healthcare Inc. (“Gambro”) from Gambro AB. Under the terms of the Consent Agreement, DaVita is required to divest 69 dialysis clinics and terminate 2 management services contracts in 35 markets across the United States.

The Consent Agreement has been placed on the public record for 30 days to solicit comments from interested persons. Comments received during this period will become part of the public record. After 30 days, the Commission will again review the Consent Agreement and the comments received, and will decide whether it should withdraw from the Consent Agreement or make it final.

Pursuant to an Agreement dated December 6, 2004, DaVita proposes to acquire Gambro from Gambro AB for approximately \$3.1 billion. The Commission’s complaint alleges that the proposed acquisition, if consummated, would violate Section 7 of the Clayton Act, as amended, 15 U.S.C. § 18, and Section 5 of the Federal Trade Commission Act, as amended, 15 U.S.C. § 45, by lessening competition in the market for the provision of outpatient dialysis services in 35 markets.

### **II. The Parties**

Headquartered in El Segundo, California, DaVita is the second largest provider of outpatient dialysis services in the United States. DaVita operates 665 outpatient dialysis clinics in 37 states and the District of Columbia at which approximately 55,000 end

## Analysis

stage renal disease (“ESRD”) patients receive treatment. In 2003, DaVita’s revenues were approximately \$2.1 billion.

Gambro AB is a publicly-traded Swedish corporation with worldwide operations focused in three business fields: operating dialysis centers, manufacturing dialysis equipment, and providing technology and products to blood centers and hospital blood banks. Gambro is Gambro AB’s entire U.S. dialysis services business. Gambro, headquartered in Denver, Colorado, is the third largest provider of outpatient dialysis services in the United States, with 565 outpatient dialysis clinics serving approximately 43,200 ESRD patients in 33 states and the District of Columbia. In 2003, Gambro’s revenues were approximately \$1.8 billion.

### **III. Outpatient Dialysis Services**

Outpatient dialysis services is the appropriate relevant product market in which to assess the effects of the proposed transaction. For patients suffering from ESRD, dialysis treatments are a life-sustaining therapy that replaces the function of the kidneys by removing toxins and excess fluid from the blood. Most ESRD patients receive dialysis treatments three times per week in sessions lasting between three and five hours. Kidney transplantation is the only alternative to dialysis for ESRD patients. However, the wait-time for donor kidneys -- during which ESRD patients must receive dialysis treatments -- can exceed five years. Additionally, many ESRD patients are not viable transplant candidates. As a result, many ESRD patients have no alternative to ongoing dialysis treatments.

The relevant geographic markets for the provision of dialysis services are local in nature. They are limited by the distance ESRD patients are willing and/or able to travel to receive dialysis treatments. Most ESRD patients are quite ill and suffer from multiple health problems. As such, it is difficult for ESRD patients to travel long distances for dialysis treatment. Generally, ESRD patients are unwilling and/or unable to travel further than 30 miles or 30 minutes to receive dialysis treatments, depending

Analysis

on traffic patterns, local geography, and the patient's proximity to the nearest center. As a result, competition among dialysis clinics occurs at a local level, corresponding to metropolitan areas or subsets thereof.

Entry into the outpatient dialysis services markets addressed by the Consent Agreement on a level sufficient to deter or counteract the likely anticompetitive effects of the proposed transaction is not likely to occur in a timely manner. The primary barrier to entry is the difficulty associated with locating nephrologists with established patient pools to serve as medical directors. By law, each dialysis clinic must have a nephrologist medical director. As a practical matter, medical directors are essential to the success of a clinic because they are the primary source of referrals. The lack of available nephrologists with an established referral stream is a significant barrier to entry into each of the relevant markets. Beyond that, entry is also inhibited where certain attributes (such as a rapidly growing ESRD population, a favorable regulatory environment, average or below nursing and labor costs, and a low penetration of managed care) are not present, as is the case in many of the geographic markets identified in the Commission's complaint.

Each of the geographic markets addressed by the Consent Agreement is highly concentrated. The proposed acquisition represents a merger to monopoly in 11 markets and would cause the number of providers to drop from 3 to 2 in 13 other markets. Additionally, concentration increases significantly in the remaining 11 markets addressed by the Consent Agreement. In each of these markets, the post-acquisition HHI exceeds 4,000, and the change in HHI is at least 800. The high post-acquisition concentration levels, along with evidence of DaVita and Gambro's head-to-head competition in these markets, indicates that the combined firm would be able to exercise unilateral market power. The evidence shows that health insurance companies and other private payors who pay for dialysis services used by their members benefit from direct competition between DaVita and Gambro when negotiating the rates to be charged by the dialysis

## Analysis

provider. As a result, the proposed combination likely would result in higher prices and diminished service and quality for outpatient dialysis services in many geographic markets.

#### **IV. The Consent Agreement**

The Consent Agreement effectively remedies the proposed acquisition's anticompetitive effects in 35 markets where both DaVita and Gambro operate dialysis clinics by requiring DaVita to divest -- prior to acquiring Gambro -- 68 outpatient dialysis clinics to Renal Advantage and one outpatient dialysis clinic to its medical directors and their partners. The Consent Agreement also requires DaVita to terminate two management services agreements pursuant to which it manages outpatient dialysis clinics on behalf of third-party owners. As with the divestitures, termination of these management services agreements will ensure that these clinics remain viable independent competitors.

As part of these divestitures, DaVita is required to obtain the agreement of the medical directors affiliated with the divested clinics to continue providing physician services after the transfer of ownership to Renal Advantage. Similarly, the Consent Agreement requires DaVita to obtain the consent of all lessors necessary to assign the leases for the real property associated with the divested clinics to Renal Advantage. These provisions ensure that Renal Advantage will have the assets necessary to operate the divested clinics in a competitive manner.

The Consent Agreement contains several additional provisions designed to ensure that the divestitures are successful. First, the Consent Agreement provides Renal Advantage with the opportunity to interview and hire employees affiliated with the divested clinics and prevents DaVita from offering these employees incentives to decline Renal Advantage's offer of employment. This will ensure that Renal Advantage has access to patient care and supervisory staff who are familiar with the clinics' patients and the local physicians. Second, the Consent Agreement prevents DaVita from contracting with the medical

Analysis

directors (or their practice groups) affiliated with the divested clinics for three years. This provides Renal Advantage with sufficient time to build goodwill and a working relationship with its medical directors before DaVita can attempt to capitalize on its prior relationships in soliciting their services. Third, to ensure continuity of patient care and records as Renal Advantage implements its quality care, billing, and supply systems, the Consent Agreement allows DaVita to provide transition services for a period of 12 months. Firewalls and confidentiality agreements have been established to ensure that competitively sensitive information is not exchanged. Fourth, the Consent Agreement requires DaVita to provide Renal Advantage with a license to use DaVita's policies and procedures, as well as the option to obtain DaVita's medical protocols, which will further enhance Renal Advantage's ability to provide continuity of care to patients. Finally, the Consent Agreement requires DaVita to provide prior notice to the Commission of its planned acquisitions of dialysis clinics located in the 35 markets addressed by the Consent Agreement. This provision ensures that subsequent acquisitions do not adversely impact competition in the markets at issue and undermine the remedial goals of the proposed order.

The Commission is satisfied that Renal Advantage is a qualified acquirer of the divested assets. Renal Advantage is a newly-formed company whose management has extensive experience operating, acquiring, and developing outpatient dialysis clinics. The company has received a substantial equity investment from Welsh, Carson, Anderson, and Stowe, which is the largest healthcare-focused private equity firm in the United States.

The Commission has appointed Mitch Nielson and John Strack of FocalPoint Medical Consulting Group ("FocalPoint") as Monitors to oversee the transition service agreements, and the implementation of, and compliance with, the Consent Agreement. Messrs. Nielson and Strack are the principles of FocalPoint, which provides consulting services to the healthcare industry.

## Analysis

The purpose of this analysis is to facilitate public comment on the Consent Agreement, and it is not intended to constitute an official interpretation of the proposed Decision and Order or the Order to Maintain Assets, or to modify their terms in any way.



Commission Opinion

**IN THE MATTER OF**

**NORTH TEXAS SPECIALTY PHYSICIANS**

OPINION OF THE COMMISSION AND FINAL ORDER IN REGARD TO  
ALLEGED VIOLATIONS OF SEC. 5 OF THE  
FEDERAL TRADE COMMISSION ACT

*Docket 9312; File No. 0210075*

*Complaint, September 16, 2003--Opinion and Final Order, November 29, 2005*

In a unanimous Opinion, the Commission addressed practices engaged in by Respondent North Texas Specialty Physicians, an association of approximately 480 physician members in the Fort Worth, Texas area. The Commission concluded that certain of the respondent's contracting activities with payors violated Section 5 of the Federal Trade Commission Act. The Final Order, among other things, prohibits the respondent from entering into, adhering to, participating in, maintaining, organizing, implementing, enforcing, or otherwise facilitating any combination, conspiracy, agreement, or understanding between physicians with respect to their provision of physician services: (1) to negotiate on behalf of any physician with any payor; (2) to deal, refuse to deal, or threaten to refuse to deal with any payor; (3) regarding any term, condition, or requirement upon which any physician deals, or is willing to deal, with any payor, including, but not limited to price terms; or (4) not to deal individually with any payor, or not to deal with any payor through any arrangement other than the respondent. The Order also prohibits the respondent from exchanging or facilitating the exchange or transfer of information among physicians concerning any physician's willingness to deal with a payor, or the terms or conditions, including price terms, on which the physician is willing to deal.

*Participants*

For the Commission: *Michael J. Bloom, Susan Raitt, Theodore Zang, Jonathan W. Platt, Elvia P. Gastelo, Mazor H. Matzkevich, Alan B. Loughnan, Matthew J. Reilly, Asheesh Agarwal, John P. Wiegand, Nancy Caban, Barbara Anthony, Thomas R. Iosso, and Louis Silvia.*

For the Respondent: *Gregory S. C. Huffman, William M. Katz, Gregory D. Binns, and Nicole Rittenhouse, Thompson & Knight LLP.*

Commission Opinion

**OPINION OF THE COMMISSION**

By LEARY, Commissioner, For A Unanimous Commission:

**I. Introduction**

This case involves the question of whether an independent physician association's contracting activities with payors amounts to unlawful horizontal price fixing, or is competitively benign activity that may enhance efficiency and innovation in the delivery of health care. The Commission has accepted numerous consent orders over the last ten years involving conduct similar to that at issue in the case at hand.<sup>1</sup> The common theme of these cases has been coordinated bargaining by groups of competing physicians, in order to increase their reimbursement rates. In these cases, competing physicians have often joined together in independent practice associations (IPAs, or networks) and agreed to boycott or refuse to deal with particular payors during contract negotiations.

---

<sup>1</sup> See, e.g., *In the Matter of San Juan IPA, Inc.*, Docket No. C-4142 (consent order issued June 30, 2005), <http://www.ftc.gov/opa/2005/07/fyi0548.htm>; *In the Matter of New Millennium Orthopaedics, LLC*, Docket No. C-4140 (consent order issued June 13, 2005), <http://www.ftc.gov/opa/2005/06/fyi0543.htm>; *In the Matter of White Sands Health Care System, L.L.C.*, Docket No. C-4130 (consent order issued Jan. 11, 2005), <http://www.ftc.gov/opa/2005/01/fyi0504.htm>; *In the Matter of Piedmont Health Alliance, Inc.*, Docket No. 9314 (consent order issued Oct. 1, 2004), <http://www.ftc.gov/opa/2004/10/fyi0457.htm>; *In the Matter of Southeastern New Mexico Physicians IPA, Inc.*, Docket No. C-4113 (consent order issued Aug. 5, 2004), <http://www.ftc.gov/opa/2004/08/fyi0445.htm>; *In the Matter of California Pacific Medical Group, Inc.*, Docket No. 9306 (consent order issued May 10, 2004), <http://www.ftc.gov/opa/2004/05/fyi0431.htm>.

Commission Opinion

When the competing physicians are not financially or clinically integrated in a manner that is likely to produce efficiencies, the Commission has consistently maintained that this type of conduct amounts to illegal price fixing.

We recognize that physicians can join together and negotiate fees in ways that do not harm competition. Health care providers (including physicians) and those who pay for their services (*i.e.*, payors) are increasingly developing new and innovative approaches to health care delivery in order to increase quality and contain costs. It is important not only to protect health care consumers from anticompetitive activity, but also to avoid interference with this procompetitive activity.

We therefore approach this case with full recognition that innovative approaches to health care should be encouraged. We also recognize the frustration of many physicians over their perceived lack of bargaining power in negotiations with large health care payors. The Commission has already provided extensive guidance on the ways to accommodate both of these concerns, consistent with the antitrust laws.<sup>2</sup>

---

<sup>2</sup> The Commission, along with the Department of Justice, recently issued a report on competition policy and health care, which was based on 27 days of public hearings covering a broad range of health care topics, all focused on ways to promote innovative, cost effective and high quality health care services. The Fed. Trade Comm'n and the U.S. Dep't of Justice, *Improving Health Care: A Dose of Competition* (July 2004), <http://www.ftc.gov/reports/healthcare/040723healthcarerpt.pdf> [hereinafter *Health Care Hearings and Report*]. In addition, Commission staff regularly issue advisory letters to physician IPAs seeking advice on proposals for financial and clinical integration. A good example is the Commission staff's advisory letter to MedSouth, Inc., where staff did not object to a clinical integration proposal by an IPA that involved joint setting of fees. Advisory Opinion Letter from Jeffrey W. Brennan, Esq., FTC, to

## Commission Opinion

This is the first physician network case in over 20 years where the Commission has the benefit of a full administrative trial and record. This case thus presents an opportunity not only to resolve a specific controversy but also to provide some guidance to the health care community on the appropriate boundary between pro-competitive and anti-competitive activities.

The Administrative Law Judge (ALJ) concluded that Respondent North Texas Specialty Physicians' (NTSP) activities constitute unlawful horizontal price fixing, and that Respondent's collective price setting was not ancillary to any procompetitive activity. After our own *de novo* review of the facts, we agree with the ALJ's conclusions and affirm his decision.<sup>3</sup> We adopt the

---

John J. Miles, Esq., Ober, Kaler, Grimes and Shriver 4 (Feb. 19, 2002), <http://www.ftc.gov/bc/adops/medsouth.htm> [hereinafter *MedSouth*]. The Commission and the Department of Justice have also issued extensive guidelines for antitrust enforcement policy in health care. See U.S. Dep't of Justice & Fed. Trade Comm'n, *Statements of Antitrust Enforcement Policy in Health Care* (1996) reprinted in 4 Trade Reg. Rep. (CCH) ¶ 13,153 [hereinafter *Health Care Statements*]; see also Thomas B. Leary, *Special Challenges for Antitrust in Health Care*, 18 No. 2 A.B.A. SEC. ANTITRUST 23 (Spring 2004).

<sup>3</sup> This opinion uses the following abbreviations for citations:

ID - Initial Decision

IDF - Numbered Findings of Fact in the Initial Decision

CX - Complaint Counsel Exhibit

RX - Respondent Exhibit

Tr. - Transcript of Testimony before the Administrative Law Judge

IH - Transcript of Investigational Hearing

Dep. - Transcript of Deposition

O.A. - Transcript of Oral Argument on Appeal

CCAB - Complaint Counsel's Appeal Brief

RAB - Respondent's Appeal Brief

Commission Opinion

findings of fact of the Initial Decision to the extent those findings are not inconsistent with this opinion.

We find that the activities of Respondent, taken as a whole, amount to horizontal price fixing which is unrelated to any procompetitive efficiencies. Respondent's conduct could be characterized as *per se* unlawful under the antitrust laws, and thus subject to summary condemnation. For the reasons explained below, however, it is more appropriate to apply the "inherently suspect" analysis of our recent decision, *Polygram Holding, Inc.*,<sup>4</sup> as affirmed by the D.C. Circuit, *Polygram Holding, Inc. v. FTC*, 416 F.3d 29 (D.C. Cir. 2005). But, we also emphasize that a *per se* analysis and an inherently suspect analysis are close neighbors, and that the determination of illegality here does not require an elaborate inquiry into effects in the market.

## II. Background

### A. Respondent's Activities

NTSP is an organization of independent physicians and physician groups that was formed, and is managed and operated by, physicians. Although its size has varied, NTSP had approximately 575 members in 2003 and 480 members at the time of trial in April 2004. IDF 32. As of 2003, NTSP was comprised of practitioners in 26 medical specialties as well as some primary

---

RR - Respondent's Reply Brief

References to investigational hearing or deposition transcripts included in the trial record as exhibits are made using the exhibit number with the witness' name and type of interview provided in parentheses: CX\_\_ (Van Wagner Dep. at \_\_).

<sup>4</sup> 5 Trade Reg. Rep. (CCH) ¶ 15,453 (FTC 2003), available at <http://www.ftc.gov/os/2003/07/polygramopinion.pdf> [hereinafter *Polygram*, or *Polygram Comm'n Op.*].

## Commission Opinion

care physicians. *Id.* These doctors are located principally in the Tarrant County, Texas area, which includes the city of Fort Worth. IDF 31. The participant physicians have distinct economic interests reflecting their separate clinical practices. IDF 35. Many members compete with one another. IDF 36.

NTSP's main functions are to negotiate and review contract proposals for member services that are submitted by payors, including insurance companies and health plans; to review payment issues; and to act as a lobbyist for its members' interests. IDF 39. NTSP negotiates both risk-sharing contracts (risk contracts)<sup>5</sup> and non-risk-sharing contracts (non-risk contracts). IDF 46. The former typically reimburse doctors on a dollar amount per patient basis, whereas the latter provide "fee-for-service" payment. IDF 13-15. The challenged conduct in this case involves solely the negotiation of non-risk contracts, which are far more common for NTSP.<sup>6</sup> IDF 46, 48-50. NTSP's original focus was on risk contracting when it was founded in 1995. IDF 19, 46. The initial interest of payors in NTSP's risk contract declined, however, and by 2001 NTSP's Board decided to center its focus on how to benefit its members for fee-for-service contracts in addition to risk contracts. IDF 46-50; CX 83 at 3. NTSP's Board has acknowledged that risk contracting "is a small part of the business." CX 83 at 3; IDF 46-50. In fact, at the time of oral argument, NTSP had only one risk contract (albeit a substantial one). IDF 49. Only about half of NTSP's physicians participate in its one risk contract. IDF 51; Van Wagner Tr. 1830; Frech Tr. 1353-54.

---

<sup>5</sup> Risk-sharing contracts are also known as capitation contracts.

<sup>6</sup> NTSP has 20 non-risk contracts. IDF 50; CX 1196 (Van Wagner IH at 14). It does not receive revenues from these contracts; it does, however, receive revenues from its one risk contract. IDF 21.

Commission Opinion

NTSP's physicians enter into a Physician Participation Agreement (PPA) with NTSP that grants NTSP the right to receive all payor offers and imposes on the physicians a duty to forward payor offers to NTSP promptly. CX 0276; CX 275 at 24. The physicians agree that they will not individually pursue a payor offer unless and until they are notified by NTSP that it has permanently discontinued negotiations with the payor. CX 0311 at 10; CX 0276; CX 1178 (Hollander Dep. at 68). Each NTSP member's PPA provides that NTSP must promptly forward (messenger) the fee reimbursement and other economic provisions of any non-risk offer to the member physicians. CX 275 at 24. If more than 50 percent of the members accept those provisions, NTSP will then proceed to negotiate the contract. IDF 67; CX 275 at 25-26. At times NTSP has gathered powers of attorney from its physicians, which give NTSP the legal authority to negotiate non-risk contracts on behalf of those physicians. CX 1173 (Deas IH at 56-57); Palmisano Tr. 1250-51.

NTSP conducts annual polls of its physicians to determine minimum reimbursement rates for use in negotiation of health maintenance organization (HMO) and preferred provider organization (PPO) product contracts with payors. CX 1195 (Van Wagner Dep. at 66-67). NTSP's polling form asks physicians individually for the minimum payments that they would accept for the provision of medical services pursuant to a fee-for-service HMO or PPO agreement. CX 0565; CX 1196 (Van Wagner IH at 26-29, 43-44, 62). NTSP uses the poll responses to calculate the mean, median, and mode (averages) of the minimum acceptable fees identified by its physicians, and then uses these measures to establish its minimum contract prices. IDF 93. NTSP then reports these measures back to its participating physicians. CX 0103 at 4-5; CX 1196 (Van Wagner IH at 26-29, 43-44, 62); CX 1042. NTSP's polling form explains to the participating physicians that "NTSP polls its affiliates and membership to establish Contracted Minimums. NTSP then utilizes these minimums when negotiating managed care contracts on behalf of its participants." CX 0387 at 1; CX 0633.

## Commission Opinion

**B. History of the Case and Summary of Initial Decision**

The Commission's complaint, issued on September 16, 2003, charges NTSP with the unlawful negotiation of agreements among its physicians on price and other terms, refusal to deal with payors except on collectively agreed-upon terms, and refusal to submit payor offers to its physicians unless the terms complied with NTSP's minimum-fee standards. Administrative Law Judge D. Michael Chappell filed an Initial Decision upholding the complaint on November 8, 2004.

In the Initial Decision the ALJ found that NTSP is controlled by its participant physicians and had taken collective action to establish and extract fee concessions from payors. ID at 52-56, 64-66, 70-83. The ALJ rejected the claim that NTSP was a single entity incapable of conspiring with its members. *Id.* at 70-71. He concluded that NTSP's conduct amounted to "a horizontal price fixing agreement." *Id.* at 86. He recognized that courts have applied *per se* analysis to horizontal price fixing, and made a number of specific findings that would support this characterization. IDF 364-80. However, he did not ultimately conclude that NTSP's conduct was *per se* unlawful. Instead, he followed the Supreme Court's analysis in *California Dental Ass'n v. FTC*, 526 U.S. 756 (1999), and distinguished NTSP's conduct from the conduct of the dentists' group in that case. ID at 85-88.

The ALJ found that the PPA gives NTSP the exclusive right initially to negotiate with payors and requires physicians to submit to NTSP offers that they may individually receive. IDF 65. Physicians may negotiate individually only after NTSP discontinues its efforts. IDF 66. The ALJ also found that NTSP reinforces this negotiation exclusivity by powers of attorney or agency authorizations it receives from its members, and that it urges its members to tell payors to communicate their offers directly to NTSP. IDF 70, 76-82.

The ALJ found that, despite the requirements in the PPA, NTSP actually messengers to its members only those non-risk



Commission Opinion

contract proposals in which reimbursement fees exceed NTSP's minimum reimbursement schedule developed from the annual poll of members. IDF 68, 85, 87. This rate is expressed as some percentage of Medicare's Resource Based Relative Value System, a fee schedule used to set the reimbursement amounts Medicare will pay for thousands of different services. IDF 10-12, 89-90. Although doctors do not consult with each other about their responses to the poll, NTSP computes the responses and informs its members of the averages. IDF 92-94. The ALJ found that this information enables members to assess the benefits of collective contracts through NTSP and reduces their uncertainty about other members' price-setting intentions. IDF 99-100.

The Initial Decision described NTSP's negotiations with three health plans – United, Cigna and Aetna, in which NTSP exercised its negotiating authority through its PPA and/or agency agreements or powers of attorney, and utilized its minimum reimbursement schedule. ID at 74-82. In several instances in these negotiations NTSP terminated, or threatened to terminate, its contract with a health plan. *Id.*

The ALJ rejected Respondent's claim that it was a single entity incapable of conspiring with its members, ID at 70-71, and held that evidence of direct agreements among physicians was not needed to demonstrate the conspiracy. *Id.* at 68-69. The ALJ relied on *Arizona v. Maricopa County Medical Society*, 457 U.S. 332, 356 (1982), where the Court found concerted action without finding that the competing physicians agreed directly with each other to set prices. The ALJ also found that NTSP had offered no plausible claim that its collective price setting was ancillary to any procompetitive activity. ID at 87. He therefore concluded that "the actions taken by NTSP to coerce health insurance payors to increase their offers of rate reimbursement or to offer more favorable economic terms to NTSP's physicians constitute an unreasonable restraint of trade." ID at 88. He also found that NTSP's actions had caused payors to increase their offers, and concluded that this fact provided sufficient evidence of anticompetitive effects, to the extent an examination of effects is

## Commission Opinion

required. *Id.* at 87. The ALJ issued an order that requires NTSP to cease and desist from collective price fixing in its negotiation of non-risk contracts and to terminate any existing non-risk contracts. *Id.* at 92-97.

C. Questions Raised by the Appeal

1. Respondent's Appeal

Respondent appeals from the ALJ's determination that its conduct violated Section 5 of the FTC Act, and also maintains that the ALJ's cease and desist order is not appropriate. Respondent's supporting arguments sometimes overlap, but may be sorted out as follows:

First, Respondent argues that the Commission lacks jurisdiction over NTSP because it is a memberless non-profit organization, which is not engaged in interstate commerce.

Second, Respondent argues that the ALJ erred in finding that Complaint Counsel had shown concerted action when there was no evidence of direct collusion among NTSP's physicians. Respondent asserts that NTSP cannot and does not bind any participating physicians to its non-risk contracts, and that any non-risk contracts to which NTSP decides to become a party must be messengered to the physicians for their individual decisions on whether to join.

Third, Respondent contends that even if Complaint Counsel had shown there was concerted action, the conduct must be analyzed under the rule of reason. Respondent argues that the ALJ therefore erred when he found a violation, because Complaint Counsel did not meet their burden to show anticompetitive effects in a properly defined relevant market.

Fourth, Respondent argues that the ALJ erred when he found that NTSP had insufficient evidence of procompetitive justifications. Respondent asserts that all the evidence available

Commission Opinion

shows that NTSP had legal and business justifications for its actions. Respondent argues that the ALJ compounded this error when he denied NTSP discovery needed to further establish its procompetitive justifications.

Fifth, Respondent argues that it was error for the ALJ to find that NTSP's conduct had a net anticompetitive effect in the absence of any showing by Complaint Counsel that there was a less restrictive alternative or that NTSP's justifications for its conduct were pretextual.

Sixth, Respondent argues that it was error for the ALJ to enter an order that was not narrowly tailored to any antitrust violation properly found.

## 2. Complaint Counsel's Appeal

Complaint Counsel appeal two aspects of the ALJ's decision, but otherwise ask that the Commission affirm the finding of liability. First, Complaint Counsel argue that it was error for the ALJ to hold it was necessary to prove a relevant market in the case of a *per se* unlawful price-fixing agreement. Complaint Counsel argue that no proof of market definition or market power is required to establish a *per se* violation, and that any naked price agreement among competitors (actual or potential) is conclusively presumed unlawful.

Second, Complaint Counsel argue that the ALJ's order is too narrow and fails to provide essential relief. Complaint Counsel argue that the core prohibitions fail to provide adequate protection against further violation. Complaint Counsel also argue that the ALJ added two unwarranted provisos that are likely to enable NTSP to continue certain conduct that the ALJ found was used to accomplish the unlawful price-fixing scheme.

Commission Opinion

### III. Jurisdictional Issues

We consider this issue first, although Respondent does not give it prominence. The Commission has jurisdiction over NTSP as a corporation only if NTSP is organized to carry on business for the pecuniary benefit of its members and NTSP's conduct at issue is "in or affecting commerce." 15 U.S.C. §§ 44, 45 (1994). Respondent contends that it was error for the ALJ to find that the FTC has jurisdiction over NTSP because NTSP is incorporated under Texas law as a "memberless" non-profit organization (and therefore its physicians are not "members" of NTSP), and none of NTSP's actions were in interstate commerce. RAB at 58-59.

We find that NTSP clearly is a "corporation" within the meaning of Section 4 of the FTC Act because NTSP is "organized to carry on business for its own profit or that of its members." 15 U.S.C. § 44. In the words of NTSP official Dr. John Johnson, "NTSP was going to be a group of physicians that would bring a voice to organizing physicians who often practiced in individual groups to hopefully be able to secure contracts, improve patient care, and provide a voice at the table for physicians. . . . [It was] to represent physicians . . . in obtaining contracts from businesses or insurance companies or in dealing with hospitals." CX 1182 (Johnson Dep. at 10-11).<sup>7</sup> NTSP's primary function – marketing its physicians to payors – satisfies the pecuniary benefit test of FTC jurisdiction. Indeed, we find that NTSP does not appear to have any purpose other than to carry on business for the profit of its members. It is not necessary for the challenged conduct to increase NTSP's members' profits, as NTSP intimates. In *California Dental*, 526 U.S. at 767 n.6, the Supreme Court stated,

---

<sup>7</sup> See also CX 350 ("NTSP was started in an attempt to provide a seat at the table of medical business for the individual specialty physicians . . . . NTSP through, [sic] PPO and risk contracts, has provided a consistent premium fee-for-service reimbursement to the members when compared with any other contracting source."); CX 550.

Commission Opinion

“[i]t should go without saying that the FTC Act does not require for Commission jurisdiction that members of an entity turn a profit on their membership, but only that the entity be organized to carry on business for members’ profit.”

NTSP’s argument that its physicians are not “members” because of the way it is incorporated elevates form over substance.<sup>8</sup> NTSP’s physicians possess sufficient indicia of membership to qualify as members within the meaning of Section 4:

- They come together with other members of their profession to promote their common business interests.
- They elect representatives to its governing board.
- They contribute funds to finance NTSP’s activities.
- NTSP internal documents refer to its physicians as “members.”

IDF 20, 21, 24, 33, 42, 44, 48, 160, 282, 326.

We further find that NTSP satisfies the interstate commerce jurisdictional requirement because NTSP’s actions to maintain physician fee levels, if successful, could be expected to affect the flow of interstate payments from out-of-state payors to NTSP physicians. There is no need to prove actual effects on interstate commerce, or to quantify the effect. The Supreme Court on numerous occasions has emphasized the breadth of federal antitrust jurisdiction, even when wholly intrastate conduct of local actors is challenged.<sup>9</sup>

---

<sup>8</sup> The mere form of incorporation is not controlling in matters of FTC jurisdiction. *See Cmty. Blood Bank of the Kansas City Area, Inc. v. FTC*, 405 F.2d 1011, 1018-19 (8th Cir. 1969).

<sup>9</sup> *See, e.g., Summit Health, Ltd. v. Pinhas*, 500 U.S. 322, 328-31 (1991); *McLain v. Real Estate Bd. of New Orleans, Inc.*, 444 U.S. 232, 241 (1980); *Hosp. Bldg. Co. v. Trs. of Rex Hosp.*, 425

Commission Opinion

#### IV. Legal Framework

In order to find liability under Section 5 of the FTC Act, we will examine first, whether there was an “agreement” between independent actors and, second, whether this agreement unreasonably restrained trade.<sup>10</sup> Our overall evaluation of NTSP’s conduct is guided by a rich jurisprudence that extends over almost 100 years,<sup>11</sup> and particularly by the very recent decision of the Supreme Court in *California Dental* – a case that was in turn followed by the Commission in its own opinion in the *Polygram* case and by the D.C. Circuit Court’s affirming opinion, *Polygram Holding*, 416 F.3d 29. We will occasionally refer to the Department of Justice and FTC *Health Care Statements*, but it should be understood that we do not consider the *Health Care Statements* as substantive authority in their own right but rather as concise summaries of what we believe the law to be. We are also informed by our own enforcement experience with combinations similar to NTSP and by the Commission’s *Health Care Hearings and Report*. In this section we will explain why we have chosen to apply the flexible tools of *Polygram* rather than a simple *per se* analysis in this case, and we will then describe *Polygram*’s methodology in more detail.

---

U.S. 738, 743-45 (1976); *Goldfarb v. Virginia State Bar*, 421 U.S. 773, 784-85 (1975).

<sup>10</sup> For purposes of this case, we can assume that the definition of “unfair methods of competition” under the FTC Act, 15 U.S.C. § 45, is the same as the definition of a “contract combination . . . or conspiracy, in restraint of trade . . . .” under Section 1 of the Sherman Act, 15 U.S.C. § 1.

<sup>11</sup> The requirement that the restraint be unreasonable – coupled with recognition that some restraints can conclusively be presumed so – dates from 1911 in *Standard Oil Co. v. United States*, 221 U.S. 1, 58 (1911).

Commission Opinion

A. Choice of Standard

The Commission's unanimous *Polygram* opinion was its first attempt to respond to the approach of the Supreme Court's *California Dental* decision. These opinions describe how the analysis of horizontal restraints has evolved over the last 100 years, and establish a flexible methodology for courts to determine whether a challenged restraint is illegal. They go beyond the simple dichotomy between categories like "*per se*" or "rule of reason," and establish a continuum within which behavior can be analyzed.

At one polar extreme, there still is a category of offenses that are considered *per se* illegal, for which liability depends solely on whether defendants did or did not do certain things. These offenses include, most prominently, so-called "naked" price fixing or market allocation agreements. Longstanding precedent holds that the courts will not entertain any arguments that these restraints will yield beneficial, or even benign, results. Parties cannot defend, for example, on the ground that prices have been set at "reasonable" levels<sup>12</sup> or that coordination is necessary for survival in times of distress.<sup>13</sup> We do not believe that the *per se* condemnation of naked restraints has been affected by anything said either in *California Dental* or *Polygram*.

There is precedent for outright *per se* condemnation of conduct that parallels the conduct in issue here. The Supreme Court held in *Maricopa*, 457 U.S. at 356-57, that traditional antitrust laws apply to price fixing in the context of physician fee negotiation, and held that it was *per se* unlawful horizontal price fixing for a

---

<sup>12</sup> See *United States v. Trenton Potteries Co.*, 273 U.S. 392, 398-99 (1927); *United States v. Addyston Pipe Steel Co.*, 85 F. 271, 288-91 (6th Cir. 1898), *aff'd* 175 U.S. 211 (1899).

<sup>13</sup> See *United States v. Socony-Vacuum Oil Co.*, 310 U.S. 150, 218-21, 229 (1940).

## Commission Opinion

group of competing physicians to agree to set a maximum fee to offer health insurers for providing medical services to patients. The means used to implement a price fixing agreement in *Maricopa* are similar to those used by NTSP. In *Maricopa*, the medical societies: (a) set a maximum price for health services that could be charged to policyholders of approved health insurance plans;<sup>14</sup> (b) used polling as a device for determining the price; (c) did not necessarily have agreement directly between physicians in the price-setting process; and (d) allowed the physicians the freedom to set their own prices.<sup>15</sup>

We also are familiar with these practices and this industry.<sup>16</sup> The Commission has issued complaints in numerous cases, which challenge conduct by physician IPAs similar to that in *Maricopa* and that in the case at hand. *See, e.g., supra* note 1. The FTC and

---

<sup>14</sup> Note that in one respect the conduct here is even worse than that condemned in *Maricopa* because NTSP has set minimum prices. *See* Section V.B.1.a.

<sup>15</sup> *Arizona v. Maricopa County Med. Soc’y*, 1979 WL 1638 at \*1 (D. Az. June 5, 1979), *aff’d*, 643 F.2d 553 (9th Cir. 1980), *rev’d on other grounds*, 457 U.S. 332 (1982).

<sup>16</sup> A *per se* characterization would not necessarily be foreclosed, even if we did not have this industry-specific experience. *Maricopa* stated that the *per se* rule does not need to “be rejustified for every industry that has not been subject to significant antitrust litigation.” 457 U.S. at 350-51. On the other hand, *Broadcast Music, Inc. v. Columbia Broadcasting System, Inc.*, 441 U.S. 1, 9 (1979), emphasized that a *per se* label is appropriate only when courts “have had considerable experience with certain business relationships.” We do not need to parse these statements closely, in light of our experience with both the industry and the practices.



Commission Opinion

Department of Justice *Health Care Statements* provide specific warning about the illegality of this type of conduct. *See Health Care Statements, supra* note 2, *Statement 8*.

Although NTSP's activities could be characterized as *per se* illegal because they are closely analogous to conduct condemned *per se* in this and other industries, we will not apply that label here and now in this particular case. There are two reasons.

First, in the years since *Maricopa* was decided, the Supreme Court has urged caution in the application of the *per se* label to conduct in a professional setting where "the economic impact . . . is not immediately obvious." *FTC v. Indiana Federation of Dentists*, 476 U.S. 447, 459 (1986); *see also California Dental*, 526 U.S. at 770-71. Some might claim that the likely economic impact of the restraints in issue here is "immediately obvious" enough to satisfy this standard, but we do not need to reach that question because we have available in this case an extensive record on which to buttress our conclusions about the likely effects of Respondent's conduct.

Second, since *Maricopa*, we have a better understanding of the potential integration efficiencies of physician IPAs. We would view NTSP's activities very differently if NTSP were able to demonstrate that the participating physicians were financially or clinically integrated in performing its numerous non-risk contracts, and thus driven by incentives similar to those present in its single remaining risk contract. Under the well-established law of ancillary restraints, recent precedents like *Polygram*, and the principles described in our *Health Care Statements* and *Competitor Collaboration Guidelines*,<sup>17</sup> Respondent could have prevailed if the integrated venture were likely to enhance

---

<sup>17</sup> Fed. Trade Comm'n and U.S. Dep't of Justice, *Antitrust Guidelines for Collaborations Among Competitors* (2000), reprinted in 4 Trade Reg. Rep. (CCH) ¶ 13,161 [hereinafter *Competitor Collaboration Guidelines*].

## Commission Opinion

efficiencies and NTSP's conduct were reasonably related to the overall agreement and reasonably necessary for achieving those efficiencies. See discussion in Section V.C.1., *infra*. This means that some initial inquiries about whether there is integration, the likely effects of integration, and the reasonableness of the specific restraint are necessary in order to decide whether to apply a rule of reason. It is of course possible to conclude we then have a *per se* case based on a *per se* illegal restraint if these initial inquiries are decided adversely to a respondent. But, it is semantically awkward to use a *per se* label once a number of "reasonableness" issues have been addressed, sometimes at length. What does it really mean to say we have a *per se* case, once we have considered and rejected justifications for a restraint? What it means, as a practical matter, is that no further proof of market effects is required; the case is over. As will be made clear in the discussion below, however, we arrive at exactly the same result when we follow the "inherently suspect" analysis outlined in *Polygram* – and the *Polygram* framework more accurately describes the actual analysis of the case.

These considerations might not deter us when we are persuaded by experience and economic logic that the potential for harm is overwhelming and the possible justifications are attenuated and uniformly rejected by courts. We would simply apply the *per se* label. In the health care sector, however, the Commission wants to encourage providers to engage in efficiency-enhancing collaborative activity.<sup>18</sup> We do not want to chill consideration of this activity by use of terminology that could

---

<sup>18</sup> See generally *MedSouth*, *supra* note 2, where Commission staff did not recommend the Commission take enforcement action against a physician IPA proposal whereby the IPA physicians would collaborate on information sharing, treatment coordination, practice protocols, and enforcement standards. See also Thomas B. Leary, *The Antitrust Implications of "Clinical Integration": An Analysis of FTC Staff's Advisory Opinion to MedSouth*, 47 ST. LOUIS U. L. J. 223 (Spring 2003).

Commission Opinion

be misunderstood. This is not a factor that was considered in *Maricopa* over twenty years ago, but we do think it is a factor that needs to be considered after a decision like *California Dental*.

So, at least this time, after the first full administrative trial in a generation, we will instead follow the methodology of *Polygram*, and consider each of Respondent's justifications in some detail. We want to emphasize again, however, that this is not the same thing as a full blown rule of reason inquiry. If we find that Respondent's proffered justifications for NTSP's inherently suspect conduct are not legitimate – after the examination that follows – it is not necessary to go on and find actual adverse market effects. See Section V.E. *infra*.

B. The *Polygram* Analysis

In the words of the D.C. Circuit, an offense can be described as “inherently suspect” when there is a “close family resemblance between the suspect practice and another practice that already stands convicted in the court of consumer welfare.” *Polygram*, 416 F.3d at 37. The determination is based on the conduct's “likely tendency to suppress competition.” *Polygram Comm'n Op. supra* note 4, at 29. As the Commission described, “[s]uch conduct ordinarily encompasses behavior that past judicial experience and current economic learning have shown to warrant summary condemnation.” *Id.* At this stage, the focus of the inquiry is on the nature on the restraint rather than on the market effects in a particular case.<sup>19</sup> If a plaintiff is able to make an initial

---

<sup>19</sup> As the D.C. Circuit pointed out in *Polygram*, this is not a fixed category. It must evolve “as economic learning and market experience evolve.” 416 F.3d at 37; see also Thomas B. Leary, *A Structured Outline for the Analysis of Horizontal Agreements*, <http://www.ftc.gov/speeches/leary/chairsshowcase.talk.pdf> at 7-10, (describing distinction between cases “that focus on the nature of the restraint” and those “that focus on the nature of the market”) (emphasis in original).

## Commission Opinion

showing that particular conduct meets these strictures, and the defendant makes no effort to advance any procompetitive justification for the conduct, then the case is concluded and the practices are condemned. *Polygram Comm'n Op. supra* note 4, at 29.

A defendant can avoid summary condemnation, however, if it can advance a legitimate justification for the practice. As we explained in *Polygram*, “[s]uch justifications may consist of plausible reasons why practices that are competitively suspect as a general matter may not be expected to have adverse consequences in the context of the particular market in question; or they may consist of reasons why the practices are likely to have beneficial effects for consumers.” *Id.* The defendant need only articulate a legitimate justification, and is not obliged to prove the competitive benefits. (Remember that the issue at this initial stage is simply whether the practice should be condemned summarily.) The proffered justifications, however, must be both cognizable under the antitrust laws and at least facially plausible. *Id.* at 30-33. The cognizable justification requirement allows a tribunal to reject as a matter of law proffered justifications that are incompatible with the goal of antitrust law to protect competition. We described cognizable justifications in our *Polygram* opinion, *id.* at 31:

Cognizable justifications ordinarily explain how specific restrictions enable the defendants to increase output or improve product quality, service, or innovation. By contrast, courts since the earliest decades of the Sherman Act have identified classes of justifications that, because they contradict the procompetition aims of the antitrust laws will not save restraints from condemnation. For example, a defendant cannot defend restraints of trade on the ground that the prices the conspirators set were reasonable, that competition itself is unreasonable or leads to socially undesirable results, or that price increases resulting from a trade restraint would attract new entry.

Commission Opinion

The D.C. Circuit expressly approved the requirement that a proposed justification be both cognizable and plausible. Even though the justification offered by *Polygram* seemed plausible “[a]t first glance,” the court rejected it as “nothing less than a frontal assault on the basic policy of the Sherman Act.” *Polygram*, 416 U.S. at 37-38 (quoting *Nat’l Soc’y of Prof’l Eng’rs*, 435 U.S. 679, 695 (1978)).

If the justification for a suspect restraint is cognizable – which is to say, admissible in the first place – a defendant must also show that it would plausibly create or improve competition. Again, to quote *Polygram*:

A justification is plausible if it cannot be rejected without extensive factual inquiry. The defendant, however, must do more than merely assert that its purported justification benefits consumers. Although the defendant need not produce detailed evidence at this stage, it must articulate the specific link between the challenged restraint and the purported justification to merit a more searching inquiry into whether the restraint may advance procompetitive goals, even though it facially appears of the type likely to suppress competition.

*Id.* at 31-32.<sup>20</sup>

---

<sup>20</sup> The concept of ancillary restraints, which allows an agreement that would otherwise be viewed as a naked restraint of trade to be evaluated in light of the procompetitive effects of an efficiency-enhancing integration of economic activity to which it is reasonably related, is subsumed in the Commission’s *Polygram* analysis. See *Polygram Comm’n Op.*, *supra* note 4, at n.42 (“[t]he ancillary restraints doctrine retains its vitality in evaluating efficiency claims. . . . [w]hether or not expressed in terms of ancillarity, the link between defendant’s “plausible” justification and a cognizable benefit must be clear.”). As will become clear after the discussion of specific facts, NTSP’s conduct is not justified under either a pre-*Polygram* ancillarity analysis, or

## Commission Opinion

If a defendant is able to advance a justification that meets both of these requirements – cognizable and plausible – the plaintiff must then make a more detailed showing that the restraints at issue are likely to harm competition. *Id.* at 32. The degree of proof required depends on the circumstances of the case and the degree to which antitrust tribunals have experience with the restraint in question. *Id.* The Supreme Court stated succinctly that the inquiry must be “meet for the case.” *California Dental*, 526 U.S. at 781. In *Polygram*, the Circuit Court used similar language, stating that, “the extent of the inquiry is tailored to the suspect conduct in each particular case,” 416 F.3d at 34. We interpret this precedent as endorsement of a “spectrum” or “sliding scale” analysis, which more accurately describes the way cases are actually decided today.<sup>21</sup>

C. The Health Care Statements

The FTC and Department of Justice *Health Care Statements* provide guidance about the agencies’ enforcement intentions on issues which are likely to arise in the health care industry. They lay out principles that we believed to be consistent with the state of the law when they were issued in 1993 and revised in 1994 and 1996. Even though the *Health Care Statements* were issued before the *California Dental* or *Polygram* opinions were written, and also before the *Competitor Collaboration Guidelines* were issued, we believe that their analysis of horizontal restraints among competing physicians is still viable and also uniquely valuable because of their specificity. The *Health Care Statements*

---

*Polygram*’s more inclusive analysis.

<sup>21</sup> We believe that this analytical framework may also help to resolve the apparent inconsistency between those decisions that use *per se* terminology and those that use rule of reason terminology in facially similar situations. See cases cited in ABA SECTION OF ANTITRUST LAW, ANTITRUST LAW DEVELOPMENTS, 53-58 (5th ed. 2002).

Commission Opinion

lay out the circumstances when a rule of reason analysis is appropriate for price-setting conduct between competing physicians and – like the analysis in *Polygram* – they allow for procompetitive justifications in certain circumstances. See *Health Care Statements*, *supra* note 2, *Statement 8*.

Price-setting conduct of physician networks qualifies for rule of reason treatment where the “physician’s integration through a network is likely to produce significant efficiencies” and the agreement on price is “reasonably necessary to realize those efficiencies.” *Health Care Statements*, *supra* note 2, *Statement 8B1*.<sup>22</sup> *The Health Care Statements* describe two different types of integration that can qualify a physician network for rule of reason treatment – financial and clinical. *Id.* The Commission has applied this analysis in numerous enforcement actions.

Although our analysis of NTSP’s conduct generally follows the legal framework outlined in *Polygram*, we also refer to the industry specific concepts identified in the *Health Care Statements* to the extent appropriate.

## V. Analysis of the Challenged Restraints

### A. Existence of an Agreement

In order to decide whether there is a violation of Section 5 of the FTC Act in this case, we will first look to see if there is an agreement. There is a fundamental distinction between unilateral and multilateral action. The matter is easy to decide when two or more separate legal entities overtly agree on a restraint that each will adopt. However, an action nominally taken by a single entity is also construed as the product of agreement for purposes of the antitrust laws when the entity is controlled by a group of competitors and is serving as the agent of the group. There are

---

<sup>22</sup> *The Competitor Collaboration Guidelines*, *supra* note 17, refer to “cognizable efficiencies” for which the restraint in issue is “reasonably necessary.” §§ 3.36(a), 3.36(b).

## Commission Opinion

many ways that association/agents can legally act for the collective benefit of the group. Associations can, for example, negotiate prices for office facilities or wages for employees; agents can establish prices for services that the association itself provides for members or non-members. These are matters of no antitrust significance, because there is no conceivable anticompetitive impact. However, if the association negotiates prices for services that the *members* will provide, the organization's conduct is considered to be that of a combination or conspiracy of its members, not unilateral action.<sup>23</sup>

The Commission has also held that when an organization is controlled by a group of competitors, the organization is viewed as a combination of its members, and their concerted actions will violate the antitrust laws if an unreasonable restraint of trade. *In the Matter of Michigan State Med. Soc'y*, 101 F.T.C. 191, 286 (1983). The Commission's long list of consent agreements in this industry are all based on this uncontroversial legal premise. *See, e.g., supra* note 1.

The basis for this jurisprudence is sound. Without it, any group of competitors could avoid antitrust liability for collective price fixing simply by acting through single organizations that they control (as many have attempted).<sup>24</sup> Thus, in order to

---

<sup>23</sup> *See, e.g., Nat'l Soc'y of Prof'l Eng'rs*, 435 U.S. at 694-96; *United States v. Sealy, Inc.*, 388 U.S. 350, 352-54 (1967). *Cf. Allied Tube & Conduit Corp. v. Indian Head, Inc.*, 486 U.S. 492, 509 (1988); *Nat'l Collegiate Athletic Ass'n v. Bd. of Regents of the Univ. of Oklahoma*, 468 U.S. 85, 99 n.18 (1984).

<sup>24</sup> *See supra* note 23. They could, for example, coordinate their activities through a single "trust." It would seem rather odd to immunize this kind of activity, given the popular name of the basic legal regime we apply here: "The Antitrust Laws."



Commission Opinion

determine if there is an agreement in this case, we must first determine whether NTSP is controlled by competing physicians.

Respondent states that NTSP is a 5.01(a) memberless non-profit corporation under Texas law.<sup>25</sup> RAB at 14. Respondent argues that because of this “memberless” status, NTSP should be viewed as a sole actor, both in management of its affairs, and in its refusal to deal with payors on non-risk contracts, and that therefore NTSP cannot be found to conspire under Federal competition law. *Id.* at 14-15. At the outset, we reject this argument. Substance prevails over form in antitrust law, and the technical manner in which an organization is incorporated does not control.<sup>26</sup> We have to look beneath the surface.

We find that NTSP is controlled by competing physicians, and therefore is not a sole actor for purposes of the antitrust laws. We agree with the ALJ’s conclusion that NTSP’s participating physicians have taken collective action to obtain higher fees from payors. ID at 53-55. The fact that NTSP physicians elect representatives from their ranks to serve on the eight-member Board of Directors of NTSP and set NTSP policy supports this conclusion. IDF 23, 24, 33, 38.

Respondent’s briefs rely heavily on *Viazis v. American Ass’n of Orthodontists*, 314 F.3d 758 (5th Cir. 2002), to assert that NTSP’s mere existence does not satisfy the concerted action requirement

---

<sup>25</sup> Section 5.01(a) of the Texas Medical Practice Act allows non-profit entities to engage in the practice of medicine for the purposes of research, medical education, or the delivery of health care to the public. TEX. OCC. CODE ANN. § 162.001 (Vernon 2004).

<sup>26</sup> In *Community Blood Bank*, 405 F.2d at 1018-19, the circuit court determined that jurisdiction was to be determined “on an ad hoc basis” and that the mere form of incorporation was not controlling.

## Commission Opinion

of Sherman Act Section 1. RAB at 12. Respondent's discussion of *Viazis* has confused the requirement of "collective action" with the separate requirement of an "unreasonable restraint of trade." *Viazis* merely states that a trade association is not by its nature a "walking conspiracy" even though it inherently involves collective action by competitors – there must also be an unreasonable restraint of trade. *Viazis*, 314 F.3d at 764. We do not disagree.

Respondent also argues that because NTSP cannot and does not bind any of its physicians to non-risk contracts, there cannot be any collusion among physicians (and therefore no agreement). RAB at 8. Respondent cites ALJ findings that the doctors did not discuss among themselves or directly enter into price agreements with one another, and points out that the ALJ's finding that there was no collusion among NTSP's physicians was based on this evidence. RAB at 11. This argument, as presented, conflates what really are two separate issues.

The first issue raised by this particular argument is whether parties can enter into an agreement absent direct communication with each other. It has long been settled that they can. In *Maricopa*, the Supreme Court found an agreement among physicians without finding that the competing physicians agreed directly with each other. 457 U.S. at 356; *see also* ID at 68. Similarly, in *Virginia Academy of Clinical Psychologists v. Blue Shield of Virginia* 624 F.2d 476, 479-81 (4th Cir. 1980), the court found collective action by a group that was controlled by its physician members without finding that the plan's individual physicians had met and agreed directly with each other. The *Health Care Statements* also explain that physicians do not have to directly agree with one another to engage in price fixing, and that a common agent can be used to exert the bargaining leverage of a group of physicians. *Health Care Statements*, *supra* note 2, *Statement* 9D1 and 9D4 n.66. In this case, it is enough that participating physicians individually authorized NTSP to take certain actions on their behalf, knowing that others were doing the

Commission Opinion

same thing.<sup>27</sup> Indirect communications of this kind are sometimes referred to as “hub-and-spoke” conspiracies.<sup>28</sup>

The second issue is whether it is possible to find that there was an agreement on price even though individual physicians were not bound to adhere to contract terms negotiated by NTSP. We address this issue in the discussion of NTSP’s restraints in Section V.B.1. immediately below (analysis of whether NTSP’s conduct amounts to price fixing). It is enough to say here that the opt-out right does not negate the existence of an agreement.

B. Restraint of Trade – *Prima Facie* Case

We next examine whether NTSP’s conduct amounts to a restraint of trade, specifically, price fixing. First we look at the factual evidence to determine whether the conduct amounts to price fixing, and is thus illegal absent a cognizable and plausible justification. We discuss different kinds of activity separately for convenience and to provide guidance about what we regard as highly suspect behavior. We want to make clear, however, that

---

<sup>27</sup> For example, NTSP would inform physicians who had not yet granted it contract negotiation authority but were considering it, the number of other member physicians who had already given NTSP that authority. CX 1066 at 1; CX 0548 at 1.

<sup>28</sup> See, e.g., *Toys “R” Us, Inc. v. FTC*, 221 F.3d 928, 934-36 (7th Cir. 2000) (finding evidence of horizontal agreement where petitioner served as “ringmaster”); *United States v. Masonite Corp.*, 316 U.S. 265, 276 (1972) (fixing of prices by one member of group pursuant to express delegation, acquiescence, or understanding just as illegal as fixing of prices by direct, joint action); *Interstate Circuit, Inc. v. United States*, 306 U.S. 208, 227 (1939) (“unlawful conspiracy may be and often is formed without simultaneous action or agreement”).

## Commission Opinion

our ultimate conclusions in this case do not stand or fall on our assessment of separate actions; the ultimate conclusions are rather predicated on the likely effects of the actions taken together.<sup>29</sup>

After discussion of the restraints separately, we then address in Section V.C. below the justifications advanced for each of them. We also describe the conduct that the Commission does not find to be price fixing in Section V.D., in order to give guidance to the health care community.

1. Challenged Restraints

a. NTSP's Use of a Poll

NTSP conducts annual polls of its physicians to determine minimum reimbursement rates for use in negotiation of HMO and PPO product contracts with payors. CX 1195 (Van Wagner Dep. at 66-67). NTSP's polling form asks the physicians individually for the minimum price that they would accept for the provision of medical services pursuant to a fee-for-service HMO or PPO agreement. CX 0565; CX 1196 (Van Wagner IH at 26-29, 43-44, 62). NTSP uses these poll responses to calculate the mean, median, and mode of the minimum acceptable fees identified by its physicians, and then uses these averages to establish its minimum contract prices. NTSP then reports these measures back to its participating physicians. CX 0103 at 4-5; CX 1196 (Van Wagner IH at 26-29, 43-44, 62); CX 1042. NTSP's polling form explains to the participating physicians that "NTSP polls its affiliates and membership to establish Contracted Minimums. NTSP then utilizes these minimums when negotiating managed care contracts on behalf of its participants." CX 0387 at 1; CX 0633.

---

<sup>29</sup> The decision to view the conduct as a whole in this case should not be understood to mean that any one of the actions is necessarily benign standing alone.

## Commission Opinion

We find that NTSP's use of a poll facilitated a price-fixing agreement among its competing physician members. Frech Tr. 1316-24; 1326. NTSP physicians were aware that NTSP would use individual member's poll responses to create group "averages" that would be used by their organization in the coming year's negotiations with payors. IDF 88-90, 93-94. It was a way to communicate to their competitors what they would like to get in the future – not what they had gotten in the past, or, indeed, what they might settle for individually. When they cast a vote on the desired minimum price for the group, they were not simply reporting past or current prices, they were telegraphing their intentions about future prices. Thus, NTSP physicians anticipated that any individual response would help to raise or lower the average fee for the group – an average that NTSP would then use in negotiating with payors. *See* IDF 88, 96-100. NTSP physician responses to the polls were *interdependent* and not independent.

Respondent argues that NTSP's use of its poll and its minimum reimbursement schedule are not concerted action and have legitimate business purposes.<sup>30</sup> RAB at 21-22. Respondent states that NTSP does not divulge to any physician or board member whether or how any other individual physician responds to the confidential poll conducted by NTSP's staff. *Id.* at 23-24. Respondent also claims that NTSP does not use the averages derived from the polls to negotiate for higher rates, and NTSP's actions related the establishment and use of the threshold rate are purely internal to NTSP. *Id.* at 21-22. Even if NTSP's becomes a party to the contract, Respondent states that each physician still has an individual right to decide whether to become a party; physicians are not bound to their poll responses, and the poll does not require or induce a physician to contract in a particular manner or even at all. *Id.* at 22. Respondent points out that less than 34 percent of the physicians responded to the poll. *Id.* at 23. Furthermore, Respondent states that when NTSP's board makes a

---

<sup>30</sup> We address Respondent's efficiency arguments associated with NTSP's poll in Section V.C. below.

## Commission Opinion

decision on a payor's offer, it is not binding on the physicians. *Id.* at 22-23.

Respondent further argues that Complaint Counsel's expert (Dr. Frech) was unable to find any evidence of collusion among physicians, and admitted that physicians chose not to contract through NTSP on more than two-thirds of the contract offers NTSP messengered. RAB at 8-10. According to Respondent, Dr. Frech also determined that physicians frequently enter individually into payor contracts at rates both above and below the threshold rate levels. RAB at 10-11, 23.

Respondent's argument that NTSP does not divulge to any physician or board member whether or how any particular physician responds to the poll is of no consequence because liability in this case is not predicated on individual discussions among physicians themselves. It is predicated on an improper delegation of individual pricing authority to a common agent. The fact that NTSP's decisions on payor offers were not binding, and often ignored, does not absolve NTSP from liability because the law is clear that agreements can be illegal even though all the price terms are not specified or adhered to. *Catalano, Inc. v. Target Sales, Inc.*, 446 U.S. 643, 647-48 (1980); *Socony-Vacuum Oil*, 310 U.S. at 218-24; and *Plymouth Dealers' Ass'n of Northern California v. United States*, 279 F.2d 128, 130-33 (9th Cir. 1960), all stand for the proposition that price fixing encompasses a broad range of actions that affect, but do not necessarily determine, the final price. *Socony-Vacuum Oil*, 310 U.S. at 223, made clear that "a combination formed for the purpose and with the effect of raising, depressing, fixing, pegging, or stabilizing the price of a commodity" is price fixing. In *High Fructose Corn Syrup Antitrust Litigation*, 295 F.3d 651, 656 (7th Cir. 2002), Judge Posner stated that "[a]n agreement to fix list prices is . . . a per se violation of the Sherman Act, even if most or for that matter all transactions occur at lower prices." Judge Posner explained that "the list price is usually the starting point for the bargaining and the higher it is (within reason) the higher the ultimately bargained price is likely to be." *Id.* Even if there is variability, NTSP's use

Commission Opinion

of a minimum schedule (obtained from polling results) affects the level at which variability occurs. NTSP's conduct thus has the same effect on price as the conduct identified in *Plymouth Dealers* and *High Fructose Corn Syrup*.

Complaint Counsel's expert, Professor Frech, explained that NTSP's minimum-fee schedule coupled with its right of first negotiation (via the PPA) hinders payors' ability to contract directly with physicians. Frech Tr. at 1315-17; 1326-27. This was confirmed by payor testimony. *See, e.g.*, Quirk Tr. at 316-17. Professor Frech also explained that the NTSP minimum reimbursement rates were higher than what some physicians were actually willing to accept, and that negotiation of a minimum price offer has the effect of raising the prices that "low end" physicians would otherwise earn, without reducing the price that "high end" physicians would receive (they can opt out). Frech Tr. 1321-24. Thus, the minimum NTSP price schedule does have a tendency to increase prices overall, and can be characterized as horizontal price fixing.<sup>31</sup>

The fact that only 34 percent of NTSP physicians responded to the polls does not alter this conclusion. A low response rate could, of course, further reduce the utility of the poll as a prediction of what individual physicians would be willing to accept – and this fact therefore actually *weakens* any argument that a poll would help payors to avoid wasted efforts. *See* discussion in Section V.C.2.b. Moreover, the fact that the poll results – whether actual predictors or not – were disclosed to *all* NTSP physicians encouraged them to reject price offers below the minimum fees indicated, Frech Tr. 1326-27, and NTSP actively

---

<sup>31</sup> *See Nat'l Elec. Contractors Ass'n, Inc. v. Nat'l Constructors Ass'n*, 678 F.2d 492, 500 (4th Cir. 1982) (*citing Yarn Processing Patent Validity Litig.*, 541 F.2d 1127, 1137 (5th Cir. 1977), *cert. denied*, 435 U.S. 910 (1977) (interference with the market forces freely setting prices sufficient to constitute price fixing)).

## Commission Opinion

encouraged them to reject the offers. *See* CX 1097 at 2; Vance Tr. 1215-18; Frech Tr. 1326-27. Finally, this disclosure of the poll results could also cause NTSP physicians to inflate their poll responses in subsequent years. *See* CX 430 (2002 annual policy form reminded physicians of prior year's averages); IDF 99-100. Thus, the poll results influenced the decisions of all NTSP physicians, regardless of whether they responded.

The manner in which NTSP utilized the minimum reimbursement schedule in its communications with payors also shows that it was using the poll for much more than just an administrative or efficiency-enhancing tool. For example, NTSP regularly informed payors that its physicians had established minimum fees for NTSP-payor agreements, identified the fee minimums, and stated that NTSP would not enter into or forward to any of its physicians payor offers that were below the minimums. CX 1196 (Van Wagner IH at 62-63, 153-54); CX 1173 (Deas IH at 26-29). This evidence is in stark contrast to the picture painted by Respondent about NTSP's activities associated with the poll, and illustrates the need for a multi-faceted definition of price fixing called for in *Socony-Vacuum Oil*.

b. NTSP's Physician Participation Agreement

NTSP's physicians enter into a membership agreement (the PPA) with NTSP that grants NTSP the right to receive all payor offers and imposes on the physicians a duty to promptly forward payor offers to NTSP. CX 0276; CX 275 at 24. Essentially the PPA grants NTSP a right of first negotiation with payors. The physicians agree that they will refrain from pursuing offers from a payor until notified by NTSP that it is permanently discontinuing negotiations with the payor. CX 0276; CX 0311 at 10; CX 1178 (Hollander Dep. at 68). Under the PPA, NTSP is supposed to deliver payor price proposals (and other economic provisions of offers) for fee-for-service contracts to its physicians. CX 0275 at 25-26.



Commission Opinion

We find that the PPA in effect renders NTSP as the sole bargaining agent of NTSP competing physicians and thus facilitates price fixing among NTSP physicians. The terms of the PPA and the manner in which NTSP has utilized them hinder the ability of payors to assemble a marketable physician network in the Fort Worth area without submitting to the collective bargaining of NTSP. Frech Tr. 1313-16.

Respondent argues that NTSP's PPA gives NTSP no authority to bind physicians, and that any non-risk contracts in which NTSP decides to join as a party must be messengered to the physicians for their own individual decisions on whether to join. RAB at 8, 19. In addition, Respondent argues that the PPA's terms do not prevent a physician from negotiating with a payor directly or through another entity. *Id.* at 19.

We find that although the PPA requires NTSP to deliver contracts to its physicians, the evidence shows that NTSP rejects and does not deliver any contract that falls below its minimum reimbursement schedule. CX 1196 (Van Wagner IH at 68-69). Other terms of the PPA are inconsistent with Respondent's assertion that any non-risk contracts must be messengered. For example, the PPA contains provisions whereby 50 percent of NTSP's membership must approve the reimbursement proposal of a payor before an offer is "messengered" by NTSP to the physicians for actual opt-in/out of the proposed contracts.<sup>32</sup> CX 0276 at 1-2. This conduct has the potential to raise the level at which variability occurs, just as the use of polling data does.

We also find that each NTSP physician's ability to opt in or out of a contract – NTSP's inability to "bind" its members to a contract – does not eliminate the existence of a price-fixing agreement when providers collectively negotiate with payors over

---

<sup>32</sup> The PPA contains another provision allowing for NTSP counter offers to payor rate proposals based on direction from at least 50 percent of NTSP's physicians. CX 0275 at 26.

## Commission Opinion

what contract terms will be offered. It is not necessary that there be uniform adherence to specific prices by individual members. In *Maricopa*, the Supreme Court found a price-fixing agreement even though the participating physicians were free to set their own prices. 457 U.S. at 356. The Commission reached a similar result in *Motor Transport Ass'n of Connecticut, Inc.*, 112 F.T.C. 309, 336 (1989), stating that association members “need not agree to a single price level in order to fix prices.”<sup>33</sup> In this case, NTSP is able to exert collective bargaining power and hence fix prices because NTSP does not messenger contracts below its minimum reimbursement schedule. Instead it rejects the contracts outright on behalf of its physicians and NTSP’s collective bargaining leverage is thus exerted before its physicians even have a chance to opt in or out of a contract.

c. Powers of Attorney

In several instances, NTSP gathered powers of attorney from members whereby NTSP was appointed as their sole bargaining agent. CX 1173 (Deas IH at 56-57); CX 1065; CX 1061. We find that NTSP used its powers of attorney in a manner similar to the way it used the PPA, and the effect is the same – namely, to solidify its power as a bargaining agent and thus facilitate its price fixing. Jagmin Tr. 1058-60; Beaty Tr. 459-60; Frech Tr. 1327-30.

Respondent argues that this conduct is not evidence of concerted action, that the forms were limited in their application to “any lawful manner,” and that NTSP used them only in

---

<sup>33</sup> See also *In the Matter of Kentucky Household Goods Carriers Assoc., Inc.*, Docket No. 9309, 2005 WL 1541548 at \*11 (FTC June 21, 2005), *review pending*, No. 05-4042 (6th Cir. Aug. 18, 2005); *cf. In re Petroleum Prods. Antitrust Litig.*, 906 F.2d 432, 445-50 (9th Cir.1990) (circulation of current price lists sufficient for liability, even without evidence of agreement to adhere to them), *cert denied*, 500 U.S. 959 (1991).

Commission Opinion

conjunction with a messenger model.<sup>34</sup> RAB at 20. Respondent emphasizes that the powers of attorney did not commit a physician to accept or reject an offer, nor did they give NTSP any power to bind any physician on a non-risk contract. *Id.*

We find however, that the terms of the powers of attorney were clear on their face and improperly granted NTSP “authority to negotiate the terms of, enter into, execute, amend, modify, extend, or terminate” the relevant contracts. CX 347. To induce physicians to grant it powers of attorney, NTSP would include in its solicitations information about the number of physicians who already had executed the powers of attorney. CX 1066; CX 0548 at 1. NTSP physicians referred payors that were attempting to contract directly with them back to NTSP, often noting the deferral was based on agency or powers of attorney held by NTSP. *Beatty Tr.* 454-60, *Grizzle Tr.* 696-98, 724; CX 0760. Furthermore, NTSP advised payors in negotiations that it represented NTSP member physicians through powers of attorney or agency. *Roberts Tr.* 540-41. In one instance, NTSP sent Aetna a list of 180 physicians who had executed powers of attorney appointing NTSP as their bargaining agent for any direct contracting with Aetna. IDF 304. Unrebutted testimony from Aetna officials shows that Aetna understood this as a clear message that these physicians would not negotiate directly with Aetna and therefore concluded that there was no practical alternative to dealing with NTSP. IDF 305-06.

d. NTSP’s Concerted Withdrawals and Refusals to Deal Except on Collective Terms

In several instances NTSP used its agency powers to terminate its members’ participation in a health plan or refused to deal with a payor because NTSP determined that the fee-for-service price paid by the payor was inadequate. CX 0546; CX 0802; CX 1054.

---

<sup>34</sup> We discuss the “messenger model” arguments separately in Section V.B.1.e. below.

## Commission Opinion

For example, when NTSP was dissatisfied at one point during negotiations with United Healthcare Services, Inc., it terminated the United contracts of 101 physicians. IDF 147-54. On another occasion, after CIGNA sent contract assignment letters to Fort Worth physicians, in an attempt to contract with them independent of NTSP, NTSP provided its members with a sample letter refusing the contract assignment and directing CIGNA to negotiate with NTSP as their agent. IDF 205. NTSP advised its physicians not to consent to the assignment, and also sent them an agency agreement authorizing NTSP to negotiate on their behalf. IDF 205. Thereafter CIGNA received 40 letters on behalf of 52 physicians that were virtually identical to the sample letter provided by NTSP. IDF 206. On two other occasions, NTSP threatened to terminate its contract with CIGNA and then later actually terminated its contract, when terms were not satisfactory to NTSP. CIGNA was then forced to capitulate to NTSP's demands. *See* IDF 221-48. We find that NTSP illegally utilized refusals to deal and termination of contracts to enhance the bargaining power of the participating physicians and command higher prices. Frech Tr. 1309-12; 1325.

Respondent argues, first, that NTSP's refusals to deal with payors are protected by the *Colgate* doctrine. RAB at 14-15, citing *United States v. Colgate & Co.*, 250 U.S. 300 (1919). This doctrine holds that a firm, acting unilaterally, may lawfully decide with whom it will, or will not, deal. *Colgate*, 250 U.S. at 307. Respondent views NTSP's refusals of payor offers as the lawful unilateral act of NTSP, and not the act of a group of horizontal competitors acting collectively through its agent, NTSP. RAB at 14-17. It reiterates for this purpose the familiar refrain that (1) NTSP does not have the ability to bind physicians, and (2) that each physician decides individually whether to accept a payor's offer. *Id.* Respondent also cites *Verizon Communications, Inc. v. Law Offices of Curtis v. Trinko, LLP*, 540 U.S. 398, 407-08 (2004), where the Supreme Court reaffirmed the *Colgate* doctrine, and warned that overly zealous enforcement of the antitrust laws

Commission Opinion

can injure competition and innovation. Respondent argues that this admonition should apply to NTSP's refusals to deal. RAB at 15.

Second, Respondent argues as a policy matter that NTSP needs the ability to refuse contracts because it faces potential liability when it becomes a party to a payor contract. RAB at 16. Respondent explains that failure to perform obligations under a contract, involvement in illegal payor conduct, and involvement in deficient medical care can all subject NTSP to liability. *Id.* Further, Respondent states that NTSP has a reputation to protect and involvement in a contract with poor performance can damage NTSP's reputation. *Id.* at 16-17.

We hold that *Colgate* is inapplicable in this case because NTSP's refusals to deal are not the unilateral acts of a single entity but rather are the collective action of all its independent physician members. NTSP's inability to bind members, and the ability of NTSP physicians to reject payor offers does not preclude the conclusion that NTSP has agreed to fix prices. There is a distinction between NTSP's simple refusal to provide services itself and NTSP's refusal to provide services on behalf of the physicians it represents.<sup>35</sup> NTSP was not acting unilaterally but in concert with its physician members. NTSP's conduct therefore does not fall within the bounds of *Colgate*, and the *Trinko* case is similarly not relevant.<sup>36</sup>

---

<sup>35</sup> See *Indiana Fed'n of Dentists*, 476 U.S. at 465 ("That a particular practice may be unlawful is not, in itself, sufficient justification for collusion among competitors to prevent it . . .") (citing *Fashion Originators' Guild of Am., Inc. v. FTC*, 312 U.S. 457, 468 (1941)).

<sup>36</sup> *Trinko* involved conduct by a single firm charged with monopolization under Section 2 of the Sherman Act, not with "contract, combination or conspiracy" under Section 1 of the Sherman Act. *Trinko*, 540 U.S. at 407. Unlike this case, there

## Commission Opinion

NTSP's further claim that its conduct is a necessary protection against liability and loss of reputation is reminiscent of the agreement that was rejected out of hand in *National Society of Professional Engineers*, 435 U.S. 679, and is entirely without factual support. NTSP itself does not need to engage in price fixing to protect itself from liability and loss of reputation.<sup>37</sup> The conduct challenged in this matter does not have anything to do with this type of potential liability, and the evidence shows that NTSP's refusals to deal were motivated by concerns about price and not liability and reputation. For example, NTSP's former president Dr. Vance summarized NTSP's success in its negotiations with United in a letter to his medical group, writing "United Health Care came to town six months ago and offered a straight, 110% of Medicare contract. . . . Through the efforts of NTSP lobbying the City [of Fort Worth] and terming [terminating] a group contract with Health Texas, United blinked. . . . This United negotiation is a template for other efforts that will need to occur in the near future and would best be coordinated by NTSP." CX 0256; *see also* CX 1199 (Vance Dep. at 316-17). Equally compelling is the fact that once payors have capitulated to NTSP's price demands, NTSP's objections disappeared. *See, e.g.*, IDF 242-48. NTSP's statements and its conduct show an overarching concern over price and not other contractual terms.

e. NTSP's Deviations from the "Messenger Model"

Respondent argues that once it decided to become a party to payor contracts it followed the so-called "messenger model" specifically described in *Health Care Statement 9C*, and hence

---

was no allegation that the defendant in *Trinko* had agreed with others to fix prices or refuse to deal.

<sup>37</sup> NTSP can communicate with its physicians on non-economic terms of a contract without price fixing. Frech Tr. 1450.

Commission Opinion

that its actions were lawful. RR at 16; *see* CX 387 at 1; CX 393 at 1; CX 186; CX 1075 at 2; CX 1122. After review of the evidence as a whole, we find that Respondent has deviated from the accepted parameters of a lawful messenger model in a manner that amounts to horizontal price fixing.

There is a wealth of guidance available on this subject. In addition to the discussion in the *Health Care Statements*, at least ten past Commission consents describe conduct that deviated from a lawful messenger model.<sup>38</sup>

Properly used, a messenger model is an arrangement designed to reduce transaction costs associated with negotiation of contracts between providers and payors; it is not a device for facilitating horizontal agreements among providers on prices or price-related terms. In a messenger model, a physician network uses the agent to convey to payors information obtained individually from the providers about the prices or price-related terms that the providers are willing to accept, but the agent does not negotiate on behalf of

---

<sup>38</sup> *See, e.g., In the Matter of Partners Health Network, Inc.*, Docket No. C-4149 (Analysis of Agreement Containing Consent Order, issued Aug. 5, 2005), <http://www.ftc.gov/os/caselist/0410100/0410100.htm>; *In the Matter of San Juan IPA, Inc.*, Docket No. C-4142 (Analysis of Agreement Containing Consent Order, issued May 19, 2005), <http://www.ftc.gov/opa/2005/05/sanjuan.htm>; *In the Matter of Preferred Health Servs., Inc.*, Docket No. C-4134 (Analysis of Agreement Containing Consent Order, issued Mar. 2, 2005), <http://www.ftc.gov/opa/2005/03/scdctors.htm>; *In the Matter of White Sands Health Care System, L.L.C.*, Docket No. C-4130 (Analysis of Agreement Containing Consent Order, issued Sep. 28, 2004), <http://www.ftc.gov/os/caselist/0310135/0310135.htm>; *In the Matter of Southeastern New Mexico Physicians IPA, Inc.*, Docket No. C-4113 (Analysis of Agreement Containing Consent Order, issued June 7, 2004), <http://www.ftc.gov/os/caselist/0310134/0310134.htm>.

## Commission Opinion

the providers. The agent may convey to the providers all contract offers made by purchasers, and each provider then makes an independent, unilateral decision to accept or reject the contract offers. Alternatively, the agent may receive authority from individual providers to accept contract offers that meet certain criteria as long as the agent does not negotiate on their behalf. The agent can also assist providers to understand the contracts offered, by supplying objective or empirical information about the terms of an offer. For example, the agent may provide a comparison of the offered terms with other contracts agreed to by network participants. On the other hand, it would be dangerous for the agent to express an opinion on the terms offered. *See Health Care Statements, supra* note 2, *Statement 9C*.

If a messenger model is used improperly, it can facilitate an unlawful price-fixing agreement. In a legal messenger model, the agent only facilitates independent, unilateral decisions of the network providers. *Id.* It is illegal to use the messenger model in a way that creates or facilitates collective decisions on prices or price-related terms.

It is necessary to look at specific facts on a case-by-case basis, because there is not necessarily any single feature that determines the outcome. Some examples of activities that can tip the balance toward illegality are: agent coordination of provider responses to a particular proposal, dissemination to network providers of the views or intentions of other network providers about the proposal, expression of an opinion on the adequacy of price terms offered, collective negotiation of price terms for the providers, or decisions not to convey an offer if the agent believes the price terms are inadequate. *Id.* A fundamental question is whether the actions of the messenger are designed to facilitate communications or, instead, to enhance the bargaining power of the providers.<sup>39</sup>

---

<sup>39</sup> There are other widely available materials describing the proper use of a messenger model. For example, in 1997, the American Medical Association's Associate General Counsel



Commission Opinion

It is important to remember that any time an agent for a group of competitors engages in any discussions that tinge on the prices they will charge, the parties are in an antitrust danger zone. The so-called messenger model, described in the *Health Care Statements*, provides what the agencies believe is a legal path through this danger zone, but it is dangerous to stray off the route. It is not enough for a physician association simply to claim that it has intended to follow the indicated path; it must show that it actually has done so.

NTSP's refusal to messenger contracts where it determined, based on the results of its prospective price poll, that less than 50 percent of NTSP physicians would join, eliminates the ability of NTSP physicians to decide unilaterally whether to accept the unmessengered contracts and hinders the ability of payors to contract individually with NTSP physicians.<sup>40</sup> We also find that NTSP's PPA, use of powers of attorney and activities associated with its poll, discussed above, are inconsistent with an acceptable use of the model. The PPA and powers of attorney allowed NTSP to negotiate on behalf of its physicians, something expressly forbidden in a proper messenger model. The poll and minimum-fee schedule enabled NTSP to coordinate physician responses to payor proposals. NTSP also went beyond the bounds of

---

advised that a messenger “may develop a schedule showing what percentage of physicians in the network would accept offers at various fee levels” but that “the messenger may not share this information with physicians,” may not negotiate with a payor over fees to be offered to network participants, and “may not decide to forgo an offer because it is too low.” Edward Hirshfeld, *Interpreting the 1996 Federal Antitrust Guidelines for Physician Joint Venture Networks*, 6 ANNALS HEALTH L. 1, 29 (1997).

<sup>40</sup> Cf. Section V.C., which discusses the ability of an agent to charge a reasonable fee for these offers that are unlikely to be accepted.

## Commission Opinion

legitimate messenger activities when it expressed its opinion both to its physician and to the payors themselves on the adequacy of price terms in contract proposals. *See Health Care Statements, supra* note 2, *Statement 9C*.

## 2. The Inherently Suspect Legal Analysis

The restraints described above, as a whole, are what we describe as inherently suspect under *Polygram*. The conduct itself can be said to have a likely tendency to suppress competition because the likelihood of anticompetitive effects from NTSP's restraints is sufficiently grounded in economic theory and supported in case law. Complaint Counsel's expert, Professor Frech, explained the economic rationale for the legal concerns about NTSP's conduct. Frech Tr. 1315-24. Through the mechanisms described above, NTSP was able to collectively set prices and present its physicians as a unified and strong force within Fort Worth. These practices reduce the risk that payors would be able to contract around NTSP, and thereby enhance NTSP's bargaining power over price. Frech Tr. 1325-27; Grizzle Tr. 730, 746-47, 750-51. Because NTSP physicians comprise a large percentage of physicians in Fort Worth, their threat to withhold services severely damages the perceived adequacy of a payor's physician network, and makes it more difficult for a payor to obtain or maintain business. Grizzle Tr. 730-31; Jagmin Tr. 1091-92; Mosely Tr. 139-40. Payors are therefore more willing to pay the NTSP physicians' consensus price because of the threat to their physician networks. Grizzle Tr. 730, 746-47, 750-51; Frech Tr. 1325. NTSP itself summarized the concern succinctly: "NTSP has become a 'gorilla network' with 124 PCP's . . . and 528 specialists." CX 0209 at 2; CX 0310. Conduct that confers on competitors a collective power over price falls within the classic definition of price fixing.

Respondent argues that the Supreme Court's *California Dental* opinion prevents the Commission from condemning NTSP's conduct without a full rule of reason analysis. Respondent's first point in this argument is simply a reiteration of a claim already

Commission Opinion

considered in another context. Respondent says that because there was no direct collusion among physicians,<sup>41</sup> NTSP's conduct meets *California Dental*'s threshold test for determining that a "quick look" rule of reason analysis is not appropriate.<sup>42</sup> RAB at 28-29. Respondent adds that a quick look rule of reason analysis is appropriate only in limited circumstances, when it can be shown that "the great likelihood of anticompetitive effects can be easily ascertained." *Id.* at 29 (citing *California Dental*, 526 U.S. at 771). Because there was no direct collusion among NTSP physicians, Respondent states that the only possible candidates for a quick look under *California Dental* are the PPA provision requiring physicians to notify NTSP of payor offers that they receive directly, and the powers of attorney. *Id.* Respondent further argues that because both of these have plausible procompetitive effects, NTSP's conduct must be judged under a full rule of reason. *Id.*

The first problem with Respondent's argument is that it depends on the faulty conclusion that there was no collusion among NTSP's physicians, simply because they did not directly communicate with each other. As discussed above in Section V.A., the physicians combined in other ways and their conduct can be characterized as price fixing. Moreover, *California Dental* essentially involved collective restrictions on advertising, not on the prices charged. The Court observed that the advertising restrictions in question were "very far from a total ban on price or

---

<sup>41</sup> As pointed out in Section V.A. above, the fact that the doctors did not communicate among themselves, but rather acted through a common agent, does not affect liability.

<sup>42</sup> We have used "inherently suspect" in *Polygram* and in this opinion to refer to conduct that may be justified in some circumstances but, absent these circumstances, can be condemned without an extensive demonstration of adverse market effects in the case at hand. We believe this level of inquiry is what the Supreme Court means by a "quick look."

## Commission Opinion

discount advertising.” *California Dental*, 526 U.S. at 773. The threshold question in *California Dental* was whether the likelihood of anticompetitive effects from restrictions on professional price and quality advertising was sufficiently verifiable in theory and in fact to fall within a general rule of illegality. *Id.* at 771. The Court determined that the restrictions were, at least on their face, designed to avoid false or deceptive advertising in a market characterized by striking disparities between the information available to the professional and the patient. *Id.* Indeed, the Court expressed concern that “the particular restrictions on professional advertising could have different effects from those ‘normally’ found in the commercial world,” *id.* at 773, and that “[t]he obvious anticompetitive effect that triggers abbreviated analysis has not been shown.” *Id.* at 778. Unlike *California Dental*, this case involves prices, not advertising; the challenged conduct therefore has the necessary “obvious anticompetitive effect,” and not something “very far” removed from it.

### C. Respondent’s Justifications

Respondent’s justifications in this case are intermingled with its arguments about the existence of an agreement. *See generally* RAB at 14-18, 28-34, 45-57. We have attempted to sort them out into separate categories, for clarity.<sup>43</sup>

---

<sup>43</sup> Our analysis here deviates somewhat from Complaint Counsel’s proffered analysis. Complaint Counsel’s arguments against Respondent’s proffered justifications are couched in terms of whether NTSP’s price fixing was ancillary to any significant productive collaboration among its participating physicians. As we mentioned above in Section IV.A., the doctrine of ancillary restraints is subsumed in the *Polygram* analysis. (The *Polygram* methodology can also be used more broadly to deal with justifications of a different kind. It could be applied, for example, in a case like *Broadcast Music*, 441 U.S. at 20-25, where the argument was that the system could not function at all without

Commission Opinion

1. Teamwork and Spillover Efficiencies

Respondent argues that its risk panel physicians “use financial and clinical integration techniques to develop team-oriented improvements in cost and quality.” RAB at 49. Respondent further argues that NTSP has a right to “limit” its involvement to non-risk contracts that will be of interest to most of its risk panel physicians, so that their participation will ensure the spillover of the efficient treatment patterns established in the risk contract. *Id.* We interpret Respondent’s use of the word “limit” as intended to explain and justify its particular activities associated with its PPA, powers of attorney, refusals to deal and deviations from the messenger model. Respondent also argues that NTSP’s poll and board minimums are tools that allow NTSP to identify when a non-risk offer will be of interest to most of its physicians, and therefore help it to enhance the spillover effects. *Id.* at 50.

We first do not accept Respondent’s premise that NTSP’s poll and efforts to “limit” NTSP’s involvement to certain non-risk contracts are justified because they will help NTSP to determine when spillover efficiencies are likely to occur. *Id.* at 48-50. The prices NTSP sets through the minimum reimbursement schedule were not prices sought by risk panel doctors, but instead were averages of the members who responded, which includes non-risk doctors. IDF 51, 87, 89-90, 93. NTSP’s Board members and senior management were never informed of individual poll responses; they received only aggregated, average results, which did not reveal to what extent risk panel physicians were likely to

---

collective agreement on price terms, or *United States v. Brown University*, 5 F.3d 658, 677 (3d Cir. 1993), where agreements on student aid could be characterized as pro-competitive overall.) When we use the terminology of *Polygram* rather than the terminology of ancillary restraints, it does not mean that we disagree with Complaint Counsel’s alternative analysis.

## Commission Opinion

participate in non-risk contracts.<sup>44</sup> IDF 94-95. Although these limitations may be prudent, they undercut an argument that the minimum reimbursement schedule could help NTSP determine when spillover efficiencies would occur. As discussed above, it is evident that the poll and limitations were designed for another purpose. *See* discussion in Section V.B.1.a.

Respondent has thus failed to articulate a logical nexus between these activities that facilitate price fixing and the claimed efficiencies. As we stated in *Polygram*, a defendant

must do more than merely assert that its purported justification benefits consumers. Although the defendant need not produce detailed evidence at this stage, it must articulate the specific link between the challenged restraint and the purported justification to merit more searching inquiry into whether the restraint may advance procompetitive goals, even though it facially appears of the type likely to suppress competition.

*Polygram Comm'n Op.*, *supra* note 4, at 31-32.

This conclusion is reinforced by the statement of NTSP's executive director, Karen Van Wagner. During an investigational hearing when she was asked the question whether reimbursement rates at or above NTSP's contracting minimums were necessary in order for NTSP to achieve clinical integration, she testified:

I think it's the other way around. We've achieved a certain degree of clinical integration. We've achieved a certain level of medical management. We've achieved a certain amount of cost savings, satisfaction, quality of care for the members. That basically is reflected in the rates that we ask the payors to

---

<sup>44</sup> Respondent even emphasized in its appeal brief that "it is impossible for [anyone] to determine the response of any specific physician or speciality, or even to determine whether they responded." RAB at 24.

Commission Opinion

give us because that's the value we provide them, so I view it the other way around. Clinical integration is necessary to justify the minimums that the members authorize us to go and try and find.

CX 1196 (Van Wagner IH at 145-46). We explained in *Polygram* that “a defendant cannot defend restraints of trade on the ground that the prices the conspirators set were reasonable, that competition itself is unreasonable or leads to socially undesirable results.” *Polygram Comm'n Op.*, *supra* note 4, at 30-31. There is no antitrust exception for particularly efficient, higher quality market participants; NTSP is not entitled to “pre-empt the working of the market” to produce the result that it believes payors should choose. *Indiana Fed'n of Dentists*, 476 U.S. at 462. Individual non-risk physicians might well be able to command higher fees from payors if they can promise superior outcomes, but this superior efficiency alone would not justify the exercise of collective bargaining power.

There are additional flaws in the spillover efficiency claim. Respondent does not explain how the NTSP physicians who only enter into non-risk contracts could achieve spillover efficiencies from NTSP's single risk contract. This is a non-trivial point, because non-risk physicians make up half of NTSP's members. Van Wagner Tr. 1830; Frech Tr. 1349. Furthermore, NTSP does not even explain why its risk panel physicians will have the incentive to apply the quality and cost control techniques they utilize on risk patients to any non-risk patients they may have. NTSP has not provided any financial incentive for them to do so, and it does nothing to promote compliance with whatever techniques have been learned under risk contracts. IDF 364-80; Deas Tr. 2553-54. NTSP does not employ the processes it uses to monitor and control the quality and utilization of services provided under its risk contracts to patient care provided under non-risk contracts. IDF 364-80; Deas Tr. 2550-54.

We also note that Respondent's counsel admitted that risk contracts are out of favor in Fort Worth, Texas. O.A. at 23; *see*

## Commission Opinion

*also* Wilensky Tr. 2192; IDF 46, 48. NTSP's actions, purportedly justified as efforts to enhance spillover efficiencies from its one risk contract, seem to be perceived by customers merely as an attempt to regulate the terms of access to the more-desired non-risk product. *See generally* Frech Tr. 1349. This justification is inconsistent with the procompetitive aims of the antitrust laws and is not cognizable.

It is worth noting that we are not challenging NTSP's sole risk contract, which involves financial integration, but which NTSP's Board has acknowledged "is a small part of the business." CX 83 at 3. Moreover, Respondent does not make the argument that NTSP's non-risk contracts are sufficiently clinically integrated, as described in *Health Care Statement 8B*, to justify an in-depth rule of reason inquiry. In fact, Respondent all but admits that its administration of these contracts does not constitute clinical integration as commonly understood – *e.g.*, exchange of clinical information, coordination of treatment, development of protocols and monitored compliance. *See, e.g., MedSouth, supra* note 2, at 4-6. Indeed, NTSP's president, Ms. Van Wagner, stated that "NTSP isn't 'there yet' in terms of clinical integration for the care of nonrisk patients."<sup>45</sup> Van Wagner Tr. 1877.

---

<sup>45</sup> Respondent argues instead that the concept of clinical integration does not encompass the full scope of conduct that is justifiable under the rule of reason, and that NTSP's "teamwork" yields sufficient cost and quality benefits. RAB at 51. We do not decide here whether there are potential justifications beyond what the Commission has accepted as "clinical" integration in the past. But Respondent's claim that NTSP's "teamwork" yields cognizable cost and quality benefits simply is not supported by significant evidence. Moreover, Respondent does not address how these nebulous "teamwork" efficiencies are dependent on its price-fixing activities.



Commission Opinion

2. The PPA, Powers of Attorney, Refusals to Deal and Refusals to Messenger Contracts

Respondent also argues that NTSP's PPA notice provision, its use of powers of attorney, its communications with physicians and payors, and its refusal to messenger contracts have plausible procompetitive effects on their own. RAB at 45-57. The PPA ostensibly increases NTSP's contracting opportunities in the marketplace by informing NTSP of new contract opportunities. *Id.* at 30. The powers of attorney ostensibly were gathered by NTSP to inform it of which and how many physicians were willing to be messengered an offer through NTSP. RAB at 31. Respondent also argues that disclosure to physicians that NTSP will not be involved in a particular payor offer will alert physicians that they need to look to other contracting avenues with payors in those situations. RAB at 33.

In addition, Respondent claims that when it informs physicians about a payor's conduct or the status of a payor offer, it is merely collecting and disseminating market information.<sup>46</sup> *Id.* at 34, 53. Respondent states that the procompetitive effects of information sharing in the health care industry, even among competing physicians, is recognized by Complaint Counsel's economic expert and the Commission's advisory opinions. *Id.* Respondent also states that its refusal to convey payor contract offers with prices that NTSP believes are not sufficiently high to attract a majority of its participating physicians is efficient because a physician network has a plausibly valid concern about resources wasted if it were to transmit a payor's offer that is of interest to less than 50 percent of the physicians. *Id.* at 32.

---

<sup>46</sup> Respondent also states that NTSP's comments to a payor about the terms that physicians might find attractive or reasonable can help to educate the payor and expedite contract negotiations. RAB at 34. For reasons discussed in Section V.D. *infra*, this kind of activity is not necessarily suspect.

## Commission Opinion

The problem with these arguments is that most efforts by competitors to collectively agree on prices could be said to save costs in negotiations with customers. (Similarly, an agreement to allocate markets is likely to reduce selling expenses.) Arguments of this kind ultimately are based on the idea that competition itself is inefficient, and are thus not cognizable under the antitrust laws.<sup>47</sup> We explained in *Polygram* that “[c]ognizable justifications ordinarily explain how specific restrictions enable the defendants to increase output or improve product quality, service, or innovation.” *Polygram* at 30. A justification will fail, however, if it contradicts the procompetitive aim of the antitrust laws. *Id.*

These purported justifications are also inconsistent with the evidence. As discussed above in Section V.B.1., the evidence shows that NTSP’s overriding purpose in each of these activities was to exploit its collective bargaining leverage over payors, not to achieve efficiencies. For example, Respondent’s assertion that NTSP helps physicians to determine when they will need to communicate with payors in other ways (because of NTSP’s refusal to deal) is absurd in light of the fact that NTSP routinely cautioned its physicians not to undermine NTSP solidarity and its pricing consensus. In an “Open Letter to the Membership,” NTSP’s Dr. Vance stated, “[w]e must continue to move forward as a group or we will surely falter as individuals.” CX 0550. In another letter, NTSP warned its physicians that fees will decline unless “NTSP or someone can provide a unifying voice for physicians.”<sup>48</sup> CX 0380 at 3. NTSP also implicitly urged its

---

<sup>47</sup> See, e.g., *Maricopa*, 457 U.S. at 346; *Nat’l Soc’y of Prof’l Eng’rs*, 435 U.S. at 689-90; *Goldfarb*, 421 U.S. at 786-87.

<sup>48</sup> See also CX 0380 at 2 (informing its members that through “direct” negotiation or affiliation with other IPAs, NTSP obtained prices “5 to 15% over Tarrant County rates”); CX 0550 (stating to members that it “has provided a consistent premium fee-for-service reimbursement to the members when compared with any

Commission Opinion

physicians to delay or forgo direct contracting during NTSP's negotiations with payors.<sup>49</sup> These actions are designed to enhance bargaining clout, not to increase efficiency from spillover effects, or to conserve resources, or to spread procompetitive benefits of information sharing.

3. Denial of Discovery Request in Support of Purported Justification

Respondent argues that the ALJ erroneously denied NTSP's discovery request for the payors' "flat file" data that would show how NTSP and other physicians performed on non-risk contracts. RAB at 45-46. Respondent claims that, without these files, it has limited capability to show how NTSP's performance compares to other physician providers. *Id.* Respondent also states that PacifiCare and Cigna had provided NTSP with some information in the normal course of business which showed that NTSP is the best performing group in the Dallas/Fort Worth Metroplex and that spillover from care under capitated contracts occurs. *Id.* at 46 n.190.

We find that the ALJ's denial of the discovery request was not detrimental to Respondent. In the absence of a specific link

---

other contracting source").

<sup>49</sup> *See, e.g.*, CX 0310 (Dr. Deas advising NTSP physicians that "discussions are ongoing with Aetna U.S. Healthcare, Cigna, and other major players which should lead to contracts that are more favorable than we would be able to achieve individually or through other contracting entities"); NTSP regularly sent "fax alerts" to its members and held "General Membership Meetings" to continually provide contracting updates for specific payor negotiations and share NTSP's poll results with the membership. CX 1178 at 21-23 (Hollander Dep. at 21-23); CX 0173 – CX 0180; CX 0182 – CX 0188; CX 0615; CX 0945; CX 0903; CX 0617; CX 0628; *see also* Frech Tr. 1326-27.

## Commission Opinion

between the challenged restraints and the purported justification, it would not have mattered if Respondent had been able to obtain further discovery and demonstrate that its physicians performed well. There is no antitrust exemption for more efficient, higher quality market participants, absent a demonstration that the challenged practices made an essential contribution to these efficiencies.<sup>50</sup> Evidence on the performance of NTSP physicians, standing alone, would not prove that nexus.

#### D. Potentially Permissible Conduct

Although we have rejected the proffered justifications for NTSP's particular activities, we do not want this opinion to be read so broadly that it would chill potentially efficient practices. We do not question that NTSP's risk contract and its physicians who participate in it achieve efficiencies, and it could even be possible for these efficiencies to spillover to its non-risk contract in certain circumstances. As we discussed above in Section IV, if an IPA can establish that its joint negotiation of price is reasonably related to an efficiency-enhancing integration of the participants' economic activity and is reasonably necessary to achieve the procompetitive benefits of that integration, the price-related activities may be lawful. A good example of this is described in the Commission staff's advisory opinion letter to MedSouth, Inc., a multi-specialty physician practice association in Denver, Colorado.<sup>51</sup>

---

<sup>50</sup> See, e.g., *Broad. Music*, 441 U.S. at 23-24 (declining to find blanket license fee plan *per se* illegal where plan contributed to integration of sales, monitoring, and enforcement against unauthorized copyright use); *Nat'l Soc'y of Prof'l Eng'rs*, 435 U.S. at 693-95 (rejecting petitioners argument that preventing inferior work justified anti-competitive agreement).

<sup>51</sup> Another example is *In the Matter of California Pacific Medical Group, Inc.*, Docket No. 9306 (consent order issued May 11, 2004), <http://www.ftc.gov/os/adjpro/d9306/index.htm>, where

Commission Opinion

Commission staff did not object to MedSouth's partial integration proposal that included joint negotiation for the sale of its participating physicians' services to payors on a fee-for-service basis. *MedSouth, supra* note 2, at 1, 8-9. Commission staff concluded that MedSouth could plausibly produce sufficient procompetitive effects to justify joint negotiations of fees. *Id.* at 1, 8. This conclusion was based on the extensive clinical resource management program that MedSouth developed for its participating physicians, and that was described in detail in the advisory opinion letter. *Id.* at 2-4, 8. It is also noteworthy that MedSouth did not plan to negotiate contracts on behalf of its physicians until after the operational plan was fully functioning.<sup>52</sup>

---

Commission staff advised California Pacific Medical Group, Inc., d/b/a Brown & Toland Medical Group, that as of that time they would not recommend action against a clinically- integrated PPO product that Brown & Toland Medical Group created after entering into a consent order with the Commission. *See* Advisory Opinion Letter from Daniel P. Ducore, Esq. and David R. Pender, Esq., FTC, to Richard A. Feinstein, Esq., Boies, Schiller & Flexner, LLP (Apr. 5, 2005), <http://www.ftc.gov/os/adjpro/d9306/050405cpbresponsetbnotice.pdf>.

<sup>52</sup> For example, MedSouth developed a web-based electronic clinical data record system that allows MedSouth physicians to access and share medical information relating to their patients, including transcribed patient records, office visit notes, lab reports, radiographic reports, treatment plans, and prescription information. *MedSouth, supra* note 2, at 3. This system could be expected to increase efficiencies by reducing duplicative testing and procedures, expediting treatment, and decreasing medical errors and adverse drug interactions. *Id.* Also important was MedSouth's plan to adopt and implement clinical practice guidelines and performance goals relating to the quality and appropriate use of services provided by its physicians. *Id.* MedSouth had in place a plan to monitor and enforce physician

## Commission Opinion

*Id.* at 4.

NTSP admittedly is not even close to having the efficiency-enhancing processes that MedSouth had committed to have before it began to negotiate for its physicians collectively. For example, NTSP has no disease management program or patient register that would improve health care quality for patients with specific, long-term conditions. Casalino Tr. 2812-14, 2839; Van Wagner Tr. 1834-36. NTSP has no data for patients under its fee-for-service contracts, and NTSP's hospital utilization management program does not apply to patients under its non-risk contracts. Casalino Tr. 2868-69; Frech Tr. 1352-53; Van Wagner Tr. 1837-38. Furthermore, NTSP does not require adherence to its clinical guidelines and protocols. Van Wagner Tr. 1843-44; *see also* Casalino Tr. 2837-39, 2840.

There could also be lawful ways for an association like NTSP to utilize some of the mechanisms discussed above, even without clinical or financial integration. NTSP could, for example, have lawfully polled its members on future fees in order to give payors a sense of the fee levels that would be acceptable to a majority of NTSP physicians, provided that (1) the results of the poll were not communicated back to the physicians in any manner, to avoid influencing their behavior; (2) NTSP did not use the polling results as a basis for determining which payor offers it would elect to messenger to the physicians; and (3) NTSP did not use the polling results to negotiate price with payors. *See Health Care Statements, supra* note 2, *Statement 5B*. NTSP could also lawfully charge an administrative fee to payors to compensate for the burden of messengering contracts that were unlikely to be accepted. For example, if a contract contained rates that were below the rate a threshold percentage of physicians were likely to consider acceptable based on the polling data, NTSP could impose a reasonable transmittal fee (to reimburse the association for an incremental burden, not to signal disapproval). If a payor refused

---

compliance with the guidelines. *Id.* at 3-4.

Commission Opinion

to pay the fee in these situations NTSP could legally refuse to messenger the contract.<sup>53</sup>

Note that these modified practices would not be justified on the ground that they contribute to efficiency of medical practice in the same way that integration does. They rather contribute to the efficiency of the contract negotiation process itself. Because they are not designed to enhance the bargaining power of the physicians, they are not suspect in the first place. They are benign even in the absence of integration.

NTSP can also act as a messenger so long as it adheres to legal standards, which the antitrust agencies have attempted to summarize in the *Health Care Statements*. As discussed above, a key to a lawful messenger model is that the IPA must refrain from using prospective polling results in determining which payor offers it would elect to messenger, and refrain from any activity that amounts to influence over physicians, negotiations on their behalf and coercion of payors. NTSP can also review and comment on non-economic terms of a contract. Furthermore, NTSP can utilize powers of attorney or agency agreements in a manner that does not facilitate a price-fixing agreement. For example, a power of attorney could legally authorize NTSP to enter a contract on behalf of a physician when a physician's stated

---

<sup>53</sup> See Advisory Opinion Letter from Jeffrey W. Brennan, Esq., FTC, to Martin J. Thompson, Esq., Manatt, Phelps & Phillips, L.L.P. (Sept. 23, 2003), <http://www.ftc.gov/bc/adops/bapp030923.htm>, (Commission staff did not object to a physician IPA proposal to refuse to administer contracts where fewer than 50 percent of the physicians accept, unless the payors agree to bear the group's contract administration costs).

## Commission Opinion

price minimum and other terms are met, so long as NTSP does not attempt to influence those key terms, or use powers of attorney to negotiate with a payor.<sup>54</sup>

There is also nothing inherently objectionable about physicians providing current price information to NTSP for a purpose that is unrelated to the actual establishment of prices. For example, NTSP physicians could agree collectively through NTSP to jointly adopt an electronic billing system that would permit them to run their offices more efficiently. If there are sufficient safeguards to shield the billing rates of individual physicians, the practice would not be suspect.

E. Necessity of Market Definition and Market Power

The ALJ held that it was necessary to define a relevant market, even when analyzing a *per se* unlawful price-fixing agreement. ID 61.<sup>55</sup> Complaint Counsel appeal the Initial Decision in part based on this conclusion, and argue that no proof of market definition or market power is required to establish a *per se* violation, citing *Socony-Vacuum Oil*, 310 U.S. at 221-22. CCAB at 35-36. Respondent argues that the rule of reason requires that the market must be defined in this case and that Complaint Counsel would have had this burden even in a *per se* case, citing *California Dental* and the Initial Decision. RAB at 36.

---

<sup>54</sup> We warn, however, that the distinction between lawful and unlawful use of powers of attorney or agency arrangements and the messenger model may require careful counseling. As evidenced by NTSP's conduct in this case, there are many different ways that a power of attorney or agency arrangement and the messenger model can be abused in a manner that facilitates price fixing.

<sup>55</sup> Although Complaint Counsel did not define the market, the ALJ found sufficient evidence to do so on his own. ID at 61-64.



## Commission Opinion

As made clear in the discussion above, we find that proof of market definition and market power is *not* required in this case because Respondent did not meet its burden of establishing a legitimate justification for NTSP's inherently suspect practices. The ALJ may have confused *identification* of a market in which anticompetitive effects are presumed to occur with *definition* of a relevant market in order to measure market share and draw inferences about market power. As we stated in *Kentucky Household Goods Carriers*, "[i]t is obviously necessary to identify the goods or services that are subject to the price-fixing or other anticompetitive restraint . . . [i]t is not necessary, however to show that these goods or services constitute a relevant antitrust product market, as described, for example, in the *Horizontal Merger Guidelines*." *Kentucky Household Goods Carriers*, Docket No. 9309, 2005 WL 1541547 at \*11.<sup>56</sup> The restraints in *Kentucky Household Goods Carriers* were found to be illegal *per se*, but this distinction does not matter. As we have explained above in Sec. III.A., if a practice is either *per se* illegal or inherently suspect, the focus is on the nature of the conduct, not the nature of the market. If there is no legitimate justification for the practice, there is no need for a burdensome inquiry into market conditions. See *FTC v. Superior Court Trial Lawyers Ass'n*, 493 U.S. 411, 433-36 (1990). Simply put, it makes no sense to undertake the exercise of market definition if it will not affect the outcome in any way.

Respondent also argues that Complaint Counsel submitted no empirical evidence in this case to prove NTSP's market power, or

---

<sup>56</sup> In fact, even in a full blown rule of reason case, it may not be necessary to calculate shares in a relevant market if more direct evidence of market effects is available. See *Indiana Fed'n of Dentists*, 476 U.S. at 460-61; *In the Matter of Schering-Plough Corp.*, Docket No. 9297, 2003 WL 22989651, at \*9,11,13 (F.T.C. Dec. 8, 2003) (citations omitted), *rev'd on other grounds*, *Schering-Plough Corp. v. F.T.C.*, 402 F.3d 1056 (11th Cir. 2005), *petition for cert. filed* (U.S. Aug. 29, 2005) (No. 05-273).

## Commission Opinion

to prove that NTSP's conduct caused an anticompetitive effect in any market. RAB at 35- 44. Respondent asserts that NTSP does not have market power and that the numerous avenues through which physicians could and did contract undermine the possibility that any market power existed. *Id.* at 40-41. The ALJ found that NTSP did not receive higher rates than those that other physicians and physician groups were already receiving. ID at 82. The ALJ found only that NTSP obtained higher rates or more beneficial economic terms than the health care payors initially offered to NTSP. *Id.* at 82-83. Respondent states that this has no antitrust significance in the absence of a showing that physicians entered into a boycott conspiracy, because NTSP as an entity can choose to participate or not in a payor offer. RAB at 42-43. Furthermore, Respondent argues that Complaint Counsel's focus on physician rates totally ignores the cost and quality effects of patient care, which are more accurate measures of competitive performance. *Id.* at 43- 44.

We agree that higher physician rates, by themselves, are of no antitrust significance. They may indeed be associated with higher quality of care or with different competitive conditions in various localities. Evidence that payors increased their initial offers similarly is ambiguous, standing alone. Those matters are not what this case is all about; this case is about a concerted effort by NTSP's participating physicians to increase their bargaining power. As discussed above, because Respondent did not meet its burden to establish a legitimate justification for this inherently suspect conduct, NTSP's conduct can be condemned with no further analysis under *Polygram* and other authorities.

## VI. Remedy

The Commission has wide discretion in its choice of a remedy for violations of Section 5 of the FTC Act. *FTC v. Nat'l Lead Co.*, 352 U.S. 419, 428 (1957); *Jacob Siegel Co. v. FTC*, 327 U.S. 608, 611 (1946). This discretion includes not just the prohibition of the illegal practice in the manner exercised in the past, but also so-called "fencing-in" relief, which refers to provisions in an order

Commission Opinion

that are broader in scope than the conduct that is declared unlawful. Fencing-in relief is deemed necessary in some cases in order to prevent future unlawful conduct.<sup>57</sup> The Commission's remedy, however, must be reasonably related to the violation. *FTC v. Ruberoid Co.*, 343 U.S. 470, 473 (1952); *Jacob Siegel*, 327 U.S. at 613.

In this case, we have the benefit of the Commission's extensive experience in crafting appropriate remedies for physician IPAs that have engaged in conduct similar to that of NTSP. Over the years the Commission has fine tuned the relief necessary to prevent future illegal conduct in these cases. To the extent order provisions in these cases have proved ineffective or unnecessary, the Commission has appropriately modified them. The order we impose in this case – which was proposed by Complaint Counsel and is somewhat different than the ALJ's order – is consistent with recent past relief accepted in settlement in similar cases, and is based on the Commission's extensive experience. We are therefore confident that the relief will effectively remedy NTSP's illegal conduct and is neither too narrow nor too broad. Our order is designed to protect the public against any further violations by NTSP, but also to allow NTSP to pursue arrangements that may produce efficiencies without significant risk of anticompetitive consequences.

As usual, Paragraph I of the order defines terms that will be used, and Paragraph II contains general prohibitions against participation in or facilitation of a conspiracy among any physicians. It specifically prohibits agreements to “negotiate”<sup>58</sup>

---

<sup>57</sup> See, e.g., *FTC v. Colgate-Palmolive Co.*, 380 U.S. 374, 395 (1965); *Kraft, Inc. v. FTC*, 970 F.2d 311, 326-27 (7th Cir. 1992).

<sup>58</sup> Although our order does not define the term “negotiate,” we intend it to incorporate the distinctions described in *Health Care Statements 4 and 5* between the lawful provision of factual information and views to payors (as in a true messenger model)

## Commission Opinion

with any payor on behalf of physicians or to refuse to deal on their behalf. A proviso to Paragraph II, however, allows NTSP to engage in “qualified” risk-sharing or clinically-integrated arrangements, and even to set prices for its physicians’ services when doing so is reasonably necessary to the joint arrangement.

In a “qualified clinically-integrated joint arrangement,” as defined by the order in Paragraph I.I., physician participants must participate in active and ongoing programs to evaluate and modify their clinical practice patterns in order to control costs and ensure the quality of services provided, and the arrangement must create a high degree of interdependence and cooperation among physicians. Any agreement concerning price or other terms of dealing must be reasonably necessary to achieve the efficiency goals of the joint arrangement. In a “qualified risk-sharing joint arrangement,” also defined by the order (Paragraph I.J.), all physician participants must share substantial financial risk in order to create incentives for the physician participants jointly to control costs and improve quality. In both cases, any agreements on price or other terms must be reasonably necessary to obtain significant efficiencies through the joint arrangement.

Paragraph III of the order allows NTSP to act as a messenger or an agent on behalf of physicians for contracts with payors, but for three years NTSP is required to notify the Commission in advance before it does so. This prior notice provision is necessary because of NTSP’s past deviations from the messenger model. We have accepted this type of prior notice provision in the past. Our order also requires NTSP to terminate any non-risk contracts it negotiated on behalf of its physicians, so NTSP does not continue to benefit from its unlawfully negotiated contracts. Paragraphs IV.B. and C. set forth the terms by which NTSP is required to terminate the contracts, and additional related requirements. The remaining provisions of our order are either administrative in

---

and efforts to enhance the collective bargaining power of the participating physicians.

Commission Opinion

nature, or relate to NTSP's requirement to notify affected persons of the existence of the order. They impose little burden on NTSP. The order terminates after twenty years.

Respondent argues that the ALJ's order is not narrowly tailored to any antitrust violation properly found. Respondent first asserts that because there was no collusion among physicians, the ALJ's order is not supported in the record. It claims, for example, that because NTSP has the right to negotiate its own contracts, the remedy cannot prohibit NTSP from negotiating contracts. And because there was no collusion among the physicians, it says termination of NTSP's existing physician contracts is not warranted. RAB at 60-62. Respondent also argues that, as worded, prohibitions on NTSP's role in payor negotiations with physicians (particularly on information exchanges among physicians) would apply to non-price as well as price terms and thus conflict with *Health Care Statements* and applicable law. *Id.* at 62.

Respondent's arguments essentially restate their rejected claim that there have been no violations. We find that the prohibitions on collective negotiation and the need to terminate existing contracts are both "reasonably related" to NTSP's unlawful conduct. We also find that the ban on collective bargaining through the use of non-price terms as well as price terms is necessary to ensure that NTSP does not seek to perpetuate its unlawful conduct by orchestrating agreements through non-price or non-economic terms. We also find that it is necessary to terminate NTSP's contracts, so that NTSP's physicians do not continue to reap the benefits of their unlawful price fixing. Even though the contracts are already terminable at will, mandatory termination is necessary to avoid the risk that payors might fear retaliation or suffer short-term competitive disadvantage if they

## Commission Opinion

voluntarily terminate a contract with NTSP. The Commission has used similar or broader fencing-in relief in other physician price-fixing cases.<sup>59</sup>

We find that the ALJ's order is inappropriately narrow in some of its core provisions and therefore fails to provide adequate protection against further violations. Paragraph II of the ALJ's order omitted provisions proposed by Complaint Counsel that would have prohibited agreements on terms of dealing with payors (*i.e.*, without regard to whether there is any agreement to "negotiate") and collective refusals to deal with payors. These limitations were based on the ALJ's view that a prohibition of agreements to refuse to deal would impose on NTSP a broad duty to contract with all payors. ID at 89. The language in our order does not mandate that result. The provisions in question have never been interpreted in that manner in numerous other orders that contain them. These provisions only prohibit conduct by NTSP "in connection with the provision of physician services." Any services provided by NTSP itself that are not directly related to the provision of physician services would not be covered and NTSP would not be forced to contract. As long as NTSP's conduct does not amount to an agreement among physicians to refuse to deal, NTSP will have the ability to refuse certain

---

<sup>59</sup> See, e.g., *In the Matter of Partners Health Network, Inc.*, Docket No. C-4149 (consent order, issued Aug. 5, 2005), <http://www.ftc.gov/os/caselist/0410100/0410100.htm>, (order requires prior notice for three years before Partners Health Network, Inc. can participate in a qualified risk-sharing joint arrangement or a qualified clinically-integrated joint arrangement); *In the Matter of New Millennium Orthopaedics, LLC*, Docket No. C-4140 (consent order, issued May 2, 2005), <http://www.ftc.gov/opa/2005/06/fyi0543.htm>, (order requires dissolution of IPA).

Commission Opinion

contracts.<sup>60</sup> Complaint Counsel have proposed the addition of the phrase “with respect to their provision of physician services” and a new definition of “physician services” in order to further clarify this point. CCAB at 64-65. We have incorporated Complaint Counsel’s proposed clarification.

Paragraph II of the ALJ’s order failed to include language proposed by Complaint Counsel that would have prohibited agreements that physicians not deal individually with payors or through entities other than NTSP. We find that this is an important provision to include in this case because NTSP facilitated a price-fixing agreement through its physicians’ agreement not to deal individually with payors while NTSP was conducting its own negotiations on their behalf *See* Section V.B.1.b. above.

The ALJ’s order also contains two unwarranted provisos to Paragraph II of the order that could enable NTSP to continue its illegal conduct: (1) a statement that nothing in the order bars NTSP from “communicating purely factual information” about a payor offer or “expressing views relevant to various health plans,”<sup>61</sup> and (2) a provision stating that nothing in the order

---

<sup>60</sup> As noted above, NTSP even has the ability to act as a “messenger” under the order. If Respondent complies with the standards for this activity, described in Section V.B.1.e. above, there would not be an order violation.

<sup>61</sup> The ALJ also limited the scope of a provision barring information exchanges. Paragraph II.B. of the ALJ’s order prohibits the exchange of information about the terms on which physicians are willing to deal with a payor, but does not include a prohibition on exchange of information about a physician’s willingness to deal with a payor. We have included this prohibition in past physician price-fixing Commission orders and believe it should be included in this order. NTSP was able to orchestrate its unlawful price-fixing scheme in part by

## Commission Opinion

would “require respondent to violate state or federal law.” ID at 94. We find that neither of the provisos is necessary to protect legitimate conduct by NTSP.<sup>62</sup> The communication of “purely factual information” is already covered by Paragraph III, which allows NTSP to act as a messenger and, given Respondent’s history, we believe that advance notification is necessary for a period of time. In addition, because we have found that there is no basis for a claim that NTSP’s refusals to deal were prompted by concerns over violations of law, we do not believe it is prudent to leave the door open for similar unfounded claims in the future. There is nothing in the order we enter that will require Respondent to engage in illegal activity.

Respondent finally argues that Complaint Counsel’s proposed changes to the ALJ’s order raise serious policy questions about the Commission’s agenda on physician teamwork efforts. RR at 24. Respondent states that Complaint Counsel’s order will chill legitimate conduct on NTSP’s part in response to illegal conduct and breaches of contract by insurance companies, and will discourage teamwork efforts among physicians which do not fit the currently narrow definitions of risk-sharing or clinical integration. *Id.* at 31. Respondent also points out that it is difficult to find any economic evidence that the Commission’s enforcement agenda has had any positive economic effect, in the effort to control total medical expenses. Respondent states that any Commission policy to arbitrarily limit innovation is questionable. *Id.* at 36-37.

---

communicating that its physicians were unwilling to deal with payors in certain situations.

<sup>62</sup> Nearly anything could be termed providing “information” and “views.” For example, NTSP’s announcement that its physicians will not contract with payors at prices below a certain level could be characterized as conveying factual “information” or as an “expression of views.”



Commission Opinion

Respondent's arguments here misunderstand the Commission's role in this industry. We have a responsibility to prosecute antitrust offenses, but, as stated at the outset, we also should foster pro-competitive, innovative delivery mechanisms for health care in this country. NTSP's illegal conduct has not helped it achieve any efficiencies. Our order, which proscribes only conduct used to carry out NTSP's unlawful price-fixing activities, will not inhibit any efforts to achieve efficiency and innovation through the teamwork or other integration of physicians. We describe in Section V.D. above the many constructive activities that an IPA can undertake, consistent with the antitrust laws. And as noted above, Paragraph II of our order allows NTSP to engage in legitimate joint arrangements and even set prices for its physicians' services, but only when doing so is reasonably necessary to achieve the efficiencies of the joint arrangement.

VII. Conclusion

For all of the reasons outlined above, we conclude that NTSP's contracting activities with payors amount to unlawful horizontal price fixing. Through the various mechanisms described above, NTSP was able to orchestrate price agreements among its physicians. In physician IPA cases like this one, the focus is not necessarily on any single price-fixing mechanism, but rather on the conduct as a whole. Here the evidence shows not only negotiation activity in aid of a collective agreement on a minimum fee schedule, but also specific enforcement mechanisms – such as the powers of attorney and collective withdrawal from payor networks – in order to coerce agreement from payors. These actions viewed as a whole leave no doubt that the overriding purpose behind NTSP's conduct was to fix prices.

This is not really a close case. NTSP's conduct is similar to conduct that has been held *per se* unlawful and summarily condemned in other contexts. For the reasons stated, we have analyzed the conduct under our more flexible *Polygram* framework, and considered each of Respondent's defenses in depth. Our ultimate conclusion is the same.

Final Order

**FINAL ORDER**

This matter having been heard by the Commission upon the appeal of Respondent and the cross-appeal of Complaint Counsel, and upon briefs and oral argument in support thereof and opposition thereto, and the Commission, for the reasons stated in the accompanying Opinion, having determined to sustain the Initial Decision with certain modifications:

**IT IS ORDERED THAT** the Initial Decision of the administrative law judge be, and it hereby is, adopted as the Findings of Fact and Conclusions of Law of the Commission, to the extent it is not inconsistent with the findings of fact and conclusions of law contained in the accompanying Opinion.

Other findings of fact and conclusions of law of the Commission are contained in the accompanying Opinion.

**IT IS FURTHER ORDERED THAT** the following Order to cease and desist be, and it hereby is, entered:

**ORDER****I.**

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

- A. “Respondent” means North Texas Specialty Physicians (“NTSP”), its officers, directors, employees, agents, attorneys, representatives, successors, and assigns; and the subsidiaries, divisions, groups, and affiliates controlled by North Texas Specialty Physicians, and the respective officers, directors, employees, agents, attorneys, representatives, successors, and assigns of each.
- B. “Participate” in an entity means: (1) to be a partner, shareholder, owner, member, or employee of such entity; or (2)

Final Order

to provide services, agree to provide services, or offer to provide services, to a payor through such entity. This definition also applies to all tenses and forms of the word “participate,” including, but not limited to, “participating,” “participated,” and “participation.”

- C. “Payor” means any person that pays, or arranges for the payment, for all or any part of any physician services for itself or for any other person. Payor includes any person that develops, leases, or sells access to networks of physicians.
- D. “Person” means both natural persons and artificial persons, including, but not limited to, corporations, unincorporated entities, and governments.
- E. “Physician” means a doctor of allopathic medicine (“M.D.”) or a doctor of osteopathic medicine (“D.O.”).
- F. “Physician services” means professional services provided to patients by physicians.
- G. “Preexisting contract” means a contract for the provision of physician services, other than the contract identified in Appendix B to this Order, that was in effect on the date of receipt by a payor that is a party to such contract of notice sent by Respondent, pursuant to Paragraph V.A.3 of this Order, of such payor’s right to terminate such contract.
- H. “Principal address” means either (1) primary business address, if there is a business address, or (2) primary residential address, if there is no business address.
- I. “Qualified clinically-integrated joint arrangement” means an arrangement to provide physician services in which:
  - 1. all physicians who participate in the arrangement participate in active and ongoing programs of the arrangement to evaluate and modify the practice patterns of, and create a

## Final Order

high degree of interdependence and cooperation among, the physicians who participate in the arrangement, in order to control costs and ensure the quality of services provided through the arrangement; and

2. any agreement concerning price or other terms or conditions of dealing entered into by or within the arrangement is reasonably necessary to obtain significant efficiencies through the arrangement.

J. “Qualified risk-sharing joint arrangement” means an arrangement to provide physician services in which:

1. all physicians who participate in the arrangement share substantial financial risk through their participation in the arrangement and thereby create incentives for the physicians who participate jointly to control costs and improve quality by managing the provision of physician services, such as risk-sharing involving:
  - a. the provision of physician services for a capitated rate;
  - b. the provision of physician services for a predetermined percentage of premium or revenue from payors;
  - c. the use of significant financial incentives (*e.g.*, substantial withholds) for physicians who participate to achieve, as a group, specified cost-containment goals; or
  - d. the provision of a complex or extended course of treatment that requires the substantial coordination of care by physicians in different specialties offering a complementary mix of services, for a fixed, predetermined price, where the costs of that course of treatment for any individual patient can vary greatly due to the individual patient’s condition, the choice, complexity, or length of treatment, or other factors; and

Final Order

2. any agreement concerning price or other terms or conditions of dealing entered into by or within the arrangement is reasonably necessary to obtain significant efficiencies through the arrangement.

**II.**

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

- A. Entering into, adhering to, participating in, maintaining, organizing, implementing, enforcing, or otherwise facilitating any combination, conspiracy, agreement, or understanding between or among any physicians with respect to their provision of physician services:
  1. to negotiate on behalf of any physician with any payor;
  2. to deal, refuse to deal, or threaten to refuse to deal with any payor;
  3. regarding any term, condition, or requirement upon which any physician deals, or is willing to deal, with any payor, including, but not limited to, price terms; or
  4. not to deal individually with any payor, or not to deal with any payor through any arrangement other than Respondent;
- B. Exchanging or facilitating in any manner the exchange or transfer of information among physicians concerning any physician’s willingness to deal with a payor, or the terms or conditions, including price terms, on which the physician is willing to deal;

## Final Order

- C. Attempting to engage in any action prohibited by Paragraphs II.A or II.B above; and
- D. Encouraging, suggesting, advising, pressuring, inducing, or attempting to induce any person to engage in any action that would be prohibited by Paragraphs II.A through II.C above.

**PROVIDED HOWEVER**, that nothing in this Paragraph II of this Order shall prohibit any agreement involving or conduct by Respondent that is reasonably necessary to form, participate in, or take any action in furtherance of a qualified risk-sharing joint arrangement or a qualified clinically-integrated joint arrangement;

**III.**

**IT IS FURTHER ORDERED** that, for three (3) years after the date this Order becomes final, Respondent shall notify the Secretary of the Commission in writing (“Notification”) at least sixty (60) days prior to entering into any arrangement with any physicians under which Respondent would act as a messenger, or as an agent on behalf of those physicians, with payors regarding contracts. The Notification shall include the identity of each proposed physician participant; the proposed geographic area in which the proposed arrangement will operate; a copy of any proposed physician participation agreement; a description of the proposed arrangement’s purpose and function; a description of any resulting efficiencies expected to be obtained through the arrangement; and a description of procedures to be implemented to limit possible anticompetitive effects, such as those prohibited by this Order. Notification is not required for Respondent’s subsequent acts as a messenger pursuant to an arrangement for which this Notification has been given. Receipt by the Commission from Respondent of any Notification, pursuant to this Paragraph III of this Order, is not to be construed as a determination by the Commission that any action described in such Notification does or does not violate this Order or any law enforced by the Commission.

Final Order

**IV.**

**IT IS FURTHER ORDERED** that Respondent shall:

- A. Within thirty (30) days after the date on which this Order becomes final, send by first-class mail, return receipt requested, a copy of this Order and the Complaint to:
1. each physician who participates, or has participated, in Respondent since January 1, 2000;
  2. each officer, director, manager, and employee of Respondent; and
  3. the chief executive officer of each payor with which Respondent has a record of having been in contact, since January 1, 2001, regarding contracting for the provision of physician services, and include in such mailing the notice specified in Appendix A to this Order;
- B. Terminate, without penalty or charge, and in compliance with any applicable laws, any preexisting contract with any payor for the provision of physician services, other than the contract identified in Appendix B to this Order, at the earliest of:
1. receipt by Respondent of a written request from a payor to terminate such contract, or
  2. the earliest termination or renewal date (including any automatic renewal date) of such contract;

**PROVIDED, HOWEVER,** a preexisting contract may extend beyond any such termination or renewal date no later than one (1) year after the date on which the Order becomes final, if prior to such termination or renewal date, (a) the payor submits to Respondent a written request to extend such contract to a specific

## Final Order

date no later than one (1) year after the date this Order becomes final, and (b) Respondent has determined not to exercise any right to terminate;

**PROVIDED FURTHER**, that any payor making such request to extend a contract retains the right, pursuant to part (1) of Paragraph IV.B of this Order, to terminate the contract at any time;

- C. Within ten (10) days after receiving a written request from a payor, pursuant to Paragraph IV.B(1) of this Order, distribute, by first-class mail, return receipt requested, a copy of that request to each physician participating in Respondent as of the date Respondent receives such request.
- D. For a period of three (3) years after the date this Order becomes final:
1. distribute by first-class mail, return receipt requested, a copy of this Order and the Complaint to:
    - a. each physician who begins participating in Respondent, and who did not previously receive a copy of this Order and the Complaint from Respondent, within thirty (30) days of the time that such participation begins;
    - b. each payor who contracts with Respondent for the provision of physician services, and who did not previously receive a copy of this Order and the Complaint from Respondent, within thirty (30) days of the time that such payor enters into such contract; and
    - c. each person who becomes an officer, director, manager, or employee of Respondent and who did not previously receive a copy of this Order and the Complaint from Respondent, within thirty (30) days of the time that he or she assumes such responsibility with Respondent; and



Final Order

2. annually publish a copy of this Order and the Complaint in an official annual report or newsletter sent to all physicians who participate in Respondent, with such prominence as is given to regularly featured articles;
- E. File a verified written report within sixty (60) days after the date this Order becomes final, and annually thereafter for three (3) years on the anniversary of the date this Order becomes final, and at such other times as the Commission may by written notice require. Each such report shall include:
1. a detailed description of the manner and form in which Respondent has complied and is complying with this Order;
  2. copies of the return receipts required by Paragraphs IV.A, IV.C, and IV.D of this Order; and
- F. Notify the Commission at least thirty (30) days prior to any proposed change in Respondent, such as dissolution, assignment, sale resulting in the emergence of a successor company or corporation, the creation or dissolution of subsidiaries, or any other change in Respondent that may affect compliance obligations arising out of this Order.

**V.**

**IT IS FURTHER ORDERED** that Respondent shall notify the Commission of any change in its principal address within twenty (20) days of such change in address.

**VI.**

**IT IS FURTHER ORDERED** that, for the purpose of determining or securing compliance with this Order, Respondent shall permit any duly authorized representative of the Commission:

## Final Order

- A. Access, during office hours and in the presence of counsel, to inspect and copy all books, ledgers, accounts, correspondence, memoranda, calendars, and other records and documents in its possession, or under its control, relating to any matter contained in this Order; and
- B. Upon five (5) days' notice to Respondent, and in the presence of counsel, and without restraint or interference from it, to interview Respondent or employees of Respondent.

**VII.**

**IT IS FURTHER ORDERED** that this Order shall terminate twenty (20) years from the date it is issued.

Final Order

## APPENDIX A

**Letter to payors with whom NTSP has a contract at the time the Order becomes final, other than a contract listed in Appendix B to the Order – to be sent within thirty (30) days after the Order becomes final**

[letterhead of Respondent NTSP]

[name of payor's CEO]  
[address]

Dear \_\_\_\_\_:

Enclosed is a copy of a complaint and a decision and order (“Order”) issued by the Federal Trade Commission against North Texas Specialty Physicians (“NTSP”).

Pursuant to Paragraph IV.B of the Order, NTSP must allow you to terminate, upon your written request, without any penalty or charge, any contracts with NTSP that are in effect at the time of your receipt of this letter.

Paragraph IV.B of the Order also provides that, if you do not terminate a contract currently in effect with NTSP, the contract will terminate on its termination or renewal date (including any automatic renewal date). However, if the contract terminates on a date prior to **[appropriate date one (1) year after Order became final]**, the contract may be extended at your written request to a date no later than **[appropriate date one (1) year after Order became final]**. The Order became final on **[appropriate date to be filled in]**. If you choose to extend the term of the contract, you may later terminate the contract at any time prior to **[appropriate date one (1) year after Order became final]**.

Final Order

Any request either to terminate or to extend the contract should be made in writing, and sent to me at the following address:  
**[NTSP's address]**.

Sincerely,

Final Order

**APPENDIX B**

Pacificare of Texas ANHC/IPA Services Agreement (Professional Capitation/Approved Nonprofit Health (sic) Corporation (dated July 1, 2000), as amended September 1, 2001 and January 1, 2003 [identified as RX 18, including pages RX0018\_001 through RX0018\_087; also identified by Bates numbers PCT 000924 through PCT 000986 and PCT 000895 through PCT 000918; and Bates numbers FTC-NTSP-PCFC 000327 through FTC-NTSP-PCFC 000389 and FTC-NTSP-PCFC 000298 through FTC-NTSP-PCFC 000321].

Complaint

**COMPLAINT**

Pursuant to the provisions of the Federal Trade Commission Act, as amended, 15 U.S.C. § 41 *et seq.*, and by virtue of the authority vested in it by said Act, the Federal Trade Commission, having reason to believe that North Texas Specialty Physicians has violated Section 5 of the Federal Trade Commission Act, 15 U.S.C. § 45, and it appearing to the Commission that a proceeding by it in respect thereof would be in the public interest, hereby issues this Complaint stating its charges in that respect as follows:

**RESPONDENT**

**PARAGRAPH 1:** Respondent North Texas Specialty Physicians (hereinafter “NTSP”) is a non-profit corporation, organized, existing, and doing business under and by virtue of the laws of

Texas, with its office and principal place of business at 1701 River Run Road, Suite 210, Fort Worth, Texas 76107.

**JURISDICTION**

**PARAGRAPH 2:** NTSP was formed by physicians to facilitate the physicians’ contracting with health insurance firms and other third-party payors (collectively, “payors”) for the provision of medical services. At all times relevant to this Complaint, participating physicians of NTSP have been engaged in the business of providing medical care for a fee. Except to the extent that competition has been restrained as alleged herein, participating physicians of NTSP have been, and are now, in competition with each other for the provision of physician services.

**PARAGRAPH 3:** While NTSP is a memberless corporation under state law, it was founded by, is controlled by, and carries on business for the pecuniary benefit of its participating physicians. Accordingly, the participating physicians are “members” of NTSP, and NTSP therefore is a “corporation,” as those terms are

Complaint

used in Section 4 of the Federal Trade Commission Act, as amended, 15 U.S.C. § 44.

**PARAGRAPH 4:** The general business practices of NTSP, including the acts and practices herein alleged, are in or affecting “commerce” as defined in the Federal Trade Commission Act, as amended, 15 U.S.C. § 44.

**OVERVIEW OF MARKET AND PHYSICIAN  
COMPETITION**

**PARAGRAPH 5:** NTSP has approximately 600 participating physicians licensed to practice medicine in the State of Texas who are engaged in the business of providing professional services to patients in the Dallas-Fort Worth metropolitan area, mostly in Fort Worth and the “Mid Cities” (collectively, the “Fort Worth area”).

**PARAGRAPH 6:** Physicians often contract with payors to establish the terms and conditions, including price terms, under which such physicians will render services to the payors’ subscribers. Physicians entering into such contracts often agree to lower compensation to obtain access to additional patients made available by the payors’ relationship with insureds. These contracts may reduce payors’ costs, enable them to lower the price of insurance, and reduce out-of-pocket medical expenditures by subscribers to the payors’ health insurance plans.

**PARAGRAPH 7:** Absent agreements among competing physicians on the terms, including price, on which they will provide services to subscribers or enrollees in health care plans offered or provided by payors, competing physicians decide individually whether to enter into contracts with payors to provide services to their subscribers or enrollees, and what prices they will accept pursuant to such contracts.

**PARAGRAPH 8:** Medicare’s Resource Based Relative Value Scale (“RBRVS”) is a system used by the United States Centers for Medicare and Medicaid Services to determine the amount to

## Complaint

pay physicians for the services they render to Medicare patients. The RBRVS approach provides a method to determine fees for specific services. In general, it is the practice of payors in the Fort Worth area to make contract offers to individual physicians or groups at a fee level specified in the RBRVS, plus a markup based on some percentage of that fee (*e.g.*, “110% of 2001 Tarrant County RBRVS”).

**PARAGRAPH 9:** To be competitively marketable in the Fort Worth area, a payor’s health insurance plan must include in its physician network a large number of primary care physicians and specialists who practice in the Fort Worth area. Many of the primary care physicians and specialists who practice in the Fort Worth area are participating physicians of NTSP.

**PARAGRAPH 10:** Competing physicians sometimes use a “messenger” to facilitate the establishment of contracts between themselves and payors in ways that do not constitute or facilitate an unlawful agreement on fees and other competitively significant terms. Such an arrangement, however, will not avoid horizontal agreement if the “messenger” or another agent negotiates fees and other competitively significant terms on behalf of the participating physicians, or facilitates the physicians’ coordinated responses to contract offers by, for example, electing not to convey a payor’s offer to them based on the agent’s, or the participants’, opinion on the appropriateness, or lack thereof, of the offer.

**RESTRAINT OF TRADE**

**PARAGRAPH 11:** NTSP’s participating physicians, including the members of its Board of Directors, constitute numerous discrete economic interests. The conduct of NTSP constitutes combined or concerted action by its participating physicians.

**PARAGRAPH 12:** NTSP, acting as a combination of competing physicians, and in combination with physicians and other physician organizations, has restrained competition among its participating physicians by, among other things:



Complaint

- A. facilitating, negotiating, entering into, and implementing agreements among its participating physicians on price and other competitively significant terms;
- B. refusing or threatening to refuse to deal with payors except on collectively agreed-upon terms; and
- C. negotiating fees and other competitively significant terms in payor contracts for NTSP's participating physicians, and refusing to submit payor offers to participating physicians unless and until price and other competitively significant terms conforming to NTSP's contract standards have been negotiated.

Complaint

**FORMATION AND OPERATION OF NTSP**

**PARAGRAPH 13:** NTSP was organized in November 1995 as a nonprofit corporation. Its initial Board of Directors, composed of three participating physicians, was established in NTSP's Certificate of Incorporation. Pursuant to NTSP's By-Laws, successor Board members are elected from among the participating physicians for three-year terms by the members of each of NTSP's sections, which are organized by medical specialty. NTSP is funded through fees paid by physicians on first becoming participating physicians and through its receipt, pursuant to its physician participation agreements, of a stated percentage of the fees paid by payors to participating physicians pursuant to certain NTSP-payor contracts. NTSP presently is composed of approximately 600 physicians, some 130 of whom are primary care physicians.

**PARAGRAPH 14:** Pursuant to a few of NTSP's contracts with payors, some of the NTSP physicians who participate in the arrangement share financial risk, for example, through the provision of services at an agreed capitated rate. However, pursuant to the great majority of NTSP's contracts with payors, those NTSP physicians who participate in the arrangement do not share any financial risk, each physician typically receiving a specified fee for each service provided. Whereas only about one-half of NTSP's participating physicians—and few if any primary care providers—participate in any risk-sharing arrangements, substantially all of NTSP's participating physicians participate in some non-risk contracts. With respect to these non-risk contracts, NTSP often has sought to negotiate for, and often has obtained, higher fees and other more advantageous terms than its individual physicians could obtain by negotiating individually with payors.

**PARAGRAPH 15:** Physicians seeking to participate in NTSP-payor contracts apply for participating physicianship. A physician becomes a participating physician by entering into a "North Texas Specialty Physicians Physician Participation Agreement" with NTSP, granting to NTSP authority to arrange for his or her

Complaint

services to be provided to persons covered by payors pursuant to agreements between NTSP and the payors. Each physician covenants that he or she will forward to NTSP for further handling payor offers the physician receives, and will refrain from pursuing any such offer until NTSP notifies the physician that it is permanently discontinuing negotiations with the payor. If, and only if, NTSP approves and enters into an agreement with a payor, NTSP then forwards the agreement to its participating physicians, who then may elect to participate (or not) in the payor's offer.

### **NTSP'S ILLEGAL ACTS AND PRACTICES**

**PARAGRAPH 16:** NTSP has engaged in various acts and practices, as more fully described subsequently, that unlawfully restrain competition among NTSP's participating physicians. NTSP has undertaken these acts and practices with the knowledge of its Directors and other participating physicians, and often at their explicit instruction.

**PARAGRAPH 17:** NTSP periodically polls its participating physicians, asking each to disclose the minimum fee, typically stated in terms of a percentage of RBRVS, that he or she would accept in return for the provision of medical services pursuant to an NTSP-payor agreement. In conformity with its agreement with its participating physicians, NTSP then calculates the mean, median, and mode ("averages") of minimum acceptable fees reported by its physicians. NTSP then reports these measures back to its participating physicians, confirming to the participating physicians that these averages will constitute the minimum fees that NTSP will entertain as the basis of any contract with a payor. Such interchanges of prospective price information among otherwise competing physicians reduce price competition among those physicians, and enable the participating physicians, acting through NTSP and otherwise, to price their services interdependently to achieve supra-competitive prices.

**PARAGRAPH 18:** Sometimes when NTSP begins discussions with a payor regarding a possible contract for the provision of

## Complaint

services by NTSP's participating physicians, NTSP informs the payor that its physicians have established fee minimums for NTSP-payor agreements, identifies those fee minimums (the poll averages referred to in the preceding Paragraph), and states that NTSP will not enter into or otherwise forward to its participating physicians any payor offer that does not satisfy those fee minimums.

**PARAGRAPH 19:** In other instances, payors have proposed to NTSP agreements, or amendments to existing agreements, for the services of its participating physicians that included proposed fee schedules that did not satisfy the NTSP physicians' fee minimums. NTSP has then advised the payors of NTSP's established fee minimums and told the payors to resubmit their proposals with fee schedules that satisfy those minimums, or otherwise actively bargained with payors as to fees to be paid NTSP's participating physicians. As a result, payors sometimes have either submitted new offers with higher fees or accepted the higher fees pressed on them by NTSP on behalf of its physicians.

**PARAGRAPH 20:** In at least one instance, NTSP, at the explicit dictate of its Directors, sought instruction from its participating physicians as to the disposition of a payor offer that already had been made. NTSP wrote to its participating physicians, reminding them of their previously agreed-to minimums and noting that the specified payor's offer approximated those minimums as to some of its medical insurance plans, but fell materially below those minimums as to other plans. NTSP then asked each of its participating physicians to respond to a poll by indicating the minimum fees, again typically stated in terms of a percentage of RBRVS, that he or she would accept in return for the provision of medical services to the specific payor's subscribers. When NTSP calculated the average minimum fees that its participating physicians would accept to contract with that payor, it found that the participating physicians collectively would not accept fees lower than the previously established minimums. It then rejected the payor's offer and explicitly refused to forward the offer to any of its participating physicians, whether or not the proposed fees

Complaint

were above any given physicians' stated minimum acceptable fees. Following refusals by NTSP to forward the proposed contract to its participating physicians and several communications between NTSP and its participating physicians attacking the payor's fee proposal as "below market," the payor increased its proposed fees to the NTSP fee minimums. Only then did NTSP enter into a contract with the payor and forward the agreement to its participating physicians, affording them the option to participate (or not) in the payor's offer.

**PARAGRAPH 21:** In addition, while seeking to negotiate fees on behalf of its participating physicians, NTSP has discouraged and prevented payors and participating physicians from negotiating directly with one another. In at least one instance, after NTSP fee negotiations with a payor broke down, NTSP orchestrated the simultaneous withdrawal of NTSP physicians from an arrangement pursuant to which numerous NTSP participating physicians had provided medical services to the payor's subscribers through another physician organization with which NTSP had contracted. This increased the pressure on the payor to contract for the services of NTSP's participating physicians through NTSP, at higher proposed fees. The payor ultimately yielded to that pressure and contracted with NTSP and its physicians at increased fee levels.

**LACK OF SIGNIFICANT EFFICIENCIES**

**PARAGRAPH 22:** The acts and practices described in Paragraphs 16 through 21, including NTSP's negotiation of fees and other competitively significant terms of contracts under which each physician is paid on a fee-for-service basis, have not been, and are not, reasonably related to any efficiency-enhancing integration. With respect to these contracts, NTSP's participating physicians do not share substantial financial risk and are not otherwise integrated in ways that would create the potential for increased quality and reduced cost of medical care that the physicians provide to patients.

Complaint

**ANTICOMPETITIVE EFFECTS**

**PARAGRAPH 23:** NTSP's acts and practices as described herein have had, or tend to have, the effect of restraining trade unreasonably and hindering competition in the provision of physician services in the Fort Worth area in the following ways, among others:

- A. price and other forms of competition among NTSP's participating physicians were unreasonably restrained;
- B. prices for physician services were increased; and
- C. health plans, employers, and individual consumers were deprived of the benefits of competition among physicians.

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

---

**NOTICE**

Notice is hereby given to the Respondent that the sixteenth day of January, 2004, at 10:00 a.m. o'clock, or such later date as determined by an Administrative Law Judge of the Federal Trade Commission, 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 a hearing will be had before an Administrative Law Judge of the Federal Trade Commission, on the charges set forth in this Complaint, at which time and place you will have the right under the Federal Trade Commission Act

Complaint

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 this Complaint.

You are notified that the opportunity is afforded you to file with the Commission an answer to this Complaint on or before the twentieth (20th) 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 allegations to be true. Such an answer shall constitute a waiver of hearings as to the facts alleged in the Complaint, and together with the Complaint will provide a record basis on which the Administrative Law Judge shall file an initial decision containing appropriate findings and conclusions and an appropriate Order disposing of the proceeding. In such answer you may, however, reserve the right to submit proposed findings and conclusions under Section 3.46 of the Commission's Rules of Practice for Adjudicative Proceedings and the right to appeal the initial decision to the Commission under Section 3.52 of said Rules.

Failure to answer within the time above provided shall be deemed to constitute a waiver of your right to appear and contest the allegations of the Complaint and shall authorize the Administrative Law Judge, without further notice to you, to find the facts to be as alleged in the Complaint and to enter an initial decision containing such findings, appropriate conclusions, and Order.

## Complaint

The Administrative Law Judge will schedule an initial prehearing scheduling conference to be held not later than 14 days after the last answer is filed by the Respondent. Unless otherwise directed by the Administrative Law Judge, the scheduling conference and further proceedings will take place at the Federal Trade Commission, 600 Pennsylvania Avenue, N.W., Room 532, Washington, D. C. 20580. Rule 3.21(a) requires a meeting of the parties' counsel as early as practicable before the prehearing scheduling conference, and Rule 3.31(b) obligates counsel for each party, within 5 days of receiving Respondent's answer, to make certain initial disclosures without awaiting a formal discovery request.

**NOTICE OF CONTEMPLATED RELIEF**

Should the Commission conclude from the record developed in any adjudicative proceeding in this matter that Respondent North Texas Specialty Physicians ("NTSP") is in violation of Section 5 of the Federal Trade Commission Act as alleged in the Complaint, the Commission may order such relief as is supported by the record and is necessary and appropriate, including, but not limited to:

1. An Order to cease and desist from entering into, adhering to, participating in, maintaining, organizing, implementing, enforcing, or otherwise facilitating any combination, conspiracy, agreement, or understanding between or among any physicians: (a) to negotiate on behalf of any physician with any payor; (b) to deal, refuse to deal, or threaten to refuse to deal with any payor; (c) regarding any term, condition, or requirement upon which any physician deals, or is willing to deal, with any payor, including, but not limited to, price terms; or (d) not to deal individually with any payor, or not to deal with any payor through any arrangement other than NTSP.
2. An Order to cease and desist from exchanging or facilitating in any manner the exchange or transfer of information among physicians concerning any physician's willingness to deal with



Complaint

a payor, or the terms or conditions, including price terms, on which the physician is willing to deal.

3. An Order to cease and desist from attempting to engage in any action prohibited by Paragraphs 1 or 2, above.
4. An Order to cease and desist from encouraging, suggesting, advising, pressuring, inducing, or attempting to induce any person to engage in any action that would be prohibited by Paragraphs 1-3, above.
5. A requirement that, for a period of five (5) years, NTSP notify the Commission prior to entering into any arrangement with any physicians under which NTSP would act as a messenger, or as an agent, on behalf of those physicians.
6. An Order requiring NTSP to terminate, without penalty or charge, and in compliance with any applicable laws, any contract that it has entered into with any payor since January 1, 1998.
7. An Order to cease and desist from engaging in, attempting to engage in, or encouraging others to engage in illegal horizontal agreements with competitors.
8. Any other provision appropriate to correct or remedy the anticompetitive practices engaged in by NTSP.
9. A requirement that NTSP distribute a copy of the Order and Complaint, within thirty (30) days after the Order becomes final, to: (a) each physician who is participating, or has participated, in NTSP since January 1, 1998; (b) each officer, director, or manager, and each employee who has or had any responsibility regarding NTSP's physician networks; and (c) each payor that NTSP has contacted, or been contacted by, since January 1, 1998, regarding contracting for the provision of physician services.

## Complaint

10. A requirement that for five (5) years after the Order becomes final, NTSP distribute a copy of the Order and Complaint, within thirty (30) days of the event triggering this requirement, to: (a) each newly participating physician in NTSP; (b) each person who becomes an officer, director, or manager, or an employee who has any responsibility regarding NTSP's physician networks; and (c) each payor that NTSP contacts, or is contacted by, regarding contracting for the provision of physician services.
11. A requirement that for five (5) years after the Order becomes final, NTSP annually publish a copy of the Order and the Complaint in an official report or newsletter sent to all physicians who participate in NTSP, and on any website maintained by or for NTSP, with such prominence as is given to regularly featured articles.
12. Requirements that NTSP file periodic compliance reports with the Commission, notify the Commission of any changes that may affect compliance obligations, and permit Commission representatives prompt access to NTSP documents and personnel for the purpose of determining or securing compliance with this Order.

WHEREFORE, THE PREMISES CONSIDERED, the Federal Trade Commission, on this sixteenth day of September, 2003, issues its Complaint against NTSP.

Initial Decision

## INITIAL DECISION

By D. Michael Chappell, Administrative Law Judge

### I. INTRODUCTION

#### A. Summary of Decision

This is a horizontal price fixing case. The Federal Trade Commission ("FTC") charges that Respondent North Texas Specialty Physicians ("NTSP"), on behalf of its participating physicians, collectively bargained with health insurance plans in order to obtain higher prices or more favorable economic terms in contracts for physician services.

Respondent NTSP is an independent practice association ("IPA") of approximately 500 physicians, the vast majority of whom are specialists who practice in Fort Worth, Texas. NTSP physicians are a significant presence and make up a large percentage of practitioners in many specialties in the Fort Worth area. One of the functions of NTSP is to receive offers from health insurance plans of Health Maintenance Organization ("HMO") or Preferred Provider Organization ("PPO") contracts ("non-risk contracts") to provide physician services in the Fort Worth, Texas area. Upon receipt of a payor offer of a non-risk contract, Respondent evaluates the offer and determines whether to send it -- messenger it -- to its participating physicians. Respondent does not messenger to its physician members any offers on non-risk contracts that fall below minimum rates established by the NTSP Board ("Board minimums"). NTSP establishes Board minimums by conducting polls among its physician members that ask each physician to disclose the minimum price that he or she would accept to provide medical services pursuant to a non-risk contract.

In its defense, Respondent asserts that it did not negotiate economic terms of non-risk contracts. Respondent further asserts that it is entirely proper for Respondent to determine whether or not to send contract offers it receives from health care members to the physicians who participate in NTSP.

## Initial Decision

The government proved its case. As explained in detail in the findings of fact and analysis below, the evidence establishes that physicians participating in NTSP, who are otherwise competitors of each other, communicated to NTSP the minimum prices that they were willing to accept for physician services and that NTSP used this information to negotiate higher rates and more favorable terms for non-risk contracts than those initially offered by various health insurance plans. Through the use of price information collected from its physician members to leverage increased offers or better terms from health insurance payors, NTSP has engaged in a combination, contract, or conspiracy that has unreasonably restrained trade. Accordingly, Complaint Counsel has demonstrated a violation of Section 5 of the FTC Act. The appropriate remedy is an order to cease and desist.

**B. Summary of Complaint and Answer**

The FTC issued its Complaint in this matter on September 16, 2003. The Complaint charges that Respondent, acting as a combination of competing physicians, has restrained competition by negotiating and entering into agreements among its participating physicians on price; refusing or threatening to refuse to deal with payors except on collectively agreed upon terms; negotiating fees in payor contracts for NTSP's participating physicians; and refusing to submit payor offers to participating physicians unless and until price and other competitively significant terms conforming to NTSP's contract standards have been negotiated. Complaint P 12. The Complaint further alleges that the acts of Respondent have had the effect of restraining trade unreasonably and hindering competition in the provision of physician services in the Fort Worth area in the following ways: price and other forms of competition among NTSP's participating physicians were unreasonably restrained; prices for physician services were increased; and health plans, employers, and individual consumers were deprived of the benefits of competition. Complaint P 23. The Complaint charges that the combination, conspiracy, acts and practices alleged in the Complaint constitute unfair methods of competition in or affecting commerce in violation of Section 5 of the Federal Trade

Initial Decision

Commission Act, as amended, 5 U. § 45. Complaint P 24.

In its Answer, filed on October 7 2003, Respondent denied the material allegations of the Complaint and asserted the following defenses: that it is a memberless non-profit corporation and therefore is not subject to the jurisdiction of the Federal Trade Commission; that NTSP' conduct does not constitute commerce as defined in the Federal Trade Commission Act; that NTSP has the right as an entity under *United States v. Colgate Co.*, 250 U. S. 300, 307 (1919) to refuse to become a party to another's contract or transaction; and that NTSP's conduct has been fair, reasonable, and justified. Answer p. 3.

### **C. Procedural Background**

On March 2, 2004, Complaint Counsel filed a Motion for Partial Summary Decision. Also on March 2, 2004, Respondent filed a Motion for Summary Decision. Respondent's motion was denied by Order dated April 9, 2004. Complaint Counsel's motion was denied by Order dated April 14, 2004. Both motions were denied on the ground that genuine issues of material fact raised by the pleadings could only be properly determined after an evidentiary hearing.

The final prehearing conference was held in Fort Worth, Texas on April 27, 2004. Trial commenced immediately following the prehearing conference. Nearly 1 500 exhibits were admitted and 17 witnesses testified, either live or by videotape. Trial concluded on May 25 2004.

On June 16 2004, both parties filed proposed findings of fact, post trial briefs, and conclusions of law. Complaint Counsel filed its response to Respondent's brief and proposed findings of fact on June 30, 2004, and filed a corrected response to Respondent's proposed findings of fact on July 1, 2004. Respondent filed its response to Complaint Counsel's brief and proposed findings of fact on June 30, 2004. Closing arguments were heard on July 21 2004.

The hearing record was closed pursuant to Commission Rule 3.44(c) by Order dated June 2004. Rule 3. 51(a) of the

## Initial Decision

Commission's Rules of Practice states that an Initial Decision shall be filed "within ninety (90) days after closing the hearing record pursuant to § 3.44(c) . . . or within such further time as the Commission may by order allow upon written request from the Administrative Law Judge." 16 C.F.R. § 3.51(a). Ninety days from the close of the record was September 7, 2004. By Certification for Extension of Time to File Initial Decision dated August 25, 2004, the Commission was requested to extend the time for filing this Initial Decision by sixty days, until November 8, 2004. By Order dated September 17 2004, the Commission granted this request and extended the date for filing the Initial Decision until November 8, 2004.

Rule 3.51(a) also states that an Initial Decision shall be filed within one year "after the issuance of the administrative complaint, except that the Administrative Law Judge may, upon a finding of extraordinary circumstances, extend the one-year deadline for a period of up to sixty (60) days." 16 C.F.R. § 3.51 (a). The Complaint in this matter was issued on September 16 2003. One year from the issuance of the Complaint was September 16, 2004. By Order dated September 14, 2004, extraordinary circumstances were found to extend the one-year deadline for a period of up to sixty days, until November 15 2004.

**D. Evidence**

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

Under the Commission's Rules of Practice, a party or a non-party may file a motion seeking in camera treatment for material, or portions thereof; offered into evidence. 16 C. § 3.45(b). The Administrative Law Judge may order that such material be placed in camera only after finding that its public disclosure will likely result in a clearly defined, serious injury to the entity requesting in camera treatment. 16 C.F.R. § 3.45(b). Pursuant to

Initial Decision

Commission Rule 3.45(b), several orders were issued granting in camera treatment to material that met the Commission's strict standard. In addition, when the parties sought to elicit testimony at trial that revealed information that had been granted in camera treatment, the hearing went into an in camera session.

In instances where a document or certain trial testimony has been given in camera treatment, but the portion of the material cited to in this Initial Decision does not rise to the level necessary for in camera treatment, such material is disclosed in the public version of this Initial Decision, pursuant to Commission Rule 3.45(a) (the AU "may disclose such in camera material to the extent necessary for the proper disposition of the proceeding"). In camera material that is used in this Initial Decision is indicated in bold font and braces ("[Redacted]") in the in camera version; it is redacted from the public version of the Initial Decision, in accordance with 16 C.F.R. § 3.45(f).

This Initial Decision addresses only material issues of fact and law. Proposed findings of fact not included in this Initial Decision were rejected, either because they were not supported by the evidence or because they were not dispositive or material to the determination of the allegations of the Complaint or the defenses thereto. The Commission has held that Administrative Law Judges are not required to discuss the testimony of each witness or all exhibits that are presented during the administrative adjudication. *In re Amrep Corp.*, 102 F.T.C. 1362, 1670 (1983). Further, administrative adjudicators are "not required to make subordinate findings on every collateral contention advanced, but only upon those issues of fact, law, or discretion which are 'material.'" *Minneapolis St. Louis Ry. Co. v. United States*, 361 U.S. 173, 193-94 (1959).

## **II. FINDINGS OF FACT**

### **A. Background**

#### **1. Organization of and contracting by physician practices**

1. Physicians often organize their practices into medical

## Initial Decision

groups, which operate as single integrated entities having a single CEO, accountant, office manager, and staff. (Casalino, Tr. 2795-96).

2. Physicians and medical groups often contract with health plans in order to increase the volume of patients available to them. (Frech, Tr. 1288-89).

3. Competing physicians and medical groups sometimes enter into arrangements with others to form independent practice associations, known as IP As. IP As are looser combinations of medical groups formed for the purpose of negotiating contracts with managed care health plans. (Casalino, Tr. 2796; Frech, Tr. 1292).

4. IP As generally lack direct authority to control the practices of their member physicians. (Casalino, Tr. 2799-2800).

## **2. Health care insurance and managed care**

5. Historically, most health care insurance coverage was indemnity insurance. The prevalence of indemnity insurance skewed incentives in such a way that consumers often neither sought to reduce price by seeking lower-priced providers, nor quantity by seeking to avoid over-utilization. (Frech, Tr. 1282-83).

6. Managed care was introduced to address these deficiencies and control the cost of health care services through health plan contracting with physicians, control of utilization, and management of care. (Frech, Tr. 1282-84, 1289).

7. One form of managed care is the Health Maintenance Organization ("HMO"). HMOs generally feature small provider panels, low co-payments for patients, and broad administrative controls to limit utilization, with no coverage for patients who choose providers outside the network. (Frech, Tr. 1283-84).

8. HMO contracts can involve a variety of physician compensation structures. In some instances, participating physicians are paid a stated fee for each service rendered. This compensation structure is referred to as fee- for-service. (Mosley, Tr. 131-32).



Initial Decision

9. A less tightly controlled form of managed care is the Preferred Provider Organization ("PPO"). Relative to HMOs, PPOs generally involve fewer administrative controls and higher patient co-payments to limit utilization, but larger physician panels and greater access to out-of-network physicians, albeit at a reduced rate of reimbursement. (Frech, Tr. 1283- 84).

10. The Medicare RBRVS fee schedule is Medicare's Resource Based Relative Value System ("RBRVS"), a system developed by the United States Centers for Medicare and Medicaid Services to determine the amount to pay physicians for each service rendered to Medicare patients. (Frech, Tr. 1286; Wilensky, Tr. 2144).

11. Health plans that contract with physicians on a fee- for- service basis often do so based on a stated percentage of the Medicare RBRVS fee schedule, which provides reimbursement rates for a large number of specific procedures. (Frech, Tr. 1286; Mosley, Tr. 137; Grizzle, Tr. 692-93).

12. The Medicare RBRVS establishes weighted values for each medical procedure, such that the application of a percentage multiplier (such as 100% for Medicare itself), enables one to determine the fees for thousands of different services simultaneously. (Frech, Tr. 1286).

### **3. Distinction between risk and non-risk agreements**

13. In a risk sharing agreement ("risk contract"), sometimes referred to as a capitation agreement, physicians participating in an HMO are paid (or share) a set dollar amount stated per member, per month, irrespective of the quantity of services rendered. (Frech, Tr. 1293; Mosley, Tr. 131-32; Wilensky, Tr. 2177-78).

14. Capitation agreements shift the risk of overutilization of medical services to the capitated physician or physician group. (Quirk, Tr. 255; Mosley, Tr. 206; Lovelady, Tr. 2638). Physicians respond to capitation and other incentive systems by modifying their utilization and other practice patterns. (Frech, Tr. 1293-94; Casalino, Tr. 2811; Lovelady, Tr. 2640-41).

Initial Decision

15. In a non-risk sharing agreement ("non-risk contract"), physicians are paid under a fee-for-service reimbursement arrangement. (CX 1177 (Grant, Dep. at 78); CX 1198 (Vance Dep. at 36)). In fee-for-service arrangements, physicians do not bear the risk of overutilization of physician services because payments are made for the services provided. (Frech, Tr. 1346-47).

16. PPOs generally utilize non-risk sharing agreements where the insurance company contracts to reimburse providers at a predetermined level for services performed by the physicians. (Mosley, Tr. 134).

## **B. North Texas Specialty Physicians**

### **1. Organization and composition**

17. NTSP is an IPA located in Fort Worth, Texas. (CX 311 at I; CX 1196 (Van Wagner 08. 29. 02 IHT at 8)). It is a nonprofit corporation organized, existing, and doing business under and by virtue of the laws of Texas, with its office and principal place of business at 1701 River Run Road, Suite 210, Fort Worth, Texas, 76107. (Complaint P 1; Answer P 1; RX 1674 (NTSP fact sheet)).

18. NTSP does not function as a clinically integrated organization for patients seen under non-risk contracts. (Casalino, Tr. 2877).

19. NTSP was formed in 1995 under section 5. 01(a) of the Texas Medical Practice Act which allows nonprofit entities to engage in the practice of medicine for the purposes of research medical education, or the delivery of health care to the public. (Van Wagner, Tr. 1489-90; RX 1674; RX 1675; RX 1676).

20. NTSP carries on business for the pecuniary benefit of its member physicians. (CX 311 at 10-11 and CX 275 at 30-31 ("NTSP shall use its best efforts to market itself and its Participating Physicians to Payors and to solicit Payor offers for the provision of Covered Services by Participating Physicians"); CX 310 (stating that NTSP physician's ability to negotiate

Initial Decision

"substantially improved" by NTSP; noting NTSP's discussions with payors" should lead to contracts that are more favorable than we would be able to achieve individually or through other contracting entities"); CX 159 at 2 (noting contractual issues addressed by NTSP include "maintaining minimal reimbursement standards for its member physicians").

21. NTSP, as an organization, receives its revenue from risk contracts and a one time fee of \$ 1,000 from each physician. (Van Wagner, 'Ir. 1552).

22. From January 1 1999 to December 22, 2003, NTSP purchased \$ 1,047,819.86 from vendors with billing addresses outside of Texas. (CX 1203; CX 1195 (Van Wagner, 01.20. Dep. at 77)). For example, NTSP purchased \$ 457,373.09 of stop loss insurance from McPhee & Associates, a California insurance broker. (CX 1203; CX 1195 (Van Wagner, 01.20. 04 Dep. at 81)).

23. NTSP's Board of Directors ("Board") is made up of eight physicians. Under NTSP' organizational documents and under Texas law, NTSP's directors, other than an "Officer Director" must be physicians who are actively engaged in the practice of medicine. (CX 275 at 7; Van Wagner, Tr. 1493-94; see also TEX. OCC. CODE ANN. § 162. 001 (Vernon 2004)).

24. The Board of Directors is elected from among NTSP's member physicians and meets once a week. (Van Wagner, Tr. 1493-94).

25. NTSP has a salaried, core administrative staff of eight people, including executive director Karen Van Wagner, provider relations staff, provider sponsored network ("PSN" development and contracting staff, data processing staff, credentialing staff; and clerical support staff. (Van Wagner, Tr. 1494-95; RX 1674).

26. NTSP's Medical Executive Committee includes the chairs of each of NTSP's specialty divisions who are elected by the member physicians within each specialty. (Deas, Tr. 2559-60; CX 275 at 5).

## Initial Decision

27. Karen Van Wagner, Ph.D. is NTSP's executive director. Van Wagner joined NTSP in 1997, roughly a year after the organization was established. (Van Wagner, Tr. 1461-62).

28. Dr. Thomas Deas is the current president and chairman of the Board of NTSP. In addition to heading the Medical Executive Committee, Deas is a medical director of NTSP. (Deas, Tr. 2524, 2556).

29. Dr. William Vance was one of the founding members of NTSP, serving as its president from 1996 until 2001. Vance was a member of the Medical Management Committee from its inception through 2002. In addition, he was the chairman of NTSP's cardiology section. His role within NTSP ceased when his practice group, Consultants in Cardiology, withdrew from NTSP in April 2002. (CX 1198 (Vance, Dep. at 9, 48, 49)).

30. Dr. John Johnson, II is a medical physician and a current member of NTSP's Board of Directors. (CX 1182 (Johnson, Dep. at 6, 13)).

## 2. Member physicians

31. NTSP has member physicians in eight counties in and around the Dallas/Fort Worth Metroplex. (Van Wagner, Tr. 1468-69). Approximately 85-88% of NTSP's member physicians are located in Tarrant County, with the majority located in Fort Worth. (Van Wagner, Tr. 1471; CX 1196 (Van Wagner, 08.29. 02 IHT at 15- 16)).

32. At the time of trial (April 2004), NTSP had approximately 480 participating physicians. (Van Wagner, Tr. 1510, 1518). In 2003, NTSP had approximately 575 participating physicians, practicing in 26 different specialties, who had signed NTSP's Physician Participation Agreement ("PPA"). (CX 311 (physician participation agreement); RX 3118 (Maness Report PP 4, 19)). In 2001, NTSP had as many as 652 physicians. (CX 209 at 2 ("NTSP has become a 'gorilla network' with approximately 124 PCP's [primary care physicians] . . . and 528 specialists.")).

Initial Decision

33. NTSP member physicians attend general membership meetings, pay dues, and elect NTSP's Board. (CX 1178 (Hollander, Dep. at 21- 34)).

34. NTSP member physicians are organized into specialty divisions, based on field of practice. (Van Wagner, Tr. 1510).

35. NTSP's member physicians have distinct economic interests, reflecting their separate clinical practices. (CX 1182 (Johnson, Dep. at 21); see also CX 524 (roster of NTSP member physicians listing multiple physicians and/or physician groups practicing the same specialty in Fort Worth)).

36. Many NTSP physicians and physician practices are in competition with one another. (CX 1182 (Johnson, Dep. at 21) ("We compete for patients. We compete at the different hospitals at which we work."); CX 550 (noting that NTSP's disagreements with payors were supported by its membership despite the fact that "short term advantage and perceived best interest are always controversial and potentially divisive, weakening the strength that our numbers provide.")).

### **3. Overview of NTSP's functions**

37. NTSP was founded in 1995 to allow a group of specialist physicians to accept economic risk on medical contracts and to participate in the medical decision-making process. NTSP has since broadened its activities to include entering into and messengering non-risk contracts and has expanded its membership to include primary care physicians ("PCPs"). (RX 1675; Vance, Tr. 587- 88; Wilensky, Tr. 2158-59).

38. The Board manages the organization, determines NTSP's minimum contract prices and evaluates contract offers. If a payor offer is at or above Board minimum rates (infra F. 83-90) and is otherwise acceptable, NTSP will messenger the offer to its member physicians. (CX 275 at 5; Van Wagner, Tr. 1642-43; Vance, Tr. 595-96; CX 1177 (Grant, Dep. at 22-24); CX 1174 (Deas, Dep. at 42)).

39. NTSP represents its member physicians and provides administrative expertise to review contracts, confront timely

## Initial Decision

payment issues, and lobby government agencies for physician issues. NTSP has evolved into a forum for its member physicians to cooperate and discuss the general and specific business of medicine and receive advice and information. (CX 350).

40. NTSP's Medical Executive Committee transmits information and feedback including the status of fee-for-service contract discussions, between NTSP's staff and Board and the membership. (CX 1174 (Deas, Dep. at 20-21); Deas, Tr. 2560).

41. NTSP communicates with its member physicians by sending faxes called "Fax Alerts" which keep its member physicians informed of the activities of NTSP, including contractual issues. (CX 1178 (Hollander, Dep. at 48); CX 1198 (Vance, Dep. at 54)).

42. NTSP holds "general membership meetings" to provide contracting updates for specific payor negotiations and to discuss and share NTSP's poll results with the membership. (CX 1178 (Hollander, Dep. at 21-23); CX 182; CX 183; CX 184; CX 186; CX 187).

#### **4. Contracts with health insurance providers**

43. NTSP "is in the business of contracting with health maintenance organizations health care networks and other payors to provide health care services through physicians and physician groups who have contracted with NTSP to provide health care services. (CX 311 at 1 (WHEREAS Recital of NTSP PPA)).

44. One of NTSP's functions is to negotiate reimbursement terms in contracts with health plans on behalf of NTSP's member physicians. (CX 159 at 2 ("Contracting issues addressed by NTSP this past year included . . . maintaining minimal reimbursement standards for its physicians."); CX 350 ("NTSP was started in an attempt to provide a seat at the table of medical business for the individual specialty physicians. . . . NTSP, through PPO and risk contracts, has provided a consistent premium fee-for-service reimbursement to the members when compared with any other contracting source."); CX 1182 (Johnson, Dep. at 10- 11) ("NTSP was going to be a group of physicians that would bring a voice to

Initial Decision

organizing physicians who often practiced in individual groups to hopefully be able to secure contracts, improve patient care, and provide a voice at the table for physicians. . . . [It was] to represent physicians . . . in obtaining contracts from businesses or insurance companies or in dealing with hospitals.")).

45. NTSP analyzes contract language from both operational and legal perspectives communicating with payors about the terms of the contract, determining the payor's payment policies and timing, mailing contracts to participating physicians, determining when physicians accept a given contract, and establishing and updating systems to track physician and plan member participation in a given contract. (Van Wagner, Tr. 1648-49; Wilensky, Tr. 2195-96; RX 3118 (Maness Report P 76); CX 1196 (Van Wagner, 08.29. 02 IHT at 56-57)). This review benefits physicians. (CX 1182 (Johnson, Dep. at 11) ("As a busy physician, I had relatively little time to look at contracts, and oftentimes did not understand the legal language in contracts, so having another organization that could review contracts and educate me as to the terms in the contracts" was a benefit.)).

46. NTSP originally focused on negotiating shared-risk contracting with health plans, but as the market moved away from risk-sharing arrangements, NTSP increasingly sought to negotiate and did negotiate non-risk contracts. (CX 195).

47. In 2001, NTSP accepted risk on only approximately 32 000 lives. (CX 616 at 2 (NTSP takes professional risk on approximately 20 000 commercial and 12 000 Medicare lives)).

48. In March 2001, NTSP's Board of Directors stated that "risk business is a small part of the business" and concluded that NTSP's "focus should center on how to benefit members on fee-for-service contracts as well." (CX 83 at 3).

49. NTSP has one risk-sharing contract -- the one it shares with PacifiCare. (CX 1177 (Grant, Dep. at 19)). Within the past five years, NTSP also had a risk contract with AmCare. (CX 1196 (Van Wagner, 08.29. 02 IHT at 14); CX 1195 (Van Wagner, 01.20. 04 Dep. at 15)).

## Initial Decision

50. NTSP has approximately twenty fee-for-service contracts, covering many more lives. (CX 1196 (Van Wagner, 08. 29. 02 IHT at 14); see also CX 265 in camera (listing, by health plan, lives covered under NTSP's non-risk contracts)).

51. Sixty percent of NTSP's physicians participate in fee-for-service contracts. Roughly half of those physicians participate in risk-sharing contracts. Some of these physicians participate in NTSP through a participation agreement under which they can gain access to NTSP's non-risk contracts, but are not eligible to participate in NTSP's risk contract. (CX 616 at 12; CX 1197 (Van Wagner, 08. 30. 02 IHT at 182, 228-29); Van Wagner, Tr. 1830; CX 1194 (Van Wagner, 11.9. 03 Dep. at 37-38)).

**C. Relevant Market**

52. In contracting for health plan services, Fort Worth employers demand significant coverage by physicians who practice in the Fort Worth area and who admit patients to Fort Worth hospitals. (Grizzle, Tr. 688-89, 722; Frech, TL 1304-05; Mosley, Tr. 141-42; Quirk, Tr. 276- 280; Jagmin, Tr. 1104-07).

53. To be competitively marketable to Fort Worth area employers, health plans must include many physicians who practice in a variety of fields in the Fort Worth area. (Grizzle, Tr. 688-89, 720, 722; Jagmin, Tr. 1104-07).

54. When buying health coverage, employers look for networks that include all of the tertiary care hospitals in an area, most of the other hospitals within the area, and a broad selection of physicians in the locale, including a wide selection of specialists within each specialty. (Jagmin, Tr. 971- 1102-03; Quirk, Tr. 270-72, 275-76).

55. Health plans try to assemble and market a panel of physicians that will satisfy employers' preferences for greater access to a wide array of conveniently located physicians without compromising the overall cost of care. (Quirk, Tr. 270-72; Jagmin, Tr. 972).



Initial Decision

56. Fort Worth employers typically would consider a network adequate if it had physicians within ten miles of at least 85%, and preferably 90%, of its employees. (Mosley, Tr. 141-42).

57. NTSP physicians agree that Fort Worth specialists are better able to address the needs of patients (and primary care physicians) located in Fort Worth than physicians located elsewhere. (E.g., CX 583 at 1-2 (Johnson, an NTSP member physician, writing: "obviously a provider network whose business is based entirely here in Fort Worth is better positioned to address the needs of both patients and physicians.") (emphasis in original). See also CX 1187 (McCallum, Dep. at 59) (NTSP Board member testifying that Dallas physicians compete in a different market than NTSP physicians)).

58. A large network of physicians located in Dallas or in We Mid-Cities, defined as the areas including Arlington, Hurst, Euless, Bedford, Colleyville, and Southlake (CX 1196 (Van Wagner, 08.29.02 IHT at 16), would not be marketable to Fort Worth employers if the network did not also have a large number of appropriate physicians located in Fort Worth. (Mosley, Tr. 142-43; Jagmin, Tr. 1103-04; Quirk, Tr. 280-82).

59. A network of physicians located in Dallas or the Mid-Cities that did not also have a large number of appropriate physicians located in Fort Worth would not achieve the geographic access required by employers with large numbers of Fort Worth employees and would not be acceptable to employers, even if they were discounted by five or ten percent, relative to those areas. (Mosley, Tr. 142-43; Quirk, Tr. 279-80).

60. If all Fort Worth physicians increased prices by five percent, health plans serving Fort Worth employers would not be able to avoid the price increase by substituting away from Fort Worth. (Grizzle, Tr. 723; Quirk Tr. 280-82; Jagmin, Tr. 1103-04).

61. NTSP physicians are a significant presence in the Fort Worth area. NTSP physicians make up a large percentage of Tarrant County practitioners in several medical specialties: 80% for pulmonary disease, 68.6% for urology, and 58.8% for cardiovascular disease. (Frech, Tr. 1299). Tarrant County includes

## Initial Decision

Fort Worth and several surrounding cities. (Quirk, Tr. 420; Maness, Tr. 1992).

62. A loss of NTSP's physicians from a health plan's network would have "a very deleterious affect" on the health plan's ability to market its product in Tarrant County. (Jagmin Tr. 1091). One health insurance plan's representative testified that, without NTSP's physicians it would suffer from significant holes in coverage for a number of specialties in Fort Worth. ([Redacted], in camera).

63. NTSP has stated that a health plan attempting to serve the employees of the City of Fort Worth "would not be able to satisfy employer/employee match or network access standards without NTSP Physicians Participating in the Network" and that, "NTSP is the only stable physician organization left in the Tarrant County market." (CX 1042. See also CX 576 at 3 (NTSP stating that "without NTSP specialists in the Aetna network, a severe network inadequacy problem will exist in Fort Worth.")).

#### **D. Contract, Combination, or Conspiracy**

##### **1. Physician Participation Agreement**

64. NTSP and its participating physicians enter into the Physician Participation Agreement ("PPA"), establishing their relationship. (CX 276 at 1).

65. The PP A grants NTSP the right to receive all payor offers and imposes on the participating physicians a duty to promptly forward those offers to NTSP. (CX 276 (Fax Alert stating that NTSP shall have "exclusive right, on behalf of its members, to receive all payor offers"); CX 275 at 24 ("NTSP shall have the right to receive all Payor Offers made to NTSP or Physician . . . If Physician receives a Payor Offer, . . . Physician will promptly forward such Payor Offer to NTSP for further handling in accordance with the provisions of this Agreement.")).

66. The PP A grants NTSP a right of first negotiation with payors, with each physician agreeing that he or she will refrain from pursuing offers from a health plan until NTSP notifies them

Initial Decision

that NTSP is permanently discontinuing negotiations with the health plan. (CX 275 at 2; CX 276; CX 311 at 8; Deas, Tr. 2405-06; CX 1178 (Hollander, Dep. at 68) ("And there were various criteria like time limits that the participating physician[s] generally agreed that they would just wait and after that time limit was expired, then they were free to negotiate on their own.")).

67. With respect to "Non Risk Payor Offers" the PP A states:

promptly after receiving any Non Risk Payor Offer, NTSP shall deliver to Physician and each other Participating Physician the Fee Schedule and other economic provisions of the Non Risk Payor Offer. Physician shall have ten (10) business days within which to accept or reject such Fee Schedule and economic provisions, with the understanding that if Physician fails so to accept or reject within such 10-day period, Physician shall be deemed to have accepted such Fee Schedule and economic provisions.

If the Participating Physicians who approve and who are deemed to have approved the Non Risk Payor Offer constitute 50% or more of all Participating Physicians, then NTSP, on behalf of Physician, shall notify the Payor of the acceptance and proceed with negotiation and execution of a Payor Agreement.

If 50% or more of the Participating Physicians request that NTSP submit a counter-proposal to the applicable Payor, then NTSP shall submit the counter-proposal to such Payor. If the counter-proposal is accepted, then NTSP, on behalf and as agent of Physician, shall proceed with negotiation and execution of a Payor Agreement with respect to such counter-proposed offer.

If the counter-proposal is not accepted by the Payor but the Payor submits its own counter-proposal, then

## Initial Decision

such counter-proposal shall be treated as a new payor offer and will be submitted to Participating Physicians in accordance with the preceding provisions.

(CX 275 at 25-26).

68. Although under the PP A, NTSP is obligated to deliver to each physician the fee schedule and other economic provisions of a non-risk payor offer (CX 275), NTSP delivered only those offers which were approved by NTSP and which met minimum levels established by the Board, as determined by the results of a poll. (Van Wagner, Tr. 1706; CX 1196 (Van Wagner, 08. 29. 02 II-IT at 29-30) (the Board does not send to physicians offers below the minimal acceptable level as determined by the results of a poll.)).

69. With respect to "Payor Offers Rejected by NTSP," the PPA states:

If NTSP rejects any Payor Offer and advises the Participating Physicians in writing that it is permanently discontinuing negotiations or if the Participating Physicians who approved and who are deemed to have approved a Non Risk Payor Offer constitute less than 50% of all Participating Physicians, then NTSP shall have no further responsibilities with respect thereto and any Participating Physician shall have the right to pursue such Payor Offer on its own behalf.

(CX 275 at 26).

70. NTSP has urged its member physicians to avoid undermining NTSP's role in negotiating contracts on behalf of its member physicians. (E.g., CX 550 (Vance's "Open Letter to the Membership": "We must continue to move forward as a group or we will surely falter as individuals"); CX 380 at 3 (NTSP warning its physicians that physician fees will decline unless "NTSP or someone can provide a unifying voice for physicians"); CX 400 at

Initial Decision

2 (NTSP warning its member physicians that without their support "it is likely NTSP will not be around the next time Aetna, Cigna, or United come to town" with unsatisfactory rate proposals.)).

71. NTSP cannot and does not bind any member physician or physician group to non-risk contracts. (Frech, Tr. 1362-64; Van Wagner, Tr. 1637, 1777).

72. NTSP's member physicians can and do contract with health plans outside of NTSP either directly, through financially integrated physician groups, or through other IP As. (Quirk Tr. 288- 89; Van Wagner, Tr. 1564, 1637; Deas, Tr. 2432).

73. There are no agreements between one or more NTSP member physicians to not participate in or to reject a non-risk payor offer. (Frech, Tr. 1365; Maness, Tr. 2048).

74. NTSP's member physicians and physician groups do not consult with each other when making decisions on non-risk payor contracts. (Maness, Tr. 2049-50).

75. NTSP's member physicians and physician groups do not know what any other physician or physician group will do in response to a non-risk payor offer. (Frech, Tr. 1436-37; Maness, Tr. 2044-46; Deas, Tr. 2423).

## **2. Power of attorney forms**

76. In the process of negotiations with United Healthcare ("United") and with Aetna Health, Inc. ("Aetna"), NTSP has solicited and obtained power of attorney forms from its member physicians, giving NTSP the legal authority to negotiate non-risk contracts on behalf of those member physicians. (CX 1173 (Deas IHT at 56-57); Palmisano, Tr. 1250-51. E.g., 347 at 2; CX 1061 at 1).

77. The power of attorney forms that NTSP provided to its physicians with respect to contract negotiations with United and Aetna state:

The undersigned . . . appoints, with full power of substitution North Texas Specialty Physicians . . . as

## Initial Decision

attorney-in- fact to act for me in any lawful way with respect to all contracts and agreements (including without limitation all prospective contracts or agreements) with and/or involving the undersigned and . . . [United Health Care / Aetna].

This power of attorney grants to the agent the authority to act on the undersigned's behalf regarding the foregoing described agreements in all respects, including the authority to negotiate the terms of, enter into, execute, amend, modify, extend or terminate any such agreements.

(CX 1061-1103 (United); CX 347-404 (Aetna)).

78. In distributing the power of attorney forms to its member physicians, NTSP has instructed its physicians to inform health care payors' representatives that NTSP is his or her contracting agent and to instruct the health care payor to contact NTSP with respect to contracting activity. (CX 1066 (United); CX 548 (Aetna)).

79. NTSP also includes in power of attorney solicitations information about the number of physicians who already have executed the power of attorney forms. (CX 1066 ("Thus far, NTSP has received 107 signed documents from NTSP member physicians assigning NTSP power of attorney to act on their behalf in regard to all contracting activity between themselves and United Healthcare."); CX 548 (NTSP sent 180 power of attorney authorizations in regard to Aetna HMO and PPO commercial products)).

80. With respect to negotiating with Cigna Healthcare ("Cigna"), NTSP requested its member physicians to sign an "authorization form" to allow NTSP to serve as its physicians' agent. (CX 332).

81. NTSP physicians have referred health plans that sought to contract directly with them back to NTSP, at times noting that the deferral was based on agency or power of attorney held by NTSP. (Beaty, Tr. 454-60; Grizzle, Tr. 696-98, 701, 709; CX 760

Initial Decision

(exhibit admitted as an exception to the hearsay rule for verbal acts and not for the truth of the matter asserted therein ["limited admission"]). See also CX 1178 (Hollander, Dep. at 116) ("If an NTSP physician had signed an agency agreement specifying that NTSP was to be their exclusive agent in connection with these contracts, then my understanding was that [the payor] had to deal with NTSP and not with the individual physician himself.").

82. NTSP has advised health plans during rate negotiations for fee-for-service contracts and at other times that it represented NTSP member physicians, through power of attorney forms, (Roberts, Tr. 540-41), or otherwise (CX 760 (limited admission) (letters from NTSP physicians to Cigna citing NTSP as their contracting "agent")); Beaty, Tr. 454-60).

### **3. Board minimums**

83. "Board minimums" are the minimal acceptable rates for NTSP to enter into non-risk contracts with health plans. (Van Wagner, Tr. 1921; Frech, Tr. 1324). Payor offers falling below Board minimums are rejected by NTSP. (Frech, Tr. 1324. E.g., F. 127, 154, 300, 341).

84. NTSP establishes Board minimum prices for use in negotiating non-risk contracts with health plans. (Van Wagner, Tr. 1642-43; Frech, Tr. 1321; e.g., CX 274 (Fax Alert stating: NTSP "utilizes these minimums when negotiating managed care contracts on behalf of its participants.")).

85. Board minimums are also used by NTSP to predict when the participation rate of NTSP's member physicians will be high enough for NTSP to messenger an offer to its member physicians. (Deas, Tr. 2433; Maness, Tr. 2079-80). Multiple times over several years, NTSP has informed health plans that its physicians have established minimum fees for NTSP-payor agreements and that NTSP will not forward to its member physicians, or enter into a contract, based on payor offers that do not satisfy those fee minimums. (Van Wagner, Tr. 1822-24; CX 1196 (Van Wagner, 08.29.02 IHT at 63, 154)).

## Initial Decision

86. Board minimums may have been utilized as early as 1997. (CX 1042 (2001 Fax Alert from NTSP to its member physicians stating "NTSP board minimums have remained constant for four years.")). NTSP conducted its first poll in either 1998 or 1999. (CX 1194 (Van Wagner, 11.19.03 Dep. at 86-87)).

87. NTSP conducts polls to determine minimum reimbursement rates for use in negotiation of non-risk contracts with health plans. (Van Wagner, Tr. 1639 ("We contact our physicians and we ask them to respond to a . . . survey on . . . what they believe are acceptable fees that they want to see in the nonrisk contracts."); CX 1196 (Van Wagner, 8.29.02 IHT at 27 ("Every year the Board asks the members to tell them what they consider to be appropriate reimbursement. . . . Once a year we poll the members and get that information from them.")); e.g., CX 565).

88. NTSP's polling form explains to the member physicians that each year, "NTSP polls its affiliates and membership to establish Contracted Minimums. NTSP then utilizes these minimums when negotiating managed care contracts on behalf of its participants." (CX 387 at 1; CX 633).

89. NTSP's polling form asks each physician to disclose the minimum price that he or she would accept for the provision of medical services pursuant to a fee-for-service HMO or PPO agreement. (CX 565; CX 1196 (Van Wagner, 08.29.02 IHT at 27)).

90. NTSP's member physicians are asked to indicate their price selection by placing a check mark next to one of several pre-printed Medicare RBRVS ranges. (CX 274; CX 565; CX 633).

91. By quoting a particular percentage of RBRVS, one can establish the prices for thousands of different services simultaneously. By using the Medicare index and a percentage of Medicare as a conversion factor, voluminous price information is reduced to a single dimension. (Frech, Tr. 1287).

92. NTSP's member physicians and physician groups do not consult with each other when responding to the poll. (Maness, Tr. 2049-50; Lonergan, Tr. 2718).



Initial Decision

93. After receiving the poll responses, NTSP calculates the mean, median, and mode ("averages") of the minimum acceptable fees identified by its physicians and establishes its minimum contract prices. (Van Wagner, Tr. 1640; CX 103; CX 387).

94. NTSP informs its physicians of the average poll results and NTSP's minimum contract prices based thereon. (Van Wagner, Tr. 1644. E.g., CX 393, CX 430, CX 1042).

95. NTSP physicians are informed only of the mean, median, and mode of the poll responses. They do not know how any other specific physician or physician group responded to the polls. (Van Wagner, Tr. 1641-44; Frech, Tr. 1436-37; Maness, Tr. 2044-46; Deas, Tr. 2423).

96. On October 15, 2001, the NTSP Board received annual poll results. Based on the poll results, NTSP established minimum prices of 125% of 2001 Medicare RBRVS for HMO products and 140% of 2001 Medicare RBRVS for PPO products as minimally acceptable fee schedules for health plan contracts. (CX 103 at 4; CX 389).

97. On November 11, 2002, NTSP conducted another annual poll to determine minimum reimbursement rates for use in negotiation of HMO and PPO products and anesthesia contracts with health plans. On its polling form sent to physicians, NTSP included the prior year's poll results, reported by mean, median, and mode. (CX 430).

98. The results of the 2002 annual poll by mean, median, and mode, for HMO were 131%, 135%, and 135%; for PPO, 146%, 145%, and 145%. NTSP reported these figures to its member physicians and stated that the "poll's objective is to identify what reimbursement levels NTSP members deem acceptable." (CX 432).

99. By providing this pricing information to its member physicians, NTSP effectively informs the physicians of the potential reward for entering into a contract with health plans through NTSP, as opposed to entering into a contract with a health plan by directly negotiating with the health plan. (Frech, Tr. 1326).

## Initial Decision

100. Such price information sharing reduces each physician's uncertainty as to the conduct of its competitors in the aggregate. (Frech, Tr. 1327; see also CX 1170 (Blue, Dep. at 33) (poll results provide "a guideline where we saw the numbers, we would like to have these rates, if possible, and it kind of gave you an idea of where the market was. So if I got other communications independently and some . . . [were] paying 80 percent of Medicare, but it looked like a lot of plans were paying 110 percent, then 80 percent of Medicare sounded pretty low.")).

**E. NTSP's Dealings with Several Health Plans****1. United Healthcare Services, Inc.****a. Corporate structure**

101. United Healthcare Services, Inc., is a wholly owned subsidiary of United Healthcare through which United Healthcare offers its PPO and other non-HMO products in Texas. (Quirk, Tr. 234-35, 239, 241, 247-48). United Healthcare of Texas is a wholly owned subsidiary of United Healthcare through which United Healthcare offers its HMO products in Texas. (Quirk, Tr. 235, 247-48). [United Healthcare Services and United Healthcare of Texas are collectively referred to as "United."]

102. United Healthcare is a subsidiary of United Health Group, a publicly traded company. (Quirk, Tr. 248; Wilensky, Tr. 2156). The success or failure of United's Texas entities are reflected in the stock price of United Healthcare. (Quirk, Tr. 248).

103. United contracts with multi-state employers, some of whom are domiciled outside of Texas but have employees in Texas, such as Raytheon and Home Depot. (Quirk, Tr. 253-54).

104. If health care costs rise in the Ft. Worth area, the pricing of the overall package to Raytheon or other national companies would be affected. (Quirk, Tr. 254-55).

Initial Decision

105. Since 1999, Thomas J. Quirk has been the CEO for the North Texas and Oklahoma Region of United Healthcare Services, Inc., and the President, Chairman of the Board and the CEO of United Healthcare of Texas. (Quirk, Tr. 234-36).

106. Quirk oversees all of United's operations for the North Texas and Oklahoma regions, which include sales for commercial employers, municipalities and school districts; account management for United's existing customers and network operations, which encompass contracting with physicians, hospitals, and other provider networks; and maintenance of those relationships. (Quirk, Tr. 235-36).

**b. NTSP's negotiations with United in 1998**

107. In July 1998, NTSP informed its member physicians that United was attempting to standardize its physician agreements by, among other things, changing the fee schedule. (CX 1005 (Fax Alert # 79)).

108. In Fax Alert # 79, NTSP sent its physicians an agency agreement for the purpose of obtaining consent to enter into negotiations. NTSP stated that "because United Healthcare has the potential to be a major payor in this market place, the NTSP Board wishes to contact them and negotiate on behalf of its membership." (CX 1005 at 2).

109. NTSP explained later that it was United's attempt to change fee schedules that prompted NTSP negotiations with United. (CX 1014).

110. NTSP encouraged its member physicians to "refrain from responding to United Healthcare while NTSP's request for agency status [was] being tabulated." (CX 1005 at 2 (capitalization omitted)).

111. Some of NTSP's physicians authorized NTSP to negotiate with United on their behalf. (E.g., CX 1006 (July 15, 1998 letter from Deas of Gastroenterology Associates of North Texas to Van Wagner allowing NTSP to serve as its agent in regard to future negotiations, including price terms, with United and instructing NTSP not to agree to any fee schedules lower than

## Initial Decision

135% of 1997 Medicare RBRVS for United's HMO product and 147% for United's PPO product); Deas, Tr. 2573-77).

112. On August 20, 1998, NTSP requested, and United granted, an extension on the time line for the assignment of contracts. (CX 1008). NTSP informed its member physicians of the extension and instructed them that they did not need to sign or return any documents or contracts to United. (CX 1008).

113. In September 1998, NTSP proposed to United that the Dallas Medicare RBRVS be used in calculating the rates for its HMO and PPO products for NTSP physicians, and informed its member physicians of this proposal in Fax Alert # 94. (CX 1010).

114. NTSP also informed its member physicians in Fax Alert # 94 that "for many specialists, Dallas rates are approximately three to five percent higher than PPO rates applied to Tarrant County." (CX 1010 at 2).

115. On October 27, 1998, in Fax Alert # 101, NTSP informed its member physicians that discussions with United had been productive, that the parties agreed to extend the deadline, and that member physicians need not take any action with regard to standardizing their United contract until this extension expired. (CX 1011).

116. United made an offer to NTSP on a non-risk contract that was below the rates available to NTSP participating physicians through another IPA, Health Texas Provider Network ("HTPN"). (Van Wagner, Tr. 1726-27).

117. HTPN, which is an affiliate IPA of Baylor Health Care System, is an organization of employed as well as independent contracted physicians in Dallas. NTSP and HTPN had an arrangement whereby NTSP member physicians would be allowed to access HTPN's payor offers. NTSP did not participate in discussions with payors regarding economic terms of HTPN contracts. (Van Wagner, Tr. 1559-60; Quirk, Tr. 311-12; RX 1947).

Initial Decision

118. On December 2, 1998, in Fax Alert # 112, NTSP informed its member physicians that NTSP proposed to United that NTSP's physicians contract with United through HTPN. (CX 1012).

119. On March 9, 1999, in Fax Alert # 12, NTSP recommended to its member physicians that they transition their existing contracts into a standard United contract, and assured them that this would have no effect on the reimbursement rates that they were receiving under their current contract. NTSP further informed its member physicians that "we [NTSP] continue our discussions with United Healthcare on proposed fee schedules for these products." (CX 1014).

120. Ultimately, a significant number of NTSP physicians accessed United through the NTSP-HTPN arrangement. (CX 1015).

**c. NTSP's negotiations with United in 2001**

121. Beginning in March 2001, NTSP member physicians contacted NTSP, asking that NTSP seek and obtain a contract with United. (CX 1117 at 1). On March 14, 2001, NTSP expressed to United its "desire for a group contract reflecting today's market." (CX 1117 at 2; Quirk, Tr. 284-89).

122. NTSP targeted United because NTSP believed that United's rates were below market rates. (CX 211 at 3 (NTSP informing its Primary Care Physician Council that they had identified United as a re-negotiating target, noting that United was becoming a significant player in the Fort Worth market and that United's rates were well below market)).

123. NTSP's discussions with United involved fee-for-service contracts. (Quirk, Tr. 291, 293-94).

124. As of March 2001, United had contracts with approximately two-thirds of the NTSP physicians, either directly or through other organizations, such as HTPN. (Quirk, Tr. 288-89). Therefore, United concluded that there was no need to enter into an agreement with NTSP. (Quirk, Tr. 289-90).

## Initial Decision

125. On April 12, 2001, NTSP reported at its Primary Care Council Meeting that the reimbursement rates under the United-HTPN contract - 130% of 1997 St. Anthony RBRVS (145% Radiology) for HMO, 145% of 1997 St. Anthony RBRVS for POS, and 145% of 1997 St. Anthony RBRVS for PPO - were below market. (CX 209 at 3; CX 1015 at 4). A majority of NTSP physicians had accepted this contract in 1999 through NTSP's affiliation with HTPN. (CX 1015 at 1).

126. In or about May 2001, notwithstanding its view that United already had a sufficient network in Fort Worth, United offered to NTSP its then standard rates in the Fort Worth area: 110% of 2001 Dallas RBRVS, which was the equivalent of 115% of 2001 Tarrant County RBRVS, to NTSP. United's offer extended one rate for both HMO and PPO products. (CX 87 at 7; CX 89 at 3; Quirk, Tr. 290, 297-98).

127. NTSP did not messenger the May 2001 offer to its physicians and rejected it for two reasons: (1) it fell below NTSP's Board minimums; and (2) it extended one rate for all products, instead of different rates for HMO and PPO products. (Quirk, Tr. 300-01; CX 87 at 7).

128. On June 19, 2001, a United representative wrote to an NTSP representative, explaining that United's offered rates were identical for HMO and PPO reimbursement because, from the physician's standpoint, each United patient is administratively the same. (CX 1027).

129. On June 25, 2001, the NTSP Board discussed United's rate offer and rejected it. (CX 89 at 3; Quirk, Tr. 300-01).

**d. NTSP's discussions with the City of Fort Worth**

130. In 2001, NTSP physicians provided health care to the majority of employees of the City of Fort Worth and their dependents under NTSP's risk contract with PacifiCare. (Mosley, Tr. 148-49, 203).

131. The City of Fort Worth, in 2001, decided to become self-insured and began accepting bids from payors to become the administrator of its health plan. (Mosley, Tr. 148-49). One of the

Initial Decision

bidders against PacifiCare was United. (Mosley, Tr. 203-05; Van Wagner, Tr. 1743).

132. NTSP learned, in the spring of 2001, that United was negotiating with the City of Fort Worth to provide health care coverage to city employees and their dependents. (CX 89 at 3).

133. NTSP believed that United was threatening to displace an NTSP risk contract. (Mosley, Tr. 206-07; Quirk, Tr. 363-65). If the City of Fort Worth selected United, the effect would be to remove this major employer's patients from NTSP's risk network (PacificCare) and substitute in its place a four-year-old non-risk contract that NTSP had with United through HTPN. (Van Wagner, Tr. 1728-29; CX 1042).

134. NTSP also had concerns about the adequacy of United's network and utilization management for the City's patient population and about United's ability to provide care to the City. (Van Wagner, Tr. 1729-35; Deas, Tr. 2424-25, 2429-30; Mosley, Tr. 185-87; Vance, Tr. 856-57; CX 1031).

135. During its negotiations with United, beginning in June 2001, NTSP encouraged its Board members to contact "any city council members they know to let them know that United's panel is not adequate." (CX 89 at 3).

136. NTSP also urged its primary care physicians to contact the Mayor and city council members to educate them about the situation with United and ask for help. (CX 211 at 3).

137. NTSP, on July 13, 2001, provided to its member physicians model letters for the purpose of contacting city officials. Attached to Fax Alert # 44 was a sample letter to the Mayor of Fort Worth with the fax number for the Mayor and the names, addresses, fax numbers, and email addresses of the members of the city council. The sample letter included the following statements:

Many of my patients are city employees or dependants and I/we have enjoyed caring for and managing their health for years. . .

## Initial Decision

I look forward for your assistance in communicating to United that they offer a reasonable solution to this situation so I/we can continue to see City Employees and their dependants without disruption. . .

In the best interest of my/our current City of Ft. Worth patients, I/we ask for your assistance in resolving this dispute before the City transitions to United Health Care.

(CX 1042 at 4).

138. On July 2, 2001, NTSP member physicians Blue, Vance, Deas, and Grant signed a letter addressed to the Mayor of Fort Worth bearing NTSP's letterhead. The letter asserted that United's rates were "well below market benchmarks" and that "NTSP simply has not and will not accept United's request for our participation in their provider network for your employees." The letter also asserted that "the City may experience significant network disruption once United officially begins their duties (up to 588 doctors no longer available)." (CX 1029 at 3-4; see also CX 1031 (July 9, 2001, letter from Vance to the Mayor of Fort Worth, stating that the City's recent switch to United placed the relationship between the City employees and their physicians "in serious jeopardy," that the United offer was "significantly below market," and stating that unless "this contractual issue is resolved," there was the "likelihood that NTSP members will no longer be available to city employees.")).

139. Other NTSP physicians wrote letters to the Mayor of Fort Worth reflecting the points discussed by NTSP in Fax Alert # 44. (CX 1036; CX 1037; CX 1041; CX 1046).

140. NTSP, as an existing provider for the City of Fort Worth, arranged a meeting with the City and communicated to the City NTSP's concerns about the adequacy of United's panel and the cost impact on the City if the City were to change from the PacifiCare risk contract to the United non-risk contract. (Mosley, Tr. 186-87, 192-93; Van Wagner, Tr. 1744; Deas, Tr. 2424-25, 2429-31).



Initial Decision

141. At the September 13, 2001 meeting with the City, NTSP representatives also told the City that United had offered rates on a non-risk contract with NTSP that were unacceptable to NTSP and that NTSP was going to reject the United offer. NTSP told the City that they may have a significantly different network on October 1, 2001, when the City would transition from PacifiCare to United. (Mosley, Tr. 186-87; CX 1042).

142. The NTSP Board informed its member physicians in Fax Alert # 44, dated July 13, 2001, that NTSP Board members met with the Mayor of Fort Worth regarding the "possible inadequacy of the United network" and stated that although they "got the attention of the Mayor, our work is not done." (CX 1042).

143. Jim C. Mosley, a health care consultant to the City of Fort Worth, contacted a representative of United and shared with United the City's concerns regarding the continuation, maintenance, and preservation of the then existing United network. The possibility that City employees might lose access to NTSP physicians was a matter of concern to the City. United was requested to maintain the network without compromising costs. (Mosley, Tr. 173, 179-80, 182; Quirk, Tr. 309).

144. On September 13, 2001, NTSP met again with representatives of the City of Fort Worth. NTSP told the City that United's new, increased PPO reimbursement offer to NTSP physicians was still unacceptable. NTSP further expressed concerns about United's practice of "bundling" claims, pursuant to which physicians who provided multiple services on a single occasion were reimbursed at a single, bundled rate (lower than the rate at which each service would be compensated if billed separately). NTSP expressed its view that United's bundling practice under-compensated physicians. (Mosley, Tr. 185-93; CX 1075).

145. Following the September 13, 2001 meeting between NTSP and the City of Fort Worth, NTSP wrote a letter to the City of Fort Worth informing the City that United continued to offer low rates. (CX 1075 (Letter from Deas to City Manager for the City of Fort Worth, noting that despite some "positive

## Initial Decision

movement," United's overall rates "may still prove inadequate" and this "may affect the overall size of United's physician network").

146. NTSP's September 13, 2001 letter to the City of Fort Worth also reported that several physician's offices refused to contract with United unless a group contract through NTSP was negotiated on their behalf and noted that NTSP's termination notice to HTPN would take effect October 21, 2001. Notification letters to patients could be sent as soon as October 1, 2001, the same day as the City was supposed to transition to United. (CX 1075).

**e. Continued negotiations and termination of HTPN contract**

147. On July 9, 2001, NTSP informed United that United's current offer of 110% RBRVS (Dallas conversion factors) for all products was below the Board minimums that NTSP could accept. NTSP told United that the Board minimums were 125% RBRVS for HMO and 140% RBRVS for PPO (Tarrant County conversion factors). (CX 1034 at 1; Quirk, Tr. 299-01).

148. On July 13, 2001, in Fax Alert # 44, the NTSP Board informed all NTSP member physicians that NTSP and United were in agreement as to basic fundamental language terms but "far apart in agreeing to a market reimbursement fee schedule." (CX 1042 at 1).

149. The NTSP Board also noted in Fax Alert # 44 that many NTSP physicians were contracted with United through HTPN. The rates under the United-HTPN contract were indexed to 114% of 2001 Tarrant County RBRVS for HMO and 127% of 2001 Tarrant County RBRVS for PPO and were reported to be below or little above Medicare for many NTSP specialties. (CX 1042). The NTSP Board contrasted the NTSP minimums of 125% of 2001 Tarrant Medicare RBRVS for HMO and 140% of Tarrant Medicare RBRVS for PPO with United's direct offer to NTSP of 110% 2001 Dallas Medicare RBRVS for all products. (CX 1042).

150. The NTSP Board, in Fax Alert # 44, also informed the member physicians that "the NTSP Board has authorized

Initial Decision

termination [of] the United Health Care contract. However, notice has not yet been sent to United as NTSP must attempt one last strategy." (CX 1042).

151. On July 23, 2001, the NTSP Board approved the termination of its participation in the United-HTPN contract. (CX 91; CX 1051B). At that time, 101 of NTSP's physicians contracted with United through the United-HTPN contract. The rest of NTSP physicians contracted with United were through direct contracts (77) or through another IP A or other organizations. (CX 1055; CX 1057; Quirk, Tr. 302-04).

152. The effective date of termination was to be October 20, 2001, less than three weeks after the City of Fort Worth had planned to transition its employee health plans from PacifiCare to United. (CX 1051B; CX 1042 at 1).

153. On July 23, 2001 NTSP sent a letter to United, submitting its ninety day notice of its termination of participation in all United products offered through HTPN ("termination letter"). NTSP sent a copy of the July 23, 2001 termination letter to the Mayor of the City of Fort Worth. (CX 1118; Quirk, Tr. 312-13).

154. NTSP explained to its member physicians, by Fax Alert # 52 dated August 9, 2001, that the United contract through HTPN was terminated because United offered rates below Board approved minimums and because of United's proposal of a single fee schedule for both HMO and PPO. (CX 1062).

**f. Poll results used to establish Board minimums**

155. United's May 2001 offer to NTSP of 110% of current Dallas Medicare RBRVS fee schedule fell below NTSP's Board minimums that had been determined by the Board based on the result of polling. (CX 1042).

156. Subsequent to the May 2001 offer, NTSP completed its annual reimbursement poll. As NTSP informed its member physicians, "this poll's objective is to identify what reimbursement levels NTSP members deem acceptable." (CX 393).

## Initial Decision

157. On October 29, 2001, in Fax Alert # 83, NTSP communicated to its member physicians the results of NTSP's annual reimbursement poll of NTSP member physicians' acceptable rates on both HMO and PPO levels. (CX 393).

158. The results of the 2001 annual poll for HMO were 128.46% (mean), 127% (median), and 127% (mode). The results for PPO were 142.07% (mean), 144.5% (median), and 144.5% (mode). "All percentages index to current Medicare rates and represent[] the percentage of Medicare that the 'average NTSP physician' would find acceptable for the next twelve months on HMO and PPO products." (CX 393).

159. On October 29, 2001, NTSP held a general membership meeting in which the offer from United was detailed along with the latest poll results which reflected a higher minimum for PPO than United's fee proposal. The PPO rate was listed as an "open issue." (CX 186 at 1).

**g. Power of attorney forms**

160. On August 9, 2001, in Fax Alert # 52, NTSP solicited power of attorney forms from NTSP member physicians because, "as with previous contracts, several members have requested that NTSP act on their behalf in regards to all contracting activity between themselves and United Health Care." (CX 1062).

161. The power of attorney provided to the physicians with Fax Alert # 52 explained to them that "this power of attorney grants to the agent the authority to act on the undersigned's behalf regarding the foregoing described agreements in all respects, including the authority to negotiate the terms of, enter into, execute, modify, extend or terminate any such agreements." (CX 1062 at 2-3).

162. A copy of Fax Alert # 52 was obtained by United. Quirk made a handwritten notation on this copy indicating United's view that United needed to redevelop a network strategy for Tarrant County. (CX 1051; Quirk, Tr. 320-21).

163. United decided to try to recruit the terminated NTSP physicians directly. (CX 1056; CX 1057 at 1). In August 2001,

Initial Decision

shortly after receiving NTSP's termination letter, United made the decision that David Beaty, Senior Network Account Manager for United, would contact all of the affected NTSP physicians whose contracts with United through HTPN were to be terminated by NTSP. (Quirk, Tr. 334; Beaty, Tr. 452, 454).

164. Beaty wrote to these physicians, inviting them to continue participation in United's network under a direct contract with United, and offered them the same reimbursement rates as they were receiving under the HTPN-United agreement. Some physicians accepted this offer. (Quirk, Tr. 334; Beaty, Tr. 452; CX 1068).

165. On August 24, 2001, in Fax Alert # 56, NTSP informed its member physicians that NTSP had been receiving calls from some NTSP physicians regarding direct contract offers that they had received from United. NTSP reported that the rates paid to the NTSP physicians through the United-HTPN arrangement were below the NTSP acceptable Board minimums and noted that this had been NTSP's reason for terminating the HTPN arrangement. (CX 1066).

166. NTSP also informed its member physicians, in Fax Alert # 56, that NTSP would "continue to pursue a direct contract with United Healthcare that meets or exceeds the fee schedule minimums set by the NTSP membership." (CX 1066).

167. Also, through Fax Alert # 56, NTSP informed its member physicians that it had already received 107 executed power of attorney forms "from NTSP members assigning NTSP power of attorney to act on their behalf in regard to all contracting activity between themselves and United Healthcare," and sought the submission of executed powers by additional member physicians. (CX 1066 at 1-2; see also CX 1002 at 1-12).

168. NTSP advised those physicians who had signed the power of attorney forms that they "should inform all United representatives who contact you that NTSP is your contracting agent for United Healthcare and instruct them to contact NTSP directly." (CX 1066 at 1; see also CX 1002 at 1-12).

## Initial Decision

169. United obtained a copy of Fax Alert # 56 and learned that NTSP had gathered 107 power of attorney forms from physicians and that NTSP was continuing to solicit additional power of attorney forms to be used in collective bargaining with United. (Quirk, Tr. 326-27, 330-31; CX 1051A).

**h. United offers increased rates**

170. In the summer of 2001, United increased its offer to All Saints Integrated Affiliates ("ASIA"), another Fort Worth IPA through which 113 NTSP physicians had contracts with United. (CX 1055; Quirk Tr. 345; 336-37). United's offer to ASIA was 125% of 2001 Tarrant County RBRVS for HMO and 130% of Tarrant County RBRVS for PPO. (Quirk, Tr. 345). United made this offer to Medical Clinic of Northern Texas ("MCNT") also. (CX 1119 at 1).

171. In September 2001, United also extended the offer of 125% of 2001 Tarrant County RBRVS for HMO and 130% of 2001 Tarrant County RBRVS for PPO to the NTSP physicians whose contracts through HTPN had been terminated. (CX 658; see also CX 1119).

172. More than ten physicians' groups participating in NTSP did not respond to United's offer at this rate, even though it was higher than rates they had prior to their pending termination, effective October 21, 2001, by NTSP. (Beaty, Tr. 454-55).

173. United's account representative contacted the physician groups that had rejected the new United offer. (Beaty, Tr. 454-55; CX 658; CX 1119). Some of those groups responded that they rejected United's offer for a direct contract because NTSP was negotiating on their behalf. (Beaty, Tr. 455, 459-60).

174. On September 5, 2001, NTSP held a general membership meeting, at which Van Wagner updated NTSP's member physicians on recent progress in contract negotiations with United. (CX 1076; CX 158).

175. On September 7, 2001, United declined NTSP's offer to attend an NTSP Board meeting. (CX 1121).

Initial Decision

176. On September 13, 2001, in Fax Alert # 60, NTSP reported to its member physicians that United had increased reimbursement levels "via a contract amendment with ASIA, as well as individual direct offers to several NTSP physicians." (CX 1076).

177. As a result of the increased offers, NTSP deferred activation of the power of attorney forms for two weeks, subject to NTSP's reconsideration. (CX 1076).

178. On September 19, 2001, NTSP informed its member physicians that in order to allow NTSP to consider the increased United offer available through ASIA or directly, NTSP would defer any further action until September 27, 2001. NTSP would then contact each member who previously gave a power of attorney to determine if those member physicians desired additional action by NTSP on their behalf. Member physicians who considered individual contracts with United were invited to review the proposed negotiated group contract. (CX 1079).

179. In a September 20, 2001 letter, United accepted NTSP's invitation to meet with the NTSP Board. (CX 1080; Quirk, Tr. 338-39).

180. On September 21, 2001, Van Wagner updated NTSP's Medical Executive Committee on contract negotiations with United. (CX 198 at 2).

181. On September 24, 2001, United representatives met with NTSP's Board. NTSP stated that it opposed United's offer of one rate for all products because the offer was below Board minimums, which were different for HMO and PPO products. NTSP told United's representatives that PPO rates should be higher than HMO rates. (Quirk, Tr. 340-41, 344).

182. At the September 24, 2001 meeting, the NTSP Board also told United that NTSP's contractual arrangement with HTPN enabled NTSP to terminate the arrangement for United's products on behalf of its physicians. (CX 1081; Van Wagner, Tr. 1727-28).

183. In a September 24, 2001 letter, Deas invited United to reopen negotiations. (CX 1084).

## Initial Decision

184. On September 24, 2001, NTSP sent a letter to its member physicians with a summary of terms to be included in any direct contract with United. The summary discussed price related terms, including: (1) United's reimbursement methodologies should not translate into less than what Medicare would have paid; and (2) a fee maximum change from 80% of usual and customary to 100% of usual and customary. (CX 1064).

185. On or about October 10, 2001, United sent NTSP a new offer. United offered NTSP an increased rate of 125% of 2001 of Tarrant County RBRVS for HMO and 130% of Tarrant County RBRVS for PPO. (CX 1088; CX 1096; Quirk, Tr. 347-49).

186. NTSP and United signed a contract for 125% of 2001, Tarrant County RBRVS for HMO and 130% of 2001 Tarrant County RBRVS for PPO, effective November 1, 2001. (CX 1095 at 10).

187. The new contract represented an increase of 10% from the initial HMO offer and of 15% from the initial PPO offer. (Quirk, Tr. 290, 297-98). Compare CX 87 at 11 (for both HMO and PPO, 115% of Tarrant County RBRVS) with CX 1095 (for HMO, 125%; for PPO, 130% of 2001 Tarrant County RBRVS).

188. The contract was an increase from United's initial offer to NTSP. But, it was the same rate that United had previously offered other IP As - ASIA and MCNT. (CX 1119). It was also a lower rate than the one given to HTPN in February 2001. (CX 1099).

189. On November 1, 2001, in Fax Alert # 84, NTSP sent the contract to its member physicians to opt in or opt out, indicating that the contract was a result of negotiations and that the 125% of the 2001 Tarrant County RBRVS for the HMO was "at the average level of acceptable reimbursement." NTSP noted to its member physicians that the PPO rate of 130% of Tarrant County RBRVS was below the acceptable average reimbursement levels determined by the NTSP Board, based on the poll results. (CX 1097; Van Wagner, Tr. 1642-43).

190. Vance, a former NTSP President who at the time was a member of the NTSP Board of Directors, summarized NTSP's



Initial Decision

success in these United negotiations to his medical group, in an effort to convince the group to continue their membership with NTSP:

United Health Care came to town six months ago and offered a straight 110% of Medicare contract. . . . Through the efforts of NTSP lobbying the City [of Fort Worth] and [terminating] a group contract with Health Texas, United blinked. United was so eager to dilute our effectiveness that they refused to negotiate with NTSP but offered an improved contract thru ASIA. The fees in the [ASIA] contract are very close to the numbers that NTSP presented as market rates for [Fort Worth] and were rejected out of hand by United officials. United has now returned to the table with NTSP at the direct request of the Commissioner of the Dept[.] of Insurance. This United negotiation is a template for other efforts that will need to occur in the near future and would best be coordinated by NTSP.

(CX 256; see also CX 1199 (Vance, Dep. at 310-11)).

191. The level of acceptance of the NTSP/United contract by NTSP member physicians was low. (CX 1100). Fax Alert # 95, dated November 19, 2001, indicates that 258 NTSP member physicians responded. (CX 1100). For HMO, 24% accepted and 76% rejected the contract. For PPO, 23% accepted and 77% rejected the contract, (CX 1001 at 2).

**i. NTSP reported United to Texas Department of Insurance**

192. NTSP reported United to the Texas Department of Insurance in 2000 and 2001 for prompt pay violations, noncompliance with contracts, and predatory pricing concerns. (Van Wagner, Tr. 1772).

193. NTSP's Board Minutes of September 24, 2001, reported that Deas met with the Texas Commissioner of Insurance to discuss predatory pricing by health plans. The Commissioner

## Initial Decision

stated that he would send letters to CEOs of major plans cautioning them against predatory pricing activities. Deas also discussed with the Commissioner the impact of HMO and PPO contracting revisions on Tarrant County physicians. (CX 100 at 3-4).

194. In August 2001, the Texas Department of Insurance fined United \$ 1.25 million and ordered it to pay restitution to providers for failing to follow Texas laws on prompt payment and clean claims. (RX 3103).

## **2. Cigna Healthcare**

### **a. Corporate structure**

195. Cigna of Texas is a subsidiary of Cigna Healthcare ("Cigna") which has its corporate headquarters in Philadelphia, Pennsylvania. (Grizzle, Tr. 669). Cigna Corporation reports consolidated earnings for the entire corporation, including Cigna of Texas. (Grizzle, Tr. 669-70).

196. A change in revenue and earnings for Cigna of Texas would affect the revenues and earnings for the entire corporation. (Grizzle, Tr. 670).

197. When Cigna contracts with multi-state employers, a single contract is signed. (Grizzle, Tr. 682). A change in costs for Cigna of Texas could affect the health insurance costs of an employer with multi-state coverage. (Grizzle, Tr. 683).

198. An increase in Cigna's costs would increase premiums which could affect Cigna's competitiveness in other states. (Grizzle, Tr. 683-85).

199. Mr. Rick Grizzle is the vice president of network development for Cigna Healthcare, with responsibilities for contracting and managing provider services in Texas, Oklahoma, and Louisiana. (Grizzle, Tr. 666-67).

Initial Decision

**b. Cigna's acquisition of Healthsource and initial contacts with NTSP**

200. In late 1997, Cigna purchased Healthsource, a company which offered both HMO and PPO products, covering approximately one million lives nationally. Many NTSP member physicians had direct contracts with Healthsource. (Grizzle, Tr. 695, 767-70).

201. For physicians with agreements with both Cigna and Healthsource, Cigna, in July 1998, informed physicians that their contracts under Healthsource would be terminated and assigned to Cigna. (CX 332; Van Wagner, Tr. 1752-53).

202. For physicians with agreements with only Healthsource, Cigna, in July 1998, requested that physicians assign their contracts from Healthsource to Cigna and informed physicians that if they did not wish to assign their contracts to Cigna, they could continue under their Healthsource agreements, as long as Healthsource products were being offered in the marketplace. (CX 332; Van Wagner, Tr. 1752-53).

203. Healthsource subsequently went out of business. (Grizzle, Tr. 770).

204. Some NTSP physicians went to NTSP regarding the change in their Healthsource contracts and requested that NTSP contact Cigna. (Van Wagner, Tr. 1752). NTSP did contact Cigna regarding these issues. (Van Wagner, Tr. 1753-54).

205. NTSP sent to its member physicians a sample letter refusing the contract assignment from Healthsource to Cigna and directing Cigna to negotiate with NTSP as their agent. NTSP also sent its member physicians an agency agreement that authorized NTSP to negotiate on the behalf of consenting member physicians. NTSP informed its physicians that "if 50% or more of NTSP member physicians concur that agency is appropriate, NTSP will contact CIGNA and Healthsource directly in regards to this matter." NTSP advised "its members not to consent to the assignment of your Healthsource provider agreements to CIGNA." (CX 332 (emphasis omitted)).

## Initial Decision

206. Cigna received 40 letters, all virtually identical to the sample letter provided by NTSP, representing 52 NTSP member physicians, in which NTSP physicians did not agree to assign to Cigna their Healthsource agreements, and which directed Cigna to negotiate with NTSP on their behalf. (CX 760 (limited admission); Grizzle, Tr. 696-98, 709, 724).

207. The physicians who did not agree to assign their Healthsource agreement to Cigna believed that they had the right to do so. (Van Wagner, Tr. 1753-54; Grizzle, Tr. 768).

208. Upon receiving these letters, Cigna concluded that the 52 physicians who had sent Cigna letters would not directly contract with Cigna and that Cigna would need to approach NTSP instead. (Grizzle, Tr. 697, 709-10, 747).

209. Cigna has entered into direct contracts with some NTSP physicians independent of NTSP. (Grizzle, Tr. 724). In some instances, the direct contract between Cigna and physician is at a higher reimbursement rate than the Cigna/NTSP contract. (Deas, Tr. 2410).

**c. NTSP's negotiations with Cigna**

210. Beginning in 1999, NTSP sought a risk contract with Cigna. (Grizzle, Tr. 775; Van Wagner, Tr. 1754-55; CX 764, in camera). NTSP and Cigna were unable to agree to a risk-sharing arrangement. (Van Wagner, Tr. 1758; CX 764, in camera).

211. Cigna and NTSP have entered into several fee-for-service agreements. These agreements are: the Letter of Agreement, the First Amendment, the Second Amendment, and the Third Amendment. (CX 764, in camera; CX 769; CX 771 at 1, in camera; CX 809, in camera; CX 810, in camera; Grizzle, Tr. 715-16; Grizzle, Tr. 723-24).

**(i) Letter of Agreement, First Amendment**

212. NTSP and Cigna entered into a Letter of Agreement (LOA) in October of 1999. The LOA only covered fee-for-service rates for Cigna's HMO business, and not its PPO business. (Grizzle, Tr. 710-11; CX 782A, in camera).

Initial Decision

213. Under the LOA, Cigna agreed to reimburse NTSP specialists, with the exception of cardiologists/cardiovascular surgeons, gastroenterologists, urologists, oncologists, and podiatrists, on a fee schedule equal to 125% of the 1998 Dallas County RBRVS. (Grizzle, Tr. 710-14; CX 782A, in camera; CX 764 at 1, in camera).

214. Cigna entered into this agreement with NTSP because Cigna believed that the core group of NTSP, the specialists in Fort Worth, were critical for Cigna. (Grizzle, Tr. 719-20).

215. The LOA was entered into by NTSP and Cigna in anticipation of a risk contract and specifically called for the establishment of a risk contract within a short time. (Van Wagner, Tr. 1757-58; CX 784, in camera; CX 782A, in camera).

216. The 1999 LOA was amended in January 2000 (First Amendment) to add PPO coverage for NTSP specialists at a reimbursement rate of 135% of Dallas County 1998 RBRVS. (CX 769; Grizzle, Tr. 714).

217. Cigna's representative, Grizzle, testified that the reimbursement rate of 125% of RBRVS on HMO and 130% of RBRVS on PPO was somewhere between 15 and 20 percent higher than Cigna's standard rates. Grizzle also testified that the rates Cigna paid to NTSP were in the "general ballpark" of the rates Cigna paid to other IP As [redacted]. (Grizzle, Tr. 716, 958-59, in camera).

**(ii) Conflicts between NTSP and Cigna**

218. NTSP believed that Cigna had breached its contract with respect to how fee schedules were loaded into Cigna's system. There were instances of a change in the fee schedule as called for by the contract where NTSP would later find that Cigna had failed to load the changes. NTSP complained to Cigna regarding Cigna's failure to pay in accordance with the agreed upon schedule and informed Cigna that NTSP considered the failure a material breach. (Grizzle, Tr. 797; Van Wagner, Tr. 1769; CX 792, in camera; RX 497; RX 960, in camera; RX 1486, in camera).

Initial Decision

**(iii) Second Amendment**

219. NTSP also believed that Cigna breached the LOA and First Amendment by not adjusting the fee schedule to current year RBRVS. (Grizzle, Tr. 799-800; Van Wagner, Tr. 1979-80).

220. The 1999 LOA was amended in May 2000 (Second Amendment) to clarify the proper year of RBRVS reimbursement. While the First Amendment to the LOA did not require that the fee schedule be adjusted annually, the Second Amendment explicitly called for an annual adjustment of the HMO and PPO schedule to current year [redacted] RBRVS. (CX 769; CX 770, in camera; CX 771, in camera; CX 800 at 2; Grizzle, Tr. 715, 740-41).

**(iv) Cardiologists**

221. Under the LOA, Cigna agreed to reimbursement of "NTSP specialists, with the exception of NTSP cardiologists/CV [cardiovascular] surgeons, gastroenterologists, urologists, oncologists and podiatrists." (Grizzle, Tr. 710-14; CX 782A, in camera).

222. NTSP's cardiologists were carved out of the LOA. (Grizzle, Tr. 927, in camera; Van Wagner, Tr. 1764-66).

223. In a carve out arrangement, certain specialists or services are outside of a capitation plan and are paid in some other manner. (Frech, Tr. 1434).

224. Although NTSP's cardiologists were initially carved out of the LOA, an addendum to the LOA gave a right of first refusal for NTSP's cardiologists to participate with Cigna if Cigna's carve out agreements with cardiologists were terminated. (Grizzle, Tr. 927, in camera; Van Wagner, Tr. 1764-66; CX 770, in camera).

225. Regarding Cigna's need for cardiologists, Cigna had contracted with American Physician Network ("APN") for cardiology services. (Grizzle, Tr. 726-27, 929-30, in camera).

Initial Decision

226. In July 2000, Cigna informed NTSP that the carve out arrangement that Cigna had with NTSP had been assigned to APN and told NTSP to work out an agreement with APN. (Grizzle, Tr. 929-30, in camera; Van Wagner, Tr. 1768; CX 775).

227. Cigna viewed its action as an assignment of the contract and believed that the LOA did not allow NTSP's cardiologists to join the Cigna fee-for-service contract if the carve out had been assigned. (Grizzle, Tr. 725).

228. NTSP viewed Cigna's action as Cigna's termination of the cardiologists' carve out agreement. NTSP believed that Cigna had breached the LOA by refusing to give NTSP's cardiologists a right of first refusal to participate in the NTSP agreement. (Grizzle, Tr. 929-30, in camera; Van Wagner, Tr. 1766-68; CX 775; CX 776; CX 784; CX 785, in camera).

229. NTSP sent Cigna a letter, dated August 2, 2000, stating that NTSP was exercising its option under the terms of the present Cigna arrangement for NTSP cardiologists to participate under the terms of the HMO arrangement. (CX 776).

230. APN subsequently submitted a fee-for-service offer to NTSP's cardiologists. (Grizzle, Tr. 726-27).

231. NTSP rejected APN's offer, in a letter dated October 6, 2000, which stated that the offer "was shared with affected members of NTSP's Cardiology Division and NTSP's board. At this point, we must decline your proposal as it does not meet our minimum reimbursement levels." (CX 777A; Grizzle, Tr. 726-27).

232. In an October 16, 2000 letter from NTSP to Cigna, NTSP stated that NTSP's Cardiology Division and Board found Cigna's proposal to be "woefully inadequate. The financial arrangements proposed were well below the agreed upon fee schedule contained in the NTSP/Cigna agreement. As a result, [APN] was notified on October 6, 2000 that [their] proposal was declined, as it did not meet minimum reimbursement levels." (CX 777).

## Initial Decision

233. The October 16, 2000 letter from NTSP to Cigna also states that "obviously Cigna's failure to resolve this issue may affect current NTSP participation and future dialogue with Cigna regarding a PSN [provider sponsored network] type risk arrangement." (CX 777; Grizzle, Tr. 730).

234. NTSP believed that it had the right to terminate its contract with Cigna if what NTSP believed to be Cigna's breaches of contract were not cured. (Grizzle, Tr. 797; Van Wagner, Tr. 1769-71; RX 497; RX 960, in camera; RX 1486, in camera).

235. Cigna performed an analysis of the impact of the potential loss of NTSP's physicians from its network. Cigna determined that NTSP's termination would leave it with gaps in specialty coverage in the Fort Worth area. (Grizzle Tr. 730-31 (stating that Cigna took the threat seriously because NTSP presents "a fairly unified force, well-represented and looked like a strong entity . . . working in Fort Worth"); CX 779, in camera (charting impact of NTSP termination by specialty)).

236. Within the next twelve months, APN went bankrupt and dissolved. Cigna then allowed NTSP's cardiologists to participate in the Cigna/NTSP agreement. (Grizzle, Tr. 731-32, 937 (in camera); Van Wagner, Tr. 1768).

**(v) Third Amendment: primary care physicians**

237. Under the 1999 contract between Cigna and NTSP, Cigna agreed to reimburse "NTSP specialists," with the exception of those specialists explicitly carved out. (Grizzle, Tr. 710-14; CX 782A, in camera).

238. NTSP sought to have its primary care physicians ("PCPs") included under its contract with Cigna. By letter dated November 9, 2000, NTSP wrote to Cigna expressing its belief that the agreement between Cigna and NTSP was in serious jeopardy due to Cigna's refusal to allow NTSP cardiologists to participate at the contracted rate. NTSP wrote: "in an effort to maintain NTSP network participation during this critical period of open enrollment, I believe a timely good faith gesture by Cigna would be appropriate." One of the terms which NTSP would consider



Initial Decision

was that, "Cigna immediately allow all of NTSP's sub-contracted Primary Care Physicians the option to participate under the terms of our HMO and PPO agreements." (CX 786, in camera; Grizzle, Tr. 732).

239. Cigna had already contracted with a sufficient number of primary care physicians at lower rates than those under the NTSP agreement. Allowing NTSP's primary care physicians to opt in to the NTSP/Cigna specialist contract would increase Cigna's costs with no additional benefit to Cigna. (Grizzle, Tr. 718-19, 733-34).

240. In order to maintain the relationship with NTSP and despite increasing its costs, Cigna offered NTSP's primary care physicians a tiered reimbursement fee schedule in which the primary care physicians would initially receive NTSP's specialist rates and would, over time, return back to a "market level." (Grizzle Tr. 735-36).

241. In December 2000, NTSP rejected Cigna's offer on behalf of its primary care physicians. (Grizzle, Tr. 736; CX 791 ("NTSPs Board absolutely cannot and will not negotiate or offer an agreement in which our PCP partners are paid less than our specialists . . . . The 125% of the then current Dallas (not Tarrant County) RBRVS must stand as per our current agreement.")).

242. On June 7, 2001, NTSP sent an email to Cigna requesting that Cigna bring NTSP primary care physicians into the NTSP/Cigna agreement on the PPO product. (CX 800 at 1).

243. By return email that same day, June 7, 2001, Cigna reiterated its resistance to NTSP's demands to include NTSP's primary care physicians at NTSP's specialist rates. (CX 800 at 2; Grizzle, Tr. 740-41).

244. NTSP subsequently, on June 12, 2001, sent a notice of termination letter to Cigna, providing Cigna with 60 days notice. NTSP's letter stated, NTSP "look[s] forward to utilizing the next 60 days in resolving the issue of Cigna not allowing our affiliated Primary Care Physicians to participate under the terms of our PPO agreement." (CX 802).

245. In response to NTSP's notice of termination letter, Cigna and NTSP negotiated a third amendment to the NTSP/Cigna

## Initial Decision

contract. (Grizzle, Tr. 749-51; Van Wagner, Tr. 1771; CX 810, in camera).

246. The 1999 LOA was amended in August 2001 (Third Amendment) [redacted] (Grizzle, Tr. 749-51, 755, 942-43, in camera; Van Wagner, Tr. 1771-72; CX 809, in camera; CX 810, in camera).

247. The Third Amendment is the current contract under which Cigna and NTSP were operating at the time of trial (April 2004), and was set to expire September 14, 2004. (CX 809, in camera; CX 810, in camera).

248. Cigna estimated that it would cost Cigna [redacted] to add more NTSP physicians to the NTSP/Cigna arrangement. These additional physicians were already individually-contracted with Cigna at "market rates." (CX 814, in camera). Cigna realized no benefit from having these additional NTSP physicians in the network. (Grizzle, Tr. 877-79, in camera).

**(vi) Third Amendment: terms**

249. The contract between NTSP and Cigna that was current at the time of trial, April 2004, the Third Amendment, is a non-risk agreement. (CX 809, in camera; CX 810, in camera; F. 251-55).

250. Under the Third Amendment, PPO reimbursement is at a rate of [redacted] and HMO reimbursement is at a rate of [redacted]. (CX 809, in camera; CX 810, in camera).

251. In NTSP's summary of the contract terms, NTSP characterizes the agreement as a "non-risk agreement." (CX 810, in camera).

252. The Third Amendment does include: capitation payments, a pay-for-performance provision, and a withhold provision. (Van Wagner, Tr. 1758-59, 1761; F. 253-55).

253. [redacted] (Grizzle, Tr. 755, 879-80, in camera).

254. [redacted] (Grizzle, Tr. 880, 896, 946-48, in camera; Van Wagner, Tr. 1974-76).

Initial Decision

255. [redacted] (Grizzle, Tr. 881-82, in camera).

**d. NTSP reported Cigna to Texas Department of Insurance**

256. NTSP reported Cigna in 2000 and 2001 to the Texas Department of Insurance for prompt pay violations, noncompliance with contracts, and predatory pricing concerns. (Van Wagner, Tr. 1772).

257. In August 2001, the Texas Department of Insurance took action against Cigna for violations of Texas claims payment laws. Cigna was fined \$ 1.25 million and ordered to pay restitution to providers as a result of Cigna's failure to comply with clean claims laws. (RX 3103).

258. In September 2001, the Texas Attorney General investigated Cigna's payment methodology. (CX 108 (Board minutes reporting Office of Attorney General's letter); RX 1290; RX 1651).

**3. Aetna Health, Inc.**

**a. Corporate structure**

259. Aetna Health, Inc., ("Aetna") is a wholly owned subsidiary of Aetna, Inc., which has its headquarters in Hartford, Connecticut. (Roberts, Tr. 474).

260. Aetna provides health insurance coverage in the North Texas area. In the Fort Worth area, Aetna currently has approximately 40,000 to 50,000 HMO members and 100,000 PPO members. (Roberts, Tr. 474; Jagmin, Tr. 981).

261. Aetna's network has about 7,200 physicians in the Dallas-Fort Worth Metroplex. (Jagmin, Tr. 1121).

262. Aetna's clients in the Fort Worth area include national companies such as Bell Helicopter and Lockheed Martin. (Roberts, Tr. 476).

263. When Aetna pays a claim in Texas, it is paid from premiums which may have come from states outside of Texas. (Roberts, Tr. 476).

## Initial Decision

264. Aetna's performance in the Fort Worth area affects Aetna's national performance because any profits or losses roll up and appear on the financial statements of the publicly traded parent company. (Roberts, Tr. 474, 477).

265. Dr. Christopher Jagmin is currently the medical director for medical policy. (Jagmin, Tr. 969). Jagmin works for Aetna, Inc., based out of Blue Bell, Pennsylvania, and he consults and advises for the North Texas area. (Jagmin, Tr. 972, 974).

266. Mr. David Roberts is employed by Aetna Health, Inc., as a network vice-president. He has worked for Aetna Health, Inc., (or another subsidiary of the national company) since 1999, when Aetna acquired Prudential. Prior to 1999, Roberts worked for Prudential. In May 2001, Roberts assumed responsibility for contracting with physicians in the North Texas area. (Roberts, Tr. 468-70).

**b. NTSP's relations with Aetna through HMS and MSM**

267. In 1994, many physicians signed an HMO risk contract and a PPO non-risk contract to treat Aetna patients through another IPA, Harris Methodist Select ("HMS"). (Van Wagner, Tr. 1692; RX 832).

268. The 1994 HMS contracts with Aetna were exclusive and were not terminable until June 30, 1999. (RX 3146).

269. Many of the physicians who had contracts with HMS signed participating physician agreements with NTSP. (RX 832).

270. In 1997, NTSP believed that HMS had breached the 1994 contracts by attempting to amend those contracts without consent, agreeing to non-exclusivity with Aetna, and failing to make full payments to physicians. (Vance, Tr. 591; Van Wagner, Tr. 1692; RX 309; RX 310; RX 832).

271. NTSP was appointed by NTSP's participating physicians to represent them in the contract dispute with HMS. (Van Wagner, Tr. 1681).

Initial Decision

272. In 1999, during the time of the contract dispute between NTSP and HMS, HMS became Medical Select Management ("MSM"). Contracts between physicians and HMS were assigned to MSM. (RX 832).

273. The contract between MSM and Aetna, which served about 115,000 patients, was primarily a "global risk deal," through which Aetna delegated almost all the medical risk to MSM under an HMO plan. (Jagmin, Tr. 984-85, 997). MSM also had a non-risk PPO contract with Aetna. (RX 832).

274. Many of NTSP's participating physicians had been contracted with MSM to provide physician services pursuant to MSM's agreements with Aetna. (Jagmin, Tr. 982).

275. In June 1999, NTSP, as the class representative for its participating physicians, sued HMS and MSM. The class action lawsuit against HMS and MSM alleged that HMS and MSM refused to honor the terms of the 1994 contract. (Van Wagner, Tr. 1652-53; RX 335; RX 849; CX 1172 (Collins, Dep. at 6-9)).

**c. NTSP's initial contract negotiations**

276. In late 1999, NTSP initiated a meeting with Aetna and proposed a direct contracting relationship between Aetna and NTSP, that would not involve MSM, under a risk contract. (Jagmin, Tr. 981-84; Van Wagner, Tr. 1700; CX 531). This meeting did not develop into broader negotiations. (Jagmin, Tr. 988-89).

277. Around April 2000, NTSP again initiated negotiations with Aetna to discuss a direct contract between NTSP and Aetna. (Jagmin, Tr. 989-90).

278. In early June 2000, NTSP met with Aetna to discuss future business and contract arrangements. (CX 177). NTSP told Aetna that its physicians might leave the MSM contract because of what NTSP perceived to be MSM's continuing breaches of contract and financial problems. (Jagmin, Tr. 983-84; Van Wagner, Tr. 1652-53, 1692-95, 1700; CX 531).

## Initial Decision

279. Subsequent to the June 2000 meeting between NTSP and Aetna, Aetna discussed internally the possible contracting scenarios with NTSP and concluded that the most favorable scenario was keeping NTSP's physicians within Aetna's current contract through MSM, rather than signing a separate contract with NTSP. This conclusion was based on Aetna's belief that a separate contract would duplicate administrative costs. (CX 525 at 1-2).

280. The internal Aetna discussion considered a scenario in which Aetna would lose most of NTSP's member physicians. This turn of events was envisioned by Aetna as a realistic possibility if NTSP's member physicians were to pull out of the MSM contract, Aetna were to fail to reach an agreement with NTSP, and only a few of NTSP's member physicians were to contract with Aetna directly. Aetna's conclusion was that this scenario would create undesirable holes in particular specialties and perhaps service areas. Under the same scenario, Aetna was also "very concerned" with the fact that many of its health plan members, especially "given their national client base," would complain that their doctor was no longer in the network. (CX 525; Jagmin, Tr. 1000-02).

281. In these internal Aetna discussions, NTSP was perceived as representing the "majority of the preferred SPECs [specialists] in [Fort] Worth," and as specialist-dominated. (CX 525 at 2).

282. In Fax Alert # 55, dated August 7, 2000, Van Wagner informed NTSP member physicians that "NTSP has started negotiations with Aetna in regards to a risk and non-risk contract. As of this date, a term sheet has been received and is being reviewed. It is the goal of both parties to implement a new contract effective January 1, 2001. Given the stages of our negotiation, NTSP will know in approximately thirty days whether or not a direct contract with Aetna will be in the best interest of its members." NTSP asked its member physicians to allow NTSP to continue discussions with Aetna for the next thirty days. (CX 942 at 2).

Initial Decision

283. An October 5, 2000 Fax Alert informed NTSP physicians that NTSP had filed suit against MSM on behalf of its member physicians and that NTSP had begun discussions with Aetna on a direct contract for Aetna HMO patients. The Fax Alert sought physicians to sign a power of attorney to authorize NTSP to represent them:

In order to pursue these initiatives to their maximum outcome, having NTSP act as the members' agent and attorney in fact in negotiations, amendments, extensions and/or terminations of Aetna contracts was suggested.

A Motion was made and passed that 66% of all affected NTSP physicians should agree to NTSP's role as agent or attorney in fact regarding this matter.

Attached to this fax is a copy of a Power of Attorney for each member's consideration. If you wish NTSP to represent you as your attorney in fact regarding your contracts with Aetna US HealthCare, . . . please sign below and fax return to the NTSP offices. . . .

(CX 347 at 1-2).

284. The power of attorney appointed NTSP to act as the signatory attorney in fact with respect to "all contracts and agreements (including without limitation all prospective contracts or agreements)" with Aetna, MSM, and other entities. (CX 347 at 4).

285. In October 2000, negotiations between NTSP and Aetna for a risk contract ended without an agreement. (Jagmin, Tr. 1006-09; CX 540 at 1).

Initial Decision

**d. Continued negotiations on a non-risk contract****(i) Initial proposals**

286. In October 2000, after NTSP and Aetna determined that they could not agree on a risk contract, NTSP and Aetna continued to negotiate for a non-risk contract only. (Jagmin, Tr. 1004-05; CX 717 at 4; CX 544 at 3).

287. With respect to rates for anesthesiologists, Aetna's initial offer to NTSP, in October 2000, was \$ 40 per unit. NTSP told Aetna that anesthesia unit rates for a PPO product were between \$ 46 and \$ 48 in the market. (Jagmin, Tr. 1017, 1034-35, 1045; CX 544 at 2, 3). In an October 20, 2000 letter, Aetna informed NTSP that an anesthesia rate of \$ 46 to \$ 48 was too high. (CX 540 at 4; Jagmin, Tr. 1017).

288. With respect to HMO and PPO products, Aetna's initial offer to NTSP, in October 2000, was based on a reference schedule that uses the same relative value units from the RBRVS schedule, but places a different multiplier on different specialties' services, based on supply and demand. (Jagmin, Tr. 1012-13). Aetna's initial offer aggregated to about 111% to 112% RBRVS for HMO and about 123% to 125% RBRVS for PPO, with some specialties being offered more or less than the aggregate, based on the scarcity or abundance of the particular specialty of the physician. (Jagmin, Tr. 1015-16, 1022-24).

289. In October 2000, NTSP sought from Aetna a non-risk contract with uniform rates of 125% RBRVS for HMO and 140% RBRVS for PPO. (Jagmin, Tr. 1023, 1033-34, 1040-41; CX 543 at 3-4).

290. NTSP's proposed rates of 125% of RBRVS for HMO and 140% of RBRVS for PPO were the same rates that physicians had been receiving for providing services to Aetna patients through the MSM contract. (Jagmin, Tr. 1023; Van Wagner, Tr. 1697; CX 538). (Compare RX 968, in camera, with RX 24 at 21).



Initial Decision

291. NTSP's proposal for both HMO and PPO was a uniform rate for all physicians, instead of the different rates to each speciality that Aetna initially had offered. (CX 543 at 3-4; Jagmin, Tr. 1023).

292. Aetna expressed concern to NTSP that a uniform rate based off of Medicare RBRVS would impose overpayment to some NTSP specialties, while other NTSP physicians might choose not to participate on the basis of underpayment, which might require Aetna to have to contract with those physicians individually at a higher rate. (Jagmin, Tr. 1031-32).

293. NTSP informed Aetna that it would not be involved in any non-risk contract that proposed different rates for different member physicians. (Roberts, Tr. 523-24; Jagmin, Tr. 1165).

294. Aetna's representative talked to physician groups to try to contract with them directly. Some of those physicians referred Aetna back to NTSP. (Jagmin, Tr. 1042-44).

295. Aetna, at the time of these negotiations, was concerned about losing physicians because it was late in the enrollment period, the time when employees choose their health plans or change their prior selections. (Jagmin, Tr. 990-91; 1060-61).

296. On November 7, 2000, NTSP sent a letter to "NTSP Members," providing them with a termination letter that NTSP's Board of Directors "is sending to . . . MSM on your behalf. . . . This termination letter notifies MSM that they are in material breach of your 1994 contract regarding the Aetna HMO." (CX 546).

297. On November 20, 2000, NTSP sent Aetna an email informing Aetna that NTSP physicians would no longer serve Aetna's patients through MSM:

North Texas Specialty Physicians' (NTSP) 260  
doctors have treated Aetna patients for over ten years.  
. . . We are pleased that Aetna has contacted us in an  
effort to work out the details for a direct contracting  
relationship. . . . If a direct contracting relationship  
between NTSP and Aetna is accomplished, all of

## Initial Decision

Aetna's PPO lives will be served directly by NTSP physicians. In addition, approximately 15,000 of the 100,000 Aetna HMO covered lives will have direct access to NTSP doctors. The remaining approximately 85,000 Aetna HMO covered citizens are contracted through Medical Select Management's Aetna contract. As of today, NTSP has notified Medical Select Management that under current contractual conditions, NTSP physicians can no longer participate.

(CX 559).

298. By November 20, 2000, Aetna made a new offer of a uniform rate based on RBRVS and increased its offer to 116% RBRVS for HMO and 140% for PPO. Aetna's offer on anesthesia rates remained at \$ 40 per unit. (CX 561; Jagmin, Tr. 1044-45, 1076-77).

299. With respect to Aetna's PPO and anesthesia offer, Van Wagner informed Aetna that she thought that Aetna's PPO fee schedule of 140% of current Medicare RBRVS would be "well received when we messenger it out by all except anesthesia. . . . As you know their contracting minimums on PPO rates were not met." Jagmin understood that most member physicians would accept the 140% rate for PPO, but that no anesthesiologist would sign up under the contract. (CX 558 at 2; Jagmin, Tr. 1052).

300. With respect to Aetna's HMO offer, NTSP did not present Aetna's HMO offer to its member physicians because the rate fell below the established Board minimums. (Van Wagner, Tr. 1927-28).

301. Aetna's representative met with NTSP's Board and had conversations with Board members and with Van Wagner and NTSP's Director of Managed Care, David Palmisano, in which both physicians and NTSP staff conveyed to Aetna that NTSP's Board minimum was 125% of RBRVS for HMO and that NTSP did not have the authority to messenger any contracts below these rates. (Jagmin, Tr. 1021-23; CX 571).

Initial Decision

**(ii) Power of attorney forms**

302. At the same time that NTSP and Aetna were discussing the non-risk contract, Van Wagner sent Aetna a list of the physicians to whom NTSP had sent power of attorney forms seeking delegation of NTSP as the organization that would conduct negotiations for them. (Jagmin, Tr. 1029; CX 534).

303. Jagmin asked both physicians and NTSP staff about the power of attorney forms and was told that the power of attorney forms assigned to NTSP direct contracting efforts between Aetna and the physicians. (Jagmin, Tr. 1029).

304. On November 10, 2000, Van Wagner informed Jagmin that NTSP had sent approximately 180 power of attorney forms from NTSP member physicians to MSM, and told Jagmin that the powers of attorney cover any direct contracting with Aetna. (CX 558 at 2).

305. Aetna believed that, with these power of attorney forms, NTSP would be representing individual physicians in negotiating with Aetna if Aetna did not enter into a contract with NTSP. (Jagmin, Tr. 1051; CX 558).

306. Because Aetna believed that NTSP was going to represent each one of the individual physicians or physician groups in a direct contract negotiation, Aetna believed that there was pressure for Aetna to enter into a contract with NTSP. (Jagmin, Tr. 1058-60).

307. In a November 2001 NTSP Board meeting that was attended by an Aetna representative, the power of attorney forms that NTSP had collected from its member physicians were referenced during the discussions between NTSP and Aetna on the proposed rates for a non-risk contract. (Roberts, Tr. 537-39).

**(iii) Re-polling of NTSP member physicians**

308. By November 21, 2000, Aetna and NTSP had reached an agreement on 140% of current Medicare RBRVS for PPO, but had not reached an agreement on HMO rates, with NTSP seeking across the board 125% of Medicare RBRVS and Aetna seeking across the board 116% of Medicare RBRVS. The parties also had

## Initial Decision

not reached an agreement on anesthesia rates. (CX 561; Jagmin, Tr. 1071-72).

309. NTSP discussed its negotiations with Aetna at an NTSP general membership meeting on November 21, 2000. (CX 180).

310. By Fax Alert # 81, dated November 29, 2000, NTSP informed its member physicians that Aetna's then current offer was an across the board fee schedule of 140% of current Medicare RBRVS for its PPO product, an across the board fee schedule of 116% of current Medicare RBRVS for its HMO product, and \$ 40 per unit for anesthesia rates for both the HMO and PPO products. (CX 565).

311. NTSP informed its member physicians in Fax Alert # 81:

In keeping with the minimum compensation standards as conveyed from the membership earlier this year, [Aetna's] PPO offer of 140% of current Medicare approximates an acceptable minimum standard. The minimum standard previously shared by the membership on an HMO product is 125% of current Medicare or approximately 9% less than Aetna's present offer. . . .

Because this is a fee-for-service offering falling below the minimum as previously shared via the messenger model to the NTSP Board, we are repolling the membership on the acceptability of the present Aetna offering. Please check in the space below what your minimum acceptable range of compensation for the Aetna HMO product is.

(CX 565).

312. The polling ballot listed ranges of rates for selection by NTSP's member physicians. Aetna's offered amounts (116% for HMO, \$ 40-42 per unit for anesthesia) were listed as the lowest "minimum acceptable range of compensation" that NTSP physicians could select on the polling ballot. (CX 565 at 2; Van Wagner, Tr. 1929-30).

Initial Decision

313. As reported at NTSP's December 4, 2000 Board meeting, sixty-one responses had been received, with the majority choosing the 121%-130% range. At that meeting, it was also noted that the termination of the contract with Aetna through MSM would be carried out in thirteen days. (CX 74 at 4).

314. On December 8, 2000, NTSP conveyed the poll results to Aetna: "the numbers on the messenger model return for the [HMO] product are as follows . . . mean: 124.89% of current medicare; mode 127.38% of current medicare; median 123.70% of current medicare." NTSP wrote to Aetna that "this response is essentially the current reimbursement rate for Aetna [HMO] lives not attached to [MSM]." (CX 571).

315. Aetna then convened an internal meeting and concluded that increasing its offer by 9% to match NTSP's proposal meant losing money on NTSP HMO services. (Jagmin, Tr. 1080).

316. On December 11, 2000, NTSP sent Fax Alert # 84 to its member physicians, containing the following statements: "The membership's message that a 125% of current Medicare HMO fee schedule is required has been transmitted to Aetna and a response on this final contractual item is expected within the next 24 to 36 hours . . . NTSP Continues To Act As Your Agent Both With Aetna Direct And With MSM. At This Point, No Further Action Is Required On Your Part . . . Please refer all contacts and materials received from either Aetna or MSM to NTSP directly." (CX 573 (emphasis omitted)).

**(iv) Aetna agrees to NTSP's proposals**

317. NTSP wrote to Aetna on December 12, 2000 to inform Aetna that Van Wagner had "polled the Board informally today" and that the NTSP Board "would urge Aetna to reconsider their position on not accepting the members[] poll results on compensation for the [HMO] direct contract." (CX 578).

318. On December 13, 2000, after receiving instructions from his general manager and regional manager to reject the HMO terms and to attempt to finalize a PPO only contract, Jagmin replied to NTSP, agreeing to proceed with the PPO contract, and

## Initial Decision

stated to NTSP that "the physician expectations for the HMO contracts are not acceptable to Aetna and are rejected." (CX 580 at 1; see also CX 582 at 1; Jagmin, Tr. 1082-83).

319. On December 15, 2000, NTSP received Aetna's final proposed IPA agreement which repeated Aetna's position: "Per your discussion with Chris Jagmin, MD, non HMO based products to be paid at 140% of then current RBRVS per the Fort Worth, TX geographic locality. Anything with no established rate is paid at Company's then current Reasonable Equitable Fee Schedule (REF). Anesthesia services at \$ 40 per unit." (CX 660).

320. The conflict between NTSP and Aetna received publicity in the marketplace. (Jagmin, Tr. 1005-06, 1081-92). Aetna received calls from large employers in Tarrant County such as the Arlington independent school district and other employers and brokers. (Jagmin, Tr. 1083, 1094).

321. On December 18, 2000, Van Wagner reported to the NTSP Board that the PPO arrangement had been completed. Van Wagner referred the Board to a letter from Commissioner Montemayor concerning complaints that the Texas Department of Insurance had recently received from physicians. Van Wagner further "reported that NTSP will continue to negotiate with Celina Burns [General Manager] of Aetna on an HMO contract. There was a lengthy discussion on an acceptable fee schedule. The membership's response when polled was 125%. The Board instructed NTSP to present 125% on a direct contract." (CX 76 at 2-3).

322. Later on December 18, 2000, Van Wagner wrote to Aetna with a status update that reflected that NTSP's proposal was: for PPO, 140% of current Medicare RBRVS, anesthesia at \$ 45.00; for HMO, 125% of current Medicare RBRVS, anesthesia at \$ 43.00. (CX 585).

323. Ultimately, Aetna agreed to NTSP's terms. On December 19, 2000, Aetna wrote to NTSP and proposed: for PPO, 140% of current Medicare RBRVS, anesthesia at \$ 45.00; for HMO, 125% of current Medicare RBRVS, anesthesia at \$ 43.00. (CX 585 at 1).

Initial Decision

324. NTSP responded to Aetna on December 19, 2000, stating that NTSP would send out a notice to its member physicians notifying them that the PPO and HMO offers are within the messenger minimums. NTSP further informed Aetna that it would tell its member physicians that they could choose whether or not to participate in the offerings. (CX 589).

325. In Fax Alert # 85, sent to NTSP member physicians on December 19, 2000, NTSP notified its member physicians of the agreed upon rates and stated, "the rates agreed upon for the direct HMO reimbursement and the PPO reimbursement meet NTSP minimum messenger model standards as shared by our members. Because of this, the Board has accepted these reimbursement levels as appropriate in completing contractual discussions in regards to these products." (CX 586 at 10).

326. NTSP forwarded the NTSP-Aetna contract to its member physicians. (CX 597; CX 615 at 1; CX 611 at 2 ("NTSP is pleased to present two new NTSP contract offerings to all NTSP Members . . .")). Ultimately, 188 NTSP member physicians signed the NTSP-Aetna contract. (Jagmin, Tr. 1088).

327. The rates of the NTSP-Aetna contract are increased from Aetna's initial proposal. Compare Jagmin, Tr. 1015-16, 1022-24; CX 544 at 2, 3 (for HMO, aggregated to about 111% to 112% RBRVS, and anesthesia at \$ 40 per unit; for PPO, aggregated to about 123% to 125% RBRVS, and anesthesia at \$ 40 per unit) with CX 585 (for HMO, 125% RBRVS, and anesthesia at \$ 43 per unit; for PPO, 140% RBRVS, anesthesia at \$ 45 per unit).

328. The rates in the 2000 Aetna-NTSP contract were identical to the Aetna-MSM rates, a contract Aetna had with another IPA. (Jagmin, Tr. 1132-33; Van Wagner, Tr. 1697, 1701-02, 1708-09).

329. Aetna's representative, Roberts, testified that Aetna's reimbursement rates to NTSP were higher than rates for other IPAs for similar services. Roberts also testified that a straight comparison could not be easily made because it depends on the total package of services that an IPA or a physician group might bring to the discussions. (Roberts, Tr. 472-73).

## Initial Decision

330. On July 10, 2001, Vance's practice group recorded the following from their practice group's Board of Directors meeting:

Aetna is now offering a 95% of Medicare contracts for all commercial business. This contract was not presented to a solo practitioner, but to Texas Oncology, a very large corporate entity. This aggressive contracting by Aetna bodes ill for any small entities attempting to contract with Aetna this year. NTSP has been successful in negotiating decent rates from Aetna but only after threatening to term the entire NTSP network last year. As I have argued for a number of years, physicians divided will be cannon fodder in this business. The hope that the Cardiology IPA will protect us from these gorillas is unrealistic. Even a 700 doctor organization such as NTSP may make only a ripple in the water in the coming days but is much more effective than any other organization at this time. Without NTSP's influence this last two years, our market level of reimbursement would be significantly below its present level.

(CX 256).

**e. Subsequent contract negotiations**

331. On August 10, 2001, NTSP submitted to Aetna a non-risk contract proposal that would incorporate NTSP's medical management and utilization management functions. NTSP's clinical integration proposal incorporated the existing NTSP-Aetna rates (125% for HMO and 140% for PPO of then current Medicare RBRVS) and proposed a contract period of three years. (CX 616; Roberts, Tr. 472-73, 488, 508, 550-51, 560; Van Wagner, Tr. 1709-12).

332. On September 28, 2001, Aetna wrote to NTSP, stating Aetna's intention to continue discussions to finalize a mutually acceptable new agreement before the end of 2001, to commence



Initial Decision

on February 1, 2002. Aetna's letter terminated Aetna's existing agreement with NTSP, effective January 31, 2002. (CX 644, in camera; Roberts, Tr. 489-90).

333. The renegotiation between Aetna and NTSP involved only non-risk components. (Roberts, Tr. 487).

334. On October 8, 2001, the NTSP Board reviewed Aetna's termination letter and decided to continue negotiations with Aetna. (CX 102 at 1-3).

335. Van Wagner informed the Board that Aetna's new proposed rates would be lower and that negotiations would be arduous. (CX 102 at 1-3).

336. On October 15, 2001, the NTSP Board received and accepted the results of the 2001 annual poll. The acceptable contract minimums as established by the annual poll were 125% of current Medicare RBRVS for HMO and 140% of current Medicare RBRVS for PPO. The Board meeting minutes further reported: "this year's polling of NTSP members as per a messenger model indicates these levels have not changed. The Board accepted this information and instructed staff to use these levels as minimally acceptable fee schedules for HMO and PPO contract offers." (CX 103 at 4-5).

337. On October 29, 2001, NTSP shared the poll results with its member physicians at a general membership meeting at which member physicians also received an update on the ongoing Aetna negotiations. (CX 186).

338. On October 30, 2001, Aetna proposed to NTSP an "Aetna Market Based Fee Schedule. For PCPs and Specialists this is 85% / 115% for the HMO Based Plans and 95% / 129% for the Non-HMO Based Plans." Aetna's "market-based fee schedule" refers to a fee schedule that Aetna uses primarily for individual physicians, but is also used with some IPAs and some groups. (CX 629; Roberts, Tr. 492-93, 568).

339. The rates Aetna offered NTSP on October 30, 2001 were based off of then current Dallas RBRVS. The proposal also included a "steering incentive," a 10% increase to those rates, for physicians in certain speciality areas that steered outpatient

## Initial Decision

procedures to one of Aetna's preferred outpatient surgery centers. (CX 629; Roberts, Tr. 492-93, 568).

340. NTSP rejected Aetna's proposal of a 10% steering fee for some specialties because the reimbursement methodology would not be applied to all of NTSP's physicians. (Roberts, Tr. 523-24; Van Wagner, Tr. 1771).

341. NTSP never distributed Aetna's October 30, 2001 offer to its membership, lacking Board authority to do so. (Van Wagner, Tr. 1713-14; Roberts, Tr. 495).

**(i) NTSP's claims of efficiencies**

342. On November 1, 2001, NTSP sent utilization data to Aetna and in an attached letter advocated against a decrease in NTSP's then current fee schedule. NTSP stated: "although NTSP's current fee schedule is higher than that proposed by Aetna at the unit cost level, budget to actual PMPM [per member, per month] historical figures indicate that significant savings will accrue to Aetna given historical utilization patterns of NTSP physicians." (CX 553).

343. Aetna believed that it was "critical to [their] organization" to determine if NTSP's efficiency claims were valid. Aetna believed that, "if, in fact, there were efficiencies and we couldn't come to terms [with NTSP], then when those services went to other physicians in the marketplace, then the costs would actually go up . . . so it was critical to us [Aetna] that we do an in-depth review of this data and try to determine if there were efficiencies and, if there were, to make sure this contract continued." (Roberts, Tr. 497).

344. NTSP provided to Aetna data derived from NTSP's risk contract with PacifiCare, though NTSP did not provide the underlying data. (Van Wagner, Tr. 1911-14; Roberts, Tr. 506-07, 520-21, 578-79).

345. Aetna was not able to run an analysis of NTSP physicians compared to other physicians due to problems with Aetna's own data. (Roberts, Tr. 560-61).

Initial Decision

346. Due to the limited data provided by NTSP and deficiencies in Aetna's own internal data, Aetna could neither validate or invalidate NTSP's claims of clinical efficiencies. (Roberts, Tr. 504-05).

**(ii) No agreement on non-risk contract**

347. On November 6, 2001, Aetna informed NTSP that its analysis of Aetna's own data did not support NTSP's efficiencies claims. "In light of this review of our data, we can not identify significant management objectives that would require any adjustment to [the] proposed fee schedule." (CX 501; Roberts, Tr. 502-03, 524-27).

348. On November 7, 2001, NTSP replied that although negotiations would proceed, "to ask high performing physicians to take pay cuts because others have not done as well will be a difficult sell." NTSP also noted that Aetna would meet with the NTSP Board. (CX 502).

349. On November 12, 2001, Aetna representatives attended an NTSP Board meeting and addressed Aetna's proposal. Aetna offered an overall reimbursement average of 118% for the HMO product and 133% for the PPO contract. (CX 106). At that Board meeting, NTSP proposed a compromise between the parties at a rate level in the low 120s, which was below NTSP's offer of 125%, but above Aetna's offer of 118%. (Roberts, Tr. 537-39).

350. At the November 12, 2001 Board meeting, NTSP informed Aetna that NTSP had collected signed power of attorney forms from its member physicians. (Roberts, Tr. 540-41).

351. Following the November 12, 2001 Board meeting, NTSP did not distribute Aetna's offer to its member physicians because the offer was below Board minimums. (CX 503; Roberts, Tr. 542-43; Van Wagner, Tr. 1642-43, 1776; Deas, Tr. 2433).

352. On November 19, 2001, the Board reviewed Aetna's latest proposal to NTSP. Van Wagner reported that it was essentially the same proposal, which was less than the minimum rates that the membership had messengered as acceptable. (CX 107 at 2-3).

## Initial Decision

353. On December 3, 2001, Aetna wrote to NTSP informing it that Aetna believed that NTSP's current level of reimbursement was not competitive and that termination of the Aetna-NTSP agreement would be effective on January 31, 2002. (CX 640).

354. On December 7, 2001, NTSP informed its member physicians that Aetna's proposal fell "below payment rates our members have messengered to NTSP as acceptable to continue negotiations." NTSP informed its members that they may contract directly with Aetna or request that Aetna re-open negotiations with NTSP. (CX 643).

355. There is no current contract between NTSP and Aetna. (Roberts, Tr. 549; Van Wagner, Tr. 1718-19).

356. After terminating the contract, Aetna sent direct offers to NTSP's member physicians. NTSP's member physicians were not prevented from dealing directly with Aetna, and Aetna was able to contract directly with many of the physicians who had been part of the NTSP-Aetna contract. (Roberts, Tr. 544-46; RX 1076; RX 9).

**f. Aetna investigated by Department of Justice, Texas Attorney General, and Texas Department of Insurance**

357. In June 1999, the Department of Justice sued Aetna over its acquisition of Prudential Insurance Company of America as an attempt to gain improper market power over doctors. (RX 451; RX 3099). NTSP assisted the Department of Justice in that investigation. (RX 451). In December 1999, Aetna signed a consent order. (RX 3100).

358. In May 2000, the Department of Justice investigated Aetna's use of an all-product requirement in its contracts. NTSP was asked to and did assist in this investigation. (CX 57).

359. The Texas Commissioner of Insurance issued admonishment letters to Aetna in December 2000 and October 2001 questioning misrepresentations Aetna and MSM were making in contract discussions and questioning the adequacy of

Initial Decision

Aetna's provider network. (CX 586; RX 3105 (Aetna ordered to pay restitution and fines for violations through October of 2001); CX 508 (Aetna's response referencing Commissioner's letter)).

360. The Texas Attorney General issued an Assurance of Voluntary Compliance ("AVC") to Aetna in April 2000. (RX 1302; CX 505). Chris Jagmin, an Aetna medical director, was disciplined in August 2001 for violating the AVC by making false representations. (RX 339). NTSP was notified of the Assurance of Voluntary Compliance with Aetna and of Jagmin's disciplinary notice. (CX 103).

361. NTSP reported several payors, including Aetna, to the Texas Department of Insurance in 2000 and 2001 for prompt pay violations, noncompliance with contracts, and predatory pricing concerns. (Van Wagner, Tr. 1772).

362. In November 2001, the Texas Department of Insurance fined Aetna \$ 1.15 million and ordered it to pay restitution to providers for failing to follow Texas laws on prompt payment and clean claims. (RX 1660; RX 1666; RX 3105).

363. In 2002, NTSP made complaints about Aetna's contracting practices to the Texas Department of Insurance. NTSP also sent a complaint letter to Aetna, with a copy to the Texas Department of Insurance. (CX 507; CX 509; CX 512; CX 513; RX 2325).

## **F. No Valid Procompetitive Justifications**

### **1. No meaningful efficiencies**

364. NTSP is not clinically integrated for patients covered under NTSP's non-risk contracts. (Van Wagner, Tr. 1878; Casalino, Tr. 2877; Frech, Tr. 1351-52).

365. NTSP does not engage in case management for PPO patients covered under NTSP's non-risk contracts. (Van Wagner, Tr. 1878).

366. NTSP's medical director has no responsibility for controlling costs for patients covered under NTSP's non-risk contracts. (Deas, Tr. 2552-53).

## Initial Decision

367. NTSP's medical management committee does not evaluate the care of patients covered under NTSP's non-risk contracts. (Deas, Tr. 2550-51).

368. NTSP's hospital utilization management program does not apply to patients covered under NTSP's non-risk contracts. (Van Wagner, Tr. 1837-38).

369. NTSP's information systems do not include data for patients covered under NTSP's non-risk contracts. (Van Wagner, Tr. 1837-41; Deas, Tr. 2488). The absence of an electronic medical records system for its non-risk patients prevents NTSP from implementing an effective reminder system for patient care at the point of care. (Casalino, Tr. 2839).

370. NTSP does not operate or refer patients to any disease management programs or patient registries which would improve health care quality for patients with specific, long-term conditions such as diabetes or congestive heart failure for patients covered under NTSP's non-risk contracts. (Casalino, Tr. 2812-14; Van Wagner, Tr. 1834-35, 1877).

371. Disease management programs typically include a nurse case manager who maintains regular contact with each patient; monitors indices of each patient's health; ensures that each patient takes prescribed medications; directs each patient to specialist physicians; and encourages each patient to participate in relevant patient education programs. (Casalino, Tr. 2812-13).

372. NTSP does not provide feedback to physicians concerning patient care under NTSP's non-risk contracts. (Lonergan, Tr. 2722-24).

373. NTSP does not require adherence to its clinical guidelines and protocols for its fee-for-service physicians and patients. (Van Wagner, Tr. 1843-44). NTSP does not provide reminders to physicians at the point of care to employ the guidelines and protocols and does not monitor physicians' adherence to them. (Casalino, Tr. 2837-39; Van Wagner, Tr. 1843-44).

Initial Decision

374. NTSP's goal of enhanced teamwork among its physicians is hindered by the lack of pediatricians, obstetricians, and cardiologists in NTSP, forcing NTSP patients needing the services of these core specialists to seek physicians outside of NTSP. (Casalino, Tr. 2854-56).

375. NTSP does not engage in meaningful patient education. The patient education features of its web site were created in 2004, after this Complaint was issued, and are largely limited to links to other public web sites. (Casalino, Tr. 2844-48).

## **2. No significant spillover benefits**

376. NTSP engages in utilization and quality control efforts in connection with two health plan agreements: its risk contract with PacifiCare, and, to a lesser extent, its HMO contract, but not its PPO contract, with Cigna. (Van Wagner, Tr. 1830-54).

377. For an IPA to achieve significant "spillover" benefits from its shared-risk patients to its non-risk patients, it would need to apply organized processes to its non-risk patients. (Casalino, Tr. 2864-65).

378. NTSP is hindered in implementing organized processes for patients under non-risk contracts because it lacks data for these patients. (Casalino, Tr. 2868-69; Frech, Tr. 1352-53).

379. NTSP physicians who do not participate in NTSP's shared-risk contract are unlikely to learn and apply techniques to control costs and to improve quality that are developed or learned in the context of that risk-sharing arrangement. (Casalino, Tr. 2859-60; Frech, Tr. 1353-54).

380. Negotiation of rates in non-risk contracts is not necessary for any efficiencies achieved from NTSP's risk panel to spillover to NTSP's non-risk panel. (Deas, Tr. 2577 (asserted spillovers from NTSP's risk to fee-for-service contracts are "completely unrelated" to NTSP's setting of minimum contract prices); Frech, Tr. 1347-51 (any spillover is unrelated to setting of Board minimums and joint negotiation)).

Initial Decision

### III. ANALYSIS AND CONCLUSIONS OF LAW

#### A. Jurisdiction

The Complaint charges Respondent North Texas Specialty Physicians ("NTSP") with violating Section 5 of the Federal Trade Commission Act, as amended ("FTC Act"). 15 U.S.C. § 45. Section 5(a)(2) of the FTC Act gives the Commission jurisdiction "to prevent persons, partnerships, or corporations . . . from using unfair methods of competition in or affecting commerce . . ." 15 U.S.C. § 45(a)(2); *Kaiser Aluminum & Chem. Corp. v. FTC*, 652 F.2d 1324, 1327 n.2 (7th Cir. 1981). See also *McLain v. Real Estate Bd. of New Orleans, Inc.*, 444 U.S. 232, 241-42 (1980); *Hosp. Bldg. Co. v. Trs. of Rex Hosp.*, 425 U.S. 738, 745-46 (1976). The FTC Act defines "corporation" to include "any company, trust, so-called Massachusetts trust, or association, incorporated or unincorporated, which is organized to carry on business for its own profit or that of its members. . . ." 15 U.S.C. § 44. See also *Community Blood Bank v. FTC*, 405 F.2d 1011, 1015-16 (8th Cir. 1969). The FTC Act definition of commerce includes "commerce among the several States." 15 U.S.C. § 44.

The "Commission has only such jurisdiction as Congress has conferred upon it by the Federal Trade Commission Act." *Community Blood Bank*, 405 F.2d at 1015. When the jurisdiction of the Commission is challenged, the Commission bears the burden of establishing its jurisdiction. *Id.* Respondent has challenged jurisdiction in this case. Respondent's Post Trial Brief ("RPTB") at 33. To establish jurisdiction, Complaint Counsel must demonstrate that NTSP is an association organized to carry on business for its own profit or that of its members. *California Dental Ass'n v. FTC*, 526 U.S. 756, 767 (1999). Complaint Counsel must also demonstrate that the acts of NTSP are in or affect commerce. *McLain*, 444 U.S. at 242.

#### 1. Actions on behalf of members

NTSP is an independent practice association ("IPA") that was formed in 1995 for the purpose of allowing a group of specialist



Initial Decision

physicians to accept economic risk on medical contracts. F. 17, 37. NTSP subsequently broadened its membership to include primary care physicians ("PCPs") and broadened its functions to include entering into non-risk contracts with health insurance plans. F. 37. Physicians establish their relationship with NTSP by entering into a Physician Participation Agreement ("PPA") with NTSP and by paying a one time fee of \$ 1,000 to NTSP. F. 21, 64. Under the PPA, NTSP negotiates non-risk contracts on behalf of its participants. F. 65-67.

NTSP is incorporated under Texas law as a non-profit entity with no members. F. 17, 19; TEX. Occ. CODE ANN. § 162.001 (Vernon 2004). Respondent asserts, that as a matter of Texas corporation law, the participating physicians of NTSP are not "members." Thus, Respondent argues, because NTSP is a memberless organization, it falls outside the definition of a "corporation" under the FTC Act and outside the jurisdiction of the Federal Trade Commission. RPTB at 33.

However, courts and the Commission look to the substance, rather than the form of incorporation, in determining jurisdiction under the FTC Act. See *California Dental*, 526 U.S. at 767; *American Med. Ass'n v. FTC*, 638 F.2d 443, 448 (2nd Cir. 1980), *aff'd* by an equally divided court, without op., 455 U.S. 676 (1982). "The mere form of incorporation does not put [an entity] outside the jurisdiction of the Commission." *Community Blood Bank*, 405 F.2d at 1019.

The substance here, as shown by the evidence, is that NTSP's participating physicians are "members," as that word is used in the FTC Act's definition of corporation. The physicians pay dues, participate in association activities, and elect the Board of Directors. F. 21, 24, 33. They meet periodically in "general membership meetings" to discuss matters in the common interest of all physicians, which sometimes includes the negotiation of health plan contracts. F. 33, 42. NTSP refers to its physicians as "members" in its internal communications. For example, the Board or administrative staff of NTSP routinely sends communications to its member physicians called "Fax Alerts," which report on matters, including matters relating to the

## Initial Decision

business interests of the physicians, and are directed to "NTSP members." E.g., F. 86, 160, 282, 326 ("NTSP is pleased to present two new NTSP contract offerings to all NTSP Members . . .").

These facts demonstrate that NTSP's participating physicians are "members" of NTSP. Cf. *Fed. Election Comm'n v. Nat'l Right to Work Comm.*, 459 U.S. 197, 205-06 (1982) (In construing the term "member" as that term is used in the Federal Election Campaign Act, the Supreme Court held that solicitations to individuals who had previously donated to a non-profit corporation did not constitute solicitation to "members," where the alleged members did not play any part in the operation or administration of the corporation and did not elect corporate officials; where there were no membership meetings; and where alleged members did not exercise any control over the expenditures of their contributions.).

The evidence also shows that NTSP acts for the pecuniary benefit of its "members." As NTSP described in a Fax Alert to "NTSP members," under the Physician Participation Agreement, "NTSP will have the exclusive right, on behalf of its members, to receive all payor offers delivered to NTSP or its members." F. 65. As set forth in the PPA entered into between NTSP and its participating physicians, "NTSP is in the business of contracting with health maintenance organizations, health care networks and other payors to provide health care services through physicians and physician groups who have contracted with NTSP to provide such health care services" and "shall use its best efforts to market itself and its Participating Physicians to Payors and solicit Payor Offers for the provision of Covered Services by Participating Physicians." F. 20, 43. See also F. 44 ("NTSP was going to be a group of physicians that would bring a voice to organizing physicians who often practiced in individual groups to hopefully be able to secure contracts. . . . It was to represent physicians . . . in obtaining contracts from businesses or insurance companies or in dealing with hospitals."). NTSP's analysis of contract language, from both operational and legal perspectives, and communications with payors about the terms of contracts constitutes benefits undertaken on behalf of NTSP's member physicians. F. 45.

Initial Decision

Further illustrating pecuniary benefits, in communications to its member physicians, NTSP has expressed satisfaction about its success in negotiating the fees to be paid to its member physicians. For example, an October 9, 2000 "Open Letter to the Membership" from Dr. Vance (then President of NTSP) notes that NTSP "started in an attempt to provide a seat at the table of medical business for the individual specialty physicians in Fort Worth," and reports that "NTSP has provided a consistent premium fee-for-service reimbursement to the members." F. 44.

The evidence shows that NTSP has negotiated fees on behalf of its member physicians under non-risk contracts with health plans, in the course of which it sought increased reimbursement rates or more favorable coverage terms for its member physicians. *Infra* III.D.2. Negotiation of the level of fees that member physicians of NTSP receive for services provided by their own profit-making physician practices has an effect on the revenues and incomes of the member physicians and thus inures an economic benefit to NTSP's member physicians.

The jurisdiction of the Federal Trade Commission extends to non-profit entities when a substantial part of the entity's total activities provides economic benefits for its members. *California Dental*, 526 U.S. at 767; *In re American Med. Ass'n*, 94 F.T.C. 701, 994 (1979). As summarized above, NTSP's activities provide pecuniary benefits for its member physicians.

## **2. Interstate commerce**

In addition, NTSP's activities are in or affect commerce, as required by the FTC Act. 15 U.S.C. § 45 (prohibiting unfair methods of competition "in or affecting commerce"). The jurisdiction of the Commission encompasses acts and practices constituting a violation of the Sherman Act. *FTC v. Cement Inst.*, 333 U.S. 683, 690 (1948). The Commission utilizes cases interpreting jurisdiction under the Sherman Act - which regulates agreements "in restraint of trade or commerce among the several States" - in analyzing its own jurisdiction. E.g., *In re Indiana*

## Initial Decision

Fed'n of Dentists, 101 F.T.C. 57, 161 (1983), rev'd on other grounds, 745 F.2d 1124 (7th Cir. 1984), rev'd, 476 U.S. 447 (1986).

The jurisdictional reach of the Sherman Act (and, thus, the FTC Act), "is coextensive with the broad-ranging power of Congress under the Commerce Clause." *Chatham Condo. Ass'n v. Century Village, Inc.*, 597 F.2d 1002, 1007 (5th Cir. 1979) (citing *Burke v. Ford*, 389 U.S. 320, 321-22 (1967) ("When competition is reduced, prices increase and unit sales decrease . . . . Thus, the state-wide wholesalers' market division inevitably affected interstate commerce.")).

For purposes of establishing antitrust jurisdiction, actions are in or affect commerce if the government demonstrates "a substantial effect on interstate commerce generated by respondents' . . . activity. Petitioners need not make the more particularized showing of an effect on interstate commerce to fix . . . rates, or by those other aspects of respondents' activities that are alleged to be unlawful." *McLain*, 444 U.S. at 242-43. Alternatively, the Supreme Court has stated that to establish federal jurisdiction, "there remains only the requirement that respondents' activities which allegedly have been infected by a price-fixing conspiracy be shown 'as a matter of practical economics' to have a not insubstantial effect on the interstate commerce involved." *Id.* at 246 (quoting *Rex Hosp.*, 425 U.S. at 745).

Although the term used in evaluating the effect on interstate commerce is "substantial" or "not insubstantial," Supreme Court precedent makes clear that an effect on commerce can be viewed as "substantial" even though "its impact on interstate commerce falls short of causing enterprises to fold or affecting market price." *Rex Hosp.*, 425 U.S. at 745. Further, "wholly local business restraints can produce the effects condemned by the Sherman Act." *Id.* at 743 (citations omitted).

For example, in *Rex Hospital*, a small proprietary hospital, Mary Elizabeth, brought suit against another hospital, Rex, under Sections 1 and 2 of the Sherman Act, alleging that Rex had conspired with others to block the expansion and relocation of

Initial Decision

Mary Elizabeth within Raleigh, North Carolina. The Court found an effect on interstate commerce based upon the allegations in the complaint that the blocked expansion of Mary Elizabeth would cause the following reverberations in commerce: a reduction in the amount of medicine and supplies purchased from out-of-state sellers; diminished revenues from out-of-state insurance companies or the federal government; a decrease in the management service fee paid to its parent company, an out-of-state corporation; and lost revenues to out-of-state lenders who were expected to finance the planned expansion. 425 U.S. at 744.

In *McLain*, the Supreme Court considered the effects on commerce of an alleged conspiracy by real estate brokers to fix brokerage rates in New Orleans. The Supreme Court held that the jurisdictional requirement was satisfied by allegations that the conspiracy affected both the sale of real estate to interstate buyers and the financing of those sales by interstate lenders. 444 U.S. at 245. Although noting that such a conspiracy would probably have an effect on "the frequency and terms of residential sales transactions," *id.* at 246, the Supreme Court did not require the plaintiff to demonstrate or allege any particular effect on the overall flow of realty-related commerce into the state. Instead, the Supreme Court explained that jurisdiction would not be defeated "by plaintiff's failure to quantify the adverse impact of defendant's conduct." *Id.* at 243. See also *Goldfarb v. Virginia State Bar*, 421 U.S. 773, 785 (1975) ("once an effect is shown, no specific magnitude need be proved").

Furthermore, "in cases involving horizontal agreements to fix prices or allocate territories within a single State, [the Supreme Court has] based jurisdiction on a general conclusion that the defendants' agreement 'almost surely' had a marketwide impact and therefore an effect on interstate commerce." *Summit Health, Ltd. v. Pinhas*, 500 U.S. 322, 331 (1991) (quoting *Burke*, 389 U.S. at 322). In *Summit Health*, the market that was impacted was "the Los Angeles market." *Id.* "In *Burke*, the Supreme Court was willing to assume an effect on interstate commerce where the conduct in question, horizontal market divisions, typically has an anticompetitive effect on interstate commerce." *Chatham Condo.*, 597 F.2d at 1007 (citation omitted).

## Initial Decision

In addition, the government "need not allege, or prove an actual effect on interstate commerce to support federal jurisdiction." *Summit Health*, 500 U.S. at 331. Though not required to prove an actual effect on interstate commerce to support federal jurisdiction, in this case, as summarized in Section III.D.2., *infra*, Complaint Counsel has demonstrated that NTSP negotiated economic terms of non-risk contracts with health insurance payors. These health insurance payors, United Healthcare ("United"), Cigna Healthcare ("Cigna"), and Aetna Health, Inc. ("Aetna"), are all national health plans, headquartered outside of Texas, that sell health care products throughout the United States. F. 101-03, 195, 197, 259, 262. As such, the health insurance providers' businesses are in interstate commerce. *Indiana Fed'n of Dentists*, 101 F.T.C. at 161. n1 Any increase in fees for physician services paid to physicians, on whose behalf NTSP negotiated increased rates, affects these multi-state companies. F. 102, 104, 196-98, 263-64.

n1 The Commission's holding that the respondent's anticompetitive activity had a substantial effect upon interstate commerce and, thus, that the Commission had jurisdiction over the complaint was not appealed by the respondent. *Indiana Federation of Dentists v. FTC*, 745 F.2d 1124, 1132 (7th Cir. 1984).

"When determining whether interstate commerce is affected by an alleged violation courts will often examine both the defendant's relationship with interstate markets and the plaintiff's." *Construction Aggregate Transport, Inc. v. Florida Rock Indus., Inc.*, 710 F.2d 752 (11th Cir. 1983) (citing *Rex Hosp.*, 425 U.S. at 741 (local actions by defendants to block relocation of hospital adversely affects interstate commerce with regard to medicines and supplies purchased by plaintiff hospital)); *Lehrman v. Gulf Oil Corp.*, 464 F.2d 26, 34-35 (5th Cir. 1972) (demise of plaintiff's business had impact on interstate flow of goods he would have sold) (alternative holding); *Heille v. City of St. Paul*, 671 F.2d 1134, 1137 (8th Cir. 1982) (examining both plaintiff's and defendant's use of goods manufactured out-of-state) (other citations omitted)).

Initial Decision

The Complaint in this case was brought by the Federal Trade Commission, and not by the insurance companies. However, the allegations of the Complaint focused on, and the evidence demonstrated, higher rates paid by the insurance companies. Higher rates and more favorable contract terms directly affect these multi-state companies. See F. 102, 104, 196-98, 263-64.

Purchases by a defendant of out-of-state goods are also a factor in determining whether an activity substantially affects interstate commerce. E.g., *Rex Hosp.*, 425 U.S. at 744 (petitioner's purchases of out-of-state medicines and supplies considered in determining "substantial effect" on interstate commerce); *Miller v. Indiana Hosp.*, 843 F.2d 139, 144 n.5 (3rd Cir. 1988) (defendant hospital's treatment of out-of-state patients, purchase of medical supplies from out-of-state, and receipt of money from out-of-state, including federal funds, satisfies the requirement of affecting interstate commerce); *Oksanen v. Page Mem. Hosp.*, 945 F.2d 696 (4th Cir. 1991) (same). See also *United States v. Robertson*, 514 U.S. 669, 672 (1995) ("[A] corporation is generally 'engaged "in commerce"' when it is itself 'directly engaged in the production, distribution, or acquisition of goods or services in interstate commerce.'" (per curiam) (quoting *United States v. Am. Bldg. Maint. Indust.*, 422 U.S. 271, 283 (1975))).

From January 1, 1999 to December 22, 2003, NTSP purchased \$ 1,047,819.86 from vendors with billing addresses outside of Texas. F. 22. For example, NTSP purchased \$ 457,373.09 of stop loss insurance from a California insurance broker. F. 22. These purchases from out-of-state sources illustrate that NTSP is directly engaged in the acquisition of goods or services in interstate commerce. This factor, together with the impact of NTSP's negotiation of rates and economic terms paid by multi-state insurance companies, demonstrates that NTSP's activities substantially affect commerce.

## Initial Decision

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

**B. Burden of Proof**

Under Commission Rule of Practice 3.51(c)(1), "an initial decision shall be based on a consideration of the whole record relevant to the issues decided, and shall be supported by reliable and probative evidence." 16 C.F.R. § 3.51(c)(1). The Commission amended its Rules of Practice, effective May 18, 2001. FTC Rules of Practice, Interim rules with request for comments, 66 Fed. Reg. 17,622 (April 3, 2001). Through the amendments, the Commission removed the requirement of Rule 3.51(c)(3) that the initial decision of an Administrative Law Judge ("ALJ") be supported by "substantial" evidence. 66 Fed. Reg. at 17,626. The Administrative Procedure Act, however, requires that an ALJ may not issue an order "except on consideration of the whole record or those parts thereof cited by a party and supported by and in accordance with the reliable, probative, and substantial evidence." Administrative Procedure Act ("APA") 5 U.S.C. § 556(d). According to Black's Law Dictionary, "probative evidence" means having the effect of proof; tending to prove, or actually proving an issue. "Substantial evidence" is defined in Black's Law Dictionary as such evidence that a reasonable mind might accept as adequate to support a conclusion. At the adjudicative level of these proceedings, any difference between "probative" evidence and "substantial" evidence is not dispositive under these standards. Therefore, all findings of fact in this Initial Decision are supported by reliable, probative, and substantial evidence.

The parties' burdens of proof are governed by Commission Rule 3.43(a), Section 556(d) of the APA, and case law. FTC Rules of Practice, Interim rules with request for comments, 66 Fed. Reg. 17,622, 17,626 (April 3, 2001). Pursuant to Commission Rule 3.43(a), "counsel representing the Commission . . . shall have the burden of proof, but the proponent of any



Initial Decision

factual proposition shall be required to sustain the burden of proof with respect thereto." 16 C.F.R. § 3.43(a). Under the APA, "except as otherwise provided by statute, the proponent of a rule or order has the burden of proof." 5 U.S.C. § 556(d). See also *Steadman v. SEC*, 450 U.S. 91, 102 (1981) (APA establishes preponderance of the evidence standard of proof for formal administrative adjudicatory proceedings).

The government bears the burden of establishing a violation of antitrust law. *United States v. E.I. duPont de Nemours & Co.*, 366 U.S. 316, 334 (1961). "The antitrust plaintiff must present evidence sufficient to carry its burden of proving that there was [an anticompetitive] agreement." *Monsanto Co. v. Spray-Rite Serv. Corp.*, 465 U.S. 752, 763 (1984). Accordingly, Complaint Counsel bears the burden of demonstrating that Respondent's actions in this case are anticompetitive.

### **C. Relevant Market**

The relevant market has two components, a geographic market and a product market. *H.J., Inc. v. Int'l Tel. & Tel.*, 867 F.2d 1531, 1537 (8th Cir. 1989). Even in a horizontal price fixing case analyzed under the per se rule, the relevant market must be defined. *Bogan v. Hodgkins*, 166 F.3d 509, 515 (2d Cir. 1999) ("It is an element of a per se case to describe the relevant market in which we may presume the anticompetitive effect would occur."); *Double D Spotting Serv., Inc. v. Supervalu, Inc.*, 136 F.3d 554, 558-59 (8th Cir. 1998) ("[A] plaintiff alleging a horizontal restraint must at least define the market and its participants.").

The relevant geographic market is the region "in which the seller operates, and to which the purchaser can practicably turn for supplies." *Tampa Elec. Co. v. Nashville Coal Co.*, 365 U.S. 320, 327 (1961). The relevant product or service market is "composed of products that have reasonable interchangeability for the purposes for which they are produced - price, use and qualities considered." *United States v. E.I. du Pont de Nemours & Co.*, 351

## Initial Decision

U.S. 377, 404 (1956); *Eastman Kodak Co. v. Image Technical Services, Inc.*, 504 U.S. 451, 481-82 (1992) (relevant market determined by the choices of products or services available to consumers).

Complaint Counsel argues "that it is unnecessary to define markets or assess market power when conduct is clearly anticompetitive, especially if (as here) there is direct evidence of actual anticompetitive effects (higher prices) as a result of the conduct." Complaint Counsel's Post Trial Reply Brief ("CCPTRB") at 13-14. Cases relied upon by Complaint Counsel hold that market power need not be demonstrated or that anticompetitive effects in the market need not be proved. However, these cases do not hold that the market need not be defined. E.g., *Todd v. Exxon Corp.*, 275 F.3d 191, 206 (2d Cir. 2001) (finding first that plaintiff has adequately defined the market before holding that "actual adverse effect on competition . . . arguably is more direct evidence of market power than calculations of elusive market share figures") (emphasis added); *Re/Max Int'l, Inc. v. Realty One, Inc.*, 173 F.3d 995, 1018 (6th Cir. 1999) ("an antitrust plaintiff is not required to rely on indirect evidence of a defendant's monopoly power, such as high market share within a defined market, when there is direct evidence that the defendant has actually set prices or excluded competition") (emphasis added). As Complaint Counsel stated in its brief, "in *Polygram Holding*, the Commission held that it was not necessary to examine evidence of respondent's market power, such as a high market share within a defined market, where there is direct evidence of price-fixing among competitors." CCPTRB at 14 (citing *In re Polygram Holding, Inc.*, 2003 FTC LEXIS 120, at \*45 n.26 (July 24, 2003) (emphasis added). Market definition and market power are different issues. No one can dispute, with any credibility, that the necessity to first define a market is the same thing as a requirement to demonstrate power within that already defined market.

Complaint Counsel's expert, Dr. Harry Edward Frech, did not attempt to prove a relevant market. Dr. Frech's testimony on this point could not be more clear:

Initial Decision

Q. And by the way, you're not positing any relevant market in this case, isn't that correct?

A. That's correct.

Frech, Tr. 1393-94. Fortuitously for Complaint Counsel, despite its misguided belief that the market need not be defined, evidence introduced at trial demonstrates that the relevant market in this case is physician services available to patients in Fort Worth, Texas (the "Fort Worth area"). See F. 52-63.

The evidence shows that primary care physicians and specialists from the Fort Worth area are important to health insurers, employers, and consumers. F. 52-62. In contracting for health plan services, Fort Worth employers demand significant coverage by physicians who practice in Fort Worth and who admit patients to Fort Worth hospitals. F. 52, 54.

Representatives from health insurance plans testified that they would not be able to effectively market their products to Fort Worth employers without a sufficient number of Fort Worth physicians covering various fields of practice in their network. F. 53. One health insurance plan conducted an independent analysis of the importance of NTSP physicians to its Fort Worth area health plan. This analysis revealed that, without NTSP physicians, there would be substantial coverage holes in the Fort Worth area in several areas of specialization. F. 62.

Health plans would not substitute physicians whose services are available in other areas such as Dallas County or the Mid-Cities area to avoid a small but significant Fort Worth area price increase. F. 58. Representatives from health insurance plans also testified that, even if the price of Fort Worth area physician services increased by five percent or greater, they would still need to have various kinds of Fort Worth area physicians included in their health plans to serve Fort Worth employers and consumers. F. 60.

NTSP has approximately 480 participating member physicians, the majority of whom are specialists. F. 32. The vast majority of NTSP physicians are located in the Fort Worth area of

## Initial Decision

Tarrant County, Texas. F. 31. NTSP physicians are a significant presence in the Fort Worth area. F. 61. NTSP physicians make up a large percentage of Tarrant County practitioners in many medical specialties: pulmonary disease (80 percent); cardiovascular disease (59 percent); and urology (69 percent). F. 61. NTSP has stated that a health plan attempting to serve the employees of the City of Fort Worth "would not be able to satisfy employer/employee match or network access standards without NTSP physicians participating in the network." F. 63.

Accordingly, the evidence establishes that the relevant market is physician services available to patients in the Fort Worth area.

**D. Horizontal Agreement**

The FTC Act's prohibition of unfair methods of competition encompasses violations of Section 1 of the Sherman Act, which prohibits agreements in restraint of trade. *California Dental*, 526 U.S. at 762 n.3. The Commission relies on Sherman Act law in adjudicating cases alleging unfair competition. *FTC v. Indiana Fed'n of Dentists*, 476 U.S. 447, 451-52 (1986); *In re California Dental Ass'n*, 121 F.T.C. 190, 292 n.5 (1996).

Section 1 of the Sherman Act prohibits "every contract, combination in the form of trust or otherwise, or conspiracy, in restraint of trade or commerce among the several States, or with foreign nations . . ." 15 U.S.C. § 1. The ban on contracts in restraint of trade extends only to unreasonable restraints of trade, i.e., restraints that impair competition. *State Oil Co. v. Khan*, 522 U.S. 3, 10 (1997); *Chicago Bd. of Trade v. United States*, 246 U.S. 231, 238 (1918).

To determine whether Complaint Counsel has established that Respondent's actions violate Section 5 of the FTC Act or Section 1 of the Sherman Act, the critical questions are: (1) whether there was a contract, combination, or conspiracy; and, if so, (2) whether the contract, combination, or conspiracy unreasonably restrained trade.

Initial Decision

## **1. Whether there was a contract, combination, or conspiracy**

### **a. Summary of facts**

One of NTSP's functions is to messenger to its member physicians the offers that NTSP receives from health insurance providers of fee-for-service, non-risk contracts ("non-risk contracts"). F. 44. NTSP enters into a Physician Participation Agreement ("PPA") with its member physicians. F. 64. The PPA grants NTSP the right to receive all payor offers and imposes on the member physicians a duty to promptly forward those offers to NTSP. F. 65. The PPA also grants NTSP a right of first negotiation with health care payors, with each physician agreeing that he or she will refrain from pursuing offers from a health plan until NTSP notifies him or her that NTSP is discontinuing negotiations with the health plan. F. 65-66. (CX 275 at 24 ("NTSP shall have the right to receive all Payor Offers made to NTSP or Physician . . . If Physician receives a Payor Offer, . . . Physician will promptly forward such Payor Offer to NTSP for further handling in accordance with the provisions of this Agreement.")).

The Board of Directors of NTSP ("Board") decides whether to send non-risk contract offers to its member physicians based on "Board minimums." F. 83. Board minimums are minimum rates established through NTSP's polling of its member physicians to determine what each physician believes are acceptable fees for non-risk contracts. F. 84, 87. (E.g., CX 1196 ("Every year the Board asks the members to tell them what they consider to be appropriate reimbursement. . . . Once a year we poll the members and get that information from them.")). NTSP's polling form asks each physician to disclose the minimum price that he or she would accept to provide medical services pursuant to a fee-for-service HMO or PPO agreement. F. 89. NTSP collects the results and calculates the mean, median, and mode ("averages") of the minimum acceptable fees. F. 93. NTSP then sends to its member physicians "Fax Alerts," that communicate to NTSP physicians the minimally acceptable fee schedules for non-risk health plan contracts. F. 94, 98, 84 (Fax Alert from NTSP to its member physicians informing them of the results of that year's poll and stating that NTSP "utilizes these minimums when negotiating

## Initial Decision

managed care contracts on behalf of its participants"). If a non-risk contract offer falls below the minimally acceptable fee schedule, NTSP, on behalf of its member physicians, rejects the offer by determining to not messenger the offer to its member physicians. F. 68, 83.

NTSP cannot and does not bind any member physician to non-risk contracts. F. 71. The PPA gives NTSP no authority to bind physicians. F. 67. Any non-risk contracts which NTSP has decided to accept are messengered by NTSP to NTSP's physicians for their individual decisions on whether or not to join. See F. 71, 72. E.g., F. 189, 326-27.

In the process of negotiations for the provision of physician services under health plans with United Healthcare ("United") and with Aetna Health, Inc. ("Aetna"), NTSP has solicited and obtained powers of attorney from its member physicians, giving NTSP the legal authority to negotiate non-risk contracts with those health plans on behalf of NTSP's member physicians. F. 76-77, 160-61, 302-04. In the process of negotiations with Cigna Healthcare ("Cigna"), NTSP requested that its member physicians sign an authorization form to allow NTSP to serve as its physicians' agent. F. 80, 205.

NTSP has encouraged its physicians to abstain from negotiating direct contracts with health plans and to refer any health plans' offers to NTSP staff in accordance with their participation agreements. F. 78, 168. NTSP's physicians have referred health plans attempting to contract directly with them back to NTSP, with the knowledge that NTSP would reject offers below Board minimum rates. F. 81. Cigna, for example, received forty virtually identical letters from physicians directing Cigna to contact NTSP, rather than the physicians, because NTSP was acting as the physicians' agent in negotiating the non-risk sharing contract in question. F. 206. When United approached individual physicians to offer direct contracts, United was also referred to NTSP. F. 173.

Initial Decision

### **b. Summary of parties' positions**

Complaint Counsel argues that the mere existence of NTSP is a combination that satisfies the combination requirement of Section 1 of the Sherman Act. Complaint Counsel's Post Trial Brief ("CCPTB") at 51 (citing *Alvord-Polk, Inc. v. Schumacher & Co.*, 37 F.3d 996, 1009 n.11 (3d Cir. 1994) ("There is . . . authority for the proposition that a trade association, in and of itself, is a unit of joint action sufficient to constitute a section 1 combination.")). Complaint Counsel further asserts that the evidence - that NTSP polled and disseminated averaged data on future prices; that NTSP set minimum rates for contracting with health plans based on this data; and that NTSP collected powers of attorney from member physicians - demonstrates that NTSP entered into a "contract, combination or conspiracy" to implement and enforce price and related agreements. CCPTB at 59-60.

Respondent argues that NTSP, as a single entity, is incapable of colluding with itself. Respondent's Post Trial Reply Brief ("RPTRB") at 7-8. Respondent further asserts that, under the Colgate doctrine, NTSP has the legal right to refuse to sign and messenger to its member physicians contractual offers that are outside NTSP's business model. RPTB at 18, 22 (citing *United States v. Colgate & Co.*, 250 U.S. 300, 307 (1919)).

### **c. Analysis**

#### **(i) Concerted action must be demonstrated**

To establish a violation of Section 1 of the Sherman Act, a plaintiff must demonstrate concerted action. *Viazis v. Am. Ass'n of Orthodontists*, 314 F.3d 758, 761 (5th Cir. 2002). "The term 'concerted action' is often used as shorthand for any form of activity meeting the section 1 'contract, combination or conspiracy' requirement." *Alvord-Polk*, 37 F.3d at 999 n.1.

In *Viazis*, the Court of Appeals for the Fifth Circuit held, "despite the fact that 'a trade association by its nature involves collective action by competitors, it is not by its nature a 'walking conspiracy', its every denial of some benefit amounting to an unreasonable restraint of trade.'" 314 F.3d at 764 (quoting

## Initial Decision

Consolidated Metal Prod., Inc. v. Am. Petroleum Inst., 846 F.2d 284, 293-94 (5th Cir. 1988)). Simply because NTSP is an organization of otherwise competing physicians does not mean that the concerted action requirement of Section 1 of the Sherman Act has automatically been satisfied. Indeed, in *Alvord-Polk*, the case relied upon by Complaint Counsel, the Court of Appeals for the Third Circuit held, "concerted action does not exist every time a trade association member speaks or acts. Instead, in assessing whether a trade association (or any other group of competitors) has taken concerted action, a court must examine all the facts and circumstances to determine whether the action taken was the result of some agreement, tacit or otherwise, among members of the association." 37 F.3d at 1007-08.

**(ii) Agreement under Maricopa**

In *Arizona v. Maricopa Co. Med. Soc'y*, 457 U.S. 332, 356-57 (1982), the complaint challenged agreements among competing physicians, who were members of medical societies or medical foundations, that set, by majority vote, the maximum fees that the physicians could claim in full payment for services to policyholders of specific health insurance plans approved by the foundations. While the Supreme Court's opinion provides little detail on the challenged agreements, more detail is available in the lower court decisions. As described by the Court of Appeals, "the challenged conduct is the setting by majority vote of maximum fees that physician members may claim in full payment for health services they provide to policyholders of [certain] approved insurance plans." *Arizona v. Maricopa Co. Med. Soc'y*, 643 F.2d 553, 554 (9th Cir. 1980), rev'd on other grounds, 457 U.S. 332 (1982). Further, the Court of Appeals noted that the foundations' "activities include polling their members from time to time to set upper limits on fees they may charge patients covered by insurance plans the [medical societies] approve." *Id.* at 554-55. At the district court level, the court found, "it is undisputed that the foundations set the maximum amount to be paid [to] physicians who agree to provide services to patients who are enrolled in insurance plans approved by the foundations. It is further undisputed that the doctors who agree to participate in the



Initial Decision

foundation-approved plans are free to set the prices they charge their patients." *Arizona v. Maricopa Co. Med. Soc'y*, 1979 U.S. Dist. LEXIS 11918, at \*2 (D. Az. 1979), *aff'd*, 643 F.2d 553 (9th Cir. 1980), *rev'd on other grounds*, 457 U.S. 332 (1982). As described by the Courts of Appeals for the Fourth Circuit and for the Ninth Circuit, the illegal agreements in Maricopa were the agreements by the participating physicians to accept set amounts that had been determined by the foundations as fees in payment for physician services to policyholders. *Ratino v. Med. Serv.*, 718 F.2d 1260, 1270 (4th Cir. 1983); *Hahn v. Oregon Physicians' Serv.*, 868 F.2d 1022, 1027 (9th Cir. 1988).

The Supreme Court in Maricopa found these agreements to be a "combination . . . [that] permitted [the physicians] to sell their services to certain customers at fixed prices and arguably to affect the prevailing market price of medical care." 457 U.S. at 356. Thus, the Supreme Court found concerted action without finding that the competing physicians agreed directly with each other to set prices and even where the participating physicians were free to set their own prices. See *id.* In so holding, the Supreme Court noted that the rule against price fixing "is violated by a price restraint that tends to provide the same economic rewards to all practitioners regardless of their skill, their experience, their training, or their willingness to employ innovative and difficult procedures in individual cases." *Id.* at 348.

In this case, there is no evidence that one or more of the member physicians agreed with each other to reject a non-risk payor offer; there is no evidence that one or more of the member physicians consulted with each other when responding to polls or making decisions on non-risk payor contracts; and, there is no evidence that any member physician knew what another physician was going to do in response to a non-risk payor offer. F. 73-75. However, Maricopa does not require such evidence.

The evidence in this case does establish that Respondent entered into agreements with physicians to negotiate non-risk contracts on behalf of those physicians and that physicians agreed to accept the rates of the non-risk contracts entered into between NTSP and health care payors. F. 44, 51, 64, 191, 326. Respondent

## Initial Decision

argues that NTSP physicians at times signed contracts with certain health plans, individually or through other physician groups, at rates different than those agreed to by NTSP. RPTB at 19. However, a price fixing conspiracy need not be perfect or complete in order to be unlawful. In re High Fructose Corn Syrup Antitrust Litig., 295 F.3d 651, 656 (7th Cir. 2002) ("An agreement to fix list prices is . . . a per se violation of the Sherman Act even if most or for that matter all transactions occur at lower prices.").

The evidence further establishes that the physicians, who are otherwise competitors of each other (F. 35-36), provided to NTSP the minimum prices that each physician or physician group would be willing to accept on a non-risk contract specifically for NTSP's use in negotiating the economic terms of non-risk contracts. F. 87-90, 96-98, 155-59, 308-16. E.g., F. 88 ("NTSP polls its affiliates and membership to establish Contracted Minimums. NTSP then utilizes these minimums when negotiating managed care contracts on behalf of its participants."). And, the evidence establishes that NTSP used this price information to obtain more favorable rates or contract terms from health insurance payors than the payors initially offered. F. 44, 170-90, 317-30. This behavior satisfies the concerted action requirement under Maricopa.

In addition, the evidence establishes that NTSP sought a uniform rate for all of its specialties, regardless of the supply or demand for specific specialty services in the market. F. 291, 293, 340. This behavior is contrary to the Supreme Court's finding in Maricopa that the rule against price fixing was violated by a price restraint that tended to provide the same economic rewards to all practitioners, regardless of skill or experience. Maricopa, 457 U.S. at 348.

The challenged concerted action in this case is similar to the agreement challenged in *Hassan v. Indep. Practice Assoc., P.C.*, 698 F. Supp. 679 (E.D. Mich. 1988). In *Hassan*, an organization of physicians and osteopaths set a maximum fee schedule that was initially based on schedules submitted by members, as well as information about fees in areas in which the organization did not

Initial Decision

operate. *Id.* at 681-82. The court concluded that, where the association and the board of directors which set the fees were made up of physicians or osteopaths, health care providers set the fee reimbursement and that, under Maricopa, there was an agreement between competitors. *Id.* at 687.

If, as in Maricopa, it is unlawful for competing physicians to set maximum prices, then, for even stronger reason, it is unlawful for competing physicians to set, through NTSP, minimum prices. See *United States v. Socony-Vacuum Oil Co., Inc.*, 310 U.S. 150, 223 (1940) ("Under the Sherman Act a combination formed for the purpose and with the effect of raising, depressing, fixing, pegging, or stabilizing the price of a commodity in interstate or foreign commerce is illegal *per se.*").

**(iii) Actions on behalf of members**

Respondent asserts that NTSP is a single entity, incapable of colluding with itself. RPTRB at 7-8. "It is not sufficient to assert, as defendants do, that a corporation cannot conspire with itself. We must look at substance rather than form." *Virginia Academy of Clinical Psychologists v. Blue Shield of Virginia*, 624 F.2d 476, 480, 481 (4th Cir. 1980) (finding action in concert where "in a real and legal sense, [defendants] are agents of their member physicians"). The substance here is that NTSP, in negotiating economic terms of non-risk contracts, did so for the pecuniary benefit of its member physicians. *Supra* III.A.1. E.g., F. 84 (NTSP utilizes these minimums determined by polls "when negotiating managed care contracts on behalf of its participants.") (emphasis added).

Respondent is an association of individual competing physicians who have not integrated their medical practices and who have separate and distinct economic interests. F. 18, 35. Where "each doctor practices medicine in his or her own individual capacity[,] each is a 'separate economic entity potentially in competition with other physicians.'" *Capital Imaging Associates, P.C. v. Mohawk Valley Med. Ass'n, Inc.*, 996 F.2d 537, 544 (2nd Cir. 1993) (quoting *Bolt v. Halifax Hosp. Med. Ctr.*, 891 F.2d 810, 819 (11th Cir. 1990)). See also *Oregon*

## Initial Decision

Physicians' Serv., 868 F.2d at 1024, 1030 (denying summary judgment where plaintiff produced sufficient evidence to permit a trier of fact to conclude that an organization founded by physicians that offered and administered a prepaid health care plan was an organization of physicians or an agent of its member physicians and may have acted for the anticompetitive interests of its member physicians).

Respondent not only is an entity composed of physicians, it is managed by a Board composed of eight physicians, elected by physicians. F. 23-24. Physician control of NTSP further undermines Respondent's argument that NTSP is a single entity with a unity of purpose. Virginia Academy of Clinical Psychologists, 624 F.2d at 481 (physician control of prepaid health care plans sufficient to bring its actions within the purview of Section 1 of the Sherman Act). See also Addino v. Genesee Valley Med. Care, Inc., 593 F. Supp. 892, 894, 896-97 (W.D.N.Y. 1984) (where board of non-profit corporation composed of half physicians and half laypersons approved all proposed rates for physician services, plaintiffs' allegation that defendant was merely a vehicle for the member physicians to fix prices was held to be more than sufficient to state a claim of conspiracy between and among defendant's member physicians); cf. Barry v. Blue Cross of California, 805 F.2d 866, 869 (9th Cir. 1986) (where plaintiffs failed to produce any evidence of physician control of the price-setting entity, court upheld the agreement as to prices and reimbursement).

Accordingly, NTSP is not a single entity with a "complete unity of purpose," incapable of conspiring with itself. See Copperweld Corp. v. Independence Tube Corp., 467 U.S. 752, 772 (1984) (no concerted action where a parent company and wholly owned subsidiary had a "unity of purpose or a common design") (citation omitted).

**(iv) Respondent's authority**

Relying on Viazis, Respondent argues that Complaint Counsel has failed to establish concerted action. RPTB at 16. In Viazis, plaintiff, an orthodontist, claimed that the action taken by an

Initial Decision

association of orthodontists to suspend plaintiff's membership in the association was concerted action, in violation of Section 1 of the Sherman Act. 314 F.3d at 761. After a hearing and appeal, the association's ethics committee found that plaintiff had violated the association's prohibition of false and misleading advertising and determined to suspend plaintiff's membership in the organization for one year. *Id.* at 761, 764. The Court of Appeals for the Fifth Circuit held that the suspension of plaintiff could "constitute action pursuant to a conspiracy only if the members of [the association] were conspiring among themselves." *Id.* at 764. Plaintiff "was unable to demonstrate that the ethics proceedings against him were a sham or that the standards applied were pretextual, so he failed to establish the existence of an unlawful conspiracy." *Id.* at 764-65.

In *Viazis*, the plaintiff presented no evidence that the proceedings against him were in any way designed to limit competition. *Id.* In this case, the evidence demonstrates that NTSP engaged in conduct that had the purpose and effect of limiting price competition among NTSP physicians and raising rates above those initially offered to NTSP on non-risk contracts. E.g., F. 187, 327. Accordingly, *Viazis* does not compel a finding that NTSP did not engage in a contract, combination, or conspiracy.

Respondent also asserts that, under *Colgate*, 250 U.S. at 307 (establishing manufacturer's right to refuse to deal) and *Verizon Communications, Inc. v. Law Offices of Curtis V. Trinko, LLP*, 124 S. Ct. 872, 880-81 (2004) (establishing network's right to refuse to make itself available), NTSP has a right to follow its own business model and to refuse to sign and messenger contractual offers that fall below Board minimums. RPTB at 22. Respondent further asserts that the Court of Appeals for the Fifth Circuit recently reiterated the right of an association to refuse to deal in its *Viazis* decision. RPTB at 22.

In *Colgate*, the United States Supreme Court held that a manufacturer has a right to deal, or refuse to deal, with whomever it likes, as long as it does so independently. 250 U.S. at 307. *Colgate* involved the unilateral decision by a single corporation,

## Initial Decision

Colgate, not to sell its products to dealers who would resell them at prices below the suggested prices set by Colgate. *Id.* at 302-03. As a single corporation, in fact and in form - unlike NTSP - Colgate could not conspire with itself. But here, where NTSP is not an entity with unity of purpose, Colgate is inapplicable. See *St. Bernard General Hosp., Inc. v. Hosp. Serv. Ass'n, Inc.*, 712 F.2d 978, 986-87 (5th Cir. 1983) (Colgate doctrine inapplicable to an association comprised of nine local hospitals).

Trinko is likewise inapplicable to the facts of this case. In *Trinko*, the Supreme Court addressed conduct by a single firm charged with monopolization under § 2 of the Sherman Act, not with "contract, combination or conspiracy" under § 1 of the Sherman Act. *Trinko*, 124 S. Ct. at 878. There was no allegation that the defendant had agreed with any other person on prices or on a refusal to deal. See *id.* The Court in *Trinko* held that the defendant was not required to make its communication network available to competitors. *Id.* at 880. The Court's holding reflects the reluctance of courts to use the antitrust laws to force competitors to cooperate with one another, recognizing that such cooperation may instead lead to collusion or reduce incentives to innovate. *Id.* at 879. Thus, *Trinko* is inapposite to a case such as this, involving an agreement on prices and concerted action.

*Viazis* also does not compel a conclusion that NTSP has a fight to refuse to sign and messenger contractual offers that fall outside NTSP's business model. In *Viazis*, the Fifth Circuit held that a plaintiff cannot show competitive harm "merely by demonstrating that the defendant 'refused without justification to promote, approve, or buy the plaintiff's product.'" 314 F.3d at 766 (quoting *Consolidated Metal Products*, 846 F.2d at 297). Respondent asserts that this case is similar to *Viazis* in that NTSP is making a decision on whether or not it wants to be involved in (i.e., "approve") a payor's offer. RPTB at 22. What makes this case different, however, is that the court in *Viazis* found that there was no evidence that the association had influence over its members' purchasing decisions or that it coerced them into rejecting plaintiff's product. 314 F.3d at 766. Here, there is evidence that NTSP influenced its member physicians to allow NTSP to negotiate economic terms of non-risk contracts on their

Initial Decision

behalf and that NTSP rejected offers that fell below Board minimum rates which NTSP had set based upon polling the member physicians. E.g., F. 65-67, 70, 83-89, 127, 155-57, 300, 311-16.

**(v) Summary**

Complaint Counsel has presented evidence "that tends to exclude the possibility that the alleged conspirators acted independently." *Matsushita Elec. Indus. Co., Ltd. v. Zenith Radio Corp.*, 475 U.S. 574, 588 (1986) (quotation omitted). The evidence, as detailed in the Findings of Fact and summarized above, establishes that NTSP and its member physicians entered into agreements to allow NTSP to negotiate on behalf of its member physicians; that NTSP established Board minimum rates by polling its member physicians to determine the minimally acceptable rate that its member physicians would accept for physician services; that NTSP used these Board minimum rates in negotiating the economic terms of non-risk contracts with health insurance plans; and that NTSP obtained for its member physicians more favorable rates or contract terms from health insurance payors than the payors initially offered. Accordingly, Complaint Counsel has demonstrated concerted action. The next required inquiry is whether Respondent's actions unreasonably restrained trade.

**2. Whether there was an unreasonable restraint of trade**

**a. Summary of facts**

A review of the actions NTSP took in its negotiation of economic terms of non-risk contracts with three health insurance payors - United, Cigna, and Aetna - demonstrates that the concerted action taken by NTSP was an unreasonable restraint of trade. As detailed in the Findings of Fact and summarized below, NTSP, on behalf of its member physicians, negotiated economic terms on non-risk contracts and entered into agreements with health care payors through which NTSP obtained higher rates or more beneficial economic terms than the health care payors initially offered to NTSP. NTSP has not demonstrated valid

## Initial Decision

procompetitive justifications for this conduct. Thus, as set forth below, Complaint Counsel has demonstrated an unreasonable restraint of trade.

**(i) Negotiations of economic terms with health plans**

The Medicare RBRVS fee schedule is Medicare's Resource Based Relative Value System ("RBRVS"), a system developed by the United States Centers for Medicare and Medicaid Services to determine the amount to pay physicians for each service rendered to Medicare patients. F. 10. Health plans that contract with physicians on a fee-for-service basis often do so based on a stated percentage of the Medicare RBRVS fee schedule, which provides reimbursement rates for a large number of specific procedures. F. 11. The Medicare RBRVS establishes weighted values for each medical procedure, such that the application of a percentage multiplier enables one to determine the fees for thousands of different services simultaneously. F. 12.

NTSP's polling form, which asks each physician to disclose the minimum price that he or she would accept for the provision of medical services pursuant to a fee-for-service HMO or PPO agreement, asks member physicians to indicate their price selection by placing a check mark next to one of several pre-printed Medicare RBRVS ranges. F. 89-90. On October 15, 2001, the NTSP Board received annual poll results. F. 96. Based on the poll results, NTSP established minimum prices of 125% of 2001 Medicare RBRVS for HMO products and 140% of 2001 Medicare RBRVS for PPO products as minimally acceptable fee schedules. F. 96. On November 11, 2002, NTSP conducted another annual poll to determine minimum reimbursement rates for use in negotiation of HMO and PPO products and anesthesia contracts with health plans. F. 97. On its 2002 polling form sent to physicians, NTSP included the 2001 poll results, reported by mean, median, and mode. F. 97. The results of the 2002 annual poll by mean, median, and mode, for HMO were 131%, 135%, and 135%; for PPO, 146%, 145%, and 145%. F. 98. As summarized below, these minimum rates were used by NTSP in its negotiation of economic terms of non-risk contracts on behalf of its member physicians.



Initial Decision

**. United**

In June 1998, NTSP sought to negotiate a non-risk contract with United, a health care payor that had been identified by NTSP as a potential major player in the market place. F. 107-08. To that end, NTSP solicited powers of attorney from its member physicians and recommended that the physicians "refrain from responding to United Healthcare while NTSP's request for agency status is being tabulated." F. 108, 110. In the course of its negotiations with United, NTSP made fee proposals to United and instructed its member physicians not to take any actions with respect to a United contract because NTSP was engaged in negotiations with United on behalf of NTSP's member physicians. F. 112-13. In the fall of 1998, United made an offer to NTSP on a non-risk contract containing rates that were below the rates available to physicians through another IPA, Health Texas Provider Network ("HTPN"). F. 116. NTSP and HTPN had an arrangement whereby NTSP physicians would be allowed to access HTPN's payor offers. F. 117. NTSP proposed to United that NTSP's member physicians contract with United through HTPN, which allowed higher rates than those offered to NTSP by United. F. 118-19. A significant number of NTSP physicians did access United through HTPN. F. 120.

In March 2001, NTSP approached United to negotiate a direct NTSP-United non-risk contract. F. 121. At that time, United already had contracts with approximately two-thirds of NTSP's member physicians, either directly or through other physician organizations such as HTPN. F. 124. Therefore, United concluded that there was no real need to enter into a contract with the remainder of NTSP physicians through an NTSP group contract. F. 124. Nevertheless, United offered NTSP its then standard rate in the Fort Worth area of 110% of 2001 Dallas RBRVS, which was the equivalent of 115% of 2001 Tarrant County RBRVS. F. 126. Without presenting the offer to its member physicians, NTSP informed United that the offer was unacceptable because it fell below NTSP's Board minimums and because it offered a single rate for both HMO and PPO products, instead of different rates for the two products. F. 127, 129, 147. In a Fax Alert to the

## Initial Decision

member physicians, NTSP's Board informed its member physicians that NTSP and United had agreed to fundamental non-economic terms, but that NTSP believed that United's rate offer was lower than NTSP's minimum price level. F. 149.

Following its rejection of the United offer, NTSP contacted a large employer, the City of Fort Worth, which was engaged in contract negotiations with United to provide health care coverage to the employees of the City of Fort Worth. F. 140, 141, 144. In July 2001, NTSP sent a letter to the Mayor of Fort Worth notifying him that United's reimbursement rates are "well below market benchmarks" and that "NTSP simply has not and will not accept United's request for our participation in their provider network for your employees." F. 138. The letter also stated that "the City may experience significant network disruption once United officially begins their duties (up to 588 doctors no longer available)." F. 138. NTSP encouraged its Board members to "contact any city council members they know to let them know that United's panel is not adequate." F. 135. NTSP also urged its primary care physicians to contact the Mayor and city council members to educate them about the situation with United and ask for assistance. F. 136.

These actions created concern among United's client, the City of Fort Worth, that NTSP physicians might drop out of United's network, leaving an inadequate network of physicians to serve its Fort Worth-based employees. F. 143. Based on these concerns, the City of Fort Worth urged United to do what was necessary to preserve its provider network. F. 143.

United, because it had a majority of NTSP physicians already under contract through HTPN, did not initially increase its offer to NTSP in the summer of 2001. NTSP, in July 2001, informed United that NTSP intended to terminate the contract that NTSP had with HTPN for the provision of physician services to United. F. 153. See also F. 150 (Fax Alert informing NTSP member physicians that "the NTSP Board has authorized termination [of] the United Health Care contract. However, notice has not yet been sent to United as NTSP must attempt one last strategy."). Subsequently, on July 23, 2001, the NTSP Board approved

Initial Decision

termination of NTSP's participation in the United-HTPN contract, effective October 20, 2001. F. 151.

In addition, NTSP solicited powers of attorney from its member physicians to enable NTSP to negotiate contracts between the physicians and United on the physicians' behalf. F. 160. Under the broad language of the power of attorney, NTSP was authorized to negotiate price terms on behalf of the member physicians: "this power of attorney grants the authority to the agent to act on the undersigned's behalf regarding the foregoing described agreements in all respects, including the authority to negotiate the terms of, enter into, execute, amend, modify, extend or terminate any such agreements." F. 161.

United learned about NTSP's efforts to solicit powers of attorney from NTSP's member physicians. F. 162. This effort, in conjunction with NTSP's termination of 108 physicians participating in United via HTPN and the concerns expressed by the City of Fort Worth to United about losing NTSP physicians from United's provider network, induced United to change its network strategy for Tarrant County. F. 162. Initially, United tried to recruit the terminated NTSP member physicians individually. F. 163. United directly offered those physicians the opportunity to return to a United contract at the same reimbursement rates that they had received under the HTPN-United agreement prior to their termination by NTSP. F. 164.

NTSP sent another Fax Alert to its member physicians in August 2001. In it, NTSP explained that it had been receiving calls from member physicians regarding direct offers that they had received from United; repeated NTSP's assessment that the United offer fell below Board minimums; noted that NTSP had already received 107 executed powers of attorney from its member physicians "to act on their behalf in regard to all contracting activity between themselves and United Healthcare"; invited the submission of executed powers of attorney by other member physicians; and advised member physicians who had already signed powers of attorney to inform United representatives that NTSP was their contracting agent and to instruct United "to contact NTSP directly." F. 165-68. NTSP

## Initial Decision

promised its member physicians that it would continue to pursue a direct contract with United that "meets or exceeds" the fee schedule minimum rates set by NTSP membership. F. 166.

United was not successful in signing contracts directly with NTSP physicians. United's initial direct contract invitation attracted only a few physicians, even though the physicians were offered the same rates that they previously received through HTPN. F. 171-72. Some of these physicians who rejected United's offer explicitly referred United back to NTSP as their negotiating agent. F. 173.

After receiving little interest in its initial direct offer to the terminated NTSP physicians, United tried to work through other Fort Worth IPAs or large medical groups. United offered 125% of 2001 Tarrant County RBRVS for HMO and 130% of 2001 Tarrant County RBRVS for PPO to two other IPAs, All Saints Affiliates and Medical Clinic of North Texas. F. 170. Next, United offered NTSP a rate of 125% of 2001 Tarrant RBRVS for HMO and 130% Tarrant RBRVS for PPO. F. 185.

NTSP and United signed a contract for 125% of 2001 Tarrant County RBRVS for HMO and 130% of 2001 Tarrant County RBRVS for PPO, effective November 1, 2001. F. 186. On November 1, 2001, NTSP sent the contract to its member physicians to opt in or opt out, indicating that the contract was a result of negotiations and that the 125% of the 2001 Tarrant County RBRVS for the HMO was "at the average level of acceptable reimbursement," but that the PPO rate of 130% was below the acceptable average reimbursement levels determined by the NTSP Board based on the poll results. F. 189. Of NTSP's member physicians, for HMO, 24% accepted, and for PPO, 23% accepted the NTSP-United contract. F. 191.

**. Cigna**

Cigna purchased Healthsource, Inc. ("Healthsource") in late 1997 and informed physicians in Healthsource's network that their contracts with Healthsource would be assigned to Cigna. F. 201-02. NTSP physicians who had contracts with Healthsource, at NTSP's direction, sent Cigna forty virtually identical letters,

Initial Decision

representing fifty-two doctors in separate practice groups, refusing assignment and stating that NTSP would be their representative and agent in negotiations with Cigna. F. 204-06.

Cigna and NTSP entered into a Letter of Agreement ("LOA") in October 1999, through which Cigna agreed to reimburse NTSP specialists, with the exception of cardiologists/CV [cardiovascular] surgeons, gastroenterologists, urologists, oncologists, and podiatrists, on a fee schedule equal to 125% of the 1998 Dallas County RBRVS. F. 212-13. Subsequently, NTSP requested, and Cigna agreed to, an amendment to the contract that insured that the rate would be adjusted annually to maintain 125% of current year RBRVS. F. 220.

Under the October 1999 LOA, Cigna entered into a non-risk contract for "NTSP specialists." F. 213, 237. Subsequently, NTSP asked Cigna to allow primary care physicians to "opt in" to the NTSP-Cigna contract. F. 238. Cigna already had an adequate number of primary care physicians in its network and determined that if NTSP's primary care physicians were allowed into Cigna's network, Cigna's overall costs would increase without any benefit to Cigna. F. 239. At times during the negotiations, in late 2000, regarding the inclusion of primary care physicians, NTSP threatened to terminate the NTSP-Cigna contract. F. 244. Cigna eventually agreed to allow NTSP's primary care physicians to opt in to the existing contract. F. 246.

In preparation for its negotiations with NTSP, Cigna analyzed the importance of having NTSP's physicians in its Fort Worth area network. F. 235. Cigna determined that NTSP's physicians made up a high percentage of many specialty practices. F. 235. Cigna also performed disruption analyses to determine the effect of losing access to NTSP's physicians. F. 235. Based on these analyses, Cigna concluded that a loss of NTSP physicians would have a significant negative impact on Cigna's network in several crucial specialties, and that, therefore, it must have those physicians in its Fort Worth area network. F. 235. Cigna also concluded, based on the identical letters it received from NTSP's member physicians designating NTSP as their agent and the threats by NTSP to terminate its contracts with Cigna, that

## Initial Decision

NTSP's physicians would only contract through NTSP and would not agree to contract individually with Cigna. F. 206, 208.

Under the contract between Cigna and NTSP that was current at the time of trial, April 2004, PPO reimbursement is at a rate of [redacted] and HMO reimbursement is at a rate of [redacted]. F. 250 (in camera). Cigna agreed to allow NTSP's primary care physicians to opt in to the contract on a fixed amount per patient basis and to provide for the future inclusion of specialists who had previously been carved out of the Cigna HMO contract. F. 246. There is insufficient evidence to determine if NTSP's demand of these rates was based on Board minimums or poll results.

**. Aetna**

Prior to 2000, many NTSP physicians served Aetna patients in the Fort Worth area through contracts that NTSP's physicians had with Medical Select Management ("MSM"), an IPA to which Aetna had delegated almost all medical risk for HMO care. F. 267, 269, 273-74. In 1999 and again in 2000, NTSP approached Aetna to obtain a direct NTSP-Aetna contract that would not involve MSM. F. 276-77. Initially, NTSP and Aetna tried to negotiate a risk contract, but after those negotiations reached a dead end, in October 2000, their negotiations shifted to non-risk, fee-for-service HMO and PPO products. F. 286.

In their negotiations on the terms of a non-risk contract, Aetna initially offered to NTSP rates that were based on a reference schedule that uses the same relative value units from the RBRVS schedule, but places a different multiplier on different specialties' services, based on supply and demand. F. 288. Aetna's initial offer aggregated to about 111% to 112% RBRVS for HMO and about 123% to 125% RBRVS for PPO, with some specialties being offered more or less than the aggregate. NTSP rejected this offer and proposed, instead, uniform rates for all specialties of 125% RBRVS for HMO and 140% RBRVS for PPO. F. 288. In November 2000, Aetna, in response to NTSP's demands, agreed to raise its PPO offer to 140% and offered a higher HMO reimbursement rate of 116%. F. 298. NTSP accepted the offered PPO rates, but continued to insist on the higher rate of 125% for its HMO contract. F. 299, 300.

Initial Decision

In the midst of negotiating the HMO rates with Aetna, NTSP decided to re-poll its member physicians "on the acceptability of the present Aetna offering." F. 311. Shortly thereafter, NTSP informed its member physicians that "the membership's message that a 125% of current Medicare HMO fee schedule is required has been transmitted to Aetna and a response on this final contractual item is expected within the next 24 to 36 hours." F. 316. NTSP further informed its member physicians that NTSP continued to act as their agent and instructed its member physicians to refer all contacts and materials received from Aetna to NTSP directly. F. 316.

During these negotiations, Aetna was subjected to pressure to reach an agreement with NTSP. In June 2000, NTSP threatened that its member physicians might immediately end their participation in the Aetna-MSM arrangement. F. 278. NTSP also sought and received approximately 180 powers of attorney from its member physicians, authorizing NTSP to act for those physicians in all transactions relating to MSM and to represent its member physicians in any negotiations with Aetna, regarding any term. F. 304. Using the authority provided by the powers of attorney, in November 2000, as previously threatened, NTSP terminated its member physicians' participation in the Aetna-MSM arrangement, citing breach of contract by MSM. F. 297. Based on the language of the powers of attorney and other NTSP statements to Aetna, Aetna believed that it could not negotiate directly with NTSP physicians. F. 306.

Ultimately, Aetna agreed to NTSP's terms. On December 19, 2000, Aetna wrote to NTSP and proposed for PPO, 140% of current Medicare RBRVS, anesthesia at \$ 45.00; for HMO, 125% of current Medicare RBRVS, anesthesia at \$ 43.00. F. 323. NTSP responded, stating that NTSP would send out a notice to its member physicians notifying them that the PPO and HMO offers were within the messenger minimums. F. 324. NTSP forwarded the NTSP-Aetna agreement to its member physicians. F. 326. One hundred and eighty-eight member physicians agreed to the NTSP-Aetna contract. F. 326.

## Initial Decision

In 2001, Aetna attempted to reduce the rates it paid to NTSP. F. 331. Aetna offered NTSP rates that Aetna believed were more in line with the market, but in some aspects were higher than Aetna's general fee schedule. F. 338-39. NTSP did not present Aetna's rate proposal to its member physicians because NTSP did not have Board authority to do so. F. 341. The Aetna-NTSP contract was terminated at the beginning of 2002. F. 332.

**(ii) Effects on prices**

The evidence establishes that NTSP, through its coordinated efforts, was able to demand higher prices from United and Aetna and more favorable terms in its contract with Cigna, than those health insurance payors initially offered. However, there is insufficient evidence to establish that the rates that United, Cigna, and Aetna agreed to with NTSP are uniformly higher than rates health insurance payors offered to other IPAs or directly to other physicians.

Several health plans estimated that they had paid increased prices as a result of NTSP's negotiation of economic terms of non-risk contracts. United agreed to a contract with rates that were an increase of 10% from their initial HMO offer and an increase of 15% from their initial PPO offer. F. 187. However, the rate that United offered to NTSP was the same rate that United had offered other IPAs. F. 188. Cigna estimated that it would cost [redacted] to shift some of its direct-contracted physicians from market compensation to NTSP compensation. F. 248 (in camera). Cigna's representative testified that the reimbursement rate of 125% of RBRVS on HMO and 130% of RBRVS on PPO was somewhere between 15 and 20 percent higher than Cigna's standard rates. F. 217. However, Cigna's representative also testified that the rates that Cigna paid to NTSP were in the "general ballpark" of the rates Cigna paid to other IPAs [redacted] F. 217 (in camera). Aetna agreed to contract rates for 2000 (uniform rates of 140% RBRVS for PPO and 125% RBRVS for HMO) that were higher than the rates Aetna initially offered (aggregated to about 123% to 125% RBRVS for PPO and to about 111% to 112% RBRVS for HMO). F. 327. Although Aetna's representative testified that the rates in the 2000 Aetna-NTSP contract were higher than other



Initial Decision

IPAs for similar services, those rates were identical to the rates in the Aetna-MSM contract. F. 328-29.

Complaint Counsel, in its post trial brief, argues that NTSP had compared the rates that its physicians were offered directly by the health plans to the rates that NTSP had succeeded in obtaining from those health plans, and concluded that: NTSP's contract rates with Aetna were at least 15 percent higher for both HMO and PPO arrangements; its contract rates with Cigna were at least 12 percent higher for HMO arrangements and 20 percent higher for PPO arrangements; and its contract rates with United were 15 percent higher for HMO arrangements. CCPTB at 21-22. However, the evidence cited by Complaint Counsel does not support these conclusions.

**(iii) Procompetitive justifications**

Respondent asserts that its conduct and business model have strong procompetitive effects and efficiencies, for both risk and non-risk contracts. The evidence presented at trial demonstrates that, with respect to non-risk contracts, NTSP's business model does not generate strong efficiencies, and that any efficiencies generated from NTSP's risk contract business do not, to a significant degree, spillover into NTSP's non-risk contract business. The evidence further establishes that any efficiencies that NTSP has achieved from its risk contract business that may spillover to NTSP's non-risk contract business are not dependent upon and do not require NTSP's negotiation of economic terms in non-risk contracts.

NTSP is not clinically integrated for patients under NTSP's non-risk contracts. F. 246. For patients covered under NTSP's non-risk contracts, NTSP does not: engage in case management; provide feedback to physicians concerning patient care; require adherence to its clinical guidelines and protocols; operate or refer patients to any disease management programs or patient registries; or engage in meaningful patient education. F. 365, 370, 372-73, 375. NTSP's medical director has no responsibility for controlling costs for patients under NTSP's non-risk contracts and NTSP's medical management committee does not evaluate the

## Initial Decision

care of patients under NTSP's non-risk contracts. F. 366-67. NTSP's hospital utilization management program does not apply to patients under NTSP's non-risk contracts and NTSP's information systems do not include data for patients under NTSP's non-risk contracts. F. 368-69.

Sixty percent of NTSP's physicians participate in non-risk contracts. Roughly half of those physicians participate in risk-sharing contracts. F. 51. NTSP physicians who do not participate in NTSP's shared risk contract are unlikely to learn and apply techniques to control costs and to improve quality that are developed or learned in the context of that risk-sharing arrangement. F. 379. Further, NTSP has not achieved significant spillover benefits from its risk business to its non-risk business because it lacks data for patients seen under non-risk contracts and thus is hindered in implementing organized processes for these patients. F. 378. Finally, NTSP does not need to set minimum contract rates in its non-risk contracts in order for any efficiencies achieved through NTSP's risk contract business to spillover to NTSP's non-risk contract business. F. 380.

**b. Summary of parties' positions**

Complaint Counsel asserts that because NTSP's acts and practices fit squarely within the conduct traditionally condemned as per se illegal, there is no need to engage in an extensive or elaborate analysis of market definition and competitive effects. CCPTB at 60. Complaint Counsel further asserts that irrespective of the standard of analysis applied, indirect evidence of Respondent's market power is unnecessary where there is direct evidence of price fixing among competitors. CCPTB at 60.

Respondent asserts that the rule of reason analysis should be applied in this case since the conduct at issue might plausibly be thought to have a net procompetitive effect, or possibly no effect at all on competition. RPTB at 4. Respondent further asserts that because Complaint Counsel has not demonstrated that the challenged conduct has a net anticompetitive effect and has not proven NTSP's market power, Complaint Counsel has not proven an unreasonable restraint of trade. RPTB at 9, 11.

Initial Decision

### **c. Analysis**

Section 1 of the Sherman Act provides that "every contract, combination in the form of trust or otherwise, or conspiracy, in restraint of trade or commerce among the several States, or with foreign nations, is declared to be illegal." 15 U.S.C. § 1. Despite its broad language, Section 1 has long been interpreted to outlaw only those restraints that are "unreasonable." *Maricopa*, 457 U.S. at 343. The Supreme Court has set forth three methods for analyzing the reasonableness of a restraint on trade: (1) *per se* analysis, for obviously anticompetitive restraints; (2) quick look analysis, for those with some procompetitive justification; and (3) the full "rule of reason," analysis for restraints whose net impact on competition is particularly difficult to determine. *Continental Airlines, Inc. v. United Airlines, Inc.*, 277 F.3d 499, 508-09 (4th Cir. 2002). In *California Dental*, the Supreme Court held, as demonstrated by the circumstances before it, "there is generally no categorical line to be drawn between restraints that give rise to an intuitively obvious inference of anticompetitive effect and those that call for more detailed treatment." *Id.* at 780-81. Instead, what is required is to look to "the circumstances, details, and logic of a restraint." *Id.* at 781. The three methods are best viewed as a continuum, on which the "amount and range of information needed" to evaluate a restraint varies, depending on how "highly suspicious" and how "unique" the restraint is. *Continental Airlines*, 277 F.3d at 509 (citing 11 Herbert Hovenkamp, *Antitrust Law* P 1911a (1998); *California Dental*, 526 U.S. at 779-81).

In *California Dental*, the challenged restraint of trade -- restrictions on both discount and nondiscount advertising -- "fail[ed] to present a situation in which the likelihood of anticompetitive effects [was] comparably obvious." *Id.* at 771. The Supreme Court held that, where competing claims about the effects of the professional advertising restrictions were plausible, the obvious anticompetitive effect that triggers abbreviated analysis had not been shown. *Id.* at 778. Thus, the Supreme Court remanded the case for a more thorough inquiry into the consequence of the challenged restraints. *Id.* at 759, 781.

## Initial Decision

However, where the effects of an agreement are "intuitively obvious" and "easily ascertained," *California Dental*, 526 U.S. at 759, 770, no elaborate study of the industry is needed to establish the illegality of the agreement. *Dagher v. Saudi Refining Inc.*, 369 F.3d 1108, 1116 (9th Cir. 2004).

Agreements among competitors to fix or set prices have been historically condemned as per se illegal. *Socony-Vacuum*, 310 U.S. at 218; *Maricopa*, 457 U.S. at 344 ("The anticompetitive potential inherent in all price-fixing agreements justifies their facial invalidation even if procompetitive justifications are offered for some."); *Catalano, Inc. v. Target Sales, Inc.*, 446 U.S. 643, 647 (1980) ("It has long been settled that an agreement to fix prices is unlawful per se. It is no excuse that the prices fixed are themselves reasonable.") (citations omitted); *Nat'l Soc'y of Prof'l Engineers v. United States*, 435 U.S. 679, 692 (1978) (noting that "price is the 'central nervous system of the economy'" and holding that "an agreement that 'interferes with the setting of price by free market forces' is illegal on its face") (citation and alteration omitted).

Courts, after *California Dental*, have applied the per se analysis to horizontal price fixing. E.g., *Dagher*, 369 F.3d at 1116 n.7 ("Because we hold that the plaintiffs have made a sufficient showing with respect to the illegality of the alliance's price fixing system under the per se rule, we need not decide whether that scheme would survive 'quick look' review."); *Freedom Holdings Inc. v. Spitzer*, 357 F.3d 205, 226 (2nd Cir. 2004); *Freeman v. San Diego Ass'n of Realtors*, 322 F.3d 1133, 1150-54 (9th Cir. 2003). "Traditional 'hard-core' price fixing remains per se unlawful under the seminal case *United States v. Socony-Vacuum Oil Co.*, 310 U.S. 150, 212-24 (1940), and its progeny." *Todd*, 275 F.3d at 198.

Courts employ the quick look approach when a restraint of trade is not illegal per se, but nevertheless has such obvious anticompetitive effects that a "full scale" rule of reason analysis is not necessary. *California Dental*, 526 U.S. at 770. "When there is an agreement not to compete in terms of price or output, 'no elaborate industry analysis is required to demonstrate the

Initial Decision

anticompetitive character of such an agreement." *NCAA v. Bd. of Regents*, 468 U.S. 85, 109 (1984).

Regardless of what method of analysis is used, "the criterion to be used in judging the validity of a restraint on trade is its impact on competition." *NCAA*, 468 U.S. at 104. "Whether the ultimate finding is the product of a presumption or actual market analysis, the essential inquiry remains the same -- whether or not the challenged restraint enhances competition." *California Dental* (quoting *NCAA*, 468 U.S. at 104). The analytical focus is on what conclusions regarding the competitive impact of a challenged restraint can confidently be drawn from the facts demonstrated by the parties. See *California Dental*, 526 U.S. at 779-81; *NCAA*, 468 U.S. at 103-04.

In *California Dental*, the complaint alleged that an association of dentists had unreasonably restricted two types of advertising: price advertising, particularly discounted fees, and advertising relating to the quality of dental services. 526 U.S. at 762. Here, the challenged restraint is a horizontal price fixing agreement: an agreement on the minimum reimbursement level that NTSP will accept on behalf of its member physicians for those physicians' services pursuant to non-risk contracts with health insurance payors. Whereas in *California Dental*, the anticompetitive effects of the restrictions on advertising were not obvious, in this case, the effects of agreements to set minimum price levels are "intuitively obvious." Thus, no elaborate study of the industry is needed to establish the illegality of NTSP's actions. See *California Dental*, 526 U.S. at 759; *Dagher*, 369 F.3d at 1116.

To the extent that an examination of effects is required, in this case, the effects of NTSP's concerted action have been to cause health insurance payors to increase their offers or agree to better terms of coverage than the payors otherwise would have, but for NTSP's collective actions. Although the evidence is not conclusive that NTSP's actions resulted in supracompetitive prices, such evidence does not defeat a finding of liability in this case. *FTC v. Superior Court Trial Lawyers Ass'n*, 493 U.S. 411, 424 (1990) (It "is no excuse that the prices fixed are themselves reasonable.") (citations omitted).

## Initial Decision

Also, in *California Dental*, the restrictions on advertising, at least on their face, were designed to avoid false or deceptive advertising and thus "might plausibly be thought to have a net procompetitive effect, or possibly no effect at all on competition." 526 U.S. at 771. Respondent asserts that NTSP's conduct might plausibly be thought to have a net procompetitive effect because NTSP's conduct and business model have strong procompetitive effects and efficiencies. RPTB at 1. Where a defendant asserts that the challenged conduct has procompetitive effects, the defendant bears the burden of establishing those procompetitive effects. *California Dental*, 526 U.S. 775 n.12. Courts evaluate whether claimed efficiencies are plausible, *NCAA*, 468 U.S. at 114; *Maricopa*, 457 U.S. at 353, and whether the challenged conduct is reasonably necessary to achieve the legitimate objective identified by a defendant. *Broadcast Music, Inc. v. CBS*, 441 U.S. 1, 19-21 (1979); *United States v. Brown Univ.*, 5 F.3d 658, 678-79 (3rd Cir. 1993).

In this case, as found in F. 364-80, and summarized above, there is no plausible and valid efficiency justification for collectively setting the prices in non-risk contracts, nor is such conduct reasonably necessary to achieve the claimed procompetitive benefits. Because the challenged restraint of trade does not have a net procompetitive effect on competition, a more thorough inquiry into the consequences of the challenged restraints is not necessary. See *California Dental*, 526 U.S. at 759, 781.

Complaint Counsel has demonstrated that the actions taken by NTSP to coerce health insurance payors to increase their offers of rate reimbursement or offer more favorable economic terms to NTSP's physicians constitute an unreasonable restraint of trade in violation of Section 1 of the Sherman Act and Section 5 of the FTC Act.

Initial Decision

## **E. Remedy**

### **1. Standards**

Pursuant to Section 5 of the Federal Trade Commission Act, upon determination that the challenged practice is an unfair method of competition, the Commission "shall issue . . . an order requiring such . . . corporation to cease and desist from using such-method of competition or such act or practice." 15 U.S.C. § 45(b); *FTC v. Nat'l Lead Co.*, 352 U.S. 419, 428 (1957) (Commission is authorized "to enter an order requiring the offender to 'cease and desist' from using such unfair method."). The remedy selected must have a "reasonable relation to the unlawful practices found to exist." *Nat'l Lead Co.*, 352 U.S. at 428.

In this case, Complaint Counsel has proven that Respondent engaged in horizontal price fixing through its negotiation, on behalf of its member physicians, of economic terms of non-risk contracts with health plan payors for the provision of physician services. The remedy necessary to bring an end to this unfair method of competition is an order requiring Respondent to cease and desist from collective price fixing in its negotiation of non-risk contracts. In addition, to the extent that there are any existing, current non-risk contracts between NTSP, negotiated on behalf of its member physicians, and any health care payor, Respondent must take actions, as set forth in the Order, to allow termination of any such existing contracts.

### **2. Provisions**

Complaint Counsel's proposed order seeks a provision requiring Respondent to cease and desist from entering into an agreement among physicians "to deal, refuse to deal, or threaten to refuse to deal with any payor" and "not to deal individually with any payor, or not to deal with any payor through any arrangement other than Respondent." Complaint Counsel's Proposed Order, Sections II.A.2, 4. Complaint Counsel explains that this provision is "intentionally broad so as to preclude respondents from engaging both in the precise conduct found

## Initial Decision

unlawful in this action and 'like and related' conduct." CCPTB at 77. See also Complaint Counsel's Opening Statement, Tr. at 60 (Complaint Counsel seeks an order "broadly requiring NTSP to messenger contracts.").

This broad request could have the effect of compelling Respondent to messenger contracts or become a party to contracts sent to it by payors, regardless of potential risks to Respondent, its member physicians, and its patients. A mandatory injunction, which compels a party to act, is an extraordinary remedy that should be granted only in compelling circumstances. *Citizens Concerned for Separation of Church and State v. City and County of Denver*, 628 F.2d 1289, 1299 (10th Cir. 1980); *Justin Indus., Inc. v. Choctaw Sec., L.P.*, 747 F. Supp. 1218, 1220 (N.D. Tex. 1990), *aff'd*, 920 F.2d 262 (5th Cir. 1990). Sufficient compelling circumstances have not been demonstrated in this case.

Moreover, Complaint Counsel's authority cited in support of its proposed relief is based only on consent decrees. CCPTB at 76. "The circumstances surrounding . . . negotiated [consent decrees] are so different that they cannot be persuasively cited in a litigation context." *United States v. E.I. du Pont de Nemours*, 366 U.S. 316, 330 n.12 (1961). Sections II.A.2 and 4 of Complaint Counsel's Proposed Order, which are not narrowly tailored to remedy the violation of law found to exist, are broader than required to remedy the unlawful conduct. A provision that could require Respondent to messenger all contracts or become a party to contracts sent to it by payors will not be ordered. Such overreaching is unnecessary. Accordingly, Sections II.A.2, 4 of Complaint Counsel's proposed order are not ordered.

In addition, any remedy must not contravene Texas health care laws, other Texas law, or federal law. E.g., 28 TEX. ADMIN. CODE § 3.3703 (laying out contracting requirements for PPOs concerning exclusivity, savings inducements, hold-harmless clauses, prompt payment, continuity of care, disclosure of opinions to patients, disclosure of economic profiling criteria, disclosure of quality assessment criteria, and termination); 29 TEX. ADMIN. CODE § 21.2817 (relating to clean claims and prompt payment); TEX. INS. CODE art. 3.70-3C (same issues as



Initial Decision

TEX. ADMIN. CODE § 3.3703). The Supreme Court recently limited an agency's remedies to those that did not conflict with other laws, statutes, and policies unrelated to the agency. *Hoffman Plastic Compounds, Inc. v. NLRB*, 535 U.S. 137, 144-45 (2002). The Order issued herewith provides that nothing in this Order shall require NTSP violate state or federal law. Further, the Order is narrowly tailored and reasonably related to the violation of law found to exist.

### **3. Duration**

Complaint Counsel has requested that the order issued in this case remain in effect for a period of twenty years. CCPTB at 79. Pursuant to the Policy Statement Regarding Duration of Competition and Consumer Protection Orders, 60 Fed. Reg. 42,569 (August 16, 1995), the Commission's stated policy is for administrative cease and desist orders to terminate after twenty years. The Order entered in this case shall remain in effect for a period of twenty years.

## **IV. SUMMARY OF CONCLUSIONS OF LAW**

1. Respondent North Texas Specialty Physicians ("NTSP") is a corporation, as "corporation" is defined by Section 4 of the Federal Trade Commission Act, ("FTC Act"), 15 U.S.C. § 44.
2. The participating physicians of NTSP are "members" of NTSP, as that term is used in the definition of "corporation" in Section 4 of the FTC Act, 15 U.S.C. § 44.
3. The jurisdiction of the Federal Trade Commission ("FTC") extends to non-profit entities when a substantial part of the entity's total activities provides economic benefits for its members.
4. A substantial part of Respondent's activities provides economic benefits for its members.
5. The acts and practices charged in the Complaint are in or affect commerce, as "commerce" is defined in Section 4 of the FTC Act, 15 U.S.C. § 44.

## Initial Decision

6. The Federal Trade Commission has jurisdiction over Respondent and over the subject matter of this proceeding, pursuant to Section 5 of the FTC Act, 15 U.S.C. § 45.
7. The relevant market is physician services available to patients in the Fort Worth, Texas area.
8. Complaint Counsel has met its burden of proof of demonstrating that Respondent engaged in an agreement in restraint of trade.
9. Respondent has engaged in a contract, combination, or conspiracy to fix prices in non-risk contracts to be charged by physicians for providing medical services to health plans' patients.
10. Respondent's contract, combination, or conspiracy unreasonably restrained trade.
11. Respondent has not met its burden of proof of demonstrating that the challenged conduct has a net procompetitive effect on competition.
12. Respondent's fixing prices in non-risk contracts does not have a plausible and valid efficiency justification.
13. Respondent's fixing prices in non-risk contracts is not reasonably necessary to create any efficiencies.
14. The acts and practices of Respondent, as set forth in paragraphs 9 and 10 above, constitute unfair methods of competition in violation of Section 5 of the FTC Act, 45 U.S.C. § 45.
15. Relief designed to remedy Respondent's unlawful activities and to require Respondent to cease and desist from collective price fixing is appropriate.
16. The Order entered herein is necessary and appropriate to remedy the violation of law found to exist.

Initial Decision

**ORDER:**

**ORDER**

**I.**

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

- A. "Respondent" means North Texas Specialty Physicians ("NTSP"), its officers, directors, employees, agents, attorneys, representatives, successors, and assigns; and the subsidiaries, divisions, groups, and affiliates controlled by North Texas Specialty Physicians, and the respective officers, directors, employees, agents, attorneys, representatives, successors, and assigns of each.
- B. "Medical group practice" means a bona fide, integrated firm in which physicians practice medicine together as partners, shareholders, owners, members, or employees, or in which only one physician practices medicine.
- C. "Participate" in an entity means: (1) to be a partner, shareholder, owner, member, or employee of such entity; or (2) to provide services, agree to provide services, or offer to provide services, to a payor through such entity. This definition also applies to all tenses and forms of the word "participate," including, but not limited to, "participating," "participated," and "participation."
- D. "Payor" means any person that pays, or arranges for the payment, for all or any part of any physician services for itself or for any other person. Payor includes any person that develops, leases, or sells access to networks of physicians.
- E. "Person" means both natural persons and artificial persons, including, but not limited to, corporations, unincorporated entities, and governments.

## Initial Decision

F. "Physician" means a doctor of allopathic medicine ("M.D.") or a doctor of osteopathic medicine ("D.O.").

G. "Preexisting contract" means a contract that was in effect on the date of receipt by a payor that is a party to such contract of notice sent by Respondent, pursuant to Paragraph IV.A.3 of this Order, of such payor's right to terminate such contract.

H. "Principal address" means either (1) primary business address, if there is a business address, or (2) primary residential address, if there is no business address.

I. "Qualified clinically-integrated joint arrangement" means an arrangement to provide physician services in which:

1. all physicians that participate in the arrangement participate in active and ongoing programs of the arrangement to evaluate and modify the practice patterns of, and create a high degree of interdependence and cooperation among, the physicians who participate in the arrangement, in order to control costs and ensure the quality of services provided through the arrangement; and
2. any agreement concerning price or other terms or conditions of dealing entered into by or within the arrangement is reasonably necessary to obtain significant efficiencies through the joint arrangement.

J. "Qualified risk-sharing joint arrangement" means an arrangement to provide physician services in which:

1. all physicians who participate in the arrangement share substantial financial risk through their participation in the arrangement and thereby create

Initial Decision

incentives for the physicians who participate jointly to control costs and improve quality by managing the provision of physician services, such as risk-sharing involving:

- a. the provision of physician services for a fixed amount per patient, per month paid by payors;
  - b. the provision of physician services for a predetermined percentage of premium or revenue from payors;
  - c. the use of significant financial incentives for physicians who participate to achieve, as a group, specified cost-containment goals; or
  - d. the provision of a complex or extended course of treatment that requires the substantial coordination of care by physicians in different specialties offering a complementary mix of services, for a fixed, predetermined price, where the costs of that course of treatment for any individual patient can vary greatly due to the individual patient's condition, the choice, complexity, or length of treatment, or other factors; and
2. any agreement concerning price or other terms or conditions of dealing entered into by or within the arrangement is reasonably necessary to obtain significant efficiencies through the joint arrangement.

Initial Decision

**II.**

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

A. Entering into, adhering to, participating in, maintaining, organizing, implementing, enforcing, or otherwise facilitating any combination, conspiracy, agreement, or understanding between or among any physicians to negotiate on behalf of any physician with any payor, regarding any term, condition, or requirement upon which any physician deals, or is willing to deal, with any payor, including, but not limited to, price terms;

B. Exchanging or facilitating in any manner the exchange or transfer of information among physicians concerning the terms or conditions, including price terms, on which any physician is willing to deal with a payor;

C. Attempting to engage in any action prohibited by Paragraph II.A or II.B, above; and

D. Encouraging, suggesting, advising, pressuring, inducing, or attempting to induce any person to engage in any action that would be prohibited by Paragraphs II.A through II.C above.

**PROVIDED, HOWEVER,** that nothing in this Order shall prohibit any agreement involving or conduct by Respondent that is reasonably necessary to form, participate in, or take any action in furtherance of a qualified risk-sharing joint arrangement or qualified clinically-integrated joint arrangement.

**PROVIDED, FURTHER,** that nothing contained in this Order shall prohibit Respondent from communicating purely factual information describing the terms and conditions of any payor offer, including objective comparisons with terms offered by other payors, or from expressing views relevant to various health plans. "Objective information" or "objective comparison"

Initial Decision

constitutes empirical data that is capable of being verified or a comparison of such data.

**PROVIDED, FURTHER**, that nothing contained in this Order shall require Respondent to violate state or federal law.

**III.**

**IT IS FURTHER ORDERED** that, for three (3) years from the date this Order becomes final, Respondent shall notify the Secretary of the Commission in writing ("Notification") at least sixty (60) days prior to entering into any arrangement with any physician under which Respondent would act as a messenger, or as an agent on behalf of the physician, with payors regarding contracts.

The Notification shall include the identity of each proposed physician participant; the proposed geographic area in which the proposed arrangement will operate; a copy of any proposed physician participation agreement; a description of the proposed arrangement's purpose and function; a description of any resulting efficiencies expected to be obtained through the arrangement; and a description of procedures to be implemented to limit possible anticompetitive effects, such as those prohibited by this Order.

Notification is not required for Respondent's subsequent acts as a messenger pursuant to an arrangement for which this Notification has been given.

Receipt by the Commission from Respondent of any Notification, pursuant to this Paragraph III, is not to be construed as a determination by the Commission that any action described in such Notification does or does not violate this Order or any law enforced by the Commission.

**IV.**

**IT IS FURTHER ORDERED** that Respondent shall:

A. Within thirty (30) days after the date on which this Order becomes final, send by first-class mail, return receipt requested, a copy of this Order to:

## Initial Decision

1. each physician who participates, or has participated, in Respondent since January 1, 2000;
2. each officer, director, manager, and employee of Respondent; and
3. the chief executive officer of each payor with which Respondent has a record of having been in contact since January 1, 2000, regarding contracting for the provision of physician services.

B. Terminate, without penalty or charge, and in compliance with any applicable laws, any preexisting contract with any payor for the provision of physician services, pursuant to a fee-for-service agreement at the earlier of:

1. receipt by Respondent of a written request from a payor to terminate such contract; or
2. the earliest termination or renewal date (including any automatic renewal date) of such contract.

Provided, however, a preexisting contract may extend beyond any such termination or renewal date no later than one (1) year after the date on which the Order becomes final, if prior to such termination or renewal date, (a) the payor submits to Respondent a written request to extend such contract to a specific date no later than one (1) year after the date this Order becomes final, and (b) Respondent has determined not to exercise any right to terminate; provided further, that any payor making such request to extend a contract retains the right, pursuant to Paragraph IV.B. 1 of this Order, to terminate the contract at any time.

C. Within ten (10) days after receiving a written request from a payor, pursuant to Paragraph IV.B.1 of this Order, distribute, by first-class mail, return receipt requested, a copy of that request to each physician participating in Respondent as of the date Respondent receives such request.



Initial Decision

D. For a period of three (3) years after the date this Order becomes final:

1. distribute by first-class mail, return receipt requested, a copy of this Order to:

a. each physician who begins participating in Respondent, and who did not previously receive a copy of this Order from Respondent, within thirty (30) days of the time that such participation begins;

b. each payor who contracts with Respondent for the provision of physician services, and who did not previously receive a copy of this Order from Respondent, within thirty (30) days of the time that such payor enters into such contract;

c. each person who becomes an officer, director, manager, or employee of Respondent and who did not previously receive a copy of this Order from Respondent, within thirty (30) days of the time that he or she assumes such responsibility with Respondent;

2. annually publish a copy of this Order in an official annual report or newsletter sent to all physicians who participate in Respondent, with such prominence as is given to regularly featured articles.

E. File a verified written report within sixty (60) days after the date this Order becomes final, and annually thereafter for three (3) years on the anniversary of the date this Order becomes final, and at such other times as the Commission may by written notice require. Each such report shall include:

## Initial Decision

1. a detailed description of the manner and form in which Respondent has complied and is complying with this Order; and
2. copies of the return receipts required by Paragraphs IV.A, IV.C, and IV.D of this Order.

F. Notify the Commission at least thirty (30) days prior to any proposed change in Respondent, such as dissolution, assignment, sale resulting in the emergence of a successor company or corporation, the creation or dissolution of subsidiaries, or any other change in Respondent that may affect compliance obligations arising out of this Order.

**V.**

**IT IS FURTHER ORDERED** that Respondent shall notify the Commission of any change in its principal address within twenty (20) days of such change in address.

**VI.**

**IT IS FURTHER ORDERED** that, for the purpose of determining or securing compliance with this Order, Respondent shall permit any duly authorized representative of the Commission:

- A. Upon written request and two (2) days' notice to Respondent, access, during office hours and in the presence of counsel, to inspect and copy all books, ledgers, accounts, correspondence, memoranda, calendars, and other records and documents in its possession, or under its control, relating to any matter contained in this Order; and
- B. Upon written request and five (5) days' notice to Respondent, and in the presence of counsel, and without restraint or interference from it, to interview Respondent or employees of Respondent, relating to any matter contained in this Order.

Initial Decision

**VII.**

**IT IS FURTHER ORDERED** that this Order shall terminate twenty (20) years from the date it is issued.

Complaint

IN THE MATTER OF

**SUPERIOR MORTGAGE CORP.**CONSENT ORDER, ETC., IN REGARD TO ALLEGED VIOLATIONS OF  
SEC. 5 OF THE FEDERAL TRADE COMMISSION ACT*Docket C-4153; File No. 0523136**Complaint, December 14, 2005--Decision, December 14, 2005*

This consent order, among other things, prohibits Respondent Superior Mortgage Corp., a New Jersey mortgage lender, from misrepresenting the extent to which it maintains and protects the privacy, confidentiality, or security of any personal information collected from or about consumers, and from violating the Safeguards Rule. The consent order also requires the respondent, for ten years, to secure biennial assessments and reports to ensure that its security program complies with the Safeguards Rule and is sufficiently effective to provide reasonable assurance that the security, confidentiality, and integrity of personal information is protected.

*Participants*

For the Commission: *Laura Mazzarella, Molly K. Crawford, Jessica L. Rich, Joel Winston and Louis Silverstein.*

For the Respondent: *Phillip Schulman, Kirkpatrick, Lockhart, Nicholson & Graham LLP*

**COMPLAINT**

The Federal Trade Commission (“Commission”), having reason to believe that Superior Mortgage Corp. has violated the provisions of the Commission’s Standards for Safeguarding Customer Information Rule (“Safeguards Rule”), 16 C.F.R. Part 314, issued pursuant to Title V of the Gramm-Leach-Bliley Act (“GLB Act”), 15 U.S.C. § 6801 *et seq.*, and the provisions of the Federal Trade Commission Act, and it appearing to the Commission that this proceeding is in the public interest, alleges:

1. Respondent Superior Mortgage Corp. (“Superior Mortgage”) is a New Jersey corporation with its principal office or place of business at 1395 Route 539, Tuckerton, New Jersey 08087. In

Complaint

addition to conducting business from its headquarters location in Tuckerton, Superior Mortgage conducts business through forty (40) branch offices located in ten different states, as well as through six separate websites.

2. Respondent is a direct lender that specializes in residential mortgage loans. As such, it is a “financial institution,” as that term is defined in Section 509(3)(A) of the GLB Act, and is therefore subject to the requirements of the Safeguards Rule.
3. The acts and practices of respondent alleged in this complaint have been in or affecting commerce, as “commerce” is defined in Section 4 of the FTC Act, 15 U.S.C. ' 44.

**SAFEGUARDS RULE**

4. The Safeguards Rule, which implements Section 501(b) of the GLB Act, was promulgated by the Commission on May 23, 2002, and became effective on May 23, 2003. The Rule requires financial institutions to protect the security, confidentiality, and integrity of customer information by developing a comprehensive written information security program that contains reasonable administrative, technical, and physical safeguards, including:
  - A. Designating one or more employees to coordinate the information security program;
  - B. Identifying reasonably foreseeable internal and external risks to the security, confidentiality, and integrity of customer information, and assessing the sufficiency of any safeguards in place to control those risks;
  - C. Designing and implementing information safeguards to control the risks identified through risk assessment, and regularly testing or otherwise monitoring the effectiveness of the safeguards' key controls, systems, and procedures;

## Complaint

- D. Overseeing service providers, and requiring them by contract to protect the security and confidentiality of customer information; and
- E. Evaluating and adjusting the information security program in light of the results of testing and monitoring, changes to the business operation, and other relevant circumstances.

**VIOLATIONS OF THE SAFEGUARDS RULE**

- 5. Through its offices and websites, respondent has collected sensitive customer information in connection with the mortgage application process, including customer names, Social Security numbers, credit histories, and bank and credit card account numbers. Since the Rule's effective date until at least May 2005, respondent failed to implement reasonable policies and procedures to protect the security and confidentiality of the information it collects.
- 6. For example, respondent failed to (a) assess risks to its customer information until more than a year after the Rule's effective date; (b) institute appropriate password policies to control access to company systems and documents containing sensitive customer information; and (c) encrypt or otherwise protect sensitive customer information before sending it by email. Respondent also failed to take reasonable steps to ensure that its service providers were providing appropriate security for customer information and addressing known security risks in a timely fashion.
- 7. By failing to implement reasonable security policies and procedures, respondent engaged in violations of the Safeguards Rule, including but not limited to:
  - A. Failing to identify reasonably foreseeable internal and external risks to the security, confidentiality, and integrity of customer information;

Complaint

- B. Failing to design and implement information safeguards to control the risks to customer information and failing to regularly test and monitor them; and
  - C. Failing to oversee service providers to ensure that they implement safeguards to protect respondent's customer information.
8. A violation of the Safeguards Rule constitutes an unfair or deceptive act or practice in violation of Section 5(a)(1) of the FTC Act.

**VIOLATIONS OF THE FTC ACT**

9. Since at least 2002, respondent has collected personal information from consumers through its Online Application Form at [www.supmort.com](http://www.supmort.com). Since at least 2003, respondent has operated five additional websites that collect personal information from consumers by linking them to the Online Application Form. This online form serves as an initial step for many consumers seeking a loan through respondent.
10. The Online Application Form collects from consumers personal information, including, but not limited to, name, address, date of birth, Social Security number, credit history, and bank and credit card account numbers.
11. Since at least 2002, respondent has disseminated or caused to be disseminated on [www.supmort.com](http://www.supmort.com) the following statement regarding the privacy and confidentiality of personal information collected through respondent's website:

All information submitted is handled by SSL encryption - see the yellow padlock at the bottom of your browser.

Exhibit A (Superior Mortgage webpage dated October 25, 2004).

## Complaint

12. Through the means described in paragraph 11, respondent has represented, expressly or by implication, that the personal information it obtained from consumers through [www.supmort.com](http://www.supmort.com) was encrypted using SSL from the time of submission until receipt by respondent.
13. In truth and in fact, the personal information obtained from consumers through [www.supmort.com](http://www.supmort.com) was not encrypted using SSL from the time of submission until it was received by respondent. Instead, respondent encrypted sensitive personal information only while it was being transmitted between a visitor's web browser and the website's server (using SSL); once the information reached the server, it was decrypted and emailed to respondent's headquarters and branch offices in clear, readable text. Therefore, the representation set forth in paragraph 12 was false or misleading.
14. The acts and practices of respondent as alleged in this complaint constitute unfair or deceptive acts or practices, in or affecting commerce, in violation of Section 5(a) of the Federal Trade Commission Act.

THEREFORE, the Federal Trade Commission this 14<sup>th</sup> day of December, 2005, has issued this complaint against respondent.



**EXHIBIT A**



# Superior Mortgage

*Our Success Is Built On Service*



If you are already dealing with a loan officer at Superior Mortgage, please [click here](#) to go to his/her page first.

For your convenience we've provided this Online Application Form. If you prefer, we can mail (or e-mail) you a form that may be completed offline. If you have any questions, please call the office number provided at the bottom of this page to speak to one of our helpful loan consultants.

After completing this form, you will be presented with a disclosure statement in which you must acknowledge reading, else your application **WILL NOT** be submitted to Superior Mortgage.

(All information submitted is handled by SSL encryption - see the yellow padlock at the bottom of your browser)

- To Apply For A Loan
- Mortgages 101
- Buying A Home
- Refinancing A Home
- Office Locations
- About Us
- Members Only
- Contact Us
- Home

[Site Map](#)



site design: E-Maxed

### Borrower Information

**Borrower Name:** First:  MI:  Last:

Daytime Phone (with area code): 1-

Evening Phone (with area code): 1-

Cell Phone (with area code): 1-

Street:  Own  Rent

City:  State:  # of Years:

Zip:  Date of Birth:

Email:

Self Employed?  Occupation:

Employer:

# of Years:  Social Security #:

Gross Monthly Income \$

Total Liquid Assets ( include cash, bank accounts, etc) \$

### Co-Borrower Information

**Co-Borrower Name:** First:  MI:  Last:

Daytime Phone (with area code): 1-

Evening Phone (with area code): 1-

Street:  Own  Rent

City:  State:  # of Years:

Zip:  Date of Birth:

Self Employed?  Occupation:

Employer:

# of Years:  Social Security #:

Gross Monthly Income \$ <input type="text"/>	
Total Liquid Assets ( include cash, bank accounts, etc) \$ <input type="text"/>	
<b>Property Information</b>	
Purchase Price: \$ <input type="text"/>	Type of Loan: <input type="text" value="Purchase"/>
Property Type: <input type="text" value="Single Family Home"/>	Occupancy Type: <input type="text" value="Primary"/>
Additional Property Information: <input type="text"/>	
Loan Amount: \$ <input type="text"/>	
Property Street Address: <input type="text"/>	City: <input type="text"/> State: <input type="text" value="DE"/>
Have you been working with a Realtor®? If yes, please supply: Realtor Name: <input type="text"/> Agency Name: <input type="text"/>	
Have you spoken to or been referred to a Superior Mortgage Loan Consultant? If yes, please supply his or her name: <input type="text"/>	
Please help us serve our clients better! How did you hear about Superior Mortgage? <input type="text" value="Internet Search Engine"/>	
If you chose <b>Other</b> above, please specify: <input type="text"/>	
<b>Misc. Information</b>	
How would you like to be contacted? Please Choose One: <input type="text"/>	
Email to contact:	

Before completing this form, please read the  
[Disclosure Regarding Application](#)



Decision and Order

## **DECISION AND ORDER**

The Federal Trade Commission having initiated an investigation of certain acts and practices of the respondent named in the caption hereof, and respondent having been furnished thereafter with a copy of a draft Complaint that the Bureau of Consumer Protection proposed to present to the Commission for its consideration and which, if issued by the Commission, would charge Respondent with violations of the Federal Trade Commission Act, 15 U.S.C. § 45 *et seq.* and the Federal Trade Commission's Standards for Safeguarding Customer Information Rule ("Safeguards Rule"), 16 C.F.R. Part 314, issued pursuant to Title V of the Gramm-Leach-Bliley Act, 15 U.S.C. § 6801 *et seq.*; and

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

The Commission having thereafter considered the matter and having determined that it has reason to believe respondent has violated the said Act and Rule, and that a Complaint should issue stating its charges in that respect, and having thereupon accepted the executed Consent Agreement and placed such Consent Agreement on the public record for a period of thirty (30) days, and having duly considered the comments filed thereafter by interested persons pursuant to Section 2.34 of its Rules, now in further conformity with the procedure described in Section 2.34 of its Rules, the Commission hereby issues its Complaint, makes the following jurisdictional findings and enters the following Order:

## Decision and Order

1. Respondent Superior Mortgage Corp. is a New Jersey corporation with its principal office or place of business at 1395 Route 539, Tuckerton, New Jersey 08087.

2. The Federal Trade Commission has jurisdiction of the subject matter of this proceeding and of Respondent, and the proceeding is in the public interest.

## ORDER

## DEFINITIONS

For purposes of this order, the following definitions shall apply:

1. “Personal information” shall mean individually identifiable information from or about an individual consumer including, but not limited to: (a) a first and last name; (b) a home or other physical address, including street name and name of city or town; (c) an email address or other online contact information, such as an instant messaging user identifier or a screen name that reveals an individual’s email address; (d) a telephone number; (e) a Social Security number; (f) a credit history; (g) a bank or credit card account number; or (h) any other information from or about an individual consumer that is combined with (a) through (g) above.

2. “Commerce” shall mean as defined in Section 4 of the Federal Trade Commission Act, 15 U.S.C. § 44.

3. Unless otherwise specified, “respondent” shall mean Superior Mortgage Corp., its successors and assigns and its officers, agents, representatives, and employees.

4. All other terms are synonymous in meaning and equal in scope to the usage of such terms in the Gramm-Leach-Bliley Act, 15 U.S.C. § 6801 *et seq.*

Decision and Order

I.

IT IS ORDERED that respondent, directly or through any corporation, subsidiary, division, or other device, in connection with the advertising, marketing, promotion, offering for sale, or sale of any product or service, in or affecting commerce, shall not misrepresent in any manner, expressly or by implication, (a) the extent to which personal information submitted by consumers through respondent's websites is protected by SSL encryption, or (b) the extent to which respondent maintains and protects the privacy, confidentiality, or security of any personal information collected from or about consumers.

II.

IT IS FURTHER ORDERED that respondent shall not, directly or through any corporation, subsidiary, division, website, or other device, violate any provision of the Gramm-Leach-Bliley Act's ("GLB Act") Standards for Safeguarding Customer Information Rule ("Safeguards Rule"), 16 C.F.R. Part 314.

In the event the Safeguards Rule is hereafter amended or modified, respondent's compliance with this Rule as so amended or modified shall not be a violation of this order.

III.

IT IS FURTHER ORDERED that, in connection with its compliance with the Safeguards Rule, respondent shall obtain an assessment and report (an "Assessment") from a qualified, objective, independent third-party professional, using procedures and standards generally accepted in the profession, within one hundred and eighty (180) days after service of the order, and biennially thereafter for ten (10) years after service of the order, that:

## Decision and Order

A. sets forth the specific administrative, technical, and physical safeguards that respondent has implemented and maintained during the reporting period;

B. explains how such safeguards are appropriate to respondent's size and complexity, the nature and scope of respondent's activities, and the sensitivity of the nonpublic personal information collected from or about consumers;

C. explains how such safeguards meet or exceed the protections required by the Safeguards Rule; and

D. certifies that respondent's security program is operating with sufficient effectiveness to provide reasonable assurance that the security, confidentiality, and integrity of nonpublic personal information is protected and, for biennial reports, has so operated throughout the reporting period.

Each Assessment shall be prepared by a person qualified as a Certified Information System Security Professional (CISSP); a person qualified as a Certified Information Systems Auditor (CISA); a person holding Global Information Assurance Certification (GIAC) from the SysAdmin, Audit, Network, Security Institute (SANS); or by a similarly qualified person or organization approved by the Associate Director for Enforcement, Bureau of Consumer Protection, Federal Trade Commission.

Respondent shall provide the first Assessment, as well as all plans, reports, studies, reviews, audits, audit trails, policies, training materials, and assessments, whether prepared by or on behalf of respondent, relied upon to prepare such Assessment to the Associate Director for Enforcement, Bureau of Consumer Protection, Federal Trade Commission, Washington, D.C. 20580, within ten (10) days after the Assessment has been prepared. Respondent shall retain all subsequent biennial Assessments until the order is terminated and shall retain all materials relied upon in preparing each such Assessment, as listed above, for a period of three (3) years after the date of preparation of such Assessment.



Decision and Order

Respondent shall provide such subsequent Assessments and related materials to the Associate Director of Enforcement within ten (10) days of request.

IV.

IT IS FURTHER ORDERED that respondent shall deliver a copy of this order to all current and future principals, officers, directors, and managers, and to all current and future employees, agents, and representatives having supervisory responsibilities with respect to the subject matter of this order. Respondent shall deliver this order to such current personnel within thirty (30) days after the date of service of this order, and to such future personnel within thirty (30) days after the person assumes such position or responsibilities.

V.

IT IS FURTHER ORDERED that respondent shall notify the Commission at least thirty (30) days prior to any change in the corporation that may affect compliance obligations arising under this order, including, but not limited to, a dissolution, assignment, sale, merger, or other action that would result in the emergence of a successor corporation; the creation or dissolution of a subsidiary, parent, or affiliate that engages in any acts or practices subject to this order; the proposed filing of a bankruptcy petition; or a change in the corporate name or address. Provided, however, that, with respect to any proposed change in the corporation about which respondent learns less than thirty (30) days prior to the date such action is to take place, respondent shall notify the Commission as soon as is practicable after obtaining such knowledge. All notices required by this Part shall be sent by certified mail to the Associate Director, Division of Enforcement, Bureau of Consumer Protection, Federal Trade Commission, Washington, D.C. 20580.

## Decision and Order

## VI.

IT IS FURTHER ORDERED that respondent shall within one hundred eighty (180) days after service of this order, and at such other times as the Federal Trade Commission may require, file with the Commission a report, in writing, setting forth in detail the manner and form in which it has complied with this order. This report shall include a copy of the initial biennial Assessment required by Part III of this order.

## VII.

This order will terminate twenty (20) years from the date of its issuance, or twenty (20) years from the most recent date that the United States or the Federal Trade Commission files a complaint (with or without an accompanying consent decree) in federal court alleging any violation of the order, whichever comes later; provided, however, that the filing of such a complaint will not affect the duration of:

- A. Any Part in this order that terminates in less than twenty (20) years;
- B. This order's application to any respondent that is not named as a defendant in such complaint; and
- C. This order if such complaint is filed after the order has terminated pursuant to this Part.

Provided, further, that if such complaint is dismissed or a federal court rules that the respondent did not violate any provision of the order, and the dismissal or ruling is either not appealed or upheld on appeal, then the order will terminate according to this Part as though the complaint had never been filed, except that the order will not terminate between the date such complaint is filed and the later of the deadline for appealing such dismissal or ruling and the date such dismissal or ruling is upheld on appeal.

Analysis

**Analysis of Proposed Consent Order to Aid Public Comment**

The Federal Trade Commission has accepted a consent agreement, subject to final approval, from Superior Mortgage Corp. (“Superior Mortgage”). Superior Mortgage is a mortgage lender specializing in residential mortgage loans with headquarters in Tuckerton, New Jersey. Superior Mortgage collects sensitive customer information, including customer names, Social Security numbers, credit histories, and bank and credit card account numbers, and is a “financial institution” subject to the Gramm-Leach-Bliley Act’s Standards for Safeguarding Customer Information Rule, 16 C.F.R. Part 314 (“Safeguards Rule”).

The proposed consent order has been placed on the public record for thirty (30) days for receipt of comments by interested persons. Comments received during this period will become part of the public record. After thirty (30) days, the Commission will again review the agreement and the comments received and will decide whether it should withdraw from the agreement and take other appropriate action or make final the agreement’s proposed order.

This matter concerns Superior Mortgage’s alleged violations of the Safeguards Rule, as well as alleged security misrepresentations to consumers on Superior Mortgage’s website. The Safeguards Rule, which became effective on May 23, 2003, requires financial institutions to implement reasonable policies and procedures to ensure the security and confidentiality of customer information, including:

- Designating one or more employees to coordinate the information security program;
- Identifying reasonably foreseeable internal and external risks to the security, confidentiality, and integrity of customer information, and assessing the sufficiency of any safeguards in place to control those risks;
- Designing and implementing information safeguards to control the risks identified through risk assessment, and regularly testing or otherwise monitoring the effectiveness of the

## Analysis

- safeguards' key controls, systems, and procedures;
- Overseeing service providers, and requiring them by contract to protect the security and confidentiality of customer information; and
  - Evaluating and adjusting the information security program in light of the results of testing and monitoring, changes to the business operation, and other relevant circumstances.

The Commission's complaint alleges that Superior Mortgage failed to implement the protections required by the Safeguards Rule and, specifically, that it failed to: (1) assess risks to its customer information until more than a year after the Safeguard Rule's effective date; (2) institute appropriate password policies to control access to company systems and documents containing sensitive customer information; (3) encrypt or otherwise protect sensitive customer information before sending it by email; and (4) take reasonable steps to ensure that its service providers were providing appropriate security for customer information and addressing known security risks in a timely fashion.

The complaint also alleges that Superior Mortgage violated Section 5 of the Federal Trade Commission Act ("FTC Act") by representing that the personal information it obtained from consumers through [www.supmort.com](http://www.supmort.com) was encrypted using SSL from the time of submission until receipt by Superior Mortgage, when in fact that information was encrypted only while it was being transmitted between a visitor's web browser and the website's server (using SSL); once the information reached the server, it was decrypted and emailed to Superior Mortgage's headquarters and branch offices in clear, readable text.

The proposed order contains provisions designed to prevent Superior Mortgage from future practices similar to those alleged in the complaint. Specifically, Part I of the proposed order prohibits Superior Mortgage from misrepresenting the extent to which it maintains and protects the privacy, confidentiality, or security of any personal information collected from or about consumers. Part II of the proposed order prohibits Superior

Analysis

Mortgage from violating the Safeguards Rule. Part III of the proposed order requires that Superior Mortgage obtain, within 180 days after being served with the final order approved by the Commission, and on a biennial basis thereafter for ten (10) years, an assessment and report from a qualified, objective, independent third-party professional, certifying that: (1) Superior Mortgage has in place a security program that provides protections that meet or exceed the protections required by the Safeguards Rule, and (2) Superior Mortgage's security program is operating with sufficient effectiveness to provide reasonable assurance that the security, confidentiality, and integrity of nonpublic personal information has been protected. This provision is substantially similar to comparable provisions obtained in prior Commission orders under the Safeguards Rule and Section 5 of the FTC Act. *See, e.g., Sunbelt Lending Servs., Inc.*, FTC Docket No. C-4129 (Jan. 7, 2005); *Tower Records*, FTC Docket No. C-4110 (June 2, 2004).

Part III of the proposed order also requires Superior Mortgage to retain documents relating to compliance. For the assessments and supporting documents, Superior Mortgage must retain the documents for three (3) years after the date that each assessment is prepared.

Parts IV through VII of the proposed order are reporting and compliance provisions. Part IV requires dissemination of the order now and in the future to persons with supervisory responsibilities. Part V ensures notification to the FTC of changes in corporate status. Part VI mandates that Superior Mortgage submit compliance reports to the FTC. Part VII is a provision "sunsetting" the order after twenty (20) years, with certain exceptions.

The purpose of this analysis is to facilitate public comment on the proposed order. It is not intended to constitute an official interpretation of the proposed order or to modify its terms in any way.

Complaint

IN THE MATTER OF

**THE PROCTER & GAMBLE COMPANY, AND THE  
GILLETTE COMPANY**CONSENT ORDER, ETC., IN REGARD TO ALLEGED VIOLATIONS OF  
SEC. 7 OF THE CLAYTON ACT AND SEC. 5 OF THE FEDERAL TRADE  
COMMISSION ACT*Docket C-4151; File No. 0510115**Complaint, September 29, 2005--Decision, December 15, 2005*

This consent order addresses the acquisition by Respondent The Procter & Gamble Company – one of the largest and most diversified suppliers of consumer products in the world – of Respondent The Gillette Company, another large supplier of consumer products. The order, among other things, requires the respondents to divest Gillette's Rembrandt® at-home teeth whitening business to a Commission-approved acquirer, within three months. The order also requires the respondents to divest Procter & Gamble's Crest® SpinBrush™ battery-powered and rechargeable toothbrush business to Church & Dwight or another Commission-approved acquirer, and to divest Gillette's Right Guard® men's antiperspirant/deodorant business to a Commission-approved acquirer within four months. In addition, the order requires Procter & Gamble to amend its joint venture agreement with Philips Oral Healthcare, Inc. -- regarding the Crest® Sonicare® IntelliClean System rechargeable toothbrush -- to allow Philips to independently market and sell the IntelliClean product. An accompanying Order to Maintain Assets requires the respondents to maintain the viability of the Rembrandt and Right Guard businesses as competitive operations until the businesses are transferred to acquirers approved by the Commission.

*Participants*

For the Commission: *Norman A. Armstrong, Jr., Stephanie C. Bovee, Andrew J. Forman, Stephanie A. Parks, Sylvia M. Brooks, Daniel Kane, Jacob Swanton, Matthew J. Reilly, Michael R. Moiseyev, Kenneth Libby, David von Nirschl, Michele Cerullo, Roberta Baruch, John Yun, Steven Tenn, Michael G. Vita and Mark Frankena.*

For the Respondent: *Joe Sims, Jones Day, and Arthur F. Golden, Davis Polk & Wardwell.*

Complaint

## COMPLAINT

Pursuant to the Clayton Act and the Federal Trade Commission Act, and its authority thereunder, the Federal Trade Commission (“Commission”), having reason to believe that Respondent The Procter & Gamble Company (“Procter & Gamble”), a corporation subject to the jurisdiction of the Commission, has agreed to acquire Respondent The Gillette Company (“Gillette”), a corporation subject to the jurisdiction of the Commission, in violation of Section 7 of the Clayton Act, as amended, 15 U.S.C. § 18, and Section 5 of the Federal Trade Commission Act, as amended, 15 U.S.C. § 45, and it appearing to the Commission that a proceeding in respect thereof would be in the public interest, hereby issues its Complaint, stating its charges as follows:

### I. RESPONDENT PROCTER & GAMBLE

1. Respondent Procter & Gamble is a corporation organized, existing and doing business under the laws of Ohio with its office and principal place of business located at One Procter & Gamble Plaza, Cincinnati, Ohio, 45202.
2. Respondent Procter & Gamble, among other things, is engaged in the research, development, manufacture, distribution, and sale of consumer products, including at-home teeth whitening products, adult battery-powered toothbrushes, and men’s antiperspirants/deodorants.
3. Respondent Procter & Gamble had worldwide net sales of approximately \$51.4 billion in its 2004 fiscal year.
4. Respondent Procter & Gamble is, and at all times relevant herein has been, engaged in commerce, as “commerce” is defined in Section 1 of the Clayton Act, as amended, 15 U.S.C. §12, and is a corporation whose business is in or affects commerce, as “commerce” is defined in Section 4 of the Federal Trade Commission Act, as amended, 15 U.S.C. § 44.

Complaint

## II. RESPONDENT GILLETTE

5. Respondent Gillette is a corporation organized, existing, and doing business under the laws of Delaware with its office and principal place of business located at the Prudential Tower Building, Suite 4800, Boston, Massachusetts, 02199.

6. Respondent Gillette, among other things, is engaged in the research, development, manufacture, distribution, and sale of consumer products, including at-home teeth whitening products, adult battery-powered toothbrushes, rechargeable toothbrushes, and antiperspirants/deodorants.

7. Respondent Gillette had worldwide net sales of approximately \$10.5 billion in its 2004 fiscal year.

8. Respondent Gillette is, and at all times herein has been, engaged in commerce, as “commerce” is defined in Section 1 of the Clayton Act, as amended, 15 U.S.C. § 12, and is a corporation whose business is in or affects commerce, as “commerce” is defined in Section 4 of the Federal Trade Commission Act, as amended, 15 U.S.C. § 44.

## III. THE PROPOSED ACQUISITION

9. Pursuant to an Agreement and Plan of Merger dated January 27, 2005, Respondent Procter & Gamble proposed to acquire 100 percent of the voting securities of Respondent Gillette for approximately \$57 billion (the “Acquisition”).

## IV. THE RELEVANT MARKETS

10. For the purposes of this Complaint, the relevant lines of commerce in which to analyze the effects of the Acquisition are the research, development, manufacture, distribution, and sale of: (a) at-home teeth whitening products; (b) adult-battery powered toothbrushes; (c) rechargeable toothbrushes; and (d) men’s



Complaint

antiperspirants/deodorants.

11. At-home teeth whitening products whiten teeth by bleaching them with either hydrogen or carbamide peroxide. These products are typically sold over-the-counter through food, drug, club, and mass merchandise channels and are marketed to be used by consumers at home. There are several different types of at-home teeth whitening products, including whitestrips, gels, pens and sticks. Whitestrips and gel products account for the vast majority of sales of at-home teeth whitening products in the United States.

12. Adult battery-powered toothbrushes are usually powered by AA or AAA batteries and either have oscillating or pulsating brush heads. The majority of adult battery-powered toothbrushes are sold for between \$5 and \$8, and the batteries and brush heads can be replaced on some, but not all, products. Adult battery-powered toothbrushes are typically marketed as upgrades over manual toothbrushes, while at the same time more affordable than sophisticated rechargeable toothbrushes.

13. Rechargeable toothbrushes contain a rechargeable battery that powers high-speed oscillating, pulsating, or vibrating brush heads. They have a separate recharging unit that needs to be plugged into an electrical outlet to recharge the battery contained in the toothbrush. Brush heads for these products are almost always replaceable. Rechargeable toothbrushes typically range in price from \$20 to \$150, and are marketed as the premium brushing option for consumers.

14. Antiperspirants/deodorants are applied under the arms to enhance personal hygiene, and are typically combined together for complete under-arm protection. Antiperspirants/deodorants are sold to specific gender-based segments in various forms, including roll-ons, traditional solids, invisible solids, gels, and aerosols. Men's antiperspirants/deodorants are unique in, among other things, their branding, packaging, fragrances, marketing, strength, and location on the shelf.

## Complaint

15. For the purposes of this Complaint, the United States is the relevant geographic area in which to analyze the effects of the Acquisition in each of the relevant lines of commerce.

**V. THE STRUCTURE OF THE RELEVANT MARKETS**

16. The relevant market for the manufacture, distribution, and sale of at-home teeth whitening products in the United States is highly concentrated whether measured by the Herfindahl-Hirschman Index (“HHI”) or two- or four-firm concentration ratios. Respondents Procter & Gamble and Gillette are the two largest suppliers of at-home teeth whitening products in the United States and are the only significant suppliers of branded at-home teeth whitening strips. Procter & Gamble is the market leader with its Crest Whitestrips® and Crest Night Effects® products, while Gillette is the second leading supplier with its Oral-B® Rembrandt® and Rembrandt® products. Together, they account for over 80% of the sales in this highly concentrated market. Accordingly, the Acquisition would significantly increase the concentration level in the United States market for at-home teeth whitening products, leaving Procter & Gamble as the dominant supplier. Respondents are actual competitors in this relevant market.

17. The relevant market for the research, development, manufacture, distribution, and sale of adult battery-powered toothbrushes in the United States is highly concentrated whether measured by HHI or two- or four-firm concentration ratios. Respondents Procter & Gamble and Gillette are the two largest suppliers of adult battery-powered toothbrushes in the United States. Procter & Gamble markets its adult battery-powered products under the Crest® SpinBrush™ brand name, while Gillette sells its adult battery-powered products under the Oral-B® brand name. Together, Respondents account for over 85% of this highly concentrated market. Accordingly, the Acquisition would significantly increase the concentration level in the United

Complaint

States market for adult battery-powered toothbrushes, leaving Procter & Gamble as the dominant supplier. Respondents are actual competitors in this relevant market.

18. The relevant market for the research, development, manufacture, distribution, and sale of rechargeable toothbrushes in the United States is highly concentrated whether measured by HHI or two- or four-firm concentration ratios. Respondent Gillette and Philips Oral Health Care, Inc. (“Philips”) are the only significant suppliers of rechargeable toothbrushes in the United States. Gillette markets a full line of rechargeable toothbrush products (*i.e.*, low-end to high-end) under the Oral-B® Braun® brand name, while Philips sells mostly mid to high-end products under the Philips® Sonicare® brand name. Respondent Procter & Gamble and Philips are joint venture partners in the development and marketing of the Crest® Sonicare® IntelliClean System (“IntelliClean”), the first integrated toothbrush/dentifrice product (*i.e.*, toothbrush that self dispenses toothpaste) sold in the United States. Pursuant to the Acquisition, Respondent Procter & Gamble would acquire the only significant competitor to its joint venture partner, Philips.

19. The relevant market for the research, development, manufacture, distribution, and sale of men’s antiperspirants/deodorants in the United States is highly concentrated whether measured by the HHI or two- or four-firm concentration ratios. Respondents are the two largest suppliers of men’s antiperspirants/deodorants in the United States. Procter & Gamble markets its men’s antiperspirants/deodorants under the Old Spice® brand name, while Gillette sells its products under the Right Guard® and Gillette Series® brand names. Together, Respondents account for over 50% of the sales in this highly concentrated market. Accordingly, the Acquisition would significantly increase the concentration level in the United States market for men’s antiperspirants/deodorants, leaving Procter & Gamble as the dominant supplier. Respondents are actual competitors in this relevant market.

Complaint

**VI. ENTRY CONDITIONS**

20. Entry into any relevant line of commerce would not be timely, likely, or sufficient to deter or counteract the anticompetitive effects of the Acquisition set forth in Paragraph 21 below. Entry into any of these markets would require the investment of extremely high sunk costs to, among other things, develop products, establish a brand name, and provide promotional funding and advertising to support the product(s), which would be difficult to justify given the market structure in the affected markets. Additionally, patents and other intellectual property create significant barriers to entry in the at-home teeth whitening, adult battery-powered, and rechargeable toothbrush markets. Even if a new entrant were willing to take on such investments, it would also face the difficult task of convincing retailers to carry its products. As a result, new entry into any of these markets sufficient to achieve a significant market impact within two years is unlikely.

**VII. EFFECTS OF THE ACQUISITION**

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

- a. by eliminating actual, direct, and substantial competition between Respondents Procter & Gamble and Gillette for the research, development, manufacture, distribution, and sale of at-home teeth whitening products, adult battery-powered toothbrushes, and men's antiperspirants/deodorants in the United States;
- b. by reducing the merged entity's incentives to adequately support and promote the IntelliClean product and joint venture;

Complaint

- c. by increasing the ability of the merged entity to unilaterally raise prices of at-home teeth whitening products, adult battery-powered toothbrushes, and men's antiperspirants/deodorants in the United States; and
- d. by reducing the merged entity's incentives to improve service or product quality for at-home teeth whitening products, adult battery-powered toothbrushes, rechargeable toothbrushes, and men's antiperspirants/deodorants in the United States.

**VII. VIOLATIONS CHARGED**

22. The Acquisition described in Paragraph 9 constitutes a violation of Section 5 of the FTC Act, as amended, 15 U.S.C. § 45.

23. The Acquisition described in Paragraph 9, if consummated, would constitute a violation of Section 7 of the Clayton Act, as amended, 15 U.S.C. § 18, and Section 5 of the FTC Act, as amended, 15 U.S.C. § 45.

WHEREFORE, THE PREMISES CONSIDERED, the Federal Trade Commission on this twenty-ninth day of September, 2005, issues its Complaint against said Respondent.

Decision and Order

**DECISION AND ORDER**

The Federal Trade Commission ("Commission"), having initiated an investigation of the proposed acquisition by Respondent The Procter & Gamble Company ("P&G") of Respondent The Gillette Company ("Gillette"), hereinafter referred to as "Respondents," and Respondents having been furnished thereafter with a copy of a draft Complaint that the Bureau of Competition proposed to present to the Commission for its consideration and that, if issued by the Commission, would charge Respondents with violations of Section 7 of the Clayton Act, as amended, 15 U.S.C. § 18, and Section 5 of the Federal Trade Commission Act, as amended, 15 U.S.C. § 45; and

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

The Commission having thereafter considered the matter and having determined that it had reason to believe that Respondents have violated the said Acts, and that a Complaint should issue stating its charges in that respect, and having thereupon issued its Complaint and an Order to Maintain Assets (attached to this Order as Appendix I), and having accepted the executed Consent Agreement and placed such Consent Agreement on the public record for a period of thirty (30) days for the receipt and consideration of public comments, now in further conformity with the procedure described in Commission Rule 2.34, 16 C.F.R. § 2.34, the Commission hereby makes the following jurisdictional findings and issues the following Decision and Order ("Order"):

Decision and Order

1. Respondent P&G is a corporation organized, existing and doing business under and by virtue of the laws of the state of Ohio, with its offices and principal place of business located at One Procter & Gamble Plaza, Cincinnati, Ohio 45202.
2. Respondent Gillette is a corporation organized, existing and doing business under and by virtue of the laws of the state of Delaware, with its offices and principal place of business located at Prudential Tower, Boston, Massachusetts 02199.
3. The Commission has jurisdiction of the subject matter of this proceeding and of Respondents, and the proceeding is in the public interest.

**ORDER**

**I.**

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

- A. "P&G" means The Procter & Gamble Company, its directors, officers, employees, agents, representatives, predecessors, successors, and assigns; and its joint ventures, subsidiaries, divisions, groups and affiliates in each case controlled by P&G, and the respective directors, officers, employees, agents, representatives, predecessors, successors, and assigns of each. After the Acquisition, P&G shall include Gillette.
- B. "Gillette" means The Gillette Company, its directors, officers, employees, agents, representatives, predecessors, successors, and assigns; and its joint ventures, subsidiaries, divisions, groups and affiliates in each case controlled by Gillette, and the respective directors, officers, employees, agents, representatives, predecessors, successors, and assigns of each.

## Decision and Order

- C. "Respondents" means P&G and Gillette, individually and collectively.
- D. "Church & Dwight" means Church & Dwight Co., Inc., a corporation organized, existing, and doing business under and by virtue of the laws of the State of Delaware, having its principal place of business located at 469 North Harrison Street, Princeton, NJ 08543.
- E. "Philips" means Philips Oral Healthcare, Inc., a corporation organized, existing, and doing business under and by virtue of the laws of the State of Washington, with its offices and principal place of business located at 35301 Center Street, Snoqualmie, Washington 98065, together with its affiliates.
- F. "Acquisition" means the acquisition contemplated by the "Agreement and Plan of Merger" dated as of January 27, 2005, among The Procter & Gamble Company, Aquarium Acquisition Corp. and The Gillette Company.
- G. "Commission" means the Federal Trade Commission.
- H. "Acquisition Date" means the earlier of the following dates:
1. the date the Respondents close on the Acquisition pursuant to the Acquisition Agreement; or
  2. the date the merger contemplated by the Acquisition Agreement becomes effective by filing the certificate of merger with the Secretary of State of the State of Delaware.
- I. "Agency(ies)" means any governmental regulatory authority or authorities in the world responsible for granting approval(s), clearance(s), qualification(s), license(s), or permit(s) for any aspect of the research, Development, manufacture, marketing, distribution, or sale of the



Decision and Order

Divestiture Products or the IntelliClean Products, respectively.

- J. “APDO Assets” means all of Respondent Gillette’s rights, title and interest in and to all assets related to Respondent Gillette’s worldwide business related to the APDO Products to the extent legally transferable, including the research, Development, manufacture, distribution, marketing, and sale of the APDO Products including, without limitation, the following:
1. all Product Intellectual Property related to the APDO Products (which shall also include the following Product Trademarks: Power Stripe<sup>®</sup>; Power Caps<sup>®</sup> and Cool Spray<sup>®</sup>, or any variations or derivatives of such Product Trademarks; *provided however*, that Respondents may receive a transitional license back for a limited period of time (as is approved by the Commission in the Remedial Agreements related to the APDO Products) to these three Product Trademarks for the purposes of winding up the use of such Product Trademarks in Respondent Gillette’s businesses associated with such Product Trademarks);
  2. perpetual, fully paid-up and royalty-free license(s) with rights to sublicense to all Product Licensed Intellectual Property to use, make, distribute, offer for sale, promote, advertise, sell, import, export, or have used, made, distributed, offered for sale, promoted, advertised, sold, imported, or exported the APDO Products anywhere in the world;
  3. all Product Manufacturing Technology related to the APDO Products;
  4. all Product Marketing Materials related to the APDO Products;
  5. all Website(s) related to the APDO Products;

## Decision and Order

6. at the Commission-approved Acquirer's option, all Product Assumed Contracts related to the APDO Products (copies to be provided to the Commission-approved Acquirer on or before the Closing Date);
7. all Respondent Gillette's books, records, and files related to the foregoing or to the APDO Products; *provided, however,* that in cases in which documents or other materials included in the APDO Assets contain information: (1) that relates both to the APDO Products and to other Products or businesses of Respondent Gillette and cannot be segregated in a manner that preserves the usefulness of the information as it relates to the APDO Products; or (2) for which Respondent Gillette has a legal obligation to retain the original copies, Respondent Gillette shall be required to provide only copies or relevant excerpts of the documents and materials containing this information. In instances where such copies are provided to the Commission-approved Acquirer, Respondent Gillette shall provide the Commission-approved Acquirer access to original documents under circumstances where copies of documents are insufficient for evidentiary or regulatory purposes. The purpose of this proviso is to ensure that Respondent Gillette provides the Commission-approved Acquirer with the above-described information without requiring Respondent Gillette completely to divest itself of information that, in content, also relates to Products and businesses other than the APDO Products;
8. list of all customers and/or targeted customers for the APDO Products and the pricing and/or planned or proposed pricing of the APDO Products for such customers;
9. at the Commission-approved Acquirer's option, all inventory in existence as of the Closing Date including, but not limited to, raw materials, packaging materials,

Decision and Order

work-in-process and finished goods related to the APDO Products;

10. all unfilled customer orders for finished goods as of the Closing Date related to the APDO Products (a list of such orders is to be provided to the Commission-approved Acquirer within two (2) days after the Closing Date); and
  11. at the Commission-approved Acquirer's option, the APDO Manufacturing Equipment.
- K. "APDO Core Employee(s)" means the Product Manufacturing Employees, the Product Marketing Employees, the Product Research and Development Employees and the Product Sales Employees related to the APDO Products.
- L. "APDO Manufacturing Equipment" means all manufacturing and other equipment located at Respondent Gillette's facility located in Andover, Massachusetts, that was used, within the one (1) year period immediately prior to the Acquisition and/or within the one (1) year period immediately prior to the Closing Date, in the research, Development, manufacture, or packaging of the APDO Products.
- M. "APDO Products" means all Products Developed, in Development, manufactured, distributed, marketed or sold by Respondent Gillette prior to the Acquisition that were marketed or sold or to be marketed or sold as Products using the Product Trademark Right Guard<sup>®</sup> or any variations or derivatives of such Product Trademark; *provided however*, that, at the Commission-approved Acquirer's option, "APDO Products" shall also include all Products Developed, in Development, manufactured, distributed, marketed or sold by Respondent Gillette prior to the Acquisition that were marketed or sold or to be marketed or sold as Products using any of the Product

## Decision and Order

Trademarks Soft&Dri<sup>®</sup> and Dry Idea<sup>®</sup> or any variations or derivatives of such Product Trademarks; *provided further*, that, pending Commission approval of the divestiture of the APDO Assets, “APDO Products” includes Products using the Product Trademarks Soft&Dri<sup>®</sup> and Dry Idea<sup>®</sup> for the purposes of any requirements under this Order or the Order to Maintain Assets to maintain assets; *provided further*, that “APDO Products” does not include Products Developed, in Development, manufactured, distributed, marketed or sold by Respondent Gillette prior to the Acquisition that were marketed or sold or to be marketed or sold as Products using the Product Trademark Gillette Series<sup>®</sup> or any variations or derivatives of such Product Trademark.

- N. “APDO Releasees” means the Commission-approved Acquirer for the APDO Products or any entity controlled by or under common control with such Commission-approved Acquirer, or any licensees, sublicensees, manufacturers, suppliers, distributors, and customers of such Commission-approved Acquirer, or of such Commission-approved Acquirer-affiliated entities.
- O. “Closing Date” means as to each Divestiture Product the date on which Respondent (or a Divestiture Trustee) closes on the divestiture of the assets relevant to such Divestiture Product pursuant to this Order.
- P. “Commission-approved Acquirer” means the following: (1) an entity that is specifically identified in this Order to acquire particular assets that the Respondents are required to assign, grant, license, divest, transfer, deliver, or otherwise convey pursuant to this Order and that has been approved by the Commission to accomplish the requirements of this Order in connection with the Commission’s determination to make this Order final; or (2) an entity approved by the Commission to acquire particular assets that the Respondents are required to assign, grant, license, divest,

Decision and Order

transfer, deliver, or otherwise convey pursuant to this Order.

- Q. “Confidential Business Information” means all information owned by, or in the possession or control of, Respondents that is not in the public domain and that is related to the research, Development, manufacture, marketing, commercialization, importation, exportation, cost, pricing, supply, sales, sales support or use of the Divestiture Product(s) or the IntelliClean Products, respectively; provided however, that “Confidential Business Information” shall not include, the following:
1. information that subsequently falls within the public domain through no violation of this Order or breach of confidentiality or non-disclosure agreement with respect to such information by Respondents;
  2. information related to the SpinBrush Products that Respondent Gillette can demonstrate it obtained without the assistance of Respondent P&G prior to the Acquisition;
  3. information related to the Rembrandt Products that Respondent P&G can demonstrate it obtained without the assistance of Respondent Gillette prior to the Acquisition;
  4. information related to the APDO Products that Respondent P&G can demonstrate it obtained without the assistance of Respondent Gillette prior to the Acquisition;
  5. information related to the IntelliClean Products that Respondent Gillette can demonstrate it obtained without the assistance of Respondent P&G prior to the Acquisition;
  6. information that is required by Law to be publically disclosed; or

## Decision and Order

7. information that does not relate to the Divestiture Product(s) or the IntelliClean Products.
- R. “Contract Manufacture” means the manufacture of a Divestiture Product or the IntelliClean Products to be supplied by Respondent or a Designee.
- S. “Designee” means any entity other than Respondents that will manufacture a Divestiture Product for a Commission-approved Acquirer.
- T. “Development” means formulation, design (including packaging design), process development, manufacturing scale-up, development-stage manufacturing, quality assurance/quality control development, Product approval and registration. “Develop” means to engage in Development.
- U. “Direct Cost” means a cost not to exceed the cost of direct labor and direct material used to provide the relevant assistance or service. “Direct Cost” to the Commission-approved Acquirer’s for its use of any of the Respondents’ employees shall not exceed the average hourly wage rate for such employee.
- V. “Divestiture Product” means a Product that is the subject of a divestiture under this Order, *i.e.*, the APDO Products, the Rembrandt Products, or the SpinBrush Products, individually and collectively.
- W. "Divestiture Trustee" means the trustee appointed by the Commission pursuant to the relevant provisions of this Order.
- X. “Domain Name” means the domain name(s) (universal resource locators) and registration(s) thereof, issued by any entity or authority that issues and maintains the domain name registration. “Domain Name” shall not include any

Decision and Order

trademark or service mark rights to such domain names other than the rights to the Product Trademarks related to the Divestiture Products.

- Y. “Governmental Entity” means any Federal, state, local or non-U.S. government, or any court, legislature, governmental agency, or governmental commission, or any judicial or regulatory authority of any government.
- Z. “High Volume Retail Account” means any retailer or distributor whose annual and/or projected aggregate annual sales in units or in dollars of a Divestiture Product in the United States on a company-wide level was or is among the top twenty highest of such sales within the United States on any of the following dates: 1) the end of the last quarter that immediately preceded the date of the public announcement of the proposed Acquisition; 2) the end of the last quarter that immediately preceded the Acquisition Date; or 3) the end of the last quarter that immediately preceded the Closing Date for the relevant assets.
- AA. “IntelliClean Products” means all Products Developed, in Development, manufactured, distributed, marketed or sold pursuant to the IntelliClean Agreement. This includes those toothbrushes marketed using the Sonicare<sup>®</sup> trademark and any variations or derivatives of such trademark and the dentifrice Product used in connection with the rechargeable toothbrush(es) that are a part of the IntelliClean Products.
- BB. “IntelliClean Agreement” means the “Commercialization Agreement (ONYX Advanced)” between Philips Oral Healthcare, Inc. and The Procter & Gamble Company dated as of August 1, 2003 including all amendments, exhibits, attachments, agreements, and schedules thereto entered into prior to the public announcement of the Acquisition, including, but not limited to, the “P&G/Philips Joint Evaluation Agreement Project

## Decision and Order

ONYX” dated October 23, 2001. The IntelliClean Agreement is attached to this Order and contained in non-public Appendix III.

- CC. “IntelliClean Amended Agreement” means the “Agreement to Amend Commercialization Agreement (ONYX Advanced)” between Philips Oral Healthcare, Inc. and The Procter & Gamble Company dated September 21, 2005, and all amendments, exhibits, attachments, agreements, and schedules thereto, related to the Product IntelliClean, that have been approved by the Commission to accomplish the requirements of this Order. The IntelliClean Amended Agreement is attached to this Order and contained in non-public Appendix III. Upon amendment of the IntelliClean Agreement in accordance with the above-described agreement to amend, the “IntelliClean Amended Agreement” shall mean the “IntelliClean Agreement” as so amended.
- DD. “Interim Monitor” means any monitor appointed pursuant to Paragraph VI of this Order or Paragraph III of the related Order to Maintain Assets.
- EE. “Law” means all laws, statutes, rules, regulations, ordinances, and other pronouncements by any Governmental Entity having the effect of law.
- FF. “Order to Maintain Assets” means the Order to Maintain Assets incorporated into and made a part of the Agreement Containing Consent Orders. The Order to Maintain Assets is attached to this Order and contained in Appendix I.
- GG. “Patents” means all patents, patent applications, and statutory invention registrations, in each case existing as of the Closing Date (*except* where this Order specifies a different time), and includes all reissues, divisions, continuations, continuations-in-part, supplementary protection certificates, extensions and reexaminations



Decision and Order

thereof, all inventions disclosed therein, all rights therein provided by international treaties and conventions, and all rights to obtain and file for patents and registrations thereto in the world, related to any Product of or owned by Respondent(s) as of the Closing Date.

- HH. “Person” means any individual, partnership, joint venture, firm, corporation, association, trust, unincorporated organization, joint venture, or other business or governmental entity, and any subsidiaries, divisions, groups or affiliates thereof.
- II. “Product” means a retail consumer good Developed, made, distributed, marketed or sold by Respondent(s).
- JJ. “Product Assumed Contracts” means all of the following contracts or agreements:
1. pursuant to which any Third Party purchases the Divestiture Product(s) from the Respondent(s);
  2. pursuant to which the Respondent(s) purchases any materials from any Third Party for use in connection with the manufacture of the Divestiture Product(s);
  3. relating to any quality control trials involving the Divestiture Product(s);
  4. relating to the marketing of the Divestiture Product(s) or educational matters relating to the Divestiture Product(s) including, but not limited to, the slotting and/or shelf spacing assignments of the Divestiture Product with the High Volume Retail Accounts;
  5. relating to the manufacture of the Divestiture Product(s);
  6. constituting confidentiality agreements involving the Divestiture Product(s);

## Decision and Order

7. involving any royalty, licensing, or similar arrangement involving the Divestiture Product(s);
8. pursuant to which any services are provided with respect to the Divestiture Product(s) or the Divestiture Product(s) business, including consultation arrangements; and/or
9. pursuant to which any Third Party collaborates with the Respondent(s) in the performance of research, Development, marketing or selling of the Divestiture Product(s) or the Divestiture Product(s) business;

*provided, however,* that where any such contract or agreement also relates to a Retained Product(s), Respondent(s) shall assign the Commission-approved Acquirer all such rights under the contract or agreement as are related to the Divestiture Product(s), but concurrently may retain similar rights for the purposes of the Retained Product(s).

KK. “Product Copyrights” means rights to all original works of authorship of any kind related to the Divestiture Product(s) or the IntelliClean Products and any registrations and applications for registrations thereof, including, but not limited to, the following: all promotional materials for retailers; all promotional materials for customers; copyrights in Development data and reports relating to the research and Development of the Divestiture Product(s) or the IntelliClean Products or of any materials used in the research, Development, manufacture, marketing or sale of the Divestiture Product(s) or the IntelliClean Products, including all raw data relating to quality trials of the Product(s), customer information, promotional and marketing materials, the Divestiture Product(s) or the IntelliClean Products sales forecasting models, Website content and advertising and display materials; all records relating to employees who accept employment with the Commission-approved Acquirer (excluding any personnel records the transfer of

Decision and Order

which is prohibited by applicable Law); all records, including customer lists, sales force call activity reports, vendor lists, sales data, slotting allowance data, speaker lists, manufacturing records, manufacturing processes, and supplier lists; all data contained in laboratory notebooks relating to the Divestiture Product(s) or the IntelliClean Products.

LL. “Product Employee Information” means the following, as and to the extent permitted by the Law:

1. a complete and accurate list containing the name of each relevant employee (including former employees who were employed by Respondent(s) within ninety (90) Days of the execution date of any Remedial Agreement);
2. with respect to each such employee, the following information:
  - a. the date of hire and effective service date;
  - b. job title or position held;
  - c. a specific description of the employee’s responsibilities related to the relevant Divestiture Product; *provided, however*, in lieu of this description, Respondent(s) may provide the employee’s most recent performance appraisal;
  - d. the base salary or current wages;
  - e. the most recent bonus paid, aggregate annual compensation for the Respondent’s last fiscal year and current target or guaranteed bonus, if any;
  - f. employment status (*i.e.*, active or on leave or disability; full-time or part-time); and

## Decision and Order

- g. any other material terms and conditions of employment in regard to such employee that are not otherwise generally available to similarly situated employees; and
3. at the Commission-approved Acquirer's option or the Proposed Acquirer's option (as applicable), copies of all employee benefit plans and summary plan descriptions (if any) applicable to the relevant employees.
- MM. "Product Intellectual Property" means all of the following related to a Divestiture Product or the IntelliClean Products (other than Product Licensed Intellectual Property):
1. Patents;
  2. Product Copyrights;
  3. Product Trademarks, trade names, Product Trade Dress, trade secrets, know-how, techniques, data, inventions, practices, methods, and other confidential or proprietary technical, business, research, Development and other information; and
  4. rights to obtain and file for patents and registrations thereof;

*provided, however*, "Product Intellectual Property" does not include the names or trade dress of "Procter & Gamble", "P&G", "Gillette", "Oral-B", "Crest", "Blend-a-Med", "Blend-a-Dent", "Blendi", "Ipana", "AZ", "Series", or the names or trade dress of any other corporations, companies, or brands owned or sold by Respondents or related logos to the extent used on Respondent P&G's or Respondent Gillette's Retained Products.

Decision and Order

NN. “Product Licensed Intellectual Property” means the following:

1. Patents that are related to a Divestiture Product or the IntelliClean Products that Respondent(s) can demonstrate have been routinely used, prior to the Acquisition Date, by either Respondent P&G or Respondent Gillette (as applicable) for a Retained Product(s) that: 1) have been marketed or sold on an extensive basis by the relevant Respondent within the two-year period immediately preceding the Acquisition; or 2) for which, prior to the announcement of the Acquisition, there was an approved brand or marketing plan to market or sell such a Retained Product on an extensive basis by the Respondents; and
2. trade secrets, know-how, techniques, data, inventions, practices, methods, and other confidential or proprietary technical, business, research, Development, and other information, and all rights in any jurisdiction to limit the use or disclosure thereof, that are related to a Divestiture Product or the IntelliClean Products and that Respondent(s) can demonstrate have been routinely used, prior to the Acquisition Date, by either Respondent P&G or Respondent Gillette (as applicable) for Retained Product(s) that: 1) have been marketed or sold on an extensive basis by the relevant Respondent within the two-year period immediately preceding the Acquisition; or 2) for which, prior to the announcement of the Acquisition, there was an approved brand or marketing plan to market or sell such a Retained Product on an extensive basis by the Respondents;

*provided however*, that, in cases where the aggregate retail sales in dollars within the two-year period immediately preceding the Acquisition of the Retained Product(s) collectively are less than the aggregate retail sales in dollars within the same period of the Divestiture Product(s) collectively, the above-described intellectual property shall be

## Decision and Order

considered, at the Commission-approved Acquirer's option, Product Intellectual Property and, thereby, subject to assignment to the Commission-approved Acquirer; *provided further, however*, that in such cases, Respondents may take a license back from the Commission-approved Acquirer for such intellectual property for use in connection with the Retained Products.

- OO. "Product Manufacturing Employees" means all salaried employees of Respondent(s) who directly have participated (irrespective of the portion of working time involved, unless such participation was part of a broad executive management portfolio above the level of value stream manager at Respondent Gillette, or consisted of oversight of legal, accounting, tax or financial compliance) in the manufacture of the Product(s), including, but not limited to, those involved in the quality assurance and quality control of the Product(s), within the eighteen (18) month period immediately prior to the Closing Date.
- PP. "Product Manufacturing Technology" means all technology, trade secrets, know-how, and proprietary information (whether patented, patentable or otherwise) related to the manufacture (including, at the Commission-approved Acquirer's option, all equipment used to manufacture) the Divestiture Products or the IntelliClean Products, respectively, including, but not limited to all product specifications, processes, product designs, plans, trade secrets, ideas, concepts, manufacturing, engineering, and other manuals, and drawings, standard operating procedures, flow diagrams, chemical, safety, quality assurance, quality control, research records, clinical data, compositions, annual product reviews, regulatory communications, and labeling and all other information related to the manufacturing process, and supplier lists.

Decision and Order

- QQ. “Product Marketing Employees” means salaried management level employees of Respondent(s) who directly have participated (irrespective of the portion of working time involved, unless such participation was a part of a broad executive management portfolio above the brand manager level, or of oversight of legal, accounting, tax or financial compliance) in the marketing, contracting, or promotion of the Divestiture Product(s) in the United States within the eighteen (18) month period immediately prior to the Closing Date. These employees include, without limitation, all management level employees having any responsibilities in the areas of sales management, brand management, sales training, market research, but excluding administrative assistants.
- RR. “Product Marketing Materials” means all marketing materials used anywhere in the world related to the Divestiture Product(s) as of the Closing Date, including, without limitation, all advertising materials, training materials, product data, price lists, mailing lists, sales materials (e.g., detailing reports; vendor lists; sales data), marketing information, (e.g., competitor information; research data; market intelligence reports; statistical programs (if any) used for marketing and sales research; customer information, including customer sales information; sales forecasting models; educational materials; Website content and advertising and display materials; speaker lists), promotional and marketing materials, artwork for the production of packaging components, television masters and other similar materials related to the Divestiture Product(s).
- SS. “Product Research and Development Employees” means all salaried employees of Respondent(s) who directly have participated (irrespective of the portion of working time involved, unless such participation was a part of a broad executive management portfolio above the section head

## Decision and Order

level at Respondent P&G or above the level of associate director at Respondent Gillette (for the APDO Products) or above the level of director at Respondent Gillette (for the Rembrandt Products), or of oversight of legal, accounting, tax or financial compliance) in the research, Development, or quality control approval process of the Divestiture Product(s) within the eighteen (18) month period immediately prior to the Closing Date.

- TT. “Product Sales Employees” means all salaried employees of Respondent(s) who have participated (irrespective of the portion of working time involved, unless such participation was a part of a broad executive management portfolio above the level of the manager for a category of Products within the customer business development team for a High Volume Retail Account or of oversight of legal, accounting, tax or financial compliance) in the marketing or promotion of the Divestiture Product(s) in the United States directly to a High Volume Retail Account for the Divestiture Product(s) during the twelve (12) month period immediately prior to the Acquisition Date until the Closing Date for the assets related to such Divestiture Product(s).
- UU. “Product Trade Dress” means the current trade dress of the Product, including but not limited to, Product packaging, and the lettering of the Product trade name or brand name.
- VV. “Product Trademark(s)” means all proprietary names or designations, trademarks, service marks, tradenames, and brand names, including registrations and applications for registration therefor (and all renewals, modifications, and extensions thereof) and all common law rights, and the goodwill symbolized thereby and associated therewith, for the Product(s).
- WW. “Proposed Acquirer” means an entity proposed by the Respondent(s) (or a Divestiture Trustee) to the



Decision and Order

Commission and submitted for the approval of the Commission as the acquirer for particular assets required to be assigned, granted, licensed, divested, transferred, delivered or otherwise conveyed by Respondent(s) pursuant to this Order.

- XX. “Rembrandt Assets” means all Respondent Gillette’s rights, title and interest in and to all assets related to Respondent Gillette’s worldwide business related to the Rembrandt Products to the extent legally transferable, including the research, Development, manufacture, distribution, marketing, and sale of the Rembrandt Products, including, without limitation, the following:
1. all Product Intellectual Property related to the Rembrandt Products;
  2. perpetual, fully paid-up and royalty-free license(s) with rights to sublicense to all Product Licensed Intellectual Property to use, make, distribute, offer for sale, promote, advertise, sell, import, export, or have used, made, distributed, offered for sale, promoted, advertised, sold, imported, or exported the Rembrandt Products worldwide;
  3. all Product Manufacturing Technology related to the Rembrandt Products;
  4. all Product Marketing Materials related to the Rembrandt Products;
  5. all Website(s) related to the Rembrandt Products;
  6. at the Commission-approved Acquirer’s option, all Product Assumed Contracts related to the Rembrandt Products (copies to be provided to the Commission-approved Acquirer on or before the Closing Date);

## Decision and Order

7. all Respondent Gillette's books, records, and files related to the foregoing or to Rembrandt Products; *provided, however*, that in cases in which documents or other materials included in the Rembrandt Assets contain information: (1) that relates both to the Rembrandt Products and to other Products or businesses of Respondent Gillette and cannot be segregated in a manner that preserves the usefulness of the information as it relates to the Rembrandt Products; or (2) for which Respondent Gillette has a legal obligation to retain the original copies, Respondent Gillette shall be required to provide only copies or relevant excerpts of the documents and materials containing this information. In instances where such copies are provided to the Commission-approved Acquirer, Respondent Gillette shall provide the Commission-approved Acquirer access to original documents under circumstances where copies of documents are insufficient for evidentiary or regulatory purposes. The purpose of this proviso is to ensure that Respondent Gillette provides the Commission-approved Acquirer with the above-described information without requiring Respondent Gillette completely to divest itself of information that, in content, also relates to Products and businesses other than the Rembrandt Products;
8. list of all customers and/or targeted customers for the Rembrandt Products and the pricing and/or planned or proposed pricing of the Rembrandt Products for such customers;
9. at the Commission-approved Acquirer's option, all inventory in existence as of the Closing Date including, but not limited to, raw materials, packaging materials, work-in-process and finished goods related to the Rembrandt Products; and
10. all unfilled customer orders for finished goods related to the Rembrandt Products as of the Closing Date (a list of

Decision and Order

such orders is to be provided to the Commission-approved Acquirer within two (2) days after the Closing Date).

- YY. “Rembrandt Core Employee(s)” means the Product Marketing Employees, the Product Sales Employees, and the Product Research and Development Employees related to the Rembrandt Products.
- ZZ. “Rembrandt Key Employee(s)” means those employees of Respondents specifically identified in Appendix IV of this Order.
- AAA. “Rembrandt IP Protected Products” means all Rembrandt Products *except* any Rembrandt Product that, as of the Closing Date, is in an earlier stage of research or Development than Stage 3 of Respondent Gillette’s SPEED (New Development Process) Program (as such program was applied to Products and in effect within the one (1) year period prior to the Acquisition Date); *provided however*, “Rembrandt IP Protected Products” also includes all Rembrandt Products specifically identified in Appendix V attached to this Order.
- BBB. “Rembrandt Products” means all Products Developed, in Development, manufactured, distributed, marketed or sold by Respondent Gillette prior to the Acquisition that were marketed or sold or to be marketed or sold as teeth whitening agents and/or as Products using such Product Trademarks Rembrandt® or any variation or derivative of such Product Trademarks.
- CCC. “Rembrandt Releasee(s)” means the Commission-approved Acquirer for the Rembrandt Products or any entity controlled by or under common control with such Commission-approved Acquirer, or any licensees, sublicensees, manufacturers, suppliers,

## Decision and Order

distributors, and customers of such Commission-approved Acquirer, or of such Commission-approved Acquirer-affiliated entities.

- DDD. “Remedial Agreement” means the following: (1) any agreement between Respondent(s) and a Commission-approved Acquirer that is specifically referenced and attached to this Order, including all amendments, exhibits, attachments, agreements, and schedules thereto, related to the relevant assets to be assigned, granted, licensed, divested, transferred, delivered, or otherwise conveyed, and that has been approved by the Commission to accomplish the requirements of the Order in connection with the Commission’s determination to make this Order final; and/or (2) any agreement between the Respondent(s) and a Commission-approved Acquirer (or between a Divestiture Trustee and a Commission-approved Acquirer) that has been approved by the Commission to accomplish the requirements of this Order, including all amendments, exhibits, attachments, agreements, and schedules thereto, related to the relevant assets to be assigned, granted, licensed, divested, transferred, delivered, or otherwise conveyed, and that has been approved by the Commission to accomplish the requirements of this Order.
- EEE. “Retained Product” means any Product(s) other than a Divestiture Product.
- FFF. “SpinBrush Assets” means all Respondent P&G’s rights, title and interest in and to all assets related to Respondent P&G’s worldwide business related to the SpinBrush Products, to the extent legally transferable, including the research, Development, manufacture, distribution, marketing, and sale of the SpinBrush Products including, without limitation, the following:

Decision and Order

1. all Product Intellectual Property related to the SpinBrush Products;
2. perpetual, fully paid-up and royalty-free license(s) with rights to sublicense to all Product Licensed Intellectual Property to use, make, distribute, offer for sale, promote, advertise, sell, import, export, or have used, made, distributed, offered for sale, promoted, advertised, sold, imported, or exported the SpinBrush Products anywhere in the world; *provided however*, such license for the Product Licensed Intellectual Property shall also include the rights to use Respondent P&G's Crest® trademark in connection with the marketing of the SpinBrush Products for a limited period as is approved by the Commission in the Remedial Agreements related to the SpinBrush Assets;
3. all Product Manufacturing Technology related to the SpinBrush Products;
4. all Product Marketing Materials related to the SpinBrush Products;
5. all Website(s) related to the Spinbrush Products;
6. at the Commission-approved Acquirer's option, all Product Assumed Contracts related to the SpinBrush Products (copies to be provided to the Commission-approved Acquirer on or before the Closing Date);
7. all Respondent P&G's books, records, files related to the foregoing or to SpinBrush Products; *provided, however*, that in cases in which documents or other materials included in the SpinBrush Assets contain information: (1) that relates both to the SpinBrush Products and to other Products or businesses of Respondent P&G and cannot be segregated in a manner that preserves the usefulness of the information as it relates to the

## Decision and Order

SpinBrush Products; or (2) for which Respondent P&G has a legal obligation to retain the original copies, Respondent P&G shall be required to provide only copies or relevant excerpts of the documents and materials containing this information. In instances where such copies are provided to the Commission-approved Acquirer, Respondent P&G shall provide the Commission-approved Acquirer access to original documents under circumstances where copies of documents are insufficient for evidentiary or regulatory purposes. The purpose of this proviso is to ensure that Respondent P&G provides the Commission-approved Acquirer with the above-described information without requiring Respondent P&G completely to divest itself of information that, in content, also relates to Products and businesses other than the SpinBrush Products;

8. list of all customers and/or targeted customers for the SpinBrush Products and the pricing and/or planned or proposed pricing of the SpinBrush Products for such customers;
  9. at the Commission-approved Acquirer's option, all inventory, including raw materials, packaging materials, work-in-process and finished goods related to the SpinBrush Products; and
  10. all unfilled customer orders for finished goods related to the SpinBrush Products as of the Closing Date (a list of such orders is to be provided to the Commission-approved Acquirer within two (2) days after the Closing Date).
- G.G.G. "SpinBrush Asset Purchase Agreement" means the "Asset Sale and Purchase Agreement" among The Procter & Gamble Company, certain of its affiliates and Church & Dwight Co., Inc. dated September 23, 2005, and all amendments, exhibits, attachments,

Decision and Order

agreements, and schedules thereto, related to the SpinBrush Assets to be divested, that have been approved by the Commission to accomplish the requirements of this Order. The SpinBrush Asset Purchase Agreement is attached to this Order and contained in non-public Appendix II.

- HHH. “SpinBrush Core Employee(s)” means the Product Marketing Employees, Product Sales Employees, and Product Research and Development Employees related to the SpinBrush Products.
- III. “SpinBrush Products” means all Products Developed, in Development, manufactured, distributed, marketed or sold by Respondent P&G prior to the Acquisition that were marketed or sold or to be marketed or sold as non-rechargeable battery-powered toothbrushes and/or as Products using the Product Trademark SpinBrush® or any variation or derivative on or prior to the Closing Date. “SpinBrush Products” includes, but is not limited to, those rechargeable battery-powered toothbrush Products Developed or in Development under Respondent P&G “Project Franklin” designation.
- JJJ. “SpinBrush Releasee(s)” means the Commission-approved Acquirer for the SpinBrush Products or any entity controlled by or under common control with such Commission-approved Acquirer, or any licensees, sublicensees, manufacturers, suppliers, distributors, and customers of such Commission-approved Acquirer, or of such Commission-approved Acquirer-affiliated entities.
- KKK. “Supply Cost” means a cost not to exceed the manufacturer’s average direct per unit cost of manufacturing the Divestiture Product for the twelve (12) month period immediately preceding the Acquisition Date. “Supply Cost” shall expressly exclude any intracompany business transfer profit.

## Decision and Order

- LLL. “Third Party(ies)” means any private entity other than the following: (1) the Respondents; or (2) the Commission-approved Acquirer.
- MMM. “Website(s)” means the content of the Website(s) located at the Domain Names, and all copyrights in such Website(s), to the extent owned by Respondents; *provided, however*, “Website” shall not include the following: (1) content owned by Third Parties and other Product Intellectual Property not owned by Respondent(s) that are incorporated in such Website(s), such as stock photographs used in the Website(s), *except* to the extent that Respondent(s) can convey its rights, if any, therein; or (2) content unrelated to the Divestiture Product(s).

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

- A. Not later than ninety (90) days after the date this Order becomes final, Respondents shall divest the Rembrandt Assets, absolutely and in good faith, and at no minimum price. Respondents shall divest the Rembrandt Assets to a Commission-approved Acquirer and only in a manner that receives the prior approval of the Commission.
- B. Any Remedial Agreement related to the Rembrandt Assets shall be deemed incorporated into this Order, and any failure by Respondents to comply with any term of such Remedial Agreement related to the Rembrandt Assets shall constitute a failure to comply with this Order.
- C. Respondents shall include in any Remedial Agreement related to the Rembrandt Assets the following provisions:



Decision and Order

1. upon reasonable notice and request from the Commission-approved Acquirer to the Respondents, Respondents shall provide in a timely manner at no greater than Direct Cost the following:
  - a. assistance and advice to enable the Commission-approved Acquirer (or the Designee of the Commission-approved Acquirer) to obtain all necessary permits and approvals from any Agency or Governmental Entity to manufacture and sell the Rembrandt Products;
  - b. assistance to the Commission-approved Acquirer (or the Designee of the Commission-approved Acquirer) to manufacture Rembrandt Products in substantially the same manner and quality employed or achieved by or on behalf of Respondent Gillette; and
  - c. consultation with knowledgeable employees of Respondents and training, at the request of the Commission-approved Acquirer and at a facility chosen by the Commission-approved Acquirer sufficient to satisfy management of the Commission-approved Acquirer that its personnel (or the Designee's personnel) are adequately trained in the manufacture of the Rembrandt Products;
2. upon reasonable notice and request from the Commission-approved Acquirer to Respondents, Respondents shall provide, in a timely manner, at no greater than Direct Cost, assistance of knowledgeable employees of the Respondents to assist the Commission-approved Acquirer to defend against, respond to, or otherwise participate in any litigation related to the Product Intellectual Property;
3. Respondents shall covenant to the Commission-approved Acquirer that Respondents shall:

## Decision and Order

- a. not join, file, prosecute or maintain any suit, in law or equity, against the Commission-approved Acquirer under Patents that are owned or licensed by Respondents as of the Acquisition Date, if such suit would have the potential to interfere with the Commission-approved Acquirer's freedom to practice in the research, Development, manufacture, use, import, export, distribution or sale of the Rembrandt IP Protected Products; *provided however*, that Respondents may receive a covenant from the Commission-approved Acquirer not to assert any Patent related to the Rembrandt Products that is assigned to the Commission-approved Acquirer from the Respondents pursuant to this Order against the Respondents for Respondents' infringement of such Patent in connection with those Products marketed or sold by Respondent P&G as teeth whitening agents immediately prior to the Acquisition Date;
  - b. not use any Confidential Business Information related to the Rembrandt Products obtained by Respondents from any person who was an employee of Respondent Gillette within the two (2) year period immediately prior to the Acquisition in any suit against the Commission-approved Acquirer under Patents that are owned or licensed by Respondents as of the Acquisition Date, if such suit would have the potential to interfere with the Commission-approved Acquirer's freedom to practice in the research, Development, manufacture, use, import, export, distribution or sale of the Rembrandt Products; and
4. Respondents shall covenant to the Commission-approved Acquirer that: (1) as a condition of any assignment, transfer or license to a Third Party of the Patents described in Paragraph II.C.3.a., the Third Party shall agree to provide a covenant whereby the Third Party covenants not to sue the Rembrandt Releasees under such

Decision and Order

Patents, if the suit would have the potential to interfere with the Commission-approved Acquirer's freedom to practice in the research, Development, manufacture, use, import, export, distribution or sale of the Rembrandt IP Protected Products; and (2) with respect to any Third Party rights licensed to Respondents as of or after the Acquisition Date, and as to which Respondents do not control the right of prosecution of any legal action, Respondents shall not actively induce, assist or participate in any legal action or proceeding relating to Rembrandt IP Protected Products against the Rembrandt Releasees, unless required by Law or contract (such contract not to be solicited or entered into for the purpose of circumventing any of the requirements of this Order).

D. Respondents shall:

1. submit to the Commission-approved Acquirer, at Respondents' expense, all Confidential Business Information related to the Rembrandt Products;
2. deliver such Confidential Business Information as follows: (1) in good faith; (2) as soon as practicable, avoiding any delays in transmission of the respective information; and (3) in a manner that ensures its completeness and accuracy and that fully preserves its usefulness;
3. pending complete delivery of all such Confidential Business Information to the Commission-approved Acquirer, provide the Commission-approved Acquirer and the Interim Monitor (if any has been appointed) with access to all such Confidential Business Information and employees who possess or are able to locate such information for the purposes of identifying the books, records, and files related to the Rembrandt Products that contain such Confidential Business Information and facilitating the delivery in a manner consistent with this

## Decision and Order

Order;

4. not use, directly or indirectly, any such Confidential Business Information related to the research, Development, manufacturing, marketing, or sale of the Rembrandt Products (other than as necessary to comply with the following: (1) the requirements of this Order; (2) the Respondents' obligations to the Commission-approved Acquirer under the terms of any Remedial Agreement related to the Rembrandt Assets; or (3) applicable Law); and
  5. not disclose or convey any such Confidential Business Information, directly or indirectly, to any person except the Commission-approved Acquirer;
  6. shall not provide, disclose or otherwise make available, directly or indirectly, any such Confidential Business Information related to the marketing or sales of the Rembrandt Assets to the employees associated with business related to the teeth whitening Products marketed and sold by Respondent P&G prior to the Acquisition (including, but not limited to, those employees with work responsibilities related to the Crest<sup>®</sup> trademark and any variations or derivatives of such trademark).
- E. Respondents shall not enforce any agreement against a Third Party or the Commission-approved Acquirer to the extent that such agreement may limit or otherwise impair the ability of the Commission-approved Acquirer to acquire the Product Manufacturing Technology related to the Rembrandt Products or related equipment from the Third Party. Such agreements include, but are not limited to, agreements with respect to the disclosure of Confidential Business Information related to such Product Manufacturing Technology.

Decision and Order

- F. Not later than ten (10) days after the Closing Date, Respondents shall grant a release to each Third Party that is subject to an agreement as described in Paragraph II.E. that allows the Third Party to provide the relevant Product Manufacturing Technology or related equipment to the Commission-approved Acquirer. Within five (5) days of the execution of each such release, Respondents shall provide a copy of the release to the Commission-approved Acquirer.
- G. Respondents shall:
1. for a period of at least six (6) months from the Closing Date, provide the Commission-approved Acquirer with the opportunity to enter into employment contracts with the Rembrandt Core Employees and Rembrandt Key Employees. This period is hereinafter referred to as the “Rembrandt Access Period”; and
  2. not later than the earlier of the following dates: (1) ten (10) days after notice by staff of the Commission to the Respondents to provide the Product Employee Information; or (2) ten (10) Days after the Closing Date, Respondents shall provide the Commission-approved Acquirer or the Proposed Acquirer with the Product Employee Information related to the Rembrandt Core Employees and Rembrandt Key Employees. Failure by Respondents to provide the Product Employee Information for any relevant employee within the time provided herein shall extend the Rembrandt Access Period with respect to that employee in an amount equal to the delay.
- H. Respondents shall:
1. during the Rembrandt Access Period, not interfere with the hiring or employing by the Commission-approved Acquirer of Rembrandt Core Employees and Rembrandt

## Decision and Order

Key Employees, and remove any impediments within the control of Respondents that may deter these employees from accepting employment with the Commission-approved Acquirer, including, but not limited to, any noncompete or nondisclosure provisions of employment or other contracts with Respondents that would affect the ability or incentive of those individuals to be employed by the Commission-approved Acquirer. In the case of the Rembrandt Key Employees, Respondents shall waive, for the benefit of the Commission-approved Acquirer, any attorney-client privilege as it pertains to the Rembrandt Products. In addition, Respondents shall not make any counteroffer to a Rembrandt Core Employee or Rembrandt Key Employee who receives a written offer of employment from the Commission-approved Acquirer;

*provided, however,* that this Paragraph II.H.1 shall not prohibit the Respondents from making offers of employment to or employing any Rembrandt Core Employee or Rembrandt Key Employee during the Rembrandt Access Period where the Commission-approved Acquirer has notified the Respondents in writing that the Commission-approved Acquirer does not intend to make an offer of employment to that employee;

*provided further* that if the Respondents notify the Commission-approved Acquirer in writing of their desire to make an offer of employment to a particular Rembrandt Core Employee or Rembrandt Key Employee and the Commission-approved Acquirer does not make an offer of employment to that employee within twenty (20) Days of the date the Commission-approved Acquirer receives such notice, the Respondents may make an offer of employment to that employee;

2. until the Closing Date, provide all Rembrandt Core Employees and Rembrandt Key Employees with reasonable financial incentives to continue in their

Decision and Order

positions and to market and promote the Rembrandt Products consistent with past practices and/or as may be necessary to preserve the marketability, viability and competitiveness of the Rembrandt Products and to ensure successful execution of the pre-Acquisition marketing plans related to the Rembrandt Products. Such incentives shall include a continuation of all employee compensation and benefits offered by Respondents until the Closing Date for the divestiture of the Rembrandt Assets has occurred, including regularly scheduled raises, bonuses, and vesting of pension benefits (as permitted by Law). In addition to the foregoing, Respondents shall provide to each Rembrandt Key Employee who accepts employment with the Commission-approved Acquirer, an incentive equal to fifty (50) percent of such employee's base annual salary to be paid upon the employee's completion of one (1) year of employment with the Commission-approved Acquirer;

*provided, however,* that nothing in this Order requires or shall be construed to require the Respondents to terminate the employment of any employee or prevent Respondents from continuing the employment of Rembrandt Core Employees or Rembrandt Key Employees (other than those conditions contained in this Order) in connection with the Acquisition or prevents the Respondents from continuing the employment of the Rembrandt Core Employees or Rembrandt Key Employees in connection with the Acquisition; and

3. for a period of one (1) year from the Closing Date, not:
  - a. directly or indirectly, solicit or otherwise attempt to induce any employee of the Commission-approved Acquirer with any amount of responsibility related to the Rembrandt Products ("Rembrandt Employee") to terminate his or her employment relationship with the Commission-approved Acquirer; or

## Decision and Order

- b. hire any Rembrandt Employee; *provided, however*, Respondents may hire any former Rembrandt Employee whose employment has been terminated by the Commission-approved Acquirer or who independently applies for employment with the Respondents, as long as such employee was not solicited in violation of the nonsolicitation requirements contained herein;

*provided, however*, Respondents may do the following: (1) advertise for employees in newspapers, trade publications or other media not targeted specifically at the Rembrandt Employees; or (2) hire a Rembrandt Employee who contacts Respondents on his or her own initiative without any direct or indirect solicitation or encouragement from the Respondents;

4. for a period of two (2) years from the Closing Date, use any Rembrandt Key Employee for work specifically related to Products for use as teeth whitening agents.
- I. Prior to the Closing Date, Respondents shall secure all consents and waivers from all Third Parties that are necessary for the divestiture of the Rembrandt Assets to the Commission-approved Acquirer, or for the continued research, Development, manufacture, sale, marketing or distribution of the Rembrandt Products by the Commission-approved Acquirer; *provided, however*, Respondents may satisfy this requirement by certifying that the Commission-approved Acquirer has executed all such agreements directly with each of the relevant Third Parties.
  - J. Respondents shall require, as a condition of continued employment post-divestiture of the Rembrandt Assets, that each Rembrandt Core Employee retained by Respondents, the direct supervisor(s) of any such employee, and any other employee retained by Respondents and designated by the Interim Monitor sign a confidentiality agreement pursuant to



Decision and Order

which such employee shall be required to maintain all Confidential Business Information related to the Rembrandt Products strictly confidential, including the nondisclosure of such information to all other employees, executives or other personnel of Respondents (other than as necessary to comply with the requirements of this Order).

- K. Respondents shall provide written notification of the restrictions on the use of the Confidential Business Information related to the Rembrandt Products by Respondents' personnel to all of Respondents' employees who:
1. are or were involved in the research, Development, manufacturing, distribution, sale or marketing of the Rembrandt Products;
  2. are involved in the research, Development, manufacturing, distribution, sale or marketing of Products for use as teeth whitening agents for Respondent P&G; and/or
  3. may have Confidential Business Information related to the Rembrandt Products.

Respondents shall give such notification by e-mail with return receipt requested or similar transmission, and keep a file of such receipts for one (1) year after the Closing Date. Respondents shall provide a copy of such notification to the Commission-approved Acquirer. Respondents shall maintain complete records of all such agreements at Respondents' corporate headquarters and shall provide an officer's certification to the Commission stating that such acknowledgment program has been implemented and is being complied with. Respondents shall provide the Commission-approved Acquirer with copies of all certifications, notifications and reminders sent to Respondents' personnel.

## Decision and Order

- L. Upon reasonable notice and request by the Commission-approved Acquirer, Respondents shall make available to the Commission-approved Acquirer, at no greater than Direct Cost, such personnel, assistance and training as the Commission-approved Acquirer might reasonably need to transfer the Rembrandt Assets, and shall continue providing such personnel, assistance and training, at the request of the Commission-approved Acquirer the Rembrandt Assets are completely transferred to the Commission-approved Acquirer or its Designee in a manner that fully preserves their usefulness.
- M. Pending divestiture of the Rembrandt Assets, Respondents shall take such actions as are necessary to maintain the full economic viability and marketability of the business associated with the Rembrandt Assets, to minimize any risk of loss of competitive potential for such business, and to prevent the destruction, removal, wasting, deterioration, or impairment of any of the Rembrandt Assets except for ordinary wear and tear.
- N. Counsel for Respondents (including in-house counsel under appropriate confidentiality arrangements) may retain unredacted copies of all documents or other materials provided to the Commission-approved Acquirer and may have access to original documents (under circumstances where copies of documents are insufficient or otherwise unavailable) provided to the Commission-approved Acquirer only in order to do the following:
1. comply with any Remedial Agreement, this Order, any Law (including, without limitation, any requirement to obtain regulatory licenses or approvals), any data retention requirement of any applicable Governmental Entity, or any taxation requirements; or
  2. defend against, respond to, or otherwise participate in any litigation, investigation, audit, process, subpoena or other

Decision and Order

proceeding relating to the divestiture or any other aspect of the Rembrandt Assets or Rembrandt business; *provided, however*, that Respondents may disclose such information as necessary for the purposes set forth in this Paragraph pursuant to an appropriate confidentiality order, agreement or arrangement;

*provided, however*, that pursuant to this Paragraph II.N., Respondents shall: (1) require those who view such unredacted documents or other materials to enter into confidentiality agreements with the Commission-approved Acquirer (but shall not be deemed to have violated this requirement if the Commission-approved Acquirer withholds such agreement unreasonably); and (2) use their best efforts to obtain a protective order to protect the confidentiality of such information during any adjudication.

- O. Respondents shall not join, file, prosecute or maintain any suit, in law or equity, against the Commission-approved Acquirer or the Rembrandt Releasee(s) for the research, Development, manufacture, use, import, export, distribution, or sale of the Rembrandt IP Protected Products in connection with the Commission-approved Acquirer's research, Development, manufacture, use, import, export, distribution, or sale of the Rembrandt IP Protected Products under the following:
1. any Patents owned or licensed by Respondents as of the Acquisition Date that claim the use of the Rembrandt IP Protected Products;
  2. any Patents owned or licensed at any time after the Acquisition Date by Respondents that claim any aspect of the research, Development, manufacture, use, import, export, distribution, or sale of the Rembrandt IP Protected Products, other than such Patents that claim inventions conceived by and reduced to practice after the Acquisition Date.

## Decision and Order

- P. Respondents shall not join, file, prosecute or maintain any suit, in law or equity, against the Commission-approved Acquirer or the Rembrandt Releasee(s) for the research, Development, manufacture, use, import, export, distribution, or sale of the Rembrandt Products in connection with the Commission-approved Acquirer's research, Development, manufacture, use, import, export, distribution, or sale of the Rembrandt Products using any Confidential Business Information related to the Rembrandt Products obtained by Respondents from any person who was an employee of Respondent Gillette within the two (2) year period immediately prior to the Acquisition.
- Q. Respondents shall not, in any jurisdiction throughout the world: (1) use the Product Trademarks related to the Rembrandt Products or any mark confusingly similar to such Product Trademarks, as a trademark, tradename, or service mark; (2) attempt to register such Product Trademarks; (3) attempt to register any mark confusingly similar to such Product Trademarks; (4) challenge or interfere with the Commission-approved Acquirer's use and registration of such Product Trademarks; or (5) challenge or interfere with the Commission-approved Acquirer's efforts to enforce its trademark registrations for and trademark rights in such Product Trademarks against Third Parties; *provided however*, that nothing in this Order shall preclude Respondents from continuing to use those trademarks, tradenames, or service marks related to the Retained Products as of the Acquisition Date.
- R. The purpose of the divestiture of the Rembrandt Assets is to ensure the continued use of the Rembrandt Assets in the same business, independent of Respondents, in which the Rembrandt Assets were engaged at the time of the announcement of the Acquisition, and to remedy the lessening of competition resulting from the Acquisition as alleged in the Commission's Complaint.

Decision and Order

### III.

#### **IT IS FURTHER ORDERED** that:

- A. Not later than ten (10) days after the Acquisition Date, Respondents shall divest the SpinBrush Assets, absolutely and in good faith, to Church & Dwight pursuant to and in accordance with the SpinBrush Asset Purchase Agreement (which agreement shall not vary or contradict, or be construed to vary or contradict, the terms of this Order, it being understood that nothing in this Order shall be construed to reduce any rights or benefits of Church & Dwight or to reduce any obligations of the Respondents under such agreement), and such agreement, if it becomes the Remedial Agreement related to the SpinBrush Assets, is incorporated by reference into this Order and made a part hereof;

*provided, however,* that if Respondents have divested the SpinBrush Assets to Church & Dwight prior to the date this Order becomes final, and if, at the time the Commission determines to make this Order final, the Commission notifies Respondents that Church & Dwight is not an acceptable purchaser of the SpinBrush Assets, then Respondents shall immediately rescind the transaction with Church & Dwight and shall divest the SpinBrush Assets within one hundred eighty (180) days from the date the Order becomes final, absolutely and in good faith, at no minimum price, to a Commission-approved Acquirer and only in a manner that receives the prior approval of the Commission;

*provided further* that if the Respondents have divested the SpinBrush Assets to Church & Dwight prior to the date this Order becomes final, and if, at the time the Commission determines to make this Order final, the Commission notifies the Respondents that the manner in which the divestiture was accomplished is not acceptable, the Commission may direct the

## Decision and Order

Respondents, or appoint a Divestiture Trustee, to effect such modifications to the manner of divestiture of the SpinBrush Assets to Church & Dwight (including, but not limited to, entering into additional agreements or arrangements) as the Commission may determine are necessary to satisfy the requirements of this Order.

*provided further, however*, the Respondents requirement as to the timing to divest the Spinbrush Assets shall be tolled pending any required approvals for such divestiture from the Commission of the European Communities but, in any event, shall not be later than ten (10) days of the Respondents' receipt of such approval.

- B. Any Remedial Agreement related to the SpinBrush Assets shall be deemed incorporated into this Order, and any failure by Respondents to comply with any term of such Remedial Agreement related to the SpinBrush Assets shall constitute a failure to comply with this Order.
- C. Respondents shall include in any Remedial Agreement related to the SpinBrush Assets the following provisions:
1. upon reasonable notice and request from the Commission-approved Acquirer to the Respondents, Respondents shall provide in a timely manner at no greater than Direct Cost the following:
    - a. assistance and advice to enable the Commission-approved Acquirer (or the Designee of the Commission-approved Acquirer) to obtain all necessary permits and approvals from any Agency or Governmental Entity to manufacture and sell the SpinBrush Products;
    - b. assistance to the Commission-approved Acquirer (or the Designee of the Commission-approved Acquirer) to manufacture the SpinBrush Products in

Decision and Order

substantially the same manner and quality employed or achieved by or on behalf of Respondent P&G; and

- c. consultation with knowledgeable employees of Respondents and training, at the request of the Commission-approved Acquirer and at a facility chosen by the Commission-approved Acquirer sufficient to satisfy management of the Commission-approved Acquirer that its personnel (or the Designee's personnel) are adequately trained in the manufacture of the SpinBrush Products;
2. upon reasonable notice and request from the Commission-approved Acquirer to Respondents, Respondents shall provide, in a timely manner, at no greater than Direct Cost, assistance of knowledgeable employees of the Respondents to assist the Commission-approved Acquirer to defend against, respond to, or otherwise participate in any litigation related to the Product Intellectual Property;
3. Respondents shall covenant to the Commission-approved Acquirer that Respondents shall not join, file, prosecute or maintain any suit, in law or equity, against the Commission-approved Acquirer under Patents that are owned or licensed by Respondents as of the Acquisition Date, if such suit would have the potential to interfere with the Commission-approved Acquirer's freedom to practice in the research, Development, manufacture, use, import, export, distribution or sale of the SpinBrush Products; *provided however*, that Respondents may receive a covenant from the Commission-approved Acquirer not to assert against the Respondents any Patent related to the SpinBrush Products that is assigned to the Commission-approved Acquirer from the Respondents pursuant to this Order; and

## Decision and Order

4. Respondents shall covenant to the Commission-approved Acquirer that: (1) as a condition of any assignment, transfer or license to a Third Party of the above-described Patents, the Third Party shall agree to provide a covenant whereby the Third Party covenants not to sue the SpinBrush Releasees under such Patents, if the suit would have the potential to interfere with the Commission-approved Acquirer's freedom to practice in the research, Development, manufacture, use, import, export, distribution or sale of the SpinBrush Products; and (2) with respect to any Third Party rights licensed to Respondents as of or after the Acquisition Date, and as to which Respondents do not control the right of prosecution of any legal action, Respondents shall not actively induce, assist or participate in any legal action or proceeding relating to the SpinBrush Products against the SpinBrush Releasees, unless required by Law or contract (such contract not to be solicited or entered into for the purpose of circumventing any of the requirements of this Order).

## D. Respondents shall:

1. submit to the Commission-approved Acquirer, at Respondents' expense, all Confidential Business Information related to the SpinBrush Products;
2. deliver such Confidential Business Information as follows: (1) in good faith; (2) as soon as practicable, avoiding any delays in transmission of the respective information; and (3) in a manner that ensures its completeness and accuracy and that fully preserves its usefulness;
3. pending complete delivery of all such Confidential Business Information to the Commission-approved Acquirer, provide the Commission-approved Acquirer and the Interim Monitor (if any has been appointed) with access to all such Confidential Business Information and



Decision and Order

employees who possess or are able to locate such information for the purposes of identifying the books, records, and files related to the SpinBrush Products that contain such Confidential Business Information and facilitating the delivery in a manner consistent with this Order;

4. not use, directly or indirectly, any such Confidential Business Information related to the research, Development, manufacturing, marketing, or sale of the SpinBrush Products (other than as necessary to comply with the following: (1) the requirements of this Order; (2) the Respondents' obligations to the Commission-approved Acquirer under the terms of any Remedial Agreement related to the SpinBrush Assets; or (3) applicable Law);
  5. not disclose or convey any such Confidential Business Information, directly or indirectly, to any person except the Commission-approved Acquirer; and
  6. shall not provide, disclose or otherwise make available, directly or indirectly, any such Confidential Business Information related to the marketing or sales of the SpinBrush Assets to the employees associated with business related to the non-rechargeable battery operated toothbrush Products marketed and sold by Respondent Gillette prior to the Acquisition (including, but not limited to, those employees with work responsibilities related to the Oral-B<sup>®</sup> trademark and any variations or derivatives of such trademark).
- E. Respondents shall not enforce any agreement against a Third Party or the Commission-approved Acquirer to the extent that such agreement may limit or otherwise impair the ability of the Commission-approved Acquirer to acquire the Product Manufacturing Technology related to the SpinBrush Products or related equipment from the Third

## Decision and Order

Party. Such agreements include, but are not limited to, agreements with respect to the disclosure of Confidential Business Information related to such Product Manufacturing Technology.

- F. Not later than ten (10) days after the Closing Date, Respondents shall grant a release to each Third Party that is subject to an agreement as described in Paragraph III.E. that allows the Third Party to provide the relevant Product Manufacturing Technology or related equipment to the Commission-approved Acquirer. Within five (5) days of the execution of each such release, Respondents shall provide a copy of the release to the Commission-approved Acquirer.
- G. Respondents shall:
1. for a period of at least six (6) months from the Closing Date, provide the Commission-approved Acquirer with the opportunity to enter into employment contracts with the SpinBrush Core Employees. This period is hereinafter referred to as the “SpinBrush Access Period”; and
  2. not later than the earlier of the following dates: (1) ten (10) Days after notice by staff of the Commission to the Respondents to provide the Product Employee Information; or (2) ten (10) Days after the Closing Date, provide the Commission-approved Acquirer or the Proposed Acquirer with the Product Employee Information related to the SpinBrush Core Employees. Failure by Respondents to provide the Product Employee Information for any relevant employee within the time provided herein shall extend the SpinBrush Access Period with respect to that employee in an amount equal to the delay.

Decision and Order

H. Respondents shall:

1. during the SpinBrush Access Period, not interfere with the hiring or employing by the Commission-approved Acquirer of SpinBrush Core Employees, and remove any impediments within the control of Respondents that may deter these employees from accepting employment with the Commission-approved Acquirer, including, but not limited to, any noncompete or nondisclosure provisions of employment or other contracts with Respondents that would affect the ability or incentive of those individuals to be employed by the Commission-approved Acquirer. In addition, Respondents shall not make any counteroffer to an SpinBrush Core Employee who receives a written offer of employment from the Commission-approved Acquirer;

*provided, however,* that this Paragraph III.H.1 shall not prohibit the Respondents from making offers of employment to or employing any SpinBrush Core Employee during the SpinBrush Access Period where the Commission-approved Acquirer has notified the Respondents in writing that the Commission-approved Acquirer does not intend to make an offer of employment to that employee;

*provided further* that if the Respondents notify the Commission-approved Acquirer in writing of their desire to make an offer of employment to a particular SpinBrush Core Employee and the Commission-approved Acquirer does not make an offer of employment to that employee within twenty (20) Days of the date the Commission-approved Acquirer receives such notice, the Respondents may make an offer of employment to that employee;

2. until the Closing Date, provide all SpinBrush Core Employees with reasonable financial incentives to continue in their positions and to market and promote the

## Decision and Order

SpinBrush Products consistent with past practices and/or as may be necessary to preserve the marketability, viability and competitiveness of the SpinBrush Products and to ensure successful execution of the pre-Acquisition marketing plans to relaunch certain SpinBrush Products. Such incentives shall include a continuation of all employee compensation and benefits offered by Respondents until the Closing Date for the divestiture of the SpinBrush Assets has occurred, including regularly scheduled raises, bonuses, and vesting of pension benefits (as permitted by Law);

*provided, however,* that nothing in this Order requires or shall be construed to require the Respondents to terminate the employment of any employee or prevents the Respondents from continuing the employment of the SpinBrush Core Employees (other than those conditions contained in this Order) in connection with the Acquisition; and

3. for a period of one (1) year from the Closing Date, not:
  - a. directly or indirectly, solicit or otherwise attempt to induce any employee of the Commission-approved Acquirer with any amount of responsibility related to SpinBrush (“SpinBrush Employee”) to terminate his or her employment relationship with the Commission-approved Acquirer; or
  - b. hire any SpinBrush Employee; *provided, however,* Respondents may hire any former SpinBrush Employee whose employment has been terminated by the Commission-approved Acquirer or who independently applies for employment with the Respondents, as long as such employee was not solicited in violation of the nonsolicitation requirements contained herein;

Decision and Order

*provided, however,* Respondents may do the following: (1) advertise for employees in newspapers, trade publications or other media not targeted specifically at the SpinBrush Employees; or (2) hire an SpinBrush Employee who contacts Respondents on his or her own initiative without any direct or indirect solicitation or encouragement from the Respondents.

- I. Prior to the Closing Date, Respondents shall secure all consents and waivers from all Third Parties that are necessary for the divestiture of the SpinBrush Assets to the Commission-approved Acquirer, or for the continued research, Development, manufacture, sale, marketing or distribution of the SpinBrush Products by the Commission-approved Acquirer;

*provided, however,* Respondents may satisfy this requirement by certifying that the Commission-approved Acquirer has executed all such agreements directly with each of the relevant Third Parties.

- J. Respondents shall require, as a condition of continued employment post-divestiture of the SpinBrush Assets, that each SpinBrush Core Employee retained by Respondents, the direct supervisor(s) of any such employee, and any other employee retained by Respondents and designated by the Interim Monitor sign a confidentiality agreement pursuant to which such employee shall be required to maintain all Confidential Business Information related to the SpinBrush Products strictly confidential, including the nondisclosure of such information to all other employees, executives or other personnel of Respondents (other than as necessary to comply with the requirements of this Order).

## Decision and Order

- K. Respondents shall provide written notification of the restrictions on the use of the Confidential Business Information related to the SpinBrush Products by Respondents' personnel to all of Respondents' employees who:
1. are or were involved in the research, Development, manufacturing, distribution, sale or marketing of the SpinBrush Products;
  2. are involved in the research, Development, manufacturing, distribution, sale or marketing of Products for use as battery operated toothbrushes for Respondent Gillette prior to the Acquisition; and/or
  3. may have Confidential Business Information related to the SpinBrush Products.

Respondents shall give such notification by e-mail with return receipt requested or similar transmission, and keep a file of such receipts for one (1) year after the Closing Date.

Respondents shall provide a copy of such notification to the Commission-approved Acquirer. Respondents shall maintain complete records of all such agreements at Respondents' corporate headquarters and shall provide an officer's certification to the Commission stating that such acknowledgment program has been implemented and is being complied with. Respondents shall provide the Commission-approved Acquirer with copies of all certifications, notifications and reminders sent to Respondents' personnel.

- L. Upon reasonable notice and request by the Commission-approved Acquirer, Respondents shall make available to the Commission-approved Acquirer, at no greater than Direct Cost (or, if the SpinBrush Asset Purchase Agreement is the Remedial Agreement for the SpinBrush Assets, then at such cost as may be provided therein), such personnel, assistance and training as the Commission-approved Acquirer might

Decision and Order

reasonably need to transfer the SpinBrush Assets, and shall continue providing such personnel, assistance and training, at the request of the Commission-approved Acquirer, until the SpinBrush Assets are completely transferred to the Commission-approved Acquirer or its Designee in a manner that fully preserves their usefulness.

- M. Pending divestiture of the SpinBrush Assets, Respondents shall take such actions as are necessary to maintain the full economic viability and marketability of the business associated with the SpinBrush Assets, to minimize any risk of loss of competitive potential for such business, and to prevent the destruction, removal, wasting, deterioration, or impairment of any of the SpinBrush Assets except for ordinary wear and tear.
- N. Counsel for Respondents (including in-house counsel under appropriate confidentiality arrangements) may retain unredacted copies of all documents or other materials provided to the Commission-approved Acquirer and may have access to original documents (under circumstances where copies of documents are insufficient or otherwise unavailable) provided to the Commission-approved Acquirer only in order to do the following:
1. comply with any Remedial Agreement, this Order, any Law (including, without limitation, any requirement to obtain regulatory licenses or approvals), any data retention requirement of any applicable Governmental Entity, or any taxation requirements; or
  2. defend against, respond to, or otherwise participate in any litigation, investigation, audit, process, subpoena or other proceeding relating to the divestiture or any other aspect of the SpinBrush Assets or SpinBrush business; *provided, however,* that Respondents may disclose such information as necessary for the purposes set forth in this Paragraph pursuant to an appropriate confidentiality order,

## Decision and Order

agreement or arrangement;

*provided, however,* that pursuant to this Paragraph III.N., Respondents shall: (1) require those who view such unredacted documents or other materials to enter into confidentiality agreements with the Commission-approved Acquirer (but shall not be deemed to have violated this requirement if the Commission-approved Acquirer withholds such agreement unreasonably); and (2) use their best efforts to obtain a protective order to protect the confidentiality of such information during any adjudication.

- O. Respondents shall not join, file, prosecute or maintain any suit, in law or equity, against the Commission-approved Acquirer or the SpinBrush Releasee(s) for the research, Development, manufacture, use, import, export, distribution, or sale of SpinBrush under the following:
1. any Patents owned or licensed by Respondents as of the Acquisition Date that claim the use of the SpinBrush Products;
  2. any Patents owned or licensed at any time after the Acquisition Date by Respondents that claim any aspect of the research, Development, manufacture, use, import, export, distribution, or sale of the SpinBrush Products, other than such Patents that claim inventions conceived by and reduced to practice after the Acquisition Date.
- P. Respondents shall not, in any jurisdiction throughout the world: (1) use the Product Trademarks related to the SpinBrush Products or any mark confusingly similar to such Product Trademarks, as a trademark, tradename, or service mark; (2) attempt to register such Product Trademarks; (3) attempt to register any mark confusingly similar to such Product Trademarks; (4) challenge or interfere with the Commission-approved Acquirer's use and registration of such Product Trademarks; or (5) challenge or interfere with



Decision and Order

the Commission-approved Acquirer's efforts to enforce its trademark registrations for and trademark rights in such Product Trademarks against Third Parties; *provided however*, that nothing in this Order shall preclude Respondents from continuing to use those trademarks, tradenames, or service marks related to the Retained Products as of the Acquisition Date.

- Q. The purpose of the divestiture of the SpinBrush Assets is to ensure the continued use of the SpinBrush Assets in the same business, independent of Respondents, in which the SpinBrush Assets were engaged at the time of the announcement of the Acquisition, and to remedy the lessening of competition resulting from the Acquisition as alleged in the Commission's Complaint.

**IV.**

**IT IS FURTHER ORDERED** that:

- A. Not later than one hundred twenty (120) days after the date this Order becomes final, Respondents shall divest the APDO Assets, absolutely and in good faith, and at no minimum price. Respondents shall divest the APDO Assets to a Commission-approved Acquirer and only in a manner that receives the prior approval of the Commission.
- B. Any Remedial Agreement related to the APDO Assets shall be deemed incorporated into this Order, and any failure by Respondents to comply with any term of such Remedial Agreement related to the APDO Assets shall constitute a failure to comply with this Order.
- C. Respondents shall include in any Remedial Agreement related to the APDO Assets the following provisions:

## Decision and Order

1. Respondents shall Contract Manufacture and deliver to the Commission-approved Acquirer, in a timely manner and under reasonable terms and conditions, a supply of finished APDO Product(s) at Respondent Gillette's Supply Cost, for a period of time sufficient to allow the Commission-approved Acquirer (or the Designee of the Commission-approved Acquirer) to be able to manufacture and to obtain all the relevant Agency approvals necessary to manufacture finished APDO Product(s) independently of Respondents;
2. during the term of the Contract Manufacture between Respondent(s) and the Commission-approved Acquirer, upon request of the Commission-approved Acquirer or Interim Monitor (if applicable), Respondents shall make available to the Commission-approved Acquirer and the Interim Monitor (if applicable) all records that relate to the manufacture of the APDO Products that are generated or created after the Closing Date;
3. upon reasonable notice and request from the Commission-approved Acquirer to the Respondents, Respondents shall provide in a timely manner at no greater than Direct Cost the following:
  - a. assistance and advice to enable the Commission-approved Acquirer (or the Designee of the Commission-approved Acquirer) to obtain all necessary permits and approvals from any Agency or Governmental Entity to manufacture and sell the APDO Products;
  - b. assistance to the Commission-approved Acquirer (or the Designee of the Commission-approved Acquirer) to manufacture the APDO Products in substantially the same manner and quality employed or achieved by or behalf of Respondent Gillette; and

Decision and Order

- c. consultation with knowledgeable employees of Respondents and training, at the request of the Commission-approved Acquirer and at a facility chosen by the Commission-approved Acquirer sufficient to satisfy management of the Commission-approved Acquirer that its personnel (or the Designee's personnel) are adequately trained in the manufacture of the APDO Products;
4. upon reasonable notice and request from the Commission-approved Acquirer to Respondents, Respondents shall provide, in a timely manner, at no greater than Direct Cost, assistance of knowledgeable employees of the Respondents to assist the Commission-approved Acquirer to defend against, respond to, or otherwise participate in any litigation related to the Product Intellectual Property;
5. Respondents shall covenant to the Commission-approved Acquirer that Respondents shall not join, file, prosecute or maintain any suit, in law or equity, against the Commission-approved Acquirer under Patents that are owned or licensed by Respondents as of the Acquisition Date, if such suit would have the potential to interfere with the Commission-approved Acquirer's freedom to practice in the research, Development, manufacture, use, import, export, distribution or sale of the APDO Products; *provided however*, that Respondents may receive a covenant from the Commission-approved Acquirer not to assert against the Respondents any Patent related to the APDO Products that is assigned to the Commission-approved Acquirer from the Respondents pursuant to this Order; and
6. Respondents shall covenant to the Commission-approved Acquirer that: (1) as a condition of any assignment, transfer or license to a Third Party of the above-described Patents, the Third Party shall agree to provide a covenant

## Decision and Order

whereby the Third Party covenants not to sue the APDO Releasees under such Patents, if the suit would have the potential to interfere with the Commission-approved Acquirer's freedom to practice in the research, Development, manufacture, use, import, export, distribution or sale of the APDO Products; and (2) with respect to any Third Party rights licensed to Respondents as of or after the Acquisition Date, and as to which Respondents do not control the right of prosecution of any legal action, Respondents shall not actively induce, assist or participate in any legal action or proceeding relating to the APDO Products against the APDO Releasees, unless required by Law or contract (such contract not to be solicited or entered into for the purpose of circumventing any of the requirements of this Order).

## D. Respondents shall:

1. submit to the Commission-approved Acquirer, at Respondents' expense, all Confidential Business Information related to the APDO Products;
2. deliver such Confidential Business Information as follows: (1) in good faith; (2) as soon as practicable, avoiding any delays in transmission of the respective information; and (3) in a manner that ensures its completeness and accuracy and that fully preserves its usefulness;
3. pending complete delivery of all such Confidential Business Information to the Commission-approved Acquirer, provide the Commission-approved Acquirer and the Interim Monitor (if any has been appointed) with access to all such Confidential Business Information and employees who possess or are able to locate such information for the purposes of identifying the books, records, and files related to the APDO Products that contain such Confidential Business Information and

Decision and Order

facilitating the delivery in a manner consistent with this Order;

4. not use, directly or indirectly, any such Confidential Business Information related to the research, Development, manufacturing, marketing, or sale of the APDO Products (other than as necessary to comply with the following: (1) the requirements of this Order; (2) the Respondents' obligations to the Commission-approved Acquirer under the terms of any Remedial Agreement related to the APDO Assets; or (3) applicable Law;

*provided however*, Respondents may use such Confidential Business Information that also relates to those Retained Products that have been marketed and sold as antiperspirants or deodorants under the Gillette Series<sup>®</sup> trademarks prior to the Acquisition to the extent necessary for Respondents to continue to manufacture, market, and sell such Retained Products; *provided, further*, Respondents shall take such actions, as may be practicable, to prevent the exploitation or use of the most recent brand plan(s) related to the APDO Products by Respondents' employees with responsibilities relating to the Retained Products to be marketed or sold as antiperspirants or deodorants;

5. not disclose or convey any such Confidential Business Information (other than as otherwise permitted under this Order), directly or indirectly, to any person except the Commission-approved Acquirer; and
6. shall not provide, disclose or otherwise make available, directly or indirectly, any such Confidential Business Information (other than as otherwise permitted under this Order) related to the marketing or sales of the APDO Assets to the employees associated with business related to Retained Products that are marketed and sold as antiperspirants or deodorants prior to the Acquisition (including, but not limited to, such employees with work

## Decision and Order

responsibilities related to the Retained Products that have been marketed and sold as antiperspirants or deodorants under the Old Spice® trademark and any variations or derivatives of such trademark prior to the Acquisition).

- E. Respondents shall not enforce any agreement against a Third Party or the Commission-approved Acquirer to the extent that such agreement may limit or otherwise impair the ability of the Commission-approved Acquirer to acquire the Product Manufacturing Technology related to the APDO Products or related equipment from the Third Party. Such agreements include, but are not limited to, agreements with respect to the disclosure of Confidential Business Information related to such Product Manufacturing Technology.
- F. Not later than ten (10) days after the Closing Date, Respondents shall grant a release to each Third Party that is subject to an agreement as described in Paragraph IV.E. that allows the Third Party to provide the relevant Product Manufacturing Technology or related equipment to the Commission-approved Acquirer. Within five (5) days of the execution of each such release, Respondents shall provide a copy of the release to the Commission-approved Acquirer.
- G. Respondents shall:
1. for a period of at least six (6) months from the Closing Date, provide the Commission-approved Acquirer with the opportunity to enter into employment contracts with the APDO Core Employees. This period is hereinafter referred to as the “APDO Access Period”; and
  2. not later than the earlier of the following dates: (1) ten (10) Days after notice by staff of the Commission to the Respondents to provide the Product Employee Information; or (2) ten (10) Days after the Closing Date,

Decision and Order

provide the Commission-approved Acquirer or the Proposed Acquirer with the Product Employee Information related to the APDO Core Employees. Failure by Respondents to provide the Product Employee Information for any relevant employee within the time provided herein shall extend the APDO Access Period with respect to that employee in an amount equal to the delay.

H. Respondents shall:

1. during the APDO Access Period, not interfere with the hiring or employing by the Commission-approved Acquirer of the APDO Core Employees, and remove any impediments within the control of Respondents that may deter these employees from accepting employment with the Commission-approved Acquirer, including, but not limited to, any noncompete or nondisclosure provisions of employment or other contracts with Respondents that would affect the ability or incentive of those individuals to be employed by the Commission-approved Acquirer. In addition, Respondents shall not make any counteroffer to an APDO Core Employee who receives a written offer of employment from the Commission-approved Acquirer;

*provided, however,* that this Paragraph IV.H.1 shall not prohibit the Respondents from making offers of employment to or employing any APDO Core Employee during the APDO Access Period where the Commission-approved Acquirer has notified the respondents in writing that the Commission-approved Acquirer does not intend to make an offer of employment to that employee;

*provided further* that if the Respondents notify the Commission-approved Acquirer in writing of their desire to make an offer of employment to a particular APDO Core Employee and the Commission-approved Acquirer does not

## Decision and Order

make an offer of employment to that employee within twenty (20) days of the date the Commission-approved Acquirer receives such notice, the Respondents may make an offer of employment to that employee;

2. until the Closing Date, provide all APDO Core Employees with reasonable financial incentives to continue in their positions and to market and promote the APDO Products consistent with past practices and/or as may be necessary to preserve the marketability, viability and competitiveness of the APDO Products and to ensure successful execution of the pre-Acquisition marketing plans related to the APDO Products. Such incentives shall include a continuation of all employee compensation and benefits offered by Respondents until the Closing Date for the divestiture of the APDO Assets has occurred, including regularly scheduled raises, bonuses, and vesting of pension benefits (as permitted by Law);

*provided, however,* that nothing in this Order requires or shall be construed to require the Respondents to terminate the employment of any employee or prevents the Respondents from continuing the employment of the APDO Core Employees (other than those conditions contained in this Order) in connection with the Acquisition; and



Decision and Order

3. for a period of one (1) year from the Closing Date, not:
- a. directly or indirectly, solicit or otherwise attempt to induce any employee of the Commission-approved Acquirer with any amount of responsibility related to APDO (“APDO Employee”) to terminate his or her employment relationship with the Commission-approved Acquirer; or
  - b. hire any APDO Employee; *provided, however,* Respondents may hire any former APDO Employee whose employment has been terminated by the Commission-approved Acquirer or who independently applies for employment with the Respondents, as long as such employee was not solicited in violation of the nonsolicitation requirements contained herein;

*provided, however,* Respondents may do the following: (1) advertise for employees in newspapers, trade publications or other media not targeted specifically at the APDO Employees; or (2) hire an APDO Employee who contacts Respondents on his or her own initiative without any direct or indirect solicitation or encouragement from the Respondents.

- I. Prior to the Closing Date, Respondents shall secure all consents and waivers from all Third Parties that are necessary for the divestiture of the APDO Assets to the Commission-approved Acquirer, or for the continued research, Development, manufacture, sale, marketing or distribution of the APDO Products by the Commission-approved Acquirer;

*provided, however,* Respondents may satisfy this requirement by certifying that the Commission-approved Acquirer has executed all such agreements directly with each of the relevant Third Parties.

## Decision and Order

- J. Respondents shall require, as a condition of continued employment post-divestiture of the APDO Assets, that each APDO Core Employee retained by Respondents, the direct supervisor(s) of any such employee, and any other employee retained by Respondents and designated by the Interim Monitor sign a confidentiality agreement pursuant to which such employee shall be required to maintain all Confidential Business Information related to the APDO Products strictly confidential, including the nondisclosure of such information to all other employees, executives or other personnel of Respondents (other than as necessary to comply with the requirements of this Order).
- K. Respondents shall provide written notification of the restrictions on the use of the Confidential Business Information related to the APDO Products by Respondents' personnel to all of Respondents' employees who:
1. are or were involved in the research, Development, manufacturing, distribution, sale or marketing of the APDO Products;
  2. are involved in the research, Development, manufacturing, distribution, sale or marketing of Respondent P&G's antiperspirant or deodorant Products;
  3. are involved in the research, Development, manufacturing, distribution, sale or marketing of Respondent Gillette's antiperspirant or deodorant Retained Products; and/or
  4. may have Confidential Business Information related to APDO.

Respondents shall give such notification by e-mail with return receipt requested or similar transmission, and keep a file of such receipts for one (1) year after the Closing Date.

Decision and Order

Respondents shall provide a copy of such notification to the Commission-approved Acquirer. Respondents shall maintain complete records of all such agreements at Respondents' corporate headquarters and shall provide an officer's certification to the Commission stating that such acknowledgment program has been implemented and is being complied with. Respondents shall provide the Commission-approved Acquirer with copies of all certifications, notifications and reminders sent to Respondents' personnel.

- L. Upon reasonable notice and request by the Commission-approved Acquirer, Respondents shall make available to the Commission-approved Acquirer, at no greater than Direct Cost such personnel, assistance and training as the Commission-approved Acquirer might reasonably need to transfer the APDO Assets, and shall continue providing such personnel, assistance and training, at the request of the Commission-approved Acquirer, until the Commission-approved Acquirer (or the Designee of the Commission-approved Acquirer) is fully able to manufacture APDO Products independently of the Respondents;

*provided, however,* the Commission may eliminate, or limit the duration of, the Respondents' obligation under this provision if the Commission determines that the Commission-approved Acquirer is not using commercially reasonable best efforts to enable itself or its Designee to manufacture the APDO Products in a facility that is independent of Respondents.

- M. Pending divestiture of the APDO Assets, Respondents shall take such actions as are necessary to maintain the full economic viability and marketability of the business associated with the APDO Assets, to minimize any risk of loss of competitive potential for such business, and to prevent the destruction, removal, wasting, deterioration, or impairment of any of the APDO Assets except for ordinary wear and tear.

## Decision and Order

- N. Counsel for Respondents (including in-house counsel under appropriate confidentiality arrangements) may retain unredacted copies of all documents or other materials provided to the Commission-approved Acquirer and may have access to original documents (under circumstances where copies of documents are insufficient or otherwise unavailable) provided to the Commission-approved Acquirer only in order to do the following:
1. comply with any Remedial Agreement, this Order, any Law (including, without limitation, any requirement to obtain regulatory licenses or approvals), any data retention requirement of any applicable Governmental Entity, or any taxation requirements; or
  2. defend against, respond to, or otherwise participate in any litigation, investigation, audit, process, subpoena or other proceeding relating to the divestiture or any other aspect of the APDO Assets or APDO business; *provided, however,* that Respondents may disclose such information as necessary for the purposes set forth in this Paragraph pursuant to an appropriate confidentiality order, agreement or arrangement;
- provided, however,* that pursuant to this Paragraph IV.N., Respondents shall: (1) require those who view such unredacted documents or other materials to enter into confidentiality agreements with the Commission-approved Acquirer (but shall not be deemed to have violated this requirement if the Commission-approved Acquirer withholds such agreement unreasonably); and (2) use their best efforts to obtain a protective order to protect the confidentiality of such information during any adjudication.
- O. Respondents shall maintain manufacturing facilities for the APDO Products that are fully capable of producing the APDO Products until the earlier of the following: 1) the Commission-approved Acquirer (or the Designee of the

Decision and Order

Commission-approved Acquirer) is otherwise fully able to manufacture the APDO Products in a facility that is independent of Respondents; or 2) the Respondents have provided to the Commission-approved Acquirer inventory of finished APDO Products sufficient to cover at least all demand anticipated by the Commission-approved Acquirer for the APDO Products during the period of time estimated for the removal, transfer, and reassembly, in a fully operational format (including any potential for delays in such removal, transfer and reassembly in such format), of the APDO Equipment to the Commission-approved Acquirer (or the Designee of the Commission-approved Acquirer);

*provided, however*, the Commission may eliminate, or limit the duration of, the Respondents' obligation under this provision if the Commission determines that the Commission-approved Acquirer is not using commercially reasonable best efforts to enable it to manufacture the APDO Products in a facility that is independent of Respondents.

- P. Respondents shall not join, file, prosecute or maintain any suit, in law or equity, against the Commission-approved Acquirer or the APDO Releasee(s) for the research, Development, manufacture, use, import, export, distribution, or sale of the APDO Products under the following:
1. any Patents owned or licensed by Respondents as of the Acquisition Date that claim the use of the APDO Products;
  2. any Patents owned or licensed at any time after the Acquisition Date by Respondents that claim any aspect of the research, Development, manufacture, use, import, export, distribution, or sale of the APDO Products, other than such Patents that claim inventions conceived by and reduced to practice after the Acquisition Date.

## Decision and Order

- Q. Respondents shall not, in any jurisdiction throughout the world: (1) use the Product Trademarks related to APDO or any mark confusingly similar to the Product Trademarks, as a trademark, tradename, or service mark; (2) attempt to register the Product Trademarks; (3) attempt to register any mark confusingly similar to the Product Trademarks; (4) challenge or interfere with the Commission-approved Acquirer's use and registration of the Product Trademarks; or (5) challenge or interfere with the Commission-approved Acquirer's efforts to enforce its trademark registrations for and trademark rights in the Product Trademarks against Third Parties; *provided however*, that nothing in this Order shall preclude Respondents from continuing to use those trademarks, tradenames, or service marks related to the Retained Products as of the Acquisition Date.
- R. The purpose of the divestiture of the APDO Assets is to ensure the continued use of the APDO Assets in the same business, independent of Respondents, in which the APDO Assets were engaged at the time of the announcement of the Acquisition, and to remedy the lessening of competition resulting from the Acquisition as alleged in the Commission's Complaint.

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

- A. Not later than twenty (20) days after the Acquisition Date, Respondents shall amend the IntelliClean Agreement in accordance with the IntelliClean Amended Agreement (which agreement shall not vary or contradict, or be construed to vary or contradict, the terms of this Order, it being understood that nothing in this Order shall be construed to reduce any rights or benefits of Philips (other than with respect to any noncompete provisions contained

Decision and Order

in the IntelliClean Agreement) or to reduce any obligations of Respondents (other than with respect to any noncompete provisions contained in the IntelliClean Agreement) under the IntelliClean Amended Agreement).

- B. The IntelliClean Agreement as amended in accordance with the IntelliClean Amended Agreement shall be deemed incorporated by reference into this Order and made a part hereof, and any failure by Respondents to comply with any term of the IntelliClean Amended Agreement, if such agreement is approved by the Commission in connection with the Commission's determination to make this Order final shall constitute a failure to comply with this Order. Any other Remedial Agreement related to the IntelliClean Products shall also be deemed incorporated into this Order, and any failure by Respondents to comply with any term of such Remedial Agreement related to the IntelliClean Products shall constitute a failure to comply with this Order.
- C. Respondents shall:
1. grant a perpetual, fully paid-up and royalty-free license(s) with rights to sublicense to all Product Intellectual Property, Product Licensed Intellectual Property, and the Product Manufacturing Technology to use, make, distribute, offer for sale, promote, advertise, sell, import, export, or have used, made, distributed, offered for sale, promoted, advertised, sold, imported, or exported the IntelliClean Products anywhere in the world; *provided however*, such license for the Product Intellectual Property shall also include the rights to use Respondent P&G's Crest® trademark in the United States and Canada in connection with the marketing of the IntelliClean Products for a limited period as is approved by the Commission in the Remedial Agreements related to the IntelliClean Products;

## Decision and Order

2. as reflected in the IntelliClean Amended Agreement, Contract Manufacture and deliver to Philip or its Designee, in a timely manner and under reasonable terms and conditions (such terms and conditions to be in a manner that preserves the full economic viability and competitiveness of the IntelliClean Products) a supply of the finished dentifrice Product used in connection with the rechargeable toothbrush(es) that are a part of the IntelliClean Products;
3. upon reasonable notice and request from Philips to the Respondents, provide in a timely manner at no greater than Direct Cost the following:
  - a. assistance and advice to enable Philips or its Designee to obtain all necessary permits and approvals from any Agency or Governmental Entity to manufacture and sell the dentifrice used in connection with the rechargeable toothbrush(es) that are a part of the IntelliClean Products;
  - b. assistance to Philips or its Designee to manufacture the dentifrice used in connection with the rechargeable toothbrush(es) that are a part of the IntelliClean Products in substantially the same manner and quality employed or achieved by or behalf of Respondent P&G; and
  - c. consultation with knowledgeable employees of Respondents and training, at the request of Philips and at a facility chosen by Philips sufficient to satisfy management of Philips that its personnel (or the Designee's personnel) are adequately trained in the manufacture of the dentifrice used in connection with the rechargeable toothbrush(es) that are a part of the IntelliClean Products.



Decision and Order

D. Respondents shall:

1. submit to Philips, at Respondents' expense, copies of all Confidential Business Information related to the research, Development, manufacture, distribution, marketing or sale of IntelliClean Products;
2. deliver such Confidential Business Information as follows: (1) in good faith; (2) as soon as practicable, avoiding any delays in transmission of the respective information; and (3) in a manner that ensures its completeness and accuracy and that fully preserves its usefulness; and
3. pending complete delivery of all such Confidential Business Information to Philips, provide Philips and the Interim Monitor (if any has been appointed) with access to all such Confidential Business Information and employees who possess or are able to locate such information for the purposes of identifying the books, records, and files related to the IntelliClean Products that contain such Confidential Business Information and facilitating the delivery in a manner consistent with this Order.

E. Respondents shall not enforce any agreement against a Third Party or Philips to the extent that such agreement may limit or otherwise impair the ability of Philips to acquire the Product Manufacturing Technology related to the IntelliClean Products or related equipment from the Third Party. Such agreements include, but are not limited to, agreements with respect to the disclosure of Confidential Business Information related to such Product Manufacturing Technology.

F. Not later than ten (10) days after the Closing Date, Respondents shall grant a release to each Third Party that is subject to an agreement as described in Paragraph V.E. that

## Decision and Order

allows the Third Party to provide the relevant Product Manufacturing Technology or related equipment to Philips. Within five (5) days of the execution of each such release, Respondents shall provide a copy of the release to Philips.

- G. For a period commencing on the date this Order becomes final and continuing for ten (10) years, Respondents shall not, without providing advance written notification to the Commission, terminate the IntelliClean Amended Agreement. Said notification shall be given on the Notification and Report Form set forth in the Appendix to Part 803 of Title 16 of the Code of Federal Regulations as amended (hereinafter referred to as “the Notification”), and shall be prepared and transmitted in accordance with the requirements of that part, except that no filing fee will be required for any such Notification. Notification shall be filed with the Secretary of the Commission, Notification need not be made to the United States Department of Justice, and Notification is required only of the Respondents and not of any other party to the transaction. Respondents shall provide two (2) complete copies (with all attachments and exhibits) of the Notification to the Commission at least thirty (30) days prior to terminating the IntelliClean Amended Agreement (hereinafter referred to as the “first waiting period”). If, within the first waiting period, representatives of the Commission make a written request for additional information or documentary material (within the meaning of 16 C.F.R. § 803.20), Respondents shall not terminate IntelliClean Amended Agreement until thirty (30) days after substantially complying with such request. Early termination of the waiting periods in this Paragraph may be requested and, where appropriate, granted by letter from the Bureau of Competition; *provided, however*, that prior notification shall not be required by this Paragraph for a transaction for which notification is required to be made, and has been made, pursuant to Section 7A of the Clayton Act, 15 U.S.C. § 18a.

Decision and Order

- H. The purpose of Paragraph V of this Order is to ensure the continued marketing and sale of the IntelliClean Products independently of Respondents and for the same purposes which it was researched, developed, manufactured, marketed and sold by Philips and Respondent P&G at the time of the announcement of the Acquisition, and to remedy the lessening of competition resulting from the Acquisition as alleged in the Commission's Complaint.

**VI.**

**IT IS FURTHER ORDERED** that:

- A. At any time after Respondents sign the Consent Agreement in this matter, the Commission may appoint a monitor ("Interim Monitor") to assure that Respondents expeditiously comply with all of their obligations and perform all of their responsibilities as required by this Order, the Order to Maintain Assets and the Remedial Agreements.
- B. The Commission shall select the Interim Monitor, subject to the consent of Respondent P&G, which consent shall not be unreasonably withheld. If Respondent P&G has not opposed, in writing, including the reasons for opposing, the selection of a proposed Interim Monitor within ten (10) days after notice by the staff of the Commission to Respondent P&G of the identity of any proposed Interim Monitor, Respondents shall be deemed to have consented to the selection of the proposed Interim Monitor.
- C. Not later than ten (10) days after the appointment of the Interim Monitor, Respondents shall execute an agreement that, subject to the prior approval of the Commission, confers on the Interim Monitor all the rights and powers necessary to permit the Interim Monitor to monitor Respondents' compliance with the relevant requirements of

## Decision and Order

the Order in a manner consistent with the purposes of the Order.

- D. If an Interim Monitor is appointed, Respondents shall consent to the following terms and conditions regarding the powers, duties, authorities, and responsibilities of the Interim Monitor:
1. The Interim Monitor shall have the power and authority to monitor Respondents' compliance with the divestiture and asset maintenance obligations and related requirements of the Order, and shall exercise such power and authority and carry out the duties and responsibilities of the Interim Monitor in a manner consistent with the purposes of the Order and in consultation with the Commission.
  2. The Interim Monitor shall act in a fiduciary capacity for the benefit of the Commission.
  3. The Interim Monitor shall serve until the later of:
    - a. the completion by Respondents of the divestiture of all relevant assets required to be assigned, granted, licensed, divested, transferred, delivered, or otherwise conveyed pursuant to this Order in a manner that fully satisfies the requirements of the Order and notification by the Commission-approved Acquirer to the Interim Monitor that it is fully capable of producing the relevant Product(s) acquired pursuant to a Remedial Agreement independently of Respondents; and fulfillment of the Respondents obligations under this Order with respect to the IntelliClean Products; or
    - b. the completion by Respondents of the last obligation under the Order pertaining to the Interim Monitor's service;

Decision and Order

*provided, however,* that the Commission may extend or modify this period as may be necessary or appropriate to accomplish the purposes of the Order.

4. Subject to any demonstrated legally recognized privilege, the Interim Monitor shall have full and complete access to Respondents' personnel, books, documents, records kept in the normal course of business, facilities and technical information, and such other relevant information as the Interim Monitor may reasonably request, related to Respondents' compliance with their obligations under the Order, including, but not limited to, their obligations related to the relevant assets. Respondents shall cooperate with any reasonable request of the Interim Monitor and shall take no action to interfere with or impede the Interim Monitor's ability to monitor Respondents' compliance with the Order.
5. The Interim Monitor shall serve, without bond or other security, at the expense of Respondents on such reasonable and customary terms and conditions as the Commission may set. The Interim Monitor shall have authority to employ, at the expense of the Respondents, such consultants, accountants, attorneys and other representatives and assistants as are reasonably necessary to carry out the Interim Monitor's duties and responsibilities.
6. Respondents shall indemnify the Interim Monitor and hold the Interim Monitor harmless against any losses, claims, damages, liabilities, or expenses arising out of, or in connection with, the performance of the Interim Monitor's duties, including all reasonable fees of counsel and other reasonable expenses incurred in connection with the preparations for, or defense of, any claim, whether or not resulting in any liability, except to the extent that such losses, claims, damages, liabilities, or expenses result from misfeasance, gross negligence,

## Decision and Order

willful or wanton acts, or bad faith by the Interim Monitor.

7. Respondents shall report to the Interim Monitor in accordance with the requirements of this Order and/or as otherwise provided in any agreement approved by the Commission. The Interim Monitor shall evaluate the reports submitted to the Interim Monitor by Respondents, and any reports submitted by the Commission-approved Acquirer with respect to the performance of Respondents' obligations under the Order or the Remedial Agreement. Within thirty (30) Days from the date the Interim Monitor receives these reports, the Interim Monitor shall report in writing to the Commission concerning performance by Respondents of their obligations under the Order.
  8. Respondents may require the Interim Monitor and each of the Interim Monitor's consultants, accountants, attorneys and other representatives and assistants to sign a customary confidentiality agreement; *provided, however*, that such agreement shall not restrict the Interim Monitor from providing any information to the Commission.
- E. The Commission may, among other things, require the Interim Monitor and each of the Interim Monitor's consultants, accountants, attorneys and other representatives and assistants to sign an appropriate confidentiality agreement related to Commission materials and information received in connection with the performance of the Interim Monitor's duties.
- F. If the Commission determines that the Interim Monitor has ceased to act or failed to act diligently, the Commission may appoint a substitute Interim Monitor in the same manner as provided in this Paragraph.
- G. The Commission may on its own initiative, or at the request of the Interim Monitor, issue such additional

Decision and Order

orders or directions as may be necessary or appropriate to assure compliance with the requirements of the Order.

- H. The Interim Monitor appointed pursuant to this Order may be the same person appointed as a Divestiture Trustee pursuant to the relevant provisions of this Order.

**VII.**

**IT IS FURTHER ORDERED** that:

- A. If Respondents have not fully complied with the obligations to assign, grant, license, divest, transfer, deliver or otherwise convey relevant assets as required by this Order, the Commission may appoint a trustee (“Divestiture Trustee”) to assign, grant, license, divest, transfer, deliver or otherwise convey the assets required to be assigned, granted, licensed, divested, transferred, delivered or otherwise conveyed pursuant to each of the relevant Paragraphs in a manner that satisfies the requirements of each such Paragraph. In the event that the Commission or the Attorney General brings an action pursuant to § 5(*l*) of the Federal Trade Commission Act, 15 U.S.C. § 45(*l*), or any other statute enforced by the Commission, Respondents shall consent to the appointment of a Divestiture Trustee in such action to assign, grant, license, divest, transfer, deliver or otherwise convey the relevant assets. Neither the appointment of a Divestiture Trustee nor a decision not to appoint a Divestiture Trustee under this Paragraph shall preclude the Commission or the Attorney General from seeking civil penalties or any other relief available to it, including a court-appointed Divestiture Trustee, pursuant to § 5(*l*) of the Federal Trade Commission Act, or any other statute enforced by the Commission, for any failure by Respondents to comply with this Order.

## Decision and Order

- B. The Commission shall select the Divestiture Trustee, subject to the consent of Respondent P&G, which consent shall not be unreasonably withheld. The Divestiture Trustee shall be a person with experience and expertise in acquisitions and divestitures. If Respondent P&G has not opposed, in writing, including the reasons for opposing, the selection of any proposed Divestiture Trustee within ten (10) days after notice by the staff of the Commission to Respondent P&G of the identity of any proposed Divestiture Trustee, Respondents shall be deemed to have consented to the selection of the proposed Divestiture Trustee.
- C. Not later than ten (10) days after the appointment of a Divestiture Trustee, Respondents shall execute a trust agreement that, subject to the prior approval of the Commission, transfers to the Divestiture Trustee all rights and powers necessary to permit the Divestiture Trustee to effect the divestiture required by this Order.
- D. If a Divestiture Trustee is appointed by the Commission or a court pursuant to this Paragraph, Respondents shall consent to the following terms and conditions regarding the Divestiture Trustee's powers, duties, authority, and responsibilities:
1. Subject to the prior approval of the Commission, the Divestiture Trustee shall have the exclusive power and authority to assign, grant, license, divest, transfer, deliver or otherwise convey the assets that are required by this Order to be assigned, granted, licensed, divested, transferred, delivered or otherwise conveyed.
  2. The Divestiture Trustee shall have one (1) year after the date the Commission approves the trust agreement described herein to accomplish the divestiture, which shall be subject to the prior approval of the Commission. If, however, at the end of the one (1) year period, the Divestiture Trustee has submitted a plan of divestiture or



Decision and Order

believes that the divestiture can be achieved within a reasonable time, the divestiture period may be extended by the Commission; *provided, however*, the Commission may extend the divestiture period only two (2) times.

3. Subject to any demonstrated legally recognized privilege, the Divestiture Trustee shall have full and complete access to the personnel, books, records and facilities related to the relevant assets that are required to be assigned, granted, licensed, divested, delivered or otherwise conveyed by this Order and to any other relevant information, as the Divestiture Trustee may request. Respondents shall Develop such financial or other information as the Divestiture Trustee may request and shall cooperate with the Divestiture Trustee. Respondents shall take no action to interfere with or impede the Divestiture Trustee's accomplishment of the divestiture. Any delays in divestiture caused by Respondents shall extend the time for divestiture under this Paragraph in an amount equal to the delay, as determined by the Commission or, for a court-appointed Divestiture Trustee, by the court.
4. The Divestiture Trustee shall use commercially reasonable efforts to negotiate the most favorable price and terms available in each contract that is submitted to the Commission, subject to Respondent's absolute and unconditional obligation to divest expeditiously and at no minimum price. The divestiture shall be made in the manner and to an acquirer as required by this Order; *provided, however*, if the Divestiture Trustee receives bona fide offers from more than one acquiring entity, and if the Commission determines to approve more than one such acquiring entity, the Divestiture Trustee shall divest to the acquiring entity selected by Respondent from

## Decision and Order

among those approved by the Commission; and, *provided further, however*, that Respondent shall select such entity within five (5) days after receiving notification of the Commission's approval.

5. The Divestiture Trustee shall serve, without bond or other security, at the cost and expense of Respondents, on such reasonable and customary terms and conditions as the Commission or a court may set. The Divestiture Trustee shall have the authority to employ, at the cost and expense of Respondents, such consultants, accountants, attorneys, investment bankers, business brokers, appraisers, and other representatives and assistants as are necessary to carry out the Divestiture Trustee's duties and responsibilities. The Divestiture Trustee shall account for all monies derived from the divestiture and all expenses incurred. After approval by the Commission of the account of the Divestiture Trustee, including fees for the Divestiture Trustee's services, all remaining monies shall be paid at the direction of the Respondents, and the Divestiture Trustee's power shall be terminated. The compensation of the Divestiture Trustee shall be based at least in significant part on a commission arrangement contingent on the divestiture of all of the relevant assets that are required to be divested by this Order.
6. Respondents shall indemnify the Divestiture Trustee and hold the Divestiture Trustee harmless against any losses, claims, damages, liabilities, or expenses arising out of, or in connection with, the performance of the Divestiture Trustee's duties, including all reasonable fees of counsel and other expenses incurred in connection with the preparation for, or defense of, any claim, whether or not resulting in any liability, except to the extent that such losses, claims, damages, liabilities, or expenses result from misfeasance, gross negligence, willful or wanton acts, or bad faith by the Divestiture Trustee.

Decision and Order

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

Decision and Order

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

- A. Within five (5) days of the Acquisition, Respondents shall submit to the Commission a letter certifying the date on which the Acquisition occurred.
- B. Within thirty (30) days after the date this Order becomes final, and every sixty (60) days thereafter until Respondents have fully complied with, the following:
  1. Paragraphs II.A, Paragraphs III.A. and IV.A. (*i.e.*, has assigned, licensed, divested, transferred, delivered or otherwise conveyed all relevant assets to the relevant Commission-approved Acquirer in a manner that fully satisfies the requirements of the Order) and Paragraph V.A. of this Order,
  2. Paragraphs II.C., II.D., II.F., III.C., III.D., III.F., IV.C., IV.D., IV.F., V.A., V.D., and V.F.; and
  3. and all its responsibilities to render transitional services to the relevant Commission-approved Acquirer as provided by this Order and the Remedial Agreement(s),

Respondents shall submit to the Commission a verified written report setting forth in detail the manner and form in which it intends to comply, is complying, and has complied with this Order. Respondent shall submit at the same time a copy of its report concerning compliance with this Order to the Interim Monitor, if any Interim Monitor has been appointed.

Respondents shall include in their reports, among other things that are required from time to time, a full description of the efforts being made to comply with the relevant Paragraphs of the Order, including a full description of all substantive contacts or negotiations related to the divestiture of the relevant

Decision and Order

assets and the identity of all Persons contacted, including, copies of all written communications to and from such Persons, all internal memoranda, and all reports and recommendations concerning completing the obligations.

- C. One (1) year after the date this Order becomes final, annually for the next nine years on the anniversary of the date this Order becomes final, and at other times as the Commission may require, Respondents shall file a verified written report with the Commission setting forth in detail the manner and form in which it has complied and is complying with the Order.

**IX.**

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

**X.**

**IT IS FURTHER ORDERED** that, for purposes of determining or securing compliance with this Order, and subject to any legally recognized privilege, and upon written request with reasonable notice to Respondents made to their principal United States offices, Respondents shall permit any duly authorized representative of the Commission:

## Decision and Order

- A. access, during business office hours of Respondents and in the presence of counsel, to all facilities and access to inspect and copy all books, ledgers, accounts, correspondence, memoranda and all other records and documents in the possession or under the control of Respondent related to compliance with this Order; and
- B. upon five (5) days' notice to Respondents and without restraint or interference from Respondent, to interview officers, directors, or employees of Respondents, who may have counsel present, regarding such matters.

**XI.**

**IT IS FURTHER ORDERED** that this Order shall terminate ten (10) years from the date on which the Order becomes final.

Decision and Order

**PUBLIC  
APPENDIX I  
ORDER TO MAINTAIN ASSETS**

**NON-PUBLIC APPENDIX II  
AGREEMENTS RELATED TO  
THE SPINBRUSH ASSETS  
[Redacted From the Public Record Version But Incorporated  
By Reference]**

**NON-PUBLIC  
APPENDIX III  
AGREEMENTS RELATED TO  
THE INTELLICLEAN PRODUCTS  
[Redacted From the Public Record Version But Incorporated  
By Reference]**

**NON-PUBLIC  
APPENDIX IV  
REMBRANDT KEY EMPLOYEES  
[Redacted From the Public Record Version But Incorporated  
By Reference]**

**NON-PUBLIC  
APPENDIX V  
RELATED TO THE DEFINITION OF  
REMBRANDT IP PROTECTED PRODUCTS  
[Redacted From the Public Record Version But Incorporated  
By Reference]**

Order

**IN THE MATTER OF**

**THE PROCTER & GAMBLE COMPANY**

**ORDER TO MAINTAIN ASSETS**

The Federal Trade Commission ("Commission"), having initiated an investigation of the proposed acquisition by Respondent The Procter & Gamble Company ("P&G") of Respondent The Gillette Company ("Gillette"), hereinafter referred to as "Respondents," and Respondents having been furnished thereafter with a copy of a draft Complaint that the Bureau of Competition proposed to present to the Commission for its consideration and that, if issued by the Commission, would charge Respondents with violations of Section 7 of the Clayton Act, as amended, 15 U.S.C. § 18, and Section 5 of the Federal Trade Commission Act, as amended, 15 U.S.C. § 45; and

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

The Commission having thereafter considered the matter and having determined to accept the executed Consent Agreement and to place such Consent Agreement on the public record for a period of thirty (30) days for the receipt and consideration of public comments, now in further conformity with the procedure described in Commission Rule 2.34, 16 C.F.R. § 2.34, the Commission hereby issues its Complaint, makes the following jurisdictional findings and issues this Order to Maintain Assets:



Order

1. Respondent P&G is a corporation organized, existing and doing business under and by virtue of the laws of the state of Ohio, with its offices and principal place of business located at One Procter & Gamble Plaza, Cincinnati, Ohio 45202.
2. Respondent Gillette is a corporation organized, existing and doing business under and by virtue of the laws of the state of Delaware, with its offices and principal place of business located Prudential Tower, Boston, Massachusetts 02199.
3. The Commission has jurisdiction of the subject matter of this proceeding and of Respondents, and the proceeding is in the public interest.

**ORDER**

**I.**

**IT IS ORDERED** that, as used in this Order to Maintain Assets, the following definitions and the definitions used in the Consent Agreement and the proposed Decision and Order (and when made final, the Decision and Order), which are attached hereto as Appendix A and incorporated herein by reference and made a part of hereof, shall apply:

- A. "P&G" means The Procter & Gamble Company, its directors, officers, employees, agents, representatives, predecessors, successors, and assigns; and its joint ventures, subsidiaries, divisions, groups and affiliates in each case controlled by P&G, and the respective directors, officers, employees, agents, representatives, predecessors, successors, and assigns of each. After the Acquisition P&G, shall include Gillette.
- B. "Gillette" means The Gillette Company, its directors, officers, employees, agents, representatives, predecessors, successors, and assigns; and its joint ventures, subsidiaries, divisions, groups and affiliates in each case controlled by Gillette, and

## Order

the respective directors, officers, employees, agents, representatives, predecessors, successors, and assigns of each.

- C. "Respondents" means P&G and Gillette, individually and collectively.
- D. "Acquisition" means the acquisition contemplated by the "Agreement and Plan of Merger" dated as of January 27, 2005, among The Proctor & Gamble Company, Aquarium Acquisition Corp. and The Gillette Company.
- E. "Acquisition Date" means the earlier of the following dates:
  - 1. the date the Respondents close on the Acquisition pursuant to the Acquisition Agreement; or
  - 2. the date the merger contemplated by the Acquisition Agreement becomes effective by filing the certificate of merger with the Secretary of State of the State of Delaware.
- F. "Commission" means the Federal Trade Commission.
- G. "Closing Date" means as to each Divestiture Product the date on which Respondent (or a Divestiture Trustee) closes on the divestiture of the assets relevant to such Divestiture Product pursuant to the Decision and Order.
- H. "Commission-approved Acquirer" means the following: (1) an entity that is specifically identified in the Decision and Order to acquire particular assets that the Respondents are required to assign, grant, license, divest, transfer, deliver, or otherwise convey pursuant to the Decision and Order and that has been approved by the Commission to accomplish the requirements of the Decision and Order in connection with the Commission's determination to make the Decision and Order final; or (2) an entity approved by the Commission to acquire particular assets that the Respondents are required to

Order

assign, grant, license, divest, transfer, deliver, or otherwise convey pursuant to the Decision and Order.

- I. “Confidential Business Information” means all information owned by, or in the possession or control of, Respondents that is not in the public domain and that is related to the research, Development, manufacture, marketing, commercialization, importation, exportation, cost, pricing, supply, sales, sales support or use of the Divestiture Product(s) or the IntelliClean Products, respectively; provided however, that “Confidential Business Information” shall not include, the following:
  1. information that subsequently falls with the public domain through no violation of this Order or breach of confidentiality or non-disclosure agreement with respect to such information by Respondents;
  2. information related to the SpinBrush Products that Respondent Gillette can demonstrate it obtained without the assistance of Respondent P&G prior to the Acquisition;
  3. information related to the Rembrandt Products that Respondent P&G can demonstrate it obtained without the assistance of Respondent Gillette prior to the Acquisition;
  4. information related to the APDO Products that Respondent P&G can demonstrate it obtained without the assistance of Respondent Gillette prior to the Acquisition;
  5. information related to the IntelliClean Products that Respondent Gillette can demonstrate it obtained without the assistance of Respondent P&G prior to the Acquisition;
  6. information that is required by Law to be publically disclosed;

## Order

7. information that does not relate to the Divestiture Product(s) or the IntelliClean Products.
- J. “Divestiture Assets” means the APDO Assets, the Rembrandt Assets and the SpinBrush Assets, individually and collectively, as defined in the Decision and Order.
- K. “Divestiture Product” means a Product that is the subject of a divestiture under this Order, *i.e.*, the APDO Products, the Rembrandt Products, or the SpinBrush Products; *provided, however*, that, for the purposes of this Order to Maintain Assets, the APDO Products shall be deemed to include all Products Developed, in Development, manufactured, distributed, marketed or sold by Respondent Gillette prior to the Acquisition that were marketed or sold or to be marketed or sold as Products using any of the Product Trademarks Soft&Dri<sup>®</sup> and Dry Idea<sup>®</sup> or any variations or derivatives of such Product Trademarks
- L. “Acquisition Date” means the date on which the Acquisition occurs.
- M. “Divestiture Core Employees” means the APDO Core Employees, the Rembrandt Core Employees, Rembrandt Key Employees, and the Spinbrush Core Employees, individually and collectively, as defined in the Decision and Order.
- N. “Interim Monitor” means any monitor appointed pursuant to Paragraph III of this Order to Maintain Assets or Paragraph VI of the Decision and Order .
- O. “Orders” means the Decision and Order and this Order to Maintain Assets.
- P. “Pre-Acquisition Marketing Plan” means any marketing or brand plan that was planned or implemented within the period immediately prior to the Acquisition and without consideration of the affects of the pending Acquisition for a

Order

Product(s) subject to divestiture under the attached Decision and Order.

- Q. “Remedial Agreement” means the following: (1) any agreement between Respondent(s) and a Commission-approved Acquirer that is specifically referenced and attached to the Decision and Order and all amendments, exhibits, attachments, agreements, and schedules thereto, related to the relevant assets to be assigned, granted, licensed, divested, transferred, delivered, or otherwise conveyed, and that have been approved by the Commission to accomplish the requirements of the Decision and Order in connection with the Commission’s determination to make the Decision and Order final; and/or (2) any agreement between the Respondent(s) and a Commission-approved Acquirer (or between a Divestiture Trustee and a Commission-approved Acquirer) that has been approved by the Commission to accomplish the requirements of the Decision and Order, and all amendments, exhibits, attachments, agreements, and schedules thereto, related to the relevant assets to be assigned, granted, licensed, divested, transferred, delivered, or otherwise conveyed that have been approved by the Commission to accomplish the requirements of the Decision and Order.

## II.

**IT IS FURTHER ORDERED** that from the date this Order to Maintain Assets becomes final:

- A. Respondents shall take such actions as are necessary to maintain the full economic viability, marketability and competitiveness of the business associated with the Divestiture Assets, to minimize any risk of loss of competitive potential for the business associated with the Divestiture Assets, and to prevent the destruction, removal, wasting, deterioration, or impairment of any of the

## Order

Divestiture Assets except for ordinary wear and tear. Respondents shall not sell, transfer, encumber or otherwise impair the full economic viability, marketability or competitiveness of the Divestiture Assets.

- B. Respondents shall maintain the operations of the Divestiture Assets in the regular and ordinary course of business and in accordance with past practice (including regular repair and maintenance of the Divestiture Assets) and/or as may be necessary to preserve the marketability, viability, and competitiveness of each of the Products associated with the Divestiture Assets and shall use their best efforts to preserve the existing relationships with, the following: suppliers; vendors including, but not limited to, the High Volume Retail Account; distributors; customers; Agencies; employees; and, others having business relations with the Divestiture Assets. Respondents' responsibilities shall include, but are not limited to, the following:
1. providing the Divestiture Assets with sufficient working capital to operate the Divestiture Assets at least at current rates of operation, to meet all capital calls with respect to the Divestiture Assets and to carry on, at least at their scheduled pace, all capital projects, business plans and promotional activities for the Divestiture Assets (including, but not limited to, such capital related to the slotting and/or shelf spacing assignments of the Divestiture Product with the High Volume Retail Accounts);
  2. continuing, at least at their scheduled pace, any additional expenditures for the Divestiture Assets authorized prior to the date the Consent Agreement was signed by Respondents including, but not limited to, all research, Development, and marketing expenditures (including, but not limited to, expenditures related to the relaunch of the Spinbrush Products);

Order

3. provide such resources as may be necessary to respond to competition against the Products associated with the Divestiture Assets and/or to prevent any diminution in retail sales of such Products during and after the Acquisition process and prior to divestiture;
  4. provide such resources as may be necessary to maintain the competitive strength and positioning of the Products associated with the Divestiture Assets at the High Volume Retail Accounts;
  5. making available for use by the Divestiture Assets funds sufficient to perform all routine maintenance and all other maintenance as may be necessary to, and all replacements of, the Divestiture Assets;
  6. providing the Divestiture Assets with such funds as are necessary to maintain the full economic viability, marketability and competitiveness of the Divestiture Assets; and
  7. providing such support services to the Divestiture Assets as were being provided to these businesses by Respondents as of the date the Consent Agreement was signed by Respondents.
- C. Respondents shall maintain a work force at least as equivalent in size, training, and expertise to what has been associated with the Divestiture Assets for the relevant Product's most recent Pre-Acquisition Marketing Plan.
- D. Until the Closing Date for each respective set of Divestiture Assets, Respondents provide all the related Divestiture Core Employees with reasonable financial incentives to continue in their positions and to market and promote the relevant Products subject to such divestiture consistent with past practices and/or as may be necessary to preserve the marketability, viability and competitiveness of such Products

## Order

pending divestiture and to ensure successful execution of the Pre-Acquisition Marketing Plans related to the relevant Products. Such incentives shall include a continuation of all employee benefits offered by Respondents until the Closing Date for the divestiture of the respective Divestiture Assets has occurred, including regularly scheduled raises, bonuses, vesting of pension benefits (as permitted by Law), and additional incentives as may be necessary to prevent any diminution of the relevant Product's competitiveness.

## E. Respondents shall:

1. during the Spinbrush Access Period, not interfere with the hiring or employing by the Commission-approved Acquirer of Spinbrush Core Employees, and shall remove any impediments within the control of Respondents that may deter these employees from accepting employment with the Commission-approved Acquirer, including, but not limited to, any noncompete provisions of employment or other contracts with Respondents that would affect the ability or incentive of those individuals to be employed by the Commission-approved Acquirer. In addition, Respondents shall not make any counteroffer to an Spinbrush Core Employee who receives a written offer of employment from the Commission-approved Acquirer;

*provided, however,* that this Paragraph II.E.1 shall not prohibit the Respondents from making offers of employment to or employing any Spinbrush Core Employee during the Spinbrush Access Period where the Commission-approved Acquirer has notified the Respondents in writing that the Commission-approved Acquirer does not intend to make an offer of employment to that employee;

*provided further* that, if the Respondents notify the Commission-approved Acquirer in writing of their desire to make an offer of employment to a particular Spinbrush Core Employee and the Commission-approved Acquirer does not



Order

make an offer of employment to that employee within twenty (20) Days of the date the Commission-approved Acquirer receives such notice, the Respondents may make an offer of employment to that employee.

F. Pending divestiture of the relevant Divestiture Assets, Respondents shall:

1. shall not provide, disclose or otherwise make available, directly or indirectly, any Confidential Business Information related to the marketing or sales of the APDO Assets to the employees associated with business related to the antiperspirant and/or deodorant Products marketed and sold by Respondent P&G prior to the Acquisition (including, but not limited to, such employees with work responsibilities related to the Old Spice<sup>®</sup> trademark and any variations or derivatives of such trademark);
2. shall not provide, disclose or otherwise make available, directly or indirectly, any Confidential Business Information related to the marketing or sales of the Rembrandt Assets to the employees associated with business related to the teeth whitening Products marketed and sold by Respondent P&G prior to the Acquisition (including, but not limited to, those employees with work responsibilities related to the Crest<sup>®</sup> trademark and any variations or derivatives of such trademark);
3. shall not provide, disclose or otherwise make available, directly or indirectly, any Confidential Business Information related to the marketing or sales of the Spinbrush Assets to the employees associated with business related to the non-rechargeable battery operated toothbrush Products marketed and sold by Respondent Gillette prior to the Acquisition (including, but not

## Order

limited to, those employees with work responsibilities related to the Oral-B<sup>®</sup> trademark and any variations or derivatives of such trademark);

4. shall institute procedures and requirements to ensure that employees identified above

a. do not provide, disclose or otherwise make available, directly or indirectly, any Confidential Business Information in contravention of this Order to Maintain Assets; and

b. do not solicit, access or use any Confidential Business Information that they are prohibited under this Order to Maintain Assets from receiving for any reason or purpose;

G. Not later than thirty (30) days following the Acquisition Date, Respondents shall provide to all of Respondents' employees and other personnel who may have access to Confidential Business Information related to each of the respective Divestiture Assets written or electronic notification of the restrictions on the use of such information by Respondents' personnel. At the same time, if not provided earlier, Respondents shall provide a copy of such notification by e-mail with return receipt requested or similar transmission, and keep an electronic file of such receipts for one (1) year after the Closing Date. Respondents shall provide a copy of the form of such notification to the Commission-approved Acquirer, the Interim Monitor(s), and the Commission. Respondents shall also obtain from each employee covered by this Paragraph II.H. an agreement to abide by the applicable restrictions. Respondents shall maintain complete records of all such agreements at Respondents' corporate headquarters and shall provide an officer's certification to the Commission stating that such acknowledgment program has been implemented and is being complied with. Respondents shall monitor the implementation by their employees and

Order

other personnel of all applicable restrictions, and take corrective actions for the failure of such employees and personnel to comply with such restrictions or to furnish the written agreements and acknowledgments required by this Order to Maintain Assets. Respondents shall provide the Commission-approved Acquirer with copies of all certifications, notifications and reminders sent to Respondents' employees and other personnel.

- H. Respondents shall adhere to and abide by the Remedial Agreements (which agreements shall not vary or contradict, or be construed to vary or contradict, the terms of the Orders, it being understood that nothing in the Orders shall be construed to reduce any obligations of Respondents under such agreement(s)), which are incorporated by reference into this Order to Maintain Assets and made a part hereof.
- I. The purpose of this Order to Maintain Assets is to maintain the full economic viability, marketability and competitiveness of the business(es) associated with the Divestiture Assets, to minimize any risk of loss of competitive potential for the business associated with the Divestiture Assets, and to prevent the destruction, removal, wasting, deterioration, or impairment of any of the Divestiture Assets except for ordinary wear and tear.

**III.**

**IT IS FURTHER ORDERED** that:

- A. At any time after Respondents sign the Consent Agreement in this matter, the Commission may appoint an Interim Monitor to assure that Respondents expeditiously comply with all of their obligations and perform all of their responsibilities as required by the Orders and the Remedial Agreements. The

## Order

Commission may appoint one or more Interim Monitors to assure Respondents' compliance with the requirements of the Orders, and the related Remedial Agreements.

- B. The Commission shall select the Interim Monitor, subject to the consent of Respondents, which consent shall not be unreasonably withheld. If Respondent P&G has not opposed, in writing, including the reasons for opposing, the selection of a proposed Interim Monitor within ten (10) Days after notice by the staff of the Commission to Respondents of the identity of any proposed Interim Monitor, Respondents shall be deemed to have consented to the selection of the proposed Interim Monitor.
- C. Not later than ten (10) Days after the appointment of the Interim Monitor, Respondents shall execute an agreement that, subject to the prior approval of the Commission, confers on the Interim Monitor all the rights and powers necessary to permit the Interim Monitor to monitor Respondents' compliance with the relevant requirements of the Orders in a manner consistent with the purposes of the Orders.
- D. If one or more Interim Monitors are appointed pursuant to this Paragraph or pursuant to the relevant provisions of the Decision and Order in this matter, Respondents shall consent to the following terms and conditions regarding the powers, duties, authorities, and responsibilities of each Interim Monitor:
  - 1. The Interim Monitor shall have the power and authority to monitor Respondents' compliance with the divestiture and asset maintenance obligations and related requirements of the Orders, and shall exercise such power and authority and carry out the duties and responsibilities of the Interim Monitor in a manner consistent with the purposes of the Orders and in consultation with the Commission;

Order

2. The Interim Monitor shall act in a fiduciary capacity for the benefit of the Commission;
3. The Interim Monitor shall serve until the later of:
  - a. the completion by Respondents of the divestiture of all relevant assets required to be assigned, granted, licensed, divested, transferred, delivered, or otherwise conveyed pursuant to this Order to Maintain Assets in a manner that fully satisfies the requirements of this Order to Maintain Assets and notification by the Commission-approved Acquirer to the Interim Monitor that it is fully capable of producing the relevant Product(s) acquired pursuant to a Remedial Agreement independently of Respondents; and fulfillment of the Respondents obligations under the Decision and Order with respect to the IntelliClean Products; or
  - b. the completion by Respondents of the last obligation under the Order pertaining to the Interim Monitor's service;

*provided, however,* that the Commission may extend or modify this period as may be necessary or appropriate to accomplish the purposes of this Order to Maintain Assets.

- E. Subject to any demonstrated legally recognized privilege, the Interim Monitor shall have full and complete access to Respondents' personnel, books, documents, records kept in the normal course of business, facilities and technical information, and such other relevant information as the Interim Monitor may reasonably request, related to Respondents' compliance with their obligations under the Orders, including, but not limited to, their obligations related to the relevant assets. Respondents shall cooperate with any

## Order

reasonable request of the Interim Monitor and shall take no action to interfere with or impede the Interim Monitor's ability to monitor Respondents' compliance with the Orders.

- F. The Interim Monitor shall serve, without bond or other security, at the expense of Respondents on such reasonable and customary terms and conditions as the Commission may set. The Interim Monitor shall have authority to employ, at the expense of the Respondents, such consultants, accountants, attorneys and other representatives and assistants as are reasonably necessary to carry out the Interim Monitor's duties and responsibilities.
- G. Respondents shall indemnify the Interim Monitor and hold the Interim Monitor harmless against any losses, claims, damages, liabilities, or expenses arising out of, or in connection with, the performance of the Interim Monitor's duties, including all reasonable fees of counsel and other reasonable expenses incurred in connection with the preparations for, or defense of, any claim, whether or not resulting in any liability, except to the extent that such losses, claims, damages, liabilities, or expenses result from misfeasance, gross negligence, willful or wanton acts, or bad faith by the Interim Monitor.
- H. Respondents shall report to the Interim Monitor in accordance with the requirements of this Order to Maintain Assets and/or as otherwise provided in any agreement approved by the Commission. The Interim Monitor shall evaluate the reports submitted to the Interim Monitor by Respondents, and any reports submitted by the Commission-approved Acquirer with respect to the performance of Respondents' obligations under the Orders or the Remedial Agreement. Within one (1) month from the date the Interim Monitor receives these reports, the Interim Monitor shall report in writing to the Commission concerning performance by Respondents of their obligations under the Orders.

Order

- I. Respondents may require the Interim Monitor and each of the Interim Monitor's consultants, accountants, attorneys and other representatives and assistants to sign a customary confidentiality agreement;

*provided, however,* that such agreement shall not restrict the Interim Monitor from providing any information to the Commission.

- J. The Commission may, among other things, require the Interim Monitor and each of the Interim Monitor's consultants, accountants, attorneys and other representatives and assistants to sign an appropriate confidentiality agreement related to Commission materials and information received in connection with the performance of the Interim Monitor's duties.
- K. If the Commission determines that the Interim Monitor has ceased to act or failed to act diligently, the Commission may appoint a substitute Interim Monitor in the same manner as provided in this Paragraph or the relevant provisions of the Decision and Order in this matter.
- L. The Commission may on its own initiative, or at the request of the Interim Monitor, issue such additional orders or directions as may be necessary or appropriate to assure compliance with the requirements of the Orders.
- M. The Interim Monitor appointed pursuant to this Order to Maintain Assets or the relevant provisions of the Decision and Order in this matter may be the same person appointed as a Divestiture Trustee pursuant to the relevant provisions of the Decision and Order.

Order

#### IV.

**IT IS FURTHER ORDERED** that within thirty (30) Days after the date this Order to Maintain Assets becomes final, and every thirty (30) Days thereafter until Respondents have fully complied with their obligations to assign, grant, license, divest, transfer, deliver or otherwise convey relevant assets as required by Paragraph II.A., III.A, IV.A. and V.A. of the related Decision and Order in this matter, Respondents shall submit to the Commission a verified written report setting forth in detail the manner and form in which it intends to comply, is complying, and has complied with this Order to Maintain Assets and the related Decision and Order; *provided, however*, that, after the Decision and Order in this matter becomes final, the reports due under this Order to Maintain Assets may be consolidated with, and submitted to the Commission at the same time as, the reports required to be submitted by Respondents pursuant to Paragraph VIII of the Decision and Order.

#### V.

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

#### VI.

**IT IS FURTHER ORDERED** that, for the purposes of determining or securing compliance with this Order to Maintain Assets, and subject to any legally recognized privilege, and upon



Order

written request with reasonable notice to Respondents made to their principal United States Office, Respondents shall permit any duly authorized representatives of the Commission:

- A. Access, during office hours of Respondents and in the presence of counsel, to all facilities and access to inspect and copy all books, ledgers, accounts, correspondence, memoranda and all other records and documents in the possession or under the control of Respondents relating to compliance with this Order to Maintain Assets; and
- B. Upon five (5) Days notice to Respondents and without restraint or interference from Respondents, to interview officers, directors, or employees of Respondents, who may have counsel present, regarding such matters.

**VII.**

**IT IS FURTHER ORDERED** that this Order to Maintain Assets shall terminate on the earlier of:

- A. Three (3) Days after the Commission withdraws its acceptance of the Consent Agreement pursuant to the provisions of Commission Rule 2.34, 16 C.F.R. § 2.34; or
- B. The day after the divestiture of all of the Divestiture Assets, as required by and described in the Decision and Order, has been completed and each Interim Monitor, in consultation with Commission staff and the Commission-approved Acquirer(s), notifies the Commission that all related assignments, conveyances, deliveries, grants, licenses, transactions, transfers and other transitions are complete, or the Commission otherwise directs that this Order to Maintain Assets is terminated.

Order

**PUBLIC**  
**APPENDIX A**  
**TO THE ORDER TO MAINTAIN ASSETS**  
**AGREEMENT CONTAINING CONSENT ORDER**  
**AND**  
**PROPOSED DECISION AND ORDER**

Analysis

## **Analysis of Agreement Containing Consent Orders to Aid Public Comment**

### **I. Introduction**

The Procter & Gamble Company (“P&G”) and The Gillette Company (“Gillette”) are both leading suppliers of consumer products worldwide. P&G proposes to acquire Gillette. The Federal Trade Commission (“Commission”) has accepted, subject to final approval, an Agreement Containing Consent Orders (“Consent Agreement”) from P&G and Gillette. The purpose of the Consent Agreement is to remedy the anticompetitive effects that would otherwise result from P&G’s proposed acquisition. Under the terms of the Consent Agreement, the parties will be required to divest: (1) Gillette’s Rembrandt® at-home teeth whitening business; (2) P&G’s Crest® SpinBrush™ battery-powered and rechargeable toothbrush business; and (3) Gillette’s Right Guard® men’s antiperspirant/deodorant (“AP/DO”) business. In addition, P&G is required to amend its joint venture agreement with Philips Oral Healthcare, Inc. (“Philips”) regarding the Crest® Sonicare® IntelliClean System (“IntelliClean”) rechargeable toothbrush.

The proposed Consent Agreement has been placed on the public record for thirty (30) days to solicit comments from interested people. Comments received during this period will become part of the public record. After thirty (30) days, the Commission will again review the proposed Consent Agreement and the comments received, and will decide whether it should withdraw from the proposed Consent Agreement or make it final.

Pursuant to an Agreement and Plan of Merger dated January 27, 2005, P&G proposes to acquire 100 percent of the voting securities of Gillette in a transaction valued at approximately \$57 billion (“Proposed Acquisition”). The Commission’s Complaint alleges that the Proposed Acquisition, if consummated, would violate Section 7 of the Clayton Act, as amended, 15 U.S.C. § 18, and Section 5 of the Federal Trade Commission Act, as amended,

## Analysis

15 U.S.C. § 45, by lessening competition in the United States markets for the research, development, manufacture, distribution, and sale of at-home teeth whitening products, adult battery-powered toothbrushes, rechargeable toothbrushes, and men's AP/DOs.

Consistent with the well-established approach to merger analysis, we have determined the appropriate product markets in which to analyze the likely competitive effects of the proposed merger. Staff initially examined whether the combination of the two companies' broad array of consumer products would be likely to have anticompetitive effects, including not only increased prices in the short term but also the creation of entry barriers that could affect price and innovation in the long term. In particular, staff investigated whether the combined entity would have an increased ability to exploit its position as a so-called "category manager" or "category captain," in order to obtain premium retailer shelf space and potentially exclude or disadvantage competitors in various broad categories, like oral care or AP/DO.

The investigation has disclosed, however, that most retailers do not look at broad categories, like oral care and AP/DO, when they decide which products to stock and sell. They generally make decisions on individual products (e.g., men's AP/DO), that are perceived to be close substitutes within these broad categories. One supplier may be preferred for an individual product even though another supplier is preferred for other products in the broad category. Moreover, most retailers are likely to employ different category captains to assist them on a product-by-product basis within the broad categories. We have therefore concluded that the loss of competition between the merging parties in broad categories is unlikely to cause competitive harm. We have instead focused on individual products within the broad categories. These individual product markets include at-home teeth whitening, battery-powered toothbrushes, and men's AP/DO. The Commission has sought and obtained relief in these relevant markets.

Analysis

## **II. The Parties**

Headquartered in Cincinnati, Ohio, P&G is one of the largest and most diversified suppliers of consumer products in the world. In 2004, P&G had worldwide net sales of approximately \$51.4 billion. With its Crest® line of products, P&G is one of the leading suppliers of oral care products in the United States. The Crest family of products includes the Crest® Whitestrips™ and Crest® Night Effects™ lines of at-home teeth whitening products and the Crest® SpinBrush™ line of battery-powered toothbrushes. P&G is also a leading supplier of men's AP/DOs under its Old Spice® brand.

Gillette, based in Boston, Massachusetts, is also one of the world's leading suppliers of consumer products. Gillette had total worldwide net sales of approximately \$10.5 billion in its 2004 fiscal year. Like P&G, Gillette is one of the leading suppliers of oral care products in the United States with its Oral-B® and Oral-B® Braun® line of manual, battery-powered, and rechargeable toothbrushes, and its Oral-B® Rembrandt® and Rembrandt® line of at-home teeth whitening products. Gillette is also a leading supplier of men's AP/DOs under its Right Guard® and Gillette® Series brands.

## **III. At-Home Teeth Whitening Products**

One of the relevant markets in which to assess the competitive effects of the Proposed Acquisition is the United States market for at-home teeth whitening products. At-home teeth whitening products whiten teeth by bleaching them with either hydrogen or carbamide peroxide. These products are typically sold over-the-counter through food, drug, club, and mass merchandise channels and are marketed to be used by the consumer at home. There are several different types of at-home teeth whitening products, including strips, gels, pens and sticks, although strip and gel products account for the vast majority of sales of at-home teeth whitening products in the United States.

## Analysis

The United States market for at-home teeth whitening products is highly concentrated, with P&G and Gillette as the two largest suppliers in this market and the only two significant suppliers of branded strips. P&G is the market leader with its Crest Whitestrips® and Crest Night Effects® products, while Gillette is the second leading supplier with its Oral-B® Rembrandt® and Rembrandt® products. Together, the parties account for over 80% of the sales in this market.

The Proposed Acquisition would significantly increase concentration in the United States market for at-home teeth whitening products, leaving P&G as the dominant supplier. By eliminating competition between the two leading suppliers, the Proposed Acquisition would likely result in higher prices, reduced innovation, and fewer product choices for consumers in this market.

#### **IV. Adult Battery-Powered Toothbrushes**

A second relevant product market in which to assess the competitive effects of the Proposed Acquisition is the United States market for adult battery-powered toothbrushes. Adult battery-powered toothbrushes are usually powered by AA or AAA batteries and either have oscillating or pulsating brush heads. The majority of adult battery-powered toothbrushes are sold at retail for between \$5 and \$8, and the batteries and brush heads can be replaced on some, but not all, products. Adult battery-powered toothbrushes are typically marketed as upgrades over manual toothbrushes and are more affordable than sophisticated rechargeable toothbrushes.

The United States market for adult battery-powered toothbrushes is highly concentrated. P&G and Gillette are the two largest suppliers in this market. P&G markets its adult battery-powered products under the Crest® SpinBrush™ brand name, while Gillette sells its adult battery-powered products under the Oral-B® brand name. Gillette also dominates the adult high-priced manual and low-priced rechargeable toothbrush segments,

Analysis

which are the segments most likely to capture any switching away from adult battery-powered toothbrushes in the face of a price increase. Together, the parties account for over 85% of the sales in the United States adult battery-powered toothbrush market.

The Proposed Acquisition would significantly increase concentration in the United States market for adult battery-powered toothbrush products, leaving P&G as the dominant supplier. By eliminating competition between the two leading suppliers, the Proposed Acquisition would likely result in higher prices, reduced innovation, and fewer product choices for consumers in this market.

## V. Rechargeable Toothbrushes

A third relevant product market in which to assess the competitive effects of the Proposed Acquisition is the United States market for rechargeable toothbrushes. Rechargeable toothbrushes contain a rechargeable battery that powers high-speed oscillating, pulsating, or vibrating brush heads. They have a separate recharging unit that plugs into an electrical outlet to recharge the battery contained in the toothbrush. Brush heads for these products are almost always replaceable. Rechargeable toothbrushes typically are sold at retail for between \$20 and \$150, and are marketed as the premium brushing option for consumers.

The United States market for rechargeable toothbrushes is highly concentrated with only two suppliers, Gillette and Philips, accounting for virtually all of the sales of these products. Gillette markets a full line of rechargeable toothbrush products under the Oral-B® Braun® brand name, while Philips sells mostly mid- to high-end products under the Philips® Sonicare® brand name. Philips and P&G also have a joint venture to co-develop and co-market the IntelliClean product, the first integrated toothbrush/dentifrice product (*i.e.*, toothbrush that self dispenses toothpaste) sold in the United States. As a result, the Proposed Acquisition would allow P&G to acquire the only significant competitor to its joint venture partner, Philips, thereby reducing

## Analysis

P&G's incentives to support the IntelliClean product. The agreement between Philips and P&G also contains non-compete provisions that, if the Proposed Acquisition were consummated, could harm consumers.

The Proposed Acquisition would eliminate P&G's incentive to fully support and promote the IntelliClean product and create a situation where the only two suppliers in the market are subject to non-compete provisions. Accordingly, the Proposed Acquisition would likely result in higher prices, reduced innovation, and fewer product choices for consumers in this market.

## VI. Men's AP/DOs

A fourth relevant product market in which to assess the competitive effects of the Proposed Acquisition is the United States market for men's AP/DOs. An antiperspirant is a substance that is used to prevent or reduce underarm sweating. A deodorant is a substance that is used to suppress underarm odor. These ingredients are typically combined together for complete underarm protection. AP/DOs are typically gender-specific and sold in various forms, including roll-ons, traditional solids, invisible solids, gels, and aerosols. Men's AP/DOs are unique in, among other things, their packaging, fragrances, marketing, formulations, and location on the shelf.

The United States market for men's AP/DOs is highly concentrated. P&G and Gillette are the two largest suppliers of men's AP/DOs in the United States. P&G markets its men's AP/DOs under the Old Spice® brand name, while Gillette sells its products under the Right Guard® and Gillette Series® brand names. Combined, the Respondents account for well over 50% of the sales in this highly concentrated market.

Accordingly, the Proposed Acquisition would significantly increase concentration in the United States market for men's AP/DOs, leaving P&G as the dominant supplier. By eliminating competition between the two leading suppliers, the Proposed



Analysis

Acquisition would likely result in higher prices and fewer product choices for consumers in this market.

### **VII. Entry**

Entry into the United States at-home teeth whitening, adult battery-powered toothbrush, rechargeable toothbrush, and men's AP/DO markets is unlikely to deter or counteract the anticompetitive effects of the Proposed Acquisition. Entry into these markets is difficult and time-consuming and would require the investment of extremely high sunk costs to, among other things, develop products, provide advertising and promotional funding, establish a strong brand name, and create a distribution network. A new entrant also faces the difficult task of convincing retailers to carry their products.

### **VIII. The Consent Agreement**

The Consent Agreement effectively remedies the Proposed Acquisition's anticompetitive effects in the relevant markets discussed above. The Consent Agreement preserves competition in these markets by requiring the divestiture of: (1) the Rembrandt at-home teeth whitening business to a Commission-approved acquirer; (2) the Crest SpinBrush battery-powered business to Church & Dwight Company, Inc. ("Church & Dwight"); and (3) the Right Guard business to a Commission-approved acquirer.<sup>1</sup> In addition, the Consent Agreement requires P&G to amend its joint venture agreement to allow Philips to independently market and sell the IntelliClean product.

---

<sup>1</sup> The Rembrandt business that will be divested includes all of Gillette's existing and future teeth whitening products. For viability reasons, the purchaser of the Right Guard business will have the option of acquiring certain manufacturing assets and/or Gillette's Soft & Dri® and Dry Idea® assets.

## Analysis

The divestiture of the Rembrandt business must take place within three (3) months and the Right Guard business within four (4) months after the date the order becomes final. The Commission's goal in evaluating possible purchasers of divested assets is to ensure that the competitive environment that existed prior to the acquisition is maintained. A proposed acquirer of divested assets must not itself present competitive problems. Should the parties fail to accomplish the divestiture within the time and in the manner required by the Consent Agreement, the Commission may appoint a trustee to divest these assets. If approved, the trustee would have the exclusive power and authority to accomplish the divestiture within one year of being appointed, subject to any necessary extensions by the Commission. The Consent Agreement requires the parties to provide the trustee with access to information related to, among other things, the Rembrandt and Right Guard businesses as necessary to fulfill his or her obligations.

The Order to Maintain Assets that is included in the Consent Agreement requires that P&G and Gillette maintain the viability of the Rembrandt and Right Guard businesses as competitive operations until the businesses are transferred to Commission-approved acquirers.<sup>2</sup> The Commission has approved Edward Gold of PricewaterhouseCoopers as the Interim Monitor pursuant to the Consent Agreement to ensure that P&G and Gillette comply with the provisions of the Order.

There are also several provisions of the Consent Agreement designed to ensure the success of the divestiture of the Crest SpinBrush business to Church & Dwight. First, the Consent Agreement requires P&G to divest its rights and assets relating to adult battery-powered toothbrushes, including all research and development data, sales and marketing materials, and intellectual

---

<sup>2</sup> The Order to Maintain Assets also requires that P&G and Gillette maintain the viability of the Soft & Dri and Dry Idea businesses.

Analysis

property. Second, P&G will provide Church & Dwight with a license to the Crest trademark, subject to minimum protections under trademark law, for use with the SpinBrush brand name that will be acquired outright by Church & Dwight. These provisions are designed to ensure that Church & Dwight can successfully transition the Crest SpinBrush family of products to a brand name of its choosing. Third, the Consent Agreement allows, and provides incentives for, P&G to render transitional services to Church & Dwight and retailers for a period of time to ensure the continuity and competitive viability of the products.

The Commission is satisfied that Church & Dwight is a well-qualified acquirer of the Crest SpinBrush business. Church & Dwight sells a variety of consumer products throughout the world, including oral care, personal care, and household products, and had total worldwide net sales of approximately \$1.5 billion in 2004. The company owns several well-known oral care brands, such as Arm & Hammer®, Aim®, and Mentadent™, and currently sells a variety of oral care products, including toothpaste and manual toothbrushes. Because of its existing business, Church & Dwight already has an experienced sales force that has relationships with major retailers and dental professionals, thereby enabling it to be a successful acquirer of the SpinBrush assets.

The Consent Agreement also requires P&G to amend its joint venture agreement with Philips regarding IntelliClean. The amended agreement, which is an attachment to the order, allows Philips to independently market and sell IntelliClean. The amended agreement also eliminates all non-compete provisions allowing both P&G and Philips to develop and sell future rechargeable toothbrush products.

The purpose of this analysis is to facilitate public comment on the Consent Agreement, and is not intended to constitute an official interpretation of the proposed Decision and Order or the Order to Maintain Assets, or to modify their terms in any way.

Complaint

IN THE MATTER OF

**JOHNSON & JOHNSON**CONSENT ORDER, ETC., IN REGARD TO ALLEGED VIOLATIONS OF  
SEC. 7 OF THE CLAYTON ACT AND SEC. 5 OF THE FEDERAL TRADE  
COMMISSION ACT*Docket C-4154; File No. 0510050**Complaint, December 21, 2005--Decision, December 21, 2005*

This consent order addresses the acquisition by Respondent Johnson & Johnson -- a comprehensive and broadly-based manufacturer of products related to all aspects of human health care -- of Guidant Corporation, which manufactures products in three broad business units: cardiac rhythm management, vascular intervention, and cardiac surgery. The order, among other things, requires the respondent to grant to Abbott Laboratories or another Commission-approved firm -- within ten days and at no minimum price -- a fully paid-up, non-exclusive, irrevocable license that permits the licensee to make and sell drug-eluting stents with a drug delivery system, which are used to treat coronary artery disease by propping open a clogged artery and eluting a drug, thereby helping to prevent renarrowing of the artery. The consent order also requires the respondent to divest to Datascope or another Commission-approved firm, within fifteen days, its endoscopic vessel harvesting product line, which is used in coronary artery bypass graft surgery to remove a patient's leg vein, arm artery, or other blood vessel; that vessel is then used as a conduit to bypass one or more blocked coronary arteries. In addition, the consent order requires the respondent to terminate its agreement to distribute the proximal anastomotic assist device -- used to avoid the need to clamp the aorta when attaching a harvested vessel to it -- of Novare Surgical System, Inc.

*Participants*

For the Commission: *Jonathan S. Klarfield, Jeffrey H. Perry, Kari A. Wallace, Brendan J. McNamara, Tammy L. Imhoff, Thomas D. Mays, Kenneth A. Libby, Sylvia M. Brooks, Katherine L. Rosenberg, Michael R. Moiseyev, Daniel P. Ducore, Elizabeth A. Schneirov, Michael G. Vita and Mark Frankena.*

For the Respondent: *Steve Newborn, Weil, Gotshal & Manges, LLP.*

Complaint

## COMPLAINT

Pursuant to the Clayton Act and the Federal Trade Commission Act, and its authority thereunder, the Federal Trade Commission (“Commission”), having reason to believe that Respondent Johnson & Johnson (“J&J”), a corporation subject to the jurisdiction of the Commission, has agreed to acquire Guidant Corporation (“Guidant”), a corporation subject to the jurisdiction of the Commission, in violation of Section 7 of the Clayton Act, as amended, 15 U.S.C. § 18, and Section 5 of the Federal Trade Commission Act (“FTC Act”), as amended, 15 U.S.C. § 45, and it appearing to the Commission that a proceeding in respect thereof would be in the public interest, hereby issues its Complaint, stating its charges as follows:

### I. DEFINITIONS

1. “Commission” means the Federal Trade Commission.
2. “J&J” or “Respondent” means Johnson & Johnson, its directors, officers, employees, agents, representatives, predecessors, successors, and assigns; its joint ventures, subsidiaries, divisions, groups and affiliates controlled by Johnson & Johnson, and the respective directors, officers, employees, agents, representatives, successors, and assigns of each.
3. “Guidant” means Guidant Corporation, its directors, officers, employees, agents, representatives, predecessors, successors, and assigns; its joint ventures, subsidiaries, divisions, groups and affiliates controlled by Guidant Corporation, and the respective directors, officers, employees, agents, representatives, successors, and assigns of each.
4. “Drug Eluting Stent” or “DES” means a stent that elutes or otherwise delivers one or more drugs or pharmaceutical compositions for the treatment of coronary artery disease.

## Complaint

5. “Endoscopic Vessel Harvesting Device” or “EVH Device” means a medical device consisting of various components to allow for the minimally-invasive removal of the saphenous vein, the radial artery, or other conduit for use in coronary artery bypass graft surgery, from a patient’s body with the use of endoscopic technology and equipment.

6. “FDA” means the United States Food and Drug Administration.

7. “Proximal Anastomotic Assist Device” or “Proximal AAD” means a medical device used to create a bloodless field, without clamping the aorta, to assist in the creation of a proximal anastomosis as part of a coronary artery bypass graft surgery.

8. “Rapid Exchange,” “Rapid Exchange delivery system” or “RX” means intraluminal catheters and stent and embolic protection delivery systems having a guidewire lumen with a proximal guidewire port located substantially remote from the proximal end of the catheter shaft.

## II. RESPONDENT

9. Respondent J&J is a corporation organized, existing, and doing business under and by virtue of the laws of the state of New Jersey, with its office and principal place of business located at One Johnson & Johnson Plaza, New Brunswick, New Jersey 08933. J&J, among other things, is engaged in the research, development, marketing and sale of interventional cardiology products, including Drug Eluting Stents, and cardiac surgery devices, including Endoscopic Vessel Harvesting Devices and Proximal Anastomotic Assist Devices.

10. J&J is, and at all times relevant herein has been, engaged in commerce, as “commerce” is defined in Section 1 of the Clayton Act as amended, 15 U.S.C. § 12, and is a corporation whose business is in or affects commerce, as “commerce” is

Complaint

defined in Section 4 of the Federal Trade Commission Act, as amended, 15 U.S.C. § 44.

### **III. ACQUIRED COMPANY**

11. Guidant is a corporation organized, existing, and doing business under and by virtue of the laws of the State of Indiana, with its office and principal place of business located at 111 Monument Circle, Indianapolis, Indiana 46204. Guidant, among other things, is engaged in the research, development, marketing, and sale of interventional cardiology products, including the research and development of Drug Eluting Stents, and cardiac surgery devices, including Endoscopic Vessel Harvesting Devices and Proximal Anastomotic Assist Devices.

12. Guidant is, and at all times relevant herein has been, engaged in commerce, as “commerce” is defined in Section 1 of the Clayton Act as amended, 15 U.S.C. § 12, and is a corporation whose business is in or affects commerce, as “commerce” is defined in Section 4 of the Federal Trade Commission Act, as amended, 15 U.S.C. § 44.

### **IV. PROPOSED ACQUISITION**

13. On December 15, 2004, J&J and Guidant entered into an agreement and plan of merger (the “Purchase Agreement”) whereby J&J agreed to acquire Guidant in a transaction valued at approximately \$25.4 billion (the “Acquisition”).

### **V. RELEVANT MARKET**

14. For the purposes of this Complaint, the relevant lines of commerce in which to analyze the effects of the Acquisition are the research, development, manufacture, and/or sale of the following products:

- a. Drug Eluting Stents;

## Complaint

- b. Endoscopic Vessel Harvesting Devices; and
- c. Proximal Anastomotic Assist Devices.

15. For the purposes of this Complaint, the United States is the relevant geographic area in which to analyze the effects of the Acquisition in the relevant lines of commerce.

## VI. STRUCTURE OF THE MARKETS

16. J&J is one of only two companies (the other is Boston Scientific Corporation) currently selling DESs in the United States. At least three other companies, including Guidant, are involved in the research and development of DESs and are poised to receive FDA approval to sell DESs in the United States in the next two to three years.

17. There are only three companies free to offer Rapid Exchange versions of their DESs: J&J, Guidant and Boston Scientific. No other company has licenses or access to the Rapid Exchange patents. Currently, over 70 percent of the DES devices sold in the United States employ the Rapid Exchange delivery system, and the percentage of DES devices sold on Rapid Exchange delivery systems in the United States is expected to continue to increase rapidly.

18. Until recently, J&J and Guidant were the sole competitors in the market for EVH Devices. Although another company, Terumo Corporation, received FDA approval for its device in January of 2005, J&J and Guidant still dominate the market for these devices, and together account for almost 100 percent of sales in the U.S. market for EVH Devices.

19. The U.S. market for Proximal AADs is also highly concentrated as measured by the Herfindahl-Hirschman Index (“HHI”). J&J and Guidant are two of only three companies that compete in the market for Proximal AADs. Guidant is the market



Complaint

leader in this market, and together with J&J, accounts for over 95 percent of unit sales of Proximal AADs in the U.S. market.

## VII. ENTRY CONDITIONS

20. Developing a Drug Eluting Stent, Endoscopic Vessel Harvesting Device, or Proximal Anastomotic Assist Device, working around and/or acquiring licenses to critical intellectual property related to those devices, obtaining FDA approval for those devices, and marketing those devices, takes significantly longer than two years. Therefore, entry into the relevant lines of commerce described in Paragraph 14 would not be timely, likely, or sufficient in magnitude, character and scope to deter or counteract the anti-competitive effects of the Acquisition.

## VIII. EFFECTS OF THE ACQUISITION

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

- a. eliminating potential competition between two of only three suppliers of Drug Eluting Stents with access to a Rapid Exchange delivery system;
- b. eliminating actual, direct and substantial competition between J&J and Guidant in the markets for the research, development, marketing, and sale of Endoscopic Vessel Harvesting Devices and Proximal Anastomotic Assist Devices;
- c. increasing the ability of the merged entity to unilaterally raise prices in the relevant markets; and
- d. reducing research and development in the relevant markets.

Complaint

**IX. VIOLATIONS CHARGED**

22. The Purchase Agreement described in Paragraph 13 constitutes a violation of Section 5 of the FTC Act, as amended, 15 U.S.C. § 45.

23. The Acquisition described in Paragraph 13, if consummated, would constitute a violation of Section 7 of the Clayton Act, as amended, 15 U.S.C. § 18, and Section 5 of the FTC Act, as amended, 15 U.S.C. § 45.

WHEREFORE, THE PREMISES CONSIDERED, the Federal Trade Commission on this 21<sup>st</sup> day of December, 2005, issues its Complaint against said Respondent.

Decision and Order

## **DECISION AND ORDER**

The Federal Trade Commission (“Commission”) having initiated an investigation of the proposed acquisition by Respondent Johnson & Johnson (“J&J” or “Respondent”) of Guidant Corporation (“Guidant”), and Respondent having been furnished thereafter with a copy of a draft of Complaint that the Bureau of Competition proposed to present to the Commission for its consideration and which, if issued by the Commission, would charge Respondent with violations of Section 7 of the Clayton Act, as amended, 15 U.S.C. § 18, and Section 5 of the Federal Trade Commission Act, as amended, 15 U.S.C. § 45; and

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

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

## Decision and Order

1. Respondent J&J is a corporation organized, existing and doing business under and by virtue of the laws of the State of New Jersey, with its offices and principal place of business located at One Johnson & Johnson Plaza, New Brunswick, NJ 08933.

2. Guidant is a corporation organized, existing and doing business under and by virtue of the laws of the State of Indiana, with its offices and principal place of business located at 111 Monument Circle, Indianapolis, IN 46204.

3. The Federal Trade Commission has jurisdiction over the subject matter of this proceeding and of Respondent, and the proceeding is in the public interest.

**ORDER****I.**

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

- A. “J&J” or “Respondent” means Johnson & Johnson, its directors, officers, employees, agents, representatives, predecessors, successors, and assigns; its joint ventures, subsidiaries, divisions, groups and affiliates controlled by Johnson & Johnson, and the respective directors, officers, employees, agents, representatives, successors, and assigns of each. After the Effective Date, the term “J&J” shall include Guidant.
  
- B. “Guidant” means Guidant Corporation, its directors, officers, employees, agents, representatives, predecessors, successors, and assigns; its joint ventures, subsidiaries, divisions, groups and affiliates controlled by Guidant Corporation, and the respective directors, officers,

Decision and Order

employees, agents, representatives, successors, and assigns of each.

- C. “Commission” means the Federal Trade Commission.
- D. “Abbott” means Abbott Laboratories, Inc., a corporation organized, existing, and doing business under and by virtue of the laws of the State of Illinois, having its principal place of business located at 100 Abbott Park Road, Abbott Park, IL 60064.
- E. “Abbott Agreement” means the “License Agreement” by and between J&J and Abbott dated August 12, 2005, and all amendments, exhibits, attachments, agreements, and schedules thereto, related to the Drug Eluting Stent Patents to be licensed, that have been approved by the Commission to accomplish the requirements of this Order. The Abbott Agreement is attached to this Order as non-public Appendix I.
- F. “Abbott Combination Stent” means the first Stent product designated and commercialized by Abbott (or Abbott’s assignee of the entire Abbott Agreement) for the treatment of coronary artery disease that includes ABT-578 in combination with one of the agents identified in non-public Appendix II.
- G. “Abbott Drug Eluting Stent” means a Stent that elutes or otherwise delivers ABT-578 alone for the treatment of coronary artery disease.
- H. “ABT-578” means the agent disclosed in U.S. Patent Nos. 6015815, 6329386, 5527907, 5583139 and 5672605, which is the active drug agent

## Decision and Order

Abbott is currently using in its clinical trial of the ZoMaxx™ stent.

- I. “Acquisition” means the acquisition contemplated by the “Agreement and Plan of Merger” dated as of December 15, 2004, by and among J&J and Guidant (“Acquisition Agreement”), whereby J&J agreed to acquire Guidant.
- J. “Actual Cost” means the cost of direct labor and direct material used to provide the relevant assistance or service, plus an allocation of overhead that is in the same proportion that was used by the Respondent on July 2, 2005.
- K. “Additional Drug Eluting Stent Patents” means all U.S. and foreign Patents of Respondent listed in Appendix III.
- L. “Agency(ies)” means any governmental regulatory authority or authorities in the world responsible for granting approval(s), clearance(s), qualification(s), license(s) or permit(s) for any aspect of the research, Development, manufacture, marketing, distribution or sale of Drug Eluting Stents or EVH Products.
- M. “Anastomotic Assist Distribution Agreement” means the September 12, 2003, Distribution Agreement by and between Ethicon, Inc., a subsidiary of Respondent, and Novare, as amended by letter dated November 30, 2004.
- N. “Business Day(s)” means any day other than a Saturday, Sunday, or federal holiday.
- O. “Closing Date” means the date on which Respondent (or a Divestiture Trustee) and a

Decision and Order

Commission-approved Acquirer consummate a transaction to grant, license, deliver or otherwise convey relevant assets pursuant to this Order.

- P. “Commission-approved Acquirer” means the following:
1. as to the Drug Eluting Stent Patents, Abbott, if Abbott has not been rejected by the Commission pursuant to Paragraph II.A. of this Order;
  2. as to the EVH Business, Datascope, if Datascope has not been rejected by the Commission pursuant to Paragraph III.A. of this Order; or
  3. an entity that receives the prior approval of the Commission to receive particular assets that the Respondent is required to grant, license, deliver or otherwise convey pursuant to this Order.
- Q. “Confidential Business Information” means all information owned by, or in the possession or control of, Respondent that is not in the public domain and that is related to the research, Development, manufacture, marketing, importation, exportation, supply, sales, sales support, or use of a Product; *provided, however*, that “Confidential Business Information” shall not include (1) information that subsequently falls within the public domain through no violation of this Order or of any confidentiality agreement with respect to such information by Respondent or (2) information that Guidant can demonstrate it obtained without the assistance of Respondent prior to the Acquisition.
- R. “Datascope” means Datascope Corp., a corporation organized, existing, and doing business under and

## Decision and Order

by virtue of the laws of the State of Delaware, having its principal place of business located at 14 Philips Parkway, Montvale, NJ 08933.

- S. “Datascope Agreement” means the “Purchase Agreement” by and between Ethicon, Inc., a subsidiary of J&J, and Datascope dated as of September 27, 2005, and all amendments, exhibits, attachments, agreements, and schedules thereto, related to the EVH Business, that have been approved by the Commission to accomplish the requirements of this Order. The Datascope Agreement is attached to this Order as non-public Appendix IV.
- T. “Designee” means any entity that will manufacture a J&J EVH Product or a Licensed EVH Product for a Commission-approved Acquirer.
- U. “Development” means all preclinical and clinical drug and/or device development activities, including test method development and stability testing, toxicology, bioequivalency, formulation, process development, manufacturing scale-up, development-stage manufacturing, quality assurance/quality control development, statistical analysis and report writing, conducting clinical trials for the purpose of obtaining any and all approvals, licenses, registrations or authorizations from any Agency necessary for the manufacture, use, storage, import, export, transport, promotion, marketing and sale of a Product (including any governmental price or reimbursement approvals), Product approval and registration, and regulatory affairs related to the foregoing. “Develop” means to engage in Development.



Decision and Order

- V. “Divestiture Trustee” means a trustee appointed by the Commission pursuant to the relevant provisions of this Order.
- W. “Drug Eluting Stent” means a Stent that elutes or otherwise delivers one or more drugs or pharmaceutical compositions for the treatment of coronary artery disease.
- X. “Drug Eluting Stent Patents” means all U.S. and foreign Patents of Respondent, other than Excluded Drug Eluting Stent Patents, that claim (1) drugs, pharmaceutical compositions, coatings or polymers used on Stents or otherwise in combination with Stents; (2) methods of manufacture, use or sale of Stents including, bearing, or otherwise in combination with such drugs, pharmaceutical compositions, coatings and/or polymers; (3) products or systems for the intravascular delivery of such Stents; and/or (4) intraluminal catheters, Stent delivery systems and embolic protection delivery systems (but not the design of Stents or embolic protection devices per se) having a guidewire lumen with a proximal guidewire port located substantially remote from the proximal end of the catheter shaft.
- Y. “Effective Date” means the earlier of the following dates:
1. the date the Respondent closes on the Acquisition Agreement; or
  2. the date the merger contemplated by the Acquisition Agreement becomes effective by filing articles of merger with the Secretary of State of the State of Indiana.

## Decision and Order

- Z. “EVH Business” means all of Respondent’s assets, tangible and intangible, businesses and goodwill, related to the research, Development, manufacture, distribution, marketing or sale of J&J EVH Products, including, without limitation, the following:
1. all EVH Intellectual Property;
  2. all EVH Manufacturing Technology;
  3. all EVH Scientific and Regulatory Material;
  4. all books, records and files related to the foregoing or to J&J EVH Products;
  5. all EVH Manufacturing Equipment;
  6. to the extent related to the J&J EVH Products, all of Respondent’s rights, titles and interests in and to the contracts entered into in the ordinary course of business with customers, suppliers, sales representatives, distributors, agents, personal property lessors, personal property lessees, licensors, licensees, consignors, and consignees, in each case that are Third Parties, including, without limitation, all of Respondent contracts with any Third Party to the extent related to the supply of components used in the manufacture of J&J EVH Products;
  7. all inventory, including raw materials, packaging materials, work-in-process and finished goods, in each case to the extent consisting of, or intended for use in the manufacture of, J&J EVH Products;
  8. all commitments and orders for the purchase of goods that have not been shipped, to the extent such goods are, or

Decision and Order

are intended for use in the manufacture of, J&J EVH Products;

9. all rights under warranties and guarantees, express or implied, with respect to J&J EVH Products; and
10. all items of prepaid expenses, to the extent related to J&J EVH Products;

*provided, however,* that “EVH Business” does not include any portion of any of the foregoing assets, businesses and goodwill that does not relate to J&J EVH Products;

*provided further, however,* that “EVH Business” does not include any of the following: (a) (i) the name “Johnson & Johnson”, “Ethicon”, “CardioVations”, or the names of any other divisions, businesses, corporations or companies owned by Respondent or (ii) any trademarks, trade names or logos used on other of Respondent’s Products; (b) any interest in real property; (c) any plant or other facilities; (d) any personal property; (e) any equipment or contracts for the sterilization, labeling or packaging of any Products; or (f) any assets, tangible and intangible, businesses or goodwill that were owned by Guidant immediately prior to the Effective Date;

*provided further, however,* that with respect to documents or other materials included in the EVH Business that contain information (a) that relates both to the J&J EVH Products and to other products or businesses of Respondent or (b) for which Respondent has a legal obligation to retain the original copies, Respondent shall be required to provide only copies or, at its option, relevant excerpts of such documents and materials, but Respondent shall provide the Commission-approved Acquirer access to the originals of such documents as necessary, it being a purpose of this proviso to ensure that Respondent not be required to divest itself completely of

## Decision and Order

records or information that relates to products or businesses other than the J&J EVH Products;

*provided further, however*, that with respect to any contract or agreement included in the EVH Business that relates both to the J&J EVH Products and to any other product, Respondent may, concurrently with assigning such contract or agreement to the extent it relates to the J&J EVH Products, retain its rights under such contract or agreement for purposes of such other product(s).

- AA. "EVH Employee Information" means the following, as and to the extent permitted by Law:
1. with respect to each EVH Employee, the following information:
    - a. the date of hire and effective service date;
    - b. job title or position held;
    - c. a specific description of the employee's responsibilities related to the EVH Business;
    - d. for sales representatives, the sales ranking as of September 30, 2005, and for other employees, the most recent performance rating;
    - e. the base salary range of all EVH Employees having the same title or position;
    - f. the aggregate annual compensation for the Respondent's last fiscal year and as targeted for the current fiscal year;
    - g. employment status (*i.e.*, active or on leave or disability; full-time or part-time); and

Decision and Order

- h. any other material terms and conditions of employment in regard to such employee that are not otherwise generally available to similarly situated employees.
  - 2. at the Commission-approved Acquirer's option, copies of all employee benefit plans and summary plan descriptions (if any) applicable to the EVH Employees.
- BB. "EVH Employees" means all those employees listed in non-public Appendix V to this Decision and Order.
- CC. "EVH Intellectual Property" means all of the following that are owned by Respondent, to the extent related to the J&J EVH Products:
- 1. Patents;
  - 2. trademarks, trade names, trade dress, trade secrets, know-how, techniques, data, inventions, practices, methods and other confidential or proprietary technical, business, research, Development and other information;
  - 3. rights to obtain and file for Patents and registrations thereof; and
  - 4. rights under any license to any of the foregoing;
- provided, however*, "EVH Intellectual Property" does not include (i) the name "Johnson & Johnson", "Ethicon", "CardioVations", or the names of any other corporations, divisions or companies owned by Respondent or (ii) any trademarks, trade names or logos used on other of Respondent's Products.
- DD. "EVH Kits" means procedural kits for endoscopic vessel harvesting, including those currently marketed by

## Decision and Order

Respondent under the trademarks CLEARGLIDE® or WATCHBAND INCISION™.

- EE. “EVH Manufacturing Equipment” means all equipment of Respondent utilized in the manufacture of J&J EVH Products, but does not include (i) any sterilization, labeling or packaging equipment or (ii) any assets utilized by Guidant in the manufacture of EVH Products immediately prior to the Effective Date.
- FF. “EVH Manufacturing Technology” means all technology, trade secrets, know-how, and proprietary information (whether patented, patentable or otherwise) related to the manufacture (including that relating to all equipment used to manufacture a J&J EVH Product in final finished form), validation, packaging, release testing, stability and shelf life of J&J EVH Products, including all product specifications, processes, product designs, plans, trade secrets, ideas, concepts, manufacturing, engineering and other manuals and drawings, standard operating procedures, flow diagrams, chemical, pharmacological, toxicological, pharmaceutical, physical and analytical, safety, efficacy, bioequivalency, quality assurance, quality control and clinical data, research records, compositions, annual product reviews, process validation reports, analytical method validation reports, specifications for stability trending and process controls, testing and reference standards for impurities in and degradation of products, technical data packages, chemical and physical characterizations, dissolution test methods and results, formulations for administration, clinical trial reports, regulatory communications and labeling of, for or with respect to the J&J EVH Products, and all other information related to the manufacturing process, supplier lists, and supplier contracts for the J&J EVH Products.

Decision and Order

- GG. “EVH Products” means endoscopic vessel harvesting Products, whether or not included in EVH Kits, but shall not mean the EVH Kits themselves.
- HH. “EVH Scientific and Regulatory Material” means all technological, scientific, chemical, biological, pharmacological, toxicological, regulatory and clinical trial materials and information related to J&J EVH Products, and all of Respondent’s rights to use such materials, in any and all jurisdictions (to the extent Respondent can legally transfer such rights).
- II. “Excluded Drug Eluting Stent Patents” means (1) Patents owned or controlled by a Third Party that does not qualify as an affiliate of Respondent as of the Closing Date, except to the extent such Third Party Patent is licensed to Respondent at the Closing Date with the right to sublicense (a) without consent or (b) by mere notice to such Third Party, and (i) without any additional payment or other consideration (other than payments or other consideration, including royalty payments, which the Commission-approved Acquirer agrees to pay or provide) and (ii) without any other undertaking by Respondent that is not a de minimis undertaking; (2) Patents or Patent applications that pertain to the manufacture, use or sale of Rapamycin or any analog of Rapamycin, except to the extent, if any, such rights pertain to ABT-578; and (3) any Patents or Patent claims solely claiming balloon material for an intraluminal catheter or Stent delivery system.
- JJ. “Excluded EVH Products” means: (1) any and all devices marketed by Respondent as (a) the HARMONIC SCALPEL® or (b) the ALLPORT® Clip Applier; (2) any and all sutures, whether or not part of any ENDOLOOP® or other vessel ligator (including, but not limited to the sutures currently marketed by Respondent as the Ethibond Excel® sutures); (3) the metal “pigtail” dissector manufactured by Storz, purchased by Respondent from

## Decision and Order

Storz, and sold by Respondent under the Storz name; (4) any endoscopes manufactured by Third Parties (including but not limited to Storz and Olympus) and previously marketed, sold or distributed by Respondent; (5) the DERMABOND® Topical Skin Adhesive; and (6) any EVH Products researched, Developed, manufactured or sold by Guidant immediately prior to the Effective Date.

- KK. “Field” means the prevention, treatment, diagnosis, or control of a particular medical condition.
- LL. “Governmental Entity” means any Federal, state, local or non-U.S. government or any court, legislature, governmental agency or governmental commission or any judicial or regulatory authority of any government.
- MM. “Interim Monitor” means a monitor appointed by the Commission pursuant to Paragraph V of this Order.
- NN. “J&J Anastomotic Assist Products” mean those anastomotic assist Products distributed and sold by J&J immediately prior to the Effective Date.
- OO. “J&J EVH Products” mean those EVH Products, other than Excluded EVH Products or Licensed EVH Products, researched, Developed, manufactured and sold by J&J immediately prior to the Effective Date, and including all such EVH Products that are introduced by Respondent on or before the Closing Date.
- PP. “Law” means all laws, statutes, rules, regulations, ordinances and other pronouncements having the effect of law by any Governmental Entity.
- QQ. “Licensed EVH Products” means the following devices, the product code numbers for which are listed in non-public Appendix VI.: (1) the device currently marketed in EVH Kits by Respondent as the ENDOPATH® Vessel



Decision and Order

Scissors; (2) the atraumatic blunt dissector (sometimes referred to as the “cherry dissector” or “Kittner dissector”) that is currently marketed in EVH Kits by Respondent; and (3) the ENDOLOOP® One Tie Vessel Ligator that is currently marketed by Respondent in the Field of endoscopic vessel harvesting (but excluding any suture that is a component of any such vessel ligator).

- RR. “Novare” means Novare Surgical Systems, Inc., a corporation organized, existing, and doing business under and by virtue of the laws of the State of Delaware, having its principal place of business located at 10231 Bubb Road, Cupertino, California 95014.
- SS. “Patents” means all patents, patent applications and statutory invention registrations in which Respondent holds rights, either through assignment or license, as of the Effective Date (except where this Order specifies a different time), and includes all reissues, divisions, continuations, continuations-in-part, to the extent the claims of such continuations-in-part are fully supported pursuant to 35 U.S.C. § 112 by such patents and/or applications owned or licensed by Respondent as of the Effective Date, substitutions, reexaminations, restorations, and/or patent term extensions thereof, all inventions disclosed therein, all rights therein provided by international treaties and conventions, and all rights to obtain and file for patents and registrations thereto, related to a Product.
- TT. “PC Coating” shall mean polymerized phosphorylcholine coating.
- UU. “Product” means any medical device or pharmaceutical, biological, or genetic composition containing any formulation or dosage of a compound referenced as its pharmaceutically, biologically or genetically active ingredient.

## Decision and Order

VV. “Remedial Agreement” means the following:

1. the Abbott Agreement, if such agreement has not been rejected by the Commission pursuant to Paragraph II.A. of this Order;
2. the Datascope Agreement, if such agreement has not been rejected by the Commission pursuant to Paragraph III.A. of this Order; and
3. any agreement between Respondent and a Commission-approved Acquirer (or between a Divestiture Trustee and a Commission-approved Acquirer) that has been approved by the Commission to accomplish the requirements of this Order, and all amendments, exhibits, attachments, agreements, and schedules thereto, related to the relevant assets to be granted, licensed, delivered or otherwise conveyed, that have been approved by the Commission to accomplish the requirements of this Order.

WW. “Stent” means stents that provide intraluminal support through the use of metal members to form a stent scaffold, which is principally responsible for intraluminal support in the treatment of coronary artery disease. “Stent” excludes stents that are bioabsorbable or comprise scaffolds principally composed of non-metallic materials, such as ceramic.

XX. “Termination Agreement” means the “Termination and Release Agreement” by and between Ethicon, Inc., a subsidiary of J&J, and Novare dated September 28, 2005, and all amendments, exhibits, attachments, agreements, and schedules thereto, related to the J&J Anastomotic Assist Products, that have been approved by the Commission to accomplish the requirements of this Order. The Termination Agreement is attached to this Order as non-public Appendix VII.

Decision and Order

YY. “Third Party(ies)” means any private entity other than the following: (1) the Respondent, or (2) the Commission-approved Acquirer.

**II.**

**IT IS FURTHER ORDERED** that:

A. Not later than ten (10) days after the Effective Date, Respondent shall grant an irrevocable, perpetual, fully paid-up and royalty-free non-exclusive license worldwide to the Drug Eluting Stent Patents to Abbott for the research, Development, manufacture, use, import, distribution, marketing or sale of Abbott Drug Eluting Stents and Abbott Combination Stents pursuant to and in accordance with the Abbott Agreement (which agreement shall not vary or contradict, or be construed to vary or contradict, the terms of this Order, it being understood that nothing in this Order shall be construed to reduce any rights or benefits of Abbott or to reduce any obligations of Respondent under such agreement);

*provided, however,* that, if Respondent has licensed the Drug Eluting Stent Patents to Abbott prior to the date this Order becomes final, and if, at the time the Commission determines to make this Order final, the Commission notifies Respondent that Abbott is not an acceptable licensee of the Drug Eluting Stent Patents, then Respondent shall (1) grant an irrevocable, perpetual, fully paid-up and royalty-free non-exclusive license worldwide to the Drug Eluting Stent Patents and the Additional Drug Eluting Stent Patents (to the extent the Commission determines that the Commission-approved Acquirer requires access to the Drug Eluting Stent Patents and the Additional Drug Eluting Stent Patents in order to manufacture or sell Drug Eluting Stents without fear of infringement of any Patents of Respondent) within six (6) months from the date the Order becomes final, absolutely and in good faith, at no minimum price, to a Commission-approved Acquirer and only in a

## Decision and Order

manner that receives the prior approval of the Commission; and (2) at Respondent's option, immediately rescind the transaction with Abbott;

*provided further, however,* that if Respondent has licensed the Drug Eluting Stent Patents to Abbott prior to the date this Order becomes final, and if, at the time the Commission determines to make this Order final, the Commission notifies the Respondent that the manner in which the license was accomplished is not acceptable, the Commission may direct the Respondent, or appoint a Divestiture Trustee, pursuant to Paragraph VI of this Order, to effect such modifications to the manner of licensing the Drug Eluting Stent Patents to Abbott for the research, Development, manufacture, use, import, distribution, marketing or sale of Abbott Drug Eluting Stents and Abbott Combination Stents for the treatment of coronary artery disease (including, but not limited to, licensing the Additional Drug Eluting Stent Patents, and entering into additional agreements or arrangements) as may be necessary to satisfy the requirements of this Order;

*provided further, however,* that Respondent may include as part of a Remedial Agreement a requirement that the Commission-approved Acquirer make: (1) a one-time fixed payment upon FDA approval or first sale in the United States, whichever comes earlier, of a Drug Eluting Stent which practices under any Drug Eluting Stent Patents or Additional Drug Eluting Stent Patents; and (2) a one-time payment in the event that the Commission-approved Acquirer transfers the license;

*provided further, however,* that Respondent may include as part of a Remedial Agreement a requirement that the Commission-approved Acquirer pay royalties to the same extent and in the same amount that Respondent pays royalties to any Third Party. Such royalties shall be paid by the Commission-approved Acquirer directly to the Third Party and Respondent shall obtain no information about such payments except for an acknowledgment that the full payment has been made, and, if

Decision and Order

not, whether the underpayment was by more than five (5) percent;

*provided further, however*, that Respondent shall not be required to license to Abbott: (1) any Patents licensed under the June 2001 License Agreement between Abbott and Cordis Corporation; and (2) any portion of the Drug Eluting Stent Patents, or rights under those patents, if Abbott does not require such patent rights in order to sell Abbott Drug Eluting Stents or Abbott Combination Stents without fear of infringement of any Patents of Respondent.

- B. Any Remedial Agreement that has been approved by the Commission between Respondent (or a Divestiture Trustee) and a Commission-approved Acquirer of the Drug Eluting Stent Patents (and, if relevant, the Additional Drug Eluting Stent Patents) shall be deemed incorporated into this Order, and any failure by Respondent to comply with any term of such Remedial Agreement related to the Drug Eluting Stent Patents (and, if relevant, the Additional Drug Eluting Stent Patents) shall constitute a failure to comply with this Order.
- C. In the event that Respondent licenses the Drug Eluting Stent Patents to Abbott, Respondent shall include in the Remedial Agreement related to the Drug Eluting Stent Patents, and Respondent shall observe, a covenant that Respondent shall not join, or file, prosecute or maintain any suit, in Law or equity, against Abbott (or Abbott's assignee of the entire Abbott Agreement) for the research, Development, manufacture, use, import, distribution, marketing or sale of the Drug Eluting Stent Products currently being used in Abbott's ZoMaxx™ and ZoMaxx™ II clinical trials, and variations of concentrations of ABT-578, stent sizes, PC Coating, catheters and/or delivery systems (excluding their balloon materials) as Abbott (or such assignee) may choose to employ under any Patents licensed to Abbott under the Abbott Agreement.

## Decision and Order

- D. In the event that Respondent licenses the Drug Eluting Stent Patents and the Additional Drug Eluting Stent Patents to a Commission-approved Acquirer other than Abbott pursuant to Section II.A of this Decision and Order, Respondent shall include in any Remedial Agreement related to the Drug Eluting Stent Patents and the Additional Drug Eluting Stent Patents, and Respondent shall observe, a covenant that Respondent shall not join, or file, prosecute or maintain any suit, in Law or equity, against the Commission-approved Acquirer (or the Commission-approved Acquirer's assignee of the entire Remedial Agreement) for the research, Development, manufacture, use, import, distribution, marketing or sale of Drug Eluting Stents identified in the Remedial Agreement under Drug Eluting Stent Patents or Additional Drug Eluting Stent Patents included in the Remedial Agreement with the Commission-approved Acquirer.
- E. Prior to the Closing Date, Respondent shall secure all consents and waivers from all Third Parties that are necessary for the licensing of the Drug Eluting Stent Patents (and, if relevant, the Additional Drug Eluting Stent Patents) to the Commission-approved Acquirer, or for the continued research, Development, manufacture, use, import, distribution, marketing or sale of Drug Eluting Stents by the Commission-approved Acquirer.
- F. If the Remedial Agreement does not license the Commission-approved Acquirer rights in and to any portion of the Additional Drug Eluting Stent Patents, then Respondent shall not seek to enjoin any transferee or acquirer of the Commission-approved Acquirer's rights to the Remedial Agreement in any action for infringement of any patent included within the Additional Drug Eluting Stent Patents; *provided, however*, that Respondent shall retain all its rights to seek past and future damages and other remedies provided for in the Patent Act (U.S.C. title 35).

Decision and Order

- G. The purpose of the grant, license, delivery and conveyance of the Drug Eluting Stent Patents (and, if relevant, the Additional Drug Eluting Stent Patents) to a Commission-approved Acquirer is to create an independent, viable and effective competitor in the Drug Eluting Stent market, and to remedy the lessening of competition resulting from the Acquisition as alleged in the Commission's Complaint.

**III.**

**IT IS FURTHER ORDERED** that:

- A. Not later than fifteen (15) Business Days after the Effective Date, Respondent shall divest the EVH Business to Datascope pursuant to and in accordance with the Datascope Agreement (which agreement shall not vary or contradict, or be construed to vary or contradict, the terms of this Order, it being understood that nothing in this Order shall be construed to reduce any rights or benefits of Datascope or to reduce any obligations of Respondent under such agreement);

*provided, however,* that, if Respondent has divested the EVH Business to Datascope prior to the date this Order becomes final, and if, at the time the Commission determines to make this Order final, the Commission notifies Respondent that Datascope is not an acceptable acquirer of the EVH Business, then Respondent shall immediately rescind the transaction with Datascope and shall divest the EVH Business within six (6) months from the date the Order becomes final, absolutely and in good faith, at no minimum price, to a Commission-approved Acquirer and only in a manner that receives the prior approval of the Commission;

*provided further, however,* that if the Respondent has divested the EVH Business to Datascope prior to the date this Order becomes final, and if, at the time the Commission determines to make this Order final, the Commission notifies the

## Decision and Order

Respondent that the manner in which the divestiture was accomplished is not acceptable, the Commission may direct the Respondent, or appoint a Divestiture Trustee, pursuant to Paragraph VI of this Order, to effect such modifications to the manner of divesting the EVH Business to Datascope (including, but not limited to, entering into additional agreements or arrangements) as may be necessary to satisfy the requirements of this Order;

*provided further, however,* that Respondent shall not be required to divest to the Commission-approved Acquirer any portion of the EVH Business if the Commission-approved Acquirer (or the Designee of the Commission-approved Acquirer) does not require such portion of the EVH Business for the continued research, Development, manufacture, use, import, distribution, marketing or sale of the J&J EVH products.

- B. Any Remedial Agreement that has been approved by the Commission between Respondent (or a Divestiture Trustee) and a Commission-approved Acquirer of the EVH Business shall be deemed incorporated into this Order, and any failure by Respondent to comply with any term of such Remedial Agreement related to the EVH Business shall constitute a failure to comply with this Order.
- C. Until the Closing Date of the EVH Business, Respondent shall take such actions as are necessary to maintain the viability and marketability of the EVH Business and to prevent the destruction, removal, wasting, deterioration, or impairment of the EVH Business, except for ordinary wear and tear and the disposition of inventory and other assets in the ordinary course of business.
- D. At the option of the Commission-approved Acquirer (to be exercised no later than 30 days after the date the Commission-approved Acquirer signs a Remedial Agreement with Respondent to effect the acquisition of the



Decision and Order

EVH Business), Respondent shall include in any Remedial Agreement the following provisions, and Respondent shall commit to satisfy the following:

1. Respondent shall (a) grant an irrevocable, perpetual, fully paid-up and royalty free (except for pass-through royalties), non-exclusive license worldwide to Patents owned or exclusively licensed by Respondent and necessary to enable the Commission-approved Acquirer (or the Designee of the Commission-approved Acquirer) to research, Develop, manufacture, use, import, distribute, market and sell Licensed EVH Products in the Field of endoscopic vessel harvesting; and (b) in furtherance of the foregoing, provide the Commission-approved Acquirer with copies of the following documents, to the extent they are owned by, or in the possession, custody or control of, Respondent and related to the Licensed EVH Products: (i) design history files, technical files, drawings, product specifications, manufacturing process descriptions, validation documentation, packaging specifications, quality control standards and regulatory records, and (ii) specifications, drawings, manufacturing process descriptions and validation documentation for molds and other tooling used in manufacturing Licensed EVH Products; *provided, however*, that any portions of the documents described in this clause (b) that do not relate to the Licensed EVH Products or the J&J EVH Products may be excluded from such copies; *provided further, however*, that as regards to any documents described in this clause (b) that are not owned by Respondent and which Respondent is prohibited by contract or Law from providing to the Commission-approved Acquirer, Respondent shall not be required to provide such documents to the Commission-approved Acquirer if Respondent has made all reasonable efforts to obtain a waiver of such prohibition but has not been successful.

## Decision and Order

2. Respondent shall, for a period of up to one (1) year after the Closing Date at no more than Respondent's Actual Cost, provide transition services necessary for the continued research, Development, manufacture, use, import, distribution, marketing or sale of J&J EVH Products and Licensed EVH Products by the Commission-approved Acquirer.
3. Respondent shall enter into an agreement to supply J&J EVH Products, Licensed EVH Products, HARMONIC SCALPEL® devices and ALLPORT® Clip Appliers to the Commission-approved Acquirer at no more than Respondent's Actual Cost for a period not longer than two (2) years following the Closing Date; *provided, however,* that Respondent may, for the term of any such supply agreement, postpone the assignment of any contract that is needed by Respondent to meet its obligations under such supply agreement.
4. Respondent shall provide to the Commission-approved Acquirer all documents or materials in Respondent's possession, custody or control as of the Effective Date to the extent related to Third Party EVH Products or EVH Products sold by Guidant prior to the Effective Date; *provided, however,* that as regards to any documents or materials described in this Paragraph III.D.4. that are not owned by Respondent and which Respondent is prohibited by contract or Law from providing to the Commission-approved Acquirer, Respondent shall not be required to provide such documents or materials to the Commission-approved Acquirer if Respondent has made all reasonable efforts to obtain a waiver of such prohibition but has not been successful; *provided further, however,* that Respondent shall not be required to provide to the Commission-approved Acquirer any documents or materials described in this Paragraph III.D.4. that were owned by, or in the possession, custody or control of, Guidant immediately prior to the Effective Date.

Decision and Order

E. Respondent shall:

1. not later than fifteen (15) days after signing the Remedial Agreement, (a) provide to the Commission-approved Acquirer a list of all EVH Employees; (b) allow the Commission-approved Acquirer to interview any EVH Employees; and (c) in compliance with all Laws, allow the Commission-approved Acquirer to inspect the EVH Employee Information;
2. not later than fifteen (15) days after signing the Remedial Agreement, provide an opportunity for the Commission-approved Acquirer: (a) to meet personally, and outside the presence or hearing of any employee or agent of Respondent, with any one or more of the EVH Employees; and (b) to make offers of employment to any one or more of the EVH Employees; *provided, however*, that the Respondent may include in any Remedial Agreement related to the EVH Business a requirement that the Commission-approved Acquirer may not make offers of employment to more than three of the sales representatives listed on non-public Appendix V. for each of the Northeast and Southeast regions, or to more than one of the sales representatives listed on non-public Appendix V. for each of the Midwest and West regions; *provided further, however*, that the Commission-approved Acquirer shall be permitted to make an offer of employment to one additional sales representative within a region for each other sales representative within that region who has already declined an offer of employment;
3. not interfere, directly or indirectly, with the hiring or employing by the Commission-approved Acquirer of EVH Employees, and shall remove any impediments or incentives within the control of Respondent that may deter these employees from accepting employment with the Commission-approved Acquirer, including, but not limited to, any non-compete provisions of employment or

## Decision and Order

other contracts with Respondent that would affect the ability or incentive of those individuals to be employed by the Acquirer, and shall not make any counteroffer to an EVH Employee who receives a written offer of employment from the Commission-approved Acquirer; *provided, however*, that nothing in this Order shall be construed to require Respondent to terminate the employment of any employee or prevent Respondent from continuing the employment of any employee;

4. provide all EVH Employees with reasonable financial incentives to continue in their positions until the Closing Date. Such incentives shall include, but are not limited to, a continuation, until the Closing Date, of all employee benefits, including regularly scheduled raises, bonuses and vesting of pension benefits (as permitted by law and for those EVH Employees covered by a pension plan), offered by Respondent;
5. provide to each EVH Employee that is offered employment by the Commission-approved Acquirer financial incentives to accept employment with the Commission-approved Acquirer on or about the Closing Date, or reimburse the Commission-approved Acquirer for its provision of such incentive. Such incentives shall include a bonus for each such employee, equal to 15% of the sum of the employee's annual base salary and total commissions (if any) for the twelve (12) months prior to the date of the Remedial Agreement, who accepts an offer of employment from the Commission-approved Acquirer within one month of the Closing Date and remains employed by the Commission-approved Acquirer for a period of six (6) months, payable by Respondent in equal installments at three (3) months and six (6) months after the commencement of the employee's employment by the Commission-approved Acquirer; and

Decision and Order

6. not, for a period of one (1) year following the Closing Date, directly or indirectly, solicit or otherwise attempt to induce any of the EVH Employees to terminate their employment with the Commission-approved Acquirer; *provided however*, that Respondent may:
  - a. advertise for employees in newspapers, trade publications or other media, or engage recruiters to conduct general employee search activities, in either case not targeted specifically at the EVH Employees, or
  - b. hire EVH Employees who apply for employment with Respondent, as long as such employees were not solicited by Respondent in violation of this Paragraph III.E.6;

*provided further however*, that this Paragraph III.E.6 shall not prohibit Respondent from making offers of employment to or employing any EVH Employee after the thirtieth day following the date of the Remedial Agreement, or where the Commission-approved Acquirer has notified Respondent in writing that the Commission-approved Acquirer does not intend to make an offer of employment to that employee, or where such an offer has been made and the employee has declined the offer.

- F. Prior to the Closing Date, Respondent shall secure all consents and waivers from all Third Parties that are necessary for the divestiture of the EVH Business, and for the continued research, Development, manufacture, use, import, distribution, marketing or sale of J&J EVH Products by the Commission-approved Acquirer (or the Designee of the Commission-approved Acquirer); *provided, however*, that Respondent shall not be required to obtain consents from customers necessary to divest contracts that, in the aggregate, represent less than 5% of Respondent's

## Decision and Order

worldwide EVH Kit sales for the period January 1, 2005 to June 30, 2005.

- G. In the event that Respondent is unable to satisfy all conditions necessary to divest any intangible asset that is a permit, license or right granted by any domestic or foreign governmental entity, Respondent shall provide such assistance as the Commission-approved Acquirer may reasonably request in the Commission-approved Acquirer's efforts to obtain a comparable permit, license or right.
- H. Other than as necessary to comply with the requirements of this Order, Respondent shall not use, directly or indirectly, any Confidential Business Information related to the research, Development, manufacture, use, import, distribution, marketing or sale of the J&J EVH Products, and shall not disclose or convey such Confidential Business Information, directly or indirectly, to any person except in connection with the divestiture of the EVH Business, and to the Divestiture Trustee, if any; *provided however*, that Respondent may continue using, outside the Field of endoscopic vessel harvesting, such Confidential Business Information as it currently uses in connection with any of the Licensed EVH Products or Excluded EVH Products.
- I. Respondent shall, to the extent permissible under applicable laws and as a condition of continued employment post-divestiture, require that each employee of Respondent with access to Confidential Business Information related to the EVH Business sign a confidentiality agreement pursuant to which such employee shall be required to maintain all such Confidential Business Information strictly confidential, including the nondisclosure of such information to all other employees, executives or other personnel of Respondent (other than as necessary to comply with the requirements of this Order); *provided however*, that:

Decision and Order

1. Respondent may use such information only to the extent necessary to defend or prosecute claims relating to assets or liabilities that are retained by Respondent after divestiture;
  2. Respondent may also continue to use, and to share with employees of Respondent having a need to know same, such Confidential Business Information as they currently use in connection with any of the Licensed EVH Products or Excluded EVH Products outside the Field of endoscopic vessel harvesting; and
  3. This Paragraph III.I. shall not apply to any Confidential Business Information related to the EVH Business that Respondent can demonstrate to the Commission that Guidant had prior to the Effective Date.
- J. Counsel for Respondent (including in-house counsel under appropriate confidentiality arrangements) may retain unredacted copies of all documents or other materials provided to the Commission-approved Acquirer and may have access to original documents provided to the Commission-approved Acquirer. Respondent's use or disclosure of any documents or materials that are retained or accessed by Respondent solely by virtue of this Paragraph III.J (and not, for example, pursuant to the third proviso of Paragraph I.Z) shall be limited to the following:
1. to comply with any Remedial Agreement, this Order, any Law (including, without limitation, any requirement to obtain regulatory licenses or approvals), any data retention requirement of any applicable Governmental Entity, or any taxation requirements;
  2. to defend against, respond to, or otherwise participate in any litigation, investigation, audit, process, subpoena or other proceeding relating to the divestiture or any other aspect of the EVH Business;

## Decision and Order

*provided, however,* that Respondent shall: (1) require those (other than Governmental Entities) who view any documents or materials that are retained or accessed by Respondent solely by virtue of this Paragraph III.J. to enter into reasonable and customary confidentiality agreements with the Commission-approved Acquirer (but shall not be deemed to have violated this requirement if the Commission-approved Acquirer withholds such agreement unreasonably); (2) inform any Governmental Entities who seek to view any documents or materials that are retained or accessed by Respondent solely by virtue of this Paragraph III.J. of Respondent's obligation to keep such information confidential, and give the Commission-approved Acquirer as much prior notice of complying with such request from the Governmental Entity as is reasonable in the circumstances, subject to any requirements of Law; and (3) use all reasonable efforts to obtain a protective order to protect the confidentiality of such information during any adjudication.

- K. The purpose of the divestiture of the EVH Business is to ensure the continuing, viable, and competitive operation of the EVH Business in the same business and in the same manner in which the EVH Business was engaged at the time of the announcement of the proposed Acquisition and to remedy the lessening of competition alleged in the Commission's complaint.

**IV.**

**IT IS FURTHER ORDERED** that:

- A. Not later than ten (10) days after the Effective Date, Respondent shall terminate the Anastomotic Assist Distribution Agreement with Novare pursuant to and in accordance with the Termination Agreement (which agreement shall not vary or contradict, or be construed to vary or contradict, the terms of this Order, it being understood that nothing in this Order shall be construed to



Decision and Order

reduce any rights or benefits of Novare or to reduce any obligations of Respondent under such agreement).

- B. The Termination Agreement shall be deemed incorporated into this Order, and any failure by Respondent to comply with any term of such Termination Agreement shall constitute a failure to comply with this Order.
- C. Other than as necessary to comply with the requirements of this Order, for such period of time as provided in the Anastomotic Assist Distribution Agreement, Respondent shall not use, directly or indirectly, any Confidential Business Information related to the research, Development, manufacture, use, import, distribution, marketing or sale of the J&J Anastomotic Assist Products, and shall not disclose or convey such Confidential Business Information, directly or indirectly, to any person except in connection with the termination of the Anastomotic Assist Distribution Agreement, and to the Divestiture Trustee, if any; *provided however*, that any Confidential Business Information related to J&J Anastomotic Assist Products that are the subject of a recall or other corrective action may be disclosed to those persons having a need to know such information for the purpose of carrying out such corrective action; *provided further, however*, that Respondent may continue using, in connection with products other than anastomotic assist Products, such Confidential Business Information related to J&J Anastomotic Assist Products as it (a) developed or obtained from sources other than Novare, and (b) currently uses in connection with products other than anastomotic assist Products.
- D. The purpose of the termination of the Anastomotic Assist Distribution Agreement is to ensure the continuing, viable, and competitive marketing, distribution and sale of the J&J Anastomotic Assist Products to the same extent in which the J&J Anastomotic Assist Products were marketed, distributed and sold at the time of the

## Decision and Order

announcement of the proposed Acquisition and to remedy the lessening of competition alleged in the Commission's complaint.

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

- A. At any time after Respondent signs the Consent Agreement in this matter, the Commission may appoint a monitor ("Interim Monitor") to assure that Respondent expeditiously complies with all of its obligations and perform all of its responsibilities as required by Paragraph III of this Order and the Remedial Agreement related to the divestiture of the EVH Business.
- B. The Commission shall select the Interim Monitor, subject to the consent of Respondent, which consent shall not be unreasonably withheld. If Respondent has not opposed, in writing, including the reasons for opposing, the selection of a proposed Interim Monitor within ten (10) days after notice by the staff of the Commission to Respondent of the identity of any proposed Interim Monitor, Respondent shall be deemed to have consented to the selection of the proposed Interim Monitor.
- C. Not later than ten (10) days after the appointment of the Interim Monitor, Respondent shall execute an agreement that, subject to the prior approval of the Commission, confers on the Interim Monitor all the rights and powers necessary to permit the Interim Monitor to monitor Respondent's compliance with the relevant requirements of this Order in a manner consistent with the purposes of this Order.
- D. If an Interim Monitor is appointed, Respondent shall consent to the following terms and conditions regarding

Decision and Order

the powers, duties, authorities, and responsibilities of the Interim Monitor:

1. The Interim Monitor shall have the power and authority to monitor Respondent's compliance with the divestiture and asset maintenance obligations and related requirements of this Order, and shall exercise such power and authority and carry out the duties and responsibilities of the Interim Monitor in a manner consistent with the purposes of this Order and in consultation with the Commission.
2. The Interim Monitor shall act in a fiduciary capacity for the benefit of the Commission.
3. The Interim Monitor shall serve until the later of:
  - a. the completion by Respondent of the divestiture of all relevant assets required to be granted, licensed, delivered, or otherwise conveyed pursuant to this Order in a manner that fully satisfies the requirements of this Order and notification by the Commission-approved Acquirer to the Interim Monitor that it (or its Designee(s)) is fully capable of producing the J&J EVH Products acquired pursuant to a Remedial Agreement independently of Respondent; or
  - b. the completion by Respondent of the last obligation under this Order pertaining to the Interim Monitor's service;

*provided, however,* that the Commission may extend or modify this period as may be necessary or appropriate to accomplish the purposes of this Order.

4. Subject to any demonstrated legally recognized privilege, the Interim Monitor shall have full and complete access to

## Decision and Order

Respondent's personnel, books, documents, records kept in the normal course of business, facilities and technical information, and such other relevant information as the Interim Monitor may reasonably request, related to Respondent's compliance with its obligations under this Order, including, but not limited to, its obligations related to the relevant assets. Respondent shall cooperate with any reasonable request of the Interim Monitor and shall take no action to interfere with or impede the Interim Monitor's ability to monitor Respondent's compliance with this Order.

5. The Interim Monitor shall serve, without bond or other security, at the expense of Respondent on such reasonable and customary terms and conditions as the Commission may set. The Interim Monitor shall have authority to employ, at the expense of the Respondent, such consultants, accountants, attorneys and other representatives and assistants as are reasonably necessary to carry out the Interim Monitor's duties and responsibilities.
6. Respondent shall indemnify the Interim Monitor and hold the Interim Monitor harmless against any losses, claims, damages, liabilities, or expenses arising out of, or in connection with, the performance of the Interim Monitor's duties, including all reasonable fees of counsel and other reasonable expenses incurred in connection with the preparations for, or defense of, any claim, whether or not resulting in any liability, except to the extent that such losses, claims, damages, liabilities, or expenses result from misfeasance, gross negligence, willful or wanton acts, or bad faith by the Interim Monitor.
7. Respondent shall report to the Interim Monitor in accordance with the requirements of this Order and/or as otherwise provided in any agreement approved by the

Decision and Order

Commission. The Interim Monitor shall evaluate the reports submitted to the Interim Monitor by Respondent, and any reports submitted by the Commission-approved Acquirer with respect to the performance of Respondent's obligations under this Order or the Remedial Agreement. Within thirty (30) days from the date the Interim Monitor receives these reports, the Interim Monitor shall report in writing to the Commission concerning performance by Respondent of its obligations under this Order.

8. Respondent may require the Interim Monitor and each of the Interim Monitor's consultants, accountants, attorneys and other representatives and assistants to sign a customary confidentiality agreement; *provided, however*, that such agreement shall not restrict the Interim Monitor from providing any information to the Commission.
- E. The Commission may, among other things, require the Interim Monitor and each of the Interim Monitor's consultants, accountants, attorneys and other representatives and assistants to sign an appropriate confidentiality agreement related to Commission materials and information received in connection with the performance of the Interim Monitor's duties.
- F. If the Commission determines that the Interim Monitor has ceased to act or failed to act diligently, the Commission may appoint a substitute Interim Monitor in the same manner as provided in this Paragraph.
- G. The Commission may on its own initiative, or at the request of the Interim Monitor, issue such additional orders or directions as may be necessary or appropriate to assure compliance with the requirements of this Order.
- H. The Interim Monitor appointed pursuant to this Order may be the same person appointed as a Divestiture Trustee pursuant to the relevant provisions of this Order.

Decision and Order

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

- A. If Respondent has not fully complied with the obligations to grant, license, deliver or otherwise convey relevant assets as required by this Order, the Commission may appoint a trustee (“Divestiture Trustee”) to grant, license, deliver or otherwise convey the assets required to be granted, licensed, delivered or otherwise conveyed pursuant to each of the relevant Paragraphs in a manner that satisfies the requirements of each such Paragraph. In the event that the Commission or the Attorney General brings an action pursuant to § 5(*l*) of the Federal Trade Commission Act, 15 U.S.C. § 45(*l*), or any other statute enforced by the Commission, Respondent shall consent to the appointment of a Divestiture Trustee in such action to grant, license, deliver or otherwise convey the relevant assets. Neither the appointment of a Divestiture Trustee nor a decision not to appoint a Divestiture Trustee under this Paragraph shall preclude the Commission or the Attorney General from seeking civil penalties or any other relief available to it, including a court-appointed Divestiture Trustee, pursuant to § 5(*l*) of the Federal Trade Commission Act, or any other statute enforced by the Commission, for any failure by Respondent to comply with this Order.
- B. The Commission shall select the Divestiture Trustee, subject to the consent of Respondent, which consent shall not be unreasonably withheld. The Divestiture Trustee shall be a person with experience and expertise in acquisitions and divestitures. If Respondent has not opposed, in writing, including the reasons for opposing, the selection of any proposed Divestiture Trustee within ten (10) days after notice by the staff of the Commission to Respondent of the identity of any proposed Divestiture Trustee, Respondent

Decision and Order

shall be deemed to have consented to the selection of the proposed Divestiture Trustee.

- C. Not later than ten (10) days after the appointment of a Divestiture Trustee, Respondent shall execute a trust agreement that, subject to the prior approval of the Commission, transfers to the Divestiture Trustee all rights and powers necessary to permit the Divestiture Trustee to effect the divestiture required by this Order.
- D. If a Divestiture Trustee is appointed by the Commission or a court pursuant to this Paragraph, Respondent shall consent to the following terms and conditions regarding the Divestiture Trustee's powers, duties, authority, and responsibilities:
1. Subject to the prior approval of the Commission, the Divestiture Trustee shall have the exclusive power and authority to grant, license, deliver or otherwise convey the assets that are required by this Order to be granted, licensed, delivered or otherwise conveyed.
  2. The Divestiture Trustee shall have one (1) year after the date the Commission approves the trust agreement described herein to accomplish the divestiture, which shall be subject to the prior approval of the Commission. If, however, at the end of the one (1) year period, the Divestiture Trustee has submitted a plan of divestiture or believes that the divestiture can be achieved within a reasonable time, the divestiture period may be extended by the Commission, or, in the case of a court-appointed Divestiture Trustee, by the court; *provided, however*, the Commission may extend the divestiture period only two (2) times.
  3. Subject to any demonstrated legally recognized privilege, the Divestiture Trustee shall have full and complete access to the personnel, books, records and facilities

## Decision and Order

related to the relevant assets that are required to be assigned, granted, licensed, divested, delivered or otherwise conveyed by this Order and to any other relevant information, as the Divestiture Trustee may request. Respondent shall develop such financial or other information as the Divestiture Trustee may request and shall cooperate with the Divestiture Trustee. Respondent shall take no action to interfere with or impede the Divestiture Trustee's accomplishment of the divestiture. Any delays in divestiture caused by Respondent shall extend the time for divestiture under this Paragraph in an amount equal to the delay, as determined by the Commission or, for a court-appointed Divestiture Trustee, by the court.

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



Decision and Order

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

6. Respondent shall indemnify the Divestiture Trustee and hold the Divestiture Trustee harmless against any losses, claims, damages, liabilities, or expenses arising out of, or in connection with, the performance of the Divestiture Trustee's duties, including all reasonable fees of counsel and other expenses incurred in connection with the preparation for, or defense of, any claim, whether or not resulting in any liability, except to the extent that such losses, claims, damages, liabilities, or expenses result from misfeasance, gross negligence, willful or wanton acts, or bad faith by the Divestiture Trustee.
7. The Divestiture Trustee shall have no obligation or authority to operate or maintain the relevant assets required to be granted, licensed, transferred, delivered or otherwise conveyed by this Order.
8. The Divestiture Trustee shall report in writing to Respondent and to the Commission every sixty (60) days concerning the Divestiture Trustee's efforts to accomplish the divestiture.

## Decision and Order

9. Respondent may require the Divestiture Trustee and each of the Divestiture Trustee's consultants, accountants, attorneys and other representatives and assistants to sign a customary confidentiality agreement; *provided, however*, such agreement shall not restrict the Divestiture Trustee from providing any information to the Commission.
- E. If the Commission determines that a Divestiture Trustee has ceased to act or failed to act diligently, the Commission may appoint a substitute Divestiture Trustee in the same manner as provided in this Paragraph.
- F. The Commission or, in the case of a court-appointed Divestiture Trustee, the court, may on its own initiative or at the request of the Divestiture Trustee issue such additional orders or directions as may be necessary or appropriate to accomplish the divestiture required by this Order.
- G. The Divestiture Trustee appointed pursuant to this Paragraph may be the same person appointed as Interim Monitor pursuant to the relevant provisions of this Order.

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

- H. Within five (5) days of the Acquisition, Respondent shall submit to the Commission a letter certifying the date on which the Acquisition occurred.
- I. Within thirty (30) days after the date this Order becomes final, and every sixty (60) Days thereafter until Respondent have fully complied with Paragraphs II.A., II.E., III.A., III.C., III.D., III.E., III.F., III.G., IV.A., and all its responsibilities to render transitional services to the Commission-approved Acquirer as provided in the Remedial Agreement(s), Respondent shall submit to the Commission a verified written report setting forth in detail

Decision and Order

the manner and form in which it intends to comply, is complying, and have complied with this Order. Respondent shall submit at the same time a copy of its report concerning compliance with this Order to the Interim Monitor, if any Interim Monitor has been appointed. Respondent shall include in its reports, among other things that are required from time to time:

1. a full description of the efforts being made to comply with the relevant Paragraphs of this Order;
2. if Abbott is rejected by the Commission pursuant to Paragraph II.A., a description of all substantive contacts or negotiations related to the licensing of the Drug Eluting Stent Patents and the identity of all parties contacted and copies of all written communications to and from such parties, all internal memoranda, and all reports and recommendations concerning completing its obligations to license the Drug Eluting Stent Patents;
3. if Datascope is rejected by the Commission pursuant to Paragraph III.A., a description of all substantive contacts or negotiations related to the divestiture of the EVH Business and the identity of all parties contacted and copies of all written communications to and from such parties, all internal memoranda, and all reports and recommendations concerning completing its obligations to divest the EVH Business;
4. a detailed plan to deliver all Confidential Business Information required to be delivered to the Commission-approved Acquirer pursuant to Paragraphs III.A. and III.D., and agreed upon by the Commission-approved Acquirer and the Interim Monitor (if applicable) and any updates or changes to such plan;
5. a description of all Confidential Business Information delivered to the Commission-approved Acquirer,

## Decision and Order

including the type of information delivered, method of delivery, and date(s) of delivery;

6. a description of the Confidential Business Information currently remaining to be delivered and a projected date(s) of delivery; and
7. a description of all technical assistance provided to the Commission-approved Acquirer during the reporting period.

**VII.**

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

**VII.**

**IT IS FURTHER ORDERED** that, for the purpose of determining or securing compliance with this Order, and subject to any legally recognized privilege, and upon written request with reasonable notice to Respondent made to its principal United States offices, Respondent shall permit any duly authorized representative of the Commission:

- A. Access, during office hours of Respondent and in the presence of counsel, to all facilities and access to inspect and copy all books, ledgers, accounts, correspondence, memoranda and all other records and documents in the possession or under the control of Respondent related to compliance with this Order; and

Decision and Order

- B. Upon five (5) days' notice to Respondent and without restraint or interference from Respondent, to interview officers, directors, or employees of Respondent, who may have counsel present, regarding such matters.

**VIII.**

**IT IS FURTHER ORDERED** that this Order shall terminate ten (10) years from the date on which this Order becomes final.

Decision and Order

**APPENDIX I  
NON-PUBLIC**

**ABBOTT AGREEMENT**

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

**APPENDIX II  
NON-PUBLIC**

**AGENTS USED IN COMBINATION WITH ABT-578**

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

Decision and Order

**APPENDIX III  
PUBLIC**

**ADDITIONAL DRUG ELUTING STENT PATENTS**

<b>ISSUED US PATENTS</b>
5,421,955
5,514,154
5,569,295
5,603,721
5,649,952
5,728,158
5,735,893
5,766,238
5,916,234
6,056,776
6,066,167
6,066,168
6,309,412
6,432,133
6,485,511
6,511,504
6,596,022
6,620,193
6,626,933
6,629,991
6,689,159
6,908,479
B1 5,421,955
<u>Pending US Applications</u>
10/626,083
11/112,143

Decision and Order

**APPENDIX IV  
NON-PUBLIC**

**DATASCOPE AGREEMENT**

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

**APPENDIX V  
NON-PUBLIC**

**EVH EMPLOYEES**

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

**APPENDIX VI  
NON-PUBLIC**

**LICENSED PRODUCT CODE NUMBERS**

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

**APPENDIX VII  
NON-PUBLIC**

**TERMINATION AGREEMENT**

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



Analysis

**Analysis of Agreement Containing Consent Order to Aid  
Public Comment**

The Federal Trade Commission (“Commission”) has accepted, subject to final approval, an Agreement Containing Consent Orders (“Consent Agreement”) from Johnson & Johnson (“J&J”). The purpose of the proposed Consent Agreement is to remedy the anticompetitive effects that would otherwise result from J&J’s acquisition of Guidant Corporation (“Guidant”). Under the terms of the proposed Consent Agreement, J&J is required to (a) grant to a third party a fully paid-up, non-exclusive, irrevocable license, enabling that third party to make and sell drug-eluting stents (“DESs”) with the Rapid Exchange (“RX”) delivery system, (b) divest to a third party J&J’s endoscopic vessel harvesting (“EVH”) product line, and (c) terminate its agreement to distribute the proximal anastomotic assist device (“AAD”) of Novare Surgical System, Inc. (“Novare”).

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

Pursuant to an Agreement and Plan of Merger dated December 15, 2004, J&J proposes to acquire Guidant in exchange for cash and voting securities in a transaction valued at approximately \$25.4 billion. The Commission’s complaint alleges that the proposed acquisition, if consummated, would violate Section 7 of the Clayton Act, as amended, 15 U.S.C. § 18, and Section 5 of the Federal Trade Commission Act, as amended, 15 U.S.C. § 45, by removing an imminent competitor from the U.S. market for DESs and by lessening competition in the U.S. markets for EVH devices and proximal AADs. The proposed Consent Agreement would remedy the alleged violations by replacing the competition that would be lost in these markets as a result of the acquisition.

## Analysis

J&J is a comprehensive and broadly-based manufacturer of products related to all aspects of human health care. In 2004, J&J generated global sales of \$47.3 billion and U.S. sales of \$27.7 billion. J&J is divided into three business segments: Consumer, Pharmaceutical, and Medical Devices and Diagnostics. The products impacted by the proposed transaction, DESs, EVH devices, and proximal AADs, fall within J&J's Medical Devices and Diagnostics segment.

Guidant manufactures products in three broad business units: cardiac rhythm management, vascular intervention, and cardiac surgery. In 2004, Guidant's sales were \$3.8 billion globally and \$2.53 billion in the United States. Guidant's DES program is part of its vascular intervention business unit, and the company's EVH device and proximal AAD are part of the cardiac surgery business unit.

**Drug -Eluting Stents**

A DES is a medical device typically consisting of a thin, metallic stent coated with an antiproliferative drug and a polymer, mounted on a delivery system. Interventional cardiologists use DESs to treat coronary artery disease, a condition caused by the build up of plaque deposits within one or more coronary arteries leading to reduced blood flow. DESs work by propping open the clogged artery or arteries and eluting a drug, which helps prevent the re-narrowing of the artery, called restenosis. DESs are the most effective minimally-invasive method for treating coronary artery disease, and other products and procedures are not economic substitutes for DESs.

DESs are sold mounted on a delivery system used to deploy the DES to the blocked area of the coronary artery. The two most common types of delivery system in the United States are over-the-wire and Rapid Exchange ("RX"). Over-the-wire delivery systems employ a long guidewire and require two operators to implant the DES. In contrast, the RX delivery system employs a shorter guidewire that can be handled by a single operator. RX

Analysis

delivery systems currently are highly preferred by physicians in the United States and are increasing in popularity. Boston Scientific Corporation and Guidant own the intellectual property rights to the RX delivery system in the United States. The companies have cross-licensed each other, and J&J has access to the RX delivery system through an agreement with Guidant. Both DESs currently on the market, J&J's Cypher® and Boston Scientific's Taxus®, are available on the RX delivery system.

The relevant geographic market in which to analyze the effects of the proposed acquisition on the DES market is the United States. DESs are medical devices that are regulated by the United States Food and Drug Administration ("FDA"). Performing the necessary clinical testing and navigating the approval process for the FDA can be burdensome and time-consuming. As such, DESs sold outside of the United States but not approved for sale in the United States do not provide viable competitive alternatives for U.S. consumers.

The U.S. market for DESs is highly concentrated; currently only two firms, J&J and Boston Scientific, have products on the market. Guidant's DES program is still in development, but it is anticipated to be one of at least three entrants, along with Medtronic, Inc. and Abbott Laboratories, likely to enter the U.S. market by the end of 2007. Guidant is the only anticipated entrant with rights to the intellectual property necessary to market a DES with the RX delivery system, the dominant delivery system in the United States.

Developing and receiving FDA approval for a DES is difficult, time-consuming and expensive. It can take hundreds of millions of dollars of research and development, significant funding for clinical trials, and an extensive amount of time to even reach the stage of seeking FDA approval. The regulatory process itself can also be time-consuming as the FDA reviews the volumes of materials and data a company submits in support of its application for approval.

## Analysis

Considering all these factors, entry into the manufacture and sale of DESs is impossible to achieve within two to three years.

In addition to the regulatory barriers facing firms seeking to enter the DES market, there are substantial intellectual property barriers an entrant must overcome. Firms must invent around or obtain licenses to patents covering nearly every aspect of a DES, including the design of stents, stent delivery systems, and the drugs and polymers used on DESs. Due to the difficulty of entry, firms must commit to entering the market years in advance of any anticipated entry, and timely and sufficient entry in response to a small but significant price increase is impossible.

The proposed acquisition would cause significant competitive harm in the market for DESs by eliminating Guidant as the only potential competitor with the ability to offer a DES on an RX delivery system. As a third RX entrant into the DES market, Guidant likely would increase competition and reduce prices for DESs. Although two other firms, Abbott and Medtronic, are poised to enter the market in the same approximate time frame as Guidant, their lack of access to the RX delivery system makes it unlikely that either company could be a substantial competitive constraint on the DES market in the near term. The proposed acquisition therefore decreases the number of potential DES suppliers with access to the RX delivery system from three to two until at least late 2008, when Guidant's key patents relating to the RX delivery system begin to expire. (The relevant Boston Scientific RX patents begin to expire this year).

The proposed Consent Agreement effectively remedies the proposed acquisition's anticompetitive effects in the market for DESs. Pursuant to the proposed Consent Agreement, the combined J&J/Guidant is required to license Guidant's intellectual property surrounding the RX delivery system at no minimum price to an up-front buyer with a DES program in development no later than ten (10) days after the acquisition is consummated. Through the course of the investigation, Commission staff gathered a great deal of information about each

Analysis

of the companies developing DES products. In particular, staff investigated potential divestiture candidates and concluded that Abbott was among the companies well-positioned to replicate the competitive impact Guidant was likely to have absent the proposed acquisition. The parties have selected Abbott as the up-front buyer for the divestiture package. Abbott is a well-known and respected pharmaceutical and diagnostics company that has a number of vascular devices on the market already or in development. It has experience with both drugs and vascular devices, a highly regarded DES design, a strong and growing vascular sales force, and the necessary manufacturing capabilities. Abbott, therefore, is poised to become a strong competitor in the DES market when it enters in the second half of 2007, approximately the same time as Guidant's anticipated date of entry. Access to the RX delivery system will allow Abbott to replace Guidant as the third entrant into the DES market with an RX delivery system.

The Commission's merger remedies are intended to maintain or to restore the competitive *status quo*. The Commission does not, as a matter of course, seek to "improve" on pre-transaction competition. Based on the evidence gathered in the investigation, the Commission has determined that the license to Abbott should replicate the competitive conditions in DESs that existed prior to the proposed transaction between J&J and Guidant. As a result, a Commission order requiring licenses to additional parties is not necessary.

Given the uncertainty inherent in a development program, the RX license contemplated by the proposed Consent Agreement is transferable, so that if Abbott's DES program is not successful, it will have the incentive and ability to transfer the RX license to another firm developing a DES, ensuring that a successful third DES firm is able to enter the market with an RX delivery system in the relevant timeframe. The proposed Consent Agreement also requires the parties to enter into a covenant not to sue Abbott in relation to certain intellectual property rights regarding stent design, stent coating and the use of certain drugs on a stent.

Analysis

**Endoscopic Vessel Harvesting Devices**

EVH devices are used in coronary artery bypass graft (“CABG”) surgery to remove a patient’s leg vein, arm artery, or other blood vessel that is then used as a conduit to bypass one or more blocked coronary arteries. EVH devices allow for a minimally-invasive procedure requiring only one to three small incisions. EVH has several clinical benefits over the other methods of vessel harvesting (the open method and bridging) both of which are much more invasive, leave large, unsightly scars and carry a greater risk of infection. Surgeons and physician’s assistants would not switch to these other methods of vessel harvesting even if the price of using EVH devices increased by five to ten percent.

As with DESs, the United States is the relevant geographic market in which to analyze the effects of the proposed acquisition on the EVH device market. EVH devices are also medical devices subject to regulation by the FDA. Receiving FDA approval to market an EVH device in the United States can be a lengthy process, but is necessary in order to sell the devices in the United States. EVH devices sold outside of the United States but not approved by the FDA for sale in the United States therefore do not provide viable competitive alternatives for U.S. consumers.

The U.S. market for EVH devices is highly concentrated with J&J and Guidant as the only competitors until very recently, when Terumo Corporation entered. Guidant currently dominates the market with over eighty percent market share. Terumo received FDA approval for its device in January, 2005 and has yet to generate significant sales.

Firms seeking to enter the market for EVH devices face regulatory hurdles and significant intellectual property barriers, both of which make entry into the market for EVH devices in the next two to three years highly unlikely. In addition, while the use of EVH devices in CABG surgery is increasing, the number of overall CABG surgeries appears to be decreasing due to, among

Analysis

other things, the increase in stenting procedures; this steady decline in the number of CABG procedures being performed in the United States makes it less likely that firms would choose to enter the EVH device market in response to a modest increase in the price of the devices.

The proposed acquisition would constitute a virtual merger to monopoly in the market for EVH devices and is likely to lead to increased prices and decreased innovation in the market for those devices. Until recently, Guidant and J&J were the only two firms to offer an EVH device in the United States, and while Terumo recently entered, it is likely that it will take several years before Terumo's device has a significant impact on the market for EVH devices.

The proposed Consent Agreement effectively remedies the proposed acquisition's anticompetitive effects in the market for EVH devices by requiring J&J to divest its EVH product line to a Commission-approved buyer at no minimum price. J&J has reached an agreement to divest the EVH business to Datascope. Datascope, a diversified medical device company, has a line of products used in cardiac surgery, including products used in CABG procedures. Pursuant to the Consent Agreement, J&J is required to accomplish the divestiture of its EVH product line no later than fifteen (15) business days after the acquisition is consummated.

The proposed Consent Agreement permits the Commission-approved buyer of the EVH product line assets to enter into a supply agreement with J&J for a period of up to two (2) years. The supply agreement may be necessary because of the need to recreate or move manufacturing and/or packaging equipment and to allow time for the acquirer to receive approval from the FDA to begin manufacturing and/or packaging EVH device kits in its own facility. This supply agreement may also be necessary to allow J&J to supply certain components of the EVH devices until the acquirer is able to procure similar components from third-party vendors.

## Analysis

In addition, the proposed Consent Agreement permits J&J to provide certain transitional services to the Commission-approved buyer of the EVH product line assets. These transitional services may be necessary for a smooth transition of the product line to the acquirer and to ensure continued and uninterrupted service to customers during the transition.

**Proximal Anastomotic Assist Devices**

Surgeons use proximal AADs in CABG procedures to avoid the need to clamp the aorta when attaching a harvested vessel to it. If a proximal AAD is not used, the surgeon must use a clamp to stop the flow of blood to a segment of the aorta while the harvested vessel is surgically attached. Using a clamp can cause calcified plaque particles to dislodge from the aorta and travel through the blood stream to the brain, risking neurological dysfunction or stroke.

The proper geographic market in which to analyze the effects of the proposed transaction on the market for proximal AADs is the United States. Proximal AADs are medical devices that must be approved by the FDA before being marketed in the United States. As with other medical devices, the clinical testing and regulatory approval process for proximal AADs can be costly and time-consuming, preventing proximal AADs approved outside of the United States but not approved within the United States from serving as a competitive alternative for U.S. consumers.

There are currently three firms in the U.S. market for proximal AADs, making it a highly concentrated market. The evidence indicates that J&J and Guidant's manual proximal AADs are each others' closest competitors. Medtronic also participates in the market with an automatic device that it recently launched in the United States. A fourth firm, St. Jude Medical, removed its automatic device, Symmetry®, from the market last year amidst reports of device failures. J&J's proximal AAD, eNclose®, was



Analysis

developed and is manufactured by Novare; J&J and Novare have a distribution agreement making J&J the sole distributor of eNclose® in the United States.

As with the other medical devices discussed, entry into the market for proximal AADs is difficult, costly, and time-consuming. Additionally, the alleged safety concerns regarding St. Jude's Symmetry device have resulted in greater scrutiny of proximal AADs by the FDA. The increased scrutiny is likely to substantially increase the cost of developing a proximal AAD. In addition, it appears that the publicity surrounding Symmetry's removal from the market has dampened physician enthusiasm for these devices. These developments, along with the declining number of overall U.S. CABG procedures, decrease the likelihood of entry into this market.

The proposed acquisition is likely to cause significant competitive harm in the market for proximal AADs by eliminating competition between J&J and Guidant and reducing the number of competitors in the market from three to two. The evidence has also shown that J&J and Guidant's products are likely each others' closest competitors in the proximal AAD market because they are more similar to each other than to Medtronic's product. The proposed acquisition is therefore likely to enable the combined J&J/Guidant to raise prices for proximal AADs unilaterally.

The proposed acquisition's anticompetitive effects in the market for proximal AADs are remedied by the proposed Consent Agreement's requirement that J&J terminate its distribution agreement with Novare for Novare's proximal AAD, eNclose. It is anticipated that it will take Novare no more than two months to find a new distribution partner for eNclose.

### **Appointment of an Interim Monitor and a Divestiture Trustee**

The proposed Consent Agreement contains a provision that allows the Commission to appoint an interim monitor to oversee

## Analysis

J&J's compliance with all of its obligations and performance of its responsibilities pursuant to the Commission's Decision and Order. The interim monitor is required to file periodic reports with the Commission to ensure that the Commission remains informed about the status of the divestitures, about the efforts being made to accomplish the divestitures, and the provision of services and assistance during the transition period for the EVH divestiture.

Finally, the proposed Consent Agreement contains provisions that allow the Commission to appoint a divestiture trustee if any or all of the above remedies are not accomplished within the time frames required by the Consent Agreement. The divestiture trustee may be appointed to accomplish any and all of the remedies required by the proposed Consent Agreement that have not yet been fulfilled upon expiration of the time period allotted for each.

The purpose of this analysis is to facilitate public comment on the proposed Consent Agreement, and it is not intended to constitute an official interpretation of the proposed Decision and Order or to modify its terms in any way.

Order

IN THE MATTER OF

**ENTERGY CORPORATION**

**ORDER REOPENING AND SETTING ASIDE ORDER**

On March 3, 2005, Entergy Corporation (“Entergy”) and Entergy-Koch, LP (“EKLP”), respondents named in the consent order issued by the Commission on January 31, 2001, in Docket No. C-3998 (“Order”), filed their Petition of Entergy and EKLP to Reopen and Set Aside Order in this matter (“Petition”). Entergy and EKLP ask the Commission to reopen and modify the Order in its entirety pursuant to Section 5(b) of the Federal Trade Commission Act, 15 U.S.C. § 45(b), and Section 2.51 of the Commission’s Rules of Practice and Procedure, 16 C.F.R. § 2.51, thereby relieving them of Entergy’s and EKLP’s reporting and posting obligations, which comprise the only ongoing performance obligations under the Order and which otherwise will continue until January 31, 2007. Respondents contend, *inter alia*, that significant changed circumstances eliminate the continuing need for the Order’s requirements. Petition at 2, 8-9. The Petition was placed on the public record for thirty days pursuant to Section 2.51(c) of the Commission’s Rules. No comments were received. For the reasons stated below, the Commission has determined to grant the Petition.

The Complaint issued with the Order in Docket No. C-3998 states that, on May 26, 2000, Entergy and Koch Industries, Inc. (“Koch”) entered into an agreement to form EKLP, a limited partnership owned equally by Entergy and Koch, and that each contributed certain assets to EKLP. (Complaint ¶ 12). Among other things, EKLP acquired Gulf South Pipeline Company LP (“Gulf South”), a major supplier of natural gas pipeline transportation in Louisiana and Mississippi, from Koch (Complaint ¶¶ 6, 12, 19). Entergy, in turn, acquired a fifty percent interest in Gulf South through EKLP, including the right to fifty percent of EKLP’s profits. (Complaint ¶ 10). At the same time, Entergy also owns regulated utilities that supply electricity to

## Order

consumers in Louisiana and western Mississippi, and that distribute natural gas to consumers in New Orleans and Baton Rouge, Louisiana. (Complaint ¶¶ 2, 13-18). Further, Gulf South is capable of supplying all of Entergy's regulated utilities in those states with natural gas transportation. (Complaint ¶ 19).

The Complaint alleges that, as a result of Entergy's fifty percent ownership of Gulf South, it would "have the incentive and ability . . . to pay EKLP prices for natural gas transportation [for its regulated utilities that are subject to state regulator's rules governing the recovery of the cost for delivery of natural gas] above prevailing market prices and to purchase a level of service above what is necessary for effective operation of Entergy's facilities." (Complaint ¶ 21). Moreover, the Complaint alleges, it would be more difficult for state and local regulators in Louisiana and western Mississippi to detect whether Entergy had improperly incurred inflated costs of natural gas transportation in its purchase from its affiliates, and to challenge such costs as having been imprudently incurred, for several reasons, including that "the process by which Entergy purchases gas transportation is not transparent." (Complaint ¶ 22). Thus, the prices of retail electricity in Louisiana and western Mississippi, and for natural gas in New Orleans and Baton Rouge, would likely increase "as a result of Entergy passing on inflated costs for natural gas transportation to consumers and the difficulties that regulators will have in reviewing and challenging Entergy's purchases of natural gas transportation." (Complaint ¶¶ 29, 35). The Order issued to prevent Entergy from paying such inflated prices by establishing procedures that Entergy and EKLP were required to implement and follow to assure the transparency of Entergy's natural gas purchases.

The Petition states that, on December 29, 2004, Entergy sold its interest in Gulf South to TGT Pipeline, LLC ("TGT"), a subsidiary of Loews Corporation and an entity unrelated to either Entergy or EKLP. Petition at 2. Since that time Entergy no longer has any ownership or financial interest in or control over Gulf South, and, therefore, no longer has any incentive to pay

Order

inflated prices for natural gas transportation. *Id.* Absent this incentive, according to the Petition, the Order's purpose to establish a transparent process for purchasing natural gas transportation no longer applies and its procedures to assure continued transparency are no longer necessary. *Id.* Moreover, according to the Petition, with the sale of Gulf South, EKLK no longer can comply with the specific posting requirements the Order imposes. *Id.* at 8-9. There is, therefore, no longer any factual basis for the concerns expressed in the Complaint and addressed by the Order. *Id.* The elimination of Entergy's ownership in Gulf South should therefore constitute a substantial change in conditions that justifies reopening and setting aside the Order. *Id.* at 9.

The Order may be reopened on the grounds set forth in Section 5(b) of the Federal Trade Commission Act, 15 U.S.C. § 45(b), 16 C.F.R. § 2.51(b). Section 5(b) provides that the Commission shall reopen an order to consider whether it should be set aside if the respondent "makes a satisfactory showing that changed conditions of law or fact" so require.<sup>1</sup> A satisfactory showing sufficient to require reopening is made when a request to reopen identifies significant changes in circumstances and shows that the changes eliminate the need for the order or make continued application of it inequitable or harmful to competition.<sup>2</sup> Where changed circumstances do not require reopening, Section

---

<sup>1</sup> See *Supplementary Information, Amendment to 16 CFR 2.51(b)*, announced August 15, 2001, ("Amendment").

<sup>2</sup> S. Rep. No. 96-500, 96th Cong., 2d Sess. 9 (1979) (significant changes or changes causing unfair disadvantage); *Louisiana-Pacific Corp.*, Docket No. C-2956, Letter to John C. Hart (June 5, 1986), at 4 (unpublished) ("Hart Letter"). See also *United States v. Louisiana-Pacific Corp.*, 967 F.2d 1372, 1376-77 (9th Cir. 1992) ("A decision to reopen does not necessarily entail a decision to modify the Order. Reopening may occur even where the petition itself does not plead facts requiring modification.").

## Order

5(b) further provides that the Commission may reopen and set aside an order when it determines that the public interest so requires. Entergy and EKLP's Petition also addresses the public interest standard, which requires that the requester make a *prima facie* showing of a legitimate public interest reason or reasons justifying relief. In this instance, however, we do not need to assess the sufficiency of Entergy's and EKLP's public interest showing because the Commission has determined that Entergy and EKLP have made the requisite satisfactory showing that changed conditions of fact require the Order to be reopened and set aside.

Upon consideration of Entergy's and EKLP's Petition and other information, the Commission has determined that the factual premise underlying the concerns that led to entry of the Order, with its detailed reporting and posting obligations, arose specifically from the acquisition of Entergy's ownership interest in Gulf South through its joint venture, EKLP. The sale of Gulf South constitutes a substantial change that eliminates the continuing need for the Order's requirements. Further, the sale of Gulf South substantially changes EKLP's ability to comply with its ongoing obligations regarding Gulf South's postings.

Entergy and EKLP, having initiated and complied to date with all the procedures, postings, and record keeping set forth in the Order, now seek relief from continuing to perform those procedures, which are no longer necessary and with which EKLP can no longer comply. For these reasons, the Commission finds that changed conditions of fact warrant reopening and setting aside the Order.

Accordingly,

**IT IS ORDERED THAT** this matter be, and it hereby is, reopened; and

Order

**IT IS FURTHER ORDERED THAT** the Commission's Order issued on January 31, 2001, hereby is set aside, as of the date of issuance of this Order.

Order

IN THE MATTER OF

**NESTLÉ HOLDINGS, INC.****ORDER REOPENING AND MODIFYING ORDER**

On March 23, 2005, Dreyer's Grand Ice Cream Holdings, Inc., and Dreyer's Grand Ice Cream, Inc. (collectively, "Respondents") filed their "Request to Reopen Proceedings and Modify Decision and Order" ("Request"). Respondents seek to modify certain terms of the divestiture agreements with CoolBrands International Inc. ("CoolBrands") at the request of CoolBrands. Specifically, Respondents seek to modify the Order in Docket No. C-4082 ("Order") to allow Respondents to continue to provide Administrative Services to CoolBrands for an additional one year beyond the twenty-one months provided in Paragraph II.H. of the Order.<sup>1</sup> Respondents also seek prior Commission approval to modify the divestiture agreements to correspond to the requested modifications. Commission approval is required because Respondents were required to divest pursuant to a divestiture agreement that received the prior approval of the Commission. For the reasons stated below, the Commission has determined to grant the Request and has reopened and modified the Order and granted approval to the modifications to the divestiture agreements.<sup>2</sup>

---

<sup>1</sup> Respondents had previously sought and received an extension of this provision from one year to twenty-one months.

<sup>2</sup> In connection with the Request, Respondents requested that the Commission eliminate the public comment period on the Request. Respondents provided no compelling reason for the Commission to vary from its normal procedures. A press release was issued shortly after the Request was filed. The Commission has determined to deny the request to eliminate the comment period.



Order

## I. BACKGROUND

This matter arose from Nestlé's 2003 acquisition of Dreyer's, valued at approximately \$2.8 billion. In order to resolve competitive concerns regarding the combination of the parties' ice cream businesses, the Consent Order required Respondents to divest assets and to enter several (confidential) arrangements with CoolBrands. In particular, the Order required the Respondents to divest: (1) all assets, businesses, and goodwill related to the manufacture, marketing, or sale of the Dreamery, Godiva ice cream and Whole Fruit brands, and (2) all assets related to Nestlé's distribution of frozen dessert products. These assets, collectively referred to as the "assets to be divested," were divested to CoolBrands on July 5, 2003. Also under the Order, Dreyer's is required to supply CoolBrands with the types and quantities of Dreamery, Godiva ice cream, and Whole Fruit products that CoolBrands requests at a price no greater than Dreyer's production costs for a period not to exceed one (1) year. At the request of CoolBrands, Dreyer's must provide distribution services for the CoolBrands' Dreamery, Godiva ice cream, and Whole Fruit products for a period not to exceed one (1) year in any areas of the U.S. where Dreyer's previously distributed these products. Respondents must also provide technical and administrative services to CoolBrands, as needed, for a period not to exceed one (1) year. Finally, the Respondents must supply sufficient volumes of additional ice cream products to CoolBrands to enable CoolBrands to profitably distribute Dreamery, Godiva ice cream, and Whole Fruit superpremium products, for a period not to exceed five (5) years.

## II. THE REQUEST

The impetus for the Respondents' Request was the desire of CoolBrands to have certain changes made to the divestiture agreements to enable it to compete more effectively. The Request seeks to reopen and modify the Order to extend the period under which Dreyer's will provide certain Administrative Services to CoolBrands, pursuant to the Transitional Services Agreement, for

## Order

an additional one year, until April 2006. The current agreement expired on April 1, 2005. CoolBrands explains that the loss of the Weight Watchers ice cream business, the integration of Kraft's yogurt business, and the sudden death of Mr. Richard Smith, an important member of the management team, has strained its management's time and prevented it from assuming the responsibilities covered by the Transitional Services Agreement. Affidavit of David J. Stein, President and CEO of CoolBrands ("Stein Affidavit") at ¶ 5.

### III. STANDARD FOR REOPENING AND MODIFYING A FINAL ORDER

The Order may be reopened and modified on the grounds set forth in § 5(b) of the Federal Trade Commission Act, 15 U.S.C. § 45(b). Section 5(b) provides that the Commission shall reopen an order to consider whether it should be modified if the respondent "makes a satisfactory showing that changed conditions of law or fact" so require.<sup>3</sup> A satisfactory showing sufficient to require reopening is made when a request to reopen identifies significant changes in circumstances and shows that the changes eliminate the need for the order or make continued application of it inequitable or harmful to competition.<sup>4</sup>

---

<sup>3</sup> See *Supplementary Information, Amendment to 16 CFR 2.51(b)*, announced August 15, 2001, ("Amendment").

<sup>4</sup> S. Rep. No. 96-500, 96th Cong., 2d Sess. 9 (1979) (significant changes or changes causing unfair disadvantage); *Louisiana-Pacific Corp.*, Docket No. C-2956, Letter to John C. Hart (June 5, 1986), at 4 (unpublished) ("Hart Letter"). See also *United States v. Louisiana-Pacific Corp.*, 967 F.2d 1372, 1376-77 (9th Cir. 1992) ("A decision to reopen does not necessarily entail a decision to modify the Order. Reopening may occur even where the petition itself does not plead facts requiring modification.").

Order

Section 5(b) also provides that the Commission may reopen and modify an order when, although changed circumstances would not require reopening, the Commission determines that the public interest so requires. Respondents are therefore invited in petitions to reopen to show how the public interest warrants the requested modification.<sup>5</sup> In the case of “public interest” requests, FTC Rule of Practice 2.51(b) requires an initial “satisfactory showing” of how modification would serve the public interest before the Commission determines whether to reopen an order and consider all of the reasons for and against its modification.

A “satisfactory showing” requires, with respect to public interest requests, that the requester make a *prima facie* showing of a legitimate public interest reason or reasons justifying relief. A request to reopen and modify will not contain a “satisfactory showing” if it is merely conclusory or otherwise fails to set forth by affidavit(s) specific facts demonstrating in detail the reasons why the public interest would be served by the modification.<sup>6</sup> This showing requires the requester to demonstrate, for example, that there is a more effective or efficient way of achieving the purposes of the order, that the order in whole or part is no longer needed, or that there is some other clear public interest that would be served if the Commission were to grant the requested relief. In addition, this showing must be supported by evidence that is credible and reliable.

If, after determining that the requester has made the required showing, the Commission decides to reopen the order, the Commission will then consider and balance all of the reasons for and against modification. In no instance does a decision to reopen

---

<sup>5</sup> Hart Letter at 5; 16 C.F.R. § 2.51.

<sup>6</sup> 16 C.F.R. § 2.51.

## Order

an order oblige the Commission to modify it,<sup>7</sup> and the burden remains on the requester in all cases to demonstrate why the order should be reopened and modified. The petitioner's burden is not a light one in view of the public interest in repose and the finality of Commission orders.<sup>8</sup> All information and material that the requester wishes the Commission to consider shall be contained in the request at the time of filing.<sup>9</sup>

#### **IV. THE ORDER WILL BE REOPENED AND MODIFIED IN THE PUBLIC INTEREST**

The Commission has determined to reopen and modify the Order as requested by Respondents. CoolBrands has shown that unanticipated changes in demand for its products have stretched its management resources, and the extension will better enable it to compete in the long term. Dreyer's has already agreed to the extension.

Specifically, CoolBrands recently lost the Weight Watchers ice cream business. Stein Affidavit at ¶ 6. Management was also involved in time-consuming litigation with Weight Watchers over the cancellation of the contract. CoolBrands recently acquired Kraft's yogurt business, and has been working hard to integrate this business. Stein Affidavit at ¶ 7. Mr. Smith's death has also impacted CoolBrands' business, causing a realignment of management duties. Stein Affidavit at ¶ 8. These developments

---

<sup>7</sup> See *United States v. Louisiana-Pacific Corp.*, 967 F.2d 1372, 1376-77 (9<sup>th</sup> Cir. 1992) (reopening and modification are independent determinations).

<sup>8</sup> See *Federated Department Stores, Inc. v. Moitie*, 425 U.S. 394 (1981) (strong public interest considerations support repose and finality).

<sup>9</sup> 16 C.F.R. § 2.51(b).

Order

have prevented CoolBrands from taking over the services covered by the Transition Services Agreement.

Respondents seek the modification under either change of fact or public interest grounds. Although the possibility that CoolBrands might lose the Weight Watchers ice cream business and acquire the Kraft yogurt business were not anticipated at the time the Order was entered, it is not clear that these changes to CoolBrands' business are unforeseeable "changes of fact" within the meaning of Section 5(b) of the FTC Act. Nevertheless, holding CoolBrands to the twenty-one month limit on obtaining Administrative Services from Dreyer's, with the resulting disruption to its operations and ability to compete, would likely diminish CoolBrands' competitive effectiveness. It is therefore in the public interest to make the change to enable CoolBrands to continue to compete in the market without disruption of its operations. Moreover, because the extension is designed to benefit the acquirer of the divested assets, and not the respondent, it is clearer that the change is in the public interest. CoolBrands has taken steps to ensure that it will be able to take over these functions by the extended deadline, and has expressed confidence that it will be able to do so. Stein Affidavit at ¶ 13.

Although the Commission has determined that Respondents have satisfied the public interest standard, the case for modification is not overwhelming. The deadlines for transitional services contained in Commission Orders are designed to provide the acquirer of divested assets with a reasonable amount of time to prepare to compete effectively in the market, and are not intended to create a long-term relationship between the seller of the assets and the acquirer. Having now extended the transitional services deadline twice at the request of CoolBrands, it is very unlikely that the Commission would further extend the deadline.

Accordingly,

**IT IS ORDERED**, That this matter be, and it hereby is, reopened; and

Order

**IT IS FURTHER ORDERED**, That paragraph II.H. of the Order be, and it hereby is, modified, as of the effective date of this order, to read as follows:

- H. At the request of the Commission Approved Acquirer, for a period not to exceed thirty- three (33) months from the date Respondents divest the Assets To Be Divested, Dreyer's shall provide Administrative Services to the Commission Approved Acquirer sufficient to enable the Commission Approved Acquirer to operate the Assets To Be Divested in a viable and competitive manner. In providing Administrative Services to the Commission Approved Acquirer, Dreyer's shall charge no more than its Service Cost of providing the Administrative Services.

Order

IN THE MATTER OF

**CHICAGO BRIDGE & IRON COMPANY N.V.**

**ORDER APPROVING RESPONDENTS' APPLICATION  
FOR APPROVAL OF MONITOR TRUSTEE AND  
MONITOR TRUSTEE AGREEMENT**

The Commission's Final Order in this matter required Respondents to retain a Monitor Trustee within 30 days of the Commission's Order becoming final. Respondents Chicago Bridge & Iron filed an Application for Approval of Proposed Monitor Trustee and Monitor Trustee Agreement on May 26, 2005. On June 3, 2005, Complaint Counsel filed a response indicating that they do not oppose Respondents' choice of Monitor Trustee and the Monitor Trustee Agreement is acceptable. The Commission has decided to approve Respondents' Application. Accordingly,

**IT IS ORDERED THAT** Respondents' Application to retain Mr. Paul J. Vallero as the Monitor Trustee in this matter is **APPROVED**; and

**IT IS FURTHER ORDERED THAT** the Monitor Trustee Agreement executed between Mr. Vallero and Respondents CB&I is **APPROVED**.

By the Commission.

Order

IN THE MATTER OF

RAMBUS INCORPORATED

**ORDER REOPENING THE RECORD TO ADMIT INTO  
EVIDENCE THE SUPPLEMENTAL EVIDENCE FILED BY  
THE PARTIES IN ACCORDANCE WITH THE  
PROVISIONS OF THE COMMISSION'S ORDER OF MAY  
13, 2005, AS AMENDED, AND DIRECTING BRIEFING OF  
ISSUES RELATED TO SUCH SUPPLEMENTAL  
EVIDENCE**

On June 17, 2005, Complaint Counsel and Respondent separately filed supplemental evidence in accordance with the terms of the Commission's Order of May 13, 2005, as modified by the Commission's Order of June 13, 2005 (hereinafter "the supplemental evidence"). After having first consulted with each other, Complaint Counsel and Respondent each filed a response to the filing of the other, neither of which raised any objection to the admission into evidence of the supplemental evidence. The Commission has determined that it should (1) reopen the record to admit into evidence the supplemental evidence and (2) order additional briefing and other proceedings in light of the admission of such evidence. Accordingly,

**IT IS ORDERED THAT** the record in this proceeding shall be, and it hereby is, **REOPENED** to admit into evidence the supplemental evidence; and

**IT IS FURTHER ORDERED THAT:**

1. On or before August 10, 2005, Complaint Counsel and Respondent shall each file amended proposed findings of fact and conclusions of law in light of the supplemental evidence, and provide cross-references to the earlier proposed findings of the parties and to the related provisions in the Initial Decision;
2. The amended proposed findings required by Paragraph 1. of



Order

this Order shall also include the identification of any misstatements or misrepresentations of fact that may have been previously made by any person during the course of this

matter that can now be identified by reason of the supplemental evidence;

3. On or before August 10, 2005, Complaint Counsel or Respondent may file any motions seeking additional relief or inferences resulting from or relating to any alleged spoliation of evidence by Respondent; and
4. On or before August 17, 2005, Complaint Counsel and Respondent shall each file their responses, if any, to the filings required or permitted by Paragraphs 1. or 3. of this Order.

By the Commission.

Order

IN THE MATTER OF

**RAMBUS INCORPORATED****ORDER DENYING COMPLAINT COUNSEL'S PETITION  
TO MODIFY THE SCHEDULE IN THE COMMISSION'S  
JULY 20, 2005 ORDER**

On July 20, 2005, the Commission entered an order reopening the record to admit supplemental evidence and directing a schedule for briefing and other filings related to such supplemental evidence. On July 28, 2005, Complaint Counsel filed a Petition asking the Commission to suspend that schedule, in light of Rambus's ongoing production to Complaint Counsel of documents Rambus recently found on its computer back-up devices and produced to the plaintiff in *Hynix Semiconductor Inc. v. Rambus Inc.*, Dkt. No. CV 00-20905 RMW (N.D. Cal.). Complaint Counsel state that they expect to be able to file a motion to admit some of these documents into the record of this proceeding by September 9, 2005, and request that the Commission postpone the briefing directed by the July 20 Order until a time at which such briefing could also address any documents produced by Rambus in the *Hynix* litigation which may be admitted into the record. In its July 29, 2005 Response, Rambus does not object to suspending the July 20 Order schedule, but indicates that it will oppose a subsequent motion to reopen the record to admit supplemental evidence from the *Hynix* litigation.

Completeness of the record, burden to the parties, and expeditious disposition of matters pending before the Commission must be balanced in order to resolve the issues raised by this Petition. The Commission does not, on balance, believe that delaying its consideration of the supplemental evidence that has already been admitted to the record of this proceeding is warranted and has, therefore, determined that the July 20 Order schedule for the briefing of issues related to that supplemental evidence should not be modified. While Complaint Counsel may at a future date seek to reopen the record to admit additional documents currently

Order

being produced by Rambus in discovery in the *Hynix* litigation,<sup>1</sup> there is no need to suspend the briefing of issues related to documents already admitted into the record. Accordingly,

**IT IS ORDERED THAT** Complaint Counsel's Petition to Modify the Schedule in the Commission's July 20, 2005 Order be, and it hereby is, **DENIED**.

---

<sup>1</sup> This disposition of the Petition should not be construed to express any view on whether the record can or should be reopened at a later date to admit materials that are currently being produced by Rambus in discovery in the *Hynix* litigation.

Order

IN THE MATTER OF

**KENTUCKY HOUSEHOLD GOODS CARRIERS  
ASSOCIATION, INC.****ORDER DENYING RESPONDENT'S MOTION FOR  
RECONSIDERATION OR, IN THE ALTERNATIVE, FOR  
A STAY OF FINAL ORDER PENDING REVIEW BY U.S.  
COURT OF APPEALS**

On July 20, 2005, Respondent Kentucky Household Goods Carriers Association, Inc. ("Kentucky Association") moved the Commission for reconsideration of its June 21, 2005 final order in this case, in light of proceedings that have taken place before the Kentucky Transportation Cabinet ("KTC") with regard to a tariff filing by the Kentucky Association proposing a rate increase.<sup>1</sup> Respondent argues that these proceedings demonstrate that the KTC's current procedures for reviewing the Kentucky Association's collective rate-making satisfy the "active supervision" requirement of the state action defense. In the alternative, Respondent seeks a stay of the Final Order pending review by an appropriate court of appeals. Complaint Counsel opposes Respondent's motion. For the reasons stated below, we deny Respondent's motion in its entirety.

**I. Motion for Reconsideration**

Pursuant to Commission Rule 3.55, 16 C.F.R. § 3.55, a petition for reconsideration "must be confined to new questions raised by the decision or final order and upon which the petitioner had no opportunity to argue before the Commission." As the Commission has previously stated:

---

<sup>1</sup> Respondent's motion is cited herein as "Resp. Mot."

Order

This standard recognizes that litigation must end at some point, and that decision makers must render their judgment based on a finite body of evidence. We thus view reconsideration of a fully-litigated opinion and order as an “extraordinary remedy which should be used sparingly.”

*Chicago Bridge & Iron Co. N.V.*, Dkt. No. 9300, 2005 FTC LEXIS 70, at \*6 (May 10, 2005) (citation omitted).

Respondent’s argument – that proceedings at the KTC with respect to the Kentucky Association’s most recent proposed rate increase (Special Supplement No. 86) demonstrate active supervision by the KTC – is not a new question raised by our decision and final order in this case. On the day of oral argument before the Commission, Respondent filed a motion for a stay, in which it argued that the KTC’s adoption of new procedures and the KTC’s actions with regard to Special Supplement No. 86 demonstrated active state supervision.<sup>2</sup> The Commission’s opinion specifically considered and rejected this argument. The Commission concluded that, although the KTC had taken some “initial steps” to augment its level of supervision over the Kentucky Association’s collective rate-making, Respondent had failed to show that the KTC’s new procedures satisfied the active supervision requirement articulated by the Supreme Court in *FTC v. Ticor Title Ins. Co.*, 504 U.S. 621 (1992), and other relevant decisions. Opinion (“Op.”) at 27. The Commission stated:

Most importantly, Respondent has not shown with precision what information the KTC will require to support proposed rate adjustments and what criteria the KTC will apply to assess the reasonableness of proposed rate adjustments. These are not questions

---

<sup>2</sup> See Respondent’s Motion for a Stay of Proceedings Pending Action by Kentucky Transportation Cabinet, filed on Jan. 24, 2005 (hereinafter cited as “1/24/05 Mot. for Stay”).

## Order

that are likely to be answered satisfactorily merely by awaiting the KTC's action with regard to the Kentucky Association's most recent tariff filing. Rather, as Respondent itself has indicated, development of a new program of supervision will take some time.

*Id.* at 27-28.

In its present motion, Respondent asserts that proceedings at the KTC that have taken place since Respondent filed its prior motion for a stay warrant reconsideration of the Commission's decision. However, a motion that "merely seeks to provide additional factual support for a position that Respondent[] ha[s] already argued . . . does not meet the mandatory requirement of Rule 3.55 that the petition present only new questions raised by Commission decisions or orders." *Chicago Bridge & Iron Co.*, 2005 FTC LEXIS 70, at \*9. *See also Novartis Corp.*, Docket No. 9279, 1999 FTC LEXIS 212, at \*1 (July 2, 1999) (denying a petition for reconsideration where the respondent "could have introduced the recent factual developments upon which it now relies before this late stage").

Moreover, the materials submitted here by Respondent suffer from the same shortcomings as the materials upon which Respondent based its prior motion for a stay. Although the KTC has conducted a hearing on the Kentucky Association's proposed rate increase, it apparently has yet to issue a decision on the matter. Thus, we still do not know what analysis the KTC will undertake or what criteria it will apply to assess the reasonableness of the proposed rate increase. Also, the materials submitted by Respondent do not clearly indicate what information the KTC will require to support the proposed rate increase. It is not clear, for example, whether the KTC will consider the information provided at the hearing regarding the costs of a single "test case" – the moving company operated by the Kentucky Association's president – to be adequate to justify the general rate increase proposed by the Kentucky Association. And although the

Order

hearing transcript indicates that the KTC has received some sort of financial statement from movers, no information is given regarding what information is contained in these financial statements. We thus conclude that Respondent has not met its burden under our rules for reconsideration of the decision and final order issued in this case. We therefore deny this portion of Respondent's motion under Commission Rule 3.55.

## II. Motion for a Stay

Section 5(g) of the Federal Trade Commission Act, 15 U.S.C. § 45(g)(2), provides that Commission adjudicative orders (except divestiture orders) take effect "upon the sixtieth day after" their date of service, unless "stayed, in whole or in part and subject to such conditions as may be appropriate, by . . . the Commission" or "an appropriate court of appeals." A party seeking a stay must first apply for such relief to the Commission, as Respondent has done here. *California Dental Ass'n* ("CDA"), Docket No. 9259, 1996 FTC LEXIS 277, at \*2 (May 22, 1996).

Pursuant to Commission Rule 3.56(c), 16 C.F.R. § 3.56(c), a motion for a stay must address the following four factors: (1) "the likelihood of the applicant's success on appeal;" (2) "whether the applicant will suffer irreparable harm if a stay is not granted," (3) "the degree of injury to other parties if a stay is granted," and (4) "why the stay is in the public interest." Rule 3.56(c) further provides that a motion for a stay must be supported by "supporting affidavits or other sworn statements, and a copy of the relevant portions of the record." *Id.* See *Toys "R" Us, Inc.*, Docket No. 9278, 1998 FTC LEXIS 224, at \*2 (Dec. 1, 1998). Here, none of the four factors supports Respondent's motion.

### A. Likelihood of Success on Appeal

Respondent's assertions of a likelihood of success on appeal merely revisit arguments that the Commission already considered and rejected in its June 21, 2005 opinion. Respondent's principal assertion is that the Commission failed to accord proper

## Order

significance to the KTC's intervention in this case and views regarding the adequacy of its level of supervision over collective rates. Resp. Mot. at 5.<sup>3</sup> As the Commission stated in its opinion, however, "the objective facts – rather than the state's opinion – determine whether the active supervision standard is met." Op. at 22 n.20. The Commission explained that:

the Supreme Court has made clear [that] states do not have unfettered discretion to determine the level of regulatory oversight that is adequate when competition has been displaced. Rather, protection from the federal antitrust laws will be granted only when the state has substituted a program of active supervision for the economic constraints of the competitive market.

*Id.* at 22 (citing *California Retail Liquor Dealers Ass'n v. Midcal Aluminum, Inc.*, 445 U.S. 97, 106 (1980)). The Commission also noted that Respondent's argument regarding the significance of the KTC's intervention was further undercut by the Commonwealth of Kentucky's submission of an *amicus* brief expressing its view that the initial decision finding no active state supervision did not conflict with state law or public policy. *Id.* at 22 n.20. Respondent offers no reason for us to question our decision on any of these points, and Respondent's renewal of its prior arguments, without more, is insufficient to justify the grant of a stay. See *Novartis Corp.*, 128 F.T.C. 233, 234 (1999); *Toys "R" Us*, 1998 FTC LEXIS 224, at \*4.

Although previous Commission decisions have held that a stay may be appropriate where the case involves difficult legal

---

<sup>3</sup> Respondent also asserts, without elaboration or explanation, that it believes the Commission wrongly interpreted the legal standards for "active supervision" contained in the Supreme Court's decisions in *Ticor* and *Midcal*. Resp. Mot. at 6.



Order

questions or a complex factual record,<sup>4</sup> this is not such a case. As the Commission stated in its opinion:

This is not a difficult case in which we are called upon to decide whether a state's implementation of certain supervisory steps but not of others satisfies the active state supervision requirement. Where, as here, the relevant state agency has not taken any of the steps that courts have identified as indicia of active supervision, it is clear that the state has not exercised "sufficient independent judgment and control so that the details of the rates or prices have been established as a product of deliberate state intervention." *Ticor*, 504 U.S. at 634-35. This conclusion is all the more compelling when the state agency has not taken the steps that the state legislature itself has identified as important for a determination of whether rates are reasonable.

Op. at 19. Under these circumstances, we find that Respondent's arguments on the merits do not support the grant of a stay.

### **B. Irreparable Harm to Respondent**

Respondent bears the burden of demonstrating that denial of a stay would cause it irreparable harm. "Simple assertions of harm or conclusory statements based on unsupported assumptions will not suffice. A party seeking a stay must show, with particularity, that the alleged irreparable injury is substantial and likely to occur absent a stay." *CDA*, 1996 FTC LEXIS 277, at \*6-7. *Accord Novartis*, 128 F.T.C. at 235; *Toys "R" Us*, 1998 FTC LEXIS 224, at \*7.

---

<sup>4</sup> *Novartis*, 128 F.T.C. at 234-35; *Toys "R" Us*, 1998 FTC LEXIS 224, at \*5; *CDA*, 1996 FTC LEXIS 277, at \*10.

## Order

Respondent asserts that if a stay is not granted and the Kentucky Association is prohibited from filing a collective tariff, it will go out of business because it is not in a position to file individual tariffs on behalf of its members, and its non-tariff activities are insignificant in nature. Resp. Mot. at 7. Respondent also asserts that its members will be irreparably injured because they will have to file individual tariffs – an undertaking “which few understand and fewer can perform in a professional and competent manner.” *Id.* However, Respondent provides no specific factual support for these assertions. Also, Respondent’s claim that the preparation of individual tariffs is necessarily a burdensome and complex undertaking would seem to be undercut by evidence in the record that movers in Kentucky who do not participate in the Kentucky Association’s tariff have been allowed to file, and do file, very simple individual tariffs. CX 116 (Debord, Dep. II at 18). Accordingly, we find that Respondent has not met its burden of showing irreparable harm.

**C. Harm to Others and the Public Interest**

Because Complaint Counsel represents the public interest in effective law enforcement, we consider the third and the fourth factors together. *See Novartis*, 128 F.T.C. at 236.

Respondent contends that if a stay is not granted and the Kentucky Association’s tariff is cancelled, the KTC and the moving public will be harmed because the KTC likely will be unable to handle the increased number of individual tariff filings on such short notice; many movers will either fail to file tariffs or will file tariffs that do not comply with state law; and confusion regarding applicable rates will provide greater opportunity for unscrupulous movers to engage in fraudulent conduct. Resp. Mot. at 7-8. Respondent made similar claims of harm in its prior motion for a stay. At that time, the Commission concluded that “there is no reason to believe that either the state’s entire system for regulating movers’ rates or the interests of the moving public will be in jeopardy” as a result of the final order. Op. at 27. Now, as then, Respondent has provided no support for its predictions of

Order

harm if a stay is not granted. Moreover, because the prohibitions against the Kentucky Association's collective rate-making contained in the Commission's final order do not take effect until 120 days after entry of the order, *see* Final Order ¶¶ II and III, the order gives considerable time for the KTC and movers in Kentucky to prepare for the transition to individual tariff filings.<sup>5</sup>

Further, as we stated in our opinion, if and when the KTC implements a program to exercise greater supervision over household goods carrier rates, Respondent can apprise the Commission of these changed circumstances in a petition to reopen the proceeding and modify or set aside the Commission order, pursuant to Commission Rule 2.51. Op. at 28. The Commission will then consider whether the new evidence sufficiently demonstrates active state supervision.

Respondent also argues that a stay of the final order is appropriate here because there is no evidence that the rates in the Kentucky Association's tariff are unreasonable or that Kentucky's regulatory program has actually caused economic harm. *Id.* at 8-9. These arguments, however, are contrary to well settled principles of antitrust law that agreements among competitors to set prices are *per se* unlawful precisely because "their nature and necessary effect are so plainly anticompetitive," *National Soc'y of Prof'l Eng'rs v. FTC*, 435 U.S. 679, 692 (1978); and that "[i]t is no excuse that the prices fixed are themselves reasonable," *Catalano, Inc. v. Target Sales, Inc.*, 446 U.S. 643, 647 (1980). *See Ticor*, 504 U.S. at 639 ("No antitrust offense is more

---

<sup>5</sup> Although there is testimony in the record that, at the KTC's existing level of staffing (*i.e.*, one employee), it would be difficult for the KTC to process a large number of individual tariffs, CX 116 (Debord, Dep. II at 9), materials submitted by Respondent in support of its prior motion for a stay indicate that the KTC is already taking steps to increase the number of personnel responsible for reviewing tariffs. *See* 1/24/05 Mot. for Stay, Ex. K.

Order

pernicious than price fixing.”). In this case, the Commission found that:

year after year, the KTC has allowed the Kentucky Association and its members to raise rates with virtually no examination of the merits of these rates. The brunt of these anticompetitive practices is being borne by consumers in Kentucky, and until the Kentucky Association can demonstrate that the state has in place a program of active supervision to ensure the reasonableness of collective rates, a cease and desist order is necessary to protect the interests of consumers, notwithstanding any hardship to Respondent and its members.

Op. at 26. Under these circumstances, we find that consideration of the harm to consumers and the public interest weighs against the grant of a stay.<sup>6</sup>

### Conclusion

We find that Respondent has not met its burden under our rules for reconsideration of the Commission’s decision in this case. We also find that the relevant factors do not support a stay of the Commission’s final order. Accordingly,

---

<sup>6</sup> Unlike cases in which respondents have merely sought a stay of collateral provisions of a final order, Respondent here seeks a stay of the final order’s core provisions enjoining unlawful activity. *See, e.g., CDA*, 1996 FTC LEXIS 277, at \*10 (“Respondent has not sought to stay those provisions of the order that prohibit continuation of the restraints found to be unlawful. Respondent has thus attempted to minimize the harm to the public interest while focusing on the provisions that create the greatest harm to itself.”).

Order

**IT IS ORDERED THAT** Respondents' Motion for Reconsideration or, in the Alternative, for a Stay of Final Order Pending Review by U.S. Court of Appeals is **DENIED**.

Order

IN THE MATTER OF

**CHICAGO BRIDGE & IRON COMPANY N.V.****ORDER GRANTING IN PART AND DENYING IN PART  
RESPONDENTS' MOTION FOR *IN CAMERA*  
TREATMENT OF MATERIAL PREVIOUSLY  
DESIGNATED AS CONFIDENTIAL**

Pursuant to Commission Rule 3.45(b), Respondents Chicago Bridge & Iron Company N.V. and Chicago Bridge & Iron Company ("CB&I" or "the Respondents") have filed a Motion for *In Camera* Treatment of Material Previously Designated as Confidential ("the Motion"). The materials for which CB&I seeks *in camera* treatment consist of Attachment B to Complaint Counsel's Response to CB&I Respondents' Further Briefing on Specific Remedy Issues ("Response"), discussions on pages 7, 13, and 14 of the Response that were redacted from the public version of the Response, and portions of the Motion and Exhibit A of the Motion (Affidavit of David Bordages). CB&I seeks *in camera* treatment of these materials for a period of five years.

CB&I asserts that the public disclosure of this material would damage CB&I's business and the information meets the Commission's criteria for granting *in camera* treatment. Motion at 4. Complaint Counsel does not oppose Respondents' Motion to the extent it seeks *in camera* treatment for the material on pages 13 and 14 of Complaint Counsel's Response and portions of CB&I's Motion and Exhibit A of the Motion. However, Complaint Counsel point out that CB&I has not provided a justification for *in camera* treatment of the material on page 7 and Attachment B of Complaint Counsel's Response and thus argue that those materials should be placed on the public record.

The Commission finds that CB&I has satisfied the standard set forth in Commission Rule 3.45(b) for those materials on pages 13 and 14 of Complaint Counsel's Response and portions of CB&I's Motion and Exhibit A of the Motion and shown that the disclosure

Order

of this information would likely result in “clearly defined, serious injury.” 16 C.F.R. § 3.45(b). *See H.P. Hood & Sons, Inc.*, 58 F.T.C. 1184, 1188 (1961); *Bristol-Myers Co.*, 90 F.T.C. 455, 456 (1977); *General Foods Corp.*, 95 F.T.C. 352, 355 (1980).

Although we recognize that Respondents have not established that Attachment B to Complaint Counsel’s Response meets this standard, the Commission believes this failure may have been inadvertent, and we have therefore granted *in camera* status for six months for this material. At the end of this period, CB&I may move to have the *in camera* period extended or, in the absence of such a motion, the material will be unsealed. The Commission has determined to make public the material on page 7, which merely references [ REDACTED ].

This material is available from public sources and therefore is not eligible for *in camera* status. *See Tr.* at 2957-58, 6869-73.

Finally, the Commission is not persuaded that *in camera* treatment should be granted for the five-year period requested by CB&I.

The information for which such treatment is being granted is temporal in nature, and its competitive sensitivity is likely to diminish over time. The Commission thus believes that a two-year period is appropriate.

Accordingly,

**IT IS ORDERED THAT** the material on pages 13 and 14 of Complaint Counsel’s Response that was redacted from the public version of the Response and portions of CB&I’s Motion and Exhibit A thereto that were redacted in the public version of the Motion shall be afforded *in camera* treatment for a period of two years from the date of this Order, at which time Respondents may show cause why those materials should not be made public; and

**IT IS FURTHER ORDERED THAT** Attachment B to Complaint Counsel’s Response shall be afforded *in camera* treatment for a period of one hundred and eighty days from the date of this Order, at which time Respondents may show cause why those materials should not be made public; and

Order

**IT IS FURTHER ORDERED THAT** Respondents' Motion is DENIED to the extent it seeks *in camera* treatment for the material on page 7 of Complaint Counsel's Response that was redacted from the public version.



Order

IN THE MATTER OF

**CHICAGO BRIDGE & IRON COMPANY N.V.**

**ORDER CLARIFYING RESPONDENTS' OBLIGATIONS  
AS TO THE PITT-DES MOINES AND CB&I CORPORATE  
NAMES**

**I. Introduction**

The Commission's Final Order in this matter required, among other things, Respondents Chicago Bridge & Iron N.V. and Chicago Bridge and Iron Company (collectively, "CB&I") to divest intellectual property for the Relevant Products and other complementary products.<sup>1</sup> On January 31, 2005, Complaint Counsel filed a petition for reconsideration that requested the Commission to modify its Final Order to make clear that only the divested entity will have rights to the PDM corporate names and CB&I will retain its rights in the CB&I corporate names.<sup>2</sup> Respondents CB&I did not oppose Complaint Counsel's Petition to the extent the petition sought to ensure that CB&I would retain all rights in its corporate name.<sup>3</sup> However, CB&I pointed out that when it acquired PDM's Engineered Construction ("EC") and Water Divisions, it received only a "one-year, non-renewable,

---

<sup>1</sup> Final Order, ¶¶ I.P, IV.A.

<sup>2</sup> Petition for Reconsideration to Clarify Respondents' Obligations as to the Pitt-Des Moines and CB&I Corporate Names, filed January 31, 2005 ("Complaint Counsel's Petition").

<sup>3</sup> Response to Complaint Counsel's Petition for Reconsideration to Clarify Respondents' Obligations as to the Pitt-Des Moines and CB&I Corporate Names, filed Feb. 10, 2005 ("CB&I's Response").

Order

non-exclusive transitional license to the use of the PDM mark.”<sup>4</sup> As a result, CB&I has no rights in PDM’s corporate name to transfer. Because we had concerns that the acquirer of the divested assets might need to use the CB&I and PDM tradename and marks to compete effectively, we ordered both PDM and CB&I to submit briefs addressing the feasibility and consequences of granting a license to their respective corporate names.

## II. PDM’s Tradename and Marks

PDM’s brief<sup>5</sup> states that when PDM sold its various divisions, it entered into covenants not to compete that impact the use of the PDM tradename and marks and suggests that obtaining waivers from some of those buyers might be advisable.<sup>6</sup> These covenants notwithstanding, however, the brief concludes that PDM likely owns the right to use the tradename “Pitt-Des Moines” and the marks “PITT-DES MOINES” and “PDM” in connection with the

---

<sup>4</sup> *Id.* at 2.

<sup>5</sup> Pitt-Des Moines, Inc. Briefing on Complaint Counsel’s Motion for Clarification, filed Apr. 6, 2005 (“Pitt-Des Moines Brief”).

<sup>6</sup> For example, in connection with PDM’s sale of its Oregon Calvert Co. to Contech Construction, PDM entered into a covenant not to compete with “any business, venture or activity engaged anywhere in the world in the Oregon Culvert Business under the names . . . ‘Pitt-Des Moines, Inc.’” through January 31, 2006. *Id.* at 4. The brief also states that the sale of PDM’s steel bridge division to Steel Bridges may impact PDM’s rights to the PDM mark and concludes that consent of Steel Bridges (and the bridge lender that holds a security interest in the same property) is advisable. *Id.* at 9-12.

Order

EC and Water Division businesses.<sup>7</sup> It thus states that PDM would be “in a position to sell or license, for reasonable consideration, such rights, either for a limited or unlimited period of time.”<sup>8</sup>

Because reputation can play a role in a tank supplier’s ability to compete in the Relevant Markets, we direct the Monitor Trustee to include in his final report to the Commission a recommendation as to whether a license to the PDM tradename and marks is necessary to allow the acquirer to compete effectively in the Relevant Markets. In making his recommendation about the acquirer’s needs for access to the PDM tradename or marks, the Monitor Trustee should ascertain whether the acquirer’s ability to bill itself as a successor to PDM necessarily depends on the use of the PDM name or marks.

For purposes of finality, we wish to make clear what the terms of such a license would be. If the Commission determines, based on the Monitor Trustee’s recommendation, that a license to the PDM name and marks is necessary for the acquirer to compete effectively in the Relevant markets, this Order requires PDM to grant to the acquirer of the divested assets a perpetual, worldwide, exclusive, royalty-free license to all the rights it has in its tradename or marks for use with the Relevant Products as defined in our Final Order. If the acquirer determines that it needs such a license, it would be (1) permanent rather than transitional, because PDM’s brief makes clear that it no longer uses or plans to use its tradename or marks in connection with the types of assets CB&I is required to divest under the Final Order, and (2) royalty-free, because PDM is not currently obtaining any revenue from the use

---

<sup>7</sup> *Id.* at 13.

<sup>8</sup> *Id.*

## Order

of its tradename or marks, and it is questionable whether it could do so in the future given certain restrictions it agreed to when it sold its EC and Water Divisions to CB&I.<sup>9</sup>

We also order CB&I to grant to the acquirer at no cost a waiver of Section 2.1.6. of the CB&I Asset Purchase Agreement as well as any other provision of that agreement that would hinder the acquirer from using the PDM tradename or marks for the Relevant Products.

The PDM brief also notes that after its April 2002 merger with Ironbridge Acquisition and subsequent name change to Ironbridge Corp., the company has used its tradename only in connection with winding-up its business. Because PDM derives no ongoing revenue from the use of the PDM mark, the brief suggests that the mark may be subject to claims of abandonment. This Order therefore prohibits CB&I from pressing any such claim or in any way interfering with the Commission-approved acquirer's use of the PDM tradename or marks for those assets defined as the Relevant Products.

### III. CB&I's Tradename and Marks

CB&I argues that it is not feasible to license the CB&I corporate name to the purchaser of the divested assets. Among other things, CB&I asserts that a transitional license would subject CB&I's reputation to risk and result in market confusion because CB&I will remain in the market. We agree with CB&I that

---

<sup>9</sup> PDM agreed not to allow "any successor or person which in competition with CB&I or its affiliates, sells, markets, distributes or deals in all or any portion of the Engineered Construction/Water Division Business to use, the names 'Pitt-Des Moines' or 'PDM,' or any variation materially derived therefrom, in connection with any business which is competitive to all or any portion of the Engineered Construction/Water Division Business." *Id.* at 6.

Order

having multiple competitors in the relevant markets – each of which could hold itself out as CB&I – would undoubtedly lead to market confusion. In addition, because we have required PDM to license its tradename and marks, if necessary, we have determined that a permanent license to the CB&I tradename is unnecessary to allow the acquirer to compete effectively in the relevant markets. Nonetheless, we do find that a limited, transitional license to the CB&I tradename and marks is necessary to ensure that the acquirer may immediately begin to use the divested assets. We emphasize here that the intent of this transitional license is not to allow the acquirer to hold itself out as CB&I in any way. Rather, its purpose is to allow the acquirer to immediately use the divested assets that bear CB&I tradename and marks or conduct other functions necessary to conducting the Relevant Business.

Accordingly,

**IT IS ORDERED THAT** the Monitor Trustee include in his final report to the Commission concerning the sale of the divested assets a recommendation with respect to whether a license of the PDM tradename or marks should be included in the divested assets in order to accomplish the purpose of the Final Order; and

**IT IS FURTHER ORDERED THAT** to the extent the Commission determines, based on the Monitor Trustee's recommendation, that a license to the PDM name and marks is necessary for the Commission-approved acquirer to compete effectively in the Relevant Markets, PDM shall grant to the Commission-approved acquirer a perpetual, worldwide, exclusive, royalty-free license to all rights it has in its tradename and marks for the purpose of engaging the Relevant Products; and

**IT IS FURTHER ORDERED THAT** CB&I is prohibited from pressing any claim of abandonment or in any way interfering with the Commission-approved acquirer using the PDM tradename or marks for those assets defined as the Relevant Products; and

Order

**IT IS FURTHER ORDERED THAT** CB&I grant to the acquirer at no cost a waiver of Section 2.1.6. of the CB&I Asset Purchase Agreement as well as any other provision of that agreement that would hinder the acquirer from using the PDM tradename or marks for the Relevant Products; and

**IT IS FURTHER ORDERED THAT** CB&I grant to the Commission-approved acquirer a license, not to exceed one-hundred and eighty (180) days, to use the corporate names “Chicago Bridge & Iron” and “CB&I,” and any related corporate, firm, or company names to the extent necessary to achieve the purpose of, and to assure compliance with, this Order.

Order

IN THE MATTER OF

**CHICAGO BRIDGE & IRON COMPANY N.V.**

**ORDER GRANTING IN PART AND DENYING IN PART  
RESPONDENTS' PETITION FOR RECONSIDERATION  
OF THE FINAL ORDER**

**I. Introduction**

On December 21, 2004, we issued a Final Order in this matter and found that Chicago Bridge & Iron Company N.V. and Chicago Bridge & Iron Company (collectively "CB&I" or "Respondents") acquired certain assets from Pitt-Des Moines, Inc. ("PDM") in violation of Section 5 of the Federal Trade Commission Act, 15 U.S.C. § 45, and Section 7 of the Clayton Act, 15 U.S.C. § 18. Accordingly, we ordered CB&I to reorganize its Industrial Division (and to the extent necessary its Water Division) into two, separate stand-alone divisions and divest one of them.

On February 1, 2005, CB&I filed a Petition to Reconsider the Opinion and Order in Light of Entry After the Close of the Record and Overbreadth ("Respondents' Petition"). Among other things, Respondents' Petition argued that the definition of Relevant Business – which defines the scope of assets that CB&I must divest – is too broad and potentially encompasses every project CB&I constructs. Respondents' Petition also requested that the Commission modify the Final Order to make clear that the relief does not extend beyond CB&I's domestic business and contracts. On May 10, 2005, we ordered Respondents to file a brief identifying those assets encompassed in the Relevant Business definition that are unnecessary to compete effectively in the Relevant Markets. We also directed Respondents to identify those

## Order

assets outside of the United States the Relevant Business definition includes and explain why those assets are unnecessary for an effective divestiture.<sup>1</sup>

Respondents have now filed their brief,<sup>2</sup> in which they argue that the Relevant Business definition includes certain assets that were not part of PDM's business and are therefore not necessary for an effective divestiture. For the reasons we discuss below, we find that Respondents have not presented sufficient evidence to rebut our initial findings that such assets are necessary for an acquirer to compete effectively in the Relevant Markets. We therefore deny Respondents' motion to narrow the scope of the Order.<sup>3</sup>

In addition, Respondents' brief argues that the Relevant Business definition in the Order should be limited to CB&I's domestic assets, because the Commission focused on competition only in the United States and CB&I acquired almost no foreign assets from PDM. We clarify here that the Order's Relevant Business definition does not require CB&I to equally divide its

---

<sup>1</sup> Decision and Order Partially Denying Respondents' Petition for Reconsideration and Directing Further Briefing on Specific Remedy Issues, issued May 10, 2005 ("Reconsideration Order").

<sup>2</sup> Respondents' Further Briefing on Specific Remedy Issues, filed June 6, 2005 ("Respondents' Brief").

<sup>3</sup> This Order uses the following abbreviations for citations to the record:

Tr. – Transcript of testimony before the  
Administrative Law Judge  
CX – Complaint Counsel's Exhibit  
Op. – Commission Opinion issued December 21,  
2004 (*in camera*).



Order

foreign assets. However, because evidence suggests that some foreign assets may be necessary for an effective divestiture to the extent that they provide an acquirer with a sufficient scale of work, we have included a provision to make certain that such assets are available if necessary. Finally, we reject Respondents' alternative suggestions for redefining the scope of the Order's divestiture requirements.

## II. The Scope of the Order

Respondents' chief explanation as to why the Order's divestiture requirement is too broad is that CB&I's business "has always exceeded the scope of PDM's EC [Engineered Construction] Division" and that these "other businesses were not and are not an integrated part of its U.S. tank business." Specifically, Respondents state that "CB&I's projects include not only construction of the Relevant Products and water tanks, but also hydrocarbon processing plants, offshore structures, pipelines, hydrocarbon storage tanks, and other steel structures and their associated systems."<sup>4</sup> According to Respondents, these complementary assets are unnecessary to compete in the Relevant Markets. Respondents thus seek the Commission to clarify that the assets subject to divestiture do not exceed those used in the Relevant Markets and water tank business.<sup>5</sup>

---

<sup>4</sup> Respondents' Brief at 4.

<sup>5</sup> We note that this position is inconsistent with the position Respondents took at trial. Specifically, Respondents' closing argument stated that "the companies have been fully integrated at the management level, at the engineering level, at the fabrication level, at the field erection level, every level, purchasing, estimating." Tr. at 8311. Respondents also noted that CB&I and PDM prior to the acquisition each made numerous products in addition to the Relevant Products and argued that as a result if the Commission were to "spin off some personnel and assets to make products in these [relevant] markets, that company

## Order

While we agree with Respondents' general point that the Commission's Order should not require CB&I to divest assets that are unnecessary to allow an acquirer to compete effectively in the Relevant Markets, we find that Respondents' arguments for narrowing the scope of the Order are not supported by the facts. PDM's Offering Memorandum states that PDM specialized in the "design, engineering, fabrication, field erection and repair of bulk liquid terminals, storage tanks, process vessels, low temperature and cryogenic storage facilities, and other steel plate structures and their related systems."<sup>6</sup> It is thus clear that PDM's EC Division did not focus solely on the design and construction of the Relevant Products but rather on numerous products and services. In addition, PDM's 2000 Business Plan makes clear that PDM's EC Division participated in the hydrocarbon industry<sup>7</sup> and targeted, among other things, pipeline, terminal, and processing plant projects.<sup>8</sup> Furthermore, CB&I's analysis of the acquisition

---

would wilt like a rose left out too long." *Id.* They added that the Relevant Products did not have enough business and that the Commission would therefore need to include "all this other stuff to make flat bottom tanks, to make gravel tanks, to make all kinds of other stuff." Tr. at 8311-12.

<sup>6</sup> CX 522 at TAN 1003379.

<sup>7</sup> CB&I's CEO testified that the hydrocarbon industry is the oil and gas business. Tr. at 4158.

<sup>8</sup> CX 94 at HOU017570 -71 (analyzing the markets in which PDM participated, including "Domestic Petroleum, Petrochemical, Industrial Gas, & Chemical" and specifically discussing refinery and tank projects); *Id.* at HOU017572-73 (discussing pipeline expansion and terminal projects). See also CX 850 at HOU019220 (tracking 2000 sales in the following market segments: Aerospace, LPG, Liquid Elements of Air (LIN/LOX), LNG, Thermal Energy Storage, Wastewater, Power, Terminals, Petroleum/Chemical, and Transportation); CX 1033 at

Order

specifically notes PDM's involvement in the petroleum and petrochemical industries and states that the PDM assets would provide CB&I with "substantial exposure to [the] upturn in [the] hydrocarbon industry."<sup>9</sup> This evidence suggests not only that PDM was actively engaged in the types of complementary products Respondents seek to exclude but also that CB&I specifically evaluated PDM's involvement in these areas and concluded that acquiring PDM assets would enhance their competitive position in them.

In addition, the business practices of both PDM and CB&I suggest that the Relevant Business definition should include assets related to the complementary products. As we have discussed, a single business unit of PDM constructed both the Relevant Products and the complementary products prior to the acquisition.<sup>10</sup> Similarly, CB&I's Industrial Division, which is responsible for designing and constructing the Relevant Products, was engaged in designing and building the types of complementary projects Respondents identify.<sup>11</sup> Once CB&I

---

3-4, (CB&I 10-K noting that PDM "specialize[d] in the design and engineering, fabrication and construction of products for the petroleum, petrochemical, cryogenic, liquified natural gas, defense and aerospace industries, as well as water storage and treatment facilities").

<sup>9</sup> CX 32 at 1.

<sup>10</sup> *See e.g.*, Tr. at 2906 (Scorsone [former head of PDM's EC division and current head of CB&I's Industrial Division] testifying that PDM's EC division "constructed facilities for the petroleum, petrochemical, natural gas, and aerospace business").

<sup>11</sup> Tr. at 4843-44 (Scorsone testifying that in addition to the Relevant Products, CB&I's Industrial Division and PDM's EC division "constructed virtually any type of structure out of

## Order

acquired the PDM assets, it integrated all of the PDM assets into the Industrial Division, which continued to design and construct projects for both the Relevant Products and those complementary products Respondents seek to exclude.<sup>12</sup> Moreover, CB&I's CEO testified that within the Industrial Division, CB&I's engineers work on both projects related to the Relevant Markets and other projects, including flat bottom tanks to store hydrocarbons and flat bottom tanks to serve water needs.<sup>13</sup> This evidence, coupled with the fact that projects in the Relevant Markets "seldom come along,"<sup>14</sup> supports the conclusion that the complementary products provide the necessary scale of work to ensure that an acquirer can compete effectively. This conclusion is further supported by the testimony of CB&I's CEO, who stated that CB&I would not reduce its engineering capacity or its project manager force in response to a 25% loss of its business in the Relevant Markets because of the "small amount of activity required to respond to the market[s]."<sup>15</sup>

---

plate steel," including "ambient-temperature flat-bottom storage tanks, pressure spheres, field-erected pressure vessels, specialty-type plate structures, bins, hoppers, aqueducts, [and] wind tunnels"). *See also* Tr. at 4807 (Scorsone testifying that CB&I's "tank-building resources are fluid throughout all of [CB&I's] organizations," including the Industrial and Water Divisions).

<sup>12</sup> See CX 1033 at 44 (CB&I 10-K noting that PDM's EC and Water Division assets have been integrated with CB&I's business units); Tr. at 4081 (Scorsone noting that CB&I hoped to achieve efficiencies by eliminating duplication in fabrication capability, construction equipment and tools, sales people, sales offices, and other facilities).

<sup>13</sup> Tr. at 4058.

<sup>14</sup> Tr. at 4159.

<sup>15</sup> Tr. at 4159. We recognize that at least one of the Relevant Markets – the LNG tank Market – has seen an increase

Order

We are mindful that the complementary products identified by Respondents comprise a significant component of CB&I's business.<sup>16</sup> However, Respondents have not convinced us that these assets are unnecessary to a divestiture of an entity that will be economically viable and a competitive force in the Relevant Markets.<sup>17</sup> Without such evidence, we cannot narrow the scope of assets subject to divestiture solely to those assets used in the

---

in demand since the acquisition. However, Respondents have presented no evidence to suggest that this increased demand has diminished the need for an LNG supplier to have the ability to perform other types of projects to have a sufficient scale of business.

<sup>16</sup> CX 1033 at 41 (“Projects for the worldwide petroleum and petrochemical industry accounted for approximately 60-70% of [CB&I's] revenues in 2001, 2000, and 1999.”)

<sup>17</sup> We recognize that the lines of business that the Order requires CB&I to divest may not precisely match those it acquired from PDM. For example, it appears that PDM did not perform turnaround work or construct refinery vessels. CX 108 at PDM-HOU00518. Similarly, it does not appear that PDM was engaged in building “offshore structures,” another type of asset identified by Respondents' brief. Respondents' Brief at 4. However, the record establishes that PDM was engaged in a broad range of products and services in the same industries that CB&I identifies as problematic and that these other projects may be necessary to provide an acquirer with a viable scale of business. CB&I has not provided any evidence on the amount of CB&I's revenues that these assets represent, or any evidence as to the specific hardship that a divestiture of these assets would create for CB&I. Consequently, CB&I has not provided specific evidence to persuade us that these assets are unnecessary for an effective divestiture. We therefore have not excluded these assets from the scope of the Order.

## Order

Relevant Markets and water tank business – especially where we have found that other evidence demonstrates that the complementary assets may be necessary to allow an acquirer to compete effectively in the Relevant Markets. This Order clarifies, however, that if the acquirer already has the necessary assets to compete effectively, CB&I need not include the complementary assets.<sup>18</sup>

In addition to their more general objections to the Order’s scope, Respondents argue that some of the Order’s language must be modified because it sweeps in a whole range of products that are “unnecessary for an effective and complete divestiture.”<sup>19</sup> Specifically, Respondents take issue with the part of the Order that requires CB&I to divest certain assets related to any “industrial process system, including but not limited to any digester, absorber, reactor, and tower.”<sup>20</sup> According to Respondents, the term “industrial process system” must be limited to the tank business to avoid overreaching.

We find that this argument reads the Order’s divestiture requirement far too broadly. The “including but not limited to” language in the Order<sup>21</sup> suggests CB&I need not necessarily include those assets not enumerated by the Order so long as the divestiture package allows an acquirer to compete effectively in the Relevant Markets. To the extent Respondents are arguing that the Order should not include assets beyond those used in the

---

<sup>18</sup> ¶ IV.A. of the Final Order allows the acquirer and monitor trustee to agree to exclude any of the complementary assets if they find them unnecessary for the acquirer to compete effectively in the Relevant Markets.

<sup>19</sup> Respondents’ Brief at 7.

<sup>20</sup> Final Order, ¶ I.P, Respondents’ Brief at 6-7

<sup>21</sup> See Final Order, ¶ I.P.

Order

Relevant Markets, we must reject their argument for the reasons similar to those we have just discussed. The record establishes that PDM participated in the types of industrial process systems enumerated in the Order's language. Furthermore, the evidence discussed above makes clear that an acquirer needs the capability to perform projects other than those in Relevant Markets to compete effectively in those markets. Given these facts, we are unpersuaded that the assets in question are unnecessary for an effective divestiture and the inclusion of those assets will hinder CB&I's ability to compete in the Relevant Markets. Respondents have not provided sufficient evidence to establish that the Order's language includes unnecessary assets or explained any specific concerns related to the divestiture of those assets. We therefore deny Respondents' request to modify the Order.<sup>22</sup>

Finally, Respondents argue that the Order should be clarified to exclude the divestiture of assets outside of the United States. Respondents rightly point out that the Commission's Opinion focused on competition in the U.S. markets, and we agree that U.S. assets are crucial to competing in the U.S. Product Markets. We therefore clarify that the focus of the Opinion and Order are CB&I's U.S. assets. However, the possibility exists that some foreign assets may be necessary for an acquirer to compete effectively. For example, in its analysis of the PDM acquisition,

---

<sup>22</sup> In addition, Respondents argue that the Order should be modified to exclude "steel plate fabrication and specialty structures" not relevant to the tank business. Respondents' Brief at 7. Respondents admit, however, that these types of assets were acquired from PDM. *Id.* Although we found that the ability to fabricate nine percent nickel steel was not an entry barrier to the LNG tank market, we noted that such facilities may be helpful in other relevant Markets. *Op.* at 41 n.249. Because Respondents have not presented any evidence to suggest that those types of assets acquired from PDM are not necessary to compete in the Relevant Markets, we must reject Respondents' argument.

## Order

CB&I noted that PDM's EC international operations comprised approximately 45% of the division's revenues.<sup>23</sup> We have thus modified the Order to include language that ensures such assets are available if they are needed to ensure the viability of the Relevant Business but makes clear that CB&I need include foreign assets only to the extent they are necessary for an acquirer to compete in the Relevant Markets. We emphasize that CB&I need not equally divide its foreign assets into the two stand-alone divisions it is required to create under the Order.

### III. Respondents' Alternative Suggestions

As an alternative to the Order, Respondents suggest that the [ ]<sup>24</sup> It is unclear from this language exactly what package of assets Respondents propose for a divestiture – especially where PDM was engaged in the design and construction of many of the assets that Respondents argue should be excluded from the

---

<sup>23</sup> CX 32 at 3.

<sup>24</sup> Respondents also argue that the tangible assets described in the Offering Memorandum – three U.S. tool and construction equipment facilities, one fabrication plant, and related equipment – constitute the assets necessary to compete in the United States. Respondents' Brief at 4. For the reasons we discussed at length in both the Opinion and Reconsideration Order, we reject Respondents' argument. Respondents argument misses that the crucial element for success in the Relevant Markets is experience, including but not limited to having specialized procedures in place to meet the unique challenges of building the relevant products, the ability to access knowledgeable supervisors and local labor, and expertise in dealing with complex regulatory requirements. *See generally*, Op. at 33-49. Reconsideration Order at 18-21. We therefore find that the divestiture suggested by Respondents will not restore the competition from the acquisition and thus decline to narrow the Order's scope in this way.



Order

definition of Relevant Business.<sup>25</sup> Furthermore, the remedy in this case must provide the acquirer with the mix of assets necessary to compete effectively in the Relevant Markets. Because CB&I acquired the PDM assets nearly four and a half years ago and has since integrated those assets into its own operations, we cannot be certain that [ ] will provide an acquirer with the mix of assets necessary to compete with CB&I and thus to adequately restore the competition lost from the acquisition.<sup>26</sup>

---

<sup>25</sup> [

]

<sup>26</sup> The Commission has recognized that assets acquired in a transaction do not necessarily form the basis for an effective divestiture. In analyzing the divestiture in MSC.Software, for example, the Commission reasoned that “[d]ivestiture of the acquired assets alone would not restore the competitive conditions that existed before the acquisitions (the status quo ante), because the 3-year old UAI and CSAR codes are no longer as commercially viable as they were when MSC acquired them. Licensing of the current version of MSC.Nastran is required to give the acquirer or acquirers what UAI and CSAR formerly had: an up-to-date product upon which to base sales and future development efforts.” *MSC.Software Corp.*, Dkt. 9299,

Order

Nonetheless, we take Respondents' point that [ ]<sup>27</sup> The possibility exists that the acquirer will already be engaged in some of the lines of business required to be divested under the Order – or in other complementary lines of business – and thus may not need to acquire all assets within the scope of the Order. We therefore have included a provision that allows the complementary assets to be excluded if the acquirer and monitor trustee find them unnecessary and agree to exclude them.<sup>28</sup> This provision should ensure that the package of assets necessary to restore competition is not overbroad.

Accordingly,

**IT IS ORDERED THAT** Respondents' Motion to modify the Order to the extent that it seeks to narrow the scope of the Relevant Business Definition is **DENIED**; and

**IT IS FURTHER ORDERED THAT** Respondents' Motion to clarify the Order to exclude CB&I's foreign assets is **GRANTED** to the extent it seeks clarification that ¶ I.P. of the Final Order does not require CB&I to equally divide its foreign assets; and

**IT IS FURTHER ORDERED THAT** Paragraph III.A of the Order is modified to provide that "Within ninety (90) days after the date on which the Order becomes final, CB&I shall reorganize its Relevant Business into two independent, stand-alone operating divisions or subsidiaries, respectively New PDM and New CB&I, each fully, equally, and independently engaged in all aspects of the Relevant Business except that any foreign assets employed by

---

(Aug. 14, 2002)(Analysis to Aid Public Comment), available at <<http://www.ftc.gov/os/2002/08/mscsoftwareanalysis.htm>>.

<sup>27</sup> [ ]

<sup>28</sup> See Final Order, ¶ IV.A.

Order

CB&I in the Relevant Business need be allocated to New PDM or New CB&I only to the extent such assets are necessary to enable New PDM and New CB&I to engage fully, equally, and independently in all aspects of the Relevant Business and need ultimately be divested by CB&I only to the extent such assets are necessary to enable the acquirer of New PDM or New CB&I to compete effectively in all aspects of the Relevant Business”; and

**IT IS FURTHER ORDERED THAT** the monitor trustee include in his final report to the Commission concerning the sale of the divested assets a recommendation with respect to whether any foreign assets, as described in Paragraph III.A, as modified, should be included in the divested assets in order to accomplish the purpose of this Order.

Order

IN THE MATTER OF

**WHITE SANDS HEALTH CARE SYSTEM, L.L.C.,****ORDER REOPENING AND MODIFYING ORDER**

Individual respondent, James Laurenza, president of respondent Dacite, Inc. (“Dacite”), has filed, on May 31, 2005, a petition to reopen and modify the Order (“Petition”), to eliminate his obligations under Paragraph VII of the Order. Paragraph VII requires him to provide certain information, when that information is not otherwise provided by respondent White Sands Health Care System, L.L.C. (“White Sands”) or respondent Alamogordo Physicians Cooperative, Inc. (“Alamogordo Physicians”). Mr. Laurenza’s Petition, filed pursuant to Section 5(b) of the Federal Trade Commission Act, 15 U.S.C. § 45(b), and Section 2.51 of the Commission’s Rules of Practice and Procedure, 16 C.F.R. § 2.51, asks the Commission to relieve him of the obligation to comply with Paragraphs V and VI of the Order, to the extent that White Sands and Alamogordo Physicians, respectively, fail to meet their compliance obligations. These ongoing obligations would otherwise continue until January 24, 2008, three years from the date the Order became final. Mr. Laurenza contends, *inter alia*, that significant changed circumstances, to wit the severance of his relationship with White Sands and Alamogordo Physicians, make him unable to continue to comply with Paragraph VII of the Order. Petition at 1. The Petition was placed on the public record for thirty days pursuant to Section 2.51(c) of the Commission’s Rules. No comments were received. For the reasons stated below, the Commission has determined to grant the Petition.

The Complaint issued with the Order in Docket No. C-4130 alleges that White Sands is a for-profit physician-hospital organization that consists of a non-profit hospital; Alamogordo Physicians, an independent practice association; and other non-physician licensed health care professionals that include certified registered nurse anesthetists. (Complaint ¶ 2). According to the

Order

Complaint, Mr. Laurenza, as general manager of White Sands, and through his company Dacite, negotiated with payors on behalf of White Sands' nurse anesthetist members and Alamogordo Physicians' physician members, although the nurse anesthetist members were otherwise in competition with each other and the physician members of Alamogordo Physicians were otherwise in competition with each other for the provision of health care services in the Alamogordo area for a fee. (Complaint ¶ 7). Further, White Sands' physician and nurse anesthetist members had agreed with each other and with White Sands not to deal individually, or through any other organization besides White Sands, with any payor with which White Sands was attempting to negotiate a contract jointly on behalf of White Sands' members. (Complaint ¶ 20).

The Complaint alleges that Respondents' actions have had, or tend to have, the effect of restraining trade unreasonably in the provision of physician and nurse anesthetist services in the Alamogordo area, and that the described combination, conspiracy, acts and practices constitute unfair methods of competition in violation of Section 5 of the Federal Trade Commission Act, 15 U.S.C. § 45. (Complaint ¶ 35). The Order was issued to prevent respondents from continuing to engage in such anticompetitive activities. (Order ¶ II). The Order further requires a three-year cooling off period during which respondents Dacite and Laurenza are prohibited from negotiating on behalf of, or advising, respondents White Sands, Alamogordo Physicians, or any provider who participates or has participated in those entities. (Order ¶ III). Paragraph IV of the Order requires specified notification from each respondent prior to entering into any messenger arrangement with any provider. Paragraphs V.A through V.E. specify White Sands' mailing, termination, notification, and compliance obligations. Although White Sands already has complied with Paragraphs V.A through V.C of the Order, its compliance obligations under Paragraph IV and Paragraphs V.D and V.E continue for three years from the date the Order becomes final, or until January 24, 2008. Paragraphs V.F. and VI specify, respectively, White Sands' and Alamogordo

## Order

Physicians' notification obligations related to corporate changes that may affect compliance obligations. These Order requirements continue until the Order terminates on January 11, 2025. The remaining paragraphs of the Order relate to obligations of each respondent and are unaffected by the severance of Mr. Laurenza's relationship with White Sands.

At issue is Paragraph VII of the Order, which provides that if neither Respondent White Sands nor Respondent Alamogordo Physicians complies with all or any portion of Paragraphs V.A through V.F of this Order, or if Respondent Alamogordo Physicians fails to comply with Paragraph VI of this Order, within sixty (60) days of the times set forth in those paragraphs, then Respondent Laurenza shall, within thirty (30) days thereafter, comply with those portions of Paragraphs V.A through V.F and Paragraph VI of this Order with which Respondent White Sands or Respondent Alamogordo Physicians did not comply.

The Petition states that, effective March 31, 2005, the relationship between Dacite and White Sands was severed so that Mr. Laurenza no longer will have access to the information necessary for him to comply with Paragraph VII, should White Sands or Alamogordo Physicians fail to satisfy any of the obligations that would trigger the application of that paragraph. Petition at 1.

The Order may be reopened on the grounds set forth in Section 5(b) of the Federal Trade Commission Act, 15 U.S.C. § 45(b), 16 C.F.R. § 2.51(b). Section 5(b) provides that the Commission shall reopen an order to consider whether it should be set aside if the respondent "makes a satisfactory showing that changed conditions of law or fact" so require.<sup>1</sup> A satisfactory showing sufficient to require reopening is made when a request to reopen identifies significant changes in circumstances and shows

---

<sup>1</sup> See *Supplementary Information, Amendment to 16 CFR 2.51(b)*, announced August 15, 2001, ("Amendment").

Order

that the changes eliminate the need for the order or make continued application of it inequitable or harmful to competition.<sup>2</sup> Where changed circumstances do not require reopening, Section 5(b) further provides that the Commission may reopen and set aside an order when it determines that the public interest so requires. The public interest standard was not raised in the Petition, and, in this instance, we do not need to assess the public interest standard, because the Commission has determined that Mr. Laurenza has made the requisite satisfactory showing that changed conditions of fact require the Order to be reopened and modified.

Upon consideration of Mr. Laurenza's Petition and other information, the Commission has determined that the factual premise underlying the requirement that Mr. Laurenza comply with those portions of the Order with which White Sands or Alamogordo Physicians fail to comply no longer exists. The severing of the relationship between Mr. Laurenza and White Sands substantially changes Mr. Laurenza's ability to comply with his continuing obligations regarding White Sands' and Alamogordo Physicians' compliance.

For these reasons, the Commission finds that changed conditions of fact warrant reopening and modifying the Order to set aside Paragraph VII. This action in no way modifies or affects the obligations of respondents White Sands or Alamogordo Physicians. Accordingly,

---

<sup>2</sup> S. Rep. No. 96-500, 96th Cong., 2d Sess. 9 (1979) (significant changes or changes causing unfair disadvantage); *Louisiana-Pacific Corp.*, Docket No. C-2956, Letter to John C. Hart (June 5, 1986), at 4 (unpublished) ("Hart Letter"). *See also United States v. Louisiana-Pacific Corp.*, 967 F.2d 1372, 1376-77 (9th Cir. 1992) ("A decision to reopen does not necessarily entail a decision to modify the Order. Reopening may occur even where the petition itself does not plead facts requiring modification.").

Order

**IT IS ORDERED** that this matter be, and it hereby is, reopened; and

**IT IS FURTHER ORDERED** that the Commission's Order issued on January 11, 2005, hereby is, as of the date of issuance of this Order, modified to set aside Paragraph VII.



Order

IN THE MATTER OF

**EVANSTON NORTHWESTERN HEALTHCARE  
CORPORATION**

**ORDER GRANTING IN PART AND DENYING IN PART  
JOINT MOTION FOR EXTENSION OF TIME AND  
LENGTH OF APPEAL BRIEFS**

Respondent Evanston Northwestern Healthcare Corporation and Complaint Counsel have filed a Joint Motion for Extension of Time and Length of Appeal Briefs (October 28, 2005) (hereinafter “Joint Motion”) requesting that the Commission extend the time for the filing of briefs on the appeal and the cross-appeal in this matter, and enlarge the word limits to which the briefs are subject. For the reasons discussed below, the Commission grants the parties’ motion for an extension of time and denies their motion for an enlargement of the word limits.

**1. Enlargement of Time**

Chief Administrative Law Judge McGuire filed his Initial Decision and Order in this matter on October 17, 2005. Respondent filed a timely Notice of Appeal on October 26, 2005, and Complaint Counsel filed a timely Notice of Cross-Appeal on October 28, 2005. Pursuant to Commission Rule 3.52(g), 16 C.F.R. § 3.52(g) (2005), Respondent is deemed the Appellant and Complaint Counsel are deemed the Cross-Appellants/Appellees. Because Respondent was served with the Initial Decision on October 24, 2005, Respondent must currently file its Appeal Brief on or before November 23, 2005. Commission Rule 3.52(b), 16 C.F.R. § 3.52 (b). If service of that and subsequent briefs is effected on the opposing parties on the date on which each brief is due, and if Complaint Counsel perfect their cross-appeal,<sup>1</sup> then

---

1

For purposes of this Order, Complaint Counsel’s cross-appeal will be deemed to have been perfected if their initial brief contains

## Order

Complaint Counsel's Answering and Cross-Appeal Brief would be due on or before December 27, 2005; Respondent's Reply and Answering Brief would be due on or before January 26, 2006; and Complaint Counsel's Rebuttal Brief would be due on or before February 6, 2006.

The time periods prescribed by the Commission Rules of Practice ordinarily should afford parties to Commission proceedings sufficient time to file pleadings and briefs of sufficient quality and detail to aid in the preparation of Commission opinions and orders. The proximity of the current briefing schedule to the Thanksgiving, Christmas, Chanukkah, and New Year's holidays, however, may interfere with that process. Accordingly, the Commission grants the portion of the Joint Motion requesting an extension of time within which to file the appellate briefs in this matter.

## **2. Enlargement of Word Count Limits**

As the Commission has previously stated, the prescribed word limits should afford parties to Commission proceedings sufficient space to file pleadings and briefs of sufficient quality and detail to aid in the preparation of Commission opinions and orders. *See, e.g., In the Matter of North Texas Specialty Physicians, Docket No. 9312, Order Denying Motion for Extension of Word Count Limits* (December 21, 2004). Commission Rule 3.52(k), 16 C.F.R. § 3.52(k), expressly provides that “[e]xtensions of word count limitations are disfavored, and will only be granted where a party can make a strong showing that undue prejudice would result from complying with the existing limit.” In support of their motion, the parties simply state that an extension of the word counts is warranted because of the “lengthy trial record and complex underlying issues,” and because of the size of some of

---

their “arguments as to any issues [Complaint Counsel] is raising on cross-appeal . . .” Commission Rule 3.52(c), 16 C.F.R. § 3.52(c).

Order

the prior pleadings and Judge McGuire's decision. Joint Motion at 3-4. These facts, offered without any elaboration as to the nature of the complexity of the issues, do not by themselves constitute the necessary strong showing to warrant extending the word count limitations. Therefore, the Commission denies the portion of the Joint Motion requesting an enlargement of the word limits prescribed by Commission Rule 3.52, 16 C.F.R. § 3.52.

Accordingly,

**IT IS ORDERED THAT** (1) Respondent shall file its Appeal Brief on or before December 16, 2005, and (2) the appeal of Respondent shall be deemed perfected "by the timely filing of an appeal brief," for purposes of Commission Rule 3.51(a), 16 C.F.R. § 3.51(a), if Respondent files its Appeal Brief by that date. Respondent's Appeal Brief shall not exceed 18,750 words in length.;

**IT IS FURTHER ORDERED THAT** (1) Complaint Counsel shall file their Answering and Cross-Appeal Brief on or before February 3, 2006, and (2) Complaint Counsel's cross-appeal shall be deemed perfected "by the timely filing of an appeal brief" if Complaint Counsel file their Answering and Cross-Appeal Brief by that date, whether or not Respondent has previously perfected its appeal. Complaint Counsel's Answering and Cross-Appeal Brief shall not exceed 26,250 words in length.;

**IT IS FURTHER ORDERED THAT** Respondent shall file its Reply and Answering Brief on or before March 15, 2006. Respondent's Reply and Answering Brief shall not exceed 18,750 words in length.;

**IT IS FURTHER ORDERED THAT** Complaint Counsel shall file their Rebuttal Brief on or before April 5, 2006. Complaint Counsel's Rebuttal Brief shall not exceed 11,250 words in length.; and

**IT IS FURTHER ORDERED THAT** all of the foregoing

Order

Briefs shall in all other respects conform to the requirements of  
Commission Rule 3.52, 16 C.F.R. § 3.52.

Order

IN THE MATTER OF

**EVANSTON NORTHWESTERN HEALTHCARE  
CORPORATION**

**ORDER GRANTING EXPEDITED MOTION AND  
PERMITTING ENLARGEMENT OF LENGTHS OF  
APPEAL BRIEFS**

Respondent Evanston Northwestern Healthcare, Inc. has filed an Expedited Motion for Extension of Length of Initial Appeal Brief (“Expedited Motion”), requesting leave to file an opening brief not to exceed 24,000 words in length. This amount is a 28 percent increase over the 18,750 word limitation prescribed by Commission Rule 3.52(b)(2). For the reasons set forth below, the Commission grants the Expedited Motion, and also enlarges by the same percentage amount the word limitations for the other three briefs that may be filed by the parties in this appeal.

This is the second motion for an extension of the word limitations filed by Respondent. By Order dated November 18, 2005, the Commission denied the portion of a previous Joint Motion filed by Respondent and Complaint Counsel that requested that the Commission enlarge the word limitations for all of the briefs by 60 percent. Commission Rule 3.52(k) expressly provides that “[e]xtensions of word count limitations are disfavored, and will only be granted where a party can make a strong showing that undue prejudice would result from complying with the existing limit.” In their Joint Motion, however, the parties based their request to extend the word limitations only on their assertions that the case involved “complex underlying issues” and on the length of the trial record, the prior pleadings, and the Initial Decision. Joint Motion at 3-4. The Commission denied the parties’ request because “[t]hese facts, offered without any elaboration as to the nature of the complexity of the issues, [did] not by themselves constitute the necessary strong showing to warrant extending the word count limitation.” November 18 Order at 2. Many of the Commission’s matters involve complex

## Order

issues and large records. To make the showing required by Commission Rule 3.52(k), a party must, at minimum, state with specificity the reasons for the request for the extension, including the precise issues to be covered in the briefs, and why those issues cannot be adequately briefed in the specified word limitations. Otherwise, any party could seek an extension to the Commission's word limitations for briefs simply by making a general assertion about the complexity of the issues in the case at issue.

Respondent's Expedited Motion states that if it is bound in its Appeal Brief to the 18,750 word limitation prescribed by Commission Rule 3.52(b)(2), it will have to omit "important arguments necessary for its defense and will so limit its discussion of other complex, nuanced and novel issues raised on this appeal as to interfere with their clarity and completeness." Expedited Motion at 2. Respondent contends that these arguments and issues include (1) whether the merger at issue produced "substantial, verified pro-competitive effects arising from improved quality of care," and if so, whether any such improvements were merger specific; (2) whether the merger produced improvements "in other areas;" (3) whether, and if so to what extent, the merger affected prices, as reflected in "complex pricing analyses and internal documentary evidence;" (4) the contours of relevant markets, and the manner in which they should be defined; and (5) whether, and if so to what extent, the merger produced unilateral anticompetitive effects. Expedited Motion at 5-7.<sup>1</sup>

The Commission expresses no opinion as to the substantive relevance or merit of any of the arguments or issues identified by Respondent with respect to the ultimate resolution of Respondent's appeal. The Commission has determined, however, that Respondent's contentions about the complexity of the issues

---

<sup>1</sup> Respondent advises that Complaint Counsel takes no position on the relief requested in Respondent's motion. Expedited Motion at 2.

Order

before the Commission, combined with the substantial size of the record in this matter, are sufficiently specific and well-founded to warrant extending the word limitation for Respondent's opening brief by the requested 28 percent amount.<sup>2</sup> Therefore, the Commission grants the Expedited Motion, and also enlarges by the same percentage amount the word limitations for the other three briefs that may be filed by the parties in this appeal.

Accordingly,

**IT IS ORDERED THAT** Respondent's Appeal Brief shall not exceed 24,000 words in length.;

**IT IS FURTHER ORDERED THAT** if Complaint Counsel perfects its Cross-Appeal, Complaint Counsel's Answering and Cross-Appeal Brief shall not exceed 33,600 words in length;<sup>3</sup>

**IT IS FURTHER ORDERED THAT** Respondent's Reply and Answering Brief shall not exceed 24,000 words in length.;

**IT IS FURTHER ORDERED THAT** Complaint Counsel's Rebuttal Brief shall not exceed 14,400 words in length.; and

**IT IS FURTHER ORDERED THAT** all of the foregoing Briefs shall in all other respects conform to the requirements of Commission Rule 3.52, 16 C.F.R. § 3.52.

---

<sup>2</sup> See *In the Matter of Rambus, Incorporated*, Docket No. 9302, Order Granting Extensions of Time To File Appellate Briefs and Increases in Word Count Limits (March 18, 2005), at 2.

<sup>3</sup> For purposes of this Order, Complaint Counsel's Cross-Appeal will be deemed to have been perfected if its Answering and Cross-Appeal Brief contains "its arguments as to any issues [Complaint Counsel] is raising on cross-appeal . . ." Commission Rule 3.52(c), 16 C.F.R. § 3.52(c). If Complaint Counsel do not perfect their cross-appeal, then their Answering Brief shall not exceed 24,000 words in length. *Id.*

The Honorable Dan Flynn  
Texas State Representative  
House District 2  
P.O. Box 2910  
Austin, TX 78768-2910

Dear Representative Flynn:

This responds to your letter dated April 12, 2005, in which you request a Commission opinion on the lawful construction of the term “cash advance item” as used in the FTC’s Funeral Rule, 16 C.F.R. § 453.1(b) (“the Funeral Rule” or “the Rule”). Specifically, you question whether a Texas trial court is correct in ruling that “all goods or services purchased from a third-party vendor, even though not included on the contract, are ‘cash advances’” under the Funeral Rule.<sup>1</sup> Correct interpretation of the

---

<sup>1</sup> It is our understanding that your request is prompted by the May 2004 decision granting partial summary judgment in *Hijar v. SCI Texas Funeral Services, Inc.*, No. 2002-740, Order Granting Plaintiff’s Motion for Partial Summary Judgment and Establishing Issues Under Rule 166a(e), T.R.C.P. and Denying Defendants’ Second Motion for Summary Judgment (County Court at Law No. 3, El Paso, May 21, 2004), in which the court held that the defendant violated the cash advance disclosure provision of the Funeral Rule by failing to disclose each fee charged to the plaintiff for the cost of advancing funds on behalf of the plaintiff for goods and services purchased from third parties and resold to plaintiff. The Court in *Hijar* based its holding on an interpretation of the term “cash advance item” that would include the following items, when purchased from a third party and resold to persons arranging funerals: “direct cremation; immediate burial; forwarding remains; receiving remains; embalming; refrigeration; other preparation; transportation; casket/cremation casket; alternative container; outside enclosure; clothing/shroud; memorial booklet; service folders/prayer cards; acknowledgment cards; flowers;



term “cash advance item” is important because it determines the breadth and impact of certain substantive provisions of the Funeral Rule that employ that term.

The Commission believes that the court is incorrect in ruling that *all* goods or services purchased from a third-party vendor are cash advance items. This interpretation sweeps far too broadly, potentially bringing within its scope every component good or service that comprise a funeral. This was not and is not the Commission’s intention in the “cash advance” provisions of the Rule. In our opinion, the term “cash advance item” in the Rule applies only to those items that the funeral provider represents expressly to be “cash advance items” or represents by implication to be procured on behalf of a particular customer and provided to that customer at the same price the funeral provider paid for them. This conclusion is based on the analysis set forth below.

### **Analysis**

The Funeral Rule<sup>2</sup> defines the term “cash advance item” as follows:

[a]ny item of service or merchandise described to a

---

shipping container; crematory services; crucifix; escorts; certified copies; public transportation; outside funeral director’s expense; vault installation; clergy/religious facility; musicians or singers; hairdressing; and permits.”

<sup>2</sup> The Commission promulgated the original Funeral Rule on September 24, 1982, making it fully effective on April 30, 1984. 47 Fed. Reg. 42260 (Sept. 24, 1982). The Commission amended the Rule in 1994, following a lengthy review proceeding, and that 1994 amended Rule continues to be in effect. 59 Fed. Reg. 1592 (Jan. 11, 1994). All references to “the Funeral Rule” or “the Rule” are to the 1994 amended Rule, currently in effect. References to the 1982 Rule are to “the original Rule.”

purchaser as a “cash advance,” “accommodation,” “cash disbursement,” or similar term. A cash advance item is also any item obtained from a third party and paid for by the funeral provider on the purchaser’s behalf. Cash advance items may include, but are not limited to: cemetery or crematory services; pallbearers; public transportation; clergy honoraria; flowers; musicians or singers; nurses; obituary notices; gratuities; and, death certificates. 16 C.F.R. § 453.1(b).

The first sentence of this definition quite clearly states that any item a funeral provider describes expressly using the words “cash advance” item (or similar words or phrases) is, in fact, a cash advance item for purposes of the Funeral Rule. The second sentence broadens the definition to cover situations when a funeral provider purports to act “on behalf” of a particular customer, more as that customer’s procurement agent rather than as a retailer serving the general public. The third sentence merely provides an illustrative list of the various types of goods or services that funeral providers typically may treat as cash advance items.

Certain substantive provisions in the Funeral Rule employ the defined term “cash advance item.” Specifically, §§ 453.3(f)(1)(ii) and 453.3(f)(2) require a funeral provider who is charging a customer more for a cash advance item than the funeral director paid for it to disclose that material fact (*i.e.*, the existence of a mark-up, but not the amount) to the customer on the statement of funeral goods and services selected by the customer.<sup>3</sup>

---

<sup>3</sup> Also, the statement of goods and services that the funeral provider must give to the customer at the conclusion of the discussion of funeral arrangements must itemize any cash advance items that are part of the agreed-upon funeral arrangements, and must state the price, or if not known, the estimated price, of those items. The Rule states: “(These prices must be given to the extent then known or reasonably ascertainable. If the prices are not known or reasonably ascertainable, a good faith estimate shall

The Commission included these “cash advance” disclosure provisions in the Rule to address a practice in the marketplace that the Commission had identified as being harmful to consumers. Specifically, some funeral providers misrepresented that they would obtain goods or services for their customers at cost, when in fact these funeral providers profited by marking up the price of the items.<sup>4</sup> The Final Staff Report on the original Funeral Rule, which is part of the rulemaking record on which the Commission relied in adopting the Rule, succinctly describes the problem:

Cash advance charges are completely separate from, and additional to, the funeral director’s own charges. They usually appear on the funeral bill under such headings as

---

be given and a written statement of the actual charges shall be provided before the final bill is paid.)” 16 C.F.R. § 453.2(b)(5)(i)(B).

<sup>4</sup> This mark-up was achieved both directly and indirectly. As noted in the Final Staff Report, “[s]ometimes, [the mark-up] has been accomplished by simply inflating the amount of the charge on the customer’s bill. In other instances, the same effect has been achieved by the funeral home securing some form of kickback or rebate from the supplier of the cash advance item after charging the customer the full price.” Final Staff Report (June 1978) at 249. Marking up cash advance items was not an uncommon practice. The Commission noted, in adopting the original Rule, that “the evidence demonstrates that many individual funeral providers do charge mark-ups for cash advances. In a 1976 survey of California funeral directors, 12% of the 291 respondents admitted charging ‘in excess of the amount actually advanced for any items of service labeled as ‘cash advances’ or ‘accommodation items.’ [The National Funeral Directors Association’s] annual survey of funeral homes indicates that, on a national level, funeral homes are receiving a 5% mark-up on cash advance items. . . .” 47 Fed. Reg. 42279 (Sept. 24, 1982).

“accommodations,” “cash disbursements,” and “cash advanced for your convenience.” This terminology clearly indicates the basic conception, both by the funeral home and the consumer; that is, that the family is simply reimbursing the funeral director for cash outlays. The traditional use of such terms, as well as the obvious fact that these items are being provided by the third party, create the expectation that the amount billed is the same as that paid or owed. . . . Our investigation revealed, however that some funeral homes have generated extra revenues by charging their customers more for cash advance items than the funeral home actually paid out.<sup>5</sup>

Based on the record evidence of this problem, as summarized and analyzed in the Final Staff Report, the Commission adopted § 453.3(f) to remedy it. As noted in the Statement of Basis and Purpose issued by the Commission when it adopted the original Rule, § 453.3(f) is intended to prevent consumers from being led to believe, incorrectly, that the cost to the consumer for a particular item is the same as the cost to the funeral provider:

[C]onsumers believe that items labeled “cash advances” . . . are being provided at cost. There is an implicit representation that the cash advance transaction involves merely a forwarding of cash by the funeral provider and a subsequent dollar-for-dollar reimbursement by the consumer . . . . The use of this term in connection with items such as flowers, obituary notices, etc., which the consumers could easily obtain from a third party, creates the expectation that the amount billed the consumer is the same as the amount paid by the funeral provider. Given this expectation, the failure to disclose the existence of a mark-up is a deceptive practice.<sup>6</sup>

---

<sup>5</sup> Final Staff Report (June 1978) at 249.

<sup>6</sup> 47 Fed. Reg. 42278-42279 (Sept. 24, 1982).

The Commission found that, in describing a particular item to a customer, a funeral provider's express use of the term "cash advance item" (or alternative formulations such as "accommodation" or "cash disbursement") implies that the cost to the customer for that item is the same as the cost to the funeral provider. Thus, in cases where a funeral provider describes an item in this manner, yet charges the customer more for it than the funeral provider paid for it, the Commission requires a corrective disclosure to prevent the customer from being deceived. Specifically, in such a circumstance, the Funeral Rule requires that the following disclosure be placed on the statement of funeral goods and services selected: "We charge you for our services in obtaining: (specify cash advance items)."<sup>7</sup> This is the scenario addressed by the first sentence in the "cash advance item" definition.

The second sentence of the definition, indicating that "[a] cash advance item is also any item obtained from a third party and paid for by the funeral provider on the purchaser's behalf," is in the nature of a "fencing-in" provision.<sup>8</sup> The Commission's intention in including this sentence is to bring within the ambit of § 453.3(f) any situation where a funeral provider might, without using the specific term "cash advance," offer to obtain an item for a particular customer that the customer could obtain on her own – purporting to act "on behalf" of that customer, more as that customer's procurement agent than as a retailer serving the general public. Specifically, the purpose of this fencing-in aspect of the definition is to deter the less scrupulous funeral provider from evading the Rule by eschewing express description of an

---

<sup>7</sup> 16 C.F.R. § 453.3(f)(2). The Rule also specifically prohibits this type of affirmative misrepresentation. 16 C.F.R. § 453.3(f)(1)(i).

<sup>8</sup> Under the "fencing-in" doctrine, the FTC may frame a remedy which extends beyond the precise illegal conduct found. *Bristol-Myers Co. v. FTC*, 738 F.2d 554, 561 (2d Cir. 1984).

item as a “cash advance item” (or alternative formulations), yet nevertheless conveying to a customer acting reasonably under the circumstances that obtaining the item involves merely a forwarding of cash by the funeral provider and a subsequent dollar-for-dollar reimbursement by the customer. The Commission’s intention, in sum, is that this part of the “cash advance item” definition function to foreclose funeral providers from attempting to sidestep the strict letter of the Rule by using implied misrepresentations rather than express ones.

In the absence of either the funeral provider’s express representation that an item is a “cash advance item” or implied representations that the item is procured for a particular customer at the funeral provider’s cost, a consumer, acting reasonably under the circumstances, would not believe that the amount he or she is billed for an item is the same as the amount the funeral provider pays its supplier. Indeed, such a belief would be contrary to a reasonable consumer’s most elementary experience in the everyday marketplace. In these circumstances, the funeral provider is generally acting like any retailer who purchases goods or services from third parties for resale to consumers.

The Commission believes that reasonable consumers generally understand that the price charged by a retail seller – including funeral providers – includes profit.<sup>9</sup> Thus, the corrective disclosure about cash advance items that § 435.3(f)(2) requires is unnecessary when the funeral provider does not mislead the customer through either express representations that the item is a “cash advance item” (or alternative formulations), or implied representations that the customer is paying no more for an item than the amount the funeral provider paid for it.

---

<sup>9</sup> As the Commission noted in the Statement of Basis and Purpose for the original Rule, “The Commission does not suggest that it is improper for funeral providers to profit on items obtained from third parties. It is clear that it is wholly proper for providers to do so.” 47 Fed. Reg. 42278 (Sept. 24, 1982).

It is worth noting that the text and structure of the Rule overall reflect the fundamental distinction between cash advance items and non-cash advance items. For items that are typically non-cash advance items, the Rule requires disclosure of the *retail* price of specified goods and services offered for sale by a funeral provider.<sup>10</sup> An obvious example is the Rule’s treatment of caskets, for which it requires a separate price list containing only the funeral provider’s *retail* price.<sup>11</sup> Therefore, items that must appear on a funeral provider’s price list<sup>12</sup> would not trigger

---

<sup>10</sup> Funeral providers must “[i]nclude on the [general] price list, in any order, the *retail* prices (expressed either as the flat fee, or as the price per hour, mile or other unit of computation) and the other information specified below for at least each of the following items, if offered for sale . . . .” The rule then lists: forwarding of remains to or receiving remains from another funeral home; direct cremation; immediate burial; transferring remains to the provider’s premises; embalming and other preparation of the body; use of the provider’s facilities and staff for viewing, for a funeral ceremony, or for a memorial service; use of the provider’s equipment and staff for a graveside service; the use of the provider’s hearse or limousine; and the provider’s basic services fee. 16 C.F.R. § 453.2(b)(4). (Emphasis supplied.)

<sup>11</sup> “The funeral provider must offer the [casket price] list upon beginning discussion of, but in any event before showing caskets. The list must contain at least the *retail* prices of all caskets and alternative containers offered which do not require special ordering, enough information to identify each, and the effective date for the price list.” 16 C.F.R. § 453.2(b)(2)(i). (Emphasis supplied.)

<sup>12</sup> Section 453.2(b)(4)(i)(C) of the Rule sets forth the minimum information that must be included on a funeral provider’s general price list. These items include: caskets; outer burial containers; forwarding of remains to or receiving remains from another funeral home; direct cremation; immediate burial;

the cash advance disclosures unless the funeral provider expressly represents the items as “cash advance items” (or alternative formulations) or represents by implication that items can be procured on behalf of the particular customer and provided at the same price the funeral provider paid for them.

Accordingly, the Commission wishes to be clear that the term “cash advance item” does not apply to *every* good or service that a funeral provider obtains from a third party. This overbroad interpretation, which potentially brings within its scope every component good or service of a funeral, does not comport with the Commission’s intention in promulgating the “cash advance” provisions of the Rule. Rather, based on a review of the original Rule and the rulemaking record, the Commission finds that the term “cash advance item” in the Rule applies only to those items that the funeral provider represents expressly to be “cash advance items” or represents by implication to be procured on behalf of a particular customer and provided to that customer at the same price the funeral provider paid for them.

---

transferring remains to the provider’s premises; embalming and other preparation of the body; use of the provider’s facilities and staff for viewing, for a funeral ceremony, or for a memorial service; use of the provider’s equipment and staff for a graveside service; the use of the provider’s hearse or limousine; and the provider’s basic services fee.



Response to Petition

Re: *Petition to Quash Civil Investigative Demand*, File No.  
051-0131

July 15, 2005

Dear Mr. Schildkraut:

This letter advises you of the disposition of the Petition to Quash Civil Investigative Demand (“Petition to Quash”) served on Aloha Petroleum, Ltd. (hereinafter “Petitioner” or “Aloha”) in conjunction with an investigation by the Federal Trade Commission (hereinafter “FTC” or “Commission”) of a proposed transaction between Aloha and Trustreet Properties, Inc. (“Trustreet”). The Petition to Quash is denied for the reasons hereinafter stated. The new date for Petitioner to comply with the Civil Investigative Demand (“CID”) is July 18, 2005.

This ruling was made by Commissioner Pamela Jones Harbour, acting as the Commission’s delegate. *See* 16 C.F.R. § 2.7(d)(4). Petitioner has the right to request review of this matter by the full Commission. Such a request must be filed with the Secretary of the Commission within three days after service of this letter.<sup>1</sup> The filing of such a request for review does not, however, stay the time for compliance established herein. 16. C.F.R. § 2.7(f).

## **I. Background and Summary**

On June 29, 2005, the Commission issued a CID to Petitioner in connection with the Commission’s investigation. Petitioner received the CID on July 5, 2005. The original return date, July 6, 2005, was extended by letter dated July 8, 2005 until July 13,

---

<sup>1</sup> This letter decision is being delivered by facsimile and express mail. The facsimile copy is being provided as a courtesy. Computation of the time for appeal should be calculated from the date you receive the original by express mail.

## Response to Petition

2005. After conferring with counsel for the Commission in accordance with the provisions of 16 C.F.R. § 2.7(d)(2), the Petition to Quash was timely filed on July 13, 2005.

The investigation involves a proposed purchase of assets by Aloha from Trustreet. Since the transaction is below the reporting thresholds established by 15 U.S.C. § 18a, the Commission's investigation has been conducted through both voluntary and compulsory requests for information.

The two-page Petition to Quash raises two issues. First, Aloha claims that the information sought is irrelevant to the Commission's deliberative process because Staff recommendation's already have been made to the Commission and because Commission Staff would not have adequate time to evaluate the information prior to the Commissioners taking any action concerning the transaction. Related to this point, Aloha asserts that the CID provided an inadequate response time and that "it typically takes months to respond" to the type of information request posed by the CID. Petition at 1.<sup>2</sup> Second, Aloha claims that production of its own records to the Commission at this time would be unfair to it because the timing of the transaction is such that a Commission decision to challenge the transaction would have to be made before Aloha could "respond to any new issues raised by Staff's analysis of the CID."<sup>3</sup> Petition at 2.

---

<sup>2</sup> Even if the Commission were to treat this cryptic statement as an assertion that compliance was too burdensome, Petitioner has failed to carry its burden of demonstrating such unreasonableness. *See* Federal Trade Commission v. Rockefeller, 591 F.2d 182, 190 (2<sup>nd</sup> Cir. 1979); and National Claims Service, Inc., 1998 FTC Lexis 192, \*8 (FTC 1998).

<sup>3</sup> This argument is based on a misperception on the part of Aloha regarding Commission procedures. As a courtesy, Commission Staff typically advises subjects of investigation of the bases upon which Staff will be recommending any

Response to Petition

## II. Analysis

When reviewed by a federal court, a CID must be enforced so long as the information sought is: (1) reasonably relevant, *i.e.*, not plainly incompetent or irrelevant to any lawful purpose of the agency; and (2) not unduly burdensome to produce. *FTC v. Invention Submission Corp.*, 965 F.2d 1086, 1089 (D.C. Cir. 1992). *See also Office of Thrift Supervision v. Vinson & Elkins*, 124 F.3d 1304, 107 (D.C. Cir. 1997).<sup>4</sup> Though the Commission is not a federal court, the standard by which the courts would evaluate the Commission's decision is the appropriate standard for the evaluation of the Petition to Quash.

---

enforcement action that might be authorized by a vote of the Commissioners. After receiving that advice from Staff, meetings with the parties may be scheduled with individual Commissioners to provide an opportunity for the subjects of the investigation to present reasons why the Commissioners should not adopt a particular Staff enforcement recommendation with which they disagree. The timing of this transaction is such that production of materials on July 18<sup>th</sup> will not provide enough time for either additional Staff discussions or Commissioner meetings before the time that the Commission must make a decision on whether it should seek to enjoin the consummation of this transaction. No legally cognizable right of Aloha would be adversely affected if such additional consultation cannot occur here. Further, the timing constraints here are not of the Commission's making. The dates by which Aloha and Trustreet have advised the Commission that this transaction must close are solely within the control of one or the other of them. If the transaction parties desire the Commission to have additional time for consultation, it is a problem uniquely within their hands to resolve.

<sup>4</sup> It also must be within an agency's authority to conduct an investigation and to issue a CID. In this merger, the Commission's authority neither is nor could be challenged.

## Response to Petition

Notably, the Petition does *not* assert that the information sought by the CID is not relevant to the transaction. Indeed, such an assertion would be impossible since the CID directly addresses issues concerning the transaction. For this reason alone, under the standard enunciated in *Invention Submission*, the Petition must be denied.

Attempting to sidestep the critical (but fatal) relevance issue, Aloha, in effect, claims that it should be excused from responding to the CID because the Commission already has sufficient information to make its decision whether to challenge the transaction. It is not, however, within Aloha's purview to make this determination. Indeed, a similar argument was rejected in *EEOC v. Med-National, Inc.*, 186 F.R.D. 609, 618 (D. Hawaii 1999). In *Med-National*, the petitioner asserted that it should not be required to respond to an administrative subpoena because the EEOC already had sufficient evidence to resolve the merits of the related claim. Citing *University of Pennsylvania v. EEOC*, 493 U.S. 182, 191 (1990), the district court held that the only germane issue as to whether it should enforce the EEOC's administrative subpoena was whether the information sought was relevant to the EEOC's investigation. The court was not to make an evaluation of whether the agency, without the information sought by the administrative subpoena, already had sufficient evidence to determine if the issue being investigated was well-founded.

Beyond these issues, and without waiving the Commission's deliberative process privilege, assuming *arguendo* that: (1) Staff's recommendations have been made to the Commission; and (2) that these recommendations were unanimous in their conclusions, the information sought in the CIDs would still be relevant to the Commission's deliberative process. Most simply stated, the Commission does not merely "rubber stamp" Staff's recommendations. Up until the moment that the Commissioners formally vote, each individual Commissioner has both the right and obligation to deliberate upon all relevant information that is legitimately available to her or him before voting as to whether the transaction does or is likely to violate any statute enforced by

Response to Petition

the Commission. Moreover, Commissioners are fully capable of evaluating such evidence directly, without the need for Staff intercession.

**III. Conclusion and Order**

For all the foregoing reasons, **IT IS ORDERED THAT** the Petition to Quash should be, and it hereby is, **DENIED**. Pursuant to Rule 2.7(e),<sup>5</sup> the new date for Petitioner to comply with the subject Subpoena and CID, as amended herein, is July 18, 2005.<sup>6</sup>

---

<sup>5</sup> 16 C.F.R. § 2.7(e).

<sup>6</sup> Petitioner is urged, but not required, to respond to the Subpoena on a rolling basis.

Response to Petition

Re: *Petition to Limit or Quash, File No. 032-3237*

October 13, 2005

Dear Mr. Seiger:

This letter advises you of the disposition of the Petition to Limit or Quash (hereinafter "Petition") filed by Garden of Life, Inc. (hereinafter "Petitioner") in conjunction with an investigation by the Federal Trade Commission (hereinafter "FTC" or "Commission"). The Petition appears to be moot.

This ruling was made by Commissioner Pamela Jones Harbour, acting as the Commission's delegate. *See* 16 C.F.R. § 2.7(d)(4). Petitioner has the right to request review of this matter by the full Commission. Such a request must be filed with the Secretary of the Commission within three days after service of this letter.<sup>1</sup>

The Petition was timely filed on March 25, 2004. At that time, the Commission had reason to believe that Petitioner intended to comply with the terms of the Civil Investigative Demand in accordance with a schedule being negotiated with Staff. A ruling on the Petition was, therefore, held in abeyance. The Commission now has reason to believe that Petitioner and Staff did negotiate a satisfactory schedule for compliance and that production has been completed. Those developments have mooted the Petition. Accordingly,

**IT IS ORDERED THAT** the Petition to Limit or Quash filed by Petitioner should be, and it hereby is, **DENIED** on the grounds that it is **MOOT**.

---

<sup>1</sup> This letter decision is being delivered by facsimile and express mail. The facsimile copy is being provided as a courtesy. Computation of the time for appeal is to be calculated from the date you received the original by express mail.

Response to Petition

Re: *Motion to Quash Civil Investigative Demands (“Motion to Quash”) Filed by Steve Wingard, Ashley Industries, LLC, Ashley Industries, LP, and Ashley Industries GP, LLC, File No. 042-3127*<sup>1</sup>

October 13, 2005

Dear Mr. Zachry:

This letter advises you of the disposition of the Movants’ Motion to Quash Civil Investigative Demands (“CIDs”) for written interrogatories, documentary materials, and oral testimony in conjunction with an investigation by the Federal Trade Commission (hereinafter “FTC” or “Commission”). The Motion is denied in part and granted in part for the reasons hereinafter stated. Pursuant to 16 C.F.R. § 2.7(e), the new date for Steve Wingard to comply with the document production CID and for the Ashley entities to comply with the CIDs for document production and interrogatory answers is October 27, 2005, and the new date for Steve Wingard to comply with the CID for oral testimony is November 10, 2005.

This ruling was made by Commissioner Pamela Jones Harbour, acting as the Commission’s delegate. *See* 16 C.F.R. § 2.7(d)(4). Petitioner has the right to request review of this matter by the full Commission. Such a request must be filed with the Secretary of the Commission within three days after service of this letter.<sup>2</sup>

---

<sup>1</sup> Ashley Industries, LLC, Ashley Industries, LP, and Ashley Industries GP, LLC will be referred to herein as “the Ashley entities.” The Ashley entities and Steve Wingard will be referred to herein as “Movants.”

<sup>2</sup> This letter decision is being delivered by facsimile and express mail. The facsimile copy is being provided as a courtesy. Computation of the time for appeal, therefore, should be calculated from the date you received the original by express mail.

Response to Petition

**I. Background and Summary**

The CIDs<sup>3</sup> were issued on June 30, 2005 – production of interrogatory answers and documents was required by July 25, 2005 and the investigational hearing was scheduled for August 8, 2005. On July 18, 2005 counsel for Movants spoke with Staff as required by Commission Rule § 2.7(d)(2), 16 C.F.R. § 2.7(d)(2). In particular, Staff were advised that Movants would only comply with the CIDs if Steve Wingard were granted immunity from prosecution. Staff advised Movants that the FTC had neither the authority to prosecute criminal claims nor the power to grant immunity from prosecution. On July 20, 2005, the Motion to Quash was filed.

**II. Movants Are Only Entitled To Relief With Regard to One of the CIDs.**

The factual basis for this Motion is the unsupported assertion of counsel that “Steve Wingard has always operated [the Ashley entities] as a sole proprietorship.” Motion at 1. The Motion is not accompanied by any affidavits or other materials under oath. In substance, Movants claim that they are entitled to relief from the commandment of the CIDs because the business records of the Ashley entities “could be used against [Steve Wingard] in a future criminal proceeding.” Motion at 2. Accordingly, it is claimed that the production of evidence required by the CIDs would violate Steve Wingard’s Constitutional rights against self-incrimination secured by the Fifth Amendment. These claims, except those made by Steve Wingard with respect to the CID directing him to respond to interrogatories, are without merit.

---

<sup>3</sup> Five separate CIDs are involved in this matter. Three were issued to Steve Wingard – one for testimony, one for interrogatory answers and one for document production. Two were issued to the Ashley entities – one for interrogatory answers and one for document production.



Response to Petition

**A. The Ashley entities have provided no factual basis for their claims under the Fifth Amendment.**

An individual is protected from the compelled provision of incriminating testimony by the Fifth Amendment under many circumstances. However, the Movants have demonstrated no factual support for their claim that such protection is available to the Ashley entities. In the first place, the privilege against compelled incriminating testimony does not extend to corporations or other collective entities. *Braswell v. United States*, 487 U.S. 99 (1988); and *Bellis v. United States*, 417 U.S. 85, 88-90 (1974). Public records of the State of Texas show that the Ashley entities are corporations or other collective entities within the meaning of the law.<sup>4</sup> As such, the Ashley entities have no rights against self-incrimination to assert. *Braswell*, 487 U.S. at 102. Additionally, the contents of the business records of the Ashley entities are not privileged. *Id.* Finally, service of the CIDs on the Ashley entities to respond to interrogatories and to produce documents also imposed on them the obligation to “find the means by which to comply because no Fifth Amendment defense

---

<sup>4</sup> On April 12, 2002, Ashley Industries GP, LLC filed Articles of Organization with the Corporations Section of the Office of the Secretary of State of the State of Texas establishing itself as a Texas limited liability company. Article Four on the first page of that document names Steve Wingard as the company’s initial registered agent. Article Five, beginning on the first page of that document, states that the company will be managed by its “members” and names Steve Wingard as its initial member. On that same date, Steve Wingard, “President and Sole Member” of Ashley Industries, LP filed its “Certificate of Limited Partnership” with the Corporations Section of the Office of Secretary of State of the State of Texas. On September 24, 2003, Steve Wingard filed a “Texas Franchise Tax Public Information Report” with the Texas Secretary of State on behalf of Ashley Industries LLC in which Steve Wingard was listed as the President, a Director, and the Registered Agent of that company.

Response to Petition

is available to it.” *Id.* at 116 (quoting *In re Sealed Case*, 832 F.2d 1268, 1282, n. 9 (DC Cir. 1987)).<sup>5</sup>

**B. Steve Wingard has provided no factual basis for his claim under the Fifth Amendment regarding the production of the business records of the Ashley entities.**

Movants, including Steve Wingard, claim that their business activities are “currently under investigation by the United States Attorney’s Office for the Western District of Texas.” Motion at 2. That fact does not by itself, however, excuse Steve Wingard from compliance with the CID for the production of documents directed to him as custodian of records for the Ashley entities.

The CID for document production only seeks the business records of the Ashley entities. Steve Wingard makes a general claim that the business records of the Ashley entities are purely private, but provides no support whatsoever for such claim. Further, Steve Wingard chose to incorporate and/or organize the Ashley entities as collective entities because of the legal

---

<sup>5</sup> Movants claim an entitlement to be treated as sole proprietorships based on the assertion that “Steve Wingard has always operated Ashley Industries as a sole proprietorship.” Motion at 1 & 4. It is unclear whether this assertion is intended to be a subtle distinction between a company “being” a sole proprietorship as opposed to a company being “operated” as a sole proprietorship. The claim fails nevertheless because Movants cite no authority upholding this apparent distinction nor do they provide any factual basis for either the fact of being sole proprietorships or for the fact that the companies are being operated as sole proprietorships. Further, even if the Ashley entities were sole proprietorships, Movants have not provided an adequate factual basis for quashing the CIDs issued to them. *See, e.g., Shapiro v. United States*, 335 U.S. 1, 18 (1948) (holding that “required records” cannot be treated as private papers subject to the privilege).

Response to Petition

advantages and protections that such organizational structures provided to him and them and may not now simply walk away from those choices in order to protect their business records from production. *United States v. Stone*, 976 F. 2d 909, 912 (4<sup>th</sup> Cir. 1992).

It is well established that “without regard to whether the subpoena is addressed to the corporation or, as here, to the individual in his capacity as a custodian, . . . a corporate custodian such as petitioner may not resist a subpoena for corporate records on Fifth Amendment grounds.” *Braswell*, 487 U.S. 108-09 (citations omitted). Even if “the act of production may prove personally incriminating” to the custodian, the custodian is not entitled to claim protection from the Fifth Amendment. *Id.* at 111-12. The Supreme “Court has consistently recognized that the custodian of corporate or entity records holds those documents in a representative rather than a personal capacity. . . . Under those circumstances, the custodian’s act of production is not deemed a personal act, but rather an act of the corporation. Any claim of Fifth Amendment privilege asserted by the agent would be tantamount to a claim of privilege by the corporation – which of course possesses no such privilege.” *Id.* at 110-11.

The *Braswell* Court held that the custodian of corporate records could not assert a Fifth Amendment privilege against the production of corporate records; however, that Court left “open the question whether the agency rationale supports compelling a custodian to produce corporate records when the custodian is able to establish, by showing for example that he is the sole employee and officer of the corporation, that the jury would inevitably conclude that he produced the records.” *Id.* at 118, n. 11. That argument fails here because Movants have not provided any evidence to show that the Ashley entities are a sole proprietorship. Additionally, the Fourth Circuit has squarely rejected that claim in *United States v. Stone*<sup>6</sup> when it held that even if a company

---

<sup>6</sup> 976 F.2d at 912 (citations omitted).

## Response to Petition

is a one-man operation, . . . it is still a corporation, a state law regulated entity that has a separate legal existence from [the individual] shielding him from its liabilities. The business could have been formed as an unincorporated sole proprietorship and production of its business records protected by the privilege against self-incrimination. . . . [The individual] chose the corporate form and gained its attendant benefits, and we hold, in accord with the decisions of sister circuits, that he cannot now disregard the corporate form to shield his business records from production.

Accordingly, we find that Steve Wingard is the custodian of the records of the Ashley entities. As such, he is not entitled to assert a claim of Fifth Amendment privilege with respect to either the production of such records or the provision of testimony “to identify or authenticate the documents for admission in evidence.” *Braswell*, 487 U.S. at 114 (quoting *Curcio v. United States*, 354 U.S. 118, 125 (1957)).

Further, since the contents of the business records of the Ashley entities were in all likelihood voluntarily prepared by them in the ordinary course of their business and not by reason of government commandment in furtherance of a criminal investigation, the contents of such documents are not likely to be entitled to any privilege, even if the Ashley entities were sole proprietorships – which they are not. *United States v. Fisher*, 425 U.S. 391, 410 (1976). This is especially true with respect to so-called “required records” which must be produced even if the privilege against compelled testimony might otherwise apply. *Shapiro*, 335 U.S. at 17.

**C. Steve Wingard may not make a blanket assertion of privilege under the Fifth Amendment with respect to the provision of oral testimony.**

Steve Wingard has failed to provide any factual basis for his claims under the Fifth Amendment with respect to oral testimony. Steve Wingard must establish a factual basis for the Commission

Response to Petition

to believe that his compelled oral testimony would subject him to “substantial and real, and not merely trifling or imaginary, hazards of incrimination.” *United States v. Apfelbaum*, 445 U.S. 115, 128 (1980) (quoting earlier Supreme Court cases – internal quotation marks omitted). Second, the privilege against compelled testimony cannot be asserted in a wholesale fashion. “A person may not make a ‘blanket assertion’ of the [Fifth Amendment] privilege.” *United States v. Aeilts*, 855 F. Supp. 1114, 1116 (C.D. CA 1994) (citing *United States v. Brown*, 918 F.2d 82, 84 (9<sup>th</sup> Cir. 1990)). The Commission’s Rules and general investigatory practice require privilege claims to be asserted in a more detailed manner to keep blanket claims of privilege from being used to sweep in unprivileged materials. *See, e.g.*, 16 C.F.R. §§ 2.7, 2.8A, and 2.9. The privilege must be asserted on a document-by-document basis, *Aeilts, supra*, and a “question-by-question basis.”<sup>7</sup> *United States v. Bodewell*, 66 F.3d 1000, 1002 (9<sup>th</sup> Cir.

---

<sup>7</sup> Because the privilege must be asserted by the witness at the time each question is propounded and in response to each such question where it can be asserted, there is no reason to excuse the attendance of Steve Wingard from the investigational hearing commanded by the CID. Further, as the Sixth Circuit pointed out in *United States v. Mayes, et al*, 512 F.2d 637, 649 (6<sup>th</sup> Cir. 1975):

The Fifth Amendment privilege against self-incrimination is a privilege personal to the witness. *United States v. Goldfarb*, 328 F.2d 280 (6<sup>th</sup> Cir. 1964). . . . While the witness is entitled to the advice of counsel before determining whether he should invoke the privilege, *United States v. Compton*, 365 F.2d 1 (6<sup>th</sup> Cir. 1966), and while it is within the discretion of the trial judge to permit counsel for the witness to invoke the privilege on his behalf, 8 *Wigmore, supra*, § 2270, the nature of the privilege is such that in the final analysis the

## Response to Petition

1995); and *Brown*, 918 F.2d at 84 (“A person must have the chance to present himself for questioning, and as to each question elect to raise or not to raise the defense.”) (internal quotation marks omitted). Accordingly, Steve Wingard’s blanket assertion of privilege under the Fifth Amendment with respect to the provision of oral testimony must be denied.

**D. Steve Wingard has adequately asserted a claim of privilege under the Fifth Amendment with respect to the CID directing him to answer interrogatories.**

Unlike the document production CID that was served on Steve Wingard, the CID for responses to interrogatories does not differentiate between the personal knowledge of Mr. Wingard and knowledge derived from the contents of the business records of the Ashley entities. Further, Mr. Wingard has asserted, albeit in a summary fashion, a separate, and plausible, claim of privilege under the Fifth Amendment as to each interrogatory that has been directed to him. Motion at 4-6.

As a general matter, a claim of privilege under the Fifth Amendment may be upheld as to an individual when that individual “reasonably believes that his testimony could ‘furnish a link in the chain of evidence needed to prosecute’ him for a crime.” *Hoffman v. United States*, 485 U.S. 479, 486 (1951). “To sustain the privilege, it need only be evident from the implications of the question, in the setting in which it is asked, that a responsive answer to the question or an explanation of why it cannot be answered might be dangerous because injurious disclosure could result.” *Id.* at 486-87. There must be a real danger of self-incrimination, not merely one that is remote or

---

controlling decision is that of the witness himself. . . . There may be a constitutional privilege against testifying and at the same time be a powerful incentive to get on the stand and tell the truth. The alternatives for the witness are seldom easy.

Response to Petition

speculative. *Zicarelli v. New Jersey State Comm'n of Investigation*, 406 U.S. 472, 478 (1972). "When the danger is not readily apparent from the implications of the question asked or the circumstances surrounding the inquiry, the burden of establishing its existence rests on the person claiming the privilege." *Estate of Fisher v. C.I.R.*, 905 F.2d 645, 649 (2<sup>nd</sup> Cir. 1990).

In this instance, counsel for Mr. Wingard has advised the Commission that Mr. Wingard's business activities are being investigated for possible criminal violations by the United States Attorney for the Western District of Texas. Further, the Commission has reason to believe that the subject of that inquiry may involve some of the same business conduct that is the subject of the Commission's investigation. A review of each of the seven interrogatories directed to Mr. Wingard shows that it is apparent from both the implications of the questions asked and the circumstances surrounding the Commission's investigation that Mr. Wingard's answers to the Commission's interrogatories may be self-incriminating to Mr. Wingard. Accordingly, his Motion to Quash must be granted, at least in part.

### III. CONCLUSION AND ORDER

For all the foregoing reasons, **IT IS ORDERED THAT** Movants' Motion to Quash should be, and it hereby is, **DENIED** with respect to the CIDs directed to Steve Wingard and the Ashley entities for document production, the CID directed to the Ashley entities for responses to interrogatories, and the CID directed to Steve Wingard for oral testimony; and **IT IS FURTHER ORDERED THAT** Movants' Motion to Quash should be, and it hereby is, **GRANTED** with respect to the CID directed to Steve Wingard for answers to interrogatories. Pursuant to 16 C.F.R. § 2.7(e), the new date for Steve Wingard to comply with the document production CID and for the Ashley entities to comply with the CIDs for document production and interrogatory answers is October 27, 2005, and the new date for Steve Wingard to comply with the CID for oral testimony is November 10, 2005.

Response to Petition

Re: *Petition to Limit and/or Quash Civil Investigative Demand*  
("Petition"), File No. 052-3182

November 17, 2005

Dear Mr. Raney:

This letter advises you of the disposition of the Petition filed by Voice Mail Broadcasting Corp. (hereinafter "Petitioner") in conjunction with an investigation by the Federal Trade Commission (hereinafter "FTC" or "Commission"). The Petition is hereby denied because it was not filed in conformity with the Commission's Rules of Practice, 16 C.F.R. § 2.7(d)(2) and because it was otherwise lacking in substantial merit. The new date for Petitioner to comply with the CID is November 28, 2005, at 9:00 a.m.

This ruling was made by Commissioner Pamela Jones Harbour, acting as the Commission's delegate. *See* 16 C.F.R. § 2.7(d)(4). Petitioner has the right to request review of this matter by the full Commission. Such a request must be filed with the Secretary of the Commission within three days after service of this letter.<sup>1</sup>

## I. BACKGROUND

On October 14, 2005, the Commission issued a CID to Petitioner in connection with an investigation by the Commission into potential violations of the Commission's "Telemarketing Sales Rule," Petition at 1. On November 3, 2005, Petitioner filed the Petition. Petitioner asks for relief from most of the specifications of the CID on the grounds that: (1) the "definition of 'voice broadcasting services' exceeds the scope of the Telemarketing Sales Rule and/or any abusive or deceptive acts or

---

<sup>1</sup> This letter decision is being delivered by facsimile and express mail. The facsimile copy is being provided as a courtesy. Computation of the time for appeal, therefore, should be calculated from the date you receive the original by express mail.



Response to Petition

practices prohibited by that rule or the FTC Act;” Petition at 1, and (2) Specification D-9 of the CID’s Schedule of Documents to be Produced “requests documents which [sic] are privileged and/or confidential based on the attorney-client privilege, trade secrets, and other applicable privileges.” Petition at 2.

**II. Petitioner Failed to Comply with the Requirements of Our Rules.**

Petitioner failed to discharge its meet-and-confer obligations under 16 C.F.R. § 2.7(d)(2). FTC rules require a petitioner to meet with Commission counsel in a “good faith” attempt to resolve any disputes raised by the production of materials in response to our compulsory process. The rule contemplates that any adjustments to avoid undue burden or unnecessary intrusion into confidential areas can be made by well-intentioned lawyers cognizant of the specific problems raised by the production demanded. It serves the exemplary public purpose of facilitating Commission investigations without unduly intruding into other areas. In this case, it does not appear that Petitioner even attempted to contact or engage the Commission’s Staff in any discussion of the merits of the claims raised in this Petition.

The obligation on the part of the recipient of FTC compulsory process to meet and confer with Commission counsel on the merits of any objections that might arise in compliance with such demands is neither a *pro forma* one nor one that can be easily excused.<sup>2</sup> Compulsory process is routinely issued by investigatory agencies without good knowledge regarding the record keeping

---

<sup>2</sup> In cases where the issue raised is primarily, if not exclusively, an issue of law, a summary meet-and-confer might be appropriate. However, where, as here, the issues are primarily mixed questions of law and fact (confidentiality, relevance and materiality), a failure on the part of counsel to engage in a meaningful meet-and-confer with Commission counsel is less tolerable.

## Response to Petition

practices of the recipients of its process. Demanding good faith attempts to resolve avoidable compliance problems is of equal interest and concern to the Commission and any process recipient. The meet-and-confer requirement provides both sides a mechanism within which adjustments can be made to competing interests in a quick and efficient manner.<sup>3</sup> Petitioner's failure to comply with the meet-and-confer requirements of FTC rules is sufficient, in and of itself, to deny the instant Petition. However, inasmuch as the Petition does not otherwise exhibit any substantial merit, it is additionally denied on that ground as well.

**III. Petitioner Failed to Provide a Factual or Legal Basis for the Relief Requested.**

The Petition asserts claims without providing any factual or legal support for those claims. This opinion has already recited the entire substantive content of the Petition in Section I, *supra*. This Petition contains no hint regarding the facts underlying the claims advanced by the Petition or any indication of the legal authority upon which Petitioner relies. We are unwilling to speculate at large on these matters about which Petitioner apparently wished us to be uninformed.

Even a casual review of the specifications of the challenged CID shows that the information requested is relevant to the subject of the Commission's investigation. Moreover, Petitioner has not argued that the Commission's investigation is outside its authority, or that the specifications are too indefinite. Accordingly, Petitioner's jurisdictional challenge is rejected. *See United States v. Morton Salt*, 338 U.S. 632, 652 (1950) ("[I]t is sufficient if the inquiry is within the authority of the agency, the demand is not too indefinite and the information sought is

---

<sup>3</sup> We understand that in most cases significant accommodation of legitimate interests can be and is achieved without the necessity of any conduct more taxing than a phone call between well-intentioned counsel.

Response to Petition

reasonably relevant.”). *See also Federal Trade Commission v. Ken Roberts Co.*, 276 F.3d 583, 587 (D.C. Cir. 2001) (“enforcement of an agency’s investigatory subpoena will be denied only when there is ‘a patent lack of jurisdiction’ in an agency to investigate or regulate”) (citations omitted).

Further, Petitioner claims privilege with respect to one specification of the CID. It, however, has not provided the Commission with a description of the information for which privilege is claimed, the actual privilege being claimed for each privileged item, or any factual basis for a claim of privilege.<sup>4</sup> Accordingly, Petitioner provides no basis for relief on this ground, and the privilege claims are denied.

#### IV. CONCLUSION

For all the foregoing reasons, the Petition should be, and it hereby is, **DENIED**. Pursuant to Rule 2.7(e),<sup>5</sup> the new date for Petitioner to comply with the subject compulsory process demands is November 28, 2005, at 9:00 a.m.

---

<sup>4</sup> Rule 2.7(d)(1) clearly requires that every “petition shall set forth all assertions of privilege or other factual and legal objections to the . . . civil investigative demand, including all appropriate arguments, affidavits and other supporting documentation.” 16 C.F.R. § 2.7(d)(1).

<sup>5</sup> 16 C.F.R. § 2.7(e).

Response to Petition

Re: *Petition of BlueHippo Funding, LLC to Quash Civil Investigative Demand* (“Petition to Quash”), File No. 052-3092

December 13, 2005

Dear Mr. Volner:

This letter advises you of the disposition of the Petition to Quash Civil Investigative Demand (“CID”) filed by BlueHippo Funding, LLC (“BlueHippo” or “Petitioner”). BlueHippo has petitioned the Commission to quash a CID issued to Wachovia Bank, NA (“Wachovia”) for “information concerning any BlueHippo account with Wachovia.” Petition at 1. The Petition is denied because BlueHippo lacks standing to challenge the CID served upon Wachovia and because the Petition to Quash is otherwise without merit. Pursuant to 16 C.F.R. § 2.7(e), Wachovia is ordered to comply with the CID on or before December 23, 2005 at 5:00 p.m. E.S.T.

This ruling was made by Commissioner Pamela Jones Harbour, acting as the Commission’s delegate. *See* 16 C.F.R. § 2.7(d)(4). Petitioner has the right to request review of this matter by the full Commission. Such a request must be filed with the Secretary of the Commission within three days after service of this letter.<sup>1</sup>

---

<sup>1</sup> This letter decision is being delivered by facsimile and express mail. The facsimile copy is being provided as a courtesy. Computation of the time for appeal, therefore, should be calculated from the date you received the original by express mail. In accordance with the provisions of 16 C.F.R. § 2.7(f), the timely filing of a request for review of this matter by the full Commission shall not stay the return date established by this decision.

Response to Petition

## I. Background and Summary

A CID was issued on August 10, 2005 to Wachovia for the bank's business records relating to BlueHippo. The CID return date was September 1, 2005. BlueHippo timely filed its Petition to Quash the CID issued to Wachovia on August 26, 2005.<sup>2</sup>

The Petition to Quash states two separate bases for relief: (1) "BlueHippo's past and present bank account information is not reasonably relevant to the scope and purpose of the investigation . . . [of] whether BlueHippo violated the Commission's 'Mail or Telephone Order Merchandise' Rule . . . or engaged in deceptive mail or telephone order shipping practices in violation of Section 5(a)(1) of the Federal Trade Commission Act;"<sup>3</sup> and (2) "BlueHippo's bank account information is proprietary and confidential business information."<sup>4</sup> Before addressing the merits of these claims, the Commission must first determine whether BlueHippo has standing to challenge a CID issued to Wachovia.

---

<sup>2</sup> Counsel for Petitioner has not informed the Commission why it chose to file the Petition to Quash without the inclusion of the "signed statement representing that counsel for the petitioner has conferred with counsel for the Commission in an effort in good faith to resolve by agreement the issues raised by the petition and has been unable to reach such an agreement." 16 C.F.R. § 2.7(d)(2). The Commission will, as a matter of discretion, determine the Petition to Quash on the merits rather than denying it for this material deficiency.

<sup>3</sup> Petition at 1.

<sup>4</sup> *Id.*

Response to Petition

**II. Petitioner Lacks Standing to Challenge the CID Issued to Wachovia.**

According to its Petition to Quash, BlueHippo is a Maryland Corporation that “markets computers, televisions, and related equipment and accessories and extends credit to customers to enable them to make purchases.” Petition at 2. Wachovia, the recipient of the CID, appears to be a wholly separate business entity with whom Petitioner claims no relationship other than that of a customer of Wachovia’s banking services.

The records sought by the CID appear to be the business records of Wachovia and not those of BlueHippo. That being the case, it is clear that the mere fact that Wachovia’s business records might contain information relevant to a Commission investigation of the business practices of BlueHippo does not give BlueHippo standing to quash a CID issued to Wachovia. *See United States v. Miller*, 425 U.S. 435, 445 (1976) (“We hold that the District Court correctly denied [depositor]’s motion to suppress, since he possessed no Fourth Amendment interest that could be vindicated by a challenge to a subpoena.”); and *Donaldson v. United States*, 400 U.S. 517, 530-31 (1971) (taxpayer cannot intervene as of right in a subpoena enforcement action in which a third party may be directed to produce records which may establish that the taxpayer is liable for taxes unless the taxpayer has shown that he/she possesses either a proprietary interest in the records or that such records are subject to some recognized privilege, e.g., work product of his attorney or account). As in *Miller* and *Donaldson*, BlueHippo has identified no interest or privilege in the business records of Wachovia sufficient to give it standing to challenge the CID issued to Wachovia.

BlueHippo’s description of the information sought by the CID as being its own “proprietary and confidential business information,” Petition at 1, is simply wrong as a matter of law and fact. The law is well settled that bank records “are not the bank customer’s private papers; they are, rather, the business records of

Response to Petition

the bank.” *Clayton Brokerage Co., Inc. v. Edward Clement*, 87 F.R.D. 569, 570 (D. MD 1980), *citing*, *Miller*, 425 U.S. at 440. Moreover, bank customers have “no legitimate ‘expectation of privacy’ in the contents of checks, deposit slips and other banking records.” *Id.* Thus, a customer, such as BlueHippo, possesses no cognizable interest in the bank’s records sufficient to provide it with standing to challenge the CID issued to Wachovia. *See, e.g., Securities and Exchange Comm’n v. First Security Bank of Utah*, 447 F.2d 166, 167 (10<sup>th</sup> Cir. 1971 (SEC administrative subpoena); and *Kelley v. United States*, 536 F.2d 897 (9<sup>th</sup> Cir. 1976) (IRS administrative summons). Thus, BlueHippo lacks standing to challenge the CID issued to Wachovia.

### **III. The Petition to Quash Is Otherwise Without Merit**

Even if BlueHippo had standing to challenge the CID issued to Wachovia, the Petition to Quash is otherwise without merit. Neither the claims of confidentiality nor those of irrelevancy advanced by BlueHippo provide any grounds for quashing the CID issued to Wachovia.

#### **A. The Information Requested Is Relevant to the Investigation.**

The CID was issued pursuant to the Resolution adopted by the Commission on May 14, 1994 permitting Staff to conduct investigations of possible violations of 16 C.F.R. § 435 (“Telemarketing Sales Rule” or “TSR”) or § 5(a)(1) of the FTC Act (15 U.S.C. § 5(a)(1)) in connection with any such sales. BlueHippo’s claim that this investigation is limited to issues related to the “timing of sales and shipments and delivery,” Petition at 2-3, is simply wrong. The CID does not evidence any limitation of the type posited by Petitioner.

The Petition to Quash appropriately cites the *Morton Salt* and *Invention Submission Corp.* cases to state the broad scope of the Commission’s investigatory reach. *United States v. Morton Salt Co.*, 338 U.S. 632, 652 (1950) (“[I]t is sufficient if the inquiry is

## Response to Petition

within the authority of the agency, the demand is not too indefinite and the information sought is reasonably relevant.”); and *Federal Trade Comm’n v. Invention Submission Corp.*, 965 F.2d 1086, 1089 (D.C. Cir. 1992) (“It is well established that a district court must enforce a federal agency’s investigative subpoena if the information is reasonably relevant . . . – or, put differently, not plainly incompetent or irrelevant to any lawful purpose of the [agency] . . . – and not unduly burdensome to produce.”) (citations and internal quotation marks omitted).

BlueHippo’s reliance on *Invention Submission Corp.* or *Federal Trade Comm’n v. Turner*, 609 F.2d 743 (5<sup>th</sup> Cir. 1980), to establish that information responsive to the CID “is not reasonably relevant to the scope and purpose of the investigation,” Petition at 1 and 5, is misplaced. The *dicta* in the *Turner* opinion, 609 F.2 at 745 (“The amount of [the subject’s] assets is not relevant to an inquiry into whether a violation of the law exists.”), is distinguishable<sup>5</sup> and was unpersuasive to the District of Columbia Circuit regarding the enforcement of pre-complaint process.<sup>6</sup> The Commission, like the

---

<sup>5</sup> *Turner* involved the question of whether the Commission might use investigative process after having issued a cease and desist order to determine whether an order violator had sufficient assets to make a consumer redress remedy a viable enforcement option. 965 F.2d at 1089. The instant investigation is a pre-complaint inquiry to determine whether sufficient evidence exists to warrant initiation of any form of enforcement action, as in *Information Submission Corp. Id.*

<sup>6</sup> The DC Circuit affirmed the order directing Invention Submission Corp. to produce its financial information in response to a CID. *Invention Submission Corp.*, 965 F.2d at 1090 (“Financial data, including evidence of relative profitability, could facilitate the Commission’s investigation of ISC in different ways, not all of which may yet be apparent. . . . And the Commission has no obligation to establish precisely the relevance of the material it seeks in an investigatory subpoena by tying that



Response to Petition

DC Circuit, finds the *Turner* case does not support granting the present Petition to Quash.

Further, BlueHippo's attempt at artificially cabining the investigation to "shipping representations and delays," Petition at 5, is at best illusory. The scope of the CID is determined by the resolution authorizing it rather than any particular theory of violation. *Invention Submission Corp.*, 965 F.2d at 1091-92 ("The Commission's compulsory process resolution did not restrict the investigation to possible oral misrepresentations, however, and we have previously made clear that 'the validity of Commission subpoenas is to be measured against the purposes stated in the resolution, and not by reference to extraneous evidence.'") (citations omitted). A review of the specifications of the challenged CID shows that the information requested is relevant to the subject of the Commission's investigation and consistent with the scope of the authorizing resolution. For example, materials produced by Wachovia may assist in the identification of parties possessing information relevant to the inquiry. Accordingly, we find the information sought by the CID relevant to the investigation and neither Petitioner nor Wachovia claim that the CID specifications are too indefinite. *See United States v. Morton Salt, supra; see also Federal Trade Commission v. Ken Roberts Co.*, 276 F.3d 583, 587 (D.C. Cir. 2001) ("enforcement of an agency's investigatory subpoena will be denied only when there is 'a patent lack of jurisdiction' in an agency to investigate or regulate") (citations omitted).

**B. The Petition to Quash Raises No Valid Claim of Privilege.**

BlueHippo's claim that the CID to Wachovia requires the provision of information that is "proprietary and confidential" to it is misplaced. See Section II., *supra*. Even if the Commission assumed that BlueHippo had a cognizable privacy interest in

---

material to a particular theory of violation.").

## Response to Petition

Wachovia's business records, BlueHippo has provided no factual or legal support for a finding that the Commission's existing protection of confidential or sensitive information is somehow inadequate. *See* 15 U.S.C. § 57b-2(f).

**IV. Conclusion and Order**

Accordingly, no grounds having been established by BlueHippo to warrant quashing the CID issued to Wachovia, **IT IS ORDERED THAT** BlueHippo's Petition to Quash should be, and it hereby is, **DENIED**.

**IT IS FURTHER ORDERED THAT** Wachovia shall respond to the CID on or before December 23, 2005 at 5:00 p.m. E.S.T. The Secretary is directed to serve a copy of this letter decision on Wachovia by facsimile and express mail.