UNITED STATES DISTRICT COURT
DISTRICT OF MINNESOTA
THIRD DIVISION

Civil File No. 4-94-CV-573

State of Minnesota,
by its Attorney General,
Hubert H. Humphrey III,

Plaintiff,

vs.

COMPLAINT

Children's Health of St. Paul,
Inc.; The Children's Hospital,
Incorporated; Minneapolis
Child Care Incorporated; and
Minneapolis Children's
Medical Center,

Defendants.

VERIFIED COMPLAINT

Plaintiff, the State of Minnesota, by its Attorney General, Hubert H. Humphrey III, on its own behalf and as parens patriae, brings this civil action to obtain equitable and other relief against the defendants named herein and complains and alleges as follows:

JURISDICTION AND VENUE

1. This complaint is brought under Sections 4 and 16 of the Clayton Act, 15 U.S.C. §§ 15 and 26, and Section 4 of the Sherman Act, 15 U.S.C. § 4, to prevent and restrain violations by the defendants, as herein alleged, of Section 7 of the Clayton Act, 15 U.S.C. § 18, and Sections 1 and 2 of the Sherman Act, 15 U.S.C. §§ 1 and 2.

2. This Court has jurisdiction of this action under 28 U.S.C. § 1337.

3. Venue is proper under Section 12 of the Clayton Act, 15 U.S.C. § 22, and 28 U.S.C. § 1391(b) and (c), because each defendant maintains an office, transacts business, has an agent, or is found within the District of Minnesota.

4. Defendant Children's Health of St. Paul, Inc. ("CHSP"), and defendant The Children's Hospital, Incorporated ("Children's Hospital"), shall be collectively referred to herein as "St. Paul Children's." They each transact business, maintain offices, and are found within the District of Minnesota. CHSP is the parent corporation and sole voting member of Children's Hospital. Among their business operations St. Paul Children's owns and operates the specialty children's hospital known as Children's Hospital located in St. Paul, Minnesota.

5. Defendant Minneapolis Child Care Incorporated ("Child Care"), and defendant Minneapolis Children's Medical Center ("MCMC"), shall be collectively referred to herein as "Minneapolis Children's." They each transact business, maintain offices, and are found within the District of Minnesota. Child Care is the parent corporation and sole voting member of MCMC. Among their business operations Minneapolis Children's owns and operates MCMC's specialty children's hospital located in Minneapolis, Minnesota.

6. St. Paul Children's and Minneapolis Children's executed a Letter of Intent on March 23, 1993, in which they agreed to a comprehensive full asset merger of both hospitals (which now compete or potentially compete with each other in the Minneapolis-St. Paul Children's Hospital market area) into a "single, integrated system of pediatric health care providers" serving the entire Minneapolis-St. Paul Children's Hospital market area. The resulting organization will have actual and complete control over both children's hospitals. The State of Minnesota alleges that this merger would violate Section 7 of the Clayton Act, 15 U.S.C. § 18, and Sections 1 and 2 of the Sherman Act, 15 U.S.C. §§ 1 and 2.

DEFINITIONS

7. "HHI" means the Herfindahl-Hirschmann Index, a measure of market concentration calculated by squaring the market share of each firm competing in the market and then summing the resulting numbers. For example, for a market consisting of four firms with shares of 30, 30, 20 and 20 percent, the HHI is 2600 (30 squared + 30 squared + 20 squared + 20 squared = 2600). The HHI, which takes into account the relative size and

distribution of the firms in a market, ranges from virtually zero to 10,000. The index approaches zero when a market is occupied by a large number of firms of relatively equal size. The index increases as the number of firms in the market decreases and as the disparity in size between the leading firms and the remaining firms increases.

8. "Minneapolis-St. Paul Metropolitan Children's Hospital market area" or "Metropolitan area," includes the 3-digit zip codes 550XX, 551XX, 553XX, and 554XX, which represent the area from which the vast majority of the admissions to St. Paul Children's and Minneapolis Children's hospitals originate.

9. "Pediatric care" is health care for children from 5 weeks of age through adolescence, generally through age 17. Health care generally, including pediatric care, is often broken down into primary, secondary, and tertiary care.

10. "Neonatal care" is care for newborns less than 5 weeks old. Neonatal care is broken down into Level I, Level II, and Level III care.

11. "Primary care" generally refers to relatively routine medical care, sometimes but not usually requiring hospitalization, usually provided by general practitioners or other physicians whose practices are not highly specialized. Primary pediatric care is that provided by general practitioners and pediatricians to children with routine illnesses or conditions. "Level I" neonatal care generally refers to primary care for healthy neonates of at least 2,500 grams birth weight.

12. "Secondary care" is generally that care provided to moderately or more seriously ill patients, sometimes by general practice physicians, but more commonly by persons practicing some formal or informal medical specialty. For purposes of this case, secondary care is inpatient care for moderately or somewhat seriously ill children. In the case of newborns, secondary care, also referred to as "Level II" neonatal care, is inpatient care for moderately ill newborns who do not need intensive care, but require 6 to 12 nursing hours per day.

13. "Tertiary care" is inpatient care for the most seriously ill patients, delivered by highly specialized staff in state-of-the-art facilities. As applied to the care of children, tertiary care includes intensive care, life support and other sophisticated medical services for severely ill children, cared for by pediatric subspecialists. Tertiary care for newborns includes, in particular, care for premature or critically ill newborns who require constant nursing care, continuous cardiopulmonary monitoring and other technologically advanced and provider-intensive care. "Level III" nursery facility is a term applied to hospital nurseries that are able to offer tertiary care to newborns.

PLAINTIFF

14. The State of Minnesota, as one of the sovereign states of the United States, brings this action pursuant to 15 U.S.C. § 26 as parens patriae to protect the economy of the state on behalf of its residents.

DEFENDANTS

15. Defendant CHSP is a nonprofit corporation organized and existing under the laws of the State of Minnesota. CHSP is located at 345 North Smith Avenue, St. Paul, Minnesota 55102. CHSP is the parent and sole voting member of defendant Children's Hospital.

16. Defendant Children's Hospital is a nonprofit corporation organized and existing under the laws of the State of Minnesota. It is located at 345 North Smith Avenue, St. Paul, Minnesota 55102. Children's Hospital operates a specialty children's hospital with 116 licensed beds, 109 of which are staffed. It has a medical staff of approximately 779 physicians and employs approximately 879 other people. It reported 1992 revenues of $54,557,000, and a net income of $3,333,000.

17. Defendant Child Care is a nonprofit corporation organized and existing under the laws of the State of Minnesota. Child Care is located at 2525 Chicago Avenue South, Minneapolis, Minnesota 55404. It is the parent and sole voting member of defendant MCMC.

18. Defendant MCMC is a nonprofit corporation organized and existing under the laws of the State of Minnesota. It is located at 2525 Chicago Avenue South, Minneapolis, Minnesota 55404. MCMC operates a specialty children's hospital with 183 licensed beds, 159 of which are staffed. It has a medical staff of approximately 770 physicians and employs approximately 1,333 other people. It reported 1992 revenues of $124,577,072, and a net income of $1,265,473.

TRADE AND COMMERCE

19. Defendants St. Paul Children's and Minneapolis Children's have jointly agreed to effect a merger of their children's hospital operations by combining at the parent corporation level, so that both of the children's hospitals, now separately owned and controlled, will come under the common ownership and control of the newly merged entity. It is expected that this combination will be achieved by having CHSP (on behalf of St. Paul Children's) and Child Care (on behalf of Minneapolis Children's) merge into a recently-formed nonprofit Minnesota corporation called Minnesota Children's Health, Inc., which will then act as a holding company controlling all the activities of the two former corporations.

20. Defendants CHSP, Children's Hospital, Child Care, and MCMC regularly purchase substantial quantities of equipment and supplies from sources outside Minnesota for use in the operation of their specialty children's hospitals in the Minneapolis-St. Paul Children's Hospital market area. CHSP, Children's Hospital, Child Care and MCMC regularly receive substantial revenues from governmental and private payors (e.g., insurance companies and the federal government under the Medicaid program) located outside Minnesota in payment for specialty children's hospital services provided by their hospitals in the Minneapolis-St. Paul Children's Hospital market area. CHSP, Children's Hospital, Child Care and MCMC are each engaged in interstate commerce and their activities are in the flow of, and substantially affect, interstate commerce.

Product Market

21. The provision of a distinct cluster of general and specialized inpatient pediatric hospital care excluding obstetrics, healthy neonates, psychiatric and chemical dependency services, constitutes a line of commerce, or relevant product market for antitrust purposes (referred to herein as the "specialty pediatric hospital market").

22. Defendants St. Paul Children's and Minneapolis Children's each offer a distinct cluster of general and specialized inpatient pediatric hospital care, excluding obstetrics and healthy neonates. Only defendants, together with the University of Minnesota Hospital and Clinic ("U of M"), offer this distinct bundle of general and specialized inpatient pediatric hospital services. Other general acute care hospitals do not offer the distinct bundle of general and specialized inpatient pediatric hospital care defendants provide. All three hospitals are located within less than eight miles of each other in the center of the Minneapolis-St. Paul Metropolitan Children's Hospital market area. Each hopsital is easily accessed by freeway from all parts of the Children's Hospital market area.

23. The University of Minnesota Hospital and Clinic ("U of M"), is primarily a research and teaching hospital. The U of M has a policy of accepting admissions only from U of M Medical School faculty or physicians with a clinical faculty appointment. Large third-party payors in the Metropolitan area (i.e., those representing the most covered lives) do not consider the U of M to be an adequate substitute for St. Paul Children's and Minneapolis Children's.

24. The cluster of general and specialized inpatient pediatric hospital care does not include healthy newborns less than 5 weeks old because (a) there is no current or potential competition between MCMC and CHSP with respect to healthy neonates, and (b) healthy neonates are the by-product of adult obstetrics, and thus are not a direct element in the market for pediatric services. Likewise, psychiatric and chemical dependency services are separate product markets because they are not uniquely available in a children's hospital setting.

25. Alternatively, the provision of tertiary-level inpatient pediatric hospital services constitutes a line of commerce or relevant product market for antitrust purposes (referred to herein as the "pediatric tertiary care market").

26. Third party payors must have in their network of health care providers a hospital capable of performing highly specialized medical procedures on children. These procedures generally fall under the category of tertiary care, and specifically include diagnoses falling under the categories of oncology, cardiology, ophthalmology, ENT, neurology, orthopedics, urology, and neonatology. Each of these subspecialties might be considered a product market; they are not demand substitutes for one another because a patient needing the services of a pediatric cardiologist cannot, for example, obtain treatment from a pediatric urologist. However, the chief reason that physicians refer patients to pediatric hospitals is that care can be provided at a facility where specialized support services (pediatric anesthesiologists, pediatric radiologists, and pediatric nurses) are present and where a number of pediatric subspecialists are available for consultation.

27. Pediatric hospitals provide only the physical setting, equipment, and specialized personnel (pediatric anesthesiologists, pediatric radiologists, and pediatric nurses) that subspecialty physicians require for their practices. Pediatric hospitals typically do not base their charges upon the type of subspecialty tertiary care provided; rather they negotiate a per-diem or per-stay charge with third party payors based on whether a patient requires a medical, surgical, or intensive care bed.

28. CHSP, MCMC, and the U of M are the only hospitals in the Metropolitan area at which physicians regularly perform tertiary services on pediatric and neonatal patients.

Geographic Market

29. The Minneapolis-St. Paul Metropolitan Children's Hospital market area, for antitrust purposes, constitutes a relevant geographic market for the provision of pediatric tertiary care and the cluster of general and specialized inpatient pediatric hospital care.

30. St. Paul Children's competes with Minneapolis Children's in the Minneapolis-St. Paul Metropolitan Children's Hospital market area in the above-defined product markets.

31. St. Paul Children's and Minneapolis Children's also represent potential competition to each other in the Minneapolis-St. Paul Metropolitan Children's Hospital market area in the above-defined product markets.

Effect on Competition

32. Competition in a hospital market lessens as the HHI of that market increases. Competition drives market participants to offer consumers lower prices, better quality, or both. This merger will result in a significant lessening of competition, as illustrated by an increase in the HHI of the markets for pediatric tertiary care and the cluster of general and specialized inpatient pediatric hospital care. The merger is therefore expected to lead to higher prices, lower quality for consumers, or both.

33. At the present time the market for the cluster of general and specialized inpatient pediatric hospital care in the Metropolitan area is highly concentrated, as measured by patient admittance data in the three specialty pediatric hospitals identified in paragraph 22, above. As a consequence of the proposed merger, the HHI in this market would increase by approximately 3852 to 7889. Thus, the effect of the proposed merger will be to move the market from an already highly concentrated market to a market that is nearing monopoly. The new, merged entity would be by far the largest market participant with approximately 88% of the market. The only possible competitor currently in the market is the U of M, with the remaining 12% of the market. If the U of M is excluded as a real competitor in the Metropolitan area specialty pediatric hospital market, the new merged entity would have a monopoly.

34. Although purchasers do not consider non-specialty community hospitals as substitutes for a specialty pediatrics facility, including non-specialty hospitals in the product market yields a very conservative assessment of the anticompetitive effects of the merger. In

this case, the HHI would increase by approximately 605 points to 1742, raising significant competitive concerns.

35. The alternative product market in the Metropolitan area, tertiary-level inpatient pediatric hospital services, is currently highly concentrated. As a consequence of the proposed merger, the HHI's for services in this alternative product market would increase dramatically. For oncology the increase is approximately 2971 points to 7636; cardiology increases 2948 points to 6889; ophthalmology increases 2642 points to 6289; ENT increases 4202 points to 8494; neurology increases 3792 points to 7764; orthopedics increases 3435 points to 6460; urology increases 3256 points to 7101; and neonatology (excluding healthy neonates) increases 4316 points to 9054. Thus, also in the alternative product market, the effect of the proposed merger would raise very serious competitive concerns, nearing monopoly in many subspecialties.

36. Entry of new competitors into either of these markets in the Minneapolis-St. Paul Metropolitan Children's Hospital market area is unlikely for several reasons. One barrier is the statutory moratorium on the construction of any new hospitals or the expansion of existing hospitals in Minnesota. Minn. Stat. § 144.551 (1993 Supp.). In addition, new major spending commitments by any health care provider are subject to reporting and possible review requirements under Minnesota's new health care cost containment legislation (known as "MinnesotaCare"). Minn. Stat. § 62J.17 (1992). Another barrier is that pediatricians in the Metropolitan area are reluctant to admit patients to anything other than a specialty pediatric hospital. In any case, a successful entrant into the market would have to devote substantial time and expense to planning and constructing a new specialty children's hospital, or to expanding existing pediatric facilities in a community hospital into the equivalent of a specialty children's hospital. Entry will not be timely, likely or sufficient in scope to counteract the lessening of competition from this merger.

37. The purpose of the merger is to enhance the parties' managed care contracting position by increasing their bargaining strength with insurance companies.

VIOLATIONS ALLEGED

COUNT I

Clayton Act, Section 7

38. Plaintiff realleges paragraphs 1 through 37.

39. Under the Letter of Intent executed on or about March 23, 1993, St. Paul Children's and Minneapolis Children's have agreed to merge their assets to become a single company under unified control. This merger will substantially increase concentration in the market for a cluster of general and specialized inpatient pediatric hospital care and/or in the market for pediatric tertiary care in the Metropolitan area.

40. The effect of the merger between St. Paul Children's and Minneapolis Children's may be substantially to lessen competition in the market for a cluster of general and specialized inpatient pediatric hospital care and/or in the market for pediatric tertiary care in the Metropolitan area in violation of Section 7 of the Clayton Act, 15 U.S.C. § 18, in the following ways, among others:

a. Actual and potential competition between St. Paul Children's and Minneapolis Children's will be eliminated; and

b. Competition generally in the market for a cluster of general and specialized inpatient pediatric hospital care and/or in the market for pediatric tertiary care in the Metropolitan area may be substantially lessened.

COUNT II

Sherman Act, Section 1, Unreasonable Restraint of Trade

41. Plaintiff realleges paragraphs 1 through 37.

42. By entering into the Letter of Intent on or about March 23, 1993, St. Paul Children's and Minneapolis Children's have agreed to restrain trade or commerce unreasonably in the market for a cluster of general and specialized inpatient pediatric hospital

care and/or in the market for pediatric tertiary care in the Metropolitan area in violation of Section 1 of the Sherman Act, 15 U.S.C. § 1.

43. This unlawful agreement to unreasonably restrain trade or commerce, if carried out, will have the following effects, among others:

a. Actual and potential competition between St. Paul Children's and Minneapolis Children's will be eliminated; and

b. Competition generally in the market for a cluster of general and specialized inpatient pediatric hospital care and/or in the market for pediatric tertiary care in the Metropolitan area may be substantially lessened.

COUNT III

Sherman Act, Section 2, Monopolization

44. Plaintiff realleges paragraphs 1 through 37.

45. The merger between Paul Children's and Minneapolis Children's, if allowed to proceed, will create a monopoly in the market for a cluster of general and specialized inpatient pediatric hospital care and/or in the market for pediatric tertiary care in the Metropolitan area in violation of Section 2 of the Sherman Act, 15 U.S.C. § 2.

46. The merger between Paul Children's and Minneapolis Children's will have the following effects, among others:

a. Actual and potential competition between St. Paul Children's and Minneapolis Children's will be eliminated; and

b. Competition generally in the market for a cluster of general and specialized inpatient pediatric hospital care and/or in the market for pediatric tertiary care in the Metropolitan area may be substantially lessened.

COUNT IV

Sherman Act, Section 2, Attempted Monopolization

47. Plaintiff realleges paragraphs 1 through 37.

48. By entering into the Letter of Intent on or about March 23, 1993, St. Paul Children's and Minneapolis Children's have engaged in anticompetitive conduct demonstrating an intent to monopolize trade or commerce in the market for a cluster of general and specialized inpatient pediatric hospital care and/or in the market for pediatric tertiary care in the Metropolitan area in violation of Section 2 of the Sherman Act, 15 U.S.C. § 2.

49. This unlawful agreement to unreasonably restrain trade or commerce, if carried out, will have a dangerous probability of achieving the following effects, among others:

a. Actual and potential competition between St. Paul Children's and Minneapolis Children's will be eliminated; and

b. A dangerous probability exists that the newly merged entity will have monopoly power in the market for a cluster of general and specialized inpatient pediatric hospital care and/or in the market for pediatric tertiary care.

PRAYER

WHEREFORE, plaintiff prays:

1. That pending final adjudication of the merits of the foregoing verified complaint, a temporary restraining order and preliminary injunction be issued against the defendants preventing and restraining each of them and all persons, successors and assigns acting on their behalf from taking any action, either directly or indirectly, in furtherance of the proposed merger of St. Paul Children's and Minneapolis Children's;

2. That the proposed merger between St. Paul Children's and Minneapolis Children's be adjudged to be in violation of Section 7 of the Clayton Act, 15 U.S.C. § 18; Section 1 of the Sherman Act, 15 U.S.C. § 1; and Section 2 of the Sherman Act, 15 U.S.C. § 2;

3. That the defendants and all persons, successors and assigns acting on their behalf be permanently enjoined from entering into or carrying out any agreement, understanding, or plan, the effect of which would be to combine St. Paul Children's and Minneapolis Children's;

4. That the plaintiff recover the costs of this action; and

5. That the plaintiff have such other further relief as the Court may deem just and proper.

Dated: _____

HUBERT H. HUMPHREY III
Attorney General
State of Minnesota

_____
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ATTORNEYS FOR PLAINTIFFS

VERIFICATION

I, Susan C. Gretz, declare:

1. I am an attorney with the Office of the Attorney General, Sate of Minnesota, Antitrust Division.

2. I am a member of the bar of this Court. My attorney license number is 209235.

3. I verify that the foregoing Complaint for and on behalf of the State of Minnesota was duly prepared under the direction of the Attorney General of the State of Minnesota, that the facts stated therein have been assembled by authorized employees and counsel for the State of Minnesota, and that the allegations therein are true and correct to the best of my knowledge, information and belief.

4. I declare under penalty of perjury that the foregoing is true and correct.

Executed in St. Paul, Minnesota on _____, 1994.

SUSAN C. GRETZ