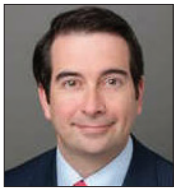
New York Law Journal
SERVING THE BENCH AND BAR SINCE 1888
WWW.NYLJ.COM
An ALM Publication
FEBRUARY 28, 2022

What the Antitrust Case Against Martin Shkreli Tells Us About the Latest Trends in Antitrust Enforcement and Shareholder Liability



By **Reed Brodsky**

And **Eric J. Stock**

On Jan. 14, 2022, the Hon. Denise Cote, U.S. District Judge for the Southern District of New York, issued her decision in *Federal Trade Commission v. Shkreli*, holding that Martin Shkreli, the former head of Vyera Pharmaceuticals, violated federal and state antitrust laws by allegedly interfering with the entry of generic competition for Vyera's drug Daraprim. See *FTC v. Martin Shkreli*, No. 20CV00706 (DLC), 2022 WL 135026 (S.D.N.Y. Jan. 14, 2022). For his participation in the conduct, Judge Cote ordered Shkreli to disgorge $64.4 million in profits and banned him for life from participating in the pharmaceutical industry. Id. at *1. The court's decision followed a seven-day bench trial in December. The New York Attorney General played a significant role in the case, bringing the action together with the Federal Trade Commission in federal court in New York. The attorneys general of six other states subsequently joined the action.

The case centered on Shkreli's conduct after Vyera, formerly known as Turing Pharmaceuticals, purchased the rights to Daraprim, a medication used to treat potentially fatal parasitic infections. In 2015, after the purchase, Vyera raised the price of Daraprim from $17.50 to $750 per pill. It also moved Daraprim from retail distribution to a closed distribution system, and entered into agreements with the two primary manufacturers for Daraprim's active pharmaceutical ingredient that restricted others' access to that ingredient. Judge Cote held that, in doing so, Vyera made it difficult for generic manufacturers to obtain sufficient samples of Daraprim to conduct bioequivalence and other studies needed for FDA approval, thus delaying the entry of generic competition for at least 18 months. Judge Cote found that this conduct violated federal and state antitrust laws, and that Shkreli himself was personally liable for such conduct due to the control he exercised over the company.

In this article, we provide several important takeaways from the *Shkreli* case that shed light not only on the latest trends in antitrust enforcement, but also the risks that major shareholders face when exercising control over companies that are vulnerable to accusations of antitrust or other legal violations.

Dramatic Price Hikes Untethered to Demand Can Lead To Intense Antitrust Scrutiny. In her

REED BRODSKY *is a partner at Gibson, Dunn & Crutcher, where he serves as co-chair of the firm's litigation practice group. He is a former Assistant U.S. Attorney in the United States Attorney's Office for the Southern District of New York.* ERIC J. STOCK, *a partner at the firm, focuses on antitrust litigation and investigations. He formerly served as Chief of the Antitrust Bureau at the New York Attorney General's Office.* JESSICA TRAFIMOW, *a recent law graduate in the firm's New York office, assisted in the preparation of this article.*

decision, Judge Cote cites fact testimony describing Shkreli's decision to dramatically increase the cost of Daraprim as the "poster child of everything that is considered wrong about the pharmaceutical industry." Id. at *11. Shkreli's over-the-top price increases, paired with his unapologetic public persona, undoubtedly drew extraordinary media and law enforcement attention to his company's business practices.

The case shows that even though there is ordinarily nothing unlawful about a company raising prices, dramatic price increases unconnected to increased demand can draw significant public attention and attract intense regulatory scrutiny. Here, that close scrutiny resulted in severe personal and professional penalties for Shkreli.

Restrictive Distribution Systems Can Be Considered an Anti-Generic Strategy. Daraprim had been in open retail distribution since the 1950s. Id. at *12. After purchasing the rights in 2015, Shkreli swiftly moved to create a highly restrictive closed distribution system. Judge Cote found that the express purpose of this change in distribution systems was to shut out generic competition. To accomplish this alleged goal, Vyera imposed class of trade restrictions that restricted who could buy Daraprim, limited the number of bottles that a single customer could purchase at a given time, bought back Daraprim inventory from wholesalers and distributors, and surveilled distributors' sales reports "to prevent the diversion of Daraprim to generic drug companies for [bioequivalence] testing." Id. at *14. Vyera also allegedly blocked access to pyrimethamine, Daraprim's active pharmaceutical ingredient, by entering into exclusive supply agreements with two of its largest manufacturers.

Judge Cote found that these practices significantly heightened the barriers to entry faced by generic manufacturers. Her finding that the restrictive agreements with distributors were illegal, anticompetitive conduct illustrates that the adoption of restrictive distribution systems—while not ordinarily unlawful—can serve as the basis for an antitrust violation where the knowing and intentional purpose and effect of such system is to impede generic entry. Accordingly, companies adopting closed distribution for legitimate and proper business reasons should carefully scrutinize such arrangements to determine whether any such measures might be viewed as having anticompetitive effects. And the same is true for agreements with suppliers that may impede generic manufacturers' access to key pharmaceutical ingredients.

Risks to Major Shareholders. Judge Cote found that Shkreli founded Vyera (initially known as Turing), was the company's first CEO, and masterminded the scheme to exclude Daraprim's generic competitors from the market. Even after he stepped down as Vyera's CEO following his December 2015 arrest, Judge Cote found that Shkreli "remained in functional control of Vyera's management and its business strategy." Id. at *28. Judge Cote relied on evidence that Shkreli continued to manage Vyera's leadership, direct corporate policy, and maintain the allegedly anticompetitive Daraprim scheme while in federal prison (serving time for an unrelated securities fraud) by wielding Shkreli's authority as the company's largest shareholder. For this conduct, Judge Cote held Shkreli personally liable under the Sherman Act and jointly and severally liable for the disgorgement remedy under New York state law.

This decision is a warning to shareholders of all types that exert a high degree of control over their companies' conduct. Where such companies are found to have engaged in anticompetitive conduct, major shareholders that

directed and controlled the business decisions behind such conduct face the risk that they themselves will be found liable as well. This case represents an extreme example of a shareholder exercising direct control over a company's operations. Nevertheless, there is a risk that federal and state enforcers, and even private plaintiffs, will try to invoke the reasoning of this decision when attempting to impose liability on shareholders in other circumstances. And while this risk may be especially significant for individual shareholders exercising control over the companies they founded, the reasoning of the decision could also arguably be applied to other types of shareholders—such as institutional shareholders—that law enforcement bodies, or private plaintiffs, may view as being the power and influence behind company management.

The New York Attorney General's Involvement Greatly Expanded the Remedies Available in the Case. The case also demonstrates the enhanced risk that companies face when antitrust investigations are undertaken by both federal and state antitrust enforcers—and, in particular, the New York Attorney General. The fact that the lawsuit was brought by both the FTC and New York Attorney General meant that Shkreli and his company faced not only the vast resources and experience of a leading federal antitrust enforcer, but also the significant additional resources—and legal remedies—available to the New York Attorney General. And, indeed, the remedies available to the New York Attorney General under New York state law made a significant difference in the outcome of the case, particularly after the U.S. Supreme Court recently ruled that the FTC lacks the power to order a company disgorge its profits. See *AMG Cap. Mgmt. v. Fed. Trade Comm'n*, 141 S. Ct. 1341 (2021). Judge Cote upheld the right of the New York Attorney General to seek disgorgement under §63(12) of the New York Executive Law, and that served as a key basis for her order requiring Shkreli to disgorge $64.4 million in profits. See *FTC v. Shkreli*, No. 20CV00706 (DLC), 2022 WL 135026 (S.D.N.Y. Jan. 14, 2022). In addition, provisions of New York law allowing a court to permanently ban individuals from an industry after a successful New York Attorney General action likely played a role in Judge Cote's finding that she had the authority to ban Shkreli from the pharmaceutical industry for life. Id. at *44.

The *Shkreli* case therefore highlights the risks posed when the FTC's enforcement powers are paired with the additional remedies afforded to certain state antitrust enforcers. Moreover, these remedies seem to have been available to the FTC and states without Mr. Shkreli having the right to a jury trial, because the FTC and state attorneys general did not pursue a traditional damages remedy.

Final Takeaways. Judge Cote's holding in *FTC v. Shkreli* is a stark reminder of the significant risks that face pharmaceutical and other companies when engaging in activities that generate significant negative media attention, such as price increases untethered to demand increases. The decision also illustrates that federal and state antitrust enforcers are not afraid to pursue novel theories of liability where they believe that business conduct is being used to impede competition. And, finally, the decision demonstrates that the risks posed by such activity also extend to institutional or other types of shareholders that exert substantial control over the activities of the company engaged in the conduct in question.