ANTITRUST AGENCIES RELEASE DRAFT VERTICAL MERGER GUIDELINES: A HEALTHCARE PERSPECTIVE

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The Department of Justice ("DOJ") Antitrust Division and the Federal Trade Commission ("FTC") recently released a draft of their updated Vertical Merger Guidelines (the "Guidelines"), the first update since 1984. Healthcare attorneys have anxiously awaited the Guidelines, hoping to gain insight into the agencies' analysis of combinations across different levels of the delivery system amid increasing enforcement. What do healthcare professionals need to know about the Guidelines and the potential impact on vertical mergers in the healthcare industry? Below, we offer our take on the Guidelines and look back at recent enforcement of vertical mergers in the industry.

OUR TAKE ON THE GUIDELINES

The Guidelines do not reflect a major departure from traditional merger analysis, but that approach to vertical mergers in and of itself is a significant change from the 1984 Guidelines. The previous Guidelines reflected the view that "non-horizontal mergers are less likely than horizontal mergers to create competitive problems," since they do not eliminate market competitors and have many pro-competitive justifications, such as lower prices and increased quality. In recent years, however, the agencies have shown increasing concern about the potential anticompetitive effects of vertical mergers, so it is not surprising that the updated Guidelines reflect this view. Under the proposed Guidelines, the agencies will now apply the same principles as those found in the Horizontal Merger Guidelines to determine whether a merger between vertically related companies will substantially lessen competition in any relevant markets. A previous alert discusses in detail the significant provisions of the Guidelines.

Despite recent and growing anticipation of future enforcement of vertical mergers in the healthcare industry, the Guidelines are silent on the topic of healthcare and do not use any healthcare-related examples. As in the horizontal merger context, the salient issue according to the draft Guidelines remains whether the proposed transaction will substantially lessen competition in the relevant markets. The draft Guidelines will be open for public comment until February 26, 2020, and additional changes could be made to the final version. [1] In light of the Guidelines, we look at several noteworthy healthcare vertical mergers below.

RECENT VERTICAL CHALLENGES IN THE HEALTHCARE INDUSTRY

In 2019, the FTC announced a settlement with UnitedHealth Group ("United") and DaVita Medical Group

("DaVita"), which resulted in United's divestiture of DaVita's Las Vegas operations. The settlement resolved the FTC's complaint that United's acquisition of DaVita would reduce competition in the Las Vegas area in markets for managed care provider organization services sold to Medicare Advantage insurers, as well as Medicare Advantage plans sold to individual Medicare Advantage members. The FTC alleged that United's acquisition of DaVita, a large combined managed care provider organization ("MCPO"), would allow United to raise the costs of its MCPO services to rival Medicare Advantage insurers.

The agencies have also successfully challenged mergers with both horizontal and vertical overlap in recent years. In 2019, the Eighth Circuit Court of Appeals upheld a 2017 preliminary injunction that halted Sanford Health's ("Sanford") acquisition of Mid Dakota Clinic ("Mid Dakota"), resulting in Sanford abandoning the acquisition. The FTC had alleged that Sanford, a healthcare system and seller of health insurance, would obtain market shares exceeding 75 percent across four practice areas through its acquisition of Mid Dakota, a provider of primary care and specialty medical and surgical services. The FTC argued that the fact that Mid Dakota was also the largest source of referrals for inpatient admissions to a competitor of Sanford was also relevant.

The challenge was very similar to the FTC's 2015 challenge of St. Luke's Health System's ("St. Luke's") acquisition of Saltzer Medical Group, a primary care provider in Idaho. Although decided based on horizontal overlap in the market for primary care, the district judge identified St. Luke's ability to constrain referrals from primary care physicians to another competing hospital system as an anticompetitive effect of the proposed acquisition.

Also, in 2018, the DOJ required CVS and Aetna to divest Aetna's Medicare Individual Part D prescription drug plan as part of its approval of CVS's acquisition of Aetna. Although commonly viewed as a vertical merger between an insurer, pharmacy benefit manager ("PBM"), and pharmacy chain, CVS also offered its own Medicare Individual Part D plan in competition with Aetna's, and the DOJ alleged that the combination would result in reduced quality and higher prices for consumers and the federal government.

In other mergers, the FTC and DOJ have investigated vertical issues but not required a remedy to approve the transaction. For example, in Cigna's 2018 acquisition of Express Scripts (another insurer-PBM merger), the DOJ conducted a six-month investigation before concluding that Cigna's acquisition of Express Scripts, a pharmacy benefit management company, would not reduce competition in the sale of PBM services or raise costs to Cigna's rivals for PBM services.

A common concern of the DOJ and FTC in these recent investigations and challenges has been the ability of the combined entity to reduce or deny supply of downstream products or services to competitors, or increase competitors' costs (also known as "foreclosure" from the market). The updated Guidelines contain a section dedicated to this concern and identify factors that DOJ and FTC will consider when analyzing vertical mergers (these factors are discussed in our previous alert).

CONCLUSION

It is difficult to predict how aggressively the current and future administrations will review vertical mergers, particularly in the healthcare industry. Clients considering mergers — particularly traditional horizontal mergers with a vertical component — are wise to work with antitrust counsel early to conduct a risk assessment of the merger and proactively prepare defenses, which can significantly reduce the risk of a challenge. K&L Gates'

health care and FDA practice and antitrust practice regularly advise clients on a broad range of healthcare and competition issues, can help assess risks, and, if necessary, can prepare defenses for anticipated mergers with vertical or horizontal components.

NOTES:

[1] The deadline for comments was originally February 11, 2020, but on February 3, DOJ and FTC announced that they were extending the deadline to February 23 and would also be holding two public workshops on the Guidelines on March 11 and 18 to further solicit public dialogue.

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