Antitrust Considerations Surrounding Health Care Consolidation Among Hospitals and Physicians

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The Affordable Care Act (“ACA”) has resuscitated the demand for hospital and health care provider mergers. The law explicitly encourages collaborative care—through, for example, financial incentives surrounding the creation of Accountable Care Organizations (“ACOs”), which are collaborative networks of doctors and hospitals that share responsibility for providing care to patients. In doing so, the law implicitly encourages consolidation of health care systems and providers. How much so? In 2009, the year before the ACA became law, there were 50 hospital merger or acquisition deals.1 In 2012, there were 105.2

But a recent health care consolidation illustrates the antitrust complications these deals can present. St. Luke’s Health System, the largest health care system in Idaho, expanded its nominal presence in the Nampa, Idaho, market by acquiring Saltzer Medical Group, the state’s largest independent group of physicians. Saltzer testified that it acquiesced to the acquisition because it recognized that it was too small to accomplish the infrastructural changes necessary to keep pace with the modernization of the medical industry. But unfortunately for Saltzer and St. Luke’s, the Federal Trade Commission (“FTC”), the State of Idaho, and two private competitors successfully challenged the deal on antitrust grounds, and a federal judge ordered divestiture.3 St. Luke’s and Saltzer have been unsuccessfully trying to ward off the undoing of the deal while their appeal is before the U.S. Court of Appeals for the Ninth Circuit.

Such challenges put health care providers in a predicament. On one hand, one set of federal laws encourages collaborative care. On the other hand, another set of federal laws can punish providers for collaborating too much. How can a provider walk this line?

The FTC has offered some direction. Its recent successful challenges of hospital deals provide lessons for any entity considering such a transaction. Further, in the past few months, FTC Chairwoman Edith Ramirez, FTC Commissioner Julie Brill, and FTC Competition Bureau Director Deborah Feinstein have commented at length about the agency’s post-ACA antitrust enforcement in the health care industry.4 When combined with the FTC’s recent enforcement actions, these remarks provide advice for providers who are considering consolidation.

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2 Id.
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What is the best way to avoid antitrust scrutiny, according to the FTC? Do not merge. Combinations that fall short of merger, such as joint ventures, and that provide for bona fide financial or clinical integration reasonably necessary to achieve consumer cost savings or improved care, may face less antitrust scrutiny. In contrast, the FTC may be more critical of completely merged entities. In these merger deals, the agency is often skeptical of two common defenses: the efficiencies defense and the failing/flailing firm defense.

Consolidating entities often argue that their consolidation creates pro-consumer efficiencies that outweigh any possible negative effects on consumers. But this argument can falter on two fronts. First, the FTC often maintains that these efficiencies can happen without a merger. For example, in St. Luke’s, the defendants asserted that they needed to merge so that Saltzer could upgrade its patient recordkeeping technology, something it had wanted to do for years but could not afford to do. The FTC successfully argued that this could happen absent the merger. As the court found, St. Luke’s had already started to share record technology with other providers with whom it had not merged. Second, even if these efficiencies are merger-specific, they still have to outweigh the anticompetitive effects of the deal. If a court is convinced that the proposed merger would lead to, for example, unjustified consumer price increases, no amount of potential efficiencies is likely to tip the scale. As the district court noted in Federal Trade Commission v. ProMedica Health System, Inc., another recent failed health care merger, “[n]o court . . . has found efficiencies sufficient to rescue an otherwise illegal merger.”

Defendants also often argue that consolidation is necessary and procompetitive because one of the parties will not be able to keep its doors open without the financial support of the other party. The legal standard for such a failing firm defense is very high, however. In ProMedica, the acquiring defendant argued on appeal that the acquired hospital was a flailing firm—not yet at the legal standard of failing, but sufficiently close to being there that the court should allow the deal to stand. The Sixth Circuit characterized this argument as the “Hail-Mary pass of presumptively doomed mergers” and rejected it.

If providers do want to consolidate, however, there are some factors that are symptomatic of the level of antitrust attention a deal will attract. Of these, market share in the local health care market is the most important. The FTC heavily weighs the Herfindahl-Hirschman Index presumptions

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6 See id. at § 11 (discussing the failing firm defense).
7 Brill, supra, note 4, at 9 (“[T]he ACA neither requires nor encourages providers to merge or otherwise consolidate, but rather encourages providers to create entities that coordinate the provision of patient care services.”); Feinstein, supra, note 4, at 2 (“[T]he ACA does not require providers to merge or consolidate and recognizes that ACOs may be formed through contractual arrangements that are well short of a merger.”).
9 Id. at *18–19.
10 See Horizontal Merger Guidelines, supra note 5, at § 10.
13 Id.
14 See Brill, supra note 4, at 4–5; Feinstein, supra note 4, at 5.
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outlined in the Horizontal Merger Guidelines. Thus it is not surprising that the agency pays greater attention to deals in markets (although they are often small) where the number of providers would drop to three or fewer, and the new entity would have a relatively large market share. Conversely, small market shares are unlikely to garner much attention; the FTC has even carved out safety zones for ACOs based on market share, although these safety zones do not extend to merged entities. Small market share should not be confused with small transactions, however—the fact that a deal is not subject to the mandatory reporting requirements of the Hart-Scott-Rodino Act does not mean that it will avoid a challenge.

A merger’s predicted effect on consumer pricing is also a significant factor in the FTC’s analysis, especially where higher prices are not due to higher quality services but instead are the result of the leverage the merger provides to the combined entity to demand higher reimbursement rates from payers. The parties’ expressed intent is not determinative, but it can be illuminative. In this regard, both of the cases discussed above demonstrate the importance of carefully managing discussions around any proposed combination or collaboration. For example, in ProMedica, the FTC relied on an email from one merging party’s CEO stressing that a main advantage of the deal would be to increase the combined entity’s ability to negotiate higher reimbursement rates while noting that the deal might increase patient costs. Evidence like this led the Sixth Circuit in that case to remark that “the [FTC’s] best witnesses were the merging parties themselves.” Similarly, in St. Luke’s, the FTC relied on one of the merging parties’ internal documents stating that the merger would increase the merged entity’s negotiating leverage and allow it to extract higher reimbursements. It is clear that the FTC will look to the intent behind a health care merger in assessing whether the merger will produce anticompetitive effects. And often, internal documents from the parties’ unmanaged discussions supply the FTC with the damning evidence it seeks.

Concerned providers should get advice. This starts with involving, as early as possible in the process, lawyers who understand the intersection of health care and antitrust laws. As stated recently by the FTC’s chairwoman, antitrust enforcement in the medical industry is a “top priority.” And, in the FTC’s eyes, “the ACA is not a free pass” to bend the manner in which the agency has traditionally enforced antitrust laws. When health care providers are considering consolidation, other concerns, such as patient care and business effects, likely come to mind before antitrust considerations. But it is becoming increasingly evident that ignoring the antitrust concerns suggested by the FTC can prove fatal to a deal.

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15 See, e.g., Brill, supra note 4, at 5.
16 See id. at 7.
19 ProMedica Health Sys., Inc., 749 F.3d at 563 (describing an email from one of the parties’ CEO in which he stated that the merger “had the greatest potential for higher hospital rates” and could “harm the community by forcing hospital rates on them” (alterations omitted)).
20 Id. at 571.
22 Ramirez, supra, note 4.
23 Brill, supra note 4, at 14.
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