Health Care Antitrust

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# FTC Successfully Obtains Divestiture of Physician Group Previously Acquired by Hospital System

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In a significant groundbreaking victory, on January 24, 2014 after a bench trial, an Idaho federal district court judge upheld the FTC's antitrust challenge to a hospital system's (St. Luke's) acquisition of a multispecialty physician group (Saltzer Medical Group) and ordered divestiture as a remedy. *FTC v. St. Luke's Health System, Ltd.,* (D. Idaho, Jan. 24, 2014). The case is notable in several respects. Particularly if upheld on appeal, it validates the increased antitrust scrutiny that physician consolidations and physician acquisitions by hospital systems are undergoing. Moreover, the hospital system defended the acquisition as a necessary step toward practicing integrated medicine and population health management—goals that underlie much of today's health care reform. The district court, while acknowledging these beneficial objectives underlying the transaction to improve the quality of medical care, said those objectives were deemed not merger specific nor sufficient to trump the substantial risk of anticompetitive price increases, where the acquisition led to a 80 percent market share for primary care physicians (PCPs).

The case involved the acquisition of Saltzer, a 41 physician multispecialty group, nearly three-quarters of whom provided primary care services, located in Nampa, Idaho. The acquiring system, St. Luke's, operated an emergency clinic with outpatient services in Nampa. It had no hospital in Nampa, but had 7 hospitals in Idaho, including the 400-plus bed St. Luke's Boise Medical Center.

The relevant product market was not disputed—Adult Primary Care Services (Adult PCP services) sold to commercially insured patients. In many health care antitrust cases, particularly in hospital merger challenges, the relevant geographic market definition has been a contentious, often dispositive, issue. While not a hospital merger, it was an important issue here as well. The court determined the geographic market here by purportedly applying the "SSNIP test"—whether all the sellers would be able to impose a small but significant, non-transitory increase in price (5 to 10 percent) and still make a profit. Relying upon payer testimony, and the facts that Blue Cross of Idaho (BCI) attempts to have PCPs in-network in every zip code where they have enrollees and that 68 percent of Nampa residents obtain their primary care in Nampa, so that health plans must offer Nampa Adult PCP services to Nampa residents to successfully compete, the court concluded that Nampa PCPs could successfully band together and obtain a 5 to 10 percent price increase. Nampa was therefore found to be a relevant geographic market.

Those conclusions led the court to calculate market concentration numbers that set off alarm bells under the Horizontal Merger Guidelines. Combined, St Luke's and Saltzer account for nearly 80 percent of Adult PCP services in Nampa. As a result of the merger, the Nampa PCP market has a post-merger HHI of 6,219, and an increase in HHI of 1,607, both of which are above the thresholds for a presumptively anticompetitive merger. Hence, the FTC received the benefit of the presumption of establishing a prima facie case under Section 7 of the Clayton Act, established in *United States v. Philadelphia Nat'l Bank*, 374 U.S. 321 (1963).

The court did not stop there in making findings of anticompetitive effect. Looking at St. Luke's hospitals, it found that

St. Luke's had leverage preacquisition, and if St. Luke's chose not to contract with BCI, BCI would have an immediately unsustainable product. The court then concluded that the acquisition would increase St. Luke's bargaining leverage. In Nampa, it found that St. Luke's and Saltzer were each other's closest substitutes. The court concluded that the acquisition adds to St. Luke's market power and weakens BCI's ability to negotiate with St. Luke's. The court found this conclusion buttressed by an internal St. Luke's email suggesting that they could improve their financial performance through a price increase and by internal Saltzer documents suggesting that they would have increased bargaining leverage to win back concessions that they had made to BCI. The court also "found" that it is likely that St. Luke's will exercise its enhanced bargaining leverage from the acquisition to charge at the higher hospital-based billing rates for more services. Finally, the court made findings of anticompetitive effects in that Saltzer referrals to St. Luke's would increase.

In the introduction to its 52-page opinion, the court acknowledged the cost and quality concerns in the health care delivery system and the need to move away from the fee-for-service reimbursement system. The court complimented St. Luke's "foresight and vision" in being early to assemble "a team committed to practicing integrated medicine in a system where compensation depended on patient outcomes." The court indicated: **"The Acquisition was intended by St. Luke's and Saltzer primarily to improve patient outcomes. The Court believes that it would have that effect if left intact, and St. Luke's is to be applauded for its efforts to improve the delivery of health care in the [relevant market.] But there are other ways to achieve the same effect that do not run afoul of the antitrust laws and do not run such a risk of increased costs."**

As a consequence, the court concluded that the "efficiencies" of enhancing coordinated care, accepting risk, and managing population health advanced by St. Luke's did not outweigh the anticompetitive effects and save the acquisition. St. Luke's argued that it believed that the best way to create a unified and committed team of physicians required to practice integrated medicine was to employ them. The court rejected that defense by making the following findings:

- There is no empirical evidence to support the theory that St. Luke's needs a core group of employed primary care physicians beyond the number it had before the acquisition to successfully make the transition to integrated care.
- Integrated care—and risk-based contracting—do not require a large number of physicians because the health plans "manage the level of risk proportionate to the level of the provider organization."
- In Idaho, independent physician groups are using risk-based contracting successfully.
- It is the committed team—and not any one specific organization structure—that is the key to integrated medicine.
- Because a committed team can be assembled without employing physicians, a committed team is not a merger-specific efficiency of the acquisition.

Similarly, the court rejected the common electronic medical record (EMR) as a merger specific efficiency. While St. Luke's touted its roll out of the EPIC EMR system, it acknowledged that it was developing an Affiliate Electronic Medical Record program that would allow independent physicians access to EPIC.

Drawing on historical case law, the court recognized that divestiture is the "remedy best suited to redress the ills of an anticompetitive merger." It was comforted by the fact that St. Luke's had represented to the court that it "will not oppose divestiture on grounds that divestiture cannot be accomplished" and that "any financial hardship to Saltzer from divestiture would be mitigated by St. Luke's payment of $9 million for goodwill and intangibles as part of the Acquisition, a payment that does not have to be paid back if the Acquisition was undone." The court rejected St. Luke's proposal to substitute separate negotiations by St. Luke's and Saltzer with health plans as an alternative to divestiture. It also rejected the FTC's proposal that St. Luke's be ordered to give the FTC prior notice of all future proposed acquisitions.

The court summarized its thinking in its conclusion. It acknowledged "health care is at a crisis point" and "the Acquisition is an attempt by St. Luke's and Saltzer to improve the quality of medical care." Nonetheless, the court determined that "the particular structure of the Acquisition—creating such a huge market share for the combined

entity—creates a substantial risk of anticompetitive price increases." It reasoned: "In a world that was not governed by the Clayton Act, the best result might be to approve the Acquisition and monitor its outcome to see if the predicted price increases actually occurred. In other words, the Acquisition could serve as a controlled experiment. But the Clayton Act is in full force, and it must be enforced. The Act does not give the Court discretion to set it aside to conduct a health care experiment."

St. Luke's has already indicated it will appeal. For now, however, this case stands as an important precedent indicating that in situations with high market shares and evidence of price increases, efficiency claims and goals consistent with health care reform may not be a sufficient shield against traditional antitrust analysis.

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