Diagnosing the FTC's Merger Enforcement in the Healthcare Industry

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The healthcare industry has seen a flurry of merger activity in 2009. But, consolidation in this industry is not new, and the Federal Trade Commission (FTC or Commission) has been closely scrutinizing healthcare transactions for years. These transactions, however, come at a juncture when the antitrust enforcement agencies are poised for more aggressive antitrust review and also when healthcare reform—and the call for more affordable healthcare—dominate the news. So, while it should come as no surprise that the FTC will be aggressive in its enforcement activities relating to potentially anticompetitive healthcare consolidations, the question remains as to how the FTC may effectuate such an objective.

The FTC's long and aggressive enforcement history with regard to hospital consolidations provides an ideal backdrop for tracing the FTC's merger policy in the broader healthcare context. From the 1990s when the antitrust authorities had little success in challenging hospital transactions[1] to the FTC's most recent successes in *Inova Health Systems Foundation*[2] and *Carilion Clinic*,[3] the FTC has sharpened its approach in challenging these transactions in an effort to increase its likelihood of success.

The 1990s and Early 2000s

Since the early 1990s, the antitrust agencies have been aggressive in challenging local hospital mergers. In a span of about 12 years, federal and state antitrust authorities brought seven hospital merger cases.[4] But, despite the antitrust authorities' efforts and concerns, they found little success.

In all of these cases, the authorities approached the analysis in the traditional manner that emphasized a narrow relevant geographic market and argued that high market share and few competitors would lead to increased healthcare costs. Many courts, however, rejected the government's narrowly defined geographic markets, finding that competition was not static and patients either already did travel or would travel to other nearby hospitals if prices increased.[5] For example, in *Federal Trade Commission v. Tenet Healthcare Corporation*, the court stated "[t]he FTC's contention that the merged hospitals would have eighty-four percent of the market for inpatient primary and secondary services within a contrived market area that stops just short of including a regional hospital . . . that is closer to many patients than the Poplar Bluff hospitals, strikes us as absurd."[6]

After defining the relevant geographic market, the courts then looked to the competitive effects of the transaction. In doing so, a number of courts gave credit to the parties' arguments regarding their non-profit status and their commitment to the community. In *United States v. Long Island Jewish Medical Center*, the court found that the hospitals already "provide millions of dollars worth of free medical care" and that "the trustees of the merging business entities include successful business and religious leaders who are not compensated for their services."[7] The court further stated that "the same profit-maximizing incentives driving private companies are less central to the merging hospitals' progress," which all "support defendants' contention that community service not profit maximization, is the hospitals' mission."[8] Finally, a handful of courts also found merit in defendants' arguments that managed care organizations' buyer power was capable of shifting business to competing hospitals.[9]

The Retrospective and Evanston Northwestern Healthcare

After this string of defeats, in August of 2002, the FTC announced the formation of the Merger Litigation Task Force that, among other things, would be "responsible for reinvigorating the Commission's hospital

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[1] *See, e.g.*, Fed. Trade Comm'n v. Tenet Healthcare Corp., 186 F.3d 1045 (8th Cir. 1999); United States v. Long Island Jewish Med. Ctr., 983 F. Supp. 121 (E.D.N.Y. 1997); California v. Sutter Health Sys., 130 F. Supp. 2d 1109 (N.D. Cal. 2001), *aff'd mem.* 217 F.3d 846 (9th Cir. 2000) (brought by the California Attorney General without federal antitrust agency involvement); Fed. Trade Comm'n v. Butterworth Health Corp., 946 F. Supp. 1285 (W.D. Mich. 1996), *aff'd mem.* 121 F.3d 708 (6th Cir. 1997); United States v. Mercy Health Servs., 902 F. Supp. 968 (N.D. Iowa 1995), *vacated as moot,* 107 F.3d 632 (8th Cir. 1997); Fed. Trade Comm'n v. Freeman Hosp., 911 F. Supp. 1213 (W.D. Mo. 1995), *aff'd,* 69 F.3d 260 (8th Cir. 1995); Fed. Trade Comm'n v. Hosp. Bd. of Directors of Lee County, 1994-1 Trade Cas. (CCH) ¶ 70,593 (M.D. Fla. 1994), *aff'd*, 38 F.3d 1184 (11th Cir. 1994).

[2] Order dismissing complaint, Inova Health Sys. Found., Dkt. No. 9326 (Fed. Trade Comm'n 2008), *available at* http://www.ftc.gov/os/adjpro/d9326/index.shtm.

[3] Consent Order, Carilion Clinic, Dkt. No. 9338 (Fed. Trade Comm'n 2009), *available at* http://www.ftc.gov/os/adjpro/d9338/index.shtm.

[4] *Tenet Healthcare Corp.*, 186 F.3d at 1045; *Long Island Jewish Med. Ctr.*, 983 F. Supp. at 121; *Sutter Health Sys.*, 130 F. Supp. 2d at 1137; *Butterworth Health Corp.*, 946 F. Supp. at 1285; *Mercy Health Servs.*, 902 F. Supp. at 968; *Freeman Hosp.*, 911 F. Supp. 1213; *Hosp. Bd. of Directors of Lee County,* 1994-1 Trade Cas. (CCH) ¶ 70,593.

[5] *See, e.g.*, *Tenet*, 186 F.3d at 1053-54; *Sutter Health Sys.*, 130 F. Supp. 2d at 1132; *Freeman Hosp.*, 911 F. Supp. at 1226-27.

[6] *Tenet*, 186 F.3d at 1053-54.

[7] *Long Island Jewish Med. Ctr.*, 983 F. Supp. at 146.

[8] *Id.*; *see also Butterworth*, 946 F. Supp. at 1297 ("The nonprofit status of the hospitals is not a dispositive consideration, but it is material."); *Freeman Hosp.*, 911 F. Supp. at 1227 ("the merging hospitals' status as nonprofit entities must also be considered").

[9] *See e.g.*, *Tenet*, 186 F.3d at 1054 ("In spite of their testimony to the contrary, the evidence shows that large, sophisticated third-party buyers can [and] do resist price increases, especially where consolidation results in cost savings to the merging entities.").

merger program, which includes a review of, and potential challenges to, consummated transactions that may have resulted in anticompetitive price increases,"[10] as well as "develop[ing] new strategies for trying them."[11] The Commission anticipated that, regardless of the conclusion of this retrospective, it would "obtain useful real-world information, allowing the Commission to update its prior assumptions about the consequences of particular transactions and the nature of competitive forces in health care."[12] Ultimately, the retrospective resulted in the Commission filing one administrative complaint.[13]

That complaint, filed in 2004, concerned the acquisition of Highland Park Hospital (Highland Park) by Evanston Northwestern Healthcare Corp. (ENH), which occurred in 2000. ENH was comprised of two hospitals, Evanston Hospital and Glenbrook Hospital. Both of these hospitals, as well as Highland Park, operated in the northern suburbs of Chicago. The FTC alleged that the transaction substantially lessened competition for "acute care inpatient hospital services sold to private payers" in the area surrounding the hospitals.[14]

Once again, in challenging the transaction, the FTC relied on a narrowly defined geographic market. But, the FTC also had a great deal of pricing information—made possible, in part, because the challenge took place after consummation—to demonstrate that pricing significantly increased immediately following the transaction. The Administrative Law Judge (ALJ) ruled in favor of the FTC[15] and the Commission affirmed the ALJ's conclusion on appeal.[16]

The Commission's opinion in *Evanston* is notable for a number of reasons. First, rather than relying solely on the traditional tools for relevant geographic market analysis in hospital transactions, such as patient flow data and patient travel times, the Commission's opinion found that the supracompetitive pricing post-transaction supported the relevant geographic market.[17] The Commission made such a finding despite acknowledging earlier in the opinion that nine hospitals were closer to the merging entity than the merging entities were to each other.[18] Second, Commissioner Rosch's concurring opinion focused on competition for hospitals to be included in provider networks, as opposed to the traditional approach of competition for patients.[19] Commissioner Rosch's approach appears to take a more expansive view of competition, which recognizes that healthcare markets are unique in that there are intermediaries—such as insurers that make the actual payments to the hospitals, and doctors that prescribe the course of treatment—that may affect the competitive process. Both the Commission's opinion and Commissioner Rosch's concurrence went a long way toward addressing the FTC's prior losses and setting a slightly modified course for challenging these types of transactions going forward.

Inova-Prince William

Building on its win in *Evanston*, the Commission challenged the attempted acquisition of Prince William Hospital (Prince William) by Inova Health System (Inova) in 2008. Inova is comprised of five hospitals in the Northern Virginia area, with a number of its hospitals recognized as among the best in the United States.[20] Prince William, on the other hand, was a 44 year-old community hospital also located in Northern Virginia.[21] The transaction would have joined these two

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[10] Press Release, Fed. Trade Comm'n, Federal Trade Commission Announces Formation of Merger Litigation Task Force (Aug. 28, 2002), *available at* http://www.ftc.gov/opa/2002/08/mergerlitigation.shtm.

[11] Timothy J. Muris, Chairman, Fed. Trade Comm'n, Everything Old is New Again: Health Care and Competition in the 21st Century," Prepared Remarks Before the 7th Annual Competition in Health Care Forum 19 (Nov. 7, 2002), *available at* http://www.ftc.gov/speeches/muris/murishealthcarespeech0211.pdf.

[12] *Id.* at 19-20.

[13] *See* Complaint, Evanston Northwestern Healthcare Corp., Dkt. No. 9315 (Fed. Trade Comm'n 2004) [hereinafter Evanston Complaint], *available at* http://www.ftc.gov/os/caselist/0110234/040210emhcomplaint.pdf. No formal report detailing the results of the retrospective has been published. Two working papers on the retrospective analysis were, however, published in January of 2009. *See* Deborah Haas-Wilson & Christopher Garmon, Two Hospital Mergers on Chicago's North Shore: A Retrospective Study (Jan. 2009), *available at* http://www.ftc.gov/be/workpapers/wp294.pdf; Aileen Thompson, The Effect of Hospital Mergers on Inpatient Prices: A Case Study of the New Hanover-Cape Fear Transaction (Jan. 2009) *available at* http://www.ftc.gov/be/workpapers/wp295.pdf.

[14] Evanston Complaint, *supra* note 13, at ¶¶ 16-17.

[15] *See* Initial Decision, Evanston Northwestern Healthcare Corp., Dkt. No. 9315 (Fed. Trade Comm'n 2005), *available at* http://www.ftc.gov/os/adjpro/d9315/051021idtextversion.pdf.

[16] *See* Opinion of the Commission, Evanston Northwestern Healthcare Corp., Dkt. No. 9315 (Fed. Trade Comm'n 2007) [hereinafter Evanston Commission Opinion], *available at* http://www.ftc.gov/os/adjpro/d9315/070806opinion.pdf. The Commission Order, however, provided for a conduct remedy, and not the structural remedy sought and obtained by the FTC staff in the ALJ's opinion. *See* Opinion of the Commission on Remedy, Evanston Northwestern Healthcare Corp., Dkt. No. 9315 (Fed. Trade Comm'n 2008), *available at* http://www.ftc.gov/os/adjpro/d9315/080428commopinionremedy.pdf.

[17] Evanston Commission Opinion, *supra* note 16, at 63-64 ("Thus, here, if complaint counsel has proven that the significant higher-than-predicted post-merger price increases resulted from market power gained through the merger, then complaint counsel has correctly defined the geographic market as the triangle formed by the three ENH hospitals."). Commissioner Rosch's concurrence went even further stating:

> Where, as here, the post-transaction record establishes that the transaction has produced unilateral anticompetitive effects, it is not essential to define the relevant market upfront using the methodology described in the Horizontal Merger Guidelines. At least the 'rough contours' of the relevant market can be identified on the basis of those effects, and that is sufficient as a matter of law."

Concurring Opinion of Commissioner J. Thomas Rosch at 2, Evanston Northwestern Healthcare Corp., Dkt. No. 9315 (Fed. Trade Comm'n 2007) [hereinafter Rosch Concurrence], *available at* http://www.ftc.gov/os/adjpro/d9315/070806rosch.pdf.

[18] Evanston Commission Opinion, *supra* note 16, at 13-14 ("There are, however, other nearby hospitals, including nine hospitals that are closer to Evanston, Glenbrook or Highland Park than they are to each other.").

[19] *See* Rosch Concurrence, *supra* note 17, at 1 (the anticompetitive effects are, in part, "based on the unique competitive dynamics of hospital markets, stemming from the bargaining between hospitals and managed care organizations ('MCOs') over inclusion in MCO networks that is described by the Commission opinion").

[20] *See* Inova Health System Awards and Recognition, *available at* http://www.inova.org/about-inova/awards-and-recognition/index.jsp. Among other awards and recognition earned by Inova, Inova Fairfax was ranked by U.S. News & World Report as one of "America's Best Hospitals," and Inova Fairfax was also ranked as one of "America's 50 Best Hospitals" by HealthGrades, an independent healthcare ratings agency that examines the quality of clinical outcomes among U.S. hospitals.

[21] After Inova and Prince William abandoned the proposed merger, Prince William placed itself back on the market and, in July of 2009, completed a merger with Novant Health, a non-profit system based in North Carolina.

non-profit entities and resulted in Inova investing $200 million in Prince William to increase bed capacity, add and upgrade facilities, and enhance the overall quality of care.[22]

The FTC alleged the merger would substantially lessen competition for general, acute care inpatient hospital services sold to private payers in Northern Virginia.[23] While the FTC alleged a narrow geographic market that excluded hospitals in Maryland and the District of Columbia, it decidedly focused the Inova Complaint on the likely price increases and the impact on individuals and businesses.[24] But, unlike *Evanston*, the FTC challenged *Inova* prior to consummation of the transaction and, therefore, did not have evidence of actual price increases. Still, the FTC alleged that not only would higher hospital prices for health insurers lead directly to higher health care costs for the plans' members, but "the most significant impact" would be on small employers and their employees, and a post-merger price increase might prevent small businesses that currently offer health insurance from doing so in the future.[25] Moreover, the Inova Administrative Complaint alleged that small employers that aspire to offer health insurance would not be able to afford such a price increase, and as a result, employees might "forego[ ] the care they can no longer afford" because the health insurance covered less or they were not offered health insurance.[26]

More significantly, the Inova Administrative Complaint demonstrates the FTC's cautious approach to quality and efficiency arguments. Despite Inova's commitment to contribute $200 million to Prince William to upgrade the facilities, add bed capacity, and improve the quality of care, the FTC alleged in its Inova Administrative Complaint that "Inova is unlikely to improve [Prince William's] quality of service or to help generate other efficiencies sufficient to offset the [m]erger's anticompetitive effects."[27] Such an allegation signals that where the FTC believes a transaction could result in less affordable healthcare, the FTC will be wary of accepting that quality and significant synergies can overcome a potential price increase. And while there were numerous important procedural changes to the FTC's approach,[28] the FTC's litigation strategy demonstrated the lengths to which the Commission will go in order to aggressively challenge transactions that may result in price increases—even where there appear to be cognizable benefits with respect to quality.

Carilion Clinic

In October of 2009, the FTC settled with Carilion Clinic (Carilion), a Virginia-based healthcare company, over its acquisition of the only two outpatient clinics in the Roanoke, Virginia area.[29] Carilion had an ownership interest in eight acute care hospitals and various other healthcare business interests in Southwest Virginia, including Roanoke Memorial Hospital and Roanoke Community Hospital. The two clinics Carilion attempted to acquire, the Center for Advanced Imaging and the Center for Surgical Excellence, were the only two clinics in Roanoke not owned by Carilion.

The FTC issued an administrative complaint alleging that Carilion's acquisition of these outpatient centers eliminated important competition that benefitted patients, employers, and health plans. The FTC further alleged that the acquisition resulted in the retention of only one competitor, HCA, the only other major hospital system in the Roanoke area.[30] The FTC press release issued with the complaint also stated that the transaction resulted in higher health care costs for outpatient services, "with out-of-pocket costs for many patients likely increasing nearly 900 percent for some treatments," and that these higher prices were subsequently "lead[ing] to higher premiums and the risk of reduced coverage for needed services."[31] Ultimately, Carilion entered into a consent order that provided for divestiture of both of the clinics it had acquired.

The FTC's actions in *Carilion* are notable for a few reasons. First, *Carilion* demonstrates that when there are, or are likely to be, price increases the FTC will extend its review of mergers to areas of healthcare—including very local practices—that previously had not been a focus for the FTC. Second, the enforcement action reiterates the FTC's concern about price effects and affordable healthcare options. Finally, *Carilion* confirms that transactions are not immune simply because they have been consummated. Rather, the FTC is going to continue to challenge transactions that they believe are likely to result, or have resulted, in increased prices.

Future Implications

The FTC has always had concern with the rising costs of healthcare and has carefully scrutinized transactions in the healthcare industry to ensure that consolidation did not contribute to increasing healthcare costs. The FTC's recent actions in *Inova* and *Carilion Clinic* are similar to, and in line with, its historic concerns and efforts, but they also demonstrate that the FTC has refined its approach in a number of ways in challenging these transactions to ensure a greater likelihood of success.

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22 Complaint for Preliminary Injunction at ¶ 28, Fed. Trade Comm'n v. Inova Health Sys. Found., No. 1:08CV460 (E.D. Va. May 12, 2008) [hereinafter Inova Complaint for Preliminary Injunction].

23 Complaint, Inova Health Sys. Found., Dkt. No. 9326 (Fed. Trade Comm'n 2008), *available at* http://www.ftc.gov/os/adjpro/d9326/080509admincomplaint.pdf [hereinafter Inova Administrative Complaint].

24 *See id.* ¶¶ 15, 21, 32.

25 *Id.* ¶ 32.

26 *Id.*

27 *Id.* ¶ 35. As part of Novant's subsequent acquisition of Prince William, Novant agreed to invest more than $240 million in Prince William's infrastructure. *See* Jennifer Buske, *Prince William Hospital Seals $240 Million Merger Deal*, Wash. Post, July 5, 2009, *available at* http://www.washingtonpost.com/wp-dyn/content/article/2009/07/02/AR2009070203396.html.

28 For a detailed discussion of the process changes, *see, e.g.*, Robert C. Jones & Aimee E. DeFilippo, *FTC Hospital Merger Challenges: Is a "Fast Track" Administrative Trial the Answer to the FTC's Federal Court Woes?*, THE ANTITRUST SOURCE (Dec. 2008).

29 *See* Agreement Containing Consent Order, *Carilion Clinic*, Dkt. No. 9338 (Fed. Trade Comm'n 2009), *available at* http://www.ftc.gov/os/adjpro/d9338/091007carilionclinicagree.pdf.

30 *See* Administrative Complaint, *Carilion Clinic*, Dkt. No. 9338 (Fed. Trade Comm'n 2009), *available at* http://www.ftc.gov/os/adjpro/d9338/090724carilioncmpt.pdf.

31 Press Release, Fed. Trade Comm'n, FTC Challenges Carilion's Acquisition of Outpatient Medical Clinics (July 24, 2009), *available at* http://www.ftc.gov/opa/2009/07/carilion.shtm.

First, the FTC continues to approach efficiency and quality arguments with extreme caution in the face of price increases—especially in the healthcare context where increasing prices are of utmost public concern. While efficiency and quality arguments are difficult to measure and therefore not easy to assess, the FTC's challenge in *Inova* seems to demonstrate that the FTC will be increasingly cautious in analyzing potential quality benefits in the face of price increases.

Second, the FTC continues to challenge consummated transactions where there have been, or there are very likely to be, price increases. As *Evanston* and, more recently, *Carilion Clinic* demonstrate, the FTC has been successful in using pricing evidence to challenge transactions that have already closed. Consequently, as a practical matter, parties to hospital consolidations must carefully consider both pre-transaction and post-transaction pricing behavior or risk a post-closing challenge by the FTC.

Third, the FTC is likely to continue the expansion of its enforcement activities into healthcare markets that have traditionally experienced low levels of enforcement. The FTC's challenge in *Carilion Clinic* demonstrates that no matter how small or how local a transaction, the FTC is willing to step in to ensure that consolidation is not the cause for a price increase.