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Expert Analysis

Court Voids Hospital Acquisition Of Physician Practice

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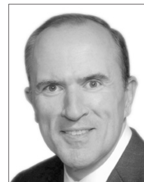

For generations, health care services in the United States have been paid for (or "reimbursed") based upon the so-called fee-for-service model. A hospital or physician develops a set of charges for their medical services. Health insurers also establish what they will pay health care providers, (e.g., 80 percent of what is charged) and what they will require their insureds to pay as deductibles and/or co-payments. Managed care plans such as health maintenance organizations contract with providers to be in their network and to accept negotiated payments as opposed to the providers' charges; the plans then offer to minimize or eliminate deductibles and co-payments to their members if the members obtain their health care services from their network providers.

The fee-for-service model has long been criticized for creating economic incentives for hospitals, physicians and other providers to maximize high-profit and expensive treatments and procedures, rather than focusing on meeting the patient's actual medical needs and paying for satisfactory patient outcomes. It is also regarded as one of the reasons for the dramatic rise in health care spending that has taken place over decades. Health care now accounts for approximately 17-18 percent of the gross domestic product, and it is estimated to grow to 20 percent in the coming years, the highest by far among industrialized nations.

There has long been a policy consensus that the economics of health care should be re-directed toward providing better quality and more cost-effective medical care, and enhancing primary and preventive care. One of the major components of the Patient Protection and Affordable Care Act[1] (ACA) is the concept of financially rewarding providers for offering better care and improved patient outcomes, and penalizing poor quality, unnecessary, or untimely care. To that end, the ACA encourages the development of larger and more integrated health care systems, such as the so-called Accountable Care Organizations, that can provide the full spectrum of patient care services, including inpatient hospital care, outpatient services, ambulatory surgery, nursing and rehabilitation care, and home health care services. In theory, such systems will reduce unnecessary and duplicative overhead, thereby lowering the costs of delivering care, as well as improving the quality of care by creating more continuity and better supervision.

The ACA has spurred countless provider combinations around the country. Many hospital systems eager to qualify as Accountable Care Organizations have been acquiring physician medical practices, making the doctors their employees, and establishing financial incentives for physician productivity and quality. However, a recent federal court decision in Idaho may have created a significant obstacle to the formation of some integrated health care delivery systems. Ironically, it came about as a result of a challenge by the Federal Trade Commission (FTC).

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St. Luke's Case

St. Luke's Health System is a not-for-profit health system in Idaho that operates three large hospitals and four smaller "critical access" hospitals in Boise, Meridian, and other nearby cities. It also operates an emergency clinic with outpatient services in the city of Nampa. The Saltzer Group is a 41-physician multi-specialty medical practice with most of its offices in Nampa, but also offices in nearby Meridian and Caldwell. It is the largest independent multi-specialty medical group in Idaho. Saltzer has 19 family practitioners and internists and 10 pediatricians, meaning that nearly three-quarters of the group provides adult or pediatric primary care services.

A recent federal court decision in Idaho may have created a significant obstacle to the formation of some integrated health care delivery systems.

Saltzer previously had attempted to affiliate or coordinate with other health care facilities in the Boise area, to no avail. In 2012, St. Luke's purchased the group for up to $16 million and entered into a five-year professional services agreement (PSA) with Saltzer's physicians. While the PSA prohibited the Saltzer physicians from being employed by or financially affiliated with other hospitals, it did allow them to have privileges at competing hospitals and to refer their patients to any practitioner or facility regardless of whether they were affiliated with St. Luke's. Saltzer believed that its linkage with St. Luke's would not only provide more integrated and cost-effective care, but would also increase access to care for Medi-

care, Medicaid and uninsured patients in communities serviced by St. Luke's and Saltzer.

A number of competing hospitals in the area filed an antitrust suit in federal court challenging St. Luke's acquisition of the Saltzer Group, claiming that it would substantially reduce competition for various types of physician and hospital inpatient and outpatient services in the areas served by St. Luke's and Saltzer. (One of the plaintiff hospitals, St. Alphonsus, had been unsuccessful in its own effort to acquire the Saltzer Group.) In turn, the FTC and Idaho's Attorney General filed separate suits also challenging the acquisition, and the cases were consolidated in March 2012. The court declined to issue a preliminary injunction, and St. Luke's proceeded to close on its acquisition of Saltzer in December 2012. After a bench trial, the court issued a decision[2] in January finding that the acquisition violated Section 7 of the Clayton Antitrust Act[3] and Idaho's Competition Act.[4]

In its decision, the court noted that the Clayton Act's §7 makes an acquisition illegal "if the effect of such acquisition may be substantially to lessen competition," and that among its purposes is to arrest the tendency to monopoly before the consumer's alternatives disappeared through merger. The court, citing various precedents, wrote that §7 deals with probabilities, not "ephemeral possibilities" of a merger's anticompetitive effects; requires a prediction of a transaction's likely effects; and places the burden on plaintiffs to show that the Saltzer acquisition would result in St. Luke's having an undue percentage share of the relevant market, and would result in a significant increase in the concentration of providers in their market.

The court explained that, once plaintiffs make such a showing, it establishes a presumption that the merger will substantially lessen competition, and that the defendants must then produce evidence clearly showing that the market's concentration inaccurately predicts the likely competitive effects of the transaction. Rebuttal evidence could include demonstrating that the anticompetitive effects of the merger will be offset by efficiencies resulting from the merger, or showing that there is ease of entry into the market, the trend of the market either toward or away from concentration, and the continuation of active price competition. If the defendants can successfully rebut the presumption of illegality, the burden then shifts back to the plaintiffs to produce additional evidence of anticompetitive effects.

Turning to the evidence presented at trial, the court found that the relevant product and geographic market for §7 analysis was adult primary care physician services in the city of Nampa. It found that it was difficult to recruit primary care physicians to come to Canyon County, where Nampa is located, and for new primary care physicians to open an office and develop a practice that could compete with St. Luke's/Saltzer. The court concluded that, entry into the market by other providers has been very difficult, and would not counteract the anticompetitive effects of the Saltzer acquisition on a timely basis.

The court found it likely that the combined entity will use its substantial market share to negotiate higher reimbursements from health plans, and charge for more ancillary services (e.g., lab tests, X-rays) at St. Luke's higher hospital billing rates, thus raising costs to consumers.

St. Luke's had argued that acquiring Saltzer and employing its physicians was the best way to create a unified and committed team of physicians required to practice integrated medicine, and created efficiencies that would far outweigh any anticompetitive effects. The court found that such efficiencies must be "merger-specific," and that employing the physicians was not the only way to create a unified and committed team of physicians.

The court also found it likely that the combined entity will use its substantial market share to negotiate higher reimbursements from health plans, and charge for more ancillary services (e.g., lab tests, X-rays) at St. Luke's higher hospital billing rates, thus raising costs to consumers. Accordingly, the court ordered St. Luke's to divest itself of the Saltzer Group.

Analysis

This is an odd decision for a number of reasons. First, the court went out of its way repeatedly to praise defendant St. Luke's "for its efforts to improve the delivery of health care," and to compliment its "foresight and vision" in moving toward "a more integrated system of care." The court cited numerous studies pointing out the many faults in the fee-for-service model, as well as studies and reports highlighting the many benefits of integrated medical care paid for on a capitation basis. However, it concluded that employing the Saltzer physicians was not the only way to achieve the goal of more integrated medical care, and suggested that the expansion of St. Luke's electronic medical record system to independent practicing physicians would facilitate more integrated medical care.

There is very little actual antitrust analysis in the decision, and the court's conclusion that the Saltzer-St. Luke's merger will lower competition and increase costs appears to be speculative at best. Moreover the court's definition of the relevant market, i.e., adult primary care services in Nampa, Idaho—is exceptionally narrow from both a geographic and a service point of view. The hospital plaintiffs alleged anticompetitive effects in pediatrics, general acute care hospital services, neurosurgery and orthopedic outpatient services, and general outpatient surgery services. The court declined to address these markets due to the fact that it had ordered divestiture based upon anticompetitive harm to the market for primary care services in Nampa.

An appeal is virtually certain for reasons that include the fact that St. Luke's purchase agreement with Saltzer allows Saltzer to keep $9 million of the purchase price if the merger is undone. We will await the results of any appeal.

The Affordable Care Act and market dynamics continue to spur combinations of providers and the development of large integrated care systems all across the nation, and across state borders. As noted earlier, the expectation is that these trends will result in better quality and continuity of care, as well as more cost-effective care. Nevertheless, acquisitions of medical providers by larger health systems should be carefully reviewed from an antitrust perspective even where, as here, no prior Hart-Scott-Rodino scrutiny was required. Acquisitions of medical providers by Accountable Care Organizations must hew as closely as possible to the antitrust safe harbors that were promulgated for such organizations.[5]

Health insurers and other payors, as well as competing providers, are watching. Clearly, so are the FTC, the Department of Justice, and state attorneys general.

1. Public Law 111-148. (P.L. 111-152 is the final law for ACA.)
2. *Federal Trade Commission v. St. Luke's Health System Ltd.*, Case No. 1:13-CV00116-BLW (D. Idaho Jan. 24, 2014).
3. 15 USC §18.
4. Idaho Code §48-101 et seq.
5. Final Statement of Antitrust Enforcement Policy Regarding Accountable Care Organizations Participating in the Medicare Shared Savings Program, 76 Fed. Reg. 67,026 (Oct. 28, 2011).

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