Federal Trade Commission (FTC) Upheld Again in Healthcare Merger Challenge

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In a long-awaited decision, on April 22, 2014 a Sixth Circuit panel unanimously upheld a 2012 Federal Trade Commission (FTC) decision ordering the divestiture of a Toledo-area hospital acquired by rival ProMedica Health System in 2010.¹ This decision closely follows the Idaho District Court January ruling in favor of the FTC, which successfully sought to require a Boise-area hospital group to divest a large provider group acquired in 2012.² Notably, neither healthcare transaction was required to be reported to the federal antitrust agencies under the Hart-Scott-Rodino Act prior to consummation.

In ruling for the FTC, the Sixth Circuit noted that the FTC’s administrative hearing had “lasted over 30 days and produced more than 8,000 pages of trial testimony and over 2,600 exhibits.”³ According to the Court of Appeals, “[t]he Commission’s analysis of this merger was comprehensive, carefully reasoned, and supported by substantial evidence in the record,” and the FTC did not abuse its discretion in requiring divestiture of the rival hospital.

Background

In January 2011, the FTC, along with the Ohio Attorney General, challenged ProMedica Health System’s (ProMedica) August 2010 acquisition of control over St. Luke’s Hospital (St. Luke’s) through a Joinder Agreement, concerned that it would significantly harm competition in the Toledo area (which is located in Lucas County, Ohio). The FTC believed that the elimination of competition between ProMedica and St. Luke’s would enhance the merged entity’s ability to obtain supra-competitive reimbursement rates from commercial health plans and their members. The FTC claimed that the transaction would reduce the number of competitors in general acute-care inpatient hospital services in Lucas County from four to three, with a combined market share of close to 60%. According to the Commission, the transaction would also reduce the number of competitors in inpatient obstetrical services in Lucas County from three to two, with a combined market share of more than 80%. On March 29, 2011, the district court granted the FTC’s motion for a preliminary injunction and required the hospitals to maintain St. Luke’s as an independent competitor pending completion of the FTC’s investigation.

After a full administrative trial, the FTC Administrative Law Judge (ALJ) issued an Initial Decision on December 5, 2011, agreeing with the FTC staff that the transaction reduced the number of competitors in the market for general acute-care inpatient hospital services from four to three, and would increase ProMedica’s bargaining power with commercial health plans, leading to higher reimbursement rates that would be passed on to the plans’ customers (local employers and their employees). The ALJ did not agree with the staff’s definition of “inpatient obstetrical services” as a separate relevant product market, but on the basis of the expected increase in consumer prices in the general acute-care inpatient hospital services market, he ordered that ProMedica divest St. Luke’s to an FTC-approved buyer within 180 days after the final order.

On March 22, 2012, the Commission upheld most of the ALJ’s Initial Decision, finding that the merger increased ProMedica’s market share far above the threshold required to create a presumption that the merger would lessen competition. The FTC ruled that ProMedica’s acquisition of St. Luke’s was likely to substantially lessen competition and increase prices for general acute-care inpatient hospital services and inpatient obstetrical
services sold to commercial health plans in Lucas County. The FTC’s Opinion defined the relevant market somewhat differently than the ALJ, but noted that “the outcome of this case is the same whether or not [inpatient obstetrical] services are included in the [general acute-care] inpatient hospital services market ... As the ALJ found, regardless of which market definition is used, market shares and concentration levels exceed the thresholds for presumptive illegality provided in the 2010 Horizontal Merger Guidelines and the case law. Respondent does not dispute this.”

The FTC rejected ProMedica’s contentions regarding the commercial health plans’ countervailing bargaining power, lack of competitive effects evidence post-transaction, likely repositioning by competitors, and St. Luke’s questionable financial viability. Thus, the Commission agreed with the ALJ and ordered ProMedica to divest St. Luke’s.

The parties appealed the decision to the Sixth Circuit. The appellate court analyzed what it believed to be extensive data considered by the FTC at the administrative level regarding product markets, concluding that the relevant product markets were: (1) a cluster market of primary (but not OB) and secondary inpatient services, and (2) a separate market for OB services. Then the court turned to ProMedica’s arguments that the FTC incorrectly presumed the merger illegal based solely on significantly high market concentration (HHI) levels, contending that such an analysis “applies only in ‘coordinated-effects’ cases, rather than in ‘unilateral-effects’ ones.” The Sixth Circuit responded by considering ProMedica’s pre-merger market shares and relatively higher price levels, and concluded that ProMedica’s pre-merger bargaining power, coupled with the HHI data, were sufficient for the FTC to apply a presumption of illegality with respect to the merger.

The court considered the merging parties’ failure to show any efficiencies or benefits to consumers. Though these types of arguments can enable merging parties to overcome the presumption of illegality, the court noted the lack of evidence contrary to the presumption, while declaring that there was “a wide range of evidence” supporting the FTC’s views on the merger. Finally, ProMedica’s use of a “weakened firm” defense was identified by the court as a “Hail-Mary pass” and, as did the FTC, the court rejected the argument due to St. Luke’s pre-merger increase in market share and “sufficient cash reserves.”

Analysis

Mergers involving hospitals and health care providers remain very much on the radar of federal and state antitrust enforcers, regardless of the size of the transaction or the fact that the merger was not challenged pre-consummation. Moreover, the Pro-Medica decision reconfirms that while a “failing company” defense to a merger suit rarely succeeds, a “sick company” defense has even less of a possibility of success.

Recently, in response to the FTC’s success in the St. Luke’s case, Rep. Jim McDermott asked the Commission to issue additional guidance on potential antitrust issues raised by Affordable Care Act (ACA)-inspired health care mergers. As noted in that court’s decision, and by Rep. McDermott, health care organization mergers can be in violation of Section 7 of the Clayton Act even when they would improve patient outcomes and quality of care -- goals of the ACA. Additional guidance would provide such organizations more clarity as they attempt the coordination encouraged by the ACA.

3 ProMedica Opinion at p. 6.
4 According to the court’s opinion, “[General acute-care] comprises four basic categories of services. The most basic are “primary services,” such as hernia surgeries, radiology services, and most kinds of inpatient obstetrical (OB) services. “Secondary services,” such as hip replacements and bariatric surgery, require the hospital to have more specialized resources. “Tertiary services,” such as brain surgery and treatments for severe burns, require even more specialized resources. And “quaternary services,” such as major organ transplants, require the most specialized resources of all. Different hospitals offer different levels of these services.” ProMedica Op., at 1-2.
6 Id. at p. 16.
7 Id. at p. 18.


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