

Health Law Alert: Ninth Circuit Affirms Acquisition of Idaho Medical Group by St. Luke's Hospital Violates Antitrust Laws

February 23, 2015

On Feb. 12, the Ninth Circuit Court of Appeals affirmed a trial victory for the Federal Trade Commission (FTC) and Saint Alphonsus Medical Center (Saint Alphonsus) in their challenge to the acquisition by the St. Luke's Health System (St. Luke's) in Idaho of the 41-physician Saltzer Medical Group (Saltzer). The Ninth Circuit affirmed the trial court's decision that the acquisition threatened competition in the market for adult primary care physician services in Nampa, Idaho, in violation of Section 7 of the Clayton Act, and further affirmed the trial court's order divesting the combined entity. The case has been closely watched since its 2012 inception because it is the first time the FTC has litigated the acquisition of a physician practice through trial.

In 2012, Saint Alphonsus, a rival health system, sued St. Luke's and Saltzer over the proposed acquisition. Shortly thereafter, St. Luke's and Saltzer completed the transaction. Following a 19-day bench trial in federal court in Idaho, Judge B. Lynn Winmill expressly noted the "troubled state of the U.S. health care system," and also "found that St. Luke's and Saltzer genuinely intended to move toward a better health care system, and expressed belief that the merger would 'improve patient outcomes if left intact'"—pro-competitive justifications offered by St. Luke's and Saltzer in favor of the acquisition. Nonetheless, Judge Winmill found that the "huge market share" of the post-merger entity "creates a substantial risk of anticompetitive price increases" in the Nampa adult primary care physician market, thus violating Section 7 of the Clayton Act. Judge Winmill ordered divestiture of the merged entity.

On appeal, the Ninth Circuit largely affirmed Judge Winmill's findings. The following are the key points of the Ninth Circuit's decision:

- The Ninth Circuit held that the trial court's decision to limit the relevant geographic market to Nampa was appropriate. St. Luke's vigorously disputed the trial court's determination, arguing that the relevant geographic market should be expanded to include Boise, thus diluting its relevant market share. In rejecting St. Luke's broader relevant geographic market definition, the trial court focused on whether a hypothetical monopolist could impose a "small but significant non-transitory increase in price" (SSNIP). The Ninth Circuit held that the trial court correctly focused on the likely response of insurers to a hypothetical demand by all primary care physicians in a particular market for a SSNIP. Importantly,

health insurance representatives testified at trial that they could not successfully market a health plan without primary care physicians in Nampa. Additional evidence at trial showed that "consumers choose physicians on factors other than price." The trial court therefore correctly held that patients choosing primary care physicians in Nampa would not change their behavior—i.e., seek care elsewhere—in the event of a small but significant increase in the price of that care.

- The Ninth Circuit affirmed the trial court's determination that the merged entity met presumptively anticompetitive market share levels. The market share numbers of the combined entity, as measured by the Herfindahl-Hirschman Index (HHI), were "well above the thresholds for a presumptively anticompetitive merger..." Specifically, Saltzer accounted for approximately half of the market and St. Luke's accounted for approximately a quarter of the market. Of note is the small size of the market at issue. Saltzer employed 16 adult primary care physicians in Nampa, St. Luke's employed 8, and plaintiff Saint Alphonsus employed 9.
- The Ninth Circuit agreed with the trial court that the combined entity would likely use its post-merger power to negotiate higher reimbursement rates from insurers for primary care physician services. Because St. Luke's and Saltzer had been each other's closest substitutes in Nampa, the acquisition limited the ability of insurers to negotiate with the merged entity. Of note is the pre-acquisition internal correspondence introduced as evidence at trial. For example, an email between St. Luke's executives discussed "pressur[ing] payors for new directed agreements." An exchange between Saltzer executives stated that "[i]f our negotiations w/Luke's go to fruition," the "the clout of the entire network" could be used to negotiate favorable terms with insurers. This should serve as a caution to parties to be cognizant of the potential impact of internal communications in the context of a deal.
- The Ninth Circuit agreed with the trial court's skepticism of St. Luke's argument that an anti-competitive merger could be justified by potential efficiencies. Even accepting the finding that the acquisition would improve health care in the area, the Ninth Circuit found that the alleged efficiencies—aligning incentives of hospitals and physicians and getting all physicians on a common electronic health record—did not overcome a highly anti-competitive transaction.
- Finally, the Ninth Circuit rejected St. Luke's proposal that divestiture be dropped as a remedy in favor of ordering St. Luke's and Saltzer to negotiate separately with health insurers.

The *St. Luke's* case is a significant victory for the FTC and may serve to embolden it and private plaintiffs to challenge other health system acquisitions of physician practices.

If you have any questions about the *St. Luke's* case or antitrust issues implicated by health care transactions, please contact Jeremy Johnson at jeremy.johnson@lathropgpm.com or 612.632.3035.