Physician Practice Mergers: The Key Antitrust Issues

This roundtable discussion is brought to you by the Antitrust Practice Group, and is co-sponsored by the Physician Organizations (Physicians) and Business Law and Governance (BLG) Practice Groups.

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Discussion Overview

- Legal framework and FTC perspective
  - Saralisa Brau (FTC)

- Market definition in physician practice mergers
  - Monica Noether, PhD (Charles River Associates)

- How merging parties can minimize antitrust risk
  - Christi Braun (Mintz Levin)
Legal Framework and FTC Perspective

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Key Concepts of Antitrust Merger Law

- Mergers and acquisitions that create or enhance market power may raise competitive concerns.

- Horizontal mergers more likely to raise antitrust concerns than vertical mergers.

- Highly fact-specific, economics-based analysis.

- Generally enforced by FTC, DOJ, state AGs, but private actions also possible.
The Legal Framework

- **Key statute:** Section 7 of the Clayton Act
  - Prohibits mergers and acquisitions whose effect “may be to substantially lessen competition”
  - Premerger (HSR) reporting and waiting period for transactions meeting certain financial thresholds
  - Act also applies to consummated deals

- **Caselaw**

- **FTC/DOJ Horizontal Merger Guidelines**
The 2010 Horizontal Merger Guidelines

- Central issue: is the merger likely to result in anticompetitive effects?

- Types of evidence the agencies consider
  - Actual effects of consummated mergers
  - Direct comparisons based on experience
  - Market shares and concentration
  - Intensity of head-to-head competition

- Sources of evidence
FTC/DOJ Approach to Merger Analysis

- Identify potential competitive concerns
- Define the relevant market
- Calculate market shares and concentration
- Analyze anticompetitive effects
  - Unilateral
  - Coordinated
  - Power buyer
- Assess likelihood of entry
- Consider procompetitive efficiencies
Physician Practice Mergers: Recent Developments

- In April 2011, first public announcement of an FTC investigation of physician practice merger/acquisition
  - Hospital announced plans to acquire assets of two cardiology practices in Spokane, WA and employ physicians
  - Commission staff investigated; expressed concerns; parties ultimately abandoned the acquisition

- Message: FTC is watching physician practice mergers
  - Watching non-HSR reportable deals
  - Working closely with state attorneys general
The Big Picture

- Competition plays an important role in health care
- Merger enforcement in health care is an FTC priority
- FTC looking beyond hospital mergers to other types of provider mergers
  - But recognize that most mergers are not likely anticompetitive, and will be reviewed on case-by-case basis
  - Demonstrated quality improvements from merger will be given substantial weight in case selection
- “Health care reform made me do it” is not an automatic defense for practice mergers raising market power concerns
Market Definition and Competitive Effects Issues in Physician Practice Mergers

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What Is The Role Of Market Definition?

- Market definition (and concentration) is a framework used by the federal antitrust agencies to assess whether a merger is likely to lessen competition.

- Merger Guidelines emphasize that market definition and concentration are not the only relevant sources of information:
  - Adverse competitive effects directly observed in a consummated merger.
  - “Natural experiments” (e.g., evidence of the effects of entry, exit, or consolidation) or comparisons of prices in markets with different competitive structures.
  - Evidence of substantial head-to-head competition between merging practices.
How Are Markets Defined?

- From the Merger Guidelines
  - “Market definition focuses solely on demand substitution factors, i.e., on customers’ ability and willingness to substitute away from one product to another in response to a price increase or a corresponding non-price change such as a reduction in product quality or service.”

- Two dimensions of market definition
  - Product market
    - What types of products do consumers view as good substitutes?
  - Geographic market
    - Where can consumers purchase these products?
How Are The Antitrust Agencies Likely To Think About Market Definition In Physician Practice Mergers?

- Focus is generally on private health plans and their members, since fee-for-service Medicare and Medicaid do not negotiate with physicians
  - The agencies may also be concerned about access or quality for Medicare and Medicaid beneficiaries
- For private health plans, how should one think about “demand substitution”?
  - Practices compete to be included in health plans’ provider networks
  - Practices compete to attract members of health plans (or referring physicians)
  - Ultimately, patients decide where to receive care, so:
    - Patients’ views of practice substitutability affects the negotiations between health plans and physician practices
    - Concern is if patients think there are few good substitutes for merging practices, the merged practice may be able to negotiate higher reimbursement rates with health plans
Product Market Definition For Physician Practices

- Antitrust agencies have previously adopted the view that physician specialties correspond to product markets
  - This view is reflected in policy statement on ACOs, which proposes calculating shares separately for approximately 50 specialties

- But the ability of physicians to provide certain services is not necessarily restricted to or common to a single specialty
  - Neurosurgeons and orthopedic surgeons both perform spine surgery
  - Orthopedic surgeons who perform spine surgery are probably not good substitutes for orthopedic surgeons who specialize in hand surgery

- Non-physician providers may also be relevant
  - Nurse practitioners can provide primary care and nurse anesthetists can deliver anesthesia
Geographic Market Definition For Physician Practices

Question: In what geographic area are physicians (or healthcare professionals) who patients view as reasonably substitutable located?

Complexities of required analysis include –

- Healthcare services are highly differentiated, and proximity is only one (important) factor that affects patients’ choices
- Willingness to travel likely varies by specialty and type of service
  - For example, cardiac surgery consultation compared to primary care office visit
- For some specialties, geographic market definition may be tied to hospital geographic market definition
  - For example, patients may only consider orthopedic surgeons with privileges at hospitals in some geographic area as reasonably substitutable
- Referral arrangements may affect choices of specialty physicians
Data To Assess Putative Market Definitions May Be Hard To Obtain

- **Product market definition for physician practices**
  - Can look at services actually provided by different specialties from merging practices’ records, but this does not address activities of other physicians
  - For some services, might be able to obtain data on operating/attending physicians from hospital discharge data
  - Information on training/certification requirements may be available

- **Geographic market definition for physician practices**
  - Data on where physicians draw patients from are not publicly available
  - May be able to obtain data from clients on where practices’ patients reside, but this does not address:
    - Where else patients at merging practices currently receive care
    - What other practices are treating patients who reside in the same area
  - Hard to take account of other determinants of choice (e.g., reputation)
Calculating Shares In A Putative Market May Be Difficult

- Even with product and geographic markets delineated, it may be difficult to calculate shares

- Potential concerns
  - Need a census of competitors
  - Shares could be based on a number of measures:
    - Number of physicians in relevant specialties
    - Number of procedures performed
    - Number of patients treated
    - Dollars of revenue
  - Should measures include only services provided to members of private health plans, or also Medicare and Medicaid beneficiaries?
  - Are physicians who provide services only on an out-of-network basis in the market?
A Few Comments On Competitive Effects

- Market definition is a framework used to assess competitive effects, but whether a merger is likely to lessen competition may depend on consideration of other factors
  - How will other physician practices respond (via expansion and entry)?
  - What effects do changes in the marketplace for physician services have on competitive dynamics?
  - Can health plans act as “powerful buyers”? 
  - Do mergers of multispecialty physician groups warrant additional scrutiny?
How Will Other Practices Respond?

- Other existing practices are unlikely to ignore merger of competing physician practices
  - Might step up recruitment efforts in response to physician practice merger
  - May try to obtain privileges at hospitals served by merging practices
  - May switch referral patterns in case of multi-specialty practices

- Entry of a new practice is also possible
  - Physicians are well educated, high income, and mobile; there is a well-developed physician-recruiting industry
  - Existing practices, hospitals, or health plans might sponsor or encourage entry
  - Presence of local (or reasonably proximate) medical schools can bolster entry story
  - But referral networks may make it difficult for new physicians to develop a practice

- These competitive moves may allay competitive concerns from the merger
Do Changes In Marketplace For Physician Services Affect Competitive Dynamics?

- There has been an increase in the number of physicians employed by hospitals or large multispecialty groups, and a corresponding decrease in the number of small practices.

- The increasing role of health information technology and clinical integration may increase minimum efficient scale, justifying mergers, but placing small practices at a competitive disadvantage.

- How will the development of ACOs change the marketplace for physician services?
Can Health Plans Act As “Powerful Buyers”? 

- Merger Guidelines recognize the role that “powerful buyers” may plan in assessing competitive effects
  - Potential sponsor of entry
  - Vertical integration with providers (e.g., Kaiser)
  - Presence may deter coordinated interactions

- The health plans that negotiate with physician groups are large, sophisticated purchasers of healthcare services

- “Powerful buyer” does not mean that market power in the sale of physician services can be counteracted by a health plan’s monopsony power
  - This argument is analogous to argument in favor of physician collective bargaining rights with health plans, which has been largely rejected
Do Mergers Of Multispecialty Physician Groups Warrant Additional Scrutiny?

- Suppose two multispecialty physician groups merge and combined share in any particular specialty does not raise competitive concerns.

- Could the merger still lessen competition by making the combined practice a “must-have”?

- Theory of competitive harm might be that a health plan failing to come to an agreement with the multispecialty practice would be too disruptive for plan members.
  - This might give the practice additional bargaining power even though there were good substitutes for any particular specialty in the practice.
Minimizing the Antitrust Risks of Practice Mergers

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Go Vertical or Conglomerate, Rather than Horizontal

- **Vertical Mergers**
  - Practice acquisition by a hospital that does not own, or employ, any physicians in the same medical specialty as the practice to be acquired
  - Merger of physicians in referrer/referee relationship or complementary
  - May be procompetitive because they reduce service delivery costs, spur innovation, or improve quality

- **Conglomerate Mergers**
  - Merger of physicians that do not compete with one another and are not in a referral relationship
  - Raise no traditional competitive concerns

- **Horizontal Mergers**
  - Mergers among physicians who practice in the same medical specialty in relatively close geographic locations (i.e., same product and geographic markets)
  - Much more likely to raise competitive concerns than vertical mergers
Avoid a Merger to a Monopoly

- Physician practices probably should not merge if:
  - There will be no remaining competitors following the merger
  - Each of the merging parties has market power on its own (i.e., greater than a 35% market share and the ability to raise price above competitive levels)
  - The merged entity will have greater than 75% market share
    - BUT not if the acquired party adds a de minimis share (i.e., 5% or less)
Ensure Entry of New Competitors Is Plausible

Entry Considerations:

- Actual history in the geographic market of entry of new physicians in response to mergers and acquisitions
- Timeliness
  - 2-3 years
  - Should be rapid enough to make a price increase by the merged entity unprofitable
- Likelihood
  - If entry would be profitable, then it will be likely
- Sufficient
  - Replicate the scale and strength of one party to the merger
Know Thy Competitors

- Best evidence of likely entry is announcement by competitor
  - Recruitment advertisements
  - Public statements regarding proposed expansion or intent to hire

- For hospital acquisitions of physician practices, the most likely party to sponsor entry is a competing hospital at risk of loss of referrals
  - Stepped-up recruitment for employment and/or privileges
    - Potential for financial assistance for relocation and new practice set up
    - Economic conflict of interest policies

- Excess capacity or demonstrable need?
Have a Good Story to Support the Merger

- Market pressures
  - Need to cover call for local hospitals
  - Desire of local hospitals to offer exclusive contracts
  - Practices unable to cover rising overhead costs alone

- Government program requirements
  - EHRs
    - High cost of implementation as compared to HITECH incentive payments
    - Penalty for failure to adopt by 2015
  - ACOs
    - Must have sufficient primary care physicians to care for 5,000 Medicare beneficiaries
  - Bundled payments
    - Ownership of physician practices makes it easy for hospitals to allocate resources
Make Valid Efficiency Arguments

- Be merger-specific
  - Why are these practices likely to achieve cost savings or better quality?

- Make sure efficiencies are measurable
  - What are costs now and how will they go down?
  - Where is quality now and how will you know if it improves?

- Efficiencies must exceed the magnitude of the projected anti-competitive effects
  - Higher prices not tied to quality improvements are suspect
  - Cost reductions need to benefit consumers

- Efficiencies can’t be gained by reducing output or availability of services
  - Shorter hours, fewer locations, fewer physicians, or fewer services are suspect
Examples of Cost Efficiencies

- Broader array of services
- Ability to purchase equipment that individual parties could not premerger
  - EMRs
  - Imaging equipment
  - Lasers
  - Radiation therapy
  - Outpatient surgical equipment and space
- Reduced cost of offering services
  - More physicians and extenders may allow a practice to offer longer office hours or weekend appointments at no greater cost
- Savings to pass on to consumers
  - Reduced overhead may mean lower fixed costs and lower prices
Examples of Quality Efficiencies

- Higher quality as a result of merger
  - May be tied to new technology, such as EMRs
    - EMRs help with tracking of care and quantifying quality
  - Can be the result of increased expertise
  - May be able to hire care coordinator or nurse to follow chronically ill patients

- Better coordination of care
  - All physicians providing call coverage are part of one practice, preferably with one patient record
  - Benefit of a vertical merger

- Ability to continue services that may have been in jeopardy due to smaller scale operations
  - When costs get too high, quality can suffer; mergers allow costs to be spread out
The Challenges of Remedies

- Pre-merger
  - Injunctive relief generally sufficient

- Post-merger
  - Divestiture
    - Whole practice
    - Individual physicians
  - Limited price increases based on settlement agreement
  - Regulatory approval for price increases
  - Separate negotiators for separate sites
Lessons for Merging Practices

- Be careful of increasing market share too much
  - Do merging practices, together, have a 35% or larger market share?
  - Do the four largest firms have a 50% or larger market share?

- Ensure there are quantifiable procompetitive efficiencies from the merger

- Ensure that there aren’t documents stating that the reason for the merger is to increase reimbursement rates

- Don’t be greedy post-merger
  - Payers will complain if prices increase significantly
  - Significant price increases will be used as proof of post-merger market power
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