KILPATRICK TOWNSEND

Insights: Alerts

FTC v. St. Luke's Health System, Ltd.: Ninth Circuit Holds that Acquisition of Physician Group Practice Violates Antitrust Laws, Requires Divestiture

February 11, 2015

Written by **Peter M. Boyle** and **Christina E. Fahmy**

On February 10, 2015, the Ninth Circuit affirmed a district court ruling in favor of the Federal Trade Commission that the acquisition of an Idaho physician group practice by St. Luke's Health System violated the antitrust laws, specifically Section 7 of the Clayton Act. Closely watched by healthcare providers and other stakeholders, the St. Luke's case is thought to be a key indicator of how courts will balance Affordable Care Act (ACA) requirements for integrated healthcare services with concerns about increasing healthcare provider concentration.

The case has been ongoing since 2012, when St. Luke's Health System acquired Saltzer Medical Group, the largest multi-specialty physician group in Idaho. Private competitor hospitals Saint Alphonsus Health System, Inc. and Treasure Valley Hospital Limited Partnership first filed suit over the deal in 2012. They were joined soon thereafter by the Federal Trade Commission and the State of Idaho, who sought to enjoin the acquisition.

The antitrust laws, in particular Section 7 of the Clayton Act, make illegal any merger or asset acquisition that may substantially lessen competition or tend to create a monopoly in any relevant market. The district court denied a preliminary injunction early in the case because the agreement did not require Saltzer to refer patients to St. Luke's, implementation of the merging parties' agreement would take place over time, and the agreement provided a process for unwinding the merger if the deal were found to be unlawful. Often, the district court's decision regarding whether or not to grant a preliminary injunction is dispositive. Nevertheless, after failing to persuade the court to enter a preliminary injunction, the FTC and the other plaintiffs in a bench trial persuaded the court that the merger violated the antitrust laws.

More specifically, the court found that the deal would harm competition in the relevant market for adult primary care physician services. Saltzer had sixteen primary care physicians ("PCPs"), the most in the Nampa, Idaho area. St. Luke's had eight PCPs and a competing hospital in the area, St. Alphonsus, had nine PCPs. Other PCPs in or around Nampa had solo or small practices. The district court found the "huge market share' of the post-merger entity 'creates a substantial risk of anticompetitive price increases' in the Nampa adult PCP market." The judge also found that the deal would increase prices and therefore harm competition in the market for hospital-based ancillary services. The court found the merger to be unlawful even though the court believed that the merging parties genuinely intended to improve the healthcare system and that the merger would

improve “patient outcomes” if left intact. Still, after weighing the potential anticompetitive effects against the deal's procompetitive benefits, the district court found that the deal on balance would be anticompetitive.

On appeal, the merging parties argued that the district court erred by defining a relevant geographic market limited to Nampa, Idaho, which excluded physicians practicing in Boise. The Ninth Circuit affirmed the lower court's finding that Nampa was the relevant geographic market with which to assess the deals competitive effects on adult PCP services. The lower court applied the SSNIP test, which the FTC and the U.S. Department of Justice identify in their Horizontal Merger Guidelines as the appropriate way to define a relevant market. That test defines a relevant market by considering likely consumer behavior if the price increases by roughly 5% – if the purchaser can switch away and avoid the increase, the options they would switch to are part of the relevant market. The Ninth Circuit acknowledged that there was evidence showing that one-third of patients could be forced to switch from PCPs in Nampa to PCPs in Boise if the post-merger entity raised prices. However, despite this evidence of ability to switch, the Ninth Circuit concluded that Nampa is the relevant geographic market because insurers need local PCPs to make their panels attractive to consumers and would therefore not be able to defeat a price increase.

The merging parties' arguments regarding competitive effects fared slightly better than their arguments on the relevant market, but still not well enough to win the day. The merging parties argued on appeal that the district court failed to take into account efficiencies that would result from the merger and therefore erred in assessing the merger's competitive effects. The Ninth Circuit noted its skepticism regarding whether efficiencies defenses are viable under prevailing Supreme Court precedent, but concurred with the district court that likely efficiencies could help show that the merged entity would become more efficient and thereby increase and not decrease competition.

Playing off themes from the Affordable Care Act, the merging parties argued that the deal would increase efficiencies and therefor competition “by creating a team of employed physicians with access to Epic, the electronic medical records systems used by St. Luke's.” And the merging parties had argued before the district court that the deal would better enable them to comply with obligations imposed on them under the Affordable Care Act by helping move to a value-based rather than volume-based pricing system. Neither the Ninth Circuit nor the district court found the purported efficiencies to be meaningful or merger-specific. The Ninth Circuit agreed with the lower court that no evidence supported that argument that St. Luke's needed a core group of employed PCPs beyond the number it had pre-merger to successfully transition to integrated care and that a “committed team” can be assembled without employing physicians. The court of appeals also rejected the argument that shared electronic medical records – or EMRs – were a merger-specific efficiency because data analytics tools are available to independent physicians.

Interestingly, the court seemed to accept that the merger would benefit patients in many ways, but according to the court, better healthcare service cannot offset the anticompetitive effects that will result from the likely price increase that insurers will have to bear. The Ninth Circuit commented that “[a]t most, the district court

concluded that St. Luke's might provide better service to patients after the merger. That is a laudable goal, but the Clayton Act does not excuse mergers that lessen competition or create monopolies simply because the merged entity can improve its operations." Accordingly, the Ninth Circuit affirmed the district court's decision that St. Luke's must divest the Saltzer practice.

The decisions by both the district court and the Ninth Circuit are significant. First, they show and tend to support the FTC's position that general recitation of purported efficiencies endorsed in the Affordable Care Act will not carry much weight with the federal antitrust agencies or the courts in an antitrust matter. Second, the case demonstrates that the FTC will challenge smaller deals not reportable under the Hart-Scott-Rodino Act, even deals to acquire physician practices, if the transaction will likely have anticompetitive effects. And finally and somewhat relatedly, the fact that the FTC will focus its resources on small healthcare deals tends to illustrate the importance that the agency places on robust competition in healthcare markets.

Related People

Peter M. Boyle

Partner

Washington, DC

t 202.508.5831

pboyle@kilpatricktownsend.com

Christina E. Fahmy

Partner

Washington, DC

t 202.508.5834

cfahmy@kilpatricktownsend.com