Demonstratives for the Rebuttal Testimony of Professor David Dranove

FTC & State of Idaho v. St. Luke's Health System & Saltzer Medical Group

No. 1:13-cv-00116

October 21, 2013

Plaintiffs' Exhibit 3130

Overview

- The Saltzer acquisition increases St. Luke's bargaining leverage and will allow the combined entity to increase reimbursements
  - St. Luke's and Saltzer are each other's closest substitutes in the Nampa PCP market
  - Will increase total payments to St. Luke's by individuals, plans, and employers—the "bottom right hand cell"
- Nampa is a well-defined relevant geographic market
  - Dr. Argue's flow analysis is not reliable
  - Dr. Argue's critical loss analysis is inappropriate and flawed

Overview, continued

- Competition promotes value in healthcare, just as in other markets
  - The Triple Aim
- Market power reduces value in healthcare, just as in other markets
  - Higher reimbursements
  - Ability to resist innovation (e.g., quality, tiering)
  - Affects negotiations of all aspects of healthcare contracts (e.g., risk-based)
- The acquisition is not necessary to efforts by St. Luke's or Saltzer to pursue clinical integration

Market dynamics and competitive effects

Two-stage competition in healthcare markets

Stage 1

Health plans form networks through negotiations with providers

↓

Health plans market their networks to area employers and individuals

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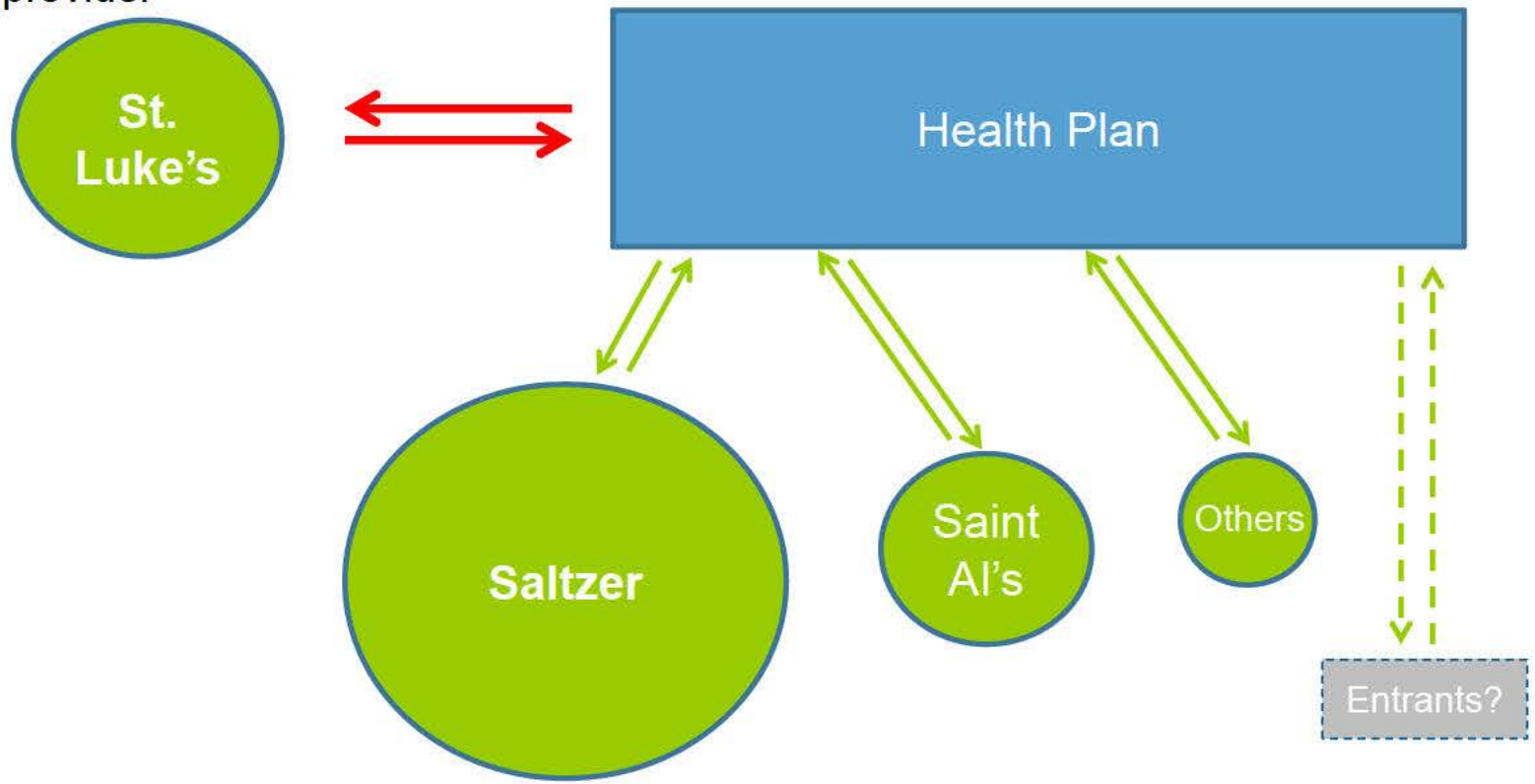
Stage 2

In-network providers compete for patients

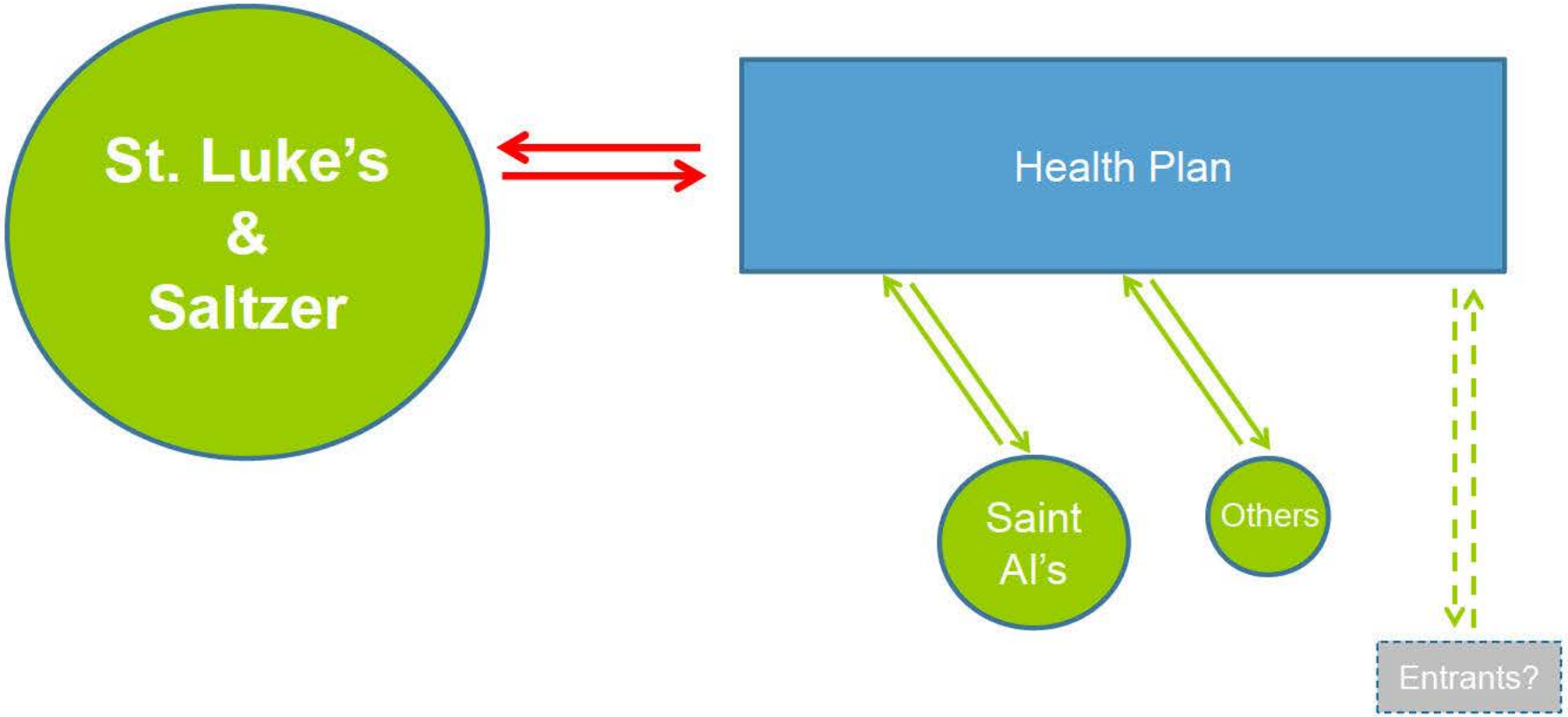
Bargaining leverage depends on substitute physician groups in the market

- *Before* the Acquisition: Saltzer PCPs offer an attractive substitute for St. Luke's PCPs, and vice versa
  - The health plan thus has a credible "outside option" when it negotiates with each provider



Bargaining leverage depends on substitute physician groups in the market

- *After* the Acquisition: the health plan loses a credible outside option, and the provider gains negotiating leverage



Antitrust analysis focuses on *changes* in provider leverage

- Payers—regardless of their size—have the same points of leverage before and after the acquisition
- Plans that offer narrow networks or tiered plans become less attractive following the acquisition
- Increased bargaining leverage can be manifested in the pricing of any of the negotiated services (the "lower right-hand cell")
- System competition with Saint Al's does not eliminate anticompetitive effects—***but for the acquisition***, Saltzer and St. Luke's also compete in Nampa

Dr. Argue misconstrues the nature of payer-provider bargaining

Any Above-Competitive Price Increase for St. Luke's Must Occur in a Market with Market Power

- Professor Dranove asserts that the transaction bestows market power in PCP services, but that St. Luke's can increase price in *any* service
  - Inconsistent with plaintiffs' antitrust theory
  - No *antitrust* explanation of how this could occur, rather, just an academic bargaining perspective
  - Raising price in any other service will result in St. Luke's losing patients to competitors

Source: Demonstrative exhibit, Testimony of David Argue, PhD at 62

The acquisition substantially increases concentration in the Nampa PCP market

Group	Visits	Pre-acquisition visits share	Post-acquisition visits share	Delta HHI
Saltzer	**6,087**	**65.5%**	**77.7%**	
St. Luke's	**1,142**	**12.3%**		
Saint Alphonsus	1,113	12.0%	12.0%	
Primary Health	451	4.8%	4.8%	**+1,607**
Terry Reilly	88	0.9%	0.9%	
All Others	419	4.5%	4.5%	
HHIs		**4,612**	**6,219**	

TX 1789 (Dranove Report) Figure 18

The acquisition is "presumed to be likely to enhance market power"

Attorney’s Eyes Only

Nampa is a well-defined relevant geographic market

Nampa is a well-defined relevant geographic market

- Extensive, consistent testimony
  - St. Luke's executives, consultants, and physicians
  - Other providers, including Primary Health
  - Health plans, including St. Luke's partner, SelectHealth
- Travel patterns
  - Claims data evidence strong patient preference for local PCPs
  - Clear bifurcation between Nampa and other areas of the Treasure Valley, especially Ada County
- All major health plans' provider networks include PCPs in all or nearly all zip codes

Dr. Argue's critical loss analysis does not undermine my conclusions

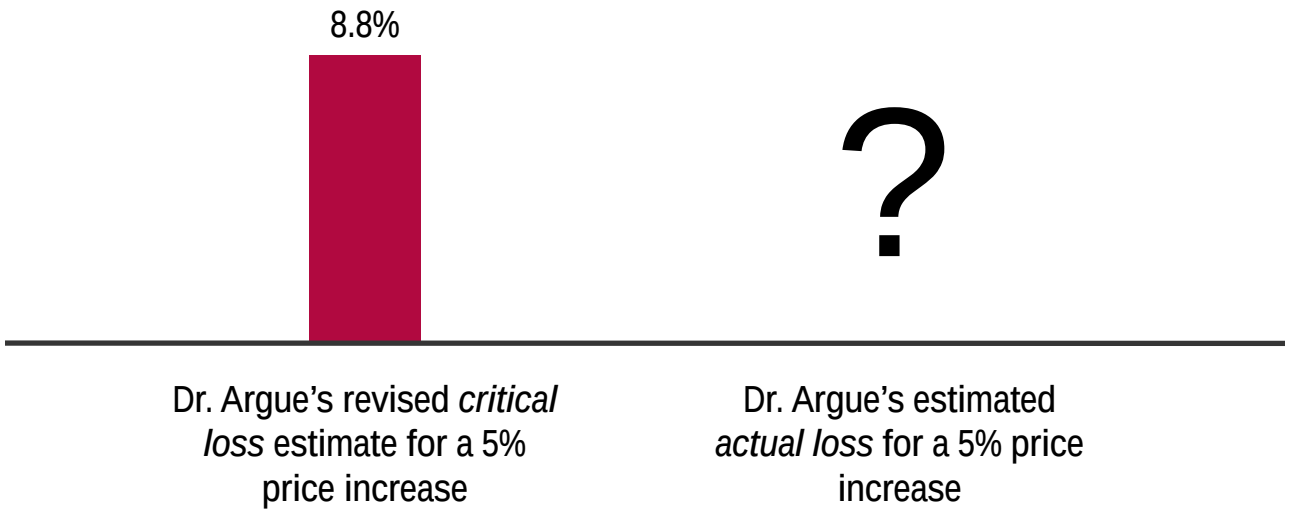
- Dr. Argue uses critical loss analysis in an effort to claim that Nampa is not a relevant geographic market
- However, critical loss analysis is not relevant or appropriate to healthcare provider markets, where reimbursements are determined in negotiations between payers and providers
- In addition, Dr. Argue's critical loss analysis is incomplete and contains errors (even after his revisions)

Critical loss is an inappropriate framework in healthcare markets

- The critical loss framework is inconsistent with how prices are determined in healthcare markets
  - Incorrectly focuses on pricing discipline imposed by marginal *patients* choosing among in-network providers
  - Choosing among in-network providers, patients are generally *price insensitive*
- Pricing discipline occurs through Stage One bargaining
  - St. Luke's leverage depends on payers' outside option, or BATNA
  - i.e., St. Luke's leverage depends on the extent to which patients consider other PCPs to be reasonable substitutes if St. Luke's is *dropped from the network* (and likewise for Saltzer)
  - The acquisition makes this substantially more difficult for payers marketing to employers and individuals in the Nampa area

Dr. Argue's critical loss analysis is incomplete

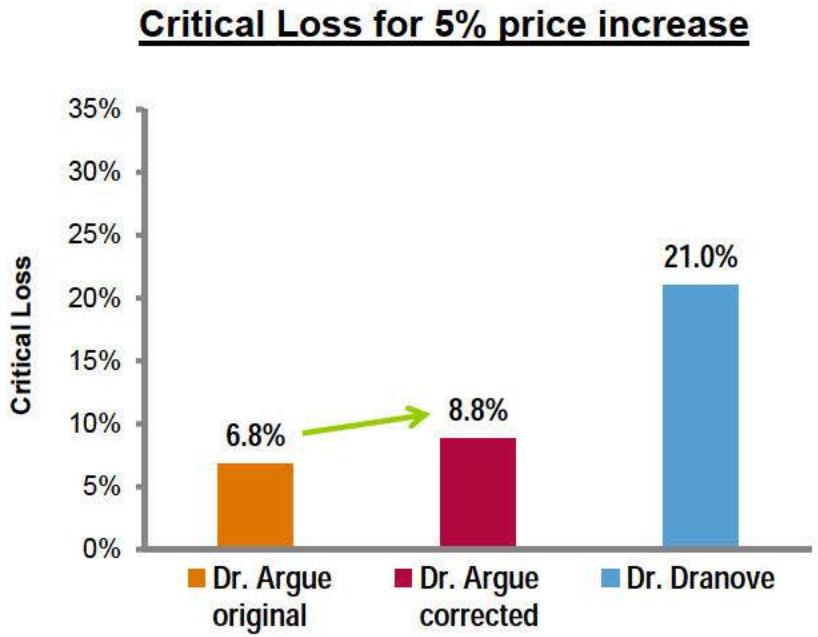
- Dr. Argue only calculated critical loss, not actual loss
- Dr. Argue merely suggests that critical loss is low
- Without an actual loss estimate, one cannot evaluate whether actual loss is above or below critical loss

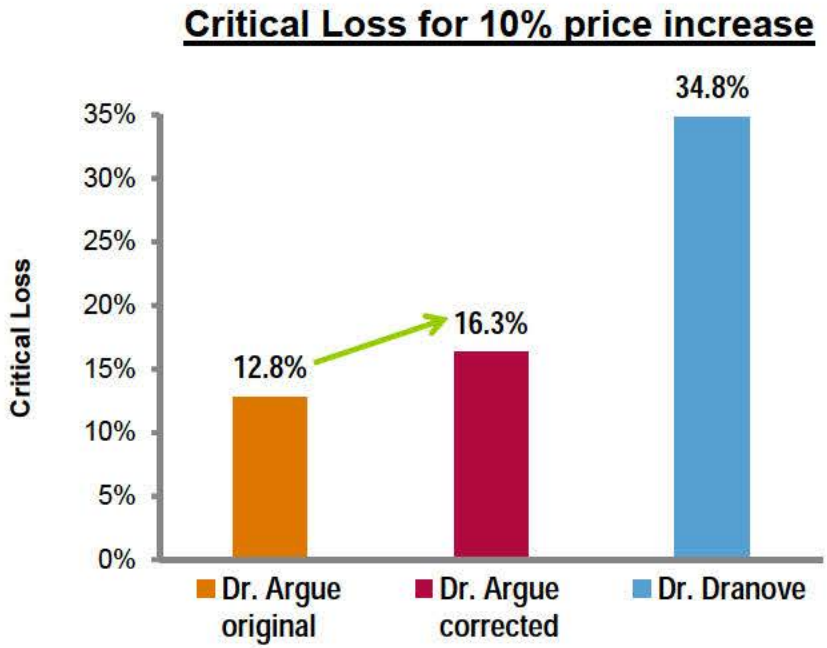


Attorney’s Eyes Only

Dr. Argue's revisions of assumptions increase his critical loss thresholds

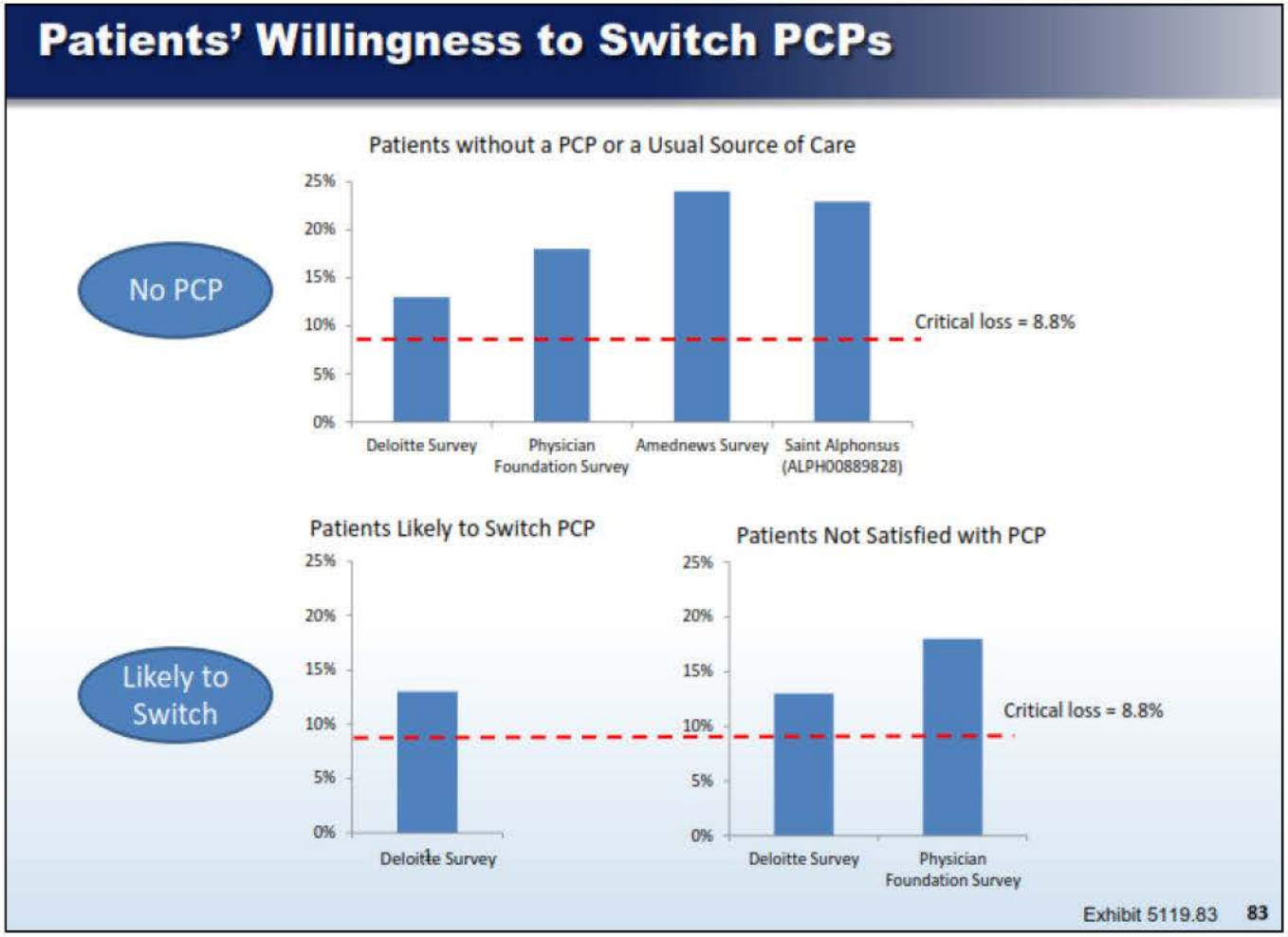
- Important: critical loss is not appropriate to this case





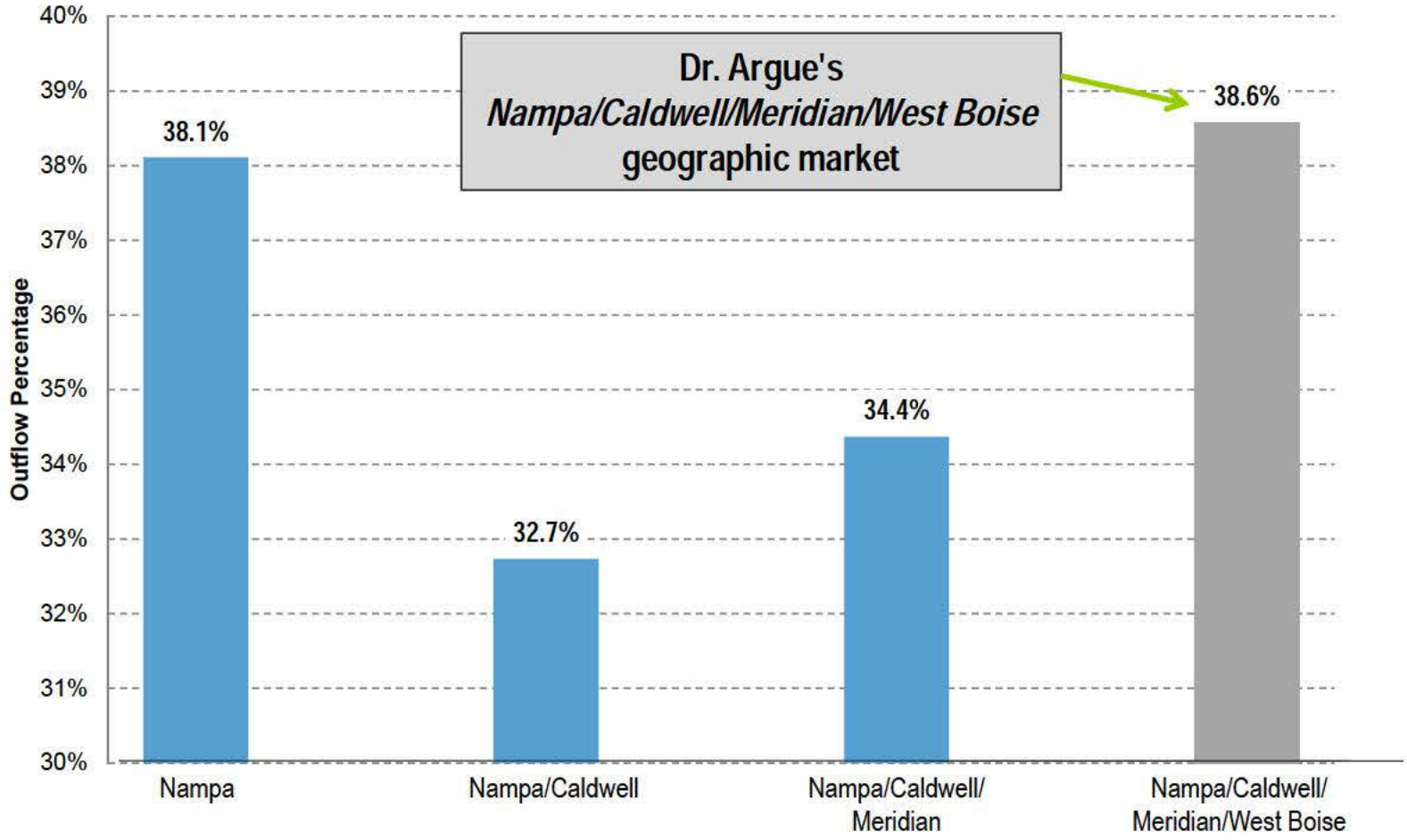
Source: Argue Report, Jul. 15, 2013, Exhibit 11; Argue Surrebuttal Report, Aug. 11, 2013, Exhibit 92; Dranove Reply Report, July 29, 2013, Figure 1.

Dr. Argue's survey data do not inform the actual loss in this case



Source: Demonstrative exhibit, Testimony of David Argue, PhD at 83

Outflow percentages are not a reliable basis for defining the relevant geographic market



TX 2396 (Argue Report) Exhibit 13, Deposition Transcript of David Argue at 177-179

Full financial integration is not necessary to achieve the benefits of clinical integration

Hospital-physician mergers are not necessary to achieving the benefits of clinical integration

- St. Luke's does not require Saltzer in order to offer an ACO or otherwise bear risk
  - Saltzer can likewise bear risk without financial integration with St. Luke's
- ACOs come in a variety of organizational forms and sizes
  - Hospital-led, physician-led, hospital-physician partnerships
  - Many have fewer than 100 affiliated physicians*
- No single best form of clinical integration
  - The ***financial incentives*** facing a provider are distinct from the ***employment situation*** facing that provider—aligning financial incentives does not require employment of physicians
  - Employment alone is not sufficient to alter the incentives facing physicians

*Source: Dranove Report, Figure 29 (citing http://www.cms.gov/apps/media/press/factsheet.asp?Counter=4405)

Primary Health shows that independent physicians can fulfill the "Triple Aim"

- Independent practice of 30 physicians
- Multiple sites, including Nampa
- Implemented health IT infrastructure with eClinicalWorks (eCW)
  - Using eCW, Primary Health is engaged in evidence-based medicine
  - Using eCW, Primary Health shares EMR data with St. Luke's and Saint Alphonsus
  - Dr. Peterman described Primary Health as "very satisfied" with eCW
- Engages in population health management
  - Quality scoring and health data analytics (e.g., diabetes care)
- According to St. Luke's CEO, Dr. Pate, Primary Health is "well on its way to fulfilling the Triple Aim"

Source: Testimony of David Peterman, 1124, 1133–36, 1138–40, 1145–48, 1151, 1157–58

The PSA with Saltzer does not advance St. Luke's stated goals

- The new organization allows St. Luke's and Saltzer to negotiate reimbursements as a single entity, but may do little to reorganize the delivery of care
- Current PSA is structured as a standard fee-for-service contract
  - wRVU based, with higher pay for performing *more* services
- No risk-based financial incentives for physicians to cooperate in controlling costs and improving quality
  - No capitation or pay-for-performance
- The September 2013 PSA amendment expressed intentions but did not change financial incentives

Professor Enthoven ignores contradictory research on vertical integration in healthcare

Research supports benefits of financial integration

- Mehrotra, et al.: patients treated by tightly integrated medical groups consistently obtained higher-quality primary care than patients treated by IPAs; hybrid groups (using a combination of employed and independent physicians) achieve benefits that IPAs do not
- Gillies, et al.: highly organized systems relying mostly on staff or salaried physicians were found to provide better care than did more loosely organized models
- Weiner: organized, prepaid group practices provide high-quality, cost-effective care with considerably fewer physicians than in other practice environments

Source: Demonstratives for the testimony of Professor Alain C. Enthoven at 25

Professor Enthoven ignores contradictory research on vertical integration in healthcare

- April 2013 Brookings report, written by 18 of the nation's top health policy analysts, specifically calls for enhanced antitrust scrutiny of provider acquisitions:
  - Policy makers should "[e]nhance the current antitrust enforcement practice of imposing ***higher standards and greater scrutiny*** for mergers relative to clinical/financial integration contracts"
  - "Financing and delivery reforms that do not require full integration of providers are ***easier to modify or undo*** than provider mergers if they do not work"
  - Models without full integration "***may also permit more flexibility*** in health care organization as further innovations occur in health care delivery"

Source: Dranove Report, ¶ 280 (Joseph Antos et al., "Bending the Curve," Engelberg Center for Healthcare Reform at Brookings, 2013, p. 31)

Conclusions

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- Nampa is the relevant geographic market
  - Even if the market is expanded significantly, conclusions are the same
- Dr. Argue has offered no well-defined relevant geographic market
  - Critical loss analysis is inappropriate, incomplete, and incorrect
- Competition promotes value in healthcare, but the acquisition substantially lessens competition
  - Increases St. Luke's bargaining leverage, ability to demand higher reimbursements, and capacity to resist innovation
- Brookings study and other research reminds us that acquisitions:
  - Are ***not necessary*** to reduce costs; and
  - ***May fail*** to reduce costs
- Efficiency claims are speculative and not merger-specific