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FTC Wins Again—Acquisition of 60 Physicians in North Dakota Blocked

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The Federal Trade Commission (FTC) won—again. In what has become an all too familiar pattern, the FTC persuaded a district court judge to block a health care transaction intended to create efficiencies and improve clinical care. The latest FTC win has health systems, doctors, and commentators asking: Is an efficiency defense ever possible in court? Are power buyers real, or just a theory? How many doctors are too many to have market power? The latest decision in the continuing battle over health care consolidation provides some new guidance, but many questions remain to be resolved by the next inevitable battle between providers seeking to create new models of care and the FTC.

Background

On December 13, 2017, the U.S. District Court for the District of North Dakota granted a motion brought by the FTC and the state of North Dakota to block Sanford Health's (Sanford) purchase of Mid Dakota Clinic (Mid Dakota).^[1] Sanford and Mid Dakota appealed the district court's order to the Eighth Circuit, and briefing before the appellate court is ongoing. The FTC's concurrent administrative challenge to the merger before an Administrative Law Judge has been pushed back until 21 days after the appeals court rules on the case.

The Relevant Parties

Sanford is a multi-national, vertically integrated health care system that operates in nine states. Sanford's network consists of 45 hospitals, 289 clinics, and more than 1,300 physicians and is primarily located in North Dakota, South Dakota, and Minnesota. Sanford expanded to the Bismarck, ND market in 2012 with the acquisition of a Bismarck-based, integrated health care system now known as Sanford Bismarck. Sanford Bismarck's operations include an acute-care hospital, eight primary care clinics, and several specialty clinics.

Mid Dakota is a multispecialty physician group comprised of approximately 60 physicians and 19 nurse practitioners and physician assistants. Mid Dakota operates nine clinics at five locations and an ambulatory surgery center, all of which are in Bismarck.

Catholic Health Initiative (Catholic Health), a third party that for purposes of this action was aligned with the FTC and the state, is a health care system operating in 18 states, including the only other acute-care hospital in the Bismarck area. In the Bismarck area, Catholic Health employs 88 physicians. Historically, Mid Dakota and Catholic Health have had a strong referral relationship—Mid Dakota is the largest source of referrals for inpatient admissions at Catholic Health's acute-care hospital, and their services have been described as complementing one another.

The Proposed Transaction

In August 2016, Sanford and Mid Dakota signed a term sheet for Sanford's purchase of Mid Dakota. In the proposed transaction, Sanford would purchase all of Mid Dakota's practice, real estate, and tangible assets.

The Court's Findings

Similar to many health care merger litigations, the principal dispute before the court was over the proper definition of the relevant markets. The FTC's definition of the relevant market—which the court accepted—is adult primary care physician services, pediatric services, OB/GYN physician services, and general surgery services sold or provided to commercial insurers and their members in a geographic area that consists of Bismarck, Mandan (a nearby city), and smaller communities within a 40 to 50-mile radius of the cities (the "Bismarck-Mandan area"). The court accepted this definition based on the FTC's expert's testimony that the four relevant physician service lines cannot be substituted in the construction of a marketable health insurance plan network by a commercial insurer.

In contrast, Sanford and Mid Dakota argued that Blue Cross Blue Shield of North Dakota's (Blue Cross of North Dakota) dominance as a commercial insurer—i.e., a "powerful buyer"—in North Dakota and its practice of using statewide reimbursement rates should be considered in defining a broader geographic market. The FTC and state argued the existence of a powerful buyer should only be considered as a defense *after* the FTC has established that the proposed transaction is presumptively illegal. The court sided with the FTC and the state on this point.

Based on the testimony of the FTC's expert, the court found that if the transaction is consummated Sanford will provide 85.7% of the adult primary care physician services in the Bismarck-Mandan area, while Catholic Health will provide 7.9% and other providers would each provide 2% or less; Sanford will provide 98.6% of the pediatrician services in the Bismarck-Mandan area; Sanford will control approximately 84.6% of the OB/GYN services in the Bismarck-Mandan area; and Sanford will be the only provider of general surgeon services in the Bismarck-Mandan area. The court therefore found that the proposed transaction will significantly increase market concentration and substantially reduce competition in each of the four physician service lines. The court accepted the FTC's argument that these increases would result in both anticompetitive price effects and a decrease in competition to provide better health care services to patients. The court found that Sanford and Mid Dakota did not present any evidence to counter the expert's calculations. Thus, the court ruled, the FTC sufficiently established that the transaction is presumptively unlawful.

For its part, Sanford and Mid Dakota argued that the proposed transaction will result in various efficiencies and synergies that will improve services to consumers in the Bismarck-Mandan area, and that those efficiencies and synergies will counteract any anticompetitive effects of the proposed transaction. For example, Sanford and Mid Dakota hired Deloitte to quantify the efficiencies in "clinical care, ancillary services, and non-clinical areas" that would likely result from the merger. Despite Deloitte's detailed report, the court largely rejected the parties' efficiencies defense, finding that the quality efficiencies cited by Sanford and Mid Dakota were not shown to be merger-specific and were insufficient to overcome the presumption of illegality.

The court also ruled that, despite Blue Cross of North Dakota's position as a "powerful buyer" in the Bismarck-Mandan area and throughout North Dakota (it is the largest commercial insurer in the state), it would still be beholden to any rate increases demanded by Sanford post-merger because of Sanford's increased bargaining leverage and the fact that Blue Cross of North Dakota cannot construct a marketable health plan in the Bismarck-Mandan area without including a post-merger Sanford. The court found that other, smaller insurers and self-insured employers would face the same concerns of rate increases.

Finally, Sanford and Mid Dakota failed to convince the court that any new entry or expansion in the Bismarck health care services market would be timely, likely, or sufficient to counteract the near-monopoly that would result from the proposed transaction.

Lessons Learned

The FTC's challenge to the proposed combination of Sanford and Mid Dakota provides several important lessons learned:

- "Small" physician acquisitions are not immune from investigation and challenge. Mid Dakota was 60 physicians. The Idaho St. Luke's challenge in 2016 was 44 doctors. How low will the FTC go in challenging physician acquisitions?
- The "power buyer" defense may not be that powerful. While arguments of power buyers have been present in several recent cases, Sanford and Mid Dakota put the argument front and center. The court took a pass at endorsing the argument in this case.
- Efficiencies continue to be under attack and have failed to persuade the fact finder of their ability to outweigh the potential for competitive harm. Are parties missing the mark in arguing efficiencies, or are they simply never going to win the day?

We do not know exactly where or who will be involved in the next merger challenge with the FTC. We can be certain that health care providers across the United States will continue to pursue consolidation in an effort to create new care models, while the FTC will continue to push back against those combinations they believe will harm competition.

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[1] *Federal Trade Comm'n v. Sanford Health*, 1:17-cv-133 (D.N.D. Dec. 15, 2017), available at https://www.ftc.gov/system/files/documents/cases/1710019_sanfordpiorder.pdf.