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Cautioning Bilateral Monopoly Markets In Health Care

Law360, New York (October 17, 2011, 12:57 PM ET) -- The Obama administration's emphasis on the creation of integrated health care delivery systems — or Accountable Care Organizations — has catapulted antitrust law to the forefront of the analysis of health care reform. There are frequent discussions of medical integration between providers, exclusive dealing arrangements between insurers and health systems, most favored nation clauses, and provider and insurer market power.

The truth in many markets is that a legacy of insurance company mergers, and provider consolidation into health systems or hospital groups, has left health care markets with what can increasingly be characterized as bilateral monopoly markets. In such markets, a dominant insurer faces off against a dominant health system in negotiating reimbursement rates for medical services.

From an antitrust perspective, the difficulty with bilateral monopoly markets is that they create a very real incentive for vertical collusive behavior between the dominant insurer and the dominant provider. The natural response is to enter into a reciprocal exclusive dealing agreement designed to keep each firm's competitors out of their respective markets. Encouraging competition at both the insurer and provider level thus becomes increasingly difficult as each firm entrenches its dominance.

The story of the relationship between the insurer Highmark Inc. and the University of Pittsburgh Medical Center ("UPMC") in the Pittsburgh and broader Allegheny County market for hospital services is a stark example of some of the perverse incentives inherent in such markets. It also provides a strong cautionary tale of the potential antitrust implications for insurers and providers alike.

The UPMC/Highmark story begins in the late 1990s and pauses, most recently, with an Oct. 4, 2011, U.S. Supreme Court decision denying certiorari of the Third Circuit's decision to reinstate a complaint alleging anti-competitive collusion by defendants UPMC and Highmark.

Before getting to that decision, however, it is useful to take a step back and look at the nature of the relationship between the two parties and the state of competition in the market over the last decade.

The Competitors

There have historically only been two main players in the Pittsburgh hospital services market: the UPMC, Pittsburgh's dominant hospital system, and West Penn Allegheny Health System Inc., Pittsburgh's second-largest hospital system. West Penn and UPMC have also traditionally been the two main competitors in the Allegheny County market for hospital services — as well as the only competitors in the market for tertiary and quaternary care services. UPMC has controlled a 55-percent share of the county's market for hospital

services while West Penn's share has hovered at around 20 percent.

Highmark Inc. has consistently been the dominant insurer in the Allegheny County market for health insurance, with a market share staying between 60 percent and 80 percent since 2000. Historically, Highmark tried to preserve competition in the market for hospital services by funding the merger of several financially distressed medical providers, as well as the creation of West Penn.

Understandably, Highmark's goal was to do what it could to minimize UPMC's ability to dominate the provider market and thereby gain leverage over Highmark to ultimately demand greater, supra-competitive reimbursement rates.

In response to UPMC's attempts to demand such excessive rates, Highmark tried forming a discounted, or low-cost, insurance product called Community Blue. Community Blue would give hospitals competing with UPMC (read West Penn) higher patient volume in return for lower reimbursement rates. In antitrust parlance, what Highmark in fact attempted to do was enter into a vertical exclusive dealing arrangement with West Penn — paying discounted rates with the promise of higher patient volume.

Not to be outdone, UPMC, in turn, created its own vertically integrated health insurance product — UPMC Health Plan — which aimed at taking business from Highmark, and indeed became Highmark's primary competitor in Allegheny County. UPMC took a number of other actions that exemplified the "healthy" state of competition in the county. For instance, it opposed the merger that created West Penn, tried to prevent Highmark from funding the merger and then attempted (with some success) to dissuade investors from purchasing West Penn bonds.

The Truce

This state of competition between dominant insurer and dominant hospital system appears to have abruptly come to an end in 2002. As alleged in West Penn's 2009 complaint against Highmark, 2002 was the year in which UPMC and Highmark buried the hatchet and agreed to a de facto reciprocal exclusive dealing agreement to keep each other's competitors out of their respective markets.

According to West Penn's fairly well documented allegations (cited by the Third Circuit as grounds for reinstating the case), UPMC agreed to use its power in the provider market to prevent Highmark competitors from gaining a foothold in the Allegheny County market for health insurance. In exchange, Highmark agreed to help strengthen UPMC and weaken West Penn.

Specifically, UPMC allegedly refused to enter into competitive provider agreements with Highmark's insurance rivals — effectively foreclosing entry of new competition in the Allegheny County health insurance market. UPMC also allegedly purposefully shrank its UPMC Health Plan by cutting the plan's advertising budget and increasing its premiums — leading to a sharp drop in enrollment and effectively removing Highmark's main insurance rival.

In returning the favor, Highmark allegedly took actions to decrease competition in the provider market by increasing its own insurance premiums in order to fund supra-competitive reimbursement rates for UPMC. It then allegedly refused to increase West Penn's reimbursement rates while eliminating its financial support for the flailing hospital. The anti-competitive coup-de-grace was likely the subsequent elimination of its own low-cost insurance plan, Community Blue, which had excluded UPMC to the benefit of West Penn.

The vertical exclusivity and reciprocity of this arrangement had predictable effects.

Insurance premiums rose in Allegheny County, as did UPMC's and Highmark's profits. Further, provider choice dropped as West Penn struggled, scaling back its services and abandoning projects to expand and improve its services and facilities.

The net results for patients in Allegheny County were higher premiums, reduced choice and reduced quality of service.

The Investigation and Competitor Lawsuit

Perhaps not surprisingly, such collaboration between a dominant insurer and a dominant provider began drawing the attention of antitrust regulators. By 2007, the Antitrust Division of the Department of Justice had launched an investigation into "any potential anticompetitive agreements affecting the local health insurance and hospital market." [1]

Not long after the regulator's investigation, West Penn filed its own private lawsuit against Highmark and UPMC alleging a conspiracy in violation of sections 1 and 2 of the Sherman Act, 15 U.S.C. §§ 1 and 2. Somewhat surprisingly given the specificity of the allegations in the complaint and the alleged anti-competitive effects on the market, the district court dismissed the suit, prompting West Penn's appeal to the Third Circuit.

In November 2010, the Third Circuit reversed the lower court's dismissal and revived the lawsuit, holding that the complaint clearly presented sufficient allegations to plausibly suggest that UPMC and Highmark were engaged in anti-competitive conduct. [2] The Third Circuit then stamped its decision as "precedential," — highlighting the importance of the ruling for future cases. UPMC and Highmark then turned to the Supreme Court in a final attempt to have the case dismissed. Last week, that Court denied the defendants' appeal and set the stage for a protracted antitrust battle in the Western District of Pennsylvania.

Back to the Future

Perhaps anticipating the high court's likely refusal to hear the case or feeling the pressure from regulators, Highmark took matters into its own hands even before the Supreme Court's October decision. In June of 2011 it announced plans to acquire West Penn making a total financial commitment of \$475 million dollars over four years, including an immediate \$50 million grant to West Penn and \$75 million to fund scholarships for students attending medical schools affiliated with West Penn and support other programs. [3]

Highmark's president and chief executive officer was quoted as saying that it was "critical to the economic and financial health of the community that Western Pennsylvanians have a choice of health care providers and that we preserve strong and valuable community institutions like the West Penn Allegheny Health System." [4]

In July, less than a month after Highmark's announcement, the Department of Justice ended its investigation into UPMC and Highmark. [5]

In describing the pending purchase of West Penn, Highmark stated that it would effectively settle its dispute with West Penn — "when we reach the final (takeover) agreement, it will address the lawsuit." [6]

According to news reports, UPMC Chief Executive Officer Jeffrey Romoff has repeatedly said that "the hospital network won't negotiate a new contract with Highmark, because the insurer has become an outright competitor of UPMC's with its bid to buy the West Penn network." [7]

As an "outright competitor" to UPMC, Highmark will once again have the incentive to increase competition in the provider market. Similarly, UPMC once again has the incentive to increase competition against Highmark in the insurance market. Indeed, UPMC has

issued an advertising campaign listing five insurance companies to call if Highmark subscribers want to continue seeing UPMC physicians.[8] Two of the five insurance plans (UPMC Health Plan and Cigna) do not yet offer insurance products to individuals in Pittsburgh although UPMC Health Plan expects to do so by Jan. 1, 2012, pending state approval.[9]

In sum, it would appear that the Allegheny market may soon be comprised of at least two, vertically integrated, ACO-type organizations vying to offer an integrated insurance/service product that can provide patients a meaningful choice for comprehensive medical services.

Perhaps the UPMC/Highmark story then should not only serve as a warning of the potentially anti-competitive effects of bilateral monopoly markets — it may also show the path to cost reduction and the future of health care delivery.

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[1] See "UPMC cooperating with anti-competition investigation," Nov. 21, 2007, Pittsburgh Post-Gazette, available at: <http://www.post-gazette.com/pg/07325/835596-28.stm>.

[2] *W. Penn Allegheny Health Sys., Inc. v. UPMC*, 627 F.3d 85 (3d Cir. 2010).

[3] See "Highmark and West Penn Allegheny Health System Announce Plans to Pursue Affiliation," June 28, 2011, available at: <http://www.wpahs.org/news/6-28-2011/highmark-and-west-penn-allegheny-health-system-announce-plans-pursue-affiliation>.

[4] *Id.*

[5] See Justice Department ends probe of UPMC, Highmark, Sept. 2, 2011, Pittsburgh Tribune-Review, available at: http://www.pittsburghlive.com/x/pittsburghtrib/news/s_754723.html#ixzz1aOVQQmbf

[6] See "US Supreme Court won't hear UPMC antitrust appeal," October 4, 2011, The Denver Post-Associated Press, available at: http://www.denverpost.com/ci_19037140.

[7] *Id.*

[8] See Highmark, UPMC uncertainty adds to patients' woes, Oct. 9, 2011, Pittsburgh Tribune-Review, available at: http://www.pittsburghlive.com/x/pittsburghtrib/business/s_760948.html; "Keep your doctor. Check your plan" campaign at: <http://www.keepyourdoc.com/>; Highmark has challenged UPMC's ad campaign as false and misleading. See Highmark says lawsuits have nothing in common, Aug. 1, 2011, Pittsburgh Tribune-Review, available at: http://www.pittsburghlive.com/x/pittsburghtrib/news/pittsburgh/s_749440.html

[9] *Id.*

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