

Economic Issues in the Analysis Of Post-Merger Hospital Conduct

**NATIONAL ECONOMIC
RESEARCH ASSOCIATES**

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Consulting Economists

A Top 10 List: Phrases Most Likely to Elicit Concerns Among Hospitals (and their Counsel)

- **No. 10: “Hi! We’re calling because we’re doing a post-merger review!”**
- **No. 9: “Your friends at Managed Care Plan, Inc. told us how to find you.”**
- **No. 8: “You’re not the target. But can you send to us your data and documents?”**
- **No. 7: “You are the target! Payors tell us that contract negotiations are more contentious.”**
- **No. 6: Area health plans tell us that reimbursement rates rose after the merger.”**

A Top 10 List: Phrases Most Likely to Elicit Concerns Among Hospitals (and their Counsel)

- **No. 5: “Why can’t prices be as low as they were before the merger?”**
- **No. 4: “Can you substantiate the efficiencies and quality of care improvements that were discussed in your pre-merger planning documents?”**
- **No. 3: “Guess what? We found that the merger actually lowered your costs.”**
- **No. 2: “We found that your prices really are higher than the prices at comparable hospitals.”**
- **No. 1: “Let’s talk about remedies.”**

No. 10: “Hi! We’re calling because we’re doing a post-merger review!”

- **Post-merger reviews allow markets to work first, which is useful in an industry where:**
 - **Most mergers have the potential to generate efficiencies**
 - **Health plans have had bargaining strength**
 - **The marketplace is dynamic and evolving**
 - **Questions have been raised about the predictive value of the tools used in a pre-merger investigation**
- **However, post-merger reviews have their blemishes due to the difficulty of:**
 - **Measuring the actual merger-induced change in price**
 - **Measuring improvements in quality and access to care**
 - **Finding and constructing relevant benchmarks**

No. 9: “Your friends at Managed Care Plan, Inc. told us how to find you.”

- **The views of health plans matter**
- **Considerations when interpreting and evaluating these views:**
 - **Causality: separating increases in price, if any, due to market power from increases due to external changes in the marketplace**
 - **Systematic effects: the experience of payors will vary widely due to heterogeneity among health plans in terms of their products, enrollment, and negotiating ability**
- **It is not sufficient to rely on the views of just a handful of health plans**
- **The views of health plans must be tested empirically**

No. 8: “You’re not the target. But can you send to us your data and documents?”

- **Information from third party hospitals can be helpful in:**
 - **Evaluating the credibility and strength of all of the sources of competition that face the merged hospital**
 - **Finding a competitive benchmark**
 - **Disentangling the effects of the merger from other confounding factors:**
 - Bargaining strengths of individual payors
 - Trends in the marketplace
 - Reactions and responses of rivals

No. 7: “You are the target! Payors tell us that contract negotiations are more contentious.”

- **What are the implications of “contentious negotiations”?**
 - **Because reimbursement rates are the product of a bargaining process, it is hard to distinguish “competitive tussle” from “anticompetitive muscle”**
- **Two sets of questions must be evaluated:**
 - **Did prices rise and what were the terms of the agreement?**
 - **Did negotiations become more contentious because of the acquisition and the elimination of a competitor in the marketplace?**
- **The answers will help develop a clear articulation of the theory of competitive harm**

No. 6: Area health plans tell us that reimbursement rates rose after the merger.”

- **Was there an increase in the actual prices paid?**
 - **Application of econometric methods: one way to account for confounding factors and the shifts in market supply and demand**
 - **Must control for changes over time and differences across hospitals**
- **A key issue: controlling for changes in patient case mix**
 - **Econometric approach**
 - **Simulation: tracking the prices paid for a cohort of patients under different contracts that may vary over time (and across hospitals)**
- **Other factors that may have affected the rise in prices:**
 - **Rising costs, health plan-specific factors, contractual terms, and shifts in market supply and demand**

No. 5: “Why can’t prices be as low as they were before the merger?”

- **Pre-merger prices are unlikely to serve as reliable benchmarks for the competitive price:**
 - **The cost of providing hospital care has been rising over time**
 - **In recent years, there has been a shift in bargaining power from health plans to hospitals, which, by itself, is not a source of anticompetitive harm**
 - **Reimbursement rates may have been below long-run competitive levels prior to the merger**
- **The competitive benchmark must be constructed based on a clear specification of the marketplace had the merger not taken place**

No. 4: “Can you substantiate the efficiencies and quality of care improvements?”

- **Most, if not all, transactions are motivated by the desire to improve the quality of care or to expand the range of services that are provided**
- **Improvements in quality are typically associated with an increase in price**
- **Quality is difficult to measure, but one alternative is to examine the investments that were made after the merger**
- **An econometric analysis of the merged hospital’s pricing over time can be useful, even if it produces an over-estimate or an upper-bound of the merger-induced price increase**

No. 3: “Guess what? We found that the merger actually lowered your costs.”

- **The expectation:**
 - **Cost savings will result in lower prices**
- **The complications:**
 - **There are many categories of costs: a decrease in merger-specific costs may have been outweighed by increases in other cost categories**
 - **Most hospital contracts are negotiated well in advance of the actual effective date of the contract, which leads to a lag between the period in which the cost savings were realized and the period in which payors would see the corresponding benefits**
 - **Prices depend not only on past and current costs; they also depend on expectations of future costs**

No. 2: “We found that your prices really are higher than the prices at comparable hospitals.”

- **The analysis must be capable of testing whether there has been a systematic anticompetitive problem that can be attributed to the merger**
- **A comparison of prices over time and across hospitals must account for:**
 - **Shifts in market supply and demand**
 - **Improvements in quality of care and access to care**
 - **Changes in hospitals and payors’ bargaining position over time**
 - **Historical costs (and cost savings) as well as expectations about the rise in future costs.**
- **An empirical study must be based on reliable data**

No. 1: “Let’s talk about remedies.”

- **Possible remedies: divestitures and price freezes**
- **Talk of a divestiture could affect hospital incentives in the short run, which could delay or cancel ongoing efforts to expand capacity, add new services, or invest in infrastructure**
- **The issue:**
 - **A post-merger review is an important enforcement initiative, but to do a review well is likely to require time and resources**
 - **Is there a way to conduct a review that can minimize the uncertainty for the merged hospital and maintain the merged hospital’s incentive to continue investing in programs that expand capacity, quality of care, and access to care?**

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