UNITED STATES OF AMERICA
FEDERAL TRADE COMMISSION
WASHINGTON, D.C. 20580

BUREAU OF COMPETITION

June 20, 1991

Martin J. Thompson
Riordan & McKinzie
California Plaza
300 South Grand Avenue
29th Floor
Los Angeles, California 90071

Dear Mr. Thompson:

This letter responds to your request for a staff advisory opinion concerning a proposal by a physician IPA network that sponsors a preferred provider organization (PPO) to negotiate prices with individual hospitals whose services will be marketed to payers as part of the PPO package. For the reasons discussed below, it does not appear the proposed conduct would violate the Federal Trade Commission Act.

According to your letter of April 11, 1991, you represent a physician IPA network that currently offers a physician-services PPO to third-party payers. The IPA uses a messenger model for pricing physician services: that is, the IPA communicates to its member physicians the proposed prices of each third-party payer that contracts with the PPO, and each physician decides individually whether to accept or reject each price proposal. The IPA wants to add hospital services to the PPO in order to offer a complete package of services to payers. However, it has been informed by payers that a messenger model will not be acceptable for the pricing of hospital services. Instead, payers want to know what hospitals will participate in the program at the time that the payer and the PPO reach an agreement.

Therefore, the IPA proposes to bargain on an individual basis with hospitals that it wants to include in the package of services it offers to third-party payers. It will solicit from each of the desired hospitals its best price offer, and then negotiate, as necessary, with any hospital whose prices must be reduced if the PPO is to be successfully marketed to third-party payers. Each hospital's bid price will be kept confidential, and the hospitals will not participate in the management of the IPA.

Your letter states that the IPA will take certain precautions to avoid facilitating collusion among the hospitals. In telephone conversations supplementing your letter, you have explained that the negotiations will be conducted by an individual or a small group of persons within the IPA; that those persons will not have any affiliation with any hospital; that the bid or other price information of a hospital will not be disclosed to other hospitals; that discussions will not be carried out in a way that would enable a hospital to ascertain the bids of other hospitals; and that hospitals' bids would not be widely disclosed within the board of directors or general membership of the IPA.

I understand from your letter that the PPO operates in a large metropolitan area within which many managed care programs compete. Hospitals typically participate in a number of managed care plans, and your client will contract with hospitals on a non-exclusive basis.

You further state that the IPA network represents less than 10% of the physicians practicing in the region serviced by the PPO. It is not yet known what percentage of hospitals in the market will participate in the program. However, the PPO will contract only with those hospitals that it feels are necessary to market the program successfully, and it is not anticipated that the combined market share of the hospitals participating in the PPO will be large.

Your letter asks for an advisory opinion on one "relatively narrow" question: whether there is "any inherent violation of law in the proposed scenario for conducting negotiations over price with individual hospitals and then contracting to commit the services of these hospitals to payers, where the organization in question is not controlled or managed by the hospitals and the organization intends to create controls calculated to prevent it from facilitating any form of collusion among competing hospitals."

The Commission approved the operation of a PPO in its advisory opinion concerning Health Care Management Associates.[1] In that instance, the PPO was organized by a firm that was not affiliated with or controlled by providers of health care

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[1] 101 F.T.C. 1014 (1983).

services or insurers. HCMA proposed to act as an intermediary between health care providers and third-party payers, negotiating on behalf of individual providers or integrated groups of providers binding agreements on the prices that each provider would accept as payment for services provided to patients covered by third-party payers that contracted with the PPO.

Your client proposes to perform a function similar to that performed by HCMA, in that it will be an intermediary between individual hospitals and individual third-party payers. While the IPA network is controlled by physicians who compete with one another, it does not, according to your letter, engage in collective price negotiation on behalf of its member physicians. Nor does it appear that the IPA network will participate in or facilitate collective negotiations by hospitals. It will simply act as an agent for individual hospitals in reaching agreements on price between the hospitals and third-party payers.

A similar arrangement was the subject of a staff opinion letter issued to The Equitable Life Assurance Society.[2] In that matter, Equitable proposed to act as an intermediary between hospitals and third-party payers in negotiating hospital reimbursement rates that would be based on the Diagnosis Related Groups ("DRGs") developed by Medicare. Specifically, Equitable proposed to identify hospitals willing to enter into agreements to accept DRG reimbursement, and to negotiate with the hospitals individually specific rates that would be binding on the hospitals and the third-party payers. There was to be no collective negotiation with hospitals, and Equitable intended to limit the availability of the rates it negotiated to payers covering no more than 15 to 20% of the population of any relevant geographic area. The staff concluded that the proposal did not appear likely to restrain competition unreasonably in any market.

The proposed negotiations between hospitals and the physician network, as you have described them, do not appear to raise serious antitrust concerns. The hospitals will not participate in the management of the physician IPA network that will conduct negotiations on behalf of individual hospitals with third-party payers, and the IPA itself will not negotiate collectively on behalf of the hospitals. Furthermore, the IPA proposes to take specific precautions to ensure the confidentiality of pricing information obtained from each

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[2] Letter from M. Elizabeth Gee to Jonathan E. Gaines (March 26, 1986).

hospital. Therefore, the proposed arrangement would not appear to be a price-fixing mechanism for hospitals, or create any other horizontal agreement that is inherently suspect under the antitrust laws.

Moreover, there does not appear to be any significant danger that the PPO will obtain market power or will be able to impede the development or operation of other managed care programs. The PPO represents fewer than 10% of the physicians practicing in the metropolitan area where the PPO operates, and does not anticipate that it will represent a large proportion of the hospital business in the area. Furthermore, the participation agreements between the PPO and the health care providers will be non-exclusive, so that providers will be able to participate in other managed care programs. Thus, the proposed conduct does not appear to create an appreciable risk of actual or attempted monopolization.

For the reasons stated above, it does not appear that the proposal you have described is likely to be an unfair method of competition in violation of the Federal Trade Commission Act. Under the Commission's Rules of Practice §1.3(c), the Commission is not bound by this staff opinion and reserves the right to rescind it at a later time. In addition, this office retains the right to reconsider the questions involved and, with notice to the requesting party, to rescind or revoke the opinion if implementation of the proposed program results in substantial anticompetitive effects, if the program is used for improper purposes, or if the public interest otherwise so requires.

Very truly yours,

Mark Horoschak

Mark J. Horoschak
Assistant Director