**IN THE UNITED STATES DISTRICT COURT**
**FOR THE NORTHERN DISTRICT OF ILLINOIS**
**EASTERN DIVISION**

FEDERAL TRADE COMMISSION

And

STATE OF ILLINOIS

Plaintiffs,

v.

ADVOCATE HEALTH CARE NETWORK,

ADVOCATE HEALTH AND HOSPITALS CORPORATION,

And

NORTHSHORE UNIVERSITY HEALTHSYSTEM

Defendants.

No. 15-cv-11473
Judge Jorge L. Alonso
Magistrate Judge Jeffrey Cole

PUBLIC VERSION

**PLAINTIFFS' POST-REMAND REPLY BRIEF IN SUPPORT OF PLAINTIFFS' MOTION FOR PRELIMINARY INJUNCTION**

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# Table of Authorities

**Cases**

# Glossary of Abbreviated Terms

Abbreviations used in Plaintiffs' Post-Remand Reply Brief in Support of Plaintiffs' Motion for Preliminary Injunction have the following meanings:

1. ***Record***

| | |
|---|---|
| OA Tr. | Transcript of Proceedings before the Seventh Circuit In the Matter of FTC and State of Illinois v. Advocate, et al. (Aug. 19, 2016) |
| D's App. Br. | Brief of Defendants-Appellees, *FTC v. Advocate Health Care Network*, 841 F.3d 460 (7th Cir. 2016) (No. 16-2472) (Aug. 1, 2016, App. Doc. No. 79) |
| D's Supp. Br. | Defendants' Supplemental Post-Hearing Memorandum in Opposition to Plaintiff's Motion for Preliminary Injunction (Dec. 14, 2016, Doc. No. 557-1) |
| PI Hrg. Tr. | Transcript of Proceedings – Preliminary Injunction Hearing (Apr. 11, 2016 through May 25, 2016) |
| P's FOF | Plaintiffs' Proposed Findings of Fact and Conclusions of Law (May 18, 2016, Doc. No. 446) |
| P's PH Br. | Plaintiffs' Post-Hearing Brief (May 18, 2016, Doc. No. 445) |

2. ***Names***

| | |
|---|---|
| Aetna | Aetna, Inc. |
| Cigna | Cigna Corp. |
| Humana | Humana Inc. |
| Land of Lincoln | Land of Lincoln Mutual Ins. Co. |
| United | United HealthCare |

## INTRODUCTION

The Seventh Circuit made two "central" findings about the commercial realities of hospital competition in Chicago's northern suburbs: (1) patients prefer to receive inpatient care locally, and (2) insurers cannot successfully market networks to employers without including at least some of the merging hospitals. Op. at 3. These commercial realities compel the conclusion that a hypothetical monopolist owning all eleven North Shore Area hospitals could profitably raise prices by at least a small but significant amount and, thus, that the North Shore Area is a relevant geographic market.

Because the commercial realities weigh so heavily against them, Defendants spend most of their post-remand brief rehashing attacks on Dr. Tenn's model. Dr. Tenn's methodology is sound and the arguments Defendants make to the contrary were either explicitly rejected by the Seventh Circuit or are inconsistent with its decision. And Defendants are wrong to imply that the question posed by the hypothetical monopolist test can only be answered by experts employing merger simulation models. In fact, the Seventh Circuit cited insurer testimony that alone establishes that it would be profitable for a hypothetical monopolist of North Shore Area hospitals to raise prices.

If this Court finds (as it must) that the relevant geographic market is no broader than the North Shore Area, it also must find that the merger is presumptively anticompetitive. In addition to establishing a presumption of illegality, the record also contains overwhelming evidence that the merger would eliminate the head-to-head competition between Advocate and NorthShore that currently benefits consumers. Without that competition, Defendants will be able to raise prices to insurers, who would choose to pay higher rates to the merged entity rather than offer networks that employers are unlikely to buy. As the Seventh Circuit held, NorthShore's own

history of post-merger price increases proves that even mergers involving a small number of hospitals in large urban areas can significantly harm consumers.

No court has ever found that a presumptively unlawful merger would generate efficiencies sufficient to outweigh its anticompetitive effects. Defendants have not come close to establishing such extraordinary efficiencies here. They continue to rely on grandiose and unsubstantiated assertions about a "high performing network," but, as Plaintiffs have repeatedly shown, to the extent that there are any consumer benefits associated with the HPN, the merger is not necessary to achieve them. Nor is the merger necessary for NorthShore to reduce its physician rates.

Faced with a presumptively unlawful merger, and the lack of significant cognizable efficiencies, the Court should enjoin the merger pending a full administrative hearing. Plaintiffs are likely to succeed on the merits and the equities weigh in favor of maintaining the current competition between Defendants during the administrative proceedings. Without a preliminary injunction, it is unlikely that Plaintiffs could obtain complete and effective relief after those proceedings conclude. Defendants' speculative claims about the HPN are not equities weighing against a preliminary injunction; any merger-specific benefits would still be available if Defendants prevail in the administrative proceedings.

## ARGUMENT

### I. Defendants Ignore the Seventh Circuit's Rulings

The Seventh Circuit found the evidence unequivocal on issues central to the commercial realities, including patient preference for local hospitals and insurers' need to include at least some of the merging firms' hospitals in networks that they market to employers. Op. at 3. Defendants disagree and argue that the evidence the Seventh Circuit relied on was vague and equivocal. According to Defendants, this Court should reach contrary conclusions about the

commercial realities or, alternatively, ignore the commercial realities and focus on an alleged "battle of the experts." To the extent that Defendants take issue with the Seventh Circuit's decision, however, they should have sought rehearing or filed a petition for certiorari; they cannot relitigate issues the appellate court decided.

For example, Defendants argue that networks that exclude all of the merging firms' North Shore Area hospitals are attractive to employers. D's Supp. Br. at 14-15. According to Defendants, the Seventh Circuit relied on insurer testimony that concerned the [redacted] and was not specific to hospitals in the northern suburbs. D's Supp. Br. at 15. (emphasis in original). Defendants made the same argument about insurer testimony in their appellate brief. *See* D's App. Br. at 20, 34. The Seventh Circuit rejected that argument and specifically held that the evidence was "not equivocal" on the point "central to the commercial reality of *hospital* competition in *this market*" that "insurers cannot market healthcare plans to employers with employees in Chicago's *northern suburbs* without including at least some of the *merging hospitals* in their networks." Op. at 3 (emphasis added).

On appeal, Defendants had argued that the commercial success of Blue Choice proves that networks that exclude both Advocate and NorthShore are "currently and successfully" marketed to employers. D's App. Br. at 38-39. During oral argument, however, Defendants conceded that Blue Choice is *not* commercially successful with employers and is primarily sold to individuals. OA Tr. 23:25-26:3. The Seventh Circuit relied on evidence about the limited appeal of Blue Choice in its decision. Op. at 23. Defendants now argue that the testimony about Blue Choice is "vague" and "does not change [the] conclusion" that employers would, in fact, be interested in networks that exclude the merged firm. D's Supp. Br. at 14. The appellate court heard Defendants' arguments about Blue Choice, however, and held that the unanimous insurer

testimony, supported by the record as a whole, shows that such a network would *not* be attractive to employers. Op. at 23.

The geographic market must correspond to these commercial realities. *See* Op. at 10. But, instead of contending in a meaningful way with the Seventh Circuit's findings, Defendants attack Dr. Tenn's model. This Court does not, however, need to resolve any alleged "battle of the experts" to grant Plaintiffs' motion. Congress "prescribed a pragmatic, factual approach to the definition of the relevant market and not a formal, legalistic one." *Id.* (quoting *Brown Shoe Co. v. United States*, 370 U.S. 294, 336 (1962)). While expert testimony is often useful in defining a market, Defendants are wrong to suggest that market definition always turns on expert analysis. In *Penn State Hershey*, for example, the Third Circuit relied on insurer testimony to find that the proposed geographic market satisfied the hypothetical monopolist test and did not cite the extensive expert testimony on that issue.[1] *See FTC v. Penn State Hershey Med. Ctr.*, 838 F.3d 327, 338-46 (3rd Cir. 2016); *cf FTC v. Penn State Hershey Med. Ctr.*, 185 F. Supp. 3d 552, 557 (M.D. Pa. 2016); *see also FTC. v. OSF Healthcare Sys.*, 852 F. Supp. 2d 1069, 1086 (N.D. Ill. 2012) ("defendants have cited no authority indicating that a merger simulation is required in order to obtain a preliminary injunction").

## II. Dr. Tenn's Testimony is Reliable and Consistent with the Seventh Circuit's Decision

Although evidence other than Dr. Tenn's testimony clearly establishes that Plaintiffs have met our burden, Dr. Tenn's analysis is reliable and consistent with the weight of the evidence.

[1] Defendants argue that *Penn State Hershey* is distinguishable because the Third Circuit found it "significant" that insurers viewed the Hershey area as a "distinct market" and testified that the merged entity could extract a price increase from them. D's Supp. Br. at 15. But nowhere in the *Penn State Hershey* decision does the court refer to those facts as "significant." Rather, the court expressly relied on the testimony of insurers that they could not market health plans that excluded the merging firms to find that the proposed market satisfied the hypothetical monopolist test. *See Penn State Hershey*, 838 F.3d at 345-46. And, in any event, the record here shows that market participants view the northern Chicago suburbs as a distinct market and that the merged firm will be able to extract price increases from insurers. *See* P's FOFs ¶¶ 11, 23-24, 47-52; P's PH Br. at 14-15.

Dr. Tenn found that 48% of the patients admitted to one of the eleven hospitals in the North Shore Area would substitute to another hospital in that market if their first-choice hospital were not available. PX06000 ¶ 99. Dr. Tenn used an approach that is consistent with the economic literature and with the Horizontal Merger Guidelines to analyze how combining all of the North Shore Area hospitals into a single entity would impact bargaining between hospitals and insurers. He concluded that it would be profitable for a hypothetical monopolist to demand a small but significant price increase from insurers, who would be willing to pay a little more to avoid excluding all North Shore Area hospitals from their networks and risk a large reduction in membership.[2] *Id.* at ¶ 110.

Defendants' criticisms of Dr. Tenn's analysis fail because they ignore or misstate the Seventh Circuit's findings. For example, Defendants argue that Dr. Tenn erred by relying on diversion ratios which, according to Defendants, the appellate court found to be "inadequate" and "insufficient." D's Supp. Br. at 1, 5. But the Seventh Circuit did *not* hold that it is inappropriate to consider patient-level diversions; it criticized how Defendants interpreted those diversions. On appeal, Defendants had argued (as they did to this Court) that "diversion ratios show that in the event of an above-market price increase at the party hospitals, most patients would be willing to divert to hospitals that the FTC excluded from its proposed market, and that insurers therefore could market a network excluding those hospitals." D's App. Br. at 39; *see also* OA Tr. 22:16-23:11. As the Seventh Circuit held, the critical flaw in Defendants' argument is that they "focus on the patients who leave [the] proposed market instead of on hospitals' market power over the patients who remain." Op. at 25; *see also id.* at 3 ("The court's analysis

[2] As the Seventh Circuit explained, employers generally try to offer plans that appeal to all of their employees. Op. at 24-25. It follows that an employer with employees in the North Shore Area would be unlikely to offer a network that a significant percentage of those employees would find unacceptable. Thus, an insurer that dropped all North Shore Area hospitals from its network could lose the vast majority of its employer group business.

erred by overlooking the market power created by the remaining patients' preferences"). Dr. Tenn does not make Defendants' error. His analysis examines the hypothetical monopolist's market power over insurers, which is informed, in part, by the preferences of patients who are reluctant to leave the North Shore Area for inpatient care. *See* Op. at 15-16 ("insurers respond to both prices and patient preferences"); *Penn State Hershey*, 838 F.3d at 342.

Defendants argue that the specific model Dr. Tenn employed is unreliable for a variety of reasons. They made the same arguments to the appellate court.[3] *See* D's App. Br. at 14, 46, 51-53; *see also* OA Tr. 44:17-21. The Seventh Circuit nonetheless concluded that Plaintiffs have made a "strong case" that the market contains a "very small" number of hospitals. Op. at 26.

That Dr. Tenn's model is reliable is evident from its results, which are fully consistent with the commercial realities. P's PH Br. at 6, 8; *see also FTC v. Sysco Corp.*, 113 F. Supp. 3d 1, 37 (D.D.C. 2015) (finding plaintiffs' expert persuasive because his conclusions were consistent with business realities). In contrast, while Dr. McCarthy agrees with Dr. Tenn that, "when two hospitals merge, there's a change in the willingness to pay because now it's more valuable to have this hospital in your network," his model predicts that an *increase* in a hospital's value to insurers would lead to that hospital receiving *lower* reimbursement rates. McCarthy PI Hrg. Tr. 1255:21-23; P's FOFs ¶¶ 82-86; P's PH Br. at 15. Dr. McCarthy's implausible results are inconsistent with economic theory and with the overwhelming weight of the evidence. *See* McCarthy PI Hrg. Tr. 1360:20-1361:2; P's FOFs ¶¶ 70, 74, 85; P's PH Br. at

[3] Defendants also argue that Dr. Tenn's model is flawed because it always predicts a price increase. As Dr. Tenn testified, if the diversions and margins are small, his model would predict a trivial price increase and the proposed market would fail the hypothetical monopolist test. Tenn PI Hrg. Tr. 589:16-20. In this case, however, the intra-market diversions are high and, given applicable margins and prices, the predicted price increase is over 5%. Tenn PI Hrg. Tr. 489:24-490:1, 493:2-9. Defendants also attack the margin information Dr. Tenn used, but using Dr. McCarthy's margin calculation in the model does not change the prediction that a hypothetical monopolist could profitably raise prices by more than 5%. *See* DX5000 McCarthy Report ¶ 104, n. 159 (using alternative margins in Dr. Tenn's model leads to an estimated price increase of over 5% from a merger of only Defendants' hospitals)

14-15. Moreover, Dr. McCarthy's model predicts that even a merger involving a large number of Chicagoland hospitals would lead to price decreases, but, as the Seventh Circuit held, NorthShore's own history proves otherwise.[4] Op. at 19.

Defendants also rehash the argument that specific hospitals outside the North Shore Area are close substitutes for the merging firms and Dr. Tenn erred by not adding those hospitals to his proposed market. *See* D's App. Br. at 30-31, 48-49; OA Tr. 27:13-28:10. Contrary to what Defendants say in their brief, the Seventh Circuit did not endorse the view that hospitals that are "closer substitutes" must be added to a proposed market even if that market satisfies the hypothetical monopolist without them. Instead, the appellate court held that "[a] geographic market does not need to include all of the firm's competitors," but only those that would "substantially constrain" the merging firms' price-increasing ability. Op. at 12.

In addition, the Seventh Circuit rejected the factual premise of Defendants' argument. Defendants had argued that the diversion ratios establish that Northwestern Memorial and other hospitals are close substitutes for the merging firms and, therefore, that those hospitals must be included in a relevant geographic market. But the appellate court held that Defendants' argument "overlooks insurers' role in the marketplace." Op. at 25 n. 5. Even if "a sizable minority of patients consider Northwestern Memorial a close substitute, it does not follow that insurers could offer it as a sufficient substitute for a commercially viable insurance network." *Id.*

On remand, Defendants claim that other evidence in the record also shows that Northwestern Memorial, Presence St. Francis, Rush, and Lurie must be included in the relevant geographic market. The evidence Defendants cite, however, merely confirms that, as the

[4] Defendants argued to the Seventh Circuit, as they do again to this Court, that it should disregard NorthShore's history of significant post-merger price increases because the healthcare industry has changed. OA Tr. 35:18-37:23. The Seventh Circuit disagreed.

diversion ratios indicate, those hospitals are options for some patients. No insurer testified that an out-of-market hospital would be an adequate substitute for the merging firms in a commercially viable network.[5]

Moreover, Defendants made the same arguments (and cited much of the same evidence) on appeal. *See* D's App. Br. at 12, 14-16, 21, 27-29, 41-42; OA Tr. 28:3-10, 32:22-33:4. Yet the Seventh Circuit held that, even if Northwestern Memorial were a close substitute for NorthShore from the perspective of insurers, and even if it were appropriate to add that hospital to the proposed market, it would not affect the outcome of this case because "there is no comparable evidence" about other hospitals. Op. at 25 n.5. Defendants have conceded their merger is presumptively unlawful even if the relevant geographic market includes the eleven North Shore Area hospitals and Northwestern Memorial. *Id.* In fact, Defendants have admitted that even if one were to add *both* Presence St. Francis and Northwestern Memorial to the proposed geographic market, their merger would meet the presumption. *See* PI Hrg. Tr. 1890:24-1891:8.

## III. Defendants' Merger Is Anticompetitive

Defendants do not dispute that, if the North Shore Area is a relevant geographic market, their merger is presumptively unlawful. The presumption is buttressed by overwhelming evidence showing that Advocate and NorthShore are close competitors, that consumers benefit from their head-to-head competition, and that the merger would allow Defendants to raise their reimbursement rates. *See* P's FOFs ¶¶ 57-74. Defendants have not produced any evidence sufficient to overcome the presumption.

[5] Defendants cite testimony from Aetna about the purported interchangeability of NorthShore and Northwestern Memorial. D's Supp. Br. at 13. But, under pointed questioning from the appellate court, Defendants admitted that the cited testimony concerned state regulatory requirements, not commercial viability. OA Tr. 28:11-30:23.

Defendants cite insurer support as evidence that their merger would not have anticompetitive effects, but the insurers admitted that they lacked a factual basis for the statements Defendants cite. *See, e.g.*, Beck (United) PI Hrg. Tr. 1123:15-20 (United has no information about cost savings); Nettesheim (Aetna) PI Hrg. Tr. 1195:19-1197:10 (Aetna has no information about cost or quality improvements); [redacted] PX03005 ¶ 17 (Land of Lincoln "has no knowledge about . . . any potential efficiencies" from the transaction). Moreover, Advocate counts United, Humana, and Land of Lincoln as supporters of the merger, but executives from each of those companies testified [redacted]

Defendants also argue that their merger will not have anticompetitive effects because, "if the HPN must always be priced lower than networks that have more hospitals, then those other hospitals necessarily constrain the price that Advocate-NorthShore can charge." D's Supp. Br. at 22. Defendants are mixing apples and oranges. The price for broad networks may limit what insurers can charge for narrow networks, but has no bearing on the merged firm's ability to demand higher reimbursement rates from insurers. The relevant question is not the price of a narrow network compared to the price of a broad network, but the price that the *merged firm* could charge for being included in an insurer's network (whether narrow or broad) compared to the prices that Defendants can charge as separate entities.

Finally, Defendants assert that the merger-specific efficiencies in this case are the "largest ever presented." D's Supp. Br. at 19. Any comparison between Defendants' alleged

efficiencies and the efficiencies claimed in other reported cases, however, only serves to highlight the absurdity of Defendants' arguments. In *FTC v. Sysco*, for example, the defendants claimed that their merger would generate $490 million in merger-specific efficiencies. 113 F. Supp. 3d at 82. To estimate the efficiencies, the defendants had engaged in a "meticulous" analysis of a "back-breaking amount of information" over an eight-month period that involved an estimated 170 employees of the merging firms and an additional 100 employees of their consultant. *Id.* Nonetheless, the district court found that the defendants had not presented sufficient verifiable evidence of their claimed efficiencies. *Id.* In contrast, Advocate and NorthShore claim that their merger will result in over $500 million in merger-specific efficiencies, but have not produced even a single document showing how Dr. Sacks calculated those efficiencies.

## IV. The Equities Favor an Injunction

An injunction pending administrative proceedings would be in the public interest. If Plaintiffs' motion is denied and Defendants merge, consumers will be deprived of the benefits of Defendants' competition during the course of the administrative proceedings and possibly forever. If Plaintiffs prevail on the merits (as they are likely to do) it will be difficult or impossible to "unscramble the eggs" and restore the lost competition. On the other hand, Defendants argue that a delay *may* prevent them from offering an HPN before 2019. As multiple insurers testified, however, Advocate can offer an HPN today. To the extent that the *merger* has any consumer benefits, those benefits will still be available after the administrative proceedings conclude. *See Penn State Hershey*, 838 F.3d at 353.

## CONCLUSION

For the foregoing reasons, this Court should grant Plaintiffs' Motion for a Preliminary Injunction.

Dated: January 11, 2017

Respectfully Submitted,

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**CERTIFICATE OF SERVICE**

I HEREBY CERTIFY that on the 11th day of January, 2017, I filed and served the foregoing on all counsel of record via the Court's electronic filing system.

/s/ Christopher Caputo

Christopher Caputo
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