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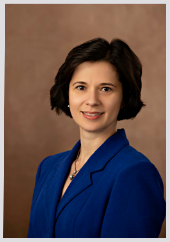
A BRIEF ANALYSIS OF POLICY AND LITIGATION

Back to the Drawing Board -- EEOC's EEO-1 Component 2 Requirement

Simona Andrei



Vice President Simona Andrei offers expertise in studies of pay equity, conducted proactively or in litigation setting. Dr. Andrei also assists clients in matters involving claims of alleged disparate impact in other employment practices and wage and hour compliance.

In 2016, the Equal Employment Opportunity Commission ("EEOC") launched an initiative to expand the data collected through its Employer Information Report (EEO-1) in an effort to "assist the agency in identifying possible pay discrimination." Specifically, the EEOC added a pay and hours reporting requirement ("Component 2") to the list of elements for data collection. However, this expanded data collection initiative by the EEOC will be short-lived. The EEOC recently announced that it will not seek approval for the continued collection of EEO-1 Component 2 data.

The EEO-1 Component 2 data consist of taxable income and hours worked in a calendar year, aggregated by twelve pay bands and the same categories as the traditional EEO-1 Component 1 data (job category, race, ethnicity, and gender). The EEOC's decision about what pay data to collect was ostensibly driven by the need to balance usefulness with the burden of collecting the data on employers. However, the EEO-1 Component 2 data seem to have failed on both fronts.

From a utility perspective, the requested Component 2 data include a measure of compensation that does not allow for appropriate pay equity comparisons, do not include any factors that could legitimately influence pay, and use job groupings that are too broad to identify similarly situated employees. The Office of Federal Contract Compliance Programs (OFCCP), the other government agency tasked with enforcing laws that prevent discrimination in the workplace, recently stated that it "will not request, accept, or use Component 2 data, as it does not expect to find significant utility in the data".

The burden of collecting EEO-1 Component 2 data on employers also has proven to be significant. Preparing the current form requires extracting and combining information from a company's Human Resources Information System (HRIS), payroll, and time keeping systems. This has been a challenging task for employers that do not have well-integrated systems.

Recent years have seen a tremendous increase in public demand for action to close existing pay gaps in general, and gender pay gaps in particular. Therefore, the EEOC is likely to renew its efforts to collect pay data and even has stated that going forward it may include a new reporting requirement by which employers would submit pay data or related information. To be prepared for such initiatives, employers should consider conducting proactive internal pay audits.

Also In This Issue

DOJ's Challenge of Atrium Health's Anti-Steering Restrictions

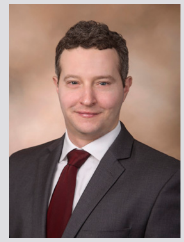
Jason L. Albert discusses the challenge of Atrium Health's anti-steering restrictions by the Department of Justice ("DOJ") and the State of North Carolina. The District Court denied Atrium's motion for a judgment on the pleadings, noting that the government alleged higher prices resulted from Atrium's anti-steering restrictions. DOJ and the State of North Carolina reached a settlement with Atrium which broadly nullified existing contractual anti-steering restrictions between Atrium and health insurers and placed limitations on future contractual arrangements between Atrium and insurers. DOJ and the State of North Carolina continued their challenge despite the Second Circuit's ruling in the Amex case. This suggests that antitrust regulators may continue to question the legality of anti-steering restrictions in healthcare settings.

Antitrust Analysis with Upward Pricing Pressure and Cost Efficiencies

Jéssica Dutra discusses upward pricing pressure ("UPP") and cost efficiencies. Dr. Dutra considers modified UPP formulations that include merger-specific cost efficiencies in various functional forms and analyzes the efficacy of the modified UPP formulations using Monte Carlo simulations. These Monte Carlo simulations indicate that the modified UPP formulations which include merger-specific cost efficiencies have lower median post-merger price predictions. The simulations also indicate that the modified UPP formulations including merger-specific cost efficiencies yield substantial gains in post-merger price prediction and merger screening accuracy. These results show that including cost efficiencies in a manner guided by the theoretical model may yield substantial improvements in accuracy of UPP as a tool in antitrust analysis.

DOJ's Challenge of Atrium Health's Anti-Steering Restrictions

Jason L. Albert



Senior Economist Jason L. Albert has worked on numerous healthcare issues, including conduct matters and hospital and physician group mergers. This article is based on a forthcoming article in ***The Antitrust Health Care Chronicle****.*

In June 2016, the United States Department of Justice ("DOJ") and the State of North Carolina filed a complaint to prevent the Charlotte-Mecklenburg Hospital Authority (later acquired by Atrium Health ("Atrium")) from enforcing the anti-steering restrictions included in its contracts with health insurers. Soon after this complaint was filed, the Second Circuit ruled that DOJ failed to meet its burden in its case against American Express Company ("Amex"), which alleged that the anti-steering contractual provisions used by Amex in its merchant contracts were anti-competitive. Despite this ruling by the Second Circuit (and the subsequent 2018 Supreme Court ruling that Amex's anti-steering provisions did not violate the antitrust laws), DOJ and the State of North Carolina continued their suit against Atrium's anti-steering contractual provisions and argued that the Amex decision was not applicable to the issues in the Atrium case. DOJ and the State of North Carolina and Atrium settled in November 2018, announcing that Atrium would not enforce its anti-steering restrictions except in highly limited circumstances. This settlement was upheld in April 2019.

> *"This suggests that antitrust regulators may continue to question the legality of anti-steering restrictions in healthcare settings."*

Atrium operated ten general acute-care hospitals in the Charlotte, North Carolina area at the time of the complaint. DOJ and the State of North Carolina alleged that Atrium was the dominant hospital system in Charlotte, with a market share of approximately fifty percent in the alleged relevant market. DOJ and the State of North Carolina further alleged that Atrium used its market power to prevent insurance companies from steering patients away from Atrium to more efficient healthcare providers.

Steering occurs when a health insurer uses economic incentives to influence a consumer to choose lower-cost or higher-quality healthcare options. There are several methods by which an insurer can steer a patient to choose more efficient care, including tiered networks, narrow networks, and providing enrollees with cost and quality information. DOJ and the State of North Carolina alleged that Atrium imposed contractual restrictions that limited an insurer's ability to steer patients using tiered networks, narrow networks, and price information.

Specifically, DOJ and the State of North Carolina alleged that Atrium constituted such a large part of the relevant market that insurers selling health insurance plans in the Charlotte area had to include Atrium providers in their networks in order to have a commercially viable product, and this dominance gave Atrium the ability to impose anti-steering restrictions in its contracts with insurers. DOJ and the State of North Carolina further alleged that the anti-steering restrictions had several effects, including higher prices charged by Atrium, reduced incentives for Atrium's competitors to lower their prices, and decreased consumer shopping and choice.

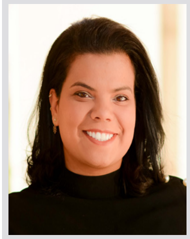
In response, Atrium argued that it was not a dominant healthcare provider and that Atrium's inclusion in a provider network was not necessary for a viable insurance product, as evidenced by United HealthCare allowing their agreement with Atrium to lapse. Atrium further argued that the DOJ and the State of North Carolina failed to assert that Atrium's alleged premium prices were the result of its anti-steering provisions, rather than Atrium's ability to offer a premium product. Finally, Atrium argued that, to the extent that it included anti-steering provisions in its contracts, these provisions were pro-competitive and led to deeper insurer discounts. For example, the anti-steering provisions mitigated the risk that, after a contract has been executed, an insurer could steer enough patient volume away from Atrium that it would cause Atrium significant financial harm.

Several months after DOJ and the State of North Carolina filed their Complaint against Atrium, the Second Circuit ruled in the Amex case – the only other case in which DOJ had challenged anti-steering restrictions. The Second Circuit ruled that the District Court in the Amex case had defined the product market too narrowly by focusing on network services to merchants and neglecting cardholders. Additionally, the Second Circuit indicated that DOJ did not offer evidence that cardholders engaged in fewer credit card transactions, or cardholder services were lower, or that

continued on page 4

Antitrust Analysis with Upward Pricing Pressure and Cost Efficiencies

Jéssica Dutra



Senior Economist Jéssica Dutra has consulted on a wide range of industries, including health care and electric power. This article is based on a paper of the same name, co-authored with Tarun Sabarwal, published in PLOS ONE in January 2020.

Upward Pricing Pressure ("UPP") is a tool that antitrust enforcers have used to estimate the potential price impact of mergers in markets with differentiated products. Additionally, antitrust enforcers are using UPP as an initial screen to estimate whether a merger may be likely to harm competition in a relevant market. For example, the Federal Trade Commission ("FTC") estimated a gross upward pricing pressure index ("GUPPI") for different local geographic areas in its review of the proposed Dollar Tree/Family Dollar merger and used these GUPPI scores as an initial screen for determining whether the proposed merger would likely harm competition in a specific geographic area. However, UPP computations do not directly predict post-merger prices or provide an estimate of accuracy of price prediction. Further, the standard application of UPP does not include cost efficiencies from a proposed merger. We extend the standard UPP formulation to include merger-specific cost efficiencies and find that the inclusion of these merger-specific cost efficiencies may yield substantial improvements in accuracy of UPP, both as a price predictor and as a merger screening tool in antitrust analysis.

UPP does not claim to provide the exact amount that the merged firm will raise prices in post-merger equilibrium. Rather, UPP provides a measure of the initial incentive to raise prices, holding fixed other economic environment parameters, such as price and level of output of other firms, demand determinants, and so on. Thus, once the market re-equilibrates to a new post-merger equilibrium, the actual change in prices may be different from the initial incentive to raise prices.

> *"We find that the modified UPP formulations ... have lower median post-merger price predictions."*

Cost efficiencies often are a motivation for mergers. The FTC and Department of Justice ("DOJ") *Horizontal Merger Guidelines* ("*Guidelines*") state that "[i]n a unilateral effects context, incremental cost reductions may reduce or reverse any increases in the merged firm's incentive to elevate price." These claimed cost efficiencies must be merger specific and verifiable for the FTC and DOJ to include them in their analyses. Thus, at least in principle, merger-specific efficiencies should be incorporated into post-merger price predictions relating to unilateral effects.

In a recent paper, Tarun Sabarwal and I model a modified UPP formulation that includes merger-specific cost efficiencies in various functional forms. We use the theoretical framework of Sonia Jaffe and E. Glen Weyl ("The First-Order Approach to Merger Analysis," *American Economic Journal: Microeconomics*, November 2013). In our model, cost efficiencies are made merger-specific by requiring them to be zero if output of either firm in the merger is zero. In other words, cost efficiencies are activated only for the merged firm and only when outputs of both merging firms are positive. To analyze the efficacy of this modified UPP formulation vis-à-vis more widely used versions, we use Monte Carlo simulation. For the demand side, we use four standard functional forms that have been widely used in merger analyses. These are Logit demand, Log-Linear demand, Linear demand, and Almost Ideal demand. We also use two different cost formulations for a total of eight different scenarios. For each scenario we estimate 5,000 mergers for a total of 40,000 mergers simulations. We find that with the inclusion of merger-specific cost efficiencies, as well as a more accurate first-order approximation to compute UPP, there are substantial gains in prediction of post-merger equilibrium prices.

The merger simulations also reveal that different measures of UPP yield different post-merger price predictions. We find that the modified UPP formulations (which include cost efficiencies) have lower median post-merger price predictions. For example, the UPP formulation incorporating merger-specific efficiencies and pass-through results in a median post-merger price increase of 1.2 percent compared to a median post-merger price increase of 10.7 percent for the UPP with no merger-specific efficiencies or pass-through. The distribution of these post-merger price predictions also varies considerably based on the measure of UPP – eighty percent of the post-merger predicted prices for the UPP formulation incorporating merger-specific efficiencies and pass-through are between -61.9 percent and 25.3 percent

continued on page 4

DOJ's Challenge of Atrium Health

Amex's pricing was set above competitive levels. Thus, the Second Circuit ruled that DOJ had failed to meet its burden and that Amex's anti-steering provisions did not violate antitrust laws.

Following the Second Circuit opinion, Atrium argued that the same flaws in DOJ's legal argument in the Amex case held in the current matter. In response, DOJ and the State of North Carolina claimed that the Amex decision was decided "on grounds that are entirely distinct from the issues in this case." Notably, DOJ and the State of North Carolina argued that the Amex case was decided based on a differing view of how to define the relevant market in a two-sided platform, which was not an issue in the Atrium proceedings.

In March 2017, the District Court denied Atrium's motion for a judgment on the pleadings. The District Court noted that the government met its burden. The District Court found that the government alleged higher prices resulted from Atrium's anti-steering restrictions, and that "these allegations are specifically the type of allegation that states a direct anticompetitive effect and a plausible claim for relief under Section 1 of the Sherman Act." Additionally, the District Court noted the government's indirect evidence – including Atrium's alleged high market share, the alleged necessity of including Atrium in a provider network for a viable insurance product, and the allegation that insurers would prefer to not have anti-steering restrictions in their contracts.

DOJ and the State of North Carolina ultimately reached a settlement with Atrium. This settlement broadly nullified existing contractual anti-steering restrictions between Atrium and health insurers and placed limitations on future contractual arrangements between Atrium and insurers. Prior to this case, DOJ had not challenged anti-steering restrictions in a healthcare setting. Further, DOJ and the State of North Carolina continued their challenge despite the Second Circuit's ruling in the Amex case. This suggests that antitrust regulators may continue to question the legality of anti-steering restrictions in healthcare settings.

Upward Pricing Pressure and Cost Efficiencies

while eighty percent of the post-merger predicted prices for the UPP with no merger-specific efficiencies or pass-through are between 2.1 percent and 27.5 percent.

We also use our simulation data to investigate the accuracy of different UPP formulations as pre-merger screening tools. UPP is being used increasingly as a pre-merger screening tool by antitrust agencies both in the United States and worldwide, mainly because it is relatively quick and easy to implement, requires less information than some other measures, and is grounded in economic theory. The typical use of UPP is to flag a merger for further scrutiny if the UPP calculation is above a given threshold, such as five percent. As UPP is not a perfect predictor of post-merger prices, this can lead to false positives and false negatives. We find that the probability of making a merger screening error decreases substantially when UPP formulations that include cost efficiencies are considered compared to UPP formulations that do not include cost efficiencies. For example, we find that the total probability of making a merger screening error decreases 96 percent when using the UPP formulation incorporating merger-specific efficiencies and pass-through compared to UPP formulations with no merger-specific efficiencies or pass-through.

In sum, we find that the modified UPP formulations including merger-specific cost efficiencies yield substantial gains in post-merger price prediction and merger screening accuracy. These results show that including cost efficiencies in a manner guided by the theoretical model may yield substantial improvements in accuracy of UPP as a tool in antitrust analysis.

EI News and Notes

Defense Verdict in Multi-Billion Dollar Antitrust Jury Trial

A jury in the United States District Court for the Eastern District of Pennsylvania reached a defense verdict regarding allegations that egg producers conspired to elevate egg prices by restricting supply. The plaintiffs were twelve of the nation's largest grocers including Kroger, Safeway, Publix and Supervalu. These grocers had opted out of an earlier class action which the egg producers also won. The opt-out plaintiffs had sought approximately $1 billion in damages before trebling while the class plaintiffs sought approximately $3 billion before trebling. EI President Jonathan L. Walker was the defendants' expert liability witness in both the opt-out and earlier class action proceedings.

Two Recent FERC Decisions

The Federal Energy Regulatory Commission ("FERC") recently approved Entergy Mississippi's proposed purchase of the Choctaw Generating Station. EI Principal John R. Morris testified that the Commission's default geographic market of MISO South was too small and that market concentration was low in the proper geographic market. Steptoe & Johnson LLP represented Entergy Mississippi before FERC.

FERC also recently affirmed its decision to remove horizontal market power mitigation conditions stemming from Louisiana Gas & Electric's merger with Kentucky Utilities in 1998. EI Principal John R. Morris provided affidavits demonstrating that the mitigation was no longer necessary because the affected customers have many good alternatives to receiving supplies from the utilities. Troutman Sanders LLP represented LG&E/KU.

Jéssica Dutra Presents at the Kansas Law Review Symposium

EI Senior Economist Jéssica Dutra presented *Paradigm Shifts on Merger Efficiencies in Antitrust Analysis* at the Kansas Law Review Symposium, themed "Antitrust Law and Policy in the 21st Century." Dr. Dutra also presented her paper *Common Ownership of Hospitals and the Price of Medical Care*, coauthored by José Azar, Donna Ginther, and David Slusky, at the Association for Public Policy Analysis and Management Conference and her paper *Antitrust Analysis with Upward Pricing Pressure and Cost Efficiencies*, a joint work with Tarun Sabarwal, at the Southern Economic Association conference in Fort Lauderdale.

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