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DOJ Sues Hospitals for Allocating Marketing

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The US Department of Justice (DOJ), joined by the State of Michigan, recently filed suit against four Michigan hospital systems for allegedly limiting competition by agreeing to allocate geographic territories for marketing efforts. Three of the four systems have reached settlements that will bar them from similar agreements and from communicating about their marketing efforts for five years. The fourth, W.A. Foote Memorial Hospital, doing business as Allegiance Health (Allegiance), continues to litigate the charges.

The four defendants own general acute care hospitals located in adjacent counties in south-central Michigan. Each defendant operates the only hospital or hospitals in its county and competes directly with the other defendants to provide the same hospital and physician services. Marketing is an important means of informing patients, physicians, and employers about the quality and range of a hospital's services, which are important factors in consumers' healthcare choices. Defendants' marketing efforts include advertising, free health screenings, physician seminars and health fairs for consumers, educational and relationship-building meetings with physicians and, in Allegiance's case, informational meetings with employers.

Economists view marketing efforts by competitors as strategic complements, meaning that a competitor will respond to a rival's increased marketing efforts by increasing its own marketing activities. A market with robust competition should include efforts by all competitors to sell their services. Nonetheless, marketing activities are costly. Moreover, they may reduce prices by making potential buyers better able to compare suppliers' prices and services. Thus, firms have incentives to jointly raise their profits by agreeing to reduce competition in marketing.

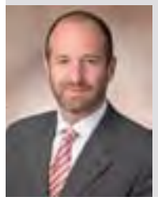
One means of reducing competition may be to allocate geographic areas for marketing efforts, as DOJ accuses the defendants of doing. DOJ alleges that the defendants had long-standing agreements to restrict marketing activities in each other's counties and actively controlled compliance with the agreements. For example, according to DOJ, Allegiance did not market oncology services in Hillsdale County and restricted its physicians from providing free seminars in that county. DOJ also cites several instances when the agreements were violated, complaints ensued, and the infringing efforts were withdrawn. According to DOJ, the defendants' actions deprived consumers, physicians, and employers of important information affecting their choice of healthcare providers and also deprived consumers of free health screenings and education.

DOJ argues that the allocation of marketing areas is a per se antitrust violation under Section 1 of the Sherman Act. Thus, the agreement allegedly is a naked restraint of trade that does not require analysis to show its anticompetitive effects on consumers or to weigh those effects against procompetitive justifications. Allegiance has yet to indicate its defense to the charges.

Also In This Issue

Analyzing *High-Tech Employee*: The Do's and Dont's of Proving (and Disproving) Class Wide Antitrust Impact in Wage Suppression Cases

Kevin W. Caves and Hal J.Singer



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In re High-Tech Employee is a high-profile class action alleging that top executives at some of Silicon Valley's most prominent companies, including Apple, Google, Intel, and Adobe, conspired to restrict recruiting and hiring of high-tech workers as a mechanism for suppressing compensation. The court certified a class consisting of approximately 60,000 technical, creative, and research and development employees. A settlement of approximately $415 million was recently approved by the court.

The class action followed on the heels of a Department of Justice (DOJ) investigation in which DOJ concluded that the defendants had entered into a web of bilateral agreements prohibiting "cold calling," which "disrupted the competitive market forces for employee talent" and "substantially diminished competition to the detriment of the affected employees who were likely deprived of competitively important information and access to better job opportunities." Although the DOJ investigation culminated in a settlement barring defendants from interfering with solicitation, cold calling, and other recruiting tactics for a period of five years, no provisions were made for monetary damages.

> "When the plaintiffs' experts use econometric tools to prove impact, the defendants' experts should reply in kind."

The record in *High Tech Employee* provides an in-depth analysis of several topics relevant to economic analysis in class certification settings. An examination of the district court's findings, along with the evidence proffered by experts for both plaintiffs and the defense, offers useful insights into some of the "do's and don'ts" of proving (and disproving) classwide impact in both wage suppression cases in particular and antitrust class actions more generally.

The DOJ investigation revealed substantial documentary evidence, as well as evidence of direct communications among the defendants. For example, Apple and Google allegedly maintained internal "Do Not Call Lists" containing the names of rival companies whose employees could not be solicited. When Apple complained to Google that the agreement had been violated, Google allegedly responded with an internal investigation and subsequently reported the results to Apple. In another exchange, Apple CEO Steve Jobs allegedly warned Google founder Sergey Brin in 2005 that "[i]f you hire a single one of these people, that means war."

The plaintiffs' expert adopted a two-step methodology to demonstrating classwide impact. The first step required the expert to identify a plausible economic theory, along with corroborating evidence, connecting the challenged conduct to a generalized anticompetitive effect (in this case, general wage suppression). In the second step, the expert must demonstrate the existence of a plausible mechanism (such as a rigid compensation structure) that would transmit these anticompetitive effects to all or a large share of the proposed class. The court stated that the plaintiffs' expert "followed a roadmap widely accepted in antitrust class actions that use evidence of general price effects plus evidence of a price structure to conclude that common evidence is capable of showing widespread harm to the class."

Plaintiffs' expert relied primarily on econometric analyses intended to show (1) that the alleged anti-solicitation agreements suppressed wages generally by imposing an informational asymmetry that inhibited the process of price discovery; and (2) that the defendants' implicit and explicit emphasis on "internal equity"—the notion that employees doing the same work should generally receive similar compensation—created uniform and rigid compensation structures, leading to classwide impact.

In attempting to defeat class certification, the defendants and their experts relied less on quantitative analysis, focusing instead on qualitative arguments and broad methodological critiques. Defendants' first primary argument was that compensation practices did not follow a rigid structure, and instead were highly individualized with compensation levels "set by hundreds of different managers who were directed to differentiate pay and reward high achieving employees." However, the court found this claim of "diminished proba-

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Recent Performance of Medicare ACOs Does Not Indicate Universally Lower Costs or Improved Quality

Lona Fowdur and John M. Gale

Lona Fowdur is a Senior Economist with EI. She specializes in Applied Industrial Organization, and has analyzed issues involving antitrust in a wide variety of industries including healthcare and energy. EI Vice President John M. Gale also has been involved in numerous health care matters.

The Centers for Medicare and Medicaid Services (CMS) recently announced the 2014 quality and financial performance results of Medicare Accountable Care Organizations (ACOs). Although performance has improved somewhat relative to 2013, overall results remain mixed. The experience with ACOs calls into question the assumption that alternatives to more formal integration arrangements like mergers and acquisitions can generate substantial cost savings with simultaneous quality improvements.

ACOs are networks of otherwise unaffiliated providers that can obtain approval from CMS to become jointly responsible for the coordinated care of an assigned Medicare patient population. Under their agreement with CMS, ACOs are eligible to participate in the Medicare Shared Savings Program (MSSP) and to receive bonuses if they generate sufficient savings and attain certain quality levels. CMS calculates the savings relative to a benchmark based on the per capita costs of care of the ACO's assigned patient population in each of the three years preceding the ACO's formation.

The potential to reduce costs while simultaneously improving quality can be extended to commercially insured patients via joint negotiations by the ACO participants with commercial health plans. In a 2012 joint policy statement, the Federal Trade Commission and the Department of Justice (the Agencies) determined that as long as an ACO fulfills CMS's eligibility criteria and uses the same governance, leadership, and administrative processes to serve patients in commercial markets, the ACO will be permitted to conduct joint negotiations with private payers, subject to some antitrust restrictions. In particular, the statement defines an antitrust safety zone whereby an ACO is considered highly unlikely to raise significant competitive concerns when its share of jointly offered services is 30 percent or less in each participant's primary service area. The relevant services include physician specialties, major diagnostic categories for inpatient services, and outpatient categories for outpatient services. To fall within the safety zone, all hospitals and outpatient-facility participants must be non-exclusive to the ACO. For ACOs that fall outside of the safety zone, the Agencies provided some guidance, including a description of the types of behavior to avoid and the process for an expedited 90-day review whereby the Agencies would evaluate the competitive impacts of the ACO under the rule of reason.

> "The experience with ACOs calls into question the assumption that alternatives to mergers and acquisitions can generate substantial cost savings.."

The performance of ACOs under the MSSP provides little evidence so far that ACOs consistently reduce costs while improving quality. Of the 404 ACOs in the MSSP program, only 92 (23%) earned shared savings for 2014. Although an additional 89 ACOs did reduce health care costs compared to their benchmark, they did not qualify for shared savings, as they did not meet their minimum savings thresholds. Moreover, more than half of ACOs did not realize any savings. CMS also reported that among ACOs that entered the program in 2012, only 37 percent generated shared savings, while 27 percent of those that entered in 2013 and 19 percent of those that entered in 2014 earned shared savings. Thus, while the likelihood of savings increases with time in the program, the majority of even the most experienced participants failed to generate savings.

With regard to quality, ACOs that reported in both 2013 and 2014 improved on 27 of 33 quality measures. Detailed performance data that could allow a formal evaluation of the extent of the progress made are not yet available. A 2014 study evaluating performance in the first year of participation did not find a significant correlation between improved quality and earned savings. Perhaps this is because in the first year of participation, ACOs were required only to report quality metrics, not to show improvements. The same study found that if quality benchmarks were in place, of the $296.8M in earned savings distributed for the first year, CMS would have withheld $71.1M due to the failure to meet the benchmarks. Another recent study of both

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Analyzing *High-Tech Employee*

tive value" because it rested primarily on "declarations from top management in their human resources, recruitment, compensation, and benefits departments," which were "drafted for the specific purpose of opposing plaintiffs' class certification motion."

Defendants' second line of argument was that the plaintiffs' expert's analyses were rendered unreliable by methodological and statistical flaws. These critiques were ultimately unpersuasive to the district court, which found that plaintiffs had presented a common method of proof that combined an econometric showing of average wage suppression with econometric and documentary evidence that such suppression would have been widespread across rigid compensation structures. For example, defendants' economists argued that plaintiffs' regressions suffered from endogeneity bias as a result of an (unspecified) omitted variable, noting that an endogeneity problem "arises when some of the same unmeasured common factors drive both the independent and dependent variables." The court was unpersuaded, noting that defendants had failed to specify what the omitted variable might be, or how its exclusion might have altered the results of plaintiffs' analysis. Similarly, defendants' experts argued at a purely conceptual level that plaintiffs' statistical evidence did not constitute proof of causation. The court rejected this argument as well, favorably citing plaintiffs' expert, who noted that economists "analyze correlations, which are routinely used. . . to draw causal conclusions when supported by compelling frameworks and complementary information."

In summary, the plaintiffs' success in obtaining class certification in *High Tech Employee* strongly suggests that, when the plaintiffs' experts use econometric tools to prove impact, the defendants' experts should reply in kind. Otherwise, defense experts risk forfeiting opportunities to convince the court that any apparent weaknesses in the plaintiffs' proof of impact are not just technical minutiae, but actually render plaintiffs' methods unreliable in practice. From the point of view of defendants, *High-Tech Employee* suggests that heavy reliance on abstract methodological critiques is a risky strategy, especially when the plaintiffs offer an econometrically intensive proof of impact. Had the defendants' arguments been complemented by more empirical analysis to demonstrate their relevance, they might have proven more persuasive to the court.

Recent Performance of ACOs

Medicare and commercial ACOs found that as of the end of 2014, less than half of the ACOs had implemented the care management and care coordination activities that were being monitored, suggesting that quality improvements were still inchoate.

CMS programs that allow participants to earn a higher level of savings by taking on more risk have had only limited success. Along with the MSSP, CMS created the Pioneer program for ACOs willing to share downside risk as an initiative designed to test the effectiveness of a higher risk-reward payment model. In the first year, only 13 of the 32 Pioneer ACOs achieved shared savings. By the end of 2014, only 20 Pioneer ACOs remained in the program and only 11 of those earned shared savings while three owed losses.

Based on CMS's initial rules, participants on Track 1 of the MSSP (with shared-savings potential, but no downside risk) would have been required to switch to Track 2 (with downside risk for realized losses) after three years of participation on Track 1. Those rules were changed earlier this year. Participants may now either remain on Track 1 or pick among several new Track 2 options that can be tailored to the risk tolerance of individual participants. CMS indicated that without the rule change, an estimated 85 percent of participants would opt out of the MSSP program. So far, only three ACOs have switched to Track 2. Since assuming more risk can increase ACOs' share of the savings they achieve, this reluctance to assume risk suggests that most participants are not optimistic about the potential for reducing costs.

The number of beneficiaries assigned to Medicare ACOs is an indicator that the ACO framework so far has only attracted a limited number of provider groups. A 2015 CMS fact sheet reports that only 7.3 million Medicare beneficiaries, approximately 15 percent of the Medicare population, are currently assigned to an ACO in the MSSP program. If ACOs can indeed lower costs and simultaneously improve quality, more providers could be expected to form such alliances or be driven out of the market.

Earlier this year, the Ninth Circuit upheld the Federal Trade Commission (FTC) challenge to an Idaho hospital's acquisition of a physician group based on the FTC's view that the claimed procompetitive efficiencies from the proposed acquisition could have been achieved without a full merger. At a workshop examining healthcare competition that the Agencies jointly hosted in February of this year, FTC Chairwoman Edith Ramirez reiterated this view and referred to ACOs as an alternative to mergers that could potentially lower healthcare costs and improve quality. Based on the mixed performance of ACOs so far, it is unclear how successful this framework will be at delivering these desired outcomes.

EI News and Notes

Study of Payment Card Benefits

EI Principal Philip B. Nelson, working with Vice President John M. Gale, Vice President Gale Mosteller, and Principal Stephen E. Siwek, released a new study, "Retailer Payment Systems: Relative Merits of Cash and Payment Cards." The study analyzes the economic costs and benefits of cash relative to payment cards. It finds that retailers that adopt a cash-only strategy have less revenue, both because they make fewer sales and because those sales are of smaller dollar value. Moreover, merchants incur significant costs associated with handling cash.

Testimony in Employment Discrimination Case

EI Vice President Michael DuMond testified at trial in the matter of *Victor Guerrero vs. California Department of Corrections and Rehabilitation* in the Northern District of California. At issue was whether the Department's background investigation procedure, which inquired whether job applicants had ever used a different Social Security Number, harmed the employment of Latino correctional officers. Dr. DuMond was retained by the State of California's Department of Justice. Assisting him in this matter were Vice Presidents Eric Mitchem, Benjamin Shippen, and Wayne Strayer.

Testimony on Class Certification and Monopolization

Dr. William Myslinski, one of EI's founders, testified in federal court three times this spring. He twice testified in class certification hearings for *In Re: Processed Egg Products Antitrust Litigation.* In denying class certification for the consumer class of indirect purchasers and the subclass of direct purchasers of egg products, the court repeatedly cited Dr. Myslinski's testimony. (A class of direct purchasers of shell eggs was certified.) Dr. Myslinski testified on behalf of defendant egg producers and egg processors, who were represented by the law firms of Weil, Gotshal & Manges; Porter Wright; Dechert; Keating, Muething & Klekamp; Buchanan, Ingersoll & Rooney; Proskauer Rose; Pepper Hamilton; Faegre, Baker, Daniels; and Kasovitz, Benson, Torres and Friedman. Dr. Myslinski also testified in *Major Mart, Inc. v. Mitchell Distributing, Inc. and Mitchell Beverage, LLC*. Mitchell, an Anheuser-Busch distributor with a 75% market share, was accused of monopolizing and attempting to monopolize beer distribution and tortious interference with business relationships. Dr. Myslinski testified on behalf of Mitchell, which was represented by Bradley Arant Boult Cummings LLP. The jury found for Mitchell on all counts.

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