FTC Wins Appeal in Pennsylvania Hospital Merger Case

On Tuesday, the FTC won its appeal in the Third Circuit, and obtained a preliminary injunction temporarily blocking the merger of the two largest hospital systems in the Harrisburg, Pennsylvania, area. The FTC sued to block the merger of Penn State Hershey Medical Center and Pinnacle Health System in December, but in May a district court judge denied the FTC's motion for a preliminary injunction.

Source Advisory Board member Thomas L. Greaney discussed the case in an earlier blog post, which highlighted the challenges posed by a recent string of losses for federal regulators overseeing hospital consolidations. The Third Circuit decision turns that trend around.

The key question in the Third Circuit appeal was whether the FTC had adequately defined the relevant geographic market. In a merger case, the relevant geographic market is the geographic area in which an individual may reasonably be expected to look for goods and services. The government must properly define the geographic market in order for the court to determine whether a merger would be anticompetitive. The district court decision concluded that the geographic market defined by the FTC – four counties making up the Harrisburg area – was insufficient under the hypothetical monopolist test, which the parties agreed controlled.

In its 3-0 decision, the Third Circuit found that the government had properly defined the geographic market, and that the district court had inappropriately applied the hypothetical monopolist test. The Third Circuit argued that the district court used half of the Elizinga-Hogarty test

rendering its decision "economically unsound and not reflective of the commercial reality of the healthcare market." In the last several years, use of Elizinga-Hogarty analysis, which is commonly applied to determine geographic markets in non-healthcare related contexts, has been "discredited", with even one of the economists after whom this theory is named declaring that it should not be used to define geographic markets for hospitals.

The Third Circuit also objected to how the district court focused solely on the effect of potential price increases on patients, without considering the effect on insurers. "Patients, in large part, do not feel the impact of prices increases. Insurers do," the court wrote. The unanimous opinion reasoned that insurers, would have no choice but to accept price increases because plans without the two merging hospitals would be unmarketable.

The decision is particularly significant because a similar appeal is currently pending in the Seventh Circuit. There, the FTC challenged the proposed merger of two Chicago hospital systems, Advocate Health Care and NorthShore University HealthSystem. As in the Third Circuit case, the district court in the Seventh Circuit case denied a preliminary injunction on the basis that the FTC improperly defined the geographic market. Check back in with us to see whether the Seventh Circuit follows the Third Circuits' emphasis on commercial realities in healthcare markets.