

# **[Case Watch] UCFW & Employers Benefit Trust v. Sutter Health: A Look at the Alleged Anticompetitive Contract Terms in the Legal Action Against Sutter**

The lawsuit alleging anticompetitive conduct by Sutter Health is scheduled to begin trial on October 7, 2019 in the Superior Court of San Francisco. In the case, California Attorney General and private parties United Food and Commercial Workers union (UFCW) and Employers Benefit Trust (UEBT) allege that Sutter Health used its position as a dominant provider of hospital services in Northern California to demand anticompetitive contract terms from insurance carriers.[1]<sup>[2]</sup> Since the factual allegations and legal claims made in both the AG and private complaints are similar, the court consolidated the cases in May 2018.[3] In this post, we review both complaints and discuss how Sutter allegedly used anticompetitive contract terms to maintain its dominant market share and charge supra-competitive prices for healthcare services in Northern California.

## **Sutter's Alleged Use of Anticompetitive Contract Terms to Exploit Market Dominance**

Sutter Health is the largest provider of general acute hospital services in Northern California. The size and reputation of the Sutter system ensure that insurance plans that include the Sutter system often appeal more to patients and employers choosing insurance coverage than narrow networks that exclude Sutter. According to the California Attorney General (AG)'s complaint, in 2016, Sutter had 193,161 hospital discharges, 873,992 emergency room visits, and 8,763,470 outpatient visits at its 24 hospitals.[4] Furthermore, the complaints assert that many of the Sutter facilities are "must-have" hospitals, such that insurance carriers are unable to create

commercially viable provider networks without including these must-have Sutter hospitals. In particular, plans serving large numbers of people must include Sutter hospitals in Tracy, Vallejo, Auburn, Crescent City, Lakeport, and Los Banos, as they are the only facilities with sufficient capacity in their geographic markets to serve the population,[5] and plans must include Sutter hospitals in Crescent City, Lakeport, and Los Banos to satisfy the network adequacy requirements of California's Knox-Keene Act in those areas.[6] As a result, the UEBT complaint asserts that every commercially viable provider network in Northern California must contain at least some Sutter hospitals.[7]

The plaintiffs further allege that Sutter leveraged its market dominance in some geographic areas to demand contract terms with insurance carriers that significantly reduced competition and allowed Sutter to charge supra-competitive prices across Northern California. Specifically, the complaints allege Sutter demanded three categories of contract terms in nearly all of its written and oral contracts:[8]

- **All-or-nothing contract provisions:** if any hospital is included in a provider network, then *all* facilities in that health system must be included in the provider network;
- **Anti-incentive (including anti-tiering or anti-steering) contract provisions:** prohibit insurance carriers from giving incentives to patients to utilize cheaper or higher value healthcare facilities (steering) or from placing a system hospital in anything other than the most favorable cost-sharing tier (tiering); and
- **Gag-clause provisions:** prohibit disclosing prices for healthcare services to a plan sponsor or patient before the service is utilized and billed.

Since Sutter has "must-have" hospitals in a few geographic areas and allegedly demanded all-or-nothing clauses in its contracts, any insurance carrier seeking to sell coverage with enrollees in these areas of Northern California must include all Sutter facilities, even the ones in more competitive markets. Furthermore, Sutter allegedly demanded anti-tiering and anti-steering provisions to prevent insurers from encouraging the use of other lower cost facilities. Finally, the gag-clause

provisions Sutter allegedly demanded would ensure that no one - not even the employers ultimately paying for the services - would know the price of these services before they are billed.

## **Legal Discussion: What are the Legal Claims Arising from these Contract Terms**

Both complaints allege Sutter's use of these contract terms violates the Cartwright Act, the primary antitrust law in California. The Cartwright Act mirrors the federal antitrust statutes, the Sherman and Clayton Acts, and the laws "are to be interpreted in harmony with one another." [9] The Sherman Act broadly prohibits "every contract, combination, ... or conspiracy in restraint of trade", [10] which the Supreme Court has refined to include price fixing, market allocation, exclusive dealing group, boycotts, price discrimination, and tying arrangements in which a firm with market power sells a product on the condition that the buyer purchase a second, tied product. Furthermore, Section 2 of the Sherman Act prohibits monopolization or intent to monopolize. [11] In contrast to the federal statutes, the Cartwright Act expressly prohibits any agreements among competitors to restrain trade, fix prices or production, or reduce competition. [12]

While the state AG has the authority to sue for violations of both the federal and state statutes, the complaints filed by the UEBT and California AG only allege violations of the Cartwright Act and California's Unfair Competition Laws. **Count 1** of both complaints alleges that Sutter's contract terms amount to price fixing for two reasons. First, the contract terms interfere with signals of price and quality, thereby preventing other providers from competing with Sutter by offering a lower price for an increased volume of patients. Second, the California AG argues that Sutter's contract terms prevent competitors from offering a narrow network, with only "must have" Sutter facilities, so customers face a reduction in products they can choose to purchase.

**Count 2** of the complaints alleges that the contract terms that allow Sutter to leverage market power in a few geographic areas amount to unreasonable restraint of trade. The UEBT complaint argues "[Sutter's] All-or-nothing, Anti-incentive and

Price Secrecy Terms...ensure not only that all Sutter hospitals will be included in nearly every Provider Network, but also that Health Plan Enrollees will actually tend to use higher-priced Sutter hospitals because they have no economic incentive to choose a more cost-effective competing hospital instead... [Therefore,] Network Vendors foreclose millions of dollars of commerce that would otherwise go to lower-priced hospital competitors at substantial savings to members of the plaintiff Class... The anticompetitive effects of Sutter's conduct far outweigh any purported...pro-competitive justifications.”[13]

In **Count 3**, both the UBET and the California AG allege that Sutter unlawfully restrained trade with the purpose of obtaining and maintaining monopoly power and that power allowed Sutter to demand supra-competitive prices. Finally, in **Count 4**, the UBET alleges that Sutter's actions are acts of unfair competition and that they have suffered injury as a result of those actions by paying inflated prices for hospital services. Under count 4, the UBET seeks equitable restitution and disgorgement of the monetary gains that Sutter obtained from unfair competition.

Similar claims were seen in the [antitrust action against Atrium Health](#) in North Carolina, where the Department of Justice (DOJ) and the North Carolina AG alleged Atrium's use of anti-incentive contract terms violated Section 1 of the Sherman Act. The [case settled](#) when Atrium agreed not to use anti-incentive provisions in any contract and to provide the DOJ and the state of North Carolina with a copy of each contract and each amendment to a contract for healthcare services in the Charlotte Area. Sutter disputes all counts of antitrust claims in its case heading into trial. The Source will closely follow the court proceedings, which is currently undergoing jury selection, and bring the latest developments and legal analysis on the Source Blog.

### **Economic Discussion: Why these Contract Provisions May Be Anticompetitive and Raise Prices**

As the legal arguments unfold in court, we take a look at how the use of these terms could amount to anticompetitive conduct, especially when used collectively. Narrow provider networks give insurance carriers greater leverage to negotiate lower payment rates or to steer patients to providers that provide high quality services at

lower prices. Specifically, since enrollees in these narrow networks face high costs if they go out of network, providers are often willing to negotiate lower reimbursement rates in return for greater patient volume. Dominant providers, however, can demand restrictive contract terms that inhibit insurance carriers from creating the most cost-effective networks. From the insurance carrier's perspective, they are content to play along as long as they know that all of their competitors receive equivalent or less-favorable terms, so they are unlikely to lose business, as all insurers can pass on the increased cost to employers and consumers as increased premiums.

In Sutter's case, the **all-or-nothing provisions** allegedly used in their contracts coupled with the must-have status of some Sutter facilities prevent insurers from constructing networks that exclude Sutter hospitals, even in geographic areas where it would be economically feasible to construct networks with high-quality, lower-priced alternative facilities. Furthermore, insurance plans with narrow networks offered only in areas with sufficient competition are unlikely to appeal to the majority of patients and employers.

Theoretically, insurers could then use tiered networks to maintain a broad network of providers and give patients a financial incentive to choose more cost-effective providers. In a method similar to tiered drug formularies, insurers using a tiered network will place high-quality, lower-cost providers on a tier of the network with minimal co-payments or cost-sharing. Higher-priced healthcare providers are then placed on a less-favorable tier, so while patients are still able get insurance coverage when seeing those providers, they also face higher out-of-pocket costs. When allowing the merger of Sutter's Alta Bates Medical Center and Summit Medical Center, the district court held that "there are numerous mechanisms through which health plans can discipline hospitals... The primary mechanism by which [plans]... keep prices low is through the 'steering' of patients." [14]

Sutter's use of **anti-incentive contract terms** could prevent an insurer from offering any financial or other incentives to patients to use lower-cost alternatives to Sutter facilities. This inability to steer patients also disincentivizes non-Sutter providers from offering discounted rates to an insurer because they would not receive an increase in number of patients due to the decrease in price. Specifically,

the anti-incentive terms Sutter allegedly demanded make it futile for any competitor to compete on price and quality. No matter how much better or cheaper another provider might be, patients will have the same out-of-pocket costs, and insurers have no way to encourage patients to utilize higher value providers.

Finally, the **gag-clause contract provisions** ensure that prices (and price differences between providers) are concealed from everyone, including self-funded payers who ultimately pay for the services. As a result, employers are unable to publish lists of providers with lower reimbursement rates that employees could use to reduce costs for the employer. The California AG alleges that the combination of these three types of contract provisions - all-or-nothing, anti-incentive, and gag-clause provisions - allow Sutter to “insulate itself from the price competition that otherwise would be present in an unfettered free market.”[15]

## **Conclusion**

The case against Sutter Health is one of the most closely watched cases in healthcare. Along with Atrium, these cases may reflect increasing oversight by regulatory authorities of the actions of dominant providers. Furthermore, the [Lower Health Care Costs bill](#), currently being considered in Congress, would ban the use of these and other typically anticompetitive contract terms in contracts between insurance carriers and healthcare providers. The Source will continue to provide detailed coverage and analysis of the Sutter case and legislative actions to prevent the anticompetitive use of contract terms.

---

[1]UBET Complaint, UFCW & Employers Benefit Trust, et al. v. Sutter Health, et al., No. CGC 14-538451 (Cal. Super. Ct. S.F. City and Cnty. 2019) [hereinafter UBET Complaint].

[2]Becerra Complaint, People of the State of California ex rel Xavier Becerra v. Sutter Health., CGC 18-565398 (Cal. Super. Ct. S.F. City and Cnty. 2019)

[hereinafter Becerra Complaint].

[3]Order to Consolidate, UFCW & Employers Benefit Trust, et al. v. Sutter Health, et al., No. CGC 14-538451 (Cal. Super. Ct. S.F. City and Cnty. 2019).

[4]Becerra Complaint,*supra* note 2, at 53.

[5]UBET Complaint, *supra* note 1, at 80.

[6]UBET Complaint,*supra* note 1, at 80 citing network adequacy laws in Cal. Health and Safety Code § 1340 *et seq.* and Cal. Code of Reg. §1300.51(H)(ii).

[7]UBET Complaint,*supra* note 1, at 91.

[8]UBET Complaint,*supra* note 1, at 20 and Becerra Complaint, *supra* note 2, at 35.

[9]Davis v. Pac. Bell, 204 F. Supp. 2d 1236, 1243 (N.D. Cal. 2002), rev'd on reconsideration, No. C 01-0260 SI, 2002 WL 35451316 (N.D. Cal. Oct. 2, 2002).

[10]15 U.S.C. §1.

[11]15 U.S.C. §2.

[12]Cal. Bus. & Prof. Code §16720.

[13]UEBT Complaint, *supra* note 1, at 151-152.

[14]California v. Sutter Health Sys., 130 F. Supp. 2d 1109, 1130 (N.D. Cal. 2001) at 1130.

[15]Becerra Complaint, *supra* note 2, at 37.