[Case Watch] UCFW & Employers Benefit Trust v. Sutter Health: Court Sets Antitrust Standards, Readying the Stage for Trial

Editor's Note: As the historic antitrust lawsuit against healthcare giant Sutter Health heads to trial, The Source will feature a series of legal analyses, including revisiting the complaints and summary judgment order, to bring readers up to speed in this one of a kind case. The trial is set for September and expected to last around 12 weeks. Continue to follow The Source Blog as we bring the latest first-hand coverage and analysis in this case.

On August 6, the California superior court heard arguments on which antitrust analysis should be used for each count of the complaints in the state and private consolidated action against Sutter Health ("Sutter"). The Source reviewed the briefs regarding the antitrust standards and attended the hearing.

This pretrial hearing is important, because antitrust standards determine the plaintiffs' level of burden in proving that Sutter's conduct is anticompetitive. In this post, we examine antitrust analysis under California's Cartwright Act, break down both sides of the arguments as they apply to each of the counts, and review the court's final ruling issued on August 12 and its implications.

Antitrust 101 – What Are Antitrust Standards?

While federal antitrust cases cite to the Sherman Act and the Clayton Act, California state court antitrust cases cite to the Cartwright Act.[1] The Cartwright Act, as California's primary antitrust law, declares as "unlawful, against public policy and void"[2] any "combination of capital, skill or acts by two or more persons" to "create

or carry out restrictions in trade or commerce" as specified.[3]

In evaluating whether a conduct violates the Cartwright Act, the courts developed two approaches to evaluate the potential restraint of trade: *per se* and *rule of reason*. Before proceeding into the weeds here, note that not all restraints of trade violate the Cartwright Act. As the California Supreme Court observed, "only unreasonable restraints of trade are prohibited."[4]

Per Se vs. Rule of Reason

Traditional "rule of reason" analysis requires the plaintiff to prove both that the conduct was anticompetitive and that the anticompetitive effects outweighed any procompetitive effects of the conduct, which often requires an intensive analysis on how the conduct promotes or suppresses competition.[5] Such an analysis would typically include "expert testimony on such matters as the definition of the relevant market and the extent of a defendant's market power."[6] While Sutter, in its brief, argues that "rule of reason" is the "presumptive standard in antitrust cases,"[7] the California Supreme Court observed that "a rule of reason inquiry is not required in every case."[8]

"Per se" analysis, on the other hand, fast tracks the "rule of reason" analysis by "identifying categories of agreements or practices that can be said to always" be anticompetitive.[9] The California Supreme Court noted that the "per se rule reflects an *irrebuttable*presumption that . . . a violation would be found under the traditional rule of reason."[10] As a result, the court would presume the defendant's conduct is anticompetitive and require no further inquiry on the conduct's effect or intention. Sutter, in its brief, argues that the "per se" analysis should only be used when "no elaborate study is needed to resolve" the anticompetitiveness of a conduct, which only comes from considerable judicial experience.[11]

"Structured" Rule of Reason

Recently, the California Supreme Court noted a "sliding scale" approach to antitrust analysis, creating a third approach that is essentially a "quick look rule of reason analysis."[12] In between the plaintiff-friendly *per se*and defendant-friendly *rule of reason* analysis, a court could allow an altered, or "structured," rule of reason

analysis. The California Supreme Court observed that such a structured rule of reason analysis could be used when "an observer with even a rudimentary understanding of economics could conclude that the arrangements in question would have an anticompetitive effect on customers and markets."[13] The structured rule of reason analysis would shift the burden of proof from the plaintiffs to the defendants by requiring the defendant to "come forward with procompetitive justifications without the plaintiff having to introduce elaborate market analysis first."[14] For example, in *In Re Cipro*, the California Supreme Court presumed that "the settling patentee has market power sufficient . . . to generate significant anticompetitive effects."[15] There, the court held that the "proof of a sufficiently large payment" from a brand name drug manufacturer to a generic manufacturer was a "surrogate" for market power.[16] Essentially, as Sutter summarized in its brief, this third type of antitrust analysis is a "lowered" rule of reason approach, requiring a "lesser showing of anticompetitive effects than under a full rule-of-reason analysis."[17]

Which Cartwright Act Standard Should the Court Use?

The briefs were limited, as Sutter recounts, "to whether a given claim is covered by the rule of reason or per se standard, without addressing the specific elements for each claim."[18]

Count 1 – Price tampering: Plaintiffs argued that vertical price tampering is per se illegal. They used the California Supreme Court case, *Oakland-Alameda County Builders' Exch. v. F. P. Lathrop Constr. Co.*,to support that both price fixing and price tampering are per se unlawful. As applied to Sutter, the plaintiffs argued: (1) Sutter's vertical agreements eliminated price competition between Sutter and other healthcare providers because of Sutter's all or nothing contract provisions, and (2) Sutter's anti-tiering contract provisions prevented the payor from offering more favorable price terms by reducing copays and reducing demand for Sutter's services. California further clarified at the hearing that such conduct constitutes price tampering because Sutter interfered with price signals by not revealing the true pricing of services and created "umbrella pricing," which caused smaller hospitals to

set their prices higher because Sutter doesn't show its prices. In response, Sutter countered that *Lathrop*applied only to horizontal agreements and a conspiracy among competitors and, thus, was not applicable here. The plaintiffs, however, urged the court to read *Lathrop* broadly and look at whether the conduct "restrains open price competition," not whether it is horizontal or vertical conduct.[19]

Count 2 – Tying: Plaintiffs argued that the Cartwright Act puts forth the elements of a tying claim and that previous courts held that such elements showed an illegal per se tying arrangement.[20] As such, the plaintiffs argued that tying was subject to a per se analysis. Sutter disagreed and noted that there is disagreement between the parties as to what establishes a tie. However, Sutter indicated that issue should be resolved during submission of jury instructions if the court accepted that tying is subject to a per se analysis. For the rest of the unreasonable restraint of trade claim, both sides agreed on a rule of reason analysis.

Count 3 – Combination to Monopolize: Plaintiffs argued that "Sutter's conduct can be analogized to horizontal per se illegal conduct," and as such, the plaintiffs "may meet their prima facie burden by using an appropriate surrogate for proving market power."[21] Using *In re Cipro* as their basis, the plaintiffs proposed a structured rule of reason, suggesting that prima facie burden is satisfied by (1) supracompetitive pricing or (2) a reduction in the diversity of tiered and narrow network products as a result of Sutter's conduct.[22] Either of these two conditions, the plaintiffs claim, can be an "appropriate surrogate [to] prove market power" by "making proof of Sutter's market power unnecessary and demonstrate[ing] Sutter's conduct is, in fact, analogous to horizontal per se illegal conduct."[23] Additionally, the plaintiffs claimed that the reduction in network products is analogous to a restraint on output, which are per se illegal. Sutter argued that there was no basis for adopting a lower standard of proof and pointed out at the hearing that the court in *In re Cipro*assumed a monopoly due to a patent and was not relevant to this case.

For all counts, Sutter argued that the court should use a traditional, full rule of reason standard, because "per se treatment" requires "considerable judicial experience with the kind of restraint at issue that the court can predict with confidence that the agreement would be found invalid if it were subjected to . . . the rule of reason."[24] Here, Sutter argued that (1) per se rules have only been applied

to horizontal arrangements, not "purely vertical" as it is here; and (2) there is no judicial experience to justify per se.[25] However, California argued at the hearing that while the U.S. Supreme Court is hostile to applying per se analysis to vertical restraints, as in *Ohio v. Am. Express Co.*,[26] California courts see horizontal and vertical restraints the same way under the Cartwright Act.[27]

Sutter further pointed out that it has presented "voluminous evidence, including lengthy reports of highly experienced and respected expert economists, showing that Sutter's agreements did not cause any higher pricing and, even if it did, that the agreements serve indisputably valid, procompetitive purposes."[28] Sutter argued that a "jury is entitled to consider those procompetitive benefits and whether they outweigh any higher pricing shown by plaintiffs."[29]

How Did the Court Rule?

Following the hearing, Judge Anne-Christine Massullo of the Superior Court of San Francisco County issued a ruling on August 12. The court rejected the plaintiffs' asks that a per se analysis should be used for the price tampering claim and that a structured rule of reason analysis should be used for the combination to monopolize claim, ruling that both will be subject to a full, traditional rule of reason analysis. However, the court agreed to a per se analysis for "tying" (see summary chart below).

Claim	UEBT & California AG Position	Sutter Health Position	Superior Court Ruling (Aug. 12, 2019)
1. Price Tampering	Per Se	Rule of Reason	Rule of Reason
2. Unreasonable Restraint of Trade (including "Tying")	Per Se for "Tying"	Rule of Reason	Per Se for "Tying"; Rule of Reason for rest of claim
3. Combination to Monopolize	"Structured" Rule of Reason	Rule of Reason	Rule of Reason

In the opinion, the court first clarified that "a dearth of judicial experience . . . is not a bar to per se treatment where a practice falls within an established per se category."[30]

For the first count, the court acknowledged that both "vertical and horizontal price fixing are per se violations of the Cartwright Act."[31] However, the court noted that the plaintiffs alleged price *tampering*, not price fixing, and noted that there are a limited number of cases involving price tampering. Furthermore, the court was not persuaded that all or nothing and anti-tiering contract provisions would amount to per se price tampering liability as described in the handful of relevant cases.

For the second count, the court noted that "the California authorities cited by Plaintiffs and Sutter are both to the effect that a tying arrangement is illegal per se."[32] As such, the court held that the tying claim should be tried under a per se analysis as requested by Plaintiffs. The rest of the unreasonable restraint of trade claim shall be subject to a full, traditional rule of reason analysis.

For the third count, the court did not believe that the plaintiffs "persuasively analogized their theory" and could not understand how the "Plaintiffs can argue that Sutter's prices are supracompetitive . . . without defining the scope of competition."[33] In fact, the court further believed that the evidence "that Sutter was able to charge supracompetitive prices appears to be evidence intended to show that Sutter plays enough of a role in the market to impair competition significantly."[34] Furthermore, the court did not believe that the "chain of reasoning [here] was analogous to the chain of reasoning in *Cipro*."[35] The court observed that in *Cipro*, there was extensive "economic scholarship and analysis" but "[h]ere, Plaintiffs cite nothing to support their inference that prevalence of tiered and narrow network products . . . shows that Sutter has market power in the Northern California Market."[36] The court held that the plaintiff's interferences depended on "implicit assumptions, which are presently unsubstantiated."[37] As such, the court will apply the traditional rule of reason to the third count.

Why Does the Antitrust Standard Matter?

One may assume that a pretrial hearing is not as important as the trial itself. However, this pretrial hearing is critical to how the trial will proceed. Oftentimes, as seen in this case, the parties seek to resolve the antitrust standard before trial to avoid ambiguity as to which analysis the court will apply.[38] Since antitrust laws,

including the Cartwright Act, are not clear on which analysis to use, how the court decides is "unusually important."[39] A court's ruling is additionally important in this matter because "juries have no ability to make this determination," leaving the courts to determine how much a plaintiff need to show to prove an antitrust violation.[40]

So, what does rule of reason standard mean for this case as it heads to trial? In general, a rule of reason analysis requires a significant amount of evidence, including expert testimony,[41] which will significantly increase the cost and time of litigation. Such an analysis is made all the more difficult given the incredible complexity of Sutter's contract provisions tried in this case. Unfortunately, antitrust cases are decided by "generalist judges, many of whom lack economics training" and juries, "who frequently lack any relevant training whatsoever."[42] As such, to advance how anticompetitive Sutter's contract provisions are, plaintiffs will have to do considerable work to not only persuade but also explain these difficult concepts. Such a level of complexity in contract provisions has only been seen once at the federal level as brought by the U.S. Department of Justice against Atrium Health, which ended in a settlement.

As such, the combination of complex anticompetitive provisions and higher rule of reason standard may present unique challenges for the plaintiffs. Moreover, as antitrust scholar Herbert Hovenkamp warned, "increased complexity can produce poorer rather than better outcomes" as an "open-ended rule of reason query" has an "arbitrary and indeterminate error rate."[43] To mitigate this, Hovenkamp proposes that antitrust analysis focus on "price and output effects rather than general welfare effects."[44] The court should adopt such an approach to help reduce litigation cost and time.

Although this pretrial decision will keep the bar high for UEBT and California to prove their case against Sutter, there is still a bright side to the ruling. While a full, traditional rule of reason analysis places a significant burden on the plaintiffs to prove that the effects of Sutter's anticompetitive conduct outweighs its procompetitive benefits, stakeholders watching the case shall have an opportunity to look under the hood of how the Northern California healthcare market works. This inside look may help researchers and stakeholders better understand just how

anticompetitive these contracts may be. In doing so, it could help policymakers craft legislation that better regulate the entity or conduct involved in increased healthcare pricing.

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[1]Cal. Bus. & Prof. Code, § 16700 et seq. Although some may assume that federal antitrust law preempts state antitrust laws, the U.S. Supreme Court observed that "Congress intended federal law to supplement, not displace, state antitrust remedies." *See California v. ARC Am. Corp.*, 490 U.S. 93, 102 (1989). As such, the California Supreme Court noted that "[i]nterpretations of federal antitrust law are at most instructive, not conclusive." *In re Cipro Cases I & II*, 61 Cal.4th 116, 142 (2015) (quoting *Aryeh v. Canon Business Solutions, Inc.*, 55 Cal.4th 1185, 1195 (2013). *See alsoState of California ex rel. Van de Kamp v. Texaco, Inc.*, 46 Cal.3d 1147, 1164 (1988). Furthermore, the California Supreme Court observed that the Cartwright Act was "broader in range and deeper in reach than the Sherman Act."*Cianci v. Superior Court*, 40 Cal.3d 903, 920 (1985).

[2]Cal. Bus. & Prof. Code § 16726.

[3]Cal. Bus. & Prof. Code § 16720.

[4]*Cipro*, 61 Cal.4th at 146 (citation omitted).

[5]*See*Herbert J. Hovenkamp, *The Rule of Reason*, 70 Fla. L. Rev.81 (2018), available at https://scholarship.law.upenn.edu/cgi/viewcontent.cgi?article=2780&context=faculty_scholarship.

[6]*Cipro*, 61 Cal.4th at 146.

[7]Opening Brief of Defendants re Antitrust Standards at 7, UFCW & Employers Benefit Trust, et al. v. Sutter Health, et al., No. CGC 14-538451 (Cal. Super. Ct. S.F. City and Cnty. 2019).

[8]*Cipro*, 61 Cal.4th at 146.

[9]*Id.*

[10]*Id.*(emphasis added) (citation omitted).

[11]Opening Brief of Defendants re Antitrust Standards at 10, 18, UFCW & Employers Benefit Trust, et al. v. Sutter Health, et al., No. CGC 14-538451 (Cal. Super. Ct. S.F. City and Cnty. 2019).

[12]*Id.*

[13]*Cipro*, 61 Cal.4th at 146-47.

[14]*Id.*at 147.

[15]*Id.*at 157.

[16]*Id.*

[17]Opening Brief of Defendants re Antitrust Standards at 8, UFCW & Employers Benefit Trust, et al. v. Sutter Health, et al., No. CGC 14-538451 (Cal. Super. Ct. S.F. City and Cnty. 2019).

[18]*Id.*at 8 fn. 1.

[19]Memorandum of Points and Authorities in Support of Plaintiffs' Motion Requesting Determination Of Antitrust Standards as to Each of Their Causes of Action at 8, 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 "Brief of Plaintiffs re Antitrust Standards").

[20]*Id.*at 11-12.

[21]*Id.*at 14.

[22]*Id.*at 12-13.

[23]*Id.*at 14, 15.

[24]Opening Brief of Defendants re Antitrust Standards at 7, UFCW & Employers Benefit Trust, et al. v. Sutter Health, et al., No. CGC 14-538451 (Cal. Super. Ct. S.F. City and Cnty. 2019).

[25]*Id.*

[26]Sutter noted that in *Ohio v. Am. Express Co.*, the U.S. Supreme Court held that "only horizontal restraints . . . qualify as unreasonable per se." 138 S. Ct. 2274, 2283-84 (2018). *Id.* at 12. Using this example among many, Sutter argued that the per se rule has been applied in "narrowly defined categories that have only become narrower over time," none of which is applicable in this case. *Id.* at 11.

[27]*See supra* note 1.

[28]Opening Brief of Defendants re Antitrust Standards at 17, UFCW & Employers Benefit Trust, et al. v. Sutter Health, et al., No. CGC 14-538451 (Cal. Super. Ct. S.F. City and Cnty. 2019).

[29]*Id.*at 18.

[30]Order re Antitrust Standards at 7, UFCW & Employers Benefit Trust, et al. v. Sutter Health, et al., No. CGC 14-538451 (Cal. Super. Ct. S.F. City and Cnty. 2019).

[31]*Id.*at 7.

[32]*Id.*at 10.

[33]*Id.*at 12.

[34]*Id.*

[35]*Id.*at 13.

[36]*Id.*

[37]*Id.*

[38]Hovenkamp, *supra* note 5, at 83.

[39]*Id.*at 87.

[40]*See id.* at 91.

[41]*See id.* at 93.

[42]*Id.*at 99.

[43]*See id.* at 99.

[44]*Id.*at 166.