

HEALTH ALERT

SPECIALTY HOSPITAL'S ANTITRUST CASE AGAINST HOSPITALS AND MANAGED CARE COMPANIES PERMITTED TO PROCEED



In the ongoing battle between physician-owned specialty hospitals and more traditional acute care hospitals, a federal court in Kansas recently issued a decision permitting a specialty hospital's antitrust case to proceed against competing hospitals and a number of managed care organizations (MCOs) that had refused to contract with the specialty hospital. In *Heartland Surgical Specialty Hospital v. Midwest Division Inc.*, D. Kan. No. 05-CV-2164 (Oct. 1, 2007), the specialty hospital alleged that the competitor hospitals and MCOs engaged in a group boycott designed to shut the specialty hospital out of the acute care market. In denying the defendants' motion for summary judgment, the court ruled that the plaintiff had provided enough evidence of a conspiracy to allow its Sherman Act claims to move forward. The decision clears the way for the case to go to trial in April 2008.

Section 1 of the Sherman Act prohibits agreements that unreasonably restrain competition (15 U.S.C. § 1). A critical issue in such matters is often whether or not an agreement exists. The *Heartland* case is particularly interesting with regard to the antitrust implications of community hospitals' responses to the emergence of specialty hospitals because it involves an allegation of conspiracy between community hospitals and managed care plans. In this regard, the case addresses an important issue for community hospitals and health plans, namely, when might their interaction with regard to a new specialty hospital support a charge of conspiracy.

The defendants in the *Heartland* case moved for summary judgment on the grounds that *Heartland* did not introduce enough evidence to support its conspiracy charge. Their motion was made against the backdrop of significant recent developments in the law regarding antitrust conspiracies. Earlier this year, the U.S. Supreme Court made it significantly more difficult for antitrust plaintiffs to sustain conspiracy charges. See *Bell Atlantic Co. v. Twombly*, 127 S. Ct. 1955 (May 27, 2007) (described in our June 1, 2007, Alert, "[Supreme Court Ruling Portends Change in Motions Practice](#)"). That challenging context makes all the more significant the *Heartland* court's decision that the plaintiff's evidence was enough to charge a conspiracy.

While the relevant evidence is discussed in more detail below, an important point for hospitals and health plans to take away from this decision is that a combination of their contractual

provisions regarding network formation, related rate-setting negotiations, informal and formal discussions of plan networks, and lobbying activity might intermix to support a charge of antitrust conspiracy against specialty hospitals.

BACKGROUND

The plaintiff, Heartland Surgical Specialty Hospital, is a physician-owned hospital that focuses on spine and upper extremity services. Its facilities are new and state of the art and it provides many of the same services usually obtained from traditional acute care hospitals.

The defendants include major MCOs and traditional acute care hospitals in the Kansas City area. The MCO defendants are competitors in the Kansas City area and together account for nearly 90 percent of the managed care enrollment in the area. The hospital defendants are competitors and account for 74 percent of net patient revenues in the Kansas City area. Heartland claims that the dominant hospital systems in the area conspired among themselves and with the dominant MCOs to prevent Heartland from obtaining network provider contracts with the MCOs.

FACTS

When Heartland opened for business, the major hospitals in and around Kansas City made no secret of the fact that they viewed physician-owned facilities like Heartland as competitive threats. Internal memoranda reflect intense strategizing by the hospitals, specifically trying to determine how they could prevent MCOs from adding what the hospitals called “niche facilities” to their networks. Through their contracts with individual MCOs, the hospitals bound the MCOs to exclude Heartland and similar facilities from their networks. Each contract had language indicating that an MCO’s attempt to add a niche facility to its network would result in a steep rate increase or termination of the hospital’s participation in the MCO network. Other provisions required that the MCO get written consent before adding a new facility to its network. In addition to these contracts, on several occasions the defendant hospitals contacted MCO defendants and sought their assurances that they would not add a facility like Heartland to their networks.

Heartland pieced together evidence to support its theory of conspiracy from information it obtained from the MCO defendants. Beginning in 2003, Heartland contacted several MCOs in an attempt to negotiate in-network contracts. The defendant MCOs declined to contract with Heartland, each citing existing contracts with the defendant hospitals that prevented them from adding to their existing networks. Several MCO representatives noted pressure from hospitals not to include specialty hospitals in their networks, or at least specialty hospitals that were not majority owned by a larger acute care hospital. Aetna, for example, responded to Heartland’s requests by simply stating that “an exclusive contract with a hospital system in town prevents us from adding” Heartland. That year Aetna went on to grant the request of every facility majority owned by a traditional hospital that asked to be admitted to the network.

Heartland pointed out that, although the contracts between defendant MCOs and hospitals were specifically designed and implemented to exclude physician-owned specialty hospitals, they nonetheless permitted other competing hospitals to join the MCOs’ networks. According to Heartland’s theory, the MCOs complied in order to keep their existing contracts with the hospitals and thus not lose their competitive edge, while at the same time negotiating reduced reimbursement rates with those hospitals. To be sure, a decision by one MCO to include Heartland in its network would result in that network having a more attractive network to sell, and Heartland asserts that because of this, the defendant MCOs agreed not to take such an action.

COURT'S FINDING

The court began by examining Heartland's theory of the economic motive of the conspiracy and determined that it was "plausible," "straightforward," and "not novel." According to the theory, the hospital defendants engaged in the conspiracy to respond to the competitive threat posed by specialty hospitals. As for the MCO defendants, Heartland alleged that they participated to assure that competitor MCOs would not have a more attractive network of physicians and facilities should they include Heartland or a physician-owned facility. Additionally, as the theory went, by working together with the hospital defendants, the MCO defendants could negotiate lower rates. The court noted that "an MCOs' profitability appears to be dependent on two factors: recruiting employer groups to subscribe to the MCOs' network and negotiating the lowest possible reimbursement rates to be paid to the hospitals in the MCOs' network," and that both factors were at play in Heartland's theory.

The court next considered the weight of the evidence to determine whether it was sufficient to allow the case to move forward to trial. The only direct evidence of a conspiracy was testimony by an MCO representative that there was "kind of the understanding, unwritten but understood" that MCOs would exclude physician-owned hospitals from their networks. The court characterized this evidence as weak because it did not specify who was included in the unwritten understanding.

However, indirect evidence of a conspiracy included the written agreements between the hospitals and MCOs and the explicit language that worked to exclude physician-owned hospitals like Heartland from an MCOs' network. The court noted that these agreements, taken individually, evidenced only an agreement between a single hospital and a single MCO, but considered together, they provided an example of "parallel business behavior," which is circumstantial evidence of an agreement. The court also considered the uncontested facts that the hospital defendants opposed specialty hospitals and had pursued legislative means to inhibit their development.

Heartland also adduced evidence that the hospitals vigorously discouraged MCOs from contracting with specialty hospitals, and that MCO defendants chose not to contract with Heartland based on the hospitals' opposition. There was also evidence that the hospitals had an existing forum wherein discussions relating to the exclusion of specialty hospitals took place, namely at marketing dinners and other health industry functions at which both major hospitals and MCOs were in attendance. Heartland showed that the hospitals communicated to the MCO defendants their desire to exclude physician-owned facilities like Heartland from the market. The court stated that communications could be viewed by a jury as "veiled threats" to the MCOs that they either cooperate or risk losing hospital defendants from their network. Moreover, the court found that there was evidence that MCO defendants were able to negotiate lower reimbursement rates in exchange for participation in the conspiracy.

The court also found evidence that the defendants worked together to create exceptions to the exclusive contract language so that specialty hospitals or facilities where one of the major hospitals owned a majority share could get into the MCO networks. As a result, the court expressed skepticism when the hospitals claimed that they had valid independent business reasons for seeking to exclude specialty hospitals from MCO networks. The court pointed out that the hospital defendants failed to explain why they were willing to work with competitors to permit other majority-owned facilities into the MCO networks, while keeping physician-owned facilities out.

Thus, despite somewhat weak direct evidence of a conspiracy, considering all of the evidence presented by Heartland as a whole, the court found that Heartland had ample circumstantial evidence to support an inference that the defendants acted in concert and not independently. As a result, the court found that the evidence presented by Heartland, combined

with a plausible economic theory and defendant's economic motives, was sufficient for the case to move forward and supported a denial of the defendants' motions for summary judgment.

CONTACT INFORMATION

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