AMERICAN HEALTH LAW ASSOCIATION

PG Briefing
January 4, 2021

If You Can't Beat Them and You Can't Join Them: Geisinger–Evangelical's Warning for Partial Acquisitions

Jeny M. Maier (Axinn Veltrop & Harkrider LLP)
Adam S. Cella (Axinn Veltrop & Harkrider LLP)

This article is brought to you by AHLA's Antitrust Practice Group.

On February 1, 2019, Geisinger Health (Geisinger) and Evangelical Community Hospital (Evangelical) executed a "Collaboration Agreement." As part of this proposed agreement, Geisinger agreed to acquire a 30% interest in Evangelical in exchange for $100 million towards intellectual property licensing and investment projects. The agreement also provides additional rights to Geisinger, including certain approvals over Evangelical's strategic decisions.

The Department of Justice (DOJ) Antitrust Division opened an investigation into the agreement shortly after it was executed, and the hospitals agreed to a hold-separate to maintain the status quo. DOJ filed a complaint on August 5, 2020 to block the partial acquisition.

Most antitrust-related transaction investigations—and particularly investigations that lead to actions to block such transactions—involve a merger or acquisition that results in a change of control. DOJ's enforcement power, however, is not limited to transactions in which a buyer gains control of a target. Section 7 of the Clayton Act specifically prohibits acquisitions of "the whole or any part" of an entity if "the effect of such acquisition may be substantially to lessen competition."[1] Antitrust enforcers can and do investigate partial acquisitions in a similar manner to merger investigations when the transaction in question gives effective control of the target to the buyer, involves substantially all of the relevant assets of the target, or otherwise provides the incentive for the parties to reduce competition between themselves or coordinate their competitive behavior as a result of the partial acquisition.

Here, at only 30% proposed ownership, DOJ does not affirmatively allege in its complaint that Geisinger will "control" Evangelical. From the hospitals' perspective, a sympathetic review of the facts suggests that the hospitals are left to face a DOJ lawsuit for attempting to inject capital into a community's health care system. The hospitals frame the "unique partnership" as an effort to "make healthcare delivery in our region more efficient, cost-effective, and simply better for the patients we serve."[2]

DOJ's complaint, however, contends that the transaction fundamentally alters the relationship between Geisinger and Evangelical and will consequently harm patients and other health care payers through diminished competition. DOJ's investigation found that the hospitals are close competitors attempting to fully integrate. The closeness of competition became clear to DOJ through the parties' market shares and documents from Geisinger and Evangelical. Further, the investigation found that the parties understood they could not fully merge, so they structured the agreement to integrate without facing antitrust scrutiny. DOJ then analyzed the agreement in light

 Copyright 2021, American Health Law Association, Washington, DC. Reprint Permission Granted.

of the parties' past practices and found a history of problematic collaboration that would only further harm competition through the entanglements created by the partial acquisition agreement.

DOJ Concluded Geisinger and Evangelical Are Close Competitors Attempting to Integrate to the Fullest Extent Possible

Geisinger and Evangelical both operate hospitals in Central Pennsylvania. Evangelical is a single independent hospital licensed for 132 overnight patients. Geisinger is an integrated health care provider operating 12 hospitals and numerous other outpatient facilities in Pennsylvania and New Jersey. The flagship Geisinger hospital is located in Central Pennsylvania and can accommodate 574 overnight patients. Geisinger Health Plan is an insurance company operated by Geisinger with approximately 600,000 members enrolled in commercial health insurance, Medicare, and Medicaid products.

DOJ focused on the market for inpatient general acute-care services, a broad cluster of inpatient medical and surgical services that require an overnight hospital stay (e.g., many orthopedic, cardiovascular, women's health, and general surgical services). DOJ does not claim these individual services are substitutes for one another; instead, it claims that the services are an appropriate product market because they are offered to patients under similar competitive conditions by similar market participants.

DOJ focuses its complaint on a six-county area in Central Pennsylvania that encompasses Evangelical and four of Geisinger's hospitals, including its flagship hospital. DOJ's complaint states that patients prefer to receive treatment close to home, and health insurers that offer plans in this area do not consider hospitals outside of the area to be reasonable substitutes.

Notably, DOJ's complaint does not just focus on the allegations of reduced competition within this product and geographic market as a result of the partial acquisition. DOJ also alleges that the transaction fundamentally alters the relationship between Geisinger and Evangelical in a way that will harm competition. To make this claim, DOJ relies on the parties' own words to substantiate both that (1) Geisinger and Evangelical are close competitors and (2) they are attempting to integrate in a way to avoid scrutiny from competition regulators.

The Parties' Market Shares and Documents Show Geisinger and Evangelical Are Close Competitors

DOJ's complaint demonstrates the closeness of competition between the parties through market shares, public comments, and ordinary course documents. The market shares by themselves suggest that Geisinger and Evangelical are close competitors in a highly concentrated market. Within the six-county area, Geisinger has a 54.6% share for inpatient general acute-care services, and Evangelical a 16.7% share. The other approximately 29% comes from just two other hospital systems.

DOJ also used the parties' own documents to evidence close competition between Geisinger and Evangelical. For example, DOJ's complaint pointed to the Evangelical CEO's statement that Geisinger and Evangelical are, for at least some patients, the only two options, stating, "if you don't get your care here [at Evangelical], you get it there [at Geisinger]."[3] Similarly, in 2016, the Evangelical CEO commented on the parties' head-to-head competition in orthopedics, stating that the hospital was "vulnerable to GMC [Geisinger Medical Center] in orthopedics."[4]

DOJ also pointed to direct price competition between the two hospitals as further evidence of the closeness of competition. For example, the parties' documents showed that Evangelical and Geisinger directly compete on price for members of certain religious groups that do not rely on insurance plans. In 2018, Evangelical lowered its prices in response to discovering Geisinger's newly lowered prices and sent a letter to the religious community "[s]o that they would know that [Evangelical's] rates were lower."[5] Evangelical's CEO articulated the price competition even more clearly, stating "Geisinger has significantly reduced its prices" prompting Evangelical "to reduce its prices" for these religious communities.[6]

 Copyright 2021, American Health Law Association, Washington, DC. Reprint Permission Granted.

The Transaction History Shows Geisinger and Evangelical Structured the Agreement to Integrate to the Fullest Extent Possible and Avoid Antitrust Scrutiny

Despite the hospitals' attempts to position their agreement as an efficiency-driven partnership to improve health care in the region, DOJ's complaint uses the parties' own words against them to paint a picture of a transaction intentionally structured to eliminate competition between the parties but without facing antitrust scrutiny.

According to the complaint, public statements and documents indicate that each of Geisinger and Evangelical recognized that a merger between the two parties would be anticompetitive. Geisinger's documents note that a full acquisition of Evangelical "[p]resented serious antitrust concerns."[7] Evangelical's CEO agreed, stating in an interview that "the state and federal government looks at these kinds of things for antitrust . . . and you can't create a monopoly. And so you know the reality of it is even if they wanted to, Geisinger would not have been able to acquire us."[8] With statements like these, DOJ argues that Geisinger and Evangelical made it clear that they knew integrating the companies would have competitive consequences.

The hospitals' executives' testimony stated that despite the known risks, the goal of the parties' agreement was to combine. According to the complaint, a senior Geisinger employee testified: "one of Geisinger's objectives was to integrate . . . to the fullest extent possible."[9] To achieve this objective, the parties set out to construct a transaction that would integrate the two hospitals without facing an antitrust investigation from state or federal authorities. As Geisinger wrote in a document, the parties viewed the agreement as "[k]inda smart really" because it "[d]oes not require AG [Attorney General] approval."[10]

Instead of competing as independent firms, or cooperating as one integrated firm through a full merger or acquisition, Evangelical and Geisinger decided to pursue a strategy of so-called "co-opetition."[11] As Evangelical's CEO explained this economic principle in an interview, Geisinger and Evangelical "can cooperate, and you can compete. And as long as both sides find wins, it works."[12] Finding "wins" through "co-opetition," however, does not find favor from the perspective of antitrust enforcers.

The Partial Acquisition Sufficiently Integrates Geisinger and Evangelical as to Disincentivize Competition

A "substantial lessening of competition" under the antitrust laws can occur even if a buyer does not acquire full control over a target company. A partial acquisition can, in fact, violate Section 7 of the Clayton Act (prohibiting mergers or acquisitions that substantially lessen competition) as well as Section 1 of the Sherman Act (prohibiting agreements that unreasonably restrain trade),[13] and DOJ alleges both types of violations here. DOJ's complaint contends that the partial acquisition would entangle Geisinger and Evangelical to such an extent that meaningful competition benefiting consumers would be lost.

In the partial acquisition context, Geisinger's economic incentive to increase prices on its own health system services—or otherwise take any action that might make Geisinger less competitive—is weaker than it would be if Geisinger were to acquire control of Evangelical. In a hypothetical full merger between Geisinger and Evangelical, Geisinger would have the economic incentive to increase its prices up to the level at which the price increase would become unprofitable due to the losses from patients switching to other competing providers. In a circumstance in which Geisinger were to acquire control over Evangelical, Geisinger could hypothetically profitably raise its prices post-merger because it would be able to recoup some of the losses associated with that price increase due to patients switching to Evangelical (which it would now own).

Here, on the other hand, by only acquiring 30% of Evangelical, Geisinger would receive a smaller benefit from any customer that switches to Evangelical in response to a post-transaction price increase by Geisinger than it would in the case of a hypothetical full merger or acquisition. Geisinger would only receive a fraction of the profits from these patients. DOJ's complaint does not dive deep into the details of the agency's theory of changed economic incentives resulting from this partial acquisition and how exactly this partial acquisition makes it more likely that Geisinger raises price post-transaction. This lack of specificity could cause challenges for DOJ at summary

 Copyright 2021, American Health Law Association, Washington, DC. Reprint Permission Granted.

judgment or trial if the parties are able to demonstrate that the acquisition does not create an incentive, or creates only a small incentive, to increase prices.[14]

Perhaps because the competitive effects resulting from the partial acquisition are ambiguous or difficult to prove, DOJ's case puts significant emphasis on the parties' conduct outside the partial acquisition to contend that, in the future, the parties are more likely to coordinate their competitive behavior than compete aggressively against each other. DOJ's case relies on the hospitals' past practices and own words to demonstrate that the parties' claims of continued competition going forward cannot be trusted. DOJ's investigation and complaint also highlighted certain aspects of the parties' partial acquisition agreement to demonstrate exactly how the agreement would weaken competition and facilitate unlawful coordination between the two hospitals.

Geisinger and Evangelical Had a History of Coordination

Without even looking at documents relating to the partial acquisition itself, DOJ identified that Geisinger and Evangelical had a history of problematic coordination with each other that, according to the complaint, would only likely worsen with the partial acquisition. This history, according to DOJ, greatly increases the risk that the partial acquisition would lead to even closer coordination of the parties' competitive behavior at the expense of consumers. The hospitals' claims of continued competition, unsurprisingly, fell on deaf ears at DOJ.

According to the complaint, the hospitals allegedly coordinated their behavior, instead of competing, even before the partial acquisition agreement by:

1. Holding regular meetings between themselves to discuss strategic growth options;
2. Sharing loan forgiveness agreement terms, which are used to recruit physicians;
3. Establishing a co-branded urgent-care center with a non-compete clause; and
4. Entering into a "no-poach" agreement not to recruit one another's employees.

These examples of coordination are supported by problematic documents and testimony as highlighted in DOJ's complaint. For example, the co-branded urgent-care center was specifically created, as Evangelical's head of marketing explained, "to build volume to our urgent care with Geisinger as a partner rather than potentially as a competitor."[15] The most concerning allegations of the actions listed above is the no-poach agreement, since DOJ has taken the policy position that such agreements between competing employers are potentially criminal—as opposed to merely civil—violations of the Sherman Act.[16] According to DOJ, the parties monitored and enforced each other's behavior under the no-poach agreement. After a recruitment effort by Geisinger targeting Evangelical's nurses, Evangelical's CEO wrote to Geisinger's CEO asking: "Can you please ask that this stop[?] Very counter to what we are trying to accomplish."[17] DOJ argues this history of close communication, cooperation, and enforcement of promises between these competitors suggests that further entanglement between the parties will also act to further limit competition.

The Partial Acquisition Agreement Fundamentally Alters the Parties' Relationship and Reduces Their Incentives to Compete

DOJ's complaint alleges that the partial acquisition agreement reduced the parties' incentives to compete in several ways.

First, the partial acquisition agreement creates a financial entanglement that ties Evangelical to Geisinger and reduces the incentive for the two parties to compete.[18] The $100 million investment from Geisinger in exchange for a 30% ownership stake in Evangelical creates an indefinite partnership that effectively prevents Evangelical from partnering with a different competitor hospital or health system. The "partnership" between the parties resulting from the partial acquisition involves money for specific projects at Evangelical already approved by Geisinger, money for unspecified projects at Evangelical that are to be approved by Geisinger, and intellectual property that will be licensed from Geisinger. This arrangement, according to DOJ, disincentivizes Evangelical

 Copyright 2021, American Health Law Association, Washington, DC. Reprint Permission Granted.

from developing competitive services or improving care that would harm its "partner," Geisinger. The 30% ownership interest in Evangelical similarly dissuades Geisinger from improving and competing to attract consumers away from Evangelical, as doing so would reduce the value of Geisinger's investment.

Second, the partial acquisition agreement gives Geisinger the ability to influence Evangelical's future strategic decisions through a right of first refusal (ROFR) with respect to significant transactions and the right to approve Evangelical's use of funds. According to DOJ, Geisinger's ROFR over any significant transactions Evangelical might enter into will deter potential procompetitive collaborations between Evangelical and other competing health care entities because Geisinger could block or delay these agreements.[19] Similarly, Geisinger's right to approve Evangelical's use of funds would give Geisinger the ability to block competition by withholding approval of any project that might facilitate Evangelical competing against Geisinger.

Third, the partial acquisition lessens Evangelical's incentives to expand its service lines to avoid angering its larger partner and risk disrupting the parties' relationship. According to the complaint, Evangelical has a history of expanding its service lines to compete more vigorously against Geisinger. Now, with closer financial ties as a result of the partial acquisition, DOJ alleges that Evangelical is more likely to view cooperation and coordination as more beneficial than competition. For example, DOJ's complaint highlighted evidence that after the partial acquisition agreement, an Evangelical executive deleted recommendations to expand orthopedic offerings from Evangelical's strategic plans and instead focused on a partnership with Geisinger in orthopedics.

Fourth, the agreement gives Geisinger and Evangelical the mechanisms to share competitively sensitive information through funding rights and necessary approval for major transactions. The agreement requires that Evangelical's requests to disburse funds from Geisinger for strategic projects be supported by business plans. The agreement also requires Evangelical to inform Geisinger of major transactions with other hospital systems. According to the complaint, these approvals require sharing competitively sensitive strategic information that otherwise would not, and should not, be shared among competitors.

Finally, the complaint contends that the agreement alters the economic incentives between the competitors that will encourage price increases. As a result of the parties' arrangement, Geisinger financially benefits from a patient choosing Evangelical because it holds a 30% interest in Evangelical. Similarly, as a result of the arrangement, Geisinger will be less sensitive to the prospect of losing patients to other competing hospitals because many of those patients would choose to go to Evangelical if Geisinger increased its prices. When a patient switches to Evangelical, Geisinger still benefits from that patient's choice, since Geisinger holds a 30% interest. As noted above, the fact that Geisinger is only acquiring 30% of Evangelical complicates the economic model DOJ will need to rely on to show an incentive to increase prices post-acquisition. Nonetheless, DOJ contends that Geisinger is incentivized to increase prices to patients and commercial insurers because the financial consequences from any price increase are smaller than before.

*   *   *

DOJ's complaint in *Geisinger-Evangelical* provides a stern warning for competing health care providers that try to avoid the antitrust laws through partial acquisitions or other devices. Here, DOJ discovered evidence not only that Geisinger and Evangelical were close competitors, but also that the parties were such close competitors they knew that they would not be able to merge or complete a full acquisition. By scrutinizing the parties' agreement and their past practices coordinating their competitive behavior with each other, it is unsurprising that DOJ took action to stop this proposal to tie two competitors together in a way that the agency alleges would lessen competition for patients and health care payers in central Pennsylvania.

[1] 15 U.S.C. § 18.

Copyright 2021, American Health Law Association, Washington, DC. Reprint Permission Granted.

[2] Press Release, *Evangelical and Geisinger Agreement Finalized* (Feb. 4, 2019) https://www.geisinger.org/about-geisinger/news-and-media/news-releases/2019/02/04/13/51/evangelical-and-geisinger-agreement-finalized.
[3] Complaint at ¶ 1, *United States v. Geisinger Health and Evangelical Community Hospital,* No. 4:20-cv-01383 (M.D. Pa. Aug. 5, 2020).
[4] *Id.* at ¶ 19.
[5] *Id.* at ¶ 21.
[6] *Id.*
[7] *Id.* at ¶ 23.
[8] *Id.*
[9] *Id.* at ¶ 25.
[10] *Id.* at ¶ 24.
[11] *Id.* at ¶ 27 and 40.
[12] *Id.* at ¶ 27.
[13] The Federal Trade Commission (FTC) normally reviews transactions between health care providers, including hospitals and hospital systems. It is somewhat unusual that this transaction between an integrated hospital system and a single hospital was reviewed by DOJ. It is likely that one of reasons DOJ conducted this investigation instead of the FTC is that DOJ can bring cases under the Sherman Act as well as the Clayton Act, while FTC cannot bring cases under the Sherman Act (although it can bring Sherman Act-type claims under Section 5 of the Federal Trade Commission Act). Because this case was brought by DOJ under both the Sherman and Clayton Acts (i.e., challenging the partial acquisition as well as the parties' other coordinated conduct) instead of just the Clayton Act (i.e., challenging just the partial acquisition), it suggests that, at least at the beginning of the investigation, FTC and DOJ did not feel confident that a 30% acquisition would lead to a strong Clayton Act Section 7 case.
[14] The parties can create additional uncertainty in the litigation by challenging DOJ's upward pricing pressure model. In a traditional health care provider merger or acquisition, the combined parties would no longer negotiate payer contracts independently. Here, Geisinger and Evangelical would still negotiate their own separate contracts with health insurers and consequently have independent decision making over price setting. This difference could cause complications for any traditional hospital merger models DOJ may choose to rely on.
[15] Complaint, *supra* note 3, at ¶ 41.
[16] In October 2016, FTC and DOJ issued joint guidance on potential violations of the antitrust laws for human resource professionals. This guidance included the warning that "[g]oing forward, the DOJ intends to proceed criminally against naked wage-fixing or no-poaching agreements." *See* Dep't of Justice Antitrust Div. and Fed. Trade Comm'n, Antitrust Guidance for Human Resource Professionals 4 (Oct. 2016), https://www.justice.gov/atr/file/903511/download. On December 9, 2020, a federal grand jury returned a criminal indictment brought by DOJ for conspiring to fix wages—the first criminal charge of this type since the guidance was issued in 2016. *See* Dep't of Just. Antitrust Div., Press Release, *Former Owner of Health Care Staffing Company Indicted for Wage Fixing: Antitrust Division Remains Committed to Prosecuting Collusion in Labor Markets* (Dec. 10, 2020), https://www.justice.gov/opa/pr/former-owner-health-care-staffing-company-indicted-wage-fixing.
[17] Complaint, *supra* note 3, at ¶ 42.
[18] As noted above, the partial acquisition, when compared to a full merger or acquisition, complicates DOJ's attempts to use an economic model to demonstrate that Geisinger will be incentivized to increase prices post-acquisition.
[19] If DOJ chooses to present a narrative that one harm from the partial acquisition is the loss of other potential partnerships that Evangelical could enter into, DOJ will need to argue and prove that: (1) there are other potential partnerships that Evangelical could reasonably enter into; and (2) these hypothetical partnerships are less harmful to competition (or more beneficial) than the Geisinger partial acquisition.

 Copyright 2021, American Health Law Association, Washington, DC. Reprint Permission Granted.