

FTC Challenge to Advocate–NorthShore Merger Continues to Gain Momentum with Addition of Illinois Attorney General

Following the Federal Trade Commission's ("FTC") move to block the proposed merger between two of Chicago's largest health systems—Downers Grove based Advocate Health Care ("Advocate") and Evanston based NorthShore University HealthSystem ("NorthShore")—Illinois Attorney General Lisa Madigan announced her office would be joining the FTC in seeking to block the proposed merger. Initially viewed as the start of a new wave of hospital affiliations in the Chicago market, this proposed merger could actually dampen further Chicago area hospital affiliations as it signals increased regulatory scrutiny.

Proposed Affiliation

In September 2014, Advocate and NorthShore entered into an affiliation agreement, pursuant to which Advocate would change its name to Advocate NorthShore Health Partners and become the sole corporate member of NorthShore. NorthShore would bring a strong research base to the table, as well as a sizeable employed physician group of nearly 800 physicians and specialists. Likewise, Advocate has a nationally recognized clinical integration program with more than 4,000 integrated physicians.

The proposed merger would comprise 17 hospitals—13 from Advocate and 4 from NorthShore—and would make it the nation's 11th largest not for profit health care system. The combined system is expected to generate over \$7 billion in annual revenues.

Advocate and NorthShore originally planned to consummate the proposed merger in early 2015; however, in April 2015, the FTC requested additional information and time to review the proposed merger. The Illinois Health Facilities and Services Review Board ("IHFSRB"), the state board responsible for approving major changes, including changes in ownership, to Illinois health care facilities, approved the merger in December 2014. The IHFSRB's approval is contingent on the merger being completed within 24 months of such approval.

POSTED:

Jan 18, 2016

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FTC and Illinois Attorney General Challenge

In December 2015, the FTC issued an administrative complaint to Advocate and NorthShore alleging unfair competition. Shortly thereafter, Illinois Attorney General Lisa Madigan announced her office would be joining the FTC in seeking to block the proposed merger. The FTC and Attorney General Madigan then proceeded to jointly file a complaint in the U.S. District Court for the Northern District of Illinois seeking a temporary restraining order and preliminary injunction to prevent the proposed merger from going forward until the FTC completes a full antitrust administrative proceeding.

In its administrative complaint, the FTC alleged the proposed merger would substantially lessen competition and cause significant harm to consumers through increased health care costs and a diminished incentive to increase health service offerings and quality improvements. In support of its challenge, the FTC defined the relevant geographic market as northern Cook County and southern Lake County, of which the combined system would control 55% of the general acute care inpatient hospital service market. The FTC went on to explain that it found the proposed merger's alleged efficiencies, including quality improvements, cost savings and the ability for the systems to participate in a low price, ultra narrow network insurance product, to be neither substantiated nor merger specific.

Advocate-NorthShore Claims FTC "Gerrymandering" Analysis

In response to the FTC challenge, NorthShore accused the FTC of gerrymandering the boundaries of the health systems' relevant geographic markets, as well as incorrectly excluding outpatient services from the antitrust analysis, in an attempt to support the FTC's challenge of the proposed merger. NorthShore believes the proposed merger will result in only a combined 22% market share of inpatient beds in its suggested six county Chicago market, as opposed to the FTC's 55% market share estimate based on portions of only two counties.

Furthermore, NorthShore alleges that even within the FTC's limited geographic market, the FTC improperly excludes select market competitors, such as Presence St. Francis Hospital in Evanston and Vista Medical Center West in Waukegan. Given the proximity of these excluded hospitals to NorthShore's own Evanston hospital, as well as to other competitors included in the FTC's analysis,

NorthShore claims these exclusions are evidence of the FTC gerrymandering the analysis to support its challenge. The resolution of this discrepancy will likely hinge on expert econometrics testimony to define the geographic market; however, Advocate and NorthShore likely have an uphill battle since long standing FTC policy is to define markets as narrowly as possible. Advocate and NorthShore have expressed a continued commitment to the proposed merger and plan to vigorously oppose the FTC challenge. The trial for the FTC's injunction request is scheduled for April 6, 2016. The FTC administrative review hearing is scheduled for May 24, 2016.

Geographic Market and Efficiency Defenses

To prevail, Advocate and NorthShore will need to convince the court that the Chicago market is much larger than the FTC portrays. Alternatively, Advocate and NorthShore may try to leverage the fragmented nature of the Chicago health care market—95 hospitals within a six-county area—and show that even with an increase in a neighborhood specific market share, the abundance of nearby health care options means the merger will have little to no competitive effect on the overall market.

In addition to arguing in favor of a broader geographic market, Advocate and NorthShore will also want to show that the affiliation would produce substantiated, merger-specific efficiencies sufficient to overcome any potential harm to competition. In its complaint, the FTC alleges the efficiencies originally proposed by the systems were nothing more than "speculative and unsubstantiated." To succeed here, the systems will need to prove that the efficiencies they put forward are attributable to the merger and cannot otherwise be achieved in a practical, more competitive way (e.g., unilateral expansion or collaborations). Given the recent expansion of both systems, however, this may be an uphill battle.

Historically, the courts have been unwilling to accept efficiency defenses such as improved purchasing power, increased discounts or better geographic coverage when both parties to the merger are already rapidly expanding and such efficiencies could be achieved through continued internal expansion. One exception to this, however, has been when a system has entered into an agreement requiring the system to pass on to the community the substantial cost savings that would be achieved. Advocate and NorthShore attempted to take a similar approach by offering to agree not to raise prices significantly if they merged; however, federal regulators were not interested in the offer. The courts



have also demonstrated an unwillingness to accept efficiency claims based on reducing overcapacity where capacity could be reduced even without a merger. In framing their efficiency defenses, Advocate and NorthShore must be cautious that the efficiencies are not ultimately produced through anticompetitive reductions in output, service or other competitively significant categories, such as system innovation.

The ultimate deciding factor in this point may be whether Advocate and NorthShore adequately prepared for this challenge in the run-up to the transaction. As Reinhart Health Care attorney Tracey Klein explains, "a key question is going to be whether Advocate and NorthShore developed and supported their alleged efficiencies before deciding to enter into the transaction, or instead, merely in response to the FTC's challenge." "Efficiency claims that are either undeveloped before, or even that first arise following an FTC complaint often do little good for those defending the legality of the merger and instead only raise more skepticism and undermine credibility with enforcement officials and the court," explains Attorney Klein. Reinhart Litigation attorney [Scott Hansen](#) further explains, "if the parties do not develop and support their efficiency arguments from the first stages of the transaction, internal communications provided to the FTC are eventually going to contradict the efficiency defense afterthoughts."

Additional Questions and Assistance

If your hospital or health system is considering affiliating, the professionals at Reinhart Boerner Van Deuren s.c. are available to assist you in reviewing your options and developing a strategy to acquire the necessary regulatory approvals. Please feel free to contact [Larri Broomfield](#) or your Reinhart attorney, to discuss any questions or concerns related to your health care organization.

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