Hospital Mergers – A New Landscape?

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Hospital price variation not based upon differences in the quality of care provided has been a public policy focus of the Health Policy Commission for a number of years. One outcome of that effort is a process by which the HPC may review proposed hospital mergers for unwanted effects on hospital prices. Another result is a statutory proposal currently being considered that would penalize some high-cost hospitals for exceeding a hospital spending target. The proposed merger between Lahey and Beth Israel Deaconess hospitals, currently under enhanced HPC review, affords us an opportunity to see how these two approaches might work together. Will the trend toward provider consolidation be allowed to continue because of regulatory constraints on hospital pricing, or will those regulatory measures in effect eliminate market-based efforts to reduce costs?

Beginning in 2013, the HPC has had the ability to subject certain health provider transactions to heightened scrutiny if there are concerns about the effect of the transaction on the provider market or on health spending benchmarks. The process begins when the provider submits a Notice of Material Change that describes the proposed transaction and its anticipated effects; if the HPC believes that the proposal is "likely to have a significant impact on the Commonwealth's ability to meet the health care cost growth benchmark, or on the competitive market," then it may conduct a heightened "Cost and Market Impact Review." This is the process now applied to the Lahey-Beth Israel merger, which may take many months to complete.

The proposed Lahey-Beth Israel merger has been described as a market-based effort to combat the so-called "Partners Effect." This effect is demonstrated, for example, by the fact that in 2014, Partners' hospitals received a third of all commercial insurance payments made to Massachusetts hospitals. The proposed merger, by creating a large competitive hospital system in eastern Massachusetts, arguably would take market share from Partners and result in lower commercial reimbursements to both systems. One concern expressed about the proposal is that, in fact, market share will be taken not from Partners but from community hospitals. Another concern is the more general skepticism that hospital mergers actually reduce prices. The HPC's CMIR review will cover, among other issues, the effect of the proposed merger on total medical expenses, the prices charged for services relative to others in the market and the merged entity's market share, as well as the accessibility and quality of services.

In 2014, the HPC subjected Partners' proposed acquisition of South Shore Hospital to the enhanced Cost and Market Impact Review. The HPC rejected the transaction on the grounds that: it would increase health care costs by many millions of dollars annually, would result in the combined entity having half of the market share for inpatient acute care services in the relevant market, both parties had above-median payment rates with payors and the acquisition would increase their ability to negotiate even higher reimbursements, and total medical expenses would increase more than savings expected to result from proposed population health management initiatives. The focus of this review was on the market effects of the proposed transaction. The conclusion of the review was that it would not have the desired market effects. Now, the same type of review will be applied to an aspirant competitor to Partners.

The impending CMIR of the Lahey-Beth Israel transaction takes place in the context of the consideration of a Senate bill that would, if enacted in its present form, penalize high-cost hospitals if a statewide target in hospital commercial health care spending growth is exceeded. As currently proposed, the three hospitals that most contributed to that excessive cost growth would be penalized. The Senate bill also calls for health insurers to certify that their hospital reimbursements do not fall below a floor (proposed to be 90 percent of statewide relative prices) and if they do, to be subject to a financial penalty. The proposal has been criticized for not imposing a cap on hospital reimbursements and for potentially encouraging hospitals to increase their prices to just below the level at which penalties might be assessed on them.

In the CMIR process, the HPC asks whether a particular action in the marketplace, such as a corporate combination, is likely to have desirable market outcomes such as decreased prices or increased service accessibility. If such outcomes appear unlikely, the HPC can seek the assistance of the Attorney General to block the transaction. The Senate bill simply identifies undesirable market outcomes, such as excessive spending growth or differential prices paid for the same services, and penalizes those it deems to have benefitted from those outcomes. In the CMIR process, the market is given an opportunity to work but the government may block the proposed transaction; under the Senate proposal, market dysfunction is a given and is attended by governmental intervention in the form of penalties.

How will these two approaches be applied to the Lahey-Beth Israel transaction? Will the potential imposition of financial penalties under the Senate proposal, if enacted, make it easier for the HPC to approve the transaction because certain of its potential undesirable market effects may thereby be eliminated or reduced? More broadly, will Massachusetts continue to take a market-based approach to the ongoing trend of provider consolidation, or will it focus instead on reimbursement controls and overall spending growth targets? The HPC, in its 2016 Cost Trends Report issued in February 2017, stated as its first policy recommendation the "fostering a value-based market in which payers and providers openly compete." It also noted a "strong consensus that hospital mergers lead to higher prices in the vast majority of cases." It seems clear that "open competition" is and will continue to be subject to state-imposed guardrails. What is less clear is whether a managed marketplace will continue to have a place for significant provider combinations.

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