OUTLINE

A Market All Its Own: the Story of Medicare Advantage as a Separate Product Market in the DOJ's Case Against the *Aetna-Humana* Merger

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Introduction

- In recent years there has been significant merger activity among health insurers.
- Two mega-insurer mergers eventually moved forward – Anthem-Cigna and Aetna-Humana.
- The government filed actions in the DC District court to enjoin both mergers.
- As a practical matter in mega-mergers like these, the DOJ has to come up with a more simplified approach to challenge the merger than the enforcers usually do when seeking to enjoin smaller transactions.
- In Aetna-Humana, the lynchpin of the government's case was that Medicare Advantage is a separate product market from Original Medicare, and the Aetna-Humana merger would substantially reduce competition in the Medicare Advantage market.
- The parties and their experts did not dispute that Original Medicare (considered along with Medicare Supplement plans), is functionally interchangeable with Medicare Advantage plans.
- The case rose and fell on whether there was *reasonable* interchangeability.
- The judge ultimately decided that consideration of *Brown Shoe* factors and an econometrics analysis both support the existence of a separate market for Medicare Advantage.
- The judge reached this result through a careful, detailed traditional analysis. His approach highlights some of the ways in which parties should assess potential mergers in future.

Legal Framework

- The government bears the initial burden in seeking to enjoin a merger to show that it may substantially lessen competition or tend to create a monopoly in a relevant market.

- If the government can show the merger would result in a firm with an undue share of the relevant market and the merger would cause a significant increase in the concentration of firms in the market, there is a presumption that it will lessen competition.

    - To rebut the presumption, merging parties can show, among other things, ease of entry into the market, a failing firm defense, or an efficiencies defense (the viability of an efficiencies defense remains uncertain. *See St. Luke's*; *Advocate*).

Background on Medicare Advantage / Original Medicare / MedSupp

- Original Medicare is the government insurance program everyone is familiar with that covers individuals once they reach the age of eligibility (currently 65).

    - It is broken into Parts – A (inpatient hospital services); B (physician and outpatient services).

        - Parts A and B are not comprehensive. There are gaps in coverage (e.g. dental, vision, and hearing) and coinsurance rates, no out of pocket maximum, and no prescription drug coverage.

        - Consumers can buy MedSupp plans to fill gaps in coverage and protect against catastrophes.

        - Consumers have to obtain prescription drug coverage separately (Medicare Part D)

    - Almost all hospitals/physicians accept Original Medicare, so it provides consumers substantial choice.

- Medicare Part C allows seniors to opt out of Original Medicare and obtain subsidized insurance through private insurers.

    - Medicare Advantage plans are the product of Medicare Part C.

        - Private insurance companies offer products with more services by, among other things, offering a narrower network of providers.

        - Medicare Advantage plans – unlike Original Medicare – often include prescription drug coverage.

        - Medicare Advantage plans often include coverage for services that fall with gaps in Original Medicare coverage such as dental, vision, and hearing.

        - There are often meaningful differences in the scope of coverage offered by different Medicare Advantage plans.

Background on Aetna/Humana Merger

- Aetna and Humana are two of the Big 5 National Insurers.
- Aetna and Humana are two of the biggest players in Medicare Advantage.
    - Together they account for 25% of Medicare Advantage enrollees.
    - DOJ identified 364 counties around the country where it argued concentration in the Medicare Advantage market would rise above the presumptively unlawful level if Aetna and Humana merged and there were no divestiture.
        - DOJ argued that the post-merger company would have a monopoly in 70 of the counties and serve 80+ percent of Medicare Advantage consumers in 80 counties.
- Aetna and Humana presented a proposed divestiture, recognizing that in some markets the post-merger concentration levels would be very high.
    - Proposed divestiture was to Molina, a managed Medicaid specialist.
    - The divestiture would have sold lives in all of the 364 counties the DOJ argued that concentration in Medicare Advantage would have been too high.
        - The size of the proposed divestiture was an indication of just how big an impact the merger would have in Medicare Advantage.

Market Definition Issue at the Heart of Aetna-Humana Case

- The case brought to a head an unresolved issue that has been swirling around in health care antitrust for a long time: is there a cognizable separate market for Medicare Advantage plans that does not include Original Medicare (considered together with MedSupp plans)?
- The DOJ constructed much of its case against the merger on the existence of a separate market for Medicare Advantage plans
- The complaint and DOJ briefing sets up the market in a way that has intuitive appeal: Medicare Advantage plans have distinct features and characteristics that differentiate them from Original Medicare/MedSupp. Although the distinctions are not as stark as some entirely dissimilar products (e.g. short-term travel health insurance vs. traditional annual commercial health insurance), there are many ways in which Medicare Advantage plans stand apart from Original Medicare.

- The parties developed a substantial body of evidence on both sides that fed into their arguments on reasonable interchangeability of Medicare Advantage and Original Medicare/MedSupp

    - Government

        - Different costs. Medicare Advantage is cheaper and has much less downside risk. Original Medicare/MedSupp is more expensive.

        - Different features. There are more services offered in Medicare Advantage plans (wellness, dental, vision, et al.); there is more room for innovation (gym memberships, wellness programs, HMO-style efficient/coordinated care models).

        - Different set of providers. Original Medicare is a broad network; Medicare Advantage is much narrower. For consumers that have strong feelings about their choice of providers, Medicare Advantage is substantially different than Original Medicare.

        - Different consumer demographics of Medicare Advantage consumers vs. Original Medicare

            - Evidence showed that seniors who opt for Medicare Advantage plans tend on average to be lower income and lower education levels than the population as a whole.

            - Original Medicare and MedSupp enrollees tend to be higher income and value provider choice over breadth of coverage and costs. Enrollees in Original Medicare and MedSupp also tended to be in smaller towns and rural areas.

            - These demographic differences suggest that while the two are functionally interchangeable, consumers may actually be falling into one camp or the other and not actually choosing between the two.

        - Switching data shows that Medicare Advantage consumers who leave a Medicare Advantage plan largely go to another Medicare Advantage plan.

    - Defendants

        - At bottom, the two products are being offered to the same set of customers – seniors – and they compete for those customers both at enrollment and over time after enrollment.

            - ~10,000 seniors age into Medicare every day. As a result there is constant pressure on Medicare Advantage to compete against Original Medicare for a bigger share of the new entrants.

        - Lots of differentiation among Medicare Advantage plans. When you start looking at the diversity within Medicare Advantage, the differences when comparing to Original Medicare start to look less significant.

        - Seniors regularly reevaluate their health care needs – it is a time of life when health care needs change significantly over periods of years. Medicare Advantage plans have to compete for Original Medicare customers even if they are losing year after year, because eventually some may be driven by cost or other pressures to reevaluate (e.g. dwindling retirement savings and unexpected rising medical costs).

        - Ordinary course of business documents and testimony that consider MedSupp and Medicare Advantage together. This evidence seemed more limited and general than DOJ's evidence that the parties treated the two separately.

        - The government treats Medicare Advantage as an alternative to Original Medicare. It markets Medicare Advantage in connection with Original Medicare and offers it at the time of initial enrollment in a way that makes the two directly pitted against each other.

        - Defendants argued (without data – relying largely on testimony) that "[d]emographics do not determine whether seniors prefer Original Medicare options or Medicare Advantage plans." They tried to make the case that every senior is different at any given decision-making point. "[N]o two seniors are exactly alike." Wooldridge (Tr. 716:10)

- <u>Econometric Evidence</u>

    - Experts assessed market using diversion ratios and hypothetical monopolist test

        - Dr. Avi Nevo – Government's economist

            - To select Medicare Advantage as the product market, Nevo considered industry evidence, switching data (which he found tied switching decisions largely to price), other empirical studies of how seniors choose their coverage, and his own nested logit model (which estimates demand in response to a price increase)

                - Nevo's nested logit model finds a diversion ratio of 70% leaving Medicare Advantage plans would go to another Medicare Advantage plan.

        - Dr. Jonathan Orszag – defendants' economist

            - Diversion ratios are more important than switching data because switching data fails to capture the critical "age-in" population that is entering the market for the first time.

        - Orszag finds diversion ratio of 50% from Medicare Advantage to Original Medicare in response to a price increase or quality drop (even Nevo finds a diversion rate of 30%).

    - Orszag argues that Nevo's analysis fails to recognize a significant portion of individual switching from Medicare Advantage plans go to Original Medicare before some of the more dissimilar Medicare Advantage plans. This is Example 6 from the Merger Guidelines.

- Opinion

    - Judge Bates was considered a relatively good draw for the defendants.

    - After the trial, he issued a thorough 150+ page opinion enjoining the merger.

        - This detailed decision is a stark contrast to some of the short decisions seen recently in provider merger cases like *Advocate* (and to a lesser extent *Hershey*) that have resulted in appeals.

    - Judge Bates resolved the case in a traditional way.

        - He started by looking at how to define the market. In doing so, he looked at functional interchangeability of Medicare Advantage and Original Medicare. However, he appropriately did not let that be the end of the inquiry. He recognized that there must be *reasonable* interchangeability – i.e. cross-price elasticity of demand.

            - The decision assesses practical indicia from *Brown Shoe*. Medicare Advantage is less expensive both on the front end and in terms of avoidance of substantial costs in the event of major medical issues. Original Medicare allows broad consumer choice; Medicare Advantage plans offer much narrower networks. Original Medicare has significant gaps in coverage and more limited services; Medicare Advantage fills those gaps (e.g. prescription drug coverage) and offers extras like gym memberships, vision, dental, and hearing.

            - MedSupp Plans can fill the gaps in Original Medicare. However, Judge Bates was persuaded by what seemed like strong evidence from the parties that Medicare Advantage and Original Medicare/MedSupp plans are not actually reasonably interchangeable in the defendants' own business. This evidence indicated that the parties thought of and treated the two quite differently from a competitive standpoint.

        - One of the worst documents for defendants was one in which an Aetna executive refers to Medicare Advantage and MedSupp plans as "apples and oranges."

    - Judge Bates also looked at switching evidence as a proxy for what consumers think of as reasonable interchangeability.

        - The switching data showed consumers with Medicare Advantage plans largely switch to other Medicare Advantage plans. The Defendants were unable to provide a convincing way to explain away the switching data.

- The defendants' argument that switching data is not an apt way to assess reasonable interchangeability in light of the number of consumers aging into Medicare did not factor heavily into the Court's analysis.

    - Judge Bates acknowledged the point but seemed unconvinced that this ongoing initial access to the market should undermine switching data as a proxy for consumer preferences.

    - This is one of the aspects of the decision that leaves antitrust practitioners without a good sense of what could be done differently. Judge Bates did not give any indication of what evidence related to the consumers aging into Medicare *could* have undermined the switching data or otherwise overcome the government's evidence of reasonable interchangeability.

    - Judge Bates also did not engage at all with the argument that Medicare Advantage needs to continue to innovate and compete for seniors as their needs change over time (e.g. decreasing retirement funds, increasing health care costs).

- Judge Bates also evaluated the parties' respective econometric evidence.

    - Judge Bates credited Nevo's demand model, which included a nesting parameter that indicated that certain seniors have a distinct preference for Medicare Advantage as compared to other coverage options.

    - Nevo's analysis found that 70 percent of seniors who respond to a price increase by leaving a Medicare Advantage plan would switch to another. This was actually below the 80 percent found in the switching data.

    - Judge Bates did not spend much time sifting through all of the ways Orszag attacked Nevo.

        - Judge Bates' decision was not driven by the econometrics.

            - Judge Bates' approach is emblematic of what parties can expect from a good judge. Other than some outliers (e.g. Judge Posner) it is unlikely that a judge will engage solely or principally in an econometric analysis. More likely, the *Brown Shoe* analysis will guide the decision-making process and the econometric evidence will need to be very strong to overcome a clear conclusion via *Brown Shoe*.

    - Conclusions from facts and circumstances.

    - In addition to siding with the DOJ on the market definition issue discussed in this paper, the Court rejected the defendants' efficiencies defense, rejected the proposed divestiture to Molina (a managed Medicaid specialist) and

- Shortly after the decision issued Aetna/Humana threw in the towel on the merger.

    - The belt-and-suspenders opinion left little room to overturn the critical market definition issue. An appellate court would have had to reject the Court's analysis under *Brown Shoe* and the assessment of the parties' econometric evidence.

        - Unfortunately, that means no additional clarity forthcoming from an appellate court on reasonable interchangeability and other more nuanced aspects of the market definition issues in this case.

Takeaways / Issues for Further Consideration

- Reasonable interchangeability can be challenging to assess, with many imperfect ways to come at it. Judge Bates seemed most influenced by the switching data and the parties' own documents.

    - The court did not dig in much to the demographics of consumers to assess whether there was actually consumer choice occurring between Original Medicare and Medicare Advantage.

    - The parties' experts were an important part of Judge Bates' analysis, but the result was not driven entirely by an econometric analysis of the transaction. Notably, Judge Bates cautioned against reliance on purely econometric evidence: "Econometric evidence can be powerful evidence, but it is not the only evidence that courts consider in defining the relevant market."

    - This opinion reinforces the importance of retaining and utilizing an expert to assess a transaction that raises reasonable interchangeability questions, but also thinking about reasonable interchangeability from a non-econometric perspective.

- There are complexities associated with consumer preferences that can make a reasonable interchangeability analysis very challenging.

    - Consider some examples: consumers buying a car; consumers buying clothing; consumers buying certain types of food (e.g. cereals) or drinks (Coca Cola); tax software vs. accountant vs. do-it-yourself.

        - Changes in price may move the needle in unexpected ways because of the strength of certain consumer preferences.

            - e.g. significant changes in price for tax software is unlikely to divert substantial numbers of consumers to do-it-yourself

        - Hard to peel apart consumer preferences in the context of a complex decision like what health plan a consumer would switch to when faced with price increase or quality drop.

- This case was another example of how merging parties' own documents can carry the day. Judge Bates seemed to be very persuaded that Original Medicare was not reasonably interchangeable with Medicare Advantage because the parties themselves treated them so differently in their own documents and business operations (e.g. separate business units for MedSupp and Medicare Advantage). It is hard to argue two products are reasonably interchangeable when your own executive refers to them as "apples and oranges."

- There remains much uncertainty regarding how courts will use Examples 5 and 6 in the Merger Guidelines to assist in a market analysis.

    - Judge Bates noted that using Example 5 there can be a proper relevant market "even if customers would substitute significantly to products outside that group in response to a price increase." He did not give any further guidance on how parties might assess how high diversion levels could be and still leave a proper market (other than noting that Example 5 uses a diversion rate of two-thirds).

    - Despite allowing a broad read of Example 5, Judge Bates took a narrow view of Example 6. He expressed concern that endorsing Orszag's application of Example 6 "would create an exception that completely swallows that rule." The opinion does not provide an alternative approach to Example 6 that allows it have any utility in this kind of situation. It is unclear how a party might use Example 6 to show that a product was improperly excluded from a product market if not in the way Orszag proposed.