Issue Brief

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America's Health Insurance Plans

Hospital and Provider Consolidation: Negative Impact on Affordability for Consumers

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Issue Brief

Introduction

There are a number of private sector and public/private initiatives underway to address affordability by lowering or constraining the growth of the health care costs faced by consumers. These initiatives involve health plans and health care providers, and range from the incremental to the potentially transformational. One development, however, threatens the success of all of these initiatives: the increasing consolidation of hospitals and other providers into systems with outsized market power.

Any effort to address the cost of health care must include, and likely begins with, addressing the cost of hospital care. It is well established that hospital price increases are "the largest contributor to increases in insurance premiums."[1] These price increases are driven by the consolidation of hospital markets, often into systems with significant market power.[2] The harmful impact of such systems is not limited to higher prices, but also includes diminished incentives to innovate or improve quality. The passage of the Affordable Care Act (ACA) has heightened attention to the need for innovation to deliver on the goals of greater access, improved quality, and lower costs. Unfortunately, the market power of hospital systems often stands as an impediment to such innovation and such improvements.

While antitrust enforcement provides one avenue for addressing this issue, its impact is necessarily limited by its case specific and, typically, prospective nature in the context of consolidation. Such enforcement should be continued and expanded to prevent the further creation or enhancement of the market power of hospital systems, but alone it will not be sufficient to address such an entrenched problem. It will be necessary to address this challenge in markets, in the regulatory arena, and in policy approaches.

The Consolidation of Hospitals into Systems

Beginning in the 1990s and continuing into recent years, a wave of hospital consolidations occurred throughout the United States.[3] While the federal antitrust agencies challenged some such transactions, the challenges were largely unsuccessful. By the early 2000s most metropolitan statistical areas (MSAs) in the country had

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highly concentrated hospital markets, often resulting from the formation of hospital systems consisting of formerly competing hospitals.[4] A Robert Wood Johnson Research Synthesis reported that between 1990 and 2003, the number of MSAs (with populations over 100,000) with highly concentrated hospital markets rose from 71% to 88%. The breadth of this concentration can also be seen by the fact that in 2006, the mean HHI[5] (a measure of market concentration used in antitrust analysis) for hospital markets was 3161, well in excess of the 2500 threshold considered concentrated under the antitrust agencies' 2010 Merger Guidelines.

The federal agencies were more successful challenging hospital transactions in the 2000s, but merger-by-merger lawsuits are not an approach well designed to deal with existing and widespread hospital market power. Hospital mergers have continued and, as noted below, have accelerated since the passage of ACA. The cumulative effect of the past and ongoing consolidation has been the entrenchment in most MSAs of hospital systems with market power, a continued rise in hospital prices, and an ongoing challenge to innovative efforts to address the problem of rising health care costs.

The Impact of Hospital Consolidation on Affordability and Quality

One consequence of the wave of provider consolidation has been the development of an extensive record of what happens to prices and quality after such mergers have occurred. The consistent result of multiple independent studies is that prices go up, substantially, when such mergers occur. Perhaps more surprisingly, but no less significantly, is the indication by such studies that quality has not improved and costs have not been lowered by such consolidations, suggesting that the "efficiencies" and other justifications offered for such mergers are illusory.

Among the research findings demonstrating that consolidation in the hospital industry is leading to higher health care costs (without improved health care quality) for consumers and employers, are:

- A September 2013 research brief by the Center for Studying Health System Change[6] reported that "it is clear that provider market power is key in price negotiations and that certain hospitals and physician groups, known as 'must-haves,' can extract prices much higher than nearby competitors." This study also concludes that "increases in provider prices explain most if not all of the increase in premiums" in recent years.
- The Massachusetts Center for Health Information and Analysis[7] recently released its "2013 Annual Report on the Massachusetts Health Care Market." In a discussion about the impact of provider consolidation, the report notes that the highest priced 25 percent of providers in Massachusetts received over 50 percent of commercial payments made to acute hospitals and physician groups in 2012. A Boston Globe article[8] pointed out that the report's findings show that as hospitals and provider groups consolidate, "larger groups often have the leverage to demand higher prices from insurers."
- A June 2012 study published by the Robert Wood Johnson Foundation (RWJF)[9] found that "increases in hospital market concentration lead to increases in the price of hospital care," and that "when hospitals merge in already concentrated markets, the price increase can be dramatic, often exceeding 20 percent." This study further cautions that "physician-hospital consolidation has not led to either improved quality or reduced costs" and, additionally, points out that consolidation "is often motivated by a desire to enhance bargaining

power by reducing competition." An earlier RWJF research project[10], focusing on hospital consolidation in the 1990s, stated: "Studies that examine consolidation among hospitals that are geographically close to one another consistently find that consolidation leads to price increases of 40 percent or more."

- An issue brief published in July 2011 by the National Institute for Health Care Management Foundation[11] found that one of the factors contributing to higher prices is "ongoing provider consolidation and enhanced negotiating strength vis-à-vis insurers, resulting in an ability to extract higher payment rates from insurers."
- An article published in June 2011 by the American Journal of Managed Care[12] found that "hospitals in concentrated markets were able to charge higher prices to commercial insurers than otherwise-similar hospitals in competitive markets."
- Paul Ginsburg and Robert Berenson, in an article published in the February 2010 edition of *Health Affairs*[13], stated that "providers' growing market power to negotiate higher payment rates from private insurers is the 'elephant in the room' that is rarely mentioned."

Individually, these studies are compelling evidence of the harm to consumers that has occurred as hospitals have rolled themselves up into systems, sometimes with staggering percentages of hospitals, physicians, and other providers in local health care markets. These studies provide the evidence for the need to act now to re-focus the delivery system on quality and efficiency, rather than market power. This is particularly compelling in a post-ACA environment.

Relationship of ACA to Hospital System Formation and Expansion

Even prior to the passage of the ACA, most hospital markets were highly concentrated, often as the result of the formation of hospital systems. Since the passage of the ACA, the pace of hospital consolidation has not diminished but instead has accelerated. According to Levin Associates, the number of hospital mergers and acquisitions in the United States has more than doubled from 50 in 2009 to 105 in 2012.[14]

Such numbers, while significant, do not capture the full extent or impact of the creation and expansion of systems. For, more recently, a great deal of provider consolidation has been occurring at the so called "vertical level." Such consolidation often involves the acquisition, or absorption, of formerly independent physician practices into hospital systems. The impact of this form of consolidation will depend upon the market specific facts and circumstances and in some instances is likely to lead to higher prices and further harm to consumers. For example, if the acquisition of physician practices reduces hospital competition because those physicians will now only refer to one hospital, consumers will suffer harm. In addition, if previously competing physicians are now consolidated under the umbrella of a single hospital system, consumers will be harmed.

While some will use the ACA as an excuse to consolidate, this is simply a red herring argument. Consolidation regardless of what causes it is harmful to the health care system and most importantly harmful for consumers. It is well established that consumers benefit from competitive provider markets. Vigorous competition in provider markets not only serves as a constraint on increasing provider costs, but also creates incentives for providers to promote quality improvements and innovation. The further consolidation of hospitals, therefore, will not only stifle attempts to provide consumers with affordable health care, but will constrain efforts to improve quality and develop innovations in care.

1 Overcoming the Pricing Power of Hospitals, 308 *Journal of the American Medical Association*, p. 1213 (2013).

2 More Evidence of the Association Between Hospital Market Concentration and Higher Prices and Profits, National Institute for Health Care Management, November 2011.

3 The Welfare Consequences of Hospital Mergers, Robert Town et al., National Bureau of Economic Research, Working Paper No. 1224, 2006.

4 For example, see Hearing on Health Care Industry Consolidation Before the Subcommittee on Health of the Committee on Ways and Means, 112th Cong., Statement of Martin Gaynor, September 9, 2011.

5 HHI (Herfindahl-Hirschman Index) is a commonly accepted measure of market concentration that is used by the Department of Justice and the Federal Trade Commission. Increases in the index indicate a decrease in competition and an increase in market power.

6 High and Varying Prices for Privately Insured Patients Underscore Hospital Market Power, Center for Studying Health System Change, September 2013.

7 2013 Annual Report on the Massachusetts Health Care Market, Massachusetts Center for Health Information and Analysis, August 2013.

8 Partners hospitals, doctors top health-payment list, *The Boston Globe*, August 14, 2013.

9 The impact of hospital consolidation–Update, Martin Gaynor, PhD and Robert Town, PhD, Robert Wood Johnson Foundation, June 2012.

10 How has hospital consolidation affected the price and quality of health care?, William B. Vogt, PhD and Robert Town, PhD, Robert Wood Johnson Foundation, February 2006.

11 Understanding U.S. Health Care Spending, National Institute for Health Care Management Foundation, July 2011.

12 Hospital Market Concentration, Pricing, and Profitability in Orthopedic Surgery and Interventional Cardiology, James C. Robinson, PhD, *American Journal of Managed Care*, June 24, 2011.

13 Unchecked Provider Clout In California Foreshadows Challenges To Health Reform, *Health Affairs*, February 2010.

14 New Laws and Rising Costs Create a Surge of Supersizing Hospitals, *New York Times*, August 12, 2013.

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