DEPARTMENT OF JUSTICE
Antitrust Division

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April 27, 2004

Terence L. Smith, M.D.
Chief of Anesthesia
Anne Arundel Medical Center
1008 West Street
Annapolis, Maryland 21401-0718

Dear Dr. Smith:

This letter responds to your request for a statement pursuant to the Department of Justice Business Review Procedure, 28 C.F.R. § 50.6, of the Department's present enforcement intentions regarding your proposal to merge all or most of the 16 solo physician practices currently providing anesthesia services at Anne Arundel Medical Center ("AAMC") into a single, integrated anesthesia group practice, which will become the sole provider of anesthesia services at AAMC. Based on the information provided in your request, as supplemented by our own investigation, the Department has no present intention to challenge the proposed merger.

Background

Because anesthesia services are essential for the performance of surgical procedures at general acute care hospitals, competent anesthesiologists who are trusted by the surgeons practicing at any given hospital must be available at all times to assist at both scheduled and emergency operations. Therefore, over time it is common for hospitals to develop relationships with a set of anesthesiologists who are largely dedicated to the performance of procedures at a particular hospital. When the anesthesiologists practicing at a hospital are independent practitioners, as is the case with the anesthesiologists practicing at AAMC, the hospital, as well as payers, must rely on the cooperation and self-discipline of the anesthesiologists

to formulate schedules, coordinate with the surgeons, and assure that adequate coverage is provided for all procedures requiring the attendance of an anesthesiologist, whether emergency or elective.

While some payers have entered into contracts with some of the anesthesiologists practicing at AAMC specifying the prices of their services, AAMC itself has no contracts with any of the anesthesiologists at this time.[1] This is in contrast to AAMC's relationship with other types of hospital-based practitioners -- *i.e.*, emergency room doctors, pathologists and radiologists. In arranging for the services of each of these physician specialties, AAMC has found it beneficial in each case to enter into contracts with a single integrated group practice, giving each group the exclusive right to perform their specialty services at AAMC and the obligation to provide all of AAMC's needs for such services. AAMC prefers this approach because of the convenience of dealing with a single physician group practice, rather than many individual doctors, to negotiate a contract, to schedule doctors' time, to enable the hospital to identify and budget for costs based on a common fee schedule, and to establish and monitor consistent quality control standards. Payers have also indicated that they prefer to work with a single, integrated practice group rather than sixteen individual physicians. This would guarantee full coverage for their enrollees and obviate complicated scheduling problems that arise when only certain doctors are contracting with them.

Merger Analysis

The Department and the courts examine the lawfulness under the antitrust laws of a merger of physician practices using the same antitrust standards that they apply to any other merger or combination of competing entities. The Clayton Act requires the delineation of the proper "line of commerce" and "area of the country" (*i.e.*, relevant product and geographic markets) and then the evaluation of the likely economic effect of the merger in that market (or markets). The merger is unlawful if it may tend substantially to lessen competition in any relevant market by creating, enhancing or facilitating the exercise of market power. *See* Department of Justice/Federal Trade Commission Horizontal Merger Guidelines, 4

[1] If the anesthesiologists merge into an integrated anesthesia group, however, AAMC intends to contract with the group about pricing terms in order to be able to offer payers "global" fee arrangements, which will cover all the expenses associated with providing a given medical procedure, such as an appendectomy. The global fee would typically include hospital stay, surgery, anesthesia, radiology, medication and any incidental expenses. According to AAMC, there is significant demand among payers for the development of such global fee arrangements, and the proposed merger will facilitate their development. In fact, some payers have already diverted some elective surgeries from AAMC to other area facilities that offer global rates.

Trade Reg. Rep. (CCH) ¶ 13,104 (April 2, 1992), § 2 ("Merger Guidelines"). "Market power" is generally defined as "the power

to control prices [or restrict output] or exclude competition." United States v. E. I. du Pont de Nemours & Co., 351 U.S. 377, 391 (1956).

In defining the relevant product (or service) market for a particular merger, the Department determines what substitutes, as a practical matter, are reasonably available to consumers of each product of the merging firms if the price of the product were raised by a small but significant amount. *See* Merger Guidelines at § 1.11. Services provided by a particular physician specialty may often be a relevant service market. *See* Statements of Antitrust Enforcement Policy in Health Care, Issued by the U.S. Department of Justice and the Federal Trade Commission, August 1996, at 76. Based on the facts of this case, it appears that anesthesia services are the relevant service market in this instance.

Next, we analyze the relevant geographic market by identifying where an anesthesia practice could be located to be a good substitute for any of the 16 merging anesthesiologists if the prices for their services rose by a small but significant amount. The participants in the market would comprise all anesthesiologists who either currently do provide anesthesia services or would likely begin providing them in the relevant geographic market within a year and without incurring significant sunk costs. *See* Merger Guidelines at § 1.3.

The information available to us suggests that the geographic market relevant to this merger could be as large as an area within a 25-mile radius of AAMC. Your submission indicates that you believe the market to be at least that large, and statements by payers that they would be willing to divert elective[2] surgeries to other area hospitals if AAMC's anesthesia prices were to rise unreasonably further bolster this hypothesis. We also understand that AAMC values maintaining the continuity of the cadre of anesthesiologists currently practicing at AAMC due to the long-standing relationships and the trust that exist among its surgeons and those anesthesiologists. AAMC officials, however, told us that they would have incentives to replace the anesthesiologists in the event of a price increase, not only because of AAMC's position as a buyer of anesthesia services, which it will become after the merger in order to contract with payers under "global" fee arrangements,[3] but also out of a desire not to lose market share through the diversion to other facilities of health plans' enrollees in need of elective procedures.

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[2] Elective surgeries are surgical procedures that can be scheduled in advance.

[3] *See* fn. 1, *supra*.

In a geographic market within the 25-mile radius of AAMC, there would be approximately 285 anesthesiologists practicing in groups of varying size at AAMC and 16 other non-military hospitals;[4] the 16 anesthesiologists at AAMC represent about 6% of that total. Even if the geographic market were smaller than the 25-mile radius hypothesized above, the number of market participants would still be relatively large. That is, there appear to be a significant number of anesthesiologists located outside, but close to, any smaller putative geographic market who likely would enter the market within a year and without incurring significant sunk costs, through the opening of satellite practices, and those anesthesiologists would impose significant competition on the merged anesthesia group.

Thus, under any plausible geographic market definition and assumptions about the number of market participants, this merger does not raise any substantial competitive concern. This conclusion is further bolstered by the lack of concern expressed by AAMC or any third-party payers who utilize AAMC that the merger is likely to cause anticompetitive effects. Given these considerations, we conclude that the merged anesthesia group should face effective competitive constraints on its ability to exercise market power in the provision of anesthesia services, and thus that the merger would not be likely to lessen competition substantially.

Since the proposed merger does not raise concern about any significant potential adverse competitive effects based on an analysis of market characteristics, we do not need to scrutinize any other factors, such as any efficiencies that are likely to result from the merger. We nevertheless note that, in the judgment of the merging anesthesiologists, AAMC, and payers, the integrated group practice formed by the merger to be the sole provider of anesthesia services at AAMC will produce substantial efficiencies; their position is consistent with the agencies' recognition of the efficiency-producing potential of appropriately designed exclusive contracts involving hospital-based integrated physician groups. *See Burnham Hospital*, 101 F.T.C. 991 (1983) -- Letter to Robert E. Nord, February 24, 1983 (radiologists); Letter to Tad R.Callister from Anne K. Bingaman, March 8, 1996 (anesthesiologists) .

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[4] The majority of these anesthesiologists practice in integrated hospital-based groups ranging in size from 4 to 21 physicians at non-teaching hospitals. The average group size is 11.6. Many of the hospitals in this group are large, sophisticated hospitals fully comparable to or exceeding AAMC in service capability. In addition, there are two large teaching hospitals in the same area: John Hopkins University has 85 faculty anesthesiologists and 75 residents; the University of Maryland has 40 faculty members and 43 residents.

Conclusion

It appears from the foregoing analysis that the proposed merger is not likely to have any significant adverse competitive effects and may, in fact, result in substantial efficiencies for the benefit of consumers and payers of anesthesia services provided at AAMC. Therefore, the Department has no present intention of challenging the proposed merger because it is not likely to lessen competition substantially. In accordance with our normal practice, however, the Department remains free to bring an enforcement action in the future should the operation of the integrated group prove anticompetitive in purpose or effect.

This statement is made in accordance with the Department's Business Review Procedure, 28 C.F.R. § 50.6, a copy of which is enclosed. Pursuant to its terms, your business review request and this letter will be made available to the public immediately. Your supporting documents will be publicly available within 30 days of the date of this letter unless you request that any part of the material be withheld in accordance with Paragraph 10(c) of the Business Review Procedure.

Sincerely,

Anne K. Bingaman