UNITED STATES OF AMERICA
BEFORE THE FEDERAL TRADE COMMISSION

In the Matter of	)	
OSF Healthcare System, a corporation, and	)	Docket No. 9349
Rockford Health System, a corporation,	)	Public Document
Respondents.	)	

RESPONDENT OSF HEALTHCARE SYSTEM'S ANSWER TO COMPLAINT

Respondent OSF Healthcare System ("OSF"), by its undersigned attorneys, for its Answer to the Complaint, states as follows:

I.

NATURE OF THE CASE

1. OSF's acquisition of RHS's assets (the "Acquisition") would substantially lessen competition for critical health care services in the Rockford, Illinois area. By ending decades of competition between OSF and RHS that has benefitted the community, the Acquisition threatens to increase total health care costs and reduce the quality of care and range of health care choices for employers and residents in the Rockford region.

ANSWER: OSF admits that it and RHS will no longer be independent competitors against each other following consummation of the transaction. OSF denies all of the remaining allegations of paragraph 1. Further answering, OSF states that its affiliation with RHS will enable them to create operational efficiencies and generate cost savings that will result in approximately $41-54 million in annual savings and over $130 million in one-time capital cost avoidance, as well as $1-2 million in revenue enhancements, that neither system could generate on its own, and to clinically integrate and innovate to expand and enhance the level, scope and quality of healthcare services they provide to residents in the Rockford area. Additionally, the

affiliation of OSF and RHS is the best, if not the only, way to adapt to the region's changing healthcare needs and achieve what "decades of competition" among the three Rockford healthcare systems has not – containment of the spiraling cost of healthcare. In short, the affiliation is procompetitive and in the public interest.

2. The Acquisition, by Respondents' own admission, is a merger to duopoly for general acute-care inpatient hospital services in the Rockford region. The Acquisition will eliminate vigorous competition between OSF and RHS, and leave the Rockford region with only one other competitor for general acute-care inpatient hospital services: SwedishAmerican Health System ("SwedishAmerican").

ANSWER: OSF denies the allegations of paragraph 2. First, there is no definition of "the Rockford region" and there is no basis on which to assess Plaintiff's claims in paragraph 2. Second, rather than eliminating competition, the affiliation will invigorate and enhance competition by creating one strong competitor to SwedishAmerican, the largest and fastest-growing hospital system in Rockford, rather than two weaker competitors. Third, the hospitals located in Rockford face increasing competition from general acute care hospitals located outside Rockford.

3. The Acquisition also will eliminate important competition for primary care physician services in the Rockford region by combining two of the three largest physician groups, and will leave SwedishAmerican as the only other large hospital-employed physician group competitor in Rockford.

ANSWER: OSF admits that the Acquisition will combine two of the three largest physician groups in the Rockford region and that SwedishAmerican will be the only other large hospital-employed physician group based in Rockford. OSF denies all of the remaining allegations of paragraph 3. SwedishAmerican, with the largest hospital-employed primary care physician group, will remain a strong competitor and there are numerous other primary care physicians who are not employed by any of the three hospitals.

4. The Acquisition will create a single dominant health system in the Rockford region, with the combined OSF/RHS controlling 64% of the general acute-care inpatient hospital

services market and over 37% of the market for primary care physician services. The Acquisition will leave just two firms, OSF and SwedishAmerican, controlling 99.5% of the general acute-care inpatient hospital services market and 58% of the market for primary care physician services.

ANSWER: OSF denies the allegations of paragraph 4. The most appropriate measure of in-patient hospitals' market share are patient discharges; using patient discharge data, the above percentages are not correct. Moreover, OSF disputes the relevant market definitions for both in-patient general acute care and primary care physicians and resultant market share percentages.

5. The Acquisition is presumptively unlawful under the relevant case law and the U.S. Department of Justice and Federal Trade Commission Horizontal Merger Guidelines ("Merger Guidelines") because of the extraordinarily high post-acquisition market shares and concentration levels in the market for general acute-care inpatient hospital services in the Rockford region. The likelihood of anticompetitive effects arising from the Acquisition, including increased reimbursement rates stemming from the creation of a dominant health system, is independently supported and confirmed by evidence from sources including health plans, local employers and physicians, third party hospitals, and the merging parties themselves.

ANSWER: OSF denies the allegations of paragraph 5. The first sentence of paragraph 5 consists of conclusions of law based on a structure constructed by Plaintiff and the Antitrust Division of the U.S. Defendant of Justice ("DOJ"), and not facts. The second sentence consists of unfounded speculation, not facts, and the affiliation will lead to pro-competitive effects by holding down costs and increasing the quality of service which will outweigh the anticompetitive effects, if any.

6. Rockford region employers and their employees would bear the costs — either directly or through higher health insurance premiums, co-pays, and other out-of-pocket health care expenses — of the rate increases likely to result from the Acquisition. Such health care cost increases force employers to reduce or eliminate health insurance benefits, force families to drop their health insurance altogether, and force some patients to delay or forego medical care that they can no longer afford.

ANSWER: OSF denies the allegations of paragraph 6. The Acquisition is not likely to be the cause of any higher health insurance premiums, co-pays or other out-of-pocket healthcare expenses and, in addition, the second sentence consists of speculation, not facts.

7. The Acquisition also would diminish the quality of care, range of health care choices, patient experience, and access to care for Rockford region residents by ending decades of important non-price competition between OSF and RHS, and by reducing the incentive for OSF and SwedishAmerican to compete aggressively post-acquisition.

ANSWER: OSF admits that it and RHS will no longer be independent competitors against each other following consummation of the transaction. OSF denies all of the remaining allegations of paragraph 7. The affiliation will improve the quality of care, the range of health care choices, patient experience, and access to care for Rockford residents. Increasing access to larger patient population, consolidating services, and increasing volumes enables physicians and clinical and administrative support teams to increase their proficiency. The affiliation will allow the new entity to create centers of excellence, attract specialists and sub-specialists, and establish residency programs with the University of Illinois College of Medicine at Rockford. OSF and SwedishAmerican will be incentivized to continue to compete after the Affiliation and the affiliated entity will be in a position to better compete against SwedishAmerican than are the two separate entities currently.

8. The price and non-price competition eliminated by the Acquisition would not be replaced by other providers. SwedishAmerican is the only other hospital that meaningfully competes for Rockford region patients, and significant barriers to entry and expansion, including regulatory requirements and substantial up-front costs, prevent new hospitals from entering the market.

ANSWER: OSF admits that for new providers to enter and offer inpatient hospital-based services they must meet regulatory requirements and expend up-front costs. OSF also admits that following its affiliation with RHS, the combined entity will face meaningful competition from SwedishAmerican, which has affiliated with the University of Wisconsin

Hospital in Madison and has opened a second hospital in Belvidere, just east of Rockford. OSF denies all of the remaining allegations of paragraph 8. In addition, other hospitals outside of Rockford, including hospitals in Madison, Chicago, Beloit, and the Quad Cities, have expanded their share of hospital-based services to Rockford area residents and will continue to attempt to expand such services.

9. The fact that the merged entity would still face at least some competition from one meaningful competitor, SwedishAmerican, is not sufficient to render the Acquisition lawful under Section 7. This conclusion is compelled by the antitrust laws — which condemn more than just mergers to monopoly — and also by the market realities in the Rockford region. Specifically, after the Acquisition, the merged system will be a virtual "must-have" for health plans seeking to offer insurance to Rockford employers and employees. This fact — and the greater leverage the merged firm will enjoy as a result — stems from the inability of commercial health plans after the Acquisition to offer an attractive provider network without contracting with the combined system.

ANSWER: OSF admits that the combined entity will face competition from SwedishAmerican, which is a meaningful competitor. OSF denies all of the remaining allegations of paragraph 9. The combined OSF-RHS will not be a "must have" system for commercial payors such that they will pay any price for OSF and RHS to be in their networks. The merged hospitals will not have greater leverage as a result of commercial healthcare plans not being able to offer an attractive provider network without the combined OSF and RHS. A preferred provider network with only one Rockford hospital system in-network is and will be an attractive and viable alternative.

10. Health plans must offer at least two of the Rockford hospitals to be marketable to local residents. As a result, every major health plan network in the Rockford region includes two, but not all three, of the Rockford hospitals. After the Acquisition, no health plan could continue to offer a multi-hospital network in Rockford without facing the substantially higher rates that will be demanded by the merged OSF and RHS.

ANSWER: OSF denies the allegations of paragraph 10. Certain health plans, such as The Alliance, offer all three Rockford hospital systems as in-network providers. In addition, members of Blue Cross Blue Shield of Illinois (OSF's largest commercial payor) can obtain

services at in-network rates at all three Rockford hospitals. One hospital system networks also are viable. Blue Cross' HMO-I is an existing one-hospital system network that includes only SwedishAmerican, as is the OSF Direct Access Network. A Rockford employer, Rockford Acromatic, has recently contracted with a one-hospital network for its employees through the OSF Direct Access Network. The merged OSF-RHS will not demand substantially higher rates as a result of their affiliation and health plans will be able to offer a network consisting of all three Rockford hospitals and both hospital systems after the affiliation.

11. The Acquisition also increases the incentive and ability for the only remaining competitors in Rockford, SwedishAmerican and OSF, to engage in anticompetitive coordinated behavior. Such coordination could include directly or indirectly sharing sensitive information related to commercial health plan contracts and negotiations, or it could involve deferring competitive initiatives that otherwise would benefit the Rockford community.

ANSWER: OSF denies the allegations of paragraph 11. OSF has not engaged in anticompetitive coordinated behavior and will not do so in the future.

12. Unless prevented, the Acquisition will substantially lessen competition and greatly enhance Respondents' market power. The Acquisition's likely anticompetitive effects will directly increase health care costs for Rockford residents, as well as lower the quality of care that they receive. Respondents' speculative efficiency and quality-of-care claims are insufficient to offset the significant anticompetitive harm likely to result from the Acquisition.

ANSWER: OSF denies the allegations of paragraph 12. The Affiliation will have procompetitive effects on the cost and quality of healthcare in Rockford. The efficiencies and increased quality of care that will result from the affiliation are not speculative, but are identified in detail, and are merger-specific. These efficiencies will enhance the procompetitive effects of the Affiliation.

II.

BACKGROUND

A.

Jurisdiction

13. OSF and RHS are, and at all relevant times have been, engaged in commerce or in activities affecting commerce, within the meaning of the Clayton Act. The Acquisition constitutes an acquisition under Section 7 of the Clayton Act.

ANSWER: OSF admits the allegations of paragraph 13.

B.

Respondents

14. Respondent OSF is a not-for-profit health care system incorporated under and by virtue of the laws of Illinois. OSF is headquartered in Peoria, Illinois. OSF owns and operates six acute care hospitals in Illinois, and a seventh hospital in northwestern Michigan. In Rockford, OSF operates St. Anthony Medical Center ("OSF St. Anthony"), which has 254 licensed beds and serves the Rockford region. OSF also owns and operates OSF St. Anthony's employed physician group, OSF Medical Group ("OSFMG"), which employs approximately 80 physicians in the Rockford region. During fiscal year 2010, OSF generated $1.7 billion in operating revenue, with OSF St. Anthony generating approximately $325 million of that total.

ANSWER: OSF denies that OSFMG employs approximately 80 physicians in the Rockford area and denies the allegations in the final sentence of paragraph 20. OSFMG does not employ any physicians; OSF employs physicians through St. Anthony Medical Center ("SAMC"). OSF admits the remaining allegations of paragraph 20, except denies that Plaintiff has defined "the Rockford region."

15. Respondent RHS is a not-for-profit health care system incorporated under and by virtue of the laws of Illinois. RHS is headquartered in Rockford, Illinois. RHS owns and operates one acute care hospital, Rockford Memorial Hospital ("Rockford Memorial"), which is located in Rockford, Illinois and serves the Rockford region. Rockford Memorial has 396 licensed beds. RHS also owns and operates Rockford Health Physicians ("RHPH"), which employs approximately 160 physicians in the Rockford region. During fiscal year 2010, RHS generated $441 million in operating revenue.

ANSWER: OSF admits the allegations of paragraph 15.

C.

Employers and Health Plans

16. Competition between hospitals occurs in two "stages." In the first stage, hospitals compete to be selected as in-network providers by health plans. To become an in-network provider, a hospital engages in bilateral negotiations with the health plan. Hospitals benefit from in-network status by gaining access to the health plan's members as patients. Health plans seek to create provider networks with geographic coverage and a scope of services sufficient to attract and satisfy employers and their employees. One of the critical terms that a hospital and a health plan agree upon during a negotiation is the reimbursement rates that the health plan will pay to the hospital when the health plan's members obtain care at the hospital's facilities or from its employed physicians.

ANSWER: OSF admits that hospital systems benefit from in-network status in health plans, and that hospital systems and health plans negotiate reimbursement rates and other contract terms. OSF denies the remaining allegations of paragraph 16. The characterization of competition as "two-staged" suggests a sequence of events that is not accurate.

17. Fully-insured employers and their employees pay premiums, co-pays, and deductibles in exchange for access to a health plan's provider network and for insurance against the cost of future care. The costs to employers and health plan members are inextricably linked to the reimbursement rates that health plans negotiate with each health care provider in their provider network. Self-insured employers have access to their health plan's network and negotiated reimbursement rates but assume all risk for the costs of care provided to their employees. Self-insured employers must pay the entirety of their employees' health care claims and, as a result, they immediately and fully incur any hospital rate increases. Therefore, regardless of whether an employer is fully-insured or self-insured, its health plan acts as its agent — and by extension acts on behalf of its employees — in creating provider networks that offer convenience, high quality of care, and negotiated reimbursement rates.

ANSWER: OSF denies the allegations of paragraph 17. Hospital rates are not negotiated in a vacuum with managed care payors. An overall contract is negotiated that can include inpatient, outpatient, and physician services. There has been and continues to be a shift from what were exclusively inpatient services to outpatient services. Costs to employers and health plan members are not "inextricably linked" to reimbursement rates that health plans negotiate with each provider, because the health plan can decide how to price its products in light of any changes in reimbursement rates, and employers can decide whether and to what degree

they will charge employees for premiums and other out-of-pocket costs independent of provider reimbursement rates. Self-insured employers do not assume all risk for the costs of health care provided to their employees because many purchase excess or umbrella insurance policies that limit liability. Self-insured employers do not necessarily "immediately" incur any hospital rate increases, and because of excess or umbrella insurance may not "fully" incur the cost of such increases. In addition, both fully insured and self-insured employers can access any commercial product available in Rockford, can switch between self-insured and fully insured status, and can choose among health plans offered by commercial health plans. Commercial health plans do not act as agents for employers and their employees in establishing provider networks and reimbursement rates, because health plans do not place the interests of employers and employees above their own interests or act as their fiduciaries.

18. In the second stage of competition, hospitals and their employed physicians compete with other in-network providers to attract patients. Health plans typically offer multiple in- network hospitals with similar out-of-pocket costs and those hospitals compete in this second stage to attract patients by offering better services, amenities, convenience, quality of care, and patient satisfaction than their competitors offer.

ANSWER: OSF denies the allegations of paragraph 18. Many hospital patients are admitted to hospitals on the basis of their physician's recommendation or requirements, and not because of the factors listed in this paragraph. OSF strives to offer excellent services and high-quality care irrespective of what its competitors are doing, consistent with the mission of the owners of OSF, the Sisters of the Third Order of Saint Francis. OSF, at SAMC and its other hospitals, cannot afford not to compete in areas of quality and patient satisfaction. The need to continue to provide high-quality services is shown by the movement of many payors to pay-for-performance based contracts and away from contracts that are based on fees for services. The characterization of a "second stage" of competition suggests a sequence of events that is not accurate.

D.

The Acquisition

19. Under the terms of the affiliation agreement signed on January 31, 2011, OSF will acquire all operating assets of RHS and become the sole corporate member of RHS. OSF will hold reserve powers over the governance and operations of RHS. OSF's reserve powers will grant it control and ultimate authority over all significant business decisions of RHS, including strategic planning, operating and capital budgets, large capital expenditures, and significant borrowing and contracting.

ANSWER: OSF admits the allegations in the first sentence of paragraph 19. OSF admits that its precise reserve powers will be as set forth in the Affiliation Agreement between OSF and RHS dated January 31, 2011. OSF denies all the remaining allegations of paragraph 19.

E.

Prior Holding by District Court of Illinois and Seventh Circuit Court of Appeals that Merger of Two Rockford Hospitals Would Violate the Antitrust Laws

20. The United States District Court for the Northern District of Illinois, Western Division ("District Court") found in 1989 that the proposed merger of Rockford Memorial and SwedishAmerican violated Section 7 of the Clayton Act. After holding a full trial on the merits, the District Court issued a permanent injunction to stop the merger and the U.S. Court of Appeals for the Seventh Circuit, in a decision written by Judge Posner, affirmed the District Court's finding of liability and upheld the permanent injunction.

ANSWER: OSF lacks knowledge or information sufficient to form a belief as to the truth of the allegation that the Court held a full trial on the merits. OSF denies that the Court's 1989 decision relating to Rockford Memorial's proposed merger with SwedishAmerican supports the Complaint in this case. At the time of the 1989 proposed merger, Rockford Memorial and SwedishAmerican were the largest and second-largest hospital systems in the Rockford area, and SAMC would not have been a viable competitor against the combined SwedishAmerican-RHS. In contrast, this proposed transaction involves the second and third largest hospital systems in the Rockford area with the largest, SwedishAmerican, being a

formidable competitor in terms of size, services, technology and its affiliation with the University of Wisconsin Hospital. In addition, there have been significant structural changes in the market since the proposed merger in 1989, including the growth of SwedishAmerican as the market leader, further deterioration of the economic situation in Rockford, and reductions in Government reimbursement to healthcare providers and the implementation of healthcare reform legislation, which make the reasoning and analysis of what may have happened in Rockford over 23 years ago under different circumstances and competitive conditions irrelevant to the analysis of OSF's affiliation with RHS today. In addition, there is no evidence that any of the three Rockford hospital systems have engaged in any communications or concerted activities such as those described by the District Court in its 1989 opinion. OSF admits the remaining allegations of paragraph 20. OSF states that the current situation is analogous to that in 1997 when the DOJ approved the merger of the then second and third largest hospital systems based in Rockford.

21. In the 1989 case, the District Court defined a relevant geographic market identical to the market alleged in this Complaint. The District Court also defined a relevant product market — general acute-care hospital inpatient services — identical to a market alleged in this Complaint. In fact, the District Court described a market structure, levels of market concentration, and entry conditions in the earlier case that are strikingly similar to those alleged in this Complaint and, on that basis, concluded that the merger of two Rockford hospitals would "produce a firm controlling an undue percentage share of the relevant market, thus increasing the likelihood of market dominance by the merged entity or collusion."

ANSWER: OSF admits that in the 1989 case, the Court defined the relevant geographic market as Boone County, the northeast portion of Ogle County, and small fractions of McHenry (zip code 61052), DeKalb (zip code 60146), and Stephenson (zip code 61019) counties. The Court labeled this area the "Winnebago-Ogle-Boone area" or "WOB." OSF also admits that the Court in the 1989 case defined a relevant product market as general acute care hospital inpatient services. OSF admits that the FTC accurately quotes a portion of one sentence of the Court's opinion in *United States v. Rockford Memorial Hosp.,* 717 F. Supp. 1251 (N.D. Ill.

1989). OSF denies all of the remaining allegations of paragraph 21. OSF states that the current situation is similar and analogous to that in 1997 when the DOJ approved the merger of the then second and third largest hospital systems based in Rockford.

22. Following a full hearing on the merits, and on facts very similar to the facts alleged in this case, the District Court issued a permanent injunction blocking the merger of two of the three Rockford hospitals. Given that the only meaningful difference between the 1989 merger and the Acquisition is the re-shuffling of the parties to the transaction, the District Court's ruling in 1989 informs this Court's assessment under Section 7 of the Clayton Act of this proposed merger of two of the three Rockford hospitals.

ANSWER: OSF lacks knowledge or information sufficient to form a belief as to the truth of the allegation that the Court in the 1989 case held a full hearing on the merits. OSF admits that the Court entered a permanent injunction blocking the merger of Rockford Memorial Hospital and Swedish American Hospital, who were then the two largest of three hospital systems in Rockford. OSF denies the remaining allegations of paragraph 22. OSF further states that the Court's 1989 decision is irrelevant to this case for, among other reasons, those stated in its answer to paragraph 20, and that the 1997 decision by the DOJ to approve the merger of the then second and third largest hospital systems based in Rockford should inform this Court's assessment of the current transaction.

III.

THE RELEVANT SERVICE MARKETS

A.

General Acute-Care Inpatient Services Market

23. The Acquisition threatens substantial harm to competition in the market for general acute-care inpatient hospital services sold to commercial health plans ("general acute-care services"). General acute-care services encompass a broad cluster of medical and surgical diagnostic and treatment services that include an overnight hospital stay, including, but not limited to, many emergency services, internal medicine services, and surgical procedures. It is appropriate to evaluate the Acquisition's likely effects across this entire cluster of services, rather than analyzing each inpatient service independently, because the group of services is offered to

Rockford region residents by the same set of competitors and under similar competitive conditions.

ANSWER: OSF denies the allegations of paragraph 23. The first sentence consists of a conclusion unsupported by any facts, and, in fact, the affiliation will have substantial pro-competitive effects. The remaining allegations ignore the competition and overlap between in-patient and out-patient services, out-migration of patients to hospitals in Madison, Chicago, the Quad Cities and elsewhere, reduced in-migration from nearby community hospitals due to increased services offered by those hospitals and by larger hospitals from Madison, Chicago, and elsewhere.

24. The general acute-care services market does not include outpatient services (those not requiring an overnight hospital stay) because such services are offered by a different set of competitors under different competitive conditions. Further, health plans and patients could not substitute outpatient services for inpatient services in response to a price increase. Similarly, the most complex and specialized tertiary and quaternary services, such as certain major surgeries and organ transplants, also are not part of the relevant cluster of services because they generally are not available in the Rockford region, are offered by a different set of suppliers under different competitive circumstances, and are not substitutes for general acute-care services.

ANSWER: OSF denies the allegations of paragraph 24. Healthcare has seen a trend of many in-patient services becoming out-patient services because of advances in medicine. Certain tertiary services are provided by the Rockford hospitals. In analyzing the competitive effects of the affiliation, it is important to consider the increasing competition from hospitals outside of Rockford to provide tertiary and quarternary services to Rockford residents, and to consider the desirability to Rockford residents of the Rockford hospital systems providing additional tertiary services and quarternary services in Rockford.

25. The District Court defined the same general acute-care services market in its 1989 opinion, which was upheld by the Seventh Circuit.

ANSWER: OSF denies the allegations of paragraph 25. The changes in the delivery of healthcare over the past 23 years have been significant. These include the shift from inpatient

to outpatient services, out-migration of patients to hospitals in Madison, Chicago, the Quad Cities, and elsewhere, and reduced in-migration from nearby community hospitals.

B.

Primary Care Physician Services

26. The Acquisition also threatens substantial competitive harm in the market for primary care physician services provided to commercially-insured adults. This market encompasses services offered by physicians practicing in internal medicine, family practice, and general practice. This relevant market does not include physician services provided by pediatricians because they typically treat only patients eighteen years old and younger. This relevant market also excludes physician services provided by obstetricians and gynecologists ("OB/GYN") because those services generally complement, rather than substitute for, general primary care physician services.

ANSWER: OSF denies the allegations of paragraph 26. The first sentence consists of a conclusion unsupported by any facts and, in fact, the Affiliation will have substantial pro-competitive effects. The stated market ignores the fact that children also are treated by physicians practicing in internal medicine, family practice and general medicine.

IV.

THE RELEVANT GEOGRAPHIC MARKET

27. The relevant geographic market in which to analyze the effects of the Acquisition in the general acute-care inpatient hospital services market is no broader than the geographic market defined by the District Court in its 1989 opinion: an area encompassing all of Winnebago County, essentially all of Boone County, the northeast portion of Ogle county, and single zip codes in McHenry, DeKalb, and Stephenson counties (referred to by the District Court as the "Winnebago-Ogle-Boone" market). Today, as was the case in 1989, this relevant geographic market accounts for 87% of the inpatient admissions of the merging parties. Notably, and in contrast to other previous hospital mergers, the precise contours of the relevant geographic market do not alter in any meaningful way the number of competitors, the market share statistics, or the ultimate conclusion that the Acquisition is likely to lead to competitive harm.

ANSWER: OSF denies the allegations of paragraph 27.

28. The appropriate geographic market is determined by examining the geographic boundaries within which a hypothetical monopolist for the services at issue could profitably raise prices by a small but significant amount.

ANSWER: OSF denies the allegations of paragraph 28.

29. Rockford region residents have a clear preference for obtaining hospital care and primary care physician services locally. As a result, health plans must include hospitals and primary care physicians from the Rockford region in their provider networks in order to meet their members' needs. Patients do not and would not go to hospitals or primary care physicians outside of the Rockford region in response to rate increases within the region. Thus, a hypothetical monopolist that controlled all of the hospitals or all of the primary care physicians in the Rockford region could profitably increase rates by at least a small but significant amount.

ANSWER: OSF admits that some Rockford residents have a preference for obtaining certain hospital care and certain primary physician services locally. Other Rockford residents have a preference for receiving hospital care in hospitals outside of Rockford and have in fact done so. OSF denies all the remaining allegations of paragraph 29.

30. In the ordinary course, OSF and RHS treat only their Rockford counterparts as meaningful competitors, and both hospitals focus their competitive efforts on providers located in Rockford. OSF and RHS define their primary service areas no broader than the Winnebago-Ogle-Boone area. Patient draw data maintained in the ordinary course by both OSF and RHS indicates that nearly all of their inpatients originate from the Winnebago-Ogle-Boone area.

ANSWER: OSF denies that its primary service area is the Winnebago-Ogle-Boone area for each of its service lines. OSF lacks knowledge or information sufficient to form a belief as to how RHS defines its primary service area. OSF denies the remaining allegations of paragraph 30.

31. The relevant geographic market in which to analyze the market for primary care physician services provided to commercially-insured adults is similarly no broader than the Winnebago-Ogle-Boone area defined by the District Court in 1989, and may be significantly more narrow. Patients are no more willing to travel to obtain primary care services than they are to obtain acute-care inpatient hospital services. Indeed, because patients generally obtain primary care services much more frequently than acute inpatient hospital services, their preference for access to local providers is significantly stronger.

ANSWER: OSF denies the allegations of paragraph 31, except that it admits that some patients prefer to obtain primary care physician services in their local communities. The 1989 matter has no relevance here for the reasons summarized in OSF's answer to paragraph 20 and because there was no primary care physician services market involved in the 1989 case.

V.

MARKET STRUCTURE AND THE ACQUISITION'S PRESUMPTIVE ILLEGALITY

A.

General Acute-Care Inpatient Services Market

32. The Acquisition will reduce the number of general acute-care hospital competitors in the Rockford region from three to two, creating a duopoly of OSF and SwedishAmerican.[1]

ANSWER: OSF admits that the affiliation will reduce the number of general acute-care hospital competitors in Rockford from three to two, but denies the remaining allegations contained in paragraph 32. Plaintiff overstates the competitive significance of the affiliation by ignoring the current demographics in the Rockford area, other regional competitors, and the excess capacity that exists. Rockford can no longer support three independent, competing full-service general acute-care inpatient hospital systems.

33. The Acquisition is presumptively unlawful by a wide margin under the relevant case law and the Merger Guidelines because it would significantly increase concentration in the already highly concentrated market for general acute-care services in the Rockford region.

ANSWER: OSF denies the allegations of paragraph 33. The allegations consist of conclusions of law based on a structure constructed by the FTC and the DOJ, and not of facts.

34. OSF's post-Acquisition market share in the general acute-care services market will be 64% (as measured by patient days), easily surpassing levels held to be presumptively unlawful by the Supreme Court. Moreover, the Acquisition would leave just two hospitals, OSF and SwedishAmerican, in control of 99.5% of the Rockford region market for general acute-care services.

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[1] The only other provider within the relevant geographic market, Rochelle Community Hospital ("Rochelle"), is located in Rochelle, Illinois, a small community 30 miles (over 40 minutes driving time) south of Rockford. As the District Court held previously, and the evidence continues to show, Rochelle is not competitively relevant to Rockford and its three hospitals. Rochelle's market share in the Rockford region is less than one half of one percent. It is a 25-bed critical access facility that offers a very limited range of services, is prohibited by the state from expanding its capacity, and serves its immediate community almost exclusively.

ANSWER: OSF admits that Rochelle Community Hospital in Rochelle, Illinois is within Ogle County and that it is licensed for 25 beds, and admits that Rochelle is a community south of Rockford. The 1989 matter has no relevance here for the reasons summarized in OSF"s answer to paragraph 20. OSF denies all the remaining allegations in footnote 1.

ANSWER: OSF denies the allegations of paragraph 34. Patient discharges, not patient days, are the most accurate measure of hospital in-patient market share, and the calculations of HHI are not therefore accurate. Also, as one federal court of appeals has explained, "[t]he Herfindahl-Hirschman Index cannot guarantee litigation victories." *United States v. Baker Hughes, Inc.*, 908 F.2d 981, 992 (D.C. Cir. 1990).

35. As described in the Merger Guidelines, the standard for measuring market concentration is the Herfindahl-Hirschman Index ("HHI"). A merger or acquisition is likely to create or enhance market power, and is presumed illegal, when the post-acquisition HHI exceeds 2500 points and the acquisition would increase the HHI by more than 200 points. Here, the general acute-care services market concentration levels drastically exceed these thresholds. The Acquisition would, as shown below, increase the HHI from 3319 to 5351, a change of 2032 points.

GENERAL ACUTE CARE INPATIENT SERVICES		
Hospital/System	**Pre-Acquisition Market Share**	**Post-Acquisition Market Share**
SwedishAmerican	35.6%	35.6%
RHS	34.3%	-
OSF	29.6%	63.9%
Rochelle	0.5%	0.5%
	Pre-Acquisition HHI	3319
	Post-Acquisition HHI	5351
	HHI Increase	2032

ANSWER: OSF admits that the Merger Guidelines, drafted by the FTC and the DOJ, discuss HHI and mergers and acquisitions. OSF refers to the complete Merger Guidelines for the contents thereof. OSF denies the remaining allegations in paragraph 35. Patient discharges, not patient days, are the most accurate measure of hospital in-patient market share, and the calculations of HHI are not therefore accurate. Also, as one federal court of appeals has explained, "[t]he Herfindahl-Hirschman Index cannot guarantee litigation victories." *United*

States v. Baker Hughes, Inc., 908 F.2d 981, 992 (D.C. Cir. 1990). OSF denies all of the remaining allegations of paragraph 35.

36. In its 1989 decision, the District Court found that the merger of two Rockford hospitals resulting in concentration figures similar to those resulting from this Acquisition "would produce a firm controlling an undue percentage share of the relevant market, thus increasing the likelihood of market dominance by the merged entity or collusion." Notably, the Rockford region is even more concentrated today than it was in 1989, due to the lack of new hospital entry, the closure of one hospital, and the acquisition of another by SwedishAmerican.

ANSWER: OSF admits that the FTC accurately quotes a portion of one sentence of the Court's opinion in *United States v. Rockford Memorial Hosp.,* 717 F. Supp. 1251 (N.D. Ill. 1989). OSF denies all of the remaining allegations of paragraph 36. The 1989 matter has no relevance here for the reasons summarized in OSF's answer to paragraph 20.

B.

Primary Care Physician Services Market

37. The Acquisition will reduce the number of hospital-employed physician groups from three to two in the Rockford region, and leave the remainder of the market highly fragmented with small independent physician practices. Under the relevant case law and the Merger Guidelines, the Acquisition raises significant competitive concerns in the primary care physician services market.

ANSWER: OSF admits that the Acquisition will reduce the number of hospital-employed physician groups from three to two in Rockford. OSF denies all of the remaining allegations of paragraph 37. Plaintiff overstates the competitive significance of the affiliation on the alleged primary care physician services market by ignoring the facts, among others, that primary care physicians can and do practice outside of a hospital-employed physician group, there are a significant number of primary care physicians who are not part of a hospital-employed physician group, and there are no significant barriers to new entry for primary care physicians.

38. The Acquisition will result in a concentrated primary care physician services market with few significant competitors. Based on the best currently-available data, OSF's post-

Acquisition market share will exceed 37%. Post-Acquisition, the two remaining hospitals, OSF and SwedishAmerican, will control 58% of the primary care physician services market in the Rockford region.

ANSWER: OSF denies the allegations of paragraph 38.

39. Under the Merger Guidelines, a merger or acquisition potentially raises significant competitive concerns that warrant scrutiny when the post-merger HHI exceeds 1500 points and the merger or acquisition increases the HHI by more than 100 points. Here, the post-Acquisition HHI in the primary care physician services market exceeds these levels by a wide margin, with an increase of 696 points to 1925. The HHI figures for the primary care physician services market are summarized in the table below.

PRIMARY CARE PHYSICIAN SERVICES*		
Hospital/System	**Pre-Acquisition Market Share**	**Post-Acquisition Market Share**
SwedishAmerican	20.4%	20.4%
OSFMG	19.9%	37.4%
RHPH	17.5%	-
University of Illinois	7.3%	7.3%
Others**	4.0%	4.0%
Independent***	30.9%	30.9%
	Pre-Acquisition HHI	1229
	Post-Acquisition HHI	1925
	HHI Increase	696

* Due to limitations in the preliminarily-available data, the primary care physician market shares and HHIs have been calculated on the basis of full-time-equivalent physicians practicing in a geographic market comprising Winnebago, Boone, and Ogle counties, which has a slightly different scope than the geographic market defined by the District Court in 1989.

** includes several small and mid-size physician groups

*** all independent physicians are treated as individual providers in HHI calculations

ANSWER: OSF admits that the Merger Guidelines, drafted by the FTC and the DOJ, discuss HHI and mergers and acquisitions. OSF refers to the complete Merger Guidelines for the contents thereof. OSF lacks knowledge or information sufficient to form a belief about the truth

of how the FTC performed its calculations of HHI for primary care physician services. OSF denies the remaining allegations in paragraph 39.

VI.

ANTICOMPETITIVE EFFECTS

A.

Loss of Price Competition And the Increased Bargaining Leverage of OSF

40. The Acquisition will end decades of significant competition between Respondents and will increase Respondents' ability and incentive to unilaterally demand higher reimbursement rates from commercial health plans.

ANSWER: OSF admits that it and RHS will no longer be independent competitors against each other following consummation of the transaction. OSF denies all of the remaining allegations of paragraph 40. MCOs and hospital systems negotiate reimbursement rates not just for general acute care inpatient services, but for outpatient services, physician services, and ancillary services as part of single negotiation (if not always a single contract). The parties focus on the estimated "total healthcare cost" of treating a MCO's insureds, not just the cost for inpatient or any other individual healthcare services. Non-price terms are a critical part of the negotiations as well. The complexity and scope of those negotiations eliminate any potential for the combined OSF/RHS to raise general acute care inpatient rates above competitive levels. MCOs also have leverage and bargaining power to resist any attempt by the combined OSF/RHS to raise prices above competitive levels. MCOs bring information to the bargaining table that healthcare providers lack, including knowledge of the rates they pay to the provider with which they are negotiating and that provider's competitors (which no other provider knows), and their insureds' historical utilization with that specific provider and the provider's competitors. This knowledge imbalance provides MCOs with bargaining leverage that the providers lack. Moreover, because of the growing underclass in Rockford, declining government reimbursement

rates and a smaller commercially-insured population, access to the MCOs' insured patients is critical to the hospital systems' financial stability. OSF and RHS cannot make up for the losses incurred in treating Medicare, Medicaid, and charity care patients without access to the commercial MCOs' insureds on an "in-network" basis. That is not true for the payors like BCBS IL, Humana, or United Healthcare, who do not need access to RHS or SAMC to be marketable or profitable. BCBS IL's take-it-or-leave-it negotiating strategy for physician reimbursement rates demonstrates this point: outside Chicago, BCBS IL has a statewide fee schedule for physician reimbursement rates from which it will not deviate or negotiate. More recently, the implementation of healthcare reform has changed and will radically change the way that healthcare providers and payors — both Government and MCOs — will negotiate with each other. There is and will continue to be a shift toward contracts that place more risk on providers for overall patient outcomes, rather than on MCOs. These shared savings and full risk arrangements that providers, including OSF, enter into are making fee-for-service reimbursement schedules increasingly irrelevant. In a risk contract, it is counterproductive for a provider to raise its fee-for-service reimbursement above competitive levels. The combined OSF-RHS will not have the ability or incentive to demand higher reimbursement rates as a result of the affiliation, and health plans will be able to offer a network consisting of all three Rockford hospitals and both hospital systems after the affiliation.

41. Today, the three Rockford hospitals are close and vigorous competitors in the markets for general acute-care services and primary care physician services. There is nearly complete overlap in the service areas of OSF, RHS, and SwedishAmerican. Rockford region residents and, by extension, the health plans that represent them, consider all three Rockford hospitals as close substitutes for one another due to their proximity and similar scope of services. Residents benefit from the competition between the three hospitals.

ANSWER: OSF admits that the three Rockford hospital systems are competitors, offer some duplication of services, and that there is some, not complete, overlap in the areas for

certain service lines of OSF, RHS, and SwedishAmerican. OSF denies that Rockford residents consider OSF and RHS to be close substitutes for each other; rather SwedishAmerican is the closest substitute for both OSF and RHS. OSF denies all of the remaining allegations of paragraph 41.

42. Rockford residents strongly prefer to have a choice of where they receive their health care services. As a result, every major health plan serving the Rockford region features a provider network with two of the three local hospitals as preferred providers. While health plans and their members might prefer to have access to all three Rockford hospitals, the hospitals provide discounts to health plans for contracting with only two Rockford hospitals.

ANSWER: OSF admits that some but not all Rockford residents prefer to have a choice of where they receive their health care services. OSF admits that it and RHS each at times provide discounts in return for expected increased patient volumes. OSF denies all of the remaining allegations of paragraph 42. Certain health plans, such as The Alliance, offer all three Rockford hospital systems as in-network providers. In addition, members of Blue Cross Blue Shield of Illinois (OSF's largest commercial payor) can obtain services at in-network rates at all three Rockford hospitals. In contrast, Blue Cross' HMO-I is a one-system network in Rockford with only SwedishAmerican in the network. The composition of a managed care organization's network is determined solely by the managed care organization, based on its strategic marketing approach, access, price, and other factors. Typically, the narrower the network, the greater the steerage and the deeper the provider discounts, while the broader the network, the less steerage there is and provider discounts are often lower. OSF also has offered discounts to health plans which have all three Rockford-based systems as in-network providers.

43. Currently, the three Rockford hospitals must compete vigorously — often through a competitive bidding process — to be included in each health plan's provider network. Due to the similarity and close substitutability of the three Rockford hospitals, health plans today believe they can build a marketable network with any two of the hospitals. As a result, the three Rockford hospitals compete for just two spots in each health plan's network, each hospital being forced to provide competitive rates or else risk exclusion from a health plan's network.

ANSWER: OSF admits that each of the three Rockford hospital systems negotiate to be included in the provider networks of some of the health plans which provide coverage in Rockford. OSF lacks knowledge or information sufficient to form a belief about the truth of the allegations about what health plans today believe as alleged in the second sentence. OSF denies all of the remaining allegations of paragraph 43. Certain health plans, such as The Alliance, offer all three Rockford hospital systems as in-network providers. In addition, members of Blue Cross Blue Shield of Illinois (OSF's largest commercial payor) can obtain services at in-network rates at all three Rockford hospitals. In contrast, Blue Cross' HMO-I is a one-hospital system network in Rockford with only SwedishAmerican in the network. The composition of a managed care organization's network is determined solely by the managed care organization, based on its strategic marketing approach, access, price, and other factors. Typically, the narrower the network, the greater the steerage and the deeper the provider discounts, while the broader the network, the less steerage there is and provider discounts are often lower. OSF also has offered discounts to health plans which have all three Rockford-based systems as in-network providers.

44. Nothing about the Acquisition will change the high value and importance that Rockford residents place on being able to choose their doctors and hospitals. Residents will continue to demand health plan provider networks that include at least two of the three Rockford hospitals, as they have for decades.

ANSWER: OSF admits that some Rockford residents place a value on being able to choose their doctors and/or hospitals, but denies that all do so. OSF denies the remaining allegations of paragraph 44. OSF and RHS will continue to have two hospital facilities after the affiliation, plus SwedishAmerican has a second hospital in Belvidere. After the affiliation, just as today, Rockford residents will not necessarily demand hospital networks that include both Rockford hospital systems.

45. After the Acquisition, no health plan will be able to offer its members access to more than one of the Rockford hospitals without first agreeing to whatever terms the merged

OSF and RHS may demand. As a result, the merged system will become even more important to health plans serving the Rockford region and thus become a virtual "must have." Health plans will no longer be able to play the three Rockford hospitals against one another. They will have to choose between contracting only with SwedishAmerican, which would restrict their members' choices and options, or accepting significantly higher reimbursement rates demanded by the newly dominant OSF.

ANSWER: OSF denies the allegations of paragraph 45. MCOs and hospital systems negotiate reimbursement rates not just for general acute care inpatient services, but for outpatient services, physician services, and ancillary services as part of single negotiation (if not always a single contract). The parties focus on the estimated "total healthcare cost" of treating a MCO's insureds, not just the cost for inpatient or any other individual healthcare services. Non-price terms are a critical part of the negotiations as well. The complexity and scope of those negotiations eliminate any potential for the combined OSF/RHS to raise general acute care inpatient rates above competitive levels. MCOs also have leverage and bargaining power to resist any attempt by the combined OSF/RHS to raise prices above competitive levels. MCOs bring information to the bargaining table that healthcare providers lack, including knowledge of the rates they pay to the provider with which they are negotiating and that provider's competitors (which no other provider knows), and their insureds' historical utilization with that specific provider and the provider's competitors. This knowledge imbalance provides MCOs with bargaining leverage that the providers lack. Moreover, because of the growing underclass in Rockford, declining government reimbursement rates and a smaller commercially-insured population, access to the MCOs' insured patients is critical to the hospital systems' financial stability. OSF and RHS cannot make up for the losses incurred in treating Medicare, Medicaid, and charity care patients without access to the commercial MCOs' insureds on an "in-network" basis. That is not true for the payors like BCBS IL, Humana, or United Healthcare, who do not need access to RHS or SAMC to be marketable or profitable. BCBS IL's take-it-or-leave-it

negotiating strategy for physician reimbursement rates demonstrates this point: outside Chicago, BCBS IL has a statewide fee schedule for physician reimbursement rates from which it will not deviate or negotiate. More recently, the implementation of healthcare reform has changed and will radically change the way that healthcare providers and payors — both Government and MCOs — will negotiate with each other. There is and will continue to be a shift toward contracts that place more risk on providers, rather than on MCOs, based upon overall patient outcomes. These shared risk and full risk arrangements that providers, including OSF, enter into are making fee-for-service reimbursement schedules increasingly irrelevant. In a risk contract, it is counterproductive for a provider to raise its fee-for-service reimbursement above competitive levels. The combined OSF-RHS will not have the ability or incentive to demand higher reimbursement rates as a result of their affiliation, and health plans will be able to offer a network consisting of both hospital systems after the affiliation.

46. Any increase in rates ultimately will be borne by the employers and residents of Rockford through increased insurance premiums and health care costs. The majority of commercially insured patients in the Rockford region are covered by health plans that are self-insured by their employers. Self-insured employers pay the full cost of their employees' health care claims and, as a result, they immediately and directly bear the full burden of higher rates charged by hospitals or physicians. Fully-insured employers also are inevitably harmed by higher rates, because health plans pass on at least a portion of hospital rate increases to these customers.

ANSWER: OSF lacks knowledge or information sufficient to form a belief about the truth of the allegations in the second sentence of paragraph 46. OSF denies all of the remaining allegations of paragraph 46. Costs to employers and health plan members are not "inextricably linked" to reimbursement rates that health plans negotiate with each provider, because the health plan can decide how to price its products in light of any changes in reimbursement rates, and employers can decide whether and to what degree they will charge employees for premiums and other out-of-pocket costs independent of provider reimbursement rates. Self-insured employers

do not assume all risk for the costs of healthcare provided to their employees because many purchase excess or umbrella insurance policies that limit liability. Self-insured employers do not necessarily "immediately" incur any hospital rate increases, and because of excess or umbrella insurance may not "fully" incur the cost of such increases.

47. Employers, in turn, will pass on their increased health care costs to their employees, in whole or in part. Employees will bear these costs in the form of higher premiums, higher co-pays, reduced coverage, or restricted services. Some Rockford region residents will forgo or delay necessary health care services because of the higher costs, and others may drop their insurance coverage altogether.

ANSWER: OSF lacks knowledge or information sufficient to form a belief about the truth of the allegations of paragraph 47.

48. OSF could also exercise its newly acquired market power after the Acquisition by preventing health plans from including SwedishAmerican in their provider networks. The effect would be to eliminate entirely the ability of Rockford residents who want access to either OSF or RHS from also utilizing SwedishAmerican without incurring higher out-of-network costs. In Peoria, a market south of Rockford where OSF is already a self-acclaimed "dominant player," OSF has successfully leveraged its market position to exclude its primary competitor from key health plans.

ANSWER: OSF denies the allegations of paragraph 48. The effect of the OSF-RHS affiliation will not eliminate the ability of Rockford residents to use SwedishAmerican without incurring higher out-of-network costs because, among other things, certain health plans, such as The Alliance, offer all three Rockford hospital systems as in-network providers and all health plans will be able to designate which providers they want in their networks. In addition, members of Blue Cross Blue Shield of Illinois (OSF's largest commercial payor) can obtain services at in-network rates at all three Rockford hospitals even though one of the hospitals is not in-network. In contrast, Blue Cross' HMO-I is a one-hospital network in Rockford with only SwedishAmerican in the network. The composition of a managed care organization's network is determined solely by the managed care organization, based on its strategic marketing approach, access, price and other factors. Typically, the narrower the network, the greater the steerage

while the deeper the provider discount, and the broader the network, the less steerage there is and provider discounts are often lower. The importance of the health plans to OSF, and the power of the health plans, as summarized in OSF's answer to paragraph 45, will prevent the combined entity from excluding any other provider.

49. Respondents' documents created in the ordinary course of business indicate that the managed care strategies of the parties encourage "capturing market share," with the ultimate goal to "build leverage" and become a "must have" system to health plans. Party executives concede that one motivation for the Acquisition was "to become bigger, to at least reclaim some leverage" against the health plans.

ANSWER: OSF admits that the phrases quoted in the first sentence of paragraph 49 are contained in one or more documents produced by a Respondent to the FTC. OSF denies the characterization of these phrases which are quoted out of context and denies all other allegations contained in paragraph 49, except that as to the second sentence of paragraph 49, OSF admits that the FTC has accurately quoted a snippet of one sentence of testimony by one of the executives of OSF-Saint Anthony Medical Center. But his full testimony in this regard was as follows:

> Q. And does that maintain your leverage or even increase it within health plans?
>
> A. It may, it may increase it somewhat, because we'll be a larger organization. But once again, when you're dealing with -- leverage, let's talk about that. This much of our business is Medicare, okay?
>
> MS. KURCZEWSKI: I just want the record to show.
>
> THE WITNESS: I'm sorry, I am making a big global-shaped thing with my hands. This much is Medicare. The rates are set. I am now making a smaller global thing, but not a small thing, this much is Medicaid, those rates are set. This, and I'm making a smaller one, is charity care, and it's getting bigger. Don't have set rates there, because nobody's paying you for anything. There's a very small universe of stuff left that we're competing over, and that universe is now being controlled increasingly by mega

> insurance plans. So, yeah, if we get a little more leverage, that would be a good thing, because it's going away every day.

50. Although SwedishAmerican will continue to act as a meaningful competitor in the Rockford region, the presence of SwedishAmerican will not prevent a post-Acquisition exercise of market power by OSF — whether it is in the form of a rate increase or exclusionary conduct. Because Rockford residents demand health plan networks that offer at least two Rockford hospitals, a network comprised exclusively of SwedishAmerican would be highly undesirable to employers and thus unlikely to have commercial success. Recent history confirms this: virtually every attempt by a health plan to market a provider network consisting of just one Rockford hospital — including one exclusive to SwedishAmerican — has failed.

ANSWER: OSF admits that following the affiliation of OSF and RHS SwedishAmerican will continue to act as a meaningful competitor to the combined entity. OSF denies all of the remaining allegations of paragraph 50. Based upon historical experience, current product offerings in Rockford, and the opinions of a number of employers, a network with only SwedishAmerican as a Rockford in-network provider would be marketable.

51. The Acquisition also will significantly increase OSF's ability to unilaterally increase rates for primary care physician services. Hospitals and health plans engage in bilateral negotiations to create networks of physicians much like they do to create networks of hospitals. Similar competitive factors dictate the outcomes of negotiations over physician services as dictate the outcomes of negotiations over hospital services. As is the case with the three Rockford hospitals, Rockford residents consider the primary care physician groups of the three local hospitals as close substitutes for each other. Therefore, the Acquisition will strengthen OSF's bargaining leverage against health plans when it is negotiating the terms of including OSFMG and RHPH physicians in the health plans' provider networks.

ANSWER: OSF denies the allegations of paragraph 51. Rockford area residents do not consider OSF and RHS to be close substitutes for each other; rather SwedishAmerican is the closest substitute for both OSF and RHS. Negotiations concerning physician reimbursements and in-patient care reimbursement generally take place at the same time. MCOs and hospital systems negotiate reimbursement rates not just for general acute care inpatient services, but for outpatient services, physician services, and ancillary services as part of single negotiation (if not always a single contract). The parties focus on the estimated "total healthcare cost" of treating a MCO's insureds, not just the cost for primary care physician services or any other individual

health care services. Non-price terms are a critical part of the negotiations as well. The complexity and scope of those negotiations eliminate any potential for the combined OSF/RHS to raise primary care physician rates above competitive levels. MCOs also have leverage and bargaining power to resist any attempt by the combined OSF/RHS to raise prices above competitive levels. MCOs bring information to the bargaining table that healthcare providers lack, including knowledge of the rates they pay to the provider with which they are negotiating and that provider's competitors (which no other provider knows), and their insureds' historical utilization with that specific provider and the provider's competitors. This knowledge imbalance provides MCOs with bargaining leverage that the providers lack. Moreover, because of the growing underclass in Rockford, declining government reimbursement rates and a smaller commercially-insured population, access to the MCOs' insured patients is critical to the hospital systems' financial stability. OSF and RHS cannot make up for the losses incurred in treating Medicare, Medicaid, and charity care patients without access to the commercial MCOs' insureds on an "in-network" basis. That is not true for the payors like BCBS IL, Humana, or United Healthcare, who do not need access to RHS or SAMC to be marketable or profitable. Blue Cross Blue Shield of Illinois, OSF's largest commercial payor, does not negotiate whatsoever with OSF concerning physician reimbursement rates, effectively adopting a "take it or leave it" approach. More recently, the implementation of healthcare reform has changed and will radically change the way that healthcare providers and payors — both Government and MCOs — will negotiate with each other. There is and will continue to be a shift toward contracts that place more risk on providers, rather than MCOs, based upon overall patient outcomes. These shared risk and full risk arrangements that providers, including OSF, enter into are making fee-for-service reimbursement schedules increasingly irrelevant. In a risk contract, it is counterproductive for a

provider to raise its fee-for-service reimbursement above competitive levels. The combined OSF/RHS will not be able to demand higher rates as a result of their affiliation, and health plans will be able to offer a network consisting of both hospital systems after the affiliation.

B.

The Acquisition will Reduce Competition Over Quality, Service, and Access

52. Residents of the Rockford region have benefitted from decades of competition between OSF and RHS to improve the quality of care, increase the scope of services, and expand access to care in the Rockford region. The Acquisition would end this important non-price competition between OSF and RHS and reduce the quality, convenience, and breadth of services local residents would otherwise enjoy.

ANSWER: OSF admits that it and RHS will no longer will be independent competitors of each other upon completion of the affiliation. OSF denies all of the remaining allegations of paragraph 52.

53. After decades of Respondents' self-described "heavy competition," all three Rockford hospitals today offer convenient access to a broad range of high quality clinical services. And despite the costs incurred to invest in new technologies and improve the quality of care over the years, all three Rockford hospitals have been, and continue to be, financially stable organizations with positive operating performances and substantial cash reserves.

ANSWER: OSF admits that all three Rockford hospital systems compete and offer some duplicative services. OSF lacks knowledge or information sufficient to form a belief about the truth of the allegations concerning SwedishAmerican's financial condition. OSF denies all of the remaining allegations of paragraph 53. OSF's SAMC has incurred operating losses in each of the last three fiscal years and has not been able to undertake all of the capital projects it needs.

54. RHS, described as a "first mover" and "market disrupter" when it comes to expanding its services or improving its technology, repeatedly spurred OSF and SwedishAmerican to respond by upgrading their own offerings. The Acquisition would eliminate RHS as an independent competitor in the Rockford region and would thereby eliminate a competitive force behind much of the innovation and expansion that has benefitted local residents over the years.

ANSWER: OSF lacks knowledge or information sufficient to form a belief about the truth of the allegations concerning the quoted phrases in the first sentence of paragraph 54. OSF admits that after the Affiliation, RHS will no longer be an independent competitor in Rockford. OSF denies all the remaining allegations of paragraph 54. The affiliated entity will be in a stronger position to innovate and expand services than either is in currently.

C.

The Acquisition Will. Increase the Incentive and Ability to Coordinate

55. The Acquisition also will diminish competition by enabling and encouraging OSF and its sole remaining competitor in the Rockford region, SwedishAmerican, to engage in coordinated interaction.

ANSWER: OSF denies the allegations of paragraph 55. OSF and SwedishAmerican do not have access to each other's reimbursement arrangements with MCOs, have not engaged in coordinated interaction, and will not do so in the future.

56. As the Seventh Circuit held in affirming the Commission's divestiture order in a prior hospital merger matter: "[t]he fewer the independent competitors in a hospital market, the easier they will find it, by presenting an unbroken phalanx of representations and requests, to frustrate efforts to control hospital costs."

ANSWER: OSF lacks knowledge or information sufficient to form a belief about the truth of the allegation about the quoted material from an unidentified judicial opinion, and denies all of the remaining allegations of paragraph 56.

57. According to the Merger Guidelines, coordination need not rise to the level of explicit agreement. It may involve a "common understanding that is not explicitly negotiated[,]" or even merely "parallel accommodating conduct not pursuant to a prior understanding."

ANSWER: OSF admits that the FTC has accurately quoted parts of sentences in the Merger Guidelines, which were drafted by the FTC and the DOJ, and refers to the Merger Guidelines in their entirety concerning their content on the subject of coordination. OSF denies all of the remaining allegations of paragraph 57.

58. The market structure and competitive dynamics in the Rockford region today are materially unchanged since the District Court found in 1989 that a merger of two of the Rockford hospitals would facilitate the likelihood of collusion among the two remaining hospital competitors. The acquisition of RHS by OSF, the latest proposed merger to duopoly in the Rockford region, is no less likely to result in coordinated interaction.

ANSWER: OSF denies the allegations of paragraph 58. The 1989 matter has no relevance here for the reasons summarized in OSF's answer to paragraph 20.

59. OSF and SwedishAmerican would have the incentive and ability to coordinate their managed care contracting strategies post-Acquisition, for example, by communicating confidential information related to health plan negotiations, either by directly contacting each other or by otherwise signaling their intentions. The two remaining hospitals could also defer competitive initiatives, such as adding amenities or expanding services, which would otherwise benefit Rockford residents. Indeed, Respondents' ordinary course documents suggest that hospital executives in the Rockford region communicate directly and indirectly in order to exchange sensitive information about strategic initiatives and health plan negotiations.

ANSWER: OSF denies the allegations of paragraph 59. OSF and SwedishAmerican do not have access to each other's reimbursement arrangements with MCOs, have not engaged in unlawful coordinated interaction, and will not do so in the future.

VII.

ENTRY BARRIERS

60. Neither hospital entry nor expansion by the sole remaining hospital competitor will deter or counteract the Acquisition's likely harm to competition in the relevant service markets.

ANSWER: OSF denies the allegations of paragraph 60. SwedishAmerican is the largest, fastest growing health system in Rockford, and its lead over OSF and RHS is increasing. In addition, OSF and RHS face increasing competition from hospitals outside of Rockford to provide tertiary and quarternary services to Rockford-area residents.

61. New hospital entry or significant expansion in the Rockford region is unlikely to occur because Illinois' Certificate of Need ("CON") statute requires an extensive application process in order to construct a hospital, add acute care beds or new clinical services to an existing hospital, or to purchase medical equipment above a capital threshold. The CON approval process is focused on the number of hospital beds per capita; the process does not contemplate or permit consideration of antitrust or competition concerns. Based on the most

recent findings of the Illinois Health Facilities and Services Review Board responsible for reviewing CON applications, any request to construct a new acute care hospital in the Rockford region is likely to be denied because the board does not believe Rockford needs any additional beds.

ANSWER: OSF admits that Illinois' Certificate of Need ("CON") statute requires an application process to add a variety of inpatient hospital-based healthcare services and sets forth a variety of criteria required to be considered pursuant to a CON application; OSF refers to that statute in its entirety for its requirements. OSF lacks knowledge or information sufficient to form a belief about the truth of the allegation about what the Illinois Health Facilities and Services Review Board is likely to do with respect to future CON applications in Rockford. OSF denies all of the remaining allegations of paragraph 61.

62. Even if new hospital entry did occur in the Rockford region, such entry would not be timely because it would take at least two to five years from the planning stages to opening doors to patients. New entry is also unlikely to be sufficient to deter or counteract the anticompetitive effects of the Acquisition because a new hospital would need to be able to replicate and offer a broad cluster of general acute-care inpatient services comparable to those offered by OSF and SwedishAmerican.

ANSWER: OSF lacks knowledge or information sufficient to form a belief about the truth of the allegations concerning the time it would take for an unidentified third party to develop a new hospital. OSF denies all of the remaining allegations of paragraph 62. SwedishAmerican is the largest, fastest growing health system in Rockford, and its lead over OSF and RHS is increasing. In addition, OSF and RHS face increasing competition from hospitals outside of Rockford to provide tertiary and quarternary services to Rockford-area residents.

63. New primary care physician entry is unlikely because most physicians in Rockford are already employed by one of the three hospitals. Further, the number of independent primary care physicians is declining because hospitals offer stability and generous benefits, while self-managing a private physician practice is costly and time-consuming. As a result, there has been very little to no entry of independent primary care physicians into the Rockford region in the last several years.

ANSWER: OSF denies the allegations of paragraph 63. There are no substantial barriers to entry for primary care physicians.

64. New competition from currently-employed Rockford physicians who leave to open a private practice is unlikely to occur, and in any event would not be timely to deter or prevent competitive harm, in part because all three Rockford hospitals require their employed physicians to sign non-compete agreements that prohibit them from practicing in or around Rockford for at least two years.

ANSWER: OSF admits that it has required some of its employed physicians to sign non-compete agreements. OSF lacks knowledge or information sufficient to form a belief about the truth of this allegation with respect to RHS or SwedishAmerican. OSF denies all of the remaining allegations of paragraph 64.

VIII.

EFFICIENCIES

65. Respondents' alleged benefits of the Acquisition fall well short of the substantial, merger-specific, well-founded, and competition-enhancing efficiencies that would be necessary to outweigh the Acquisition's significant harm to competition in Rockford. No court ever has found, without being reversed, that efficiencies rescue an otherwise illegal transaction. Relevant case law indicates that "extraordinary" efficiencies are required to justify an acquisition, such as this one, with vast potential to harm competition.

ANSWER: OSF denies the allegations of paragraph 65. The efficiencies and increased quality of care that will result from the affiliation are not speculative, but are identified in detail and are merger-specific. These efficiencies will enhance the procompetitive effects of the Affiliation.

66. The alleged efficiencies are unfounded and unreliable. Respondents have refused to answer questions or reveal underlying data and analysis in support of their claims on the grounds that such material was prepared under the direction of antitrust counsel in anticipation of litigation, and thus constitutes attorney work product. The made-for-litigation efficiency claims, therefore, were unambiguously "generated outside of the usual business planning process." Even an analysis based on the information available to date reveals that Respondents' efficiency claims are speculative, exaggerated, and contradicted by the testimony of party executives.

ANSWER: OSF denies the allegations of paragraph 66. Respondents answered many questions about the efficiencies they project that the affiliation will generate, including presenting SAMC's CEO for a full day of testimony solely on that subject. The efficiencies and increased quality of care that will result from the affiliation are not speculative, but are identified in detail, and are merger-specific. These efficiencies will enhance the procompetitive effects of the Affiliation.

67. Many of the alleged efficiencies also are not merger-specific because they could be accomplished unilaterally without any merger or acquisition, or through an affiliation with an alternative purchaser. The same litigation consultants who generated the estimates of the savings that may result from the Acquisition produced two separate reports detailing tens of millions of dollars in annual savings that RHS and OSF could accomplish on their own.

ANSWER: OSF denies the allegations of paragraph 67. The efficiencies and increased quality of care that will result from the affiliation are not speculative, but are identified in detail, and are merger-specific. These efficiencies will enhance the procompetitive effects of the Affiliation. The projected savings which each hospital could accomplish on its own were part of a "sales pitch" to obtain additional work, not the result of a detailed, comprehensive study, and the savings were separate and apart from those in the detailed, comprehensive study completed in December 2010.

68. Any claim that the Acquisition is necessary for the parties to survive or continue to compete as full-service independent hospitals is speculative and unsupported by market realities. In fact, RHS and SwedishAmerican made similar claims to the District Court in 1989, and OSF and SwedishAmerican repeated them again during an effort to merge in 1997. Despite their repeated dire predictions, OSF, RHS, and SwedishAmerican have continued to compete successfully over the course of the last two decades and, today, each remains a financially stable, full-service hospital providing high-quality care to the community.

ANSWER: OSF admits that it and SwedishAmerican showed efficiencies in connection with their proposed affiliation in 1997, which affiliation was approved by the DOJ. OSF admits that it, RHS, and SwedishAmerican are competing hospital systems. OSF denies all of the remaining allegations of paragraph 68. The 1989 matter has no relevance here for the

reasons summarized in OSF's answer to paragraph 20. In contrast, the decision by the DOJ to approve the proposed affiliation eight years later, in 1997, is instructive, and the weakened economic conditions in Rockford and the changes in the delivery of healthcare since 1997 reinforce the DOJ's decision in 1997.

IX.

VIOLATION

COUNT I - ILLEGAL ACQUISITION

69. The allegations of Paragraphs 1 through 68 above are incorporated by reference as though fully set forth.

ANSWER: OSF incorporates its answers to paragraphs 1 through 68 above as if fully set forth herein.

70. The Acquisition, if consummated, would substantially lessen competition in the relevant markets in violation of Section 7 of the Clayton Act, as amended, 15 U.S.C. § 18.

ANSWER: OSF denies the allegations of paragraph 70.

WHEREFORE, respondent OSF Healthcare System respectfully requests that the Administrative Law Judge (1) dismiss the Complaint in its entirety with prejudice; (2) deny the FTC all of its requested relief; (3) award OSF its costs of suit, including attorneys' fees; and (4) grant it such other and further relief as the Administrative Law Judge deems just and proper.

December 12, 2011

Respectfully submitted,

OSF HEALTHCARE SYSTEM

By: /s/Alan I. Greene
One of Its Attorneys

Alan I. Greene
Matthew J. O'Hara
Kristin M. Kurczewski
Hinshaw & Culbertson LLP
222 N. LaSalle, Suite 300
Chicago, IL 60601
(312) 704-3000
agreene@hinshawlaw.com
mohara@hinshawlaw.com
kkurczewski@hinshawlaw.com

Michael F. Iasparro
Hinshaw & Culbertson LLP
100 Park Avenue
Rockford, IL 61105
(815) 490-4900
miasparro@hinshawlaw.com

CERTIFICATE OF SERVICE

I hereby certify that on this 12th day of December, 2011, a copy of OSF Healthcare System's Answer to Complaint was served on the following via electronic mail:

Matthew J. Reilly
Jeffrey H. Perry
Kenneth W. Field
Federal Trade Commission
600 Pennsylvania Ave., N.W.
Washington, D.C. 20580

mreilly@ftc.gov
jperry@ftc.gov
kfield@ftc.gov

Attorneys for Plaintiff Federal Trade Commission

David Marx, Jr.
William P. Schuman
Amy J. Carletti
McDermott Will & Emery LLP
227 West Monroe Street
Chicago, IL 60606
Telephone: (312) 372-2000
Facsimile: (312) 984-7700
dmarx@mwe.com
wschuman@mwe.com
acarletti@mwe.com

Attorneys for Defendant Rockford Health System

Donald S. Clark
Office of the Secretary
Federal Trade Commission
600 Pennsylvania Avenue, NW, H-113
Washington, DC 20580

I hereby certify that on this 12th day of December, 2011, a copy of OSF Healthcare System's Answer to Complaint was served via hand delivery upon:

The Honorable D. Michael Chappell
Chief Administrative Law Judge
Federal Trade Commission
600 Pennsylvania Avenue, NW, H-110
Washington, DC 20580

/s/Alan I. Greene
Attorney for OSF Healthcare System