AMA AMERICAN MEDICAL ASSOCIATION

CMA California Medical Association
Physicians dedicated to the health of Californians

October 26, 2009

Honorable Ronald M. George, Chief Justice
and Honorable Associate Justices
California Supreme Court
350 McAllister Street
San Francisco, California 94102

Re: Letter of Amici Curiae in Support of Petition for Review
Henstorf v. State Compensation Insurance Fund, Supreme Court No. S176974
(2nd App. Dist. No. B210943)

Dear Chief Justice George and Associate Justices:

Pursuant to rule 8.500(g) of the California Rules of Court, the American Medical Association ("AMA") and the California Medical Association ("CMA") (collectively, "Amici") urge the Court to grant review in this case, for the following reasons.

A. Amici are Concerned that the Lower Court's Decision Immunizes Blatantly Anticompetitive Conduct.

The AMA, an Illinois not-for-profit corporation, is the largest organization of physicians, residents, and medical students in the United States. Its objects are "to promote the science and art of medicine and the betterment of public health." Its members practice in all areas of medical specialization and in every state, including California.[1]

The CMA is a non-profit, incorporated professional association of approximately 35,000 physicians practicing in the State of California. CMA's membership includes California physicians engaged in the private practice of medicine in all specialties. CMA's primary purposes are "to promote the science and art of medicine, the care and well-being of patients, the protection of public health and the betterment of the medical profession." CMA and its members share the objective of promoting high quality, cost-effective health care for

[1] Amici appear herein on their own behalves and as representatives of the Litigation Center of the American Medical Association and the State Medical Societies. The Litigation Center is a coalition of the AMA and the state medical societies of every state and the District of Columbia. Its purpose is to represent the general interests of the medical profession in the courts, according to AMA policy.

the people of California.

Amici urge this Court to review the lower court's decision because it widens the gulf between the law in two California appellate court districts, the First and Second Appellate Districts. In the First Appellate District, the conduct of bargaining units formed under the statutes applicable in this case is regulated by California antitrust law. (These statutes are Business and Professions Code section 16770(g) ("section 16770(g)"), Health and Safety Code section 1342.6 ("section 1342.6"), and/or Insurance Code section 10133.6 ("section 10133.6") (collectively referred to as the "statutes")). But, as a result of the lower court's decision, the conduct of such bargaining units within the Second Appellate District continues to be exempt from California antitrust law. The California Supreme Court needs to resolve this conflict and to adopt the First Appellate District's interpretation—the one that the California Legislature clearly intended. This Court's review is also crucial because California insurance markets are concentrated and the lower court's opinion will allow health insurers to exercise market power in physician markets. This will have the effect of depressing physician reimbursements below competitive levels, and will endanger access to patient care.

B. This Court should Grant Review to Resolve a Conflict that Exists in California Appellate Districts Concerning Whether the Statutes Provide Absolute Immunity from Antitrust Liability.

A conflict exists between the First and Second Appellate Districts regarding whether or not the statutes confer absolute antitrust immunity on contracting units purportedly formed under those statutes. In the last opinion, the Second Appellate District held that the statutes immunized a contracting unit created by the arrangement between Blue Cross of California ("BCC") and the State Compensation Insurance Fund ("SCIF") from *any* antitrust liability. In reaching this conclusion, the Second Appellate District relied on *Lori Rubinstein Physical Therapy, Inc., v. PTPN, Inc.*, 148 Cal. App. 4th 1130 (2007) ("*Rubinstein*"). The question the *Rubinstein* court faced was whether preferred provider contracts between PTPN, a network of physical therapy practices, and BCC were immune from the antitrust allegations of physical therapy practices that had been excluded from those contracts. The *Rubinstein* court found that the statutes immunized the contractual arrangements of PTPN and BCC from *any* antitrust liability.

However, in *Reynolds v. California Dental Service*, 200 Cal. App. 3d 590 (1988), the First Appellate District reached a contrary result. There, the plaintiffs alleged that a dental health service plan, California Dental Service ("CDS"), was formed in order to unlawfully fix prices for dental services. *Id.* at 595-596. Although the *Reynolds* court ruled that sections

16770(g) and 1342.6 authorized the creation of provider-controlled contracting units like CDS despite their potential for competitive harm, the court did *not* hold that sections 16770(g) and 1342.6 absolutely immunized CDS from antitrust liability. Instead, the First Appellate District concluded that CDS' anticompetitive effects were to be evaluated under the rule of reason. Underlying the First Appellate District's conclusion was a recognition that "[s]ince the Legislature intended to authorize the formation of groups such as CDS, and given its directive that such arrangements be considered 'presumptively legitimate enterprises,' the Legislature apparently contemplated that antitrust challenges to health care provider groups" formed under the statutes "would be judged under the rule of reason" as opposed to the more rigorous per se rule. *Id.* at 599-600; *see Arizona v. Maricopa County Medical Society*, 457 U.S. 332 (1982). And, contrary to the Second Appellate District, the First Appellate District's interpretation of sections 16770(g) and 1342.6 is consistent with the California Supreme Court's pronouncements that antitrust exemptions are not favored. *See, e.g., Cianci v. Superior Court*, 40 Cal. 3d 903, 923 (1985) (stating that there is "a heavy presumption against implicit exemptions" to the Cartwright Act [Business and Professions Code section 16700 *et seq.*], and citing *Marin County Bd. Of Realtors, Inc. v. Palsson*, 16 Cal. 3d 920, 927-28 (1976), for the proposition that "the Legislature intended to exclude from the [Cartwright] Act only what the Act expressly excludes").

Amici urge this Court to resolve the conflict between the First and Second Appellate Districts by adopting the First Appellate District's interpretation of the statutes—an interpretation that is not only faithful to the California Supreme Court's pronouncements that antitrust exemptions are disfavored, but an interpretation that the California Legislature clearly intended.

C. The Legislature Intended that Horizontal Price Fixing Agreements between Insurers are to be Subject to Antitrust Rule of Reason Analysis.

The statutes were enacted as pro-competitive legislation designed to encourage the development of preferred provider organizations (PPOs). *See Rubinstein*, 148 Cal. App. 4th at 136-1137. More specifically, just as PPOs were being formed in California in response to California legislation enacted in 1982 that permitted their creation, the U.S. Supreme Court decided *Maricopa*. The *Maricopa* court ruled that a physician-sponsored PPO engaged in a per se illegal price fixing conspiracy when it set the maximum fees its member physicians could charge insurers. Proponents of AB 707, which became the statutes, believed that *Maricopa* was having a chilling effect on PPO formation. Proponents of AB 707 argued that this chilling effect occurred because opponents of particular PPOs were using *Maricopa* to bring, or threaten to bring, per se antitrust allegations against those who had formed, or were considering forming, PPOs. The State of California attempted to rectify this problem by

enacting the statutes. For example, section 16770(g) states:

> It is the intent of the Legislature, therefore, that the formation of groups and combinations of providers and purchasing groups for the purpose of creating efficient-sized contracting units be recognized as the creation of a new product within the health care marketplace, and be subject, therefore, only to those antitrust prohibitions applicable to the conduct of other presumptively legitimate enterprises.

Sections 1342.6 and 10133.6 contain language virtually identical to section 16770(g). *See Rubinstein*, 148 Cal. App. 4th at 355.

The legislative history of AB 707 demonstrates that the statutes were intended to protect contracting units formed under the statutes from the application of the per se antitrust rule used in *Maricopa*. For example, the August 19, 1985, report from the Senate Committee on the Judiciary concerning AB 707 noted that AB 707 was intended to "require state courts to use the *rule of reason*, instead of the illegal *per se* standard, in any antitrust litigation challenging the formation of groups or combinations of health care providers and insurers." That same report also stated that, "[a]ccording to the author's office, the bill [AB 707] is intended to require any health care combination challenged under the Cartwright Act to be gauged by the rule of reason test, and not deemed to be illegal per se," and that "for antitrust actions which challenge health care combinations...the business practice would be measured by the rule of reason test rather than being deemed, as under federal law, illegal per se." The Senate Committee report also added that the sponsor of AB 707:

> argues that the *Maricopa* court prematurely condemned health care combinations as illegal price fixing and per se violations of the Sherman Act, and that the more proper standard for assessing these arrangements (which he believes to offer significant benefits and to be procompetitive) is the rule of reason test.

The California Governor's veto of the 1984 version of AB 707, when considered in conjunction with 1985 correspondence between the Governor and AB 707's sponsor, also strongly supports the argument that the statutes were intended only to provide protection from *per se* antitrust analysis. At the time of the Governor's 1984 veto, the enrolled version of AB 707 contained the following language:

> It is the intent of the Legislature, therefore, that the formation of groups and combinations of providers and purchasing groups for the purpose of creating

> efficient-sized contracting units be recognized as the creation of a new product within the health care marketplace and, for that reason and to that extent, be *exempt* from state and federal antitrust laws. (*Italics added.*)

The 1984 version of AB 707 was intended to provide a blanket antitrust *exemption* for contracting units formed under the statutes. The Governor's veto message stated that although AB 707 was intended to "overcome the objections" set forth in *Maricopa*, *i.e.*, the *per se* application of the antitrust laws to PPOs, the Governor vetoed AB 707 because AB 707 did not "meet the tests as set forth in *Maricopa*." In other words, the Governor vetoed AB 707 because the bill exempted contracting units from potential antitrust liability under *both* the *per se* and rule of reason tests.

In response to the Governor's 1984 veto message, the 1985 California legislative session saw the introduction of a revised AB 707. The 1984 and 1985 versions of AB 707 differed substantively in only one respect—the 1985 version of AB 707 abandoned any reference to an antitrust exemption. In place of exemption language, enacted AB 707 stated:

> It is the intent of the Legislature, therefore, that the formation of groups and combinations of providers and purchasing groups for the purpose of creating efficient-sized contracting units be recognized as the creation of a new product within the health care marketplace, and be subject, therefore, only to those antitrust prohibitions applicable to the conduct of other presumptively legitimate enterprises.

The 1985 version of AB 707 removed any reference to an antitrust exemption in order to address the Governor's concern that the statutes should not provide a blanket exemption from antitrust liability. That the California Legislature did not intend the statutes to provide absolute immunity from antitrust liability also is shown in AB 707's sponsor's 1985 correspondence to the Governor subsequent to AB 707's legislative passage. AB 707's sponsor wrote, in part:

> When last year's version of Assembly Bill 707 came to you, it took a totally different approach from this year's legislation.
>
> After your veto message, I spent some time attempting to develop an approach which would avoid the complications of immunity from anti-trust law. I believe that the approach contained in this year's version of AB 707 will satisfy you.
>
> Basically, the bill does the following:

1. No exemption from antitrust activity is given in this bill.

2. However, in regard to the use of health care contracting the legislation directs the courts to apply the "rule of reason" test to such activities.

This latest approach, far more moderate than the one I attempted last year, has, I believe, led to some of the muting of the opposition.

The legislative record shows that in 1985, the California Legislature did not intend the statutes to provide absolute immunity from potential antitrust liability to contracting units formed under those statutes. Instead, the statutes were intended only to protect such contracting units from the type of *per se* antitrust scrutiny to which the U.S. Supreme Court subjected the defendant in *Maricopa*. The 1985 California Legislature never intended the statutes to immunize contracting units from antitrust scrutiny under the rule of reason.

D. The Lower Court's Opinion will Allow Health Insurers to Possess Market Power in Physician Markets, Resulting in Consumer Injury.

The complaint in this case alleges that the contracting unit created by the arrangement between SCIF and BCC is a "monopsonist," meaning that it has market power on the buy-side of the market. *See Weyerhaeuser Co. v. Ross-Simmons Hardware Lumber Co.*, 549 U.S. 312, 320 (2007). The SCIF/BCC bargaining unit has few, if any, competitors. (*See* First Amended Complaint at 18-19.) Even if, in the future trial of this case, competitors were found to exist in some of the geographic areas relevant to this case, these competitors are likely to possess a substantially smaller market share than the SCIF/BCC bargaining unit.

Allowing the SCIF/BCC bargaining unit to possess monopsony power harms consumers. This concern regarding consumer harm was emphasized by R. Hewitt Pate, a former Assistant Attorney General of the Antitrust Division, in a 2003 statement before the Senate Judiciary Committee:

> A casual observer might believe that if a merger lowers the price the merged firm pays for its inputs, consumers will necessarily benefit. The logic seems to be that because the input purchaser is paying less, the input purchaser's customers should expect to pay less also. But that is not necessarily the case. Input prices can fall for two entirely different reasons, one of which arises from a true economic efficiency that will tend to result in lower prices for final consumers. The other, in contrast, represents an efficiency-reducing exercise of market power that will reduce economic welfare, lower prices for suppliers,

and may well result in higher prices charged to final consumers.

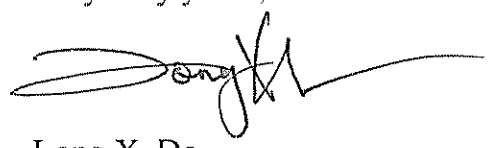
Moreover, monopsonists' ability to reduce physician payments below competitive levels leads to a reduction in services that harms consumers, *even if* the direct prices paid by subscribers do not increase. *See* Gregory J. Werden, *Monopsony and the Sherman Act: Consumer Welfare in a New Light*, 74 ANTITRUST L.J 707 (2007) (explaining reasons to challenge monopsony power even where there is no immediate impact on consumers); Marius Schwartz, *Buyer Power Concerns and the Aetna- Prudential Merger*, Address Before the 5th Annual Health Care Antitrust Forum at Northwestern University School of Law at 4-6 (Oct. 20, 1999) (noting that anticompetitive effects can occur even if the conduct does not adversely affect the ultimate consumers who purchase the end-product), online at <http://www.usdoj.gov/atr/public/spceches/3924.wpd>.

In the instant case, Appellants' forced acceptance of depressed payment rates is having a negative impact on the quantity of services that Appellants are able provide to injured workers. For example, Appellants have been forced to reduce their office hours, cut back on staff and/or equipment, and/or invest less in continuing education—all of which are detrimental to workers' compensation patients.

If left standing, the lower court's opinion will give free reign to the creation of health insurer monopsonies that may have disastrous consequences for patient access to necessary medical care. This prospect alone warrants review by the Court.

For the foregoing reasons, Amici respectfully urge the Court to grant review in this case.

Very truly yours,



Long X. Do
Legal Counsel & Director of Litigation
California Medical Association
On behalf of the AMA and CMA

PROOF OF SERVICE

I, Judith A. Givens, hereby declare:

I am employed in Sacramento, California. I am over the age of eighteen years and am not a party to the above-entitled action. My business address is 1201 J Street, Suite 200, Sacramento, California 95814. On October 26, 2009, I served the document as indicated below:

Letter of Amici Curiae in Support of Petition for Review in *Henstorf v. State Compensation Insurance Fund*, Supreme Court No. S176974 (2nd App. Dist. No. B210943)

U.S. Mail: By placing true copies thereof in sealed envelopes addressed as set forth below, with first-class postage thereon fully prepaid and causing such envelopes to be placed for collection and mailing on that date in accordance with ordinary business practice for deposit in the United States at Sacramento, California.

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I declare under penalty of perjury under the laws of the State of California that the foregoing is true and correct. Executed this 26th day of October 2009, at Sacramento, California.

Judith A. Givens

Judith A. Givens