# Testimony of David Balto, Senior Fellow, Center for American Progress

## Before the Pennsylvania State Senate, Committee on Banking and Insurance
## on the
## UPMC-Highmark Dispute

**September 13, 2011**

David Balto
1350 I Street NW
Washington, DC 20005
202-789-5424

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Chairman White and other members of the committee, I appreciate the opportunity to testify before you today about competition in the Pittsburgh healthcare market. I am David Balto, a senior fellow at the Center for American Progress and also the former policy director of the Federal Trade Commission. In over 25 years as a public servant and antitrust attorney, I have had firsthand experience in evaluating competition in various healthcare markets. I have testified before your committee and Congress on several occasions on healthcare competition and, as a former public servant, brought numerous healthcare enforcement actions. My testimony today is based on that experience, my review of the record in the House hearing and my conversations with the University of Pittsburgh Medical Center ("UPMC"), Highmark, other market participants including unions, employers, and consumer groups.

**Pittsburgh Healthcare Competition**

As I mentioned, I have a great deal of experience in examining competition in healthcare markets. Most observers would agree that the Pittsburgh health insurance market is not a particularly competitively healthy. Pittsburgh is the third most concentrated health insurance market in the United States. Highmark's market share consistently exceeds 65%. That dominant position has led to consistently higher insurance premiums, which have increased at double digit rates for the past several years, notwithstanding relatively small increases in healthcare provider rates. As significant, Highmark's reserves, currently over $4.7 billion, are far more substantial than other similarly situated insurance companies. Moreover, there has been little to no entry or expansion in the market even though as the 23rd largest metropolitan area in the United States, it appears to offer an attractive opportunity. All of these factors, increasing prices, substantial reserves and lack of entry, provide powerful evidence that Highmark has market power. Ultimately, the level of concentration in this market is both unusual and counterproductive to controlling costs.

Competition in the hospital market in Pittsburgh is somewhat better, though not as robust as in many other metropolitan markets. There are two hospital systems, UPMC and West Penn, and the Pittsburgh area is also served by over 12 community hospitals. UPMC has a significant share of this hospital market. West Penn traditionally has been a weaker competitor and has suffered through financial problems for several years. Accordingly, a number of concerns have been posed over the past few years about West Penn's long-term viability. UPMC on the other hand, has been repeatedly acknowledged for consistent excellence in clinical care and customer satisfaction. It has been on the U.S. News and World Report's Honor Roll for the past 12 consecutive years and earned the highest ranking for overall satisfaction by a health insurer in Pennsylvania in 2011, according to a survey by J.D. Power and Associates. UPMC offers a wide variety the highest level of services and is recognized as a national leader in the delivery of healthcare.

Many people looking at this situation might imagine that a market with a clearly dominant health insurance company and a large hospital system is the worst of all possible worlds, but that is not the case in Pittsburgh. What would be of far greater concern to consumers would be if Highmark and UPMC, recognizing each other's dominance, colluded to raise both reimbursement rates and premiums. These types of de facto alliances between dominant insurers and dominant hospital systems occur in numerous other metropolitan markets and harm consumers with higher costs and reduced quality. Few people observing the nature of the relationship between UPMC and Highmark, however, would conclude that there was any type of truce or mutual accommodation between the two companies. West Penn brought a recent antitrust case alleging the existence of such a truce, but after the Department of Justice Antitrust Division investigated the allegations, the DOJ chose to close the investigation—a decision which seems wholly appropriate. UPMC and Highmark fight tooth and nail. To give one example, UPMC made a tremendous investment to create the major rival to Highmark – the UPMC Health Plan. Similarly, UPMC strongly opposed Highmark’s proposed acquisition of Independence Blue Cross. In addition, both UPMC and Highmark engage in almost endless battles in the courtroom. Pittsburgh stands out among all markets as one where the largest insurance company and largest hospital appear to be aggressive adversaries-- an adversarial relationship that ultimately benefits consumers.

**The Critical Changes in the Pittsburgh Market**

These hearings are being held because of three critically important changes in the marketplace:

1. UPMC has entered into favorable contracts with national health insurers including Aetna, United, Cigna, and Health America which will significantly facilitate their entry and expansion into the Pittsburgh market. Up until now these firms were unable to be fully effective competitors because they could not get a favorable contractual agreement with UPMC. UPMC has agreed to foster their entry by offering them "market rates" which puts them on a comparable level with rates offered in other markets.

2. Highmark has entered into an agreement to help protect the viability of West Penn. By entering into this agreement, Highmark is fundamentally changing its position in the market from simply being a health insurer to being an integrated delivery system managing not only health insurance, but also the provision of medical care.

3. UPMC has stated that it will not continue to contract with Highmark after the expiration of their ongoing contract which is scheduled to expire in June 2012.

**Some Observations**

Let me make several observations about these changes. First, the competitive problem in the Pittsburgh market is clearly Highmark's dominance in the insurance market which has raised the cost of health insurance and led to a greater number of uninsured consumers. The endemic problem in the market is that concentration. UPMC's newly instated arrangements with health insurers offer the best opportunity in decades for competition to break out in the Pittsburgh health insurance market. With these new UPMC arrangements with the four insurance companies, there now will be six providers of health insurance in the market (Highmark, Aetna, Cigna, United, Health America, and the UPMC Health Plan). Two of those entities will be fully integrated systems: Highmark and UPMC Health Plan. This will create a far more robust level of competition.

One need not have a PhD in economics to predict the impact of these changes. We only need to look at the insurance market in Central Pennsylvania. In an examination of the potential merger between Highmark and Independence Blue Cross, the Insurance Commissioner examined the impact of Highmark's entry into Central Pennsylvania. The Commissioner concluded that entry led to more robust insurance competition, relatively lower premiums, and greater competition for providers. Competition in Southeastern Pennsylvania has also been spurred by expansion by the national insurers. Consumers in Pittsburgh deserve the rivalry among health insurers that Pennsylvania consumers benefit from throughout the rest of the state.

Indeed, there was testimony presented at the House hearing stating that the Pittsburgh market is experiencing an outbreak of competition. Cigna has begun a major recruitment effort. Contracting competition has led to smaller premium increases. This is a snapshot at the beginning of the competitive race, but it appears promising.

Second, Highmark's arrangement with West Penn significantly changes the dynamic for health care competition among providers. Up until now, consumers could rely on Highmark as an "honest broker" seeking the lowest reimbursement rate from all providers and making network decisions generally based on cost. Now that it owns West Penn however, it will no longer be an independent referee. By becoming an integrated system, it will have not only the incentive, but the imperative to direct subscribers to its own network of hospitals. It will be essential for Highmark to recover its investment by driving consumers to West Penn hospitals to the disadvantage of other providers.

Third, the Highmark alliance with West Penn poses a serious competitive threat to the UPMC alliances. If UPMC is effectively forced to give access to its rival that will undermine its ability to offer the more attractive rates to the national health insurers. Moreover, if Highmark has equal access to UPMC it can free ride on UPMC, by selling "access" to UPMC, but directing consumers to West Penn hospitals.

Certainly, the competitive viability of West Penn is a concern for the market and we should applaud Highmark's commitment to help fund West Penn. However it's unclear whether the only potential alternative for West Penn to remain viable was an acquisition by Highmark. There may have been other alternatives including acquisitions by other hospital systems which may have kept West Penn in the market.

In addition, one should consider whether Highmark can form a viable network without UPMC hospitals. West Penn will provide a solid base of hospitals which can be supported by the numerous community hospitals in the market. There appears to be a viable alternative hospital network.

Highmark argues that it and its subscribers will be significantly disadvantaged by the termination of the UPMC contract. In particular, it has identified access to the Hillman Cancer Center and the Magee-Women's Hospital as being very important. This is a concern that must be carefully evaluated. I have three observations. First, West Penn has hospitals that provide high quality cancer and women's care and indeed, those services are widely available at other community hospitals. Second, it is important to distinguish whether a facility provides "unique" services or there is simply "consumer preference" for a facility. One can conceive of compelling access to a facility providing truly unique and essential services, and indeed UPMC may need to grapple with ways of providing such access, but requiring access because consumers <u>prefer</u> a more attractive or newer facility seems like a poor policy choice. Finally, UPMC has not suggested that Highmark subscribers will be denied access, but rather, that Highmark will no longer have preferential rates for those subscribers. Highmark can, however, always cover its subscribers and not pass on the additional costs.

Ultimately, the likely outcome of these changes offers a tremendous opportunity for a better marketplace for consumers. With six health insurers competing aggressively for consumers, we should see a significant decrease in the cost of health insurance, and better access to healthcare. Additionally, partnering West Penn with the significant expertise and financial resources of Highmark offers the potential for increased hospital competition.

I want to close with remarks about your constituents who I know are at the core of the concerns you bring to today's hearings. As a former public servant and consumer advocate, I am sensitive to these concerns. I remember when I was a staff attorney at the Antitrust Division in the 1980s trying to explain why the DOJ forced the dismantling of AT&T. Those consumers were terrified of change but 25 years later the benefits of the break up of AT&T have led to phenomenal consumer benefits.

Competition and change work hand in hand in the marketplace. Consumers may fear change especially when dealing with a market like healthcare, but they should welcome competition and choice that have clearly been lacking from the health insurance marketplace in Pittsburgh for years. There are things both UPMC and Highmark can and should do to ensure that consumers understand change and can manage it, including being transparent about the transition period and explaining that the changes in the Pittsburgh market are in fact not unique. Well managed change here will spur the opportunity for competition and ultimately consumers should benefit.

I appreciate the chance to testify before your committee and welcome your questions.