UNITED STATES OF AMERICA
Federal Trade Commission
WASHINGTON, D.C. 20580

Office of Policy Planning
Bureau of Economics
Bureau of Competition

July 10, 2015

The Honorable Marilyn W. Avila
North Carolina House of Representatives
2217 Legislative Building
16 W. Jones Street
Raleigh, NC 27601-1096

Dear Representative Avila:

The staffs of the Federal Trade Commission's ("FTC") Office of Policy Planning, Bureau of Economics, and Bureau of Competition[1] appreciate the opportunity to respond to your invitation for comments on North Carolina House Bill 200 ("HB200").[2] As described in your letter, HB200 "is intended to exempt diagnostic centers, ambulatory surgical facilities and psychiatric hospitals from Certificate of Need regulation." The bill also prohibits limitations on the number of operating rooms and gastrointestinal procedure rooms, and contains requirements to "ensure the provision of charity care, to require annual reporting and to facilitate coordination with hospitals." To the extent that HB200 narrows the application of North Carolina's Certificate of Need ("CON") law, it likely represents a procompetitive improvement in the law as compared with the status quo.

CON laws have the laudable goals of reducing health care facility costs and improving access to care.[3] However, CON laws can prevent the efficient functioning of health care markets in several ways that may undermine those goals. First, they often create barriers to entry and expansion, limit consumer choice, and stifle innovation. Second, CON laws can be prone to exploitation by incumbent firms seeking to thwart or delay entry by new competitors. Third, as recently illustrated by the Commission's experience in the *Phoebe Putney* case, CON laws can deny consumers the benefit of an effective divestiture-based remedy following the consummation of an anticompetitive merger. Finally, CON laws appear to have generally failed to control health care costs. For these reasons, each of which we explain more fully below, FTC staff supports HB200.[4]

I. The FTC's Interest and Experience in Health Care Competition

Congress has charged the FTC with enforcing the Federal Trade Commission Act, which prohibits unfair methods of competition and unfair or deceptive acts or practices in or affecting commerce.[5] Competition is at the core of America's economy,[6] and vigorous competition among sellers in an open marketplace gives consumers the benefits of lower prices, higher quality goods and services, greater access to goods and services, and innovation.[7] Pursuant to its statutory mandate, the FTC seeks to identify business practices, laws, and regulations that may impede competition without providing countervailing benefits to consumers.

Because of the importance of health care competition to the economy and consumer welfare, anticompetitive conduct in health care markets has long been a priority of the FTC's enforcement, study, and advocacy efforts. The FTC has extensive experience investigating anticompetitive mergers and business practices by hospitals, pharmaceutical companies, and physicians. It also has devoted significant resources to the examination of the health care industry by sponsoring various workshops and studies. Through the agency's competition advocacy program, FTC staff has encouraged states to consider the competitive impact of various health care-related legislative proposals, including CON laws.[8]

II. North Carolina's CON Law and HB200

North Carolina's CON law requires regulatory approval for entry by, or expansion of, a wide variety of health service facilities and health care activities.[9] Covered facilities include, for example, hospitals, nursing homes, home health agency offices, ambulatory care facilities, and hospice programs.[10] Covered activities include, among others, the construction, development, or other establishment of health service facilities, certain capital expenditures over $2,000,000, changes in bed capacity, transplantation services, and the acquisition of certain types of medical equipment.[11]

The CON process can be time-consuming. In North Carolina, CON applications are made to the state Department of Health and Human Services' Division of Health Service Regulation (the "Division"). According to the Division's summary of the CON process, CON applications are subject to a 30-day public comment period, during which any person may file a written comment. Though no longer required for all applications, a public hearing may be held in some cases. The Division considers all comments and public hearing materials in its evaluation of CON applications and has between 90 and 150 days to review an application. Its decisions may be appealed to an administrative law judge within 30 days, and that judge has 270 days to rule. Further appeal to the North Carolina court of appeals is also permitted.[12] Therefore, the CON process can delay entry by—at a minimum—many months, even when a CON is ultimately granted.

HB200 proposes to narrow North Carolina's CON law to exempt diagnostic centers, ambulatory surgical facilities, gastrointestinal endoscopy rooms, and psychiatric hospitals from the CON process. The bill also would prohibit limitations on the number of operating rooms and gastrointestinal endoscopy rooms. Finally, the bill includes certain new licensing requirements for ambulatory surgical facilities.[13] These licensing provisions require that facilities provide a certain amount of indigent care and provide additional documentation prior to operating in rural areas. HB200 does not appear to change the CON comment or review process.

III. Analysis of Likely Competitive Effects of HB200

Competition in health care markets can benefit consumers by containing costs, improving quality, and encouraging innovation.[14] Indeed, price competition generally results in lower prices, and, thus, broader access to health care products and services, while non-price competition can promote higher quality and encourage innovation. CON laws may suppress these substantial benefits of competition by limiting the availability of new or expanded health care services. For these reasons, the Commission and its staff have advocated that states with CON laws reconsider whether those laws best serve the needs of their citizens, and staff supports the bill at issue here, HB200.[15]

A. CON Laws Create Barriers to Entry, Which May Suppress More Cost-Effective, Innovative, and Higher Quality Health Care Options

CON laws, such as North Carolina's, prevent new entrants from offering health care services without first obtaining a state-issued approval. By interfering with the market forces that normally determine supply of services, CON laws tend to suppress competition and shield incumbent health care providers from competition from new entrants.[16] As a result, they can:

- Delay, and raise the cost of, entry by firms that are potentially able to offer new, more cost-effective, or higher quality services;
- Reduce the ability of the market to respond to consumer demand for different treatment options, settings, or prices; and
- Remove or delay the competitive pressures that typically incentivize incumbent firms to innovate, improve existing services, or introduce new ones.[17]

Because HB200 would exempt certain facilities from North Carolina's CON law, it may mitigate these potentially anticompetitive consequences of the CON process for the types of entities it covers. As a result, it could enable North Carolina's health care consumers to benefit from additional competition as new facilities can more easily enter the market.

B. The CON Process May Be Prone to Exploitation by Competitors Seeking to Protect Their Market Share

In addition to disrupting the market forces that typically determine the supply of services, CON laws may further harm competition because competitors may take advantage of the CON process to protect their market share. For instance, an incumbent firm may file challenges or comments to a potential competitor's CON application merely for the purpose of thwarting or delaying competition. As noted in the FTC-DOJ report, *Improving Health Care: A Dose of Competition*, existing firms can use the CON process "to forestall competitors from entering an incumbent's market."[18] More recently, a 2012 House Select Committee Report on North Carolina's CON process described stakeholder concerns "that some appeals may be brought solely for the purpose of delay."[19] The committee identified the need to "deter the bringing of frivolous, harassing, or meritless appeals."[20] The misuse of the CON process by competitors not only can cause delay, but also can divert scarce resources away from health care innovation as potential entrants incur legal, consulting, and lobbying expenses responding to competitor challenges.[21] HB200, by narrowing the applicability of North Carolina's CON law, would eliminate the opportunity for this type of exploitation with respect to exempted health service facilities.

We also note that Section 7(f)(4) of HB200 requires ambulatory surgical facilities seeking licenses to operate in counties with populations under 100,000 people to obtain written support and a written transfer agreement from each hospital located within the county.[22] Although we recognize that this provision may be intended to ensure access to care and patient safety, it also could be improperly used by incumbent hospitals to block a potential competitor's license. We respectfully encourage you to consider whether there are other ways – less prone to anticompetitive manipulation – to achieve access and patient safety goals.

C. CON Laws Can Impede Effective Antitrust Remedies

As the FTC's recent experience in *FTC v. Phoebe Putney* demonstrates, CON laws can entrench anticompetitive mergers by limiting the ability to implement effective structural remedies. *Phoebe Putney* involved a challenge to the merger of two hospitals in Albany, Georgia.[23] The FTC alleged that the merger had created a monopoly in the provision of inpatient general acute-care hospital services sold to commercial health plans in Albany and its surrounding areas, but ultimately was unable to achieve a remedy that would have restored competition to the marketplace due to Georgia's CON laws and regulations.[24] As the Commission explained in its statement on the matter, "[w]hile [divestiture] would have been the most appropriate and effective remedy to restore the lost competition in Albany and the surrounding six-county area from this merger to monopoly, Georgia's [CON] laws and regulations unfortunately render a divestiture in this case virtually impossible."[25] The Commission statement further noted that the case "illustrates how state CON laws, despite their original and laudable goal of reducing health care facility costs, often act as a barrier to entry to the detriment of competition and healthcare consumers."[26] Thus, HB200, by narrowing the applicability of North Carolina's CON law, could preserve antitrust as a tool to remedy anticompetitive conduct in some health care markets.

D. CON Laws Appear to Have Generally Failed to Control Costs

States originally adopted CON programs, in part, as a way to mitigate the incentives created by cost-based reimbursement. A primary goal of CON laws was to control health care costs by preventing overinvestment in health facilities and the resulting misallocation of resources.[27] Empirical studies on balance suggest that these laws have generally failed in their cost containment goals.[28] The empirical evidence also fails to consistently show increases in health care spending in states that have removed their CON programs, and in fact, one recent study shows that Medicare expenditures for cardiac procedures fell following repeal of CON regulations.[29]

IV. Conclusion

FTC staff recognizes that states must weigh a variety of policy objectives when considering health care legislation such as HB200. But, as described above, CON laws raise considerable competitive concerns and generally do not appear to achieve their alleged benefits for health care consumers. For these reasons, FTC staff supports HB200.

FTC staff appreciates the opportunity to provide our input on HB200. We hope that our comments will be of assistance as you consider these issues.

Respectfully submitted,

Marina Lao, Director
Office of Policy Planning

Francine Lafontaine, Director
Bureau of Economics

Deborah L. Feinstein, Director
Bureau of Competition

---

[1] This staff letter expresses the views of the FTC's Office of Policy Planning, Bureau of Competition, and Bureau of Economics. The letter does not necessarily represent the views of the FTC or of any individual Commissioner. The Commission, however, has voted to authorize staff to submit these comments. Commissioner Wright concurred in the Commission's vote to authorize staff to submit these comments, and also submitted a concurring comment.

[2] Letter from the Honorable Representative Marilyn W. Avila, N.C. House of Representatives, to Marina Lao, Director, Office of Policy Planning, Federal Trade Commission (May 8, 2015); H.B. 200, 2015 Gen. Assemb., Reg. Sess. (N.C. 2015).

[3] As noted, CON laws have been promulgated with aims in addition to lowering costs and prices, such as increasing access to critical care. *See, e.g.*, The Lewin Group, An Evaluation of Illinois' Certificate of Need Program: Prepared for the State of Illinois Commission on Government Forecasting and Accountability (Feb. 2007), available at http://cgfa.ilga.gov/Upload/LewinGroupEvalCertOfNeed.pdf. This letter does not address those other goals and the extent to which CON laws do or do not achieve them.

[4] We are aware that the North Carolina General Assembly is considering several options with respect to the CON law, and that the legislative status remains fluid as of the drafting of this letter. We note that the budget recently approved by the Senate contains a provision calling for a phased repeal of the CON law. Our comments in this letter are limited to HB200 upon which we were invited to comment, but to the extent that the Senate bill repeals CON altogether, our comments would be relevant to consideration of that bill as well.

[5] Federal Trade Commission Act, 15 U.S.C. § 45 (2006).

[6] *Standard Oil Co. v. FTC*, 340 U.S. 231, 248 (1951) ("The heart of our national economic policy has long been faith in the value of competition.").

[7] *See Nat'l Soc'y of Prof'l Eng'rs v. United States*, 435 U.S. 679, 695 (1978) (The antitrust laws reflect "a legislative judgment that ultimately competition will produce not only lower prices, but also better goods and services. . . . The

assumption that competition is the best method of allocating resources in a free market recognizes that all elements of a bargain—quality, service, safety, and durability—and not just the immediate cost, are favorably affected by the free opportunity to select among alternative offers.").

[8] A description of, and links to, the FTC's various, health care-related activities can be found at https://www.ftc.gov/tips-advice/competition-guidance/industry-guidance/health-care.

[9] *See* N.C. Gen. Stat. § 131E-178 (2015).

[10] *See id.* § 176(9b).

[11] *See id.* § 176(16).

[12] *See* N.C. Division of Health Service Reg., Healthcare Planning and Certificate of Need Section, Overview of Certificate of Need, *available at* http://www.ncdhhs.gov/dhsr/coneed/overview.html (last visited June 1, 2015).

[13] *See* H.B. 200, 2015 Gen. Assemb., Reg. Sess. (N.C. 2015).

[14] *See* Federal Trade Comm'n & U.S. Dep't of Justice, Improving Health Care: A Dose of Competition, Executive Summary, at 4 (July 2004), *available at* https://www.ftc.gov/sites/default/files/documents/reports/improving-health-care-dose-competition-report-federal-trade-commission-and-department-justice/040723healthcarerpt.pdf [hereinafter A Dose of Competition].

[15] *See* A Dose of Competition, *supra* note 14; *see also* Joint Statement of the Antitrust Division of the U.S. Department of Justice and the Federal Trade Commission Before the Illinois Task Force on Health Planning Reform (Sept. 15, 2008), *available at* https://www.ftc.gov/sites/default/files/documents/advocacy_documents/ftc-and-department-justice-written-testimony-illinois-task-force-health-planning-reform-concerning/v080018illconlaws.pdf [hereinafter DOJ-FTC Illinois Testimony]; Prepared Statement of the Federal Trade Commission Before the Florida State Senate (Apr. 2, 2008) [hereinafter FTC Florida Statement], *available at* https://www.ftc.gov/sites/default/files/documents/advocacy_documents/ftc-prepared-statement-florida-senate-concerning-florida-certificate-need-laws/v080009florida.pdf; Prepared Statement of the Federal Trade Commission Before the Standing Committee on Health, Education, & Social Services of the Alaska House of Representatives (Feb. 15, 2008) [hereinafter FTC Alaska Statement], *available at* https://www.ftc.gov/sites/default/files/documents/advocacy_documents/ftc-written-testimony-alaska-house-representatives-concerning-alaska-certificate-need-laws/v080007alaska.pdf.

[16] *See* A Dose of Competition, *supra* note 14, ch. 8 at 4.

[17] *See id*; *see also* DOJ-FTC Illinois Testimony, *supra* note 15, at 6.

[18] A Dose of Competition, *supra* note 14, Executive Summary at 22.

[19] North Carolina General Assembly, House Select Committee on the Certificate of Need Process and Related Hospital Issues, Final Report to the 2013 House of Representatives, at 13 (Dec. 2012), *available at* http://www.ncleg.net/documentsites/committees/HSCCONPRHI/12-06-12/12-06-12%20HSCCON%20Final%20Report.pdf.

[20] *Id.*

[21] What makes this conduct more concerning is the fact that much of it, even if exclusionary and anticompetitive, may be shielded from federal antitrust scrutiny, because it involves protected petitioning of the state government. *See* DOJ-FTC Joint Illinois Testimony, *supra* note 15, at 6-7; FTC Florida Statement, *supra* note 15, at 8-9; FTC Alaska Statement, *supra* note 15, at 8-9.

[22] *See* H.B. 200, *supra* note 13.

[23] *See generally In re Phoebe Putney Health Sys., Inc.*, Dkt. No. 9348, *available at* https://www.ftc.gov/enforcement/cases-proceedings/111-0067/phoebe-putney-health-system-inc-phoebe-putney-memorial.

[24] The Eleventh Circuit affirmed the district court's dismissal of the case on state action grounds and dissolved the stay that had prevented the parties from consummating the merger. The Supreme Court reversed, finding against state action immunity. *See FTC v. Phoebe Putney Health Sys. Inc.*, 133 S. Ct. 1003, 1011 (2013).

[25] *In re Phoebe Putney Health Sys., Inc.*, Dkt. No. 9348, Statement of the Federal Trade Commission, at 1 (Mar. 31, 2015), *available at* https://www.ftc.gov/system/files/documents/public_statements/634181/150331phoebeputneycommstmt.pdf.

[26] *Id.* at 3.

[27] *See* A Dose of Competition, *supra* note 14, ch. 8 at 2; Christine L. White et. al., Antitrust and Healthcare: A Comprehensive Guide 527 (2013).

[28] *See, e.g.*, Patrick A. Rivers, Myron D. Fottler & Jemima A. Frimpong, *The Effects of Certificate of Need Regulation on Hospital Costs*, 36 J. Health Care Fin. 1, 12 (2010); DOJ-FTC Illinois Testimony, *supra* note 15, at 5 & nn.16-18 (collecting studies on the effects of CON laws); The Lewin Group Report, *supra* note 3, at i-ii ("Based on our review of relevant literature and our independent analysis, it is clear that the evidence on cost containment is weak . . . ."); *but see* Michael D. Rosko & Ryan L. Mutter, *The Association of Hospital Cost-Inefficiency with Certificate-of-Need Regulation*, 71 Med. Care Res. & mRev. 280 (2014) (finding lower hospital cost-inefficiency in CON states than non-CON states).

[29] *See* Vivian Ho & Meei-Hsiang Ku-Goto, *State Deregulation and Medicare Costs for Acute Cardiac Care*, 70(2) Med. Care Res. & Rev. 201 (2013) ("Removal of CON regulations is also associated with lower Medicare reimbursements pre patient for both CABG and PCI.").