Private Equity and Corporatization of Health Care

Erin C. Fuse Brown, JD, MPH
Catherine C. Henson Professor of Law, Director of the Center for Law, Health & Society, Georgia State University College of Law

Nov. 11, 2023
PNHP Conference Session: Problems with the Commodification of Health Care
My journey down the PE rabbit hole:

Private Equity and the Corporatization of Health Care

Private Equity Investment As A Divining Rod For Market Failure: Policy Responses To Harmful Physician Practice Acquisitions

A Doctrine in Name Only — Strengthening Prohibitions against the Corporate Practice of Medicine
Overview

• **Trends** in corporate investment in health care, the PE model

• Potential **harms** of PE investment in physician practices

• **Policy levers** to address PE and corporate entry into health care markets
Changes in Corporate Ownership of Physicians

Types of Corporate Owners:

1. Hospitals and Hospital Systems

2. “Other” Corporate Entities: Private Equity, Health Insurers (e.g., UnitedHealth Optum), Retailers (e.g., Amazon, Walgreens)
Hospital and Other Corporate Ownership

As of 2022, 51% of MD’s were employed by hospitals, an 11% increase during the three-year study period.

As of 2022, 21.8% of physicians were employed by “other” corporate entities, a 43% increase over a three-year period.

Avalere Health (2022)
Insurers + Pharmacy + PBM + Physicians = “Pay-vider”

- 10-year deal (2022) with Walmart (5,000 pharmacies)
- Many physician acquisitions through Optum
- 70,000 Physicians & 2,200 clinics

Example: Atrius Health
Insurers + Pharmacy + PBM + Physicians = “Pay-vider”

- **Aetna**: $69 Billion (2018)
- **CVS**: $10.6 Billion (2023) → 10,000 pharmacies
- **Oak Street Health**: $8 Billion (2022)
- **Signify Health**: 600 PCPs, 169 clinics

Song Z, under review
Private Equity investment in health care

Figure 1. Total PE Deals in Healthcare* — Reported Deal Value, Estimated Deal Value, and Reported Deal Count, 2010-2020

- PE capital investment in health care grew from $5 billion in 2000 to $100 billion in 2018
- Total value of health care deals 2010-2020: $750 billion
- Physician practice acquisitions grew from 39 to 221 deals annually 2010-2019 (1,283 deals in total the decade)
• PE acquisitions of physician practices increasing in last 5 years
  
• We lumped these into 3 main categories:
  • Hospital-based
  • Office-based
  • Value-based payment & Primary Care

Data source: Irving Levin Associates
Classic Model of a Private Equity Acquisition

Management Fees

PE Firm

GP

2% of equity

20% after hurdle

98% of equity

Limited Partners

US Pension Funds (>1/3), endowments, sovereign funds, wealthy people

Management Fees

PE Fund

30% Equity

70% Debt

Acquire

Hospital, Practice

Lenders

(Bank)

Assets as Collateral

IPO (5-10%)

Corporate (20%) – Optum, CVS, Amazon

2° PE (65%)

Exit

3-7 yrs

Returns: first 8%, then 80%

Returns: fixed rate

Exit 20% after hurdle

PE Fund

30% Equity

70% Debt

Acquire

Hospital, Practice

Lenders

(Bank)

Assets as Collateral

IPO (5-10%)

Corporate (20%) – Optum, CVS, Amazon

2° PE (65%)

Exit

3-7 yrs

Returns: first 8%, then 80%

Returns: fixed rate

PE Firm

GP

2% of equity

20% after hurdle

98% of equity

Limited Partners

US Pension Funds (>1/3), endowments, sovereign funds, wealthy people

Management Fees

PE Fund

30% Equity

70% Debt

Acquire

Hospital, Practice

Lenders

(Bank)

Assets as Collateral

IPO (5-10%)

Corporate (20%) – Optum, CVS, Amazon

2° PE (65%)

Exit

3-7 yrs

Returns: first 8%, then 80%

Returns: fixed rate

PE Firm

GP

2% of equity

20% after hurdle

98% of equity

Limited Partners

US Pension Funds (>1/3), endowments, sovereign funds, wealthy people

Management Fees

PE Fund

30% Equity

70% Debt

Acquire

Hospital, Practice

Lenders

(Bank)

Assets as Collateral

IPO (5-10%)

Corporate (20%) – Optum, CVS, Amazon

2° PE (65%)

Exit

3-7 yrs

Returns: first 8%, then 80%

Returns: fixed rate

PE Firm

GP

2% of equity

20% after hurdle

98% of equity

Limited Partners

US Pension Funds (>1/3), endowments, sovereign funds, wealthy people

Management Fees

PE Fund

30% Equity

70% Debt

Acquire

Hospital, Practice

Lenders

(Bank)

Assets as Collateral

IPO (5-10%)

Corporate (20%) – Optum, CVS, Amazon

2° PE (65%)

Exit

3-7 yrs

Returns: first 8%, then 80%

Returns: fixed rate

PE Firm

GP

2% of equity

20% after hurdle

98% of equity

Limited Partners

US Pension Funds (>1/3), endowments, sovereign funds, wealthy people

Management Fees

PE Fund

30% Equity

70% Debt

Acquire

Hospital, Practice

Lenders

(Bank)

Assets as Collateral

IPO (5-10%)

Corporate (20%) – Optum, CVS, Amazon

2° PE (65%)

Exit

3-7 yrs

Returns: first 8%, then 80%

Returns: fixed rate

PE Firm

GP

2% of equity

20% after hurdle

98% of equity

Limited Partners

US Pension Funds (>1/3), endowments, sovereign funds, wealthy people

Management Fees

PE Fund

30% Equity

70% Debt

Acquire

Hospital, Practice

Lenders

(Bank)

Assets as Collateral

IPO (5-10%)

Corporate (20%) – Optum, CVS, Amazon

2° PE (65%)

Exit

3-7 yrs

Returns: first 8%, then 80%

Returns: fixed rate

PE Firm

GP

2% of equity

20% after hurdle

98% of equity

Limited Partners

US Pension Funds (>1/3), endowments, sovereign funds, wealthy people

Management Fees

PE Fund

30% Equity

70% Debt

Acquire

Hospital, Practice

Lenders

(Bank)

Assets as Collateral

IPO (5-10%)

Corporate (20%) – Optum, CVS, Amazon

2° PE (65%)

Exit

3-7 yrs

Returns: first 8%, then 80%

Returns: fixed rate

PE Firm

GP

2% of equity

20% after hurdle

98% of equity

Limited Partners

US Pension Funds (>1/3), endowments, sovereign funds, wealthy people

Management Fees

PE Fund

30% Equity

70% Debt

Acquire

Hospital, Practice

Lenders

(Bank)

Assets as Collateral

IPO (5-10%)

Corporate (20%) – Optum, CVS, Amazon

2° PE (65%)

Exit

3-7 yrs

Returns: first 8%, then 80%

Returns: fixed rate

PE Firm

GP

2% of equity

20% after hurdle

98% of equity

Limited Partners

US Pension Funds (>1/3), endowments, sovereign funds, wealthy people

Management Fees

PE Fund

30% Equity

70% Debt

Acquire

Hospital, Practice

Lenders

(Bank)

Assets as Collateral

IPO (5-10%)

Corporate (20%) – Optum, CVS, Amazon

2° PE (65%)

Exit

3-7 yrs

Returns: first 8%, then 80%

Returns: fixed rate

PE Firm

GP

2% of equity

20% after hurdle

98% of equity

Limited Partners

US Pension Funds (>1/3), endowments, sovereign funds, wealthy people

Management Fees

PE Fund

30% Equity

70% Debt

Acquire

Hospital, Practice

Lenders

(Bank)

Assets as Collateral

IPO (5-10%)

Corporate (20%) – Optum, CVS, Amazon

2° PE (65%)

Exit

3-7 yrs

Returns: first 8%, then 80%

Returns: fixed rate

PE Firm

GP

2% of equity

20% after hurdle

98% of equity

Limited Partners

US Pension Funds (>1/3), endowments, sovereign funds, wealthy people

Management Fees

PE Fund

30% Equity

70% Debt

Acquire

Hospital, Practice

Lenders

(Bank)

Assets as Collateral

IPO (5-10%)

Corporate (20%) – Optum, CVS, Amazon

2° PE (65%)

Exit

3-7 yrs

Returns: first 8%, then 80%

Returns: fixed rate

PE Firm

GP

2% of equity

20% after hurdle

98% of equity

Limited Partners

US Pension Funds (>1/3), endowments, sovereign funds, wealthy people

Management Fees

PE Fund

30% Equity

70% Debt

Acquire

Hospital, Practice

Lenders

(Bank)

Assets as Collateral

IPO (5-10%)

Corporate (20%) – Optum, CVS, Amazon

2° PE (65%)

Exit

3-7 yrs

Returns: first 8%, then 80%

Returns: fixed rate

PE Firm

GP

2% of equity

20% after hurdle

98% of equity

Limited Partners

US Pension Funds (>1/3), endowments, sovereign funds, wealthy people

Management Fees

PE Fund

30% Equity

70% Debt

Acquire

Hospital, Practice

Lenders

(Bank)

Assets as Collateral

IPO (5-10%)

Corporate (20%) – Optum, CVS, Amazon

2° PE (65%)

Exit

3-7 yrs

Returns: first 8%, then 80%

Returns: fixed rate
Building Market Share: Platform + Add-On Model

Strategy:
- Market share
- Referrals
- Efficiencies
- Increase volume
- Negotiating power
- Sell for higher multiples

Transaction structure:
- PE firm funds transaction
- MSO acquires assets from practices and employs administrative staff
- MSO agreement with Platform Practice
- Platform practice employs clinical staff

Private Equity Fund Management Co.

ABC Dermatology Platform Practice

Dr. Freckles Add-on practice

Dr. Mole Add-on practice

Dr. Sun & Co. Add-on practice

Source: Zhu and Polsky (2021) NEJM; Gandhi and Song (2019) JAMA
How is PE different than traditional corporate investment?

<table>
<thead>
<tr>
<th>Private Equity</th>
<th>Traditional for-profit buyers, publicly traded corporations</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Highly leveraged:</strong> Target receives less capital, mostly debt.</td>
<td>Transaction does not typically add to target’s debt burden</td>
</tr>
<tr>
<td><strong>Short-term horizon:</strong> increase value and exit 3-7 years</td>
<td>Going concern – exit is not necessary to generate returns</td>
</tr>
<tr>
<td><strong>Moral hazard:</strong> PE firm can profit even if target fails. Plenty of upside, little downside risk.</td>
<td>Investors’ fortunes are tied to the target’s success.</td>
</tr>
<tr>
<td>- Debt on target’s balance sheet</td>
<td>Public company’s share values, credit ratings, etc. are pegged to performance of subsidiaries.</td>
</tr>
<tr>
<td>- Losses limited to small equity investment</td>
<td>Repeat or institutional actors have regulatory and reputational capital to maintain.</td>
</tr>
<tr>
<td>- Minimal hit to reputation</td>
<td></td>
</tr>
</tbody>
</table>

Adapted from: Atul Gupta, NIHCM Webinar, Understanding the Growth & Influence of Private Equity in Health Care, June 6, 2023.
Potential Harms

Harm 1: Consolidation, Cost increases
Concentration of market power, up-coding, aggressive risk-adjustment.

Harm 2: Patient Care
Staffing reduction, cost-cutting, closure of less profitable services or facilities

Harm 3: Workforce
Physician burnout, exit, staffing cuts, loss of autonomy
Relative to controls, PE acquisitions increased:

- Charges: 20%
- Prices: 11%
- Aggregate volume: 16%
- Unique patients: 26%
- New patient visits: 38%
- Long visits (>30min): 9%
Corporate investment → Financialized health care

• Corporate investment in physician services is driving a trend toward the financialization of health care, with investors mining health care service organizations to extract wealth.

• The primary goal of financialized health care is profit, while quality of patient care is a secondary concern and cost control is anathema.
## Policy Levers

<table>
<thead>
<tr>
<th>Legal or Policy Response</th>
<th>Risk of Harm Addressed</th>
</tr>
</thead>
<tbody>
<tr>
<td>Antitrust enforcement (e.g., FTC v. USAP)</td>
<td>Consolidation and price increases</td>
</tr>
<tr>
<td>Close payment loopholes (e.g., No Surprises Act)</td>
<td>Cost increases from exploiting loopholes for profit</td>
</tr>
<tr>
<td>Fraud and abuse enforcement (FCA, Stark, AKS)</td>
<td>Overutilization, up-coding, self-referrals</td>
</tr>
<tr>
<td>State employment laws (Corporate practice prohibitions, gag-clauses, non-competes,</td>
<td>Clinical workforce harms, loss of autonomy, moral distress, burnout</td>
</tr>
<tr>
<td>whistleblower protection)</td>
<td></td>
</tr>
<tr>
<td>Ownership transparency</td>
<td>Opacity obscures the problem, allows for political capture</td>
</tr>
</tbody>
</table>

How does single-payer or universal health care reforms address corporatization? (Beware Medicare Advantage for all)
Takeaways

• Corporate investors have flooded the market, increasing the financialization of healthcare

• This poses sufficient risks to warrant an immediate policy response

• We already have many tools to address the risks of corporate investments in physician practices, but they may need sharpening

• The policies should target the market failures, payment loopholes, consolidation themselves

• Ultimately, these policy levers may be insufficient to address corporatization of health care – need to renovate the foundational market orientation health care