

The Benefits of Pre-litigation Mediation

By MICHAEL A. CASSIDY

Since the private equity issue was last addressed in the Bulletin in the Summer of 2022, the volume of health care private equity deals has subsided somewhat, according to statistics presented at the March 2023 Pennsylvania Bar Institute Health Law Conference, and that has generally been attributed to unfavorable market conditions affecting investments of all types.

However, although the volume has leveled off or in some cases subsided, enforcement and investigation activity appears to be ramping up. In March 2023, the House Ways and Means Committee hosted an investigative hearing on “private equity’s expanded role in the US healthcare system”. As you might expect from a federal investigation, conducted by politicians with media present, the tone of the meeting was more hostile rather than supportive. Two quotes will set that stage:

“It’s past time for a bright light to be shined on how private equity ownership in our healthcare system affects patient safety, costs and jobs. Private equity’s influence stretches like an octopus arms through the American healthcare system and born heavily by the most vulnerable: communities of color, rural underserved areas, the elderly, people with disabilities...private equity’s expansion into healthcare is troubling because private equity’s focus on profits is often at odds with what is best for patient care. Private equity’s business involves buying companies, saddling them with debt, and then squeezing them like oranges for every dollar.”

—House Committee on Ways and Means Sub-Committee on Oversight Chair Rep. Bill Pascrell

“I’m so concerned about the increasingly outsized influence of private equity on our healthcare system. Private equity firms are investment firms set up to increase profits for their shareholders, not to provide better quality medicine. We saw that issue up close last year as the committee considered the role of PE firms in the increase of patients receiving surprise medical bills.”

—House of Representatives
Judy Chu (D-CA)

This concern for suspected ulterior financial motives behind these clinical investments is not unfounded, because the healthcare business system is drastically different from most other business environments, in that professional fees paid from government third party payers cannot be raised unilaterally at all, payments from large third party commercial insurance systems are very difficult to raise, if at all. This leaves revenue enhancement possibilities limited to situations in which the private equity roll ups have created leverage, which is one of the goals, or situations in which there is significant self-pay patient activity, i.e. aesthetics, dermatology, rehabilitation, and specialties that have significant ancillary revenue opportunities such as ambulatory surgery centers. Revenue can only be increased in most instances by increased volume, not increased charges. This “fee obstacle” was what precipitated many of the bankruptcies in the 1990s physician practice management ventures, as mentioned in my prior article.

Please note that the potential for ulterior financial motives does not automatically presume that the intent is somehow suspect, in the same way that potential medical malpractice concerns does not legitimately question the clinical motives of all other providers. These are simply potential risks involved in the transactions, and they should be evaluated appropriately.



Legal Summary

Similar issues were raised with respect to the private equity acquisition of Hahnemann Hospital. In the article titled “The Death of Hahnemann Hospital” published in the New Yorker magazine in May 2021, the author, Chris Pomoroski, speculates that the PE acquisition of Hahnemann Hospital was always, at least partially, a real estate play. Senator Bernie Sanders was quoted in the article as saying:

“If an investment banker like Joel Freedman is able to shut down Hahnemann and make a huge profit by turning this hospital into luxury condos, it will send a signal to every vulture fund on Wall Street that they can do the same thing, in community after community after community”.

Just from a historical perspective, it should be noted that Hahnemann has had an illustrious clinical history but a recently troubled financial history. Hahnemann was acquired by AHERF, the forerunner of Allegheny Health Network, in 1993. Tenet Healthcare bought Hahnemann out of the AHERF

bankruptcy in 1998. Tenet went through its own bankruptcy difficulties and, in 2018, sold its remaining Philadelphia assets, i.e. Hahnemann Hospital and St. Christopher’s Hospital, to American Academic Health System, which then closed Hahnemann Hospital in June of 2019.

Additional Investigative and Enforcement Activity

In 2017, a whistleblower suit was filed against Surgery Partners, Inc. in United States ex rel. Cho and Baker v. Surgery Partners, Inc. alleging liability on behalf of the private equity managers because of their management control and direction. However, federal appeals court recently upheld the dismissal of the whistleblower suit against the private equity firm, HIG Capital.

In February of 2021, the National Bureau of Economic Research published a paper by Atul Gupta, Sabrina T. Howell, Constantine



Yannelis and Abhinav Gupta positing that their research shows that “PE ownership increases short term mortality of Medicare patients by 10%, in nursing homes”.

In November of 2022, the Office of the Attorney General of the State of New York and the NY Medicaid Fraud Control Unit filed an action against Comprehensive at Orleans LLC, d/b/a The Villages of Orleans Health and Rehabilitation Center, alleging inadequate care at the facility and naming not only the nursing home facility, i.e. “The Villages”, but the real property holding company, the management company, an entity identified as the pass-through entity “Villages of Orleans LLC” and various other investors.

Conclusion

Multiple sources, including CMS, have reported that healthcare spending in the USA exceeded \$4 trillion in 2022, and constituted almost 19% of USA GDP. Therefore, it is obvious that the healthcare sector will provide massive investment opportunities. Those of us who “advise” healthcare clients obviously must recognize all points of view.

A graphic for the Allegheny County Medical Society (ACMS) social media presence. It features a man in a white lab coat and blue lanyard looking at a smartphone. The background is a blurred office setting. The text “ACMS is on social media!” is prominently displayed. Below it, a line of text says “Follow the society wherever you go for updates on news, events, and everything Allegheny County Medical Society.” and “STAY TUNED FOR MORE”. At the bottom, there are four social media icons with their respective handles: Instagram (@ALLEGHENYCOUNTYMS), Facebook (ALLEGHENY COUNTY MEDICAL SOCIETY), Twitter (@ALLEGHENYCMS), and LinkedIn (ALLEGHENY COUNTY MEDICAL SOCIETY).