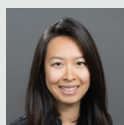


The Growth of Private Equity in US Health Care: Impact and Outlook

EXECUTIVE SUMMARY

Private equity (PE) investment plays a growing and significant role in the financing of health care in the United States. In 2022, an estimated 863 health care related service deals were closed by PE firms, after reaching a peak of 1,013 transactions in 2021 (PitchBook Data Inc., 2022). More than 90% of PE-related takeovers or investments are not reviewed as there is little regulation of PE investment (Schulte, 2022). Private equity firms prioritize short-term profits, typically moving on from their health care investments within three to seven years (Bruch et al., 2020). While PE investment in health care may improve operational or technological efficiencies, there are concerns about the effects on cost, quality, and utilization of care. Overall, research has found that PE involvement in health care has led to changes in the workforce, increased costs and utilization, mixed effects on quality of care, and a lower percentage of Medicare patient discharges, implying an increase in privately insured patients with higher reimbursement rates (Bruch et al., 2023; Bruch et al., 2021; Offodile II et al., 2021; Bruch et al., 2020).

CONVERSATION WITH THE RESEARCHERS



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Q: How does private equity involvement impact health care consumers?

Song: There are at least three ways in which PE acquisitions have affected patients. First is through influencing access to care. In the earlier years of PE activity, acquired hospitals frequently closed less profitable service lines and sometimes closed entirely. Second is through prices. PE acquisitions have been shown to increase charges and negotiated prices, which translate into higher cost-sharing and are ultimately passed on to taxes or lost wages. Third is through utilization, as the volume and intensity of services have also changed in inpatient and outpatient settings following PE acquisition.

Zhu: Evidence also suggests mixed results on quality of care. The most consistent evidence has been an increase in prices and spending. This is important because when prices go up in the health care system, this often translates into higher patient costs.

Q: Where do you foresee private equity involvement in health care going?

Zhu: PE often leverages a first mover advantage by being first to a market area – it enters a particular industry, quickly consolidates, and exits. Our data suggests that PE has now entered into nearly every field in health care, particularly those that participate in value-based payment arrangements. I think PE will increasingly look at targeted approaches that will easily weather economic downturn, and respond creatively to growing policy and regulatory interest in their investments and effects.

Song: As long as there is minimal risk to PE firms from leveraged buyouts, tax benefits, few transparency requirements, and little regulation, PE acquisitions in health care will likely continue. Recent turmoil in US banking and interest rate hikes have made it more expensive to borrow, potentially making PE funding attractive to providers. PE firms face some headwinds nonetheless. Insurers are also acquiring practices, which raises the prices of acquisition and makes it harder for PE to exit with a profit quickly. Laws to stop surprise billing also help curtail profits.

Q: Why are many providers interested in selling to private equity firms?

Song: Human labor, physical capital, supplies, malpractice insurance, and other costs all chip away at margin, separate from the non-financial costs of managing a care delivery entity. As Jane said earlier, PE offers providers a source of capital, which many need or are looking for. Sometimes providers may seek out PE as much as PE targets providers for acquisition.

Zhu: A willing buyer needs a willing seller, and for many physician practice owners, the alternative to PE is not remaining independent, it's an eventual sale to another corporate entity. For older practice owners seeking an exit after a lifetime of practice building, PE may have the advantage of continued equity.

Q: What are the current policies that enable private equity in health care to expand?

Zhu: PE serves as an important source of capital to many health care entities in order to keep up with large competitors. In many ways, PE is both a response to and an accelerator of broader health system trends. PE is particularly adept at identifying undervalued and underperforming entities. At the same time, PE activity is not subject to a ton of scrutiny for several reasons - transactions are often not transparent, which makes it hard to track, PE's strategy allows smaller transactions to escape reporting, and PE is permitted to treat its profits at a lower capital gains tax rate.

Song: About 90% of PE transactions are exempt from federal review. Yet these smaller acquisitions in suburban and rural markets can have large effects on competition. Regulatory agencies are relatively under-resourced to provide oversight. Moreover, inherent features of health care have facilitated entry, including fragmented practices, predictable third-party payment, and reliability of demand for health care.

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RESEARCH ROUND UP

Private equity firms' increased participation in the health care sector may be due to a variety of factors, including limited regulation, a fragmented delivery system, an aging population, and multiple avenues of profitability and cost reduction (Cerullo et al., 2022B). While more research is needed, it is important to understand the current research on the effects of PE involvement on cost, quality, and utilization of care.

Cost

After PE acquisition of independent physician practices or contracting with PE firms, studies found increases in the charged amount per claim and allowed amount per claim (the maximum amount a health plan will pay for a covered service) (Bruch et al., 2020; Singh et al., 2022A; La Forgia et al., 2022; Offodile et al., 2021).

A cohort study of PE-acquired hospitals found increases in charge to cost ratios (the charged amount compared to the actual cost of the medical expense), including a \$407 increase in total charge per inpatient day (Bruch et al., 2020). Singh et al. (2022A) uncovered a \$23 rise in the allowed amount per claim and an average increase of \$71 charged per claim when comparing PE-acquired and non-acquired practices across three specialties. Utilizing commercial claims data, La Forgia et al. (2022) reported an even greater increase in the allowed amount per claim among anesthesia practitioners: \$116.39. Offodile II et al. (2021) studied PE-acquired hospitals between 2003 and 2017 and observed higher charge to cost ratios in PE-acquired sites than non-acquired sites. However, not all studies found that PE acquisition leads to increased costs. When comparing acquired and non-acquired hospitals between 2005 and 2014, Cerullo et al. (2022B) reported at least a \$432 decline in costs per discharge.

Consolidation

Private equity firms are highly incentivized to consolidate health care providers in order to maximize profits (Scheffler et al., 2021). Private equity firm purchasing of independent physician practices typically follows a "platform and add-on" approach, where the firm acquires an established clinical practice ("the platform") and then acquires smaller, additional practices ("the add-ons") (Zhu & Polsky, 2021). This approach allows PE firms to continually build market power; however, consolidation and subsequent acquisitions have anticompetitive effects (Brown et al., 2021; Matthews & Roxas, 2022; Scheffler et al., 2021). A growing body of research has found that consolidation in health care leads to increased prices and lowered or stagnated quality of care (King, 2023; Beaulieu et al., 2020; Capps et al., 2018; Cooper et al., 2018; Baker et al., 2014).

Utilization of Care

The ongoing PE focus on maximizing short-term revenue increases the risk of overutilization of health care, or the use of unnecessary or low-value care. A study of three specialties found a 37.9% increase in visits by new patients and a 25.8% increase in unique patients seen at PE-acquired sites (Singh et al., 2022A). These findings may be the result of changes in management and practice operations under PE ownership (Bruch et al., 2023; Singh et al., 2022A). Braun et al. (2021) found that among dermatology practices, there was a 15% increase in patients seen. However, in the adjusted difference-in-differences results, acquisition was not statistically associated with changes in patients seen (Braun et al., 2021). Cerullo et al. (2022B) also found an increase in patient throughput and inpatient utilization.

Quality of Care

Consolidation of practices has led to changes in quality of care received by patients. Although, declines in quality have not been as strongly found in competitive markets, where pre-existing incentives for Centers for Medicare & Medicaid Services quality metrics exist (Matthews & Roxas, 2022).

A study of 21 million Medicare beneficiaries with acute medical conditions found an association between PE-acquisition and significantly lower inpatient mortality and 30-day mortality among patients with acute myocardial infarction. For patients admitted with acute stroke, the comorbidity burden also decreased slightly (Cerullo et al., 2022A). In another study among 204 hospitals acquired by PE firms between 2005 and 2017, greater improvements in process quality measures were observed when compared to non-acquired hospitals (Bruch et al., 2020). It is important to note that when the Hospital Corporation of America (HCA) hospitals were removed from Bruch et al.'s (2020) data set, quality metrics declined and acquired hospitals performed worse. The HCA company has had a long-term focus on quality metrics. Also, a more recent study by Bruch et al. (2021) observed that among community hospitals acquired in 2018, a year after the scope of the previous study, patients at acquired hospitals had slightly lower patient experience scores.

Geographic Dispersion

Private equity firms' tactics to acquire practices may accelerate consolidation of practices in the same geographic market or across several regions, impacting patients' choice in where they receive care and potentially creating gaps in care (Matthews & Roxas, 2022; Johnson & Frakt, 2020). There is substantial variation in PE involvement across the country. Singh et al. (2022B) found that across six office-based specialties, PE penetration was highest in DC, Arizona, New Jersey, Maryland, Connecticut, and Florida. There were no identifiable acquisitions in 11 states. Offodile II et al. (2021) found higher activity in mid-Atlantic and Southern states. Though more research is needed to understand why PE involvement is more heavily concentrated in some regions, it may, in part, be due to state regulations that incentivize investment.

POLICY

Private equity transactions are difficult to regulate and often not reviewed by antitrust authorities, as they tend to be below the federal mandatory reporting threshold (Federal Trade Commission A, 2020). More than 90% of PE-related takeovers or investments are not reviewed as there is little regulation of PE investment (Schulte, 2022). The acquisitions that are reviewed can still have widespread impacts on health care markets. Monitoring PE firms' ownership and consolidation of practices is especially important as reducing competition may have long-term effects on pricing and spending. In some cases, state reform may be more successful than passing federal antitrust legislation, which may face hurdles (Cai & Song, 2023). Currently, Oregon and Massachusetts have programs in place to monitor antitrust activity and review health care transactions (Davison et al., 2023).

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