The Regulatory & Policy Levers Affecting Private Equity Growth

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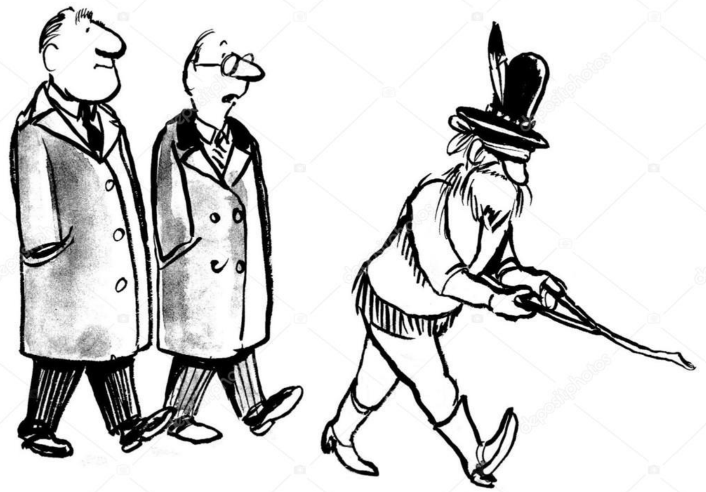
Premise:

- PE and corporate investors are extremely adept at identifying and exploiting health care market failures (hence, functions as a divining rod)
- Identifying the revenue playbook will point to the policy response



"This guy is great at finding revenue streams."

Playbook: Hospital-Based Physicians

E.g., Emergency, Anesthesiology, Radiology, Hospitalists

- Exploit market failure and payment loophole: Surprise out-of-network billing.
- Stay out-of-network as a revenue strategy.
- Threat of surprise billing to increase in-network rates.

Policy Response: No Surprises Act of 2020 (and state surprise billing laws before that)

Playbook: Office-Based (Proceduralists)

E.g., Dermatology, Ophthalmology, Gastroenterology, Orthopedics

- Office-based, outpatient specialties not target of hospital-buyers
- Predominantly fee-for-service. Steady commercial and Medicare revenue stream + cash revenue (e.g., Lasik, cosmetic derm)
- Wraparound services (e.g., physician-administered drugs, pathology, physical therapy)
- Increase volume of patients, procedures, intensity of procedures, reduce staffing levels

Playbook: Value-Based Payment, Primary Care Practices

- “Platform” model builds extensively on existing “must have” group. Partner with payers to create vertically integrated pay-vider.
- Aggressively code of diagnoses to garner higher risk-adjusted payments from MA plans
- Grow MA population, maximize capitated “budget,” reduce costs with utilization management
- Capture patient data and referrals for other service offerings (e.g., pharmacy)

Policy Lever: Close payment loopholes

1. Close payment loopholes exploited by PE investors
   - E.g., The No Surprises Act, state surprise billing laws
2. Change Medicare Part B payment system for physician-administered drugs
3. Increase Medicare Advantage coding-intensity adjustment, increase recoupment of overpayments via RADV audits, increase difficulty for star ratings

Policy Lever: Antitrust Enforcement

1. Increase antitrust scrutiny to counteract vertical consolidation
   - But, physician practice acquisitions “fly under the radar”
   - FTC/DOJ reluctant to challenge vertical and cross-market mergers (e.g., CVS-Oak Street)
2. Federal government:
   - Remove exemption for reporting smaller physician deals
   - FTC should study PE-driven consolidation in physician markets
3. States can pass laws to scrutinize below-the-radar deals

Policy Lever: Fraud and Abuse Enforcement

1. Increase fraud and abuse enforcement to address up-coding, unnecessary care, self-referrals for wrap-arounds
2. PE-firms, corporate owners are deep pockets who can be found liable for knowing participation in revenue strategies of up-coding, unnecessary services, self-referrals (in violation of False Claims Act)
3. Complex structure of platform + add-on practices can violate Stark Law, Anti-Kickback Statute

Policy Lever: State Employment, Corporate Practice of Medicine Laws

1. Restrict the scope, duration, and applicability of physician non-competes
2. Restrict “non-disparagement” gag clauses for patient care or fraud and abuse
3. Strengthen the corporate practice of medicine laws to restrict lay-control over clinical concerns *and* practice management

Policy Lever: Targeting PE itself

1. Closing the carried interest tax loophole
   - PE 20% investment profits taxed at long-term capital gains rate (20%) vs ordinary income (37%), not subject to self-employment taxes.
   - Inflation Reduction Act (2022) would have fixed, but Krysten Sinema insisted it be taken out.
2. Transparency of PE ownership in health care
   - Recent House E&C bill would require providers to publicly report parent company, ownership structure, and key transactions.

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

Additional resources

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

Erin Fuse Brown, Loren Adler, Erin Duffy, Paul B. Ginsburg, Mark Hall, and Samuel Valdez

USC-Brookings Schaeffer Initiative for Health Policy

This report is available online at:
https://www.brookings.edu/essay/private-equity-investment-as-a-divining-rod-for-market-failure-policy-responses-to-harmful-physician-practice-acquisitions/

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https://papers.ssrn.com/sol3/papers.cfm?abstract_id=4373557