Private Equity Acquisition of Physician Practices - Caveat emptor

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What is Private Equity?

Private Equity Firm
(General Partner)

Limited Partners (Investors)
(public pension funds, corporate pension funds, insurance companies,
high net-worth individuals, family offices, endowments, foundations,
fund-of-funds, sovereign wealth funds, etc.)

Ownership of the Fund

Private Equity Fund
(Limited Partnership)

The Fund’s ownership of the portfolio investments

Investment

Investment

Investment
The Growth of Private Equity in Health Care 2010-2020

Scheffler RM, et.al., American Antitrust Institute 2021
What Ever Happened to the Corporate Practice of Medicine Bar?

- It no longer exists in some states
- In most states the private equity firms work through a Physician Management Company (PMC), or Management Services Organization (MSO) which is legal…..
Private Equity Usually Invests in Physician Practices Via Physician Management Companies

AHLA- 2020
What Ever Happened to the Corporate Practice of Medicine Bar?

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- Practice revenue flows to the PMC, then to the physicians, with "excess" to the PE entity
- PE entity usually appoints the practice physician "leader", who is affiliated with the PE entity
Why are Physicians Selling to Private Equity?

- Falling practice revenue
- High malpractice costs—anesthesia, E.R.
- One time cash payments—9-12x annual practice “profit”
- Capital for practice expansion/market consolidation
- Converting part of physician income to capital gains, via a lower “salary”
- Administrative simplification
Potential Impact on Practice Structure, and Professional Independence

- Pressure to cut costs-staffing (an expectation going in), service and quality
- Pressure to substitute physician ancillary providers
- Pressure to do more procedures than appropriate
- Physicians are usually “locked-in” by PMC contract, known as “captive physician model”
- This is different from hospital ownership of physician practices—the time frame makes the incentives different
Is the Model Sustainable Long Term?

- The Phycor and MedPartners PMC experience in the 1990s
- Revenue enhancement and cost cutting are finite in medicine; this is not Silicon Valley
- 5-7 year timeline for private equity exit-20-30% expected return to investors
- Who will be the “greater fool”?
An Ethical Problem for Physicians

“You can’t serve two masters. You can’t serve patients and investors”

Dr. Michael Rains-U.S Dermatology Partners in Bloomberg Business Week-“How Private Equity is Ruining American Health Care”- May 20, 2020
What Can Be Done?

- Federal Trade Commission oversight—the $94M threshold for reporting practice acquisitions
- The “Bully Pulpit”
  - AMA communication of the issues to physicians to promote general awareness
  - A review and updating of the AMA Code of Medical Ethics with special attention to professionalism issues related to private equity practice acquisition
References


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• Zhu JM, et.al. Private equity acquisition of physician medical groups across specialties, 2013-2016. 2020 (Research Letter) JAMA 323(7)663-665

• Reinhardt UE. The rise and fall of the physician practice management industry: Can Wall Street efficiently value health care? 2020 Health Affairs 19(1)42-55

• Bruch JD, et.al. Changes in hospital income, use, and quality associated with private equity acquisition. 2020 JAMA Intern Med 180(11)1428-1435
References


• ** If you have a hour to spare and want to watch a discussion of how private equity works from those who help design these investments