

Insights

STATE REGULATION OF PHYSICIAN PRACTICE TRANSACTIONS: WHAT INVESTORS NEED TO KNOW

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In recent years, private equity firms and retail giants like CVS and Walmart have acquired many physician practices and physician practice management organizations across the country. As healthcare has become increasingly dominated by national, for-profit corporations, many states have correspondingly increased their oversight of such transactions, citing concerns about patient choice, quality of care and increase in healthcare costs.

Most recently, New York^[1] and California^[2] have passed legislation that requires parties to a material transaction involving a physician practice or, notably, in New York, a management services organization, to provide prior notice of the transaction to regulatory authorities in the state. As described below, the materiality threshold for reporting is low – many previously unregulated transactions will require review. While neither state statute gives the reviewing body the authority to block the proposed transaction, the regulators are permitted to refer the transaction to the state’s attorney general for additional review. In addition, details of the transaction are in many cases subject to public review and comment.

Below are summary dropdowns comparing select, key provisions of the new California and New York statutes, *as they relate to physician practice and physician management company transactions*. Note that the California regulations cited below have not been formally adopted, so are subject to change. For example, in the first draft of the regulations, physician management services organizations were included in the purview of the regulations, but in the most recent draft, distributed on October 9, 2023, that provision was removed. Comments to the revised regulations were due back to regulators by October 17, 2023.

| | New York | California |
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| Agency | New York State Department of Health (“NYDH”) | California’s Office of Health Care Affordability (“OHCA”) |
| Statute Effective Date | August 1, 2023 | January 1, 2024 (for transactions entered into on or after April 1, 2024) |
| Which entities are subject to the | Health care entities, including, | Health care entities, including |

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| <p>regulations?</p> | <p>physician practices and management services organizations or similar entities providing all or substantially all administrative or management services under contract with one or more physician practices.</p> | <p>“physician organizations”, i.e., in relevant part, a medical group practice (however organized) that is comprised of 25 or more physicians or has less than 25 physicians but is a high-cost outlier (i.e., its costs for the same services provided are substantially higher compared to the statewide average).</p> |
| <p>What is a “material” transaction?</p> | <p>Any of the following (but only if the transaction results in a health care entity increasing its total in-state revenue by more than \$25 million):</p> <ul style="list-style-type: none"> ▪ a merger with a health care entity; ▪ an acquisition of one or more health care entities, including, but not limited to, the assignment, sale, or other conveyance of assets, voting securities, membership or partnership interest, or the transfer of control; ▪ an affiliation agreement or contract formed between a health care entity and another person; or ▪ the formation of a partnership, joint venture, accountable care organization, parent organization, or management services organization for the | <p>Any of the following:</p> <ul style="list-style-type: none"> ▪ A transaction concerning the provision of health care services that is assessed to have a fair market value of \$25 million or more. ▪ A transaction likely to increase annual revenue of any health care entity that is a party to the transaction by at least \$10 million or 20% of annual revenue at normal levels of operation or utilization. ▪ A transaction that involves the sale, transfer, lease, exchange, option, encumbrance, or other disposition of 20% or more of the assets of any health care entity in the transaction. ▪ A transaction involving a transfer or change in control, responsibility, or |

purpose of administering contracts with health plans, third-party administrators, pharmacy benefit managers, or health care providers as prescribed by the commissioner by regulation.

governance of a health care entity.

- A transaction where an entity is negotiating or administering contracts with payers on behalf of one or more providers where the transaction involves an affiliation, partnership, joint venture, accountable care organization, parent corporation, management services organization, or other organization.
- A transaction involving the formation of a new health care entity, affiliation, partnership, joint venture, or parent corporation for the provision of health services in California that is projected to have at least \$25 million in annual revenue at normal or stabilized levels of utilization or operation or have control of assets related to the provision of health care services valued at \$25 million or more.
- A transaction involving a health care entity joining, merging, or affiliating with another health care entity, affiliation, partnership, joint venture, or parent corporation related to the

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| | | <p>provision of health care services where any health care entity has at least \$10 million in annual revenue.</p> <ul style="list-style-type: none"> ▪ A transaction that changes the form of ownership of a health care entity that is a party to a transaction, including but not limited to change from a physician-owned to private equity-owned and publicly held to a privately held form of ownership. ▪ A transaction where a health care entity has been a party to a transaction regarding the provision of health care services in California with another party in the transaction within ten years prior to the current transaction. |
| Timeline for notice submission | 30 days prior to the target closing date. | 90 days prior to the target closing date. |
| Penalties | The NYDH may fine entities up to \$2,000 per day of non-compliance and an additional \$5,000 if the non-compliance poses a serious threat to health and safety. | Not specified. |
| Information subject to public review and comment | <p>Yes – NYDH will post:</p> <ul style="list-style-type: none"> ▪ Summary of transaction ▪ Explanation of groups likely to be impacted by the transaction | Yes, if OCHA determines the proposed transaction is likely to have a risk of significant impact on market competitions, the state’s ability to meet cost targets or costs for purchasers and consumers, then OCHA is |

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| | <ul style="list-style-type: none"> ▪ Information about services currently provided by health care entity, commitments by the health care entity to continue such services and any services that will be reduced or eliminated ▪ Details about how to submit comments. | <p>required to make the notice of material change publicly available, including all information and materials submitted to the office for review.</p> <p>Health care entities can mark certain documentation as confidential (including stock purchase agreements and certain other financial information).</p> |
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There is pending legislation in many other states (e.g., North Carolina, Pennsylvania, Maine and Oregon) that, if passed, would similarly impact certain physician practice transactions that have heretofore been exempt from any formalized state regulatory scrutiny. We anticipate that this trend will continue to grow, and prior notice and disclosure requirements will become increasingly common in the industry.

As such, it is important for acquirers to add compliance with these new state laws as a fundamental element of their transaction program strategy. As a threshold matter, careful consideration must be given to whether the relevant state review process is triggered by the transaction. These new laws are complex and nuanced, so effective legal counsel is essential. If compliance is required, proactive communication with the target about timing, submittal of information to the regulatory authority and strategy for response to regulator inquiries is necessary to set appropriate expectations and maintain goodwill with the target.

Changes will also need to be made to template transaction documentation to account for these new laws, including, for example, updating conditions to close, accounting for a delayed closing (if the investor previously pursued a simultaneous sign and close strategy) and reviewing indemnification provisions to account for any appropriate shifts in risk allocation.

BCLP has significant experience navigating novel, complex regulatory requirements like the new laws passed in California and New York. Please contact Jennifer C. Hutchens, Kelly Koening or any member of our Healthcare and Life Science industry team to discuss.

FOOTNOTES

[1] NY Pub. Health L. § 4550, et seq.

RELATED PRACTICE AREAS

- Healthcare & Life Sciences

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