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Private Capital's Impact on Health Care Insolvency Proceedings

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Introduction to the Panel

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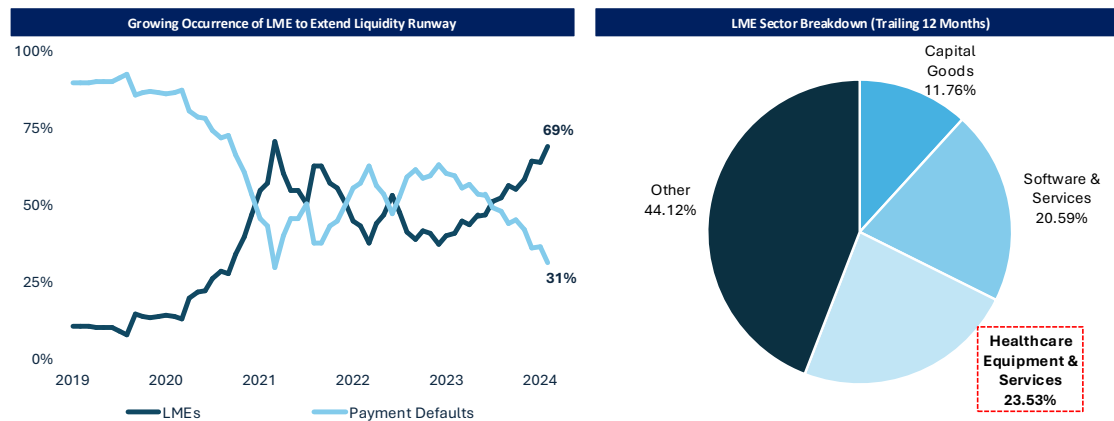
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Healthcare Sector | Key Considerations Post-Election



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Liability Management | Increasing Execution in 2024



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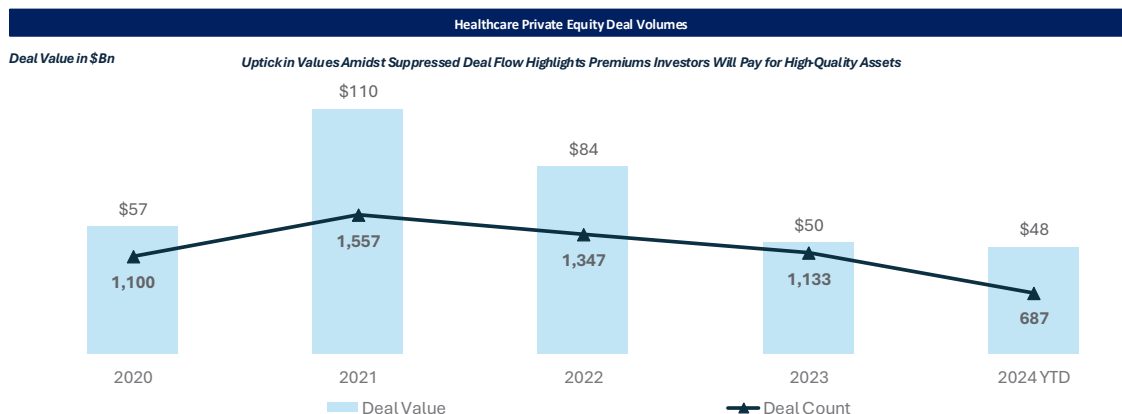
Liability Management | Recent Liability Management Exercises

Select Recent LMEs					
Date	Company	Sector	LME Type	Ratings Action	S&P Rating
9/16/2024	Pretium Packaging	Industrials	Distressed Exchange	Downgrade	SD
9/13/2024	Carestream Dental	Healthcare	Distressed Exchange	Downgrade	SD
9/11/2024	Windstream Services	Media & Entertainment	Consent Solicitation	None	B-
9/5/2024	Beasley Broadcasting	Media & Entertainment	Super-Priority Loan, Distressed Exchange	Downgrade	CC
9/3/2024	Lumen Technologies	Technology	Distressed Exchange	Downgrade	CC
8/27/2024	McAfee Enterprise	Technology	Super-Priority Loan, Distressed Exchange	Upgrade	CCC+
8/22/2024	SIRVA Inc	Logistics	Super-Priority Loan, Distressed Exchange	Upgrade	CCC+
8/27/2024	McAfee Enterprise	Technology	Super-Priority Loan, Distressed Exchange	Upgrade	CCC+
8/15/2024	Brightspeed	Media & Entertainment	Super-Priority Loan, Distressed Exchange	Upgrade	CCC+
8/7/2024	Community Health Systems	Healthcare	Distressed Exchange	Downgrade	SD
7/29/2024	Team Health	Healthcare	Refinancing	Upgrade	B-



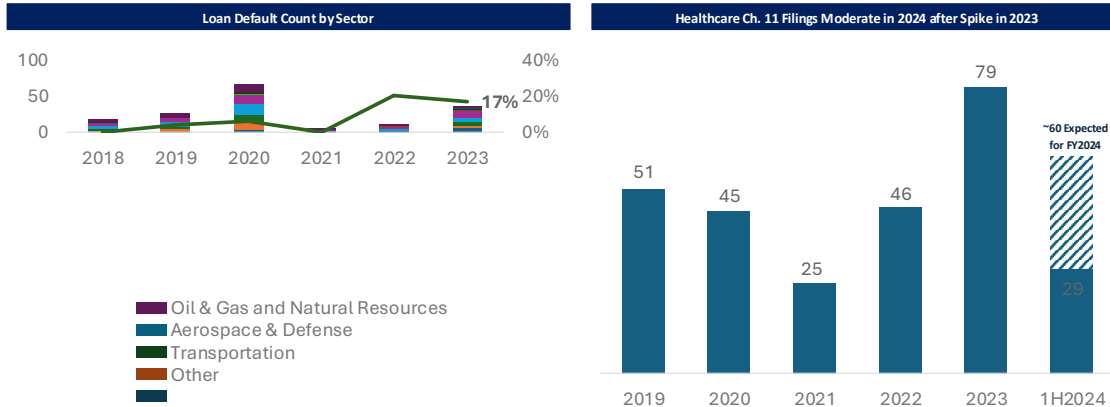
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Healthcare M&A | Sponsor-Backed Transaction Environment and Outlook



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Economic Headwinds Facing the Healthcare Industry

- Vastly increased labor costs
- Difficulty in recruiting staff at any cost
- Vacancy and other underperformance issues
- Increased costs of medical and other supplies
- Costs of technology in an “arms race” between providers
- Inability to increase reimbursement rates
- Population demographics
- Widespread perception of fraud against Medicare/Medicaid
- Increase of bad debt / uncollectible receivables
- Cyber threats
- Infrastructure costs to build



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8

Impact of Private Equity on the Healthcare Industry

- Private equity (PE) has become a major player in the US healthcare sector, investing primarily in biotechnology and pharmaceuticals, but also in hospitals, nursing homes, physician practices, and more.
- Nationally, between 2019-2023, PE deals to acquire health care service providers totaled \$46.9 billion and represented over half of all PE deals in the broad health care economy. PE firms now own approximately 8% of all private hospitals in the U.S.
- PE participation certainly has the potential for positive impacts, they also raise concerns about patient care and costs. See S. 4503 – Corporate Crimes Against Healthcare Act of 2024 (Introduced by US Senators Elizabeth Warren (D-Mass.) and Ed Markey (D-Mass.))



State and Federal Regulators Act

- PE participation certainly has the potential for positive impacts, they also raise concerns about patient care and costs.
- For example, in response to the Steward bankruptcy, Senators Elizabeth Warren (D-Mass.) and Ed Markey (D-Mass.) introduced **The Corporate Crimes Against Health Care Act**, which would have, among other things, (1) created a criminal penalty of up to 6 years in prison for executives who “loot” health care entities like nursing homes and hospitals, if that looting results in a patient’s death; (2) provided state attorneys general and the DOJ with the power to claw back all compensation, including salaries, issued to private equity and portfolio company executives within a 10-year period before or after an acquired health care firm experiences serious, avoidable financial difficulties due to that looting; and (3) prohibited payments from federal health programs to entities that sell assets or use assets for a loan collateral made to a REIT, with an exemption for current arrangements.
- California’s Governor vetoed AB 3129, citing concerns regarding the redundancy of the bill with the California’s Office of Health Care Affordability’s existing authority to review and evaluate health care transactions in the state. AB 3129 would have required PE and hedge fund investors to obtain consent from the state AG for certain health care investments and would have imposed restrictions on management relationships between PE and hedge fund-backed MSOs/DSOs and physician, psychiatric and dental practices.



Private Equity Investment Is Pervasive

- Private equity investors spent more than \$200 billion on health care acquisitions in 2021 alone, and \$1 trillion in the period 2013-2023.
- Private equity firms have long been active in hospital, nursing home, and home care settings. More recently, acquisitions of physician practices have skyrocketed, especially in high-margin specialties like dermatology, urology, gastroenterology, and cardiology. Private equity acquisitions of U.S. physician practices rose sixfold over a decade, from 75 deals in 2012 to 484 in 2021.
- A recent study showed that in 13 percent of metropolitan areas, a single private equity firm owns more than half of the physician market for certain specialties. One area of considerable private equity investment has been physician practices through add-on consolidation, and then selling the entity in 3–8 years (“exit”).
- With regard to PE exits from dermatology, ophthalmology, and gastroenterology (physician specialties with the largest number of acquisitions between 2016 and 2020): of 807 acquisitions, over half (51.6%) of PE-acquired practices underwent an exit within 3 years of initial investment. In nearly all instances (97.8%), PE firms exited investments through secondary buyouts, where physician practices were resold to other PE firms with larger investment funds.
- Between investment and exit, PE firms increased the number of physician practices affiliated with the PE firm by an average of 595% in 3 years.



Private Equity Investment In Healthcare Is Not New

- Generally, private equity in health care is a form of for-profit ownership reflecting investment in health care facilities by private parties.
- Public, investor-owned organizations sell shares to the public that trade on a stock exchange. UnitedHealth Group, which now owns thousands of physician practices, is one example. Another is Hospital Corporation of America. These organizations are regulated by multiple federal laws and agencies, including the U.S. Securities and Exchange Commission.
- Shares of private, investor-owned organizations — such as private equity-owned firms — are not traded on public markets. As such, they aren’t required to follow the same regulations as public companies.
- Private equity is not new to health care. Private investors have always invested in and owned health care facilities, including individual physicians who invest in and own their for-profit private practices, and physicians and other private investors have long owned health care facilities, such as specialty hospitals, dialysis units, ambulatory surgical centers, and imaging units.



Shifts In Private Equity Investment In Healthcare

- There have been two key shifts in recent years.
- The first is in who's doing the investing. Instead of physicians or small groups of investors using their own funds, investors now also include firms that manage funds for large groups of wealthy individuals or institutions. Fund managers and their investors may have little knowledge of health care, viewing it as just another market opportunity.
- The second change relates to how they're investing.
- A third approach to getting a quick return is to flip the asset, for a large multiple of the original price. To attract such a buyer, however, the private equity firm must boost the organization's profits, which usually requires rapidly cutting costs, raising prices, or increasing the number of services provided.



Private Capital's Increasing Role in Healthcare Restructuring

- With the increasing role of private capital (debt and/or equity) in health care businesses, from hospitals to specialty practices, the financial pressures, challenging payor reimbursement rates, and regulatory environment have led to a growing number of restructurings and bankruptcies in this sector.
- Health care insolvency proceedings involving private-equity ownership and use of private capital have significant impact on restructuring strategies, regulatory and compliance challenges, patient care considerations, and the role of the courts in balancing financial recovery with public health concerns.



Legal and Business Structures

- Key legal and business structures of private equity funds that invest into health care business include:
- Platform and add on models,
- Loans to repay investors,
- Selling assets and creating an “propco” and “opco” structure,
- Management services organization (in jurisdictions that regulate the corporate practice of medicine), and
- Rolls ups.



Private Capital Legal Structures

- key legal structures of private capital agreements include:
- pledge of equity interests,
- warrants, and
- earn-outs.



Legal Issues Facing Distressed Health Care

- The key legal issues facing a distressed health care business seeking to restructure their capital or sell their business assets through a bankruptcy or other insolvency proceeding include:
- Government regulators including state attorney generals,
- Government payors, including Medicare, Medicaid, Tri-Care,
- Anti-trust considerations,
- Jurisdiction,
- Treatment of Government Provider Agreements, and
- Government payors right to recoup/setoff postpetition.



Recent Developments in Related Bankruptcy Law

- Recent developments in bankruptcy law related to the ability of a healthcare entity to restructure include:
- Application of the automatic stay to stop a government suspension of payments, even in the face of “credible allegations of fraud.”
- Application of the Bankruptcy Code to curtail a state Attorney General’s powers to alter the terms of a sale pursuant to section 363.
- Can the Bankruptcy Court adjudicate Medicare controversies without exhaustion of administrative remedies?
- Can a debtor sell a Medicare/Medicaid provider agreement under section 363 or must it be transferred as a contract under section 365?



Control Over Disposition of Nonprofit Assets

- California Corporations Code gives the AG the authority to approve, deny or condition any sale or change of control of a nonprofit general acute care hospital, or other “health facility” with a fair market value in excess of \$3 million.
- Section 363(d) of the Bankruptcy Code requires that a trustee can only sell or lease nonprofit property in accordance with non-bankruptcy law.
- Section 541(f) of the Bankruptcy Code allows a nonprofit to transfer property to a non-tax exempt entity if it would be permitted outside of bankruptcy.
- Section 1129(a)(16) of the Bankruptcy Code requires that a court confirm a plan only if all property transfers in the plan comply with non-bankruptcy law.
- A bankruptcy court in California determined conditions imposed on a sale by the California attorney general were an interest in property and that the debtor could sell free and clear of those interests. *In re Verity Health Sys. of Cal., Inc.*, No. 2:18-BK-20151-ER, 2019 WL 5585007 (Bankr. C.D. Cal. Oct. 23, 2019), vacated by No. 2:18-BK-20151-ER, 2019 WL 6519342 (Bankr. C.D. Cal. Nov. 13, 2019).



Does the Bankruptcy Court Have Jurisdiction?

- Some courts say “No” based on the legislative history. *In re Bayou Shores SNF*, 828 F.3d 1297 (11th Cir. 2016): “Because we are persuaded that the 1984 amendments to § 405(h) were a codification and not a substantive change, we ... hold that § 405(h) bars § 1334 jurisdiction over claims that ‘arise under [the Medicare Act].’”
- Other courts (3rd, 5th and 9th Circuits) say “Yes” and have held that the statutory bar on federal jurisdiction over unexhausted Medicare disputes does not apply to bankruptcy court jurisdiction under 28 U.S.C. §1334. *In re Benjamin*, 932 F.3d 293 (5th Cir. 2019) (“With respect to the majority of our sister circuits, we reject the non-textual approach exemplified by the Eleventh Circuit and join the Ninth Circuit in applying the third sentence’s plain meaning—a meaning that, everyone agrees, does not bar §1334 jurisdiction.”); *In University Medical Center*, 973 F.3d 1065 (3rd Cir. 1992); *Sullivan v. Town & Country Home Nursing Servs., Inc. (In re Town & Country Home Nursing Servs., Inc.)*, 963 F.2d 1146 (9th Cir. 1992).



Provider Agreement: Executory Contract or Not?

- *PAMC, Ltd. v. Sebelius*, 747 F.2d 1214, 1221 (9th Cir. 2014) ("[Here we hold that] '[u]pon joining the Medicare program, however, the hospitals received a statutory entitlement, not a contractual right.'"); *Memorial Hospital v. Heckler*, 706 F.2d 1130, 1136-37 (11th Cir. 1983) (holding that "[u]pon joining the Medicare program, however, the hospitals received a statutory entitlement, not a contractual right."); *In re Verity Health System of California, Inc.*, 606 B.R. 843 (Bankr. C.D. Cal. 2019) (Comprehensive discussion holding Medicaid provider agreement a statutory entitlement rather than an executory contract.); *In re BDK Health Management, Inc.*, 1998 WL 34188241 (Bankr. M.D. Fla. Nov. 16, 1991).
- *In re Vitalsigns Homecare, Inc.*, 396 B.R. 232, 239 (Bankr. D. Mass. 2008) ("[M]ajority of bankruptcy courts considering the Medicare-provider relationship conclude that the Medicare provider agreement, with its attendant benefits and burdens is an executory contract.").



Thank you!

•Questions?



Faculty

Samuel R. Maizel is a partner at Dentons US LLP in Los Angeles and leads the firm's distressed health care industry restructuring efforts nationwide. His practice includes bankruptcy matters as well as financial restructurings, both in and out of court. Mr. Maizel has served as lead counsel to debtors, trustees, buyers of assets, state attorneys generals and creditors' committees, and has served as a trustee, examiner, patient care ombudsman and consumer privacy ombudsman in chapter 7, 9 and 11 cases. His most recent debtor representations include Curitec, a durable medical equipment supplier that filed in Houston; Borrego Community Health Foundation, a chain of 19 federally qualified health care centers that filed in San Diego; Astria Health, a chain of nonprofit hospitals that filed in Yakima, Wash.; and Verity Health System of California, a chain of six hospitals and the second-largest nonprofit hospital bankruptcy case in U.S. history, which filed in Los Angeles. Mr. Maizel has lectured extensively, is widely published, and has been interviewed on television and radio. He is the only lawyer in the U.S. ranked in both health care and bankruptcy by *Chambers and Partners* and *The Best Lawyers in America*. A Fellow of the American College of Bankruptcy, Mr. Maizel was named a "Legal Visionary" by the *Los Angeles Times* in 2023; recognized as one of its "Top 100 Lawyers for 2022" by the *Los Angeles Business Journal*; awarded the "Outstanding Lawyer Award" for distinguished service as outside counsel to nonprofit organizations by the American Bar Association in 2022; and named by the *Daily Journal* as one of California's "Top Healthcare Lawyers" in 2021. In addition, Global M&A Network named him "Restructuring Lawyer of the Year" in 2020. In addition, he has been listed in *Super Lawyers* every year since 2007. Mr. Maizel received his B.S. in 1977 from the U.S. Military Academy at West Point, his M.A. from Georgetown University in government in 1983 and his J.D. in 1985 from George Washington University School of Law, where he won the Jacob Burns Prize for excellence in appellate advocacy and served as president of the Moot Court Board.

Jennifer L. Nassiri is a partner in the Finance and Bankruptcy Practice Group of Sheppard Mullin's Century City office in Los Angeles. She counsels secured and unsecured creditors, creditors' committees, licensors and licensees of intellectual property, landlords and tenants, equityholders and corporate officers, and special committees, among others, in the health care, retail, real estate, manufacturing, automotive and media and entertainment industries, in connection with pre-bankruptcy planning, restructurings and liquidations, both in chapter 11 and out of court. Ms. Nassiri has experience counseling chapter 11 debtors, lenders, special servicers, property owners, asset-purchasers, insiders and chapter 11 trustees, including liquidating trustees in a broad spectrum of complex issues in bankruptcy. Her practice includes chapter 11 plan litigation, § 363 sales, valuation disputes, debtor-in-possession financing, preference and fraudulent transfer litigation, and assignments for the benefit of creditors. She frequently counsels intellectual property licensors and licensees in distressed transactions and bankruptcy. Ms. Nassiri also has experience in the health care space, where she specifically guides clients through the complex world of distressed hospitals and nursing homes in chapter 11. She received her B.A. *cum laude* from the University of California, Los Angeles in 1996, where she was a member of the Golden Key National Honor Society, and her J.D. from Loyola Law School in 2000, where she made the Dean's List and was a member of the Phi Delta Phi Honor Society.

James R. Porter, ACA, JIEB, CIRA, CPE is a senior managing director in Accordion Partners's Turnaround & Restructuring Practice in Charlotte, N.C. He has 30 years of experience working with

clients across multiple industries, but he has focused on health care for the last 15 years. Mr. Porter has a broad range of experience in helping organizations solve problems involving the complicated interactions of business processes, workforce and regulatory matters. He has worked in the U.K. and the U.S. in both formal (*e.g.*, chapter 11 bankruptcy) and informal (*e.g.*, workout) situations. In addition to his C-level advisory experience, Mr. Porter has served in management capacities as CFO and treasurer at a number of distressed hospitals. Prior to joining Accordion Partners, he was a senior manager at ToneyKorf Partners, where he was involved in numerous situations involving merger activity with distressed hospitals. Prior to that, he was a principal in Grant Thornton's Restructuring practice, where he was responsible for all aspects of the client lifecycle, from relationship development through the execution of complex, transformational initiatives that drove significant operational improvements for his clients. Mr. Porter's consulting career has spanned numerous industries, including health care, manufacturing and telecom. He received his B.S. in mechanical engineering from Nottingham University, U.K.

Daniel M. Simon is a partner in the Atlanta office of McDermott Will & Emery, where he represents public and private companies, secured and unsecured creditors, acquirers of distressed assets, and investors in all aspects of corporate restructuring transactions. He represents a diverse range of clients spanning numerous industries in complex and contentious bankruptcy cases. Mr. Simon regularly helps clients navigate large-scale, complex, corporate bankruptcies, cross-border restructurings and a variety of special distressed transactions across industries. He also regularly lectures and publishes articles on restructuring topics, and has led several seminars held by leading industry organizations, including the Turnaround Management Association. Mr. Simon has been recognized as a Recommended Lawyer in 2022 in *Legal 500 USA*, and he received the Chapter 11 Reorganization of the Year in 2019 by The M&A Advisor for his work on ExGen Texas Power and the divestment of Handley Power to Exelon, and The M&A Advisor's Emerging Leaders Award in 2017. Mr. Simon is admitted to practice in Illinois and Georgia. He received his B.A. in 2005 from Vanderbilt University and his J.D. in 2008 from Duke University School of Law, where he served on the *Duke Law Journal*.