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Private Equity's Impact on the Nursing Home Industry

By Ben Seal

As COVID-19 tore through the United States in March 2020, nursing homes rapidly emerged as ground zero in the pandemic. Inhabited by vulnerable elderly and disabled residents, and staffed by overworked caregivers, American nursing homes became their own makeshift triage centers. Visitors were turned away. Family members, fearing the worst, kept calling, desperate for good news. In many cases, staff were too overwhelmed by outbreaks to even answer the phone.


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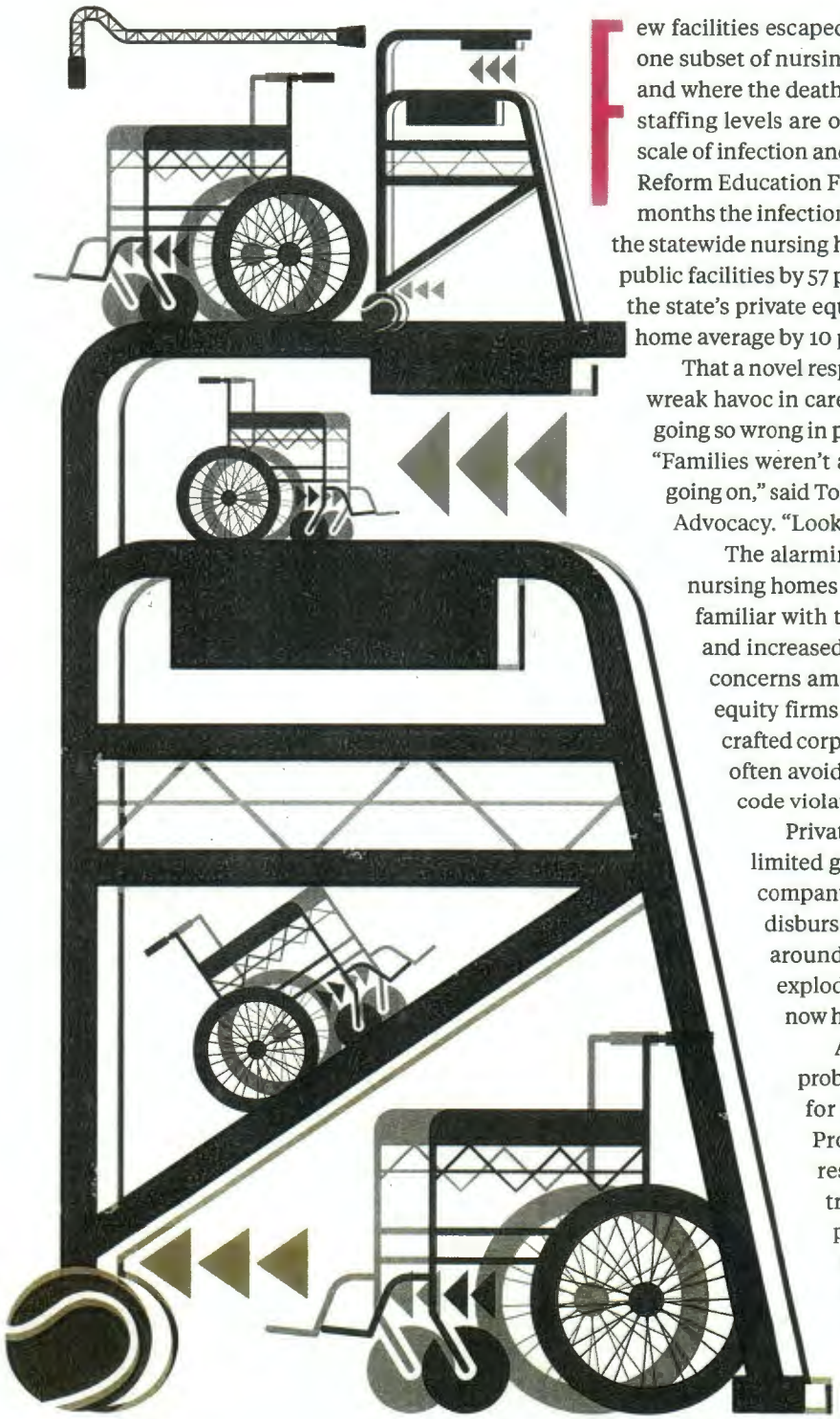

Few facilities escaped the first phase of the pandemic unscathed, but there was one subset of nursing homes where the virus spread with even greater ferocity—and where the death toll was even higher. Private equity-owned facilities, where staffing levels are often minimized to maximize profits, suffered an outsized scale of infection and death. According to a study by the Americans for Financial Reform Education Fund (AFREF), in New Jersey during the pandemic's first five months the infection rate at nursing homes with private equity owners exceeded the statewide nursing home average by 25 percent and the average rate at the state's public facilities by 57 percent. And the same study reported that the fatality rate in the state's private equity-owned nursing homes exceeded the statewide nursing home average by 10 percent.

That a novel respiratory virus that poses the greatest risk to the elderly would wreak havoc in care facilities was, in retrospect, predictable. But whatever was going so wrong in private equity nursing homes was invisible beyond their walls. "Families weren't allowed in, so people had very little idea what was actually going on," said Toby Edelman, senior policy attorney at the Center for Medicare Advocacy. "Looking in a window was hardly an answer."

The alarming scope of the damage that Covid inflicted on residents of nursing homes owned by private equity firms comes as no surprise to those familiar with the broader history of insufficient staffing, inadequate care and increased mortality at these facilities—a track record that has raised concerns among legislators, regulators and policy advocates. As private equity firms expanded their control in the nursing home industry, they crafted corporate structures that have enabled them to reap profits while often avoiding accountability for the disproportionate levels of health-code violations and death at their skilled nursing facilities.

Private equity firms typically work by pooling investments from a limited group of partners into a fund to purchase a stake in a private company with growth potential, then sell that stake years later and disburse the profits to the fund's partners. This structure has been around for decades, but it didn't take off until the 1980s and has exploded this century; thousands of American private equity firms now hold roughly $6 trillion in combined assets under management.

As their reach has expanded, their critics charge, so have the problems they have caused. According to a report from the Center for Popular Democracy and the Private Equity Stakeholder Project, private equity firms have been directly or indirectly responsible for 1.3 million lost jobs in retail and related industries in the last decade, while a study from the AFREF blamed private equity for more than half of bankruptcies since 2015. Critics have also assailed them for increasing tuition and student debt in higher education, and for unaffordable rents and higher eviction rates in the housing market.

In health care, private equity's stake has grown twentyfold over the past 20 years, and, according to a June 2021 study from the Medicare Payment Advisory Commission,

these firms now own 11 percent of nursing homes in the United States. Meanwhile, baby boomers are reaching the age at which they will begin to need these services and the proportion of elders in the population is ballooning: The nursing home industry overall is expected to grow to $240 billion by 2025.

Some studies suggest that private equity's participation in this sector has come at the expense of resident safety. A study published by the National Bureau of Economic Research (NBER) and led by Atul Gupta, an assistant professor of health care management at the Wharton School, reported that private equity ownership increases the short-term mortality of Medicare patients by 10 percent, accounting for nearly 2,000 unnecessary deaths each year.

Private equity's business model is built on the expectation of a significant return on investment over a short time frame. This model "is the exact opposite of what a primary goal should be in health care, which is to serve patients and deliver quality care," said David R. Hoffman, a practice professor of law at Drexel Kline whose consulting firm is a state and federal monitor for long-term care facilities. "Entities are entitled to a reasonable profit, but not at the sake of endangering patients."

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The Private Equity Playbook

Between 2000 and 2018, private equity's stake in the health care industry overall grew from $5 billion to $100 billion. Its focus on nursing homes also grew in that time, spurred by the enormous potential of an industry in which 70 percent of facilities are run as for-profits and 75 percent of the revenue comes from Medicare and Medicaid.

Robert I. Field, a Drexel Kline Law professor and director of the university's JD and Master of Public Health (MPH) dual-degree program, has studied the relationship between the public and private sectors in health care and how government policies impact the care provided in private facilities. In nursing homes, he said, the relationship is becoming increasingly dysfunctional.

"Private equity is taking that partnership to an extreme," Field said. "It's no longer a collaboration in the interests of better health care. It's becoming a raw profit-making opportunity."

In Pennsylvania, for example, Medicaid reimburses nursing homes $235 per resident per day, generating a reliable stream of revenue that makes it easy to manipulate costs to maximize profits.

"What could be better if you're running a business than a guaranteed customer base backed up by a large federal insurance pool?" asked Barry R. Furrow, a Drexel Kline professor and director of the school's health law program.

*Drexel Kline Law professors **David R. Hoffman, Robert I. Field** and **Barry R. Furrow** have studied the impact of private equity ownership on nursing home care.*

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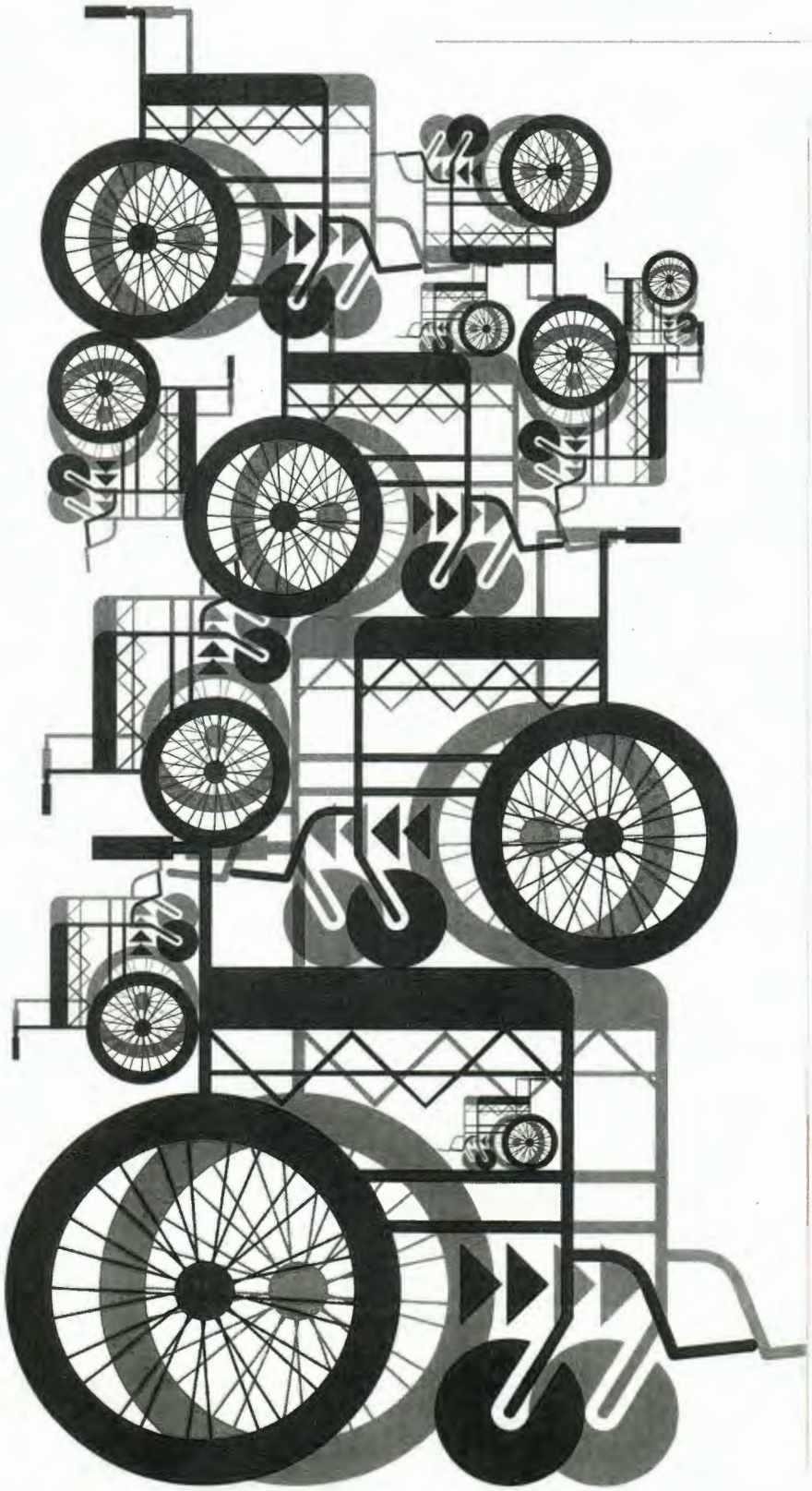

With such a secure source of revenue available, private equity firms operating nursing homes follow what has become a well-established playbook to send as much money as possible to the bottom line, legal scholars and long-term care experts say. Rather than acquiring a business, maximizing efficiency and flipping it for a profit—as they might do in another industry, such as retail, for example—these firms instead use complex corporate arrangements to impose excessive fees on the facilities they acquire and turn their real estate into an asset that can survive a potential bankruptcy.

Their first step after purchasing a facility or chain is to create a series of limited liability companies to separate the property, assets and operations. Putting the property in the hands of a tax-advantaged real estate investment trust (REIT), for example, allows a private equity firm to use a "sale-leaseback" agreement to charge nursing homes escalating rent, in addition to maintenance costs, insurance and taxes. Shielded by layers of corporate armor, private equity can effectively function as a well-protected landlord, reaping the significant rewards of property ownership from a captive tenant, while avoiding any consequences from litigation, regulatory scrutiny or even bankruptcy.

The second move in the playbook is the establishment of a series of related companies, all owned by the same private equity firm, but each offering a different product or service—payroll processing, food services, linens, pharmacy, facility management or medical devices, for example—that can be sold to a nursing home and its residents at excessive prices. In some cases, the result is a collection of hundreds of companies across a nursing home chain, all feeding back to the same private equity firm. This structure makes it all the more challenging for prosecutors, regulators and residents' families to hold private equity accountable for the most damaging impact of its operation of a nursing home: the reduced staffing that can result in patient harm.

The NBER study found that private equity ownership leads to a 3 percent decline in hours per patient-day provided by nursing assistants who serve as the primary caregivers in nursing homes and whose employment represents their largest cost. Overall staffing declines by 1.4 percent. Coupled with a 50 percent increase in the use of antipsychotic medication—dangerous in elderly patients but one way of coping with insufficient staffing—the

Allison Hoffman of the University of Pennsylvania Carey Law School is an expert on health care law, including elder care policies and Medicare.

result is a level of care that falls short of regulators' expectations and can be life-threatening. In the New Jersey study, private equity-owned facilities provided residents with 20 percent fewer nursing hours than public and nonprofit facilities, and they were cited for deficiency violations 50 percent more often.

Pam Walz is a supervising attorney in the health and independence unit at Philadelphia's Community Legal Services. "Anything that affects staff affects residents," she said. "Staffing levels are key to quality of care."

Walz has partnered with the Service Employees International Union (SEIU), which represents nursing home workers in Pennsylvania. She has found that nursing aides regularly lament the challenges of working with insufficient staff, "how exhausting it is, how demoralizing it is and how dangerous it is, because injuries happen when you don't have enough people," she said.

In other industries, private equity can find efficiencies to exploit. But there are no cost-effective methods for improving the welfare of nursing home residents, Furrow argued. Taking care of the elderly and disabled unavoidably requires lots of care and lots of attention.

"The irony of it is they're sitting on lots of money they could invest in nursing homes, but that's not their model," he continued.

Instead, private equity firms—and, increasingly, other for-profit chains—apply an approach that can be particularly harmful given the realities of the industry and the needs of the people it exists to serve.

The Impact of Insufficient Oversight and Regulation

A growing group of individuals, agencies and institutions are struggling to protect nursing home residents by bringing private equity-owned and other for-profit nursing homes into compliance. Their most significant challenge is the lack of transparency in the ownership and operation of these entities. It is typically unclear when a purchaser is backed by private equity, let alone how the tangled web of related parties is woven and who is truly responsible when something goes wrong.

"Regulators have just started to pay attention to and track these transactions, so that is positive, because it's the first step to being able to regulate them," said Allison Hoffman, a deputy dean at the University of Pennsylvania Carey Law School and an expert on health care law and policy. "But it could be too little, too late."

For residents, the workers charged with their care and residents' families, a sale—to private equity or otherwise—can be distressing. In the case of a private equity purchase, in particular, it is often all but impossible to determine who is actually in charge.

"The problem," explained Walz, "is that a sale happens behind closed doors. Nobody tells residents or families or staff. The first time anybody knows about it is when the name changes on the door or, for residents, when the uniforms change."

Lacking the resources to adequately review a sale—and, often, without the regulatory structure that would require a comprehensive review—states struggle to fulfill their watchdog role, Toby Edelman said. In some cases, this lack of effective oversight allows individuals with a checkered history at previous facilities to acquire new ones.

"The states just let them do what they want," she said. "It's terrifying and getting worse."

Litigation under the Federal False Claims Act, which was designed to prevent contractors from defrauding the government, and monitoring under the 1987 Nursing Home Reform Act, which established basic rights and services for residents of nursing homes, have both failed to prevent the harm caused by insufficient staffing and

Toby Edelman is senior policy attorney at the Center for Medicare Advocacy. She has been representing older people in long-term care facilities since 1977.

substandard care, lawyers and advocates say. Settlements are typically paid by nursing home operators, rather than the private equity firms that own them, and corporate integrity agreements are toothless.

"Most of the time the settlements are pathetic. These companies have stolen millions and millions of dollars [from Medicare and Medicaid] and they're settling for a fraction of that," said Charlene Harrington, professor emerita of sociology and nursing at the University of California San Francisco (UCSF). "And then they put in a monitor and basically nothing happens."

What's worse, Edelman said, is that the public remains in the dark once a corporate integrity agreement is announced, muting its impact. Medicare offers consumers the Care Compare web site, she explained, but that site provides no information to the public that a nursing home is part of a chain that's included in a corporate integrity agreement.

"People have no knowledge of that," she continued. "The corporate integrity agreement becomes a slap on the wrist because it's all secret and nothing really changes to improve care for residents."

Enforcement is made all the more challenging, of course, when the most powerful tool in the arsenal—closing a facility—will have the most punishing impact on residents and their families, said Field. "Enforcers' hands are tied," he explained. "You don't want to resort to the nuclear option."

Authorities Take Notice

In the wake of mounting research and reporting on private equity's perilous push into long-term care, state and federal authorities are beginning to take notice.

"As Wall Street firms take over more nursing homes, quality in those homes has gone down and costs have gone up," President Joe Biden said in his 2022 State of the Union address. "That ends on my watch."

In February, on the heels of a report from the Government Accountability Office urging improved transparency, the Biden administration proposed a rule that would require nursing homes to provide additional information to the Centers for Medicare and Medicaid Services (CMS) about their ownership and management. It would also force facilities to clarify whether their owners

Antitrust enforcement offers another avenue for preventing private equity from expanding its stake in long-term care at the expense of patient safety.

are private equity investors or real estate investment trusts.

Although they acknowledge the Biden administration's commitment to the issue, some experts nonetheless question whether the regulations will generate sufficient information to provide a clear picture of the finances and ownership activity at private equity-owned nursing homes. Harrington argues that CMS should require private equity-run facilities to file consolidated cost reports, like those provided to the Securities and Exchange Commission by publicly traded nursing homes, to provide a complete view of how their money is spent.

At the state level, new regulations in Pennsylvania will require public notice of ownership changes at nursing homes and will raise the minimum staffing level—although because of industry pushback, the increase is only 70 percent of what the state's Department of Health requested. New York and New Jersey, meanwhile, have recently passed legislation establishing a ratio of revenue that must be spent directly on resident care—90 percent in New Jersey and 70 percent in New York, which also capped nursing home profits at 5 percent. An industry lawsuit fighting the New York law claimed the state would have clawed back $824 million in profits if the law had been in effect in 2019.

More states are also seeking to better apply their certificate-of-need laws, which require regulatory approval for the establishment or expansion of health care facilities, to oversee private equity's role in the nursing home industry, Allison Hoffman said.

Advocates and legal scholars point to two recent state-level prosecutions as models for effective enforcement. In New York, Attorney General Letitia James sued three separate nursing home operators and their related companies for siphoning off between $16 million and $22 million in government funds using a complex corporate scheme straight from the private equity playbook. In addition to demonstrating poor care and low staffing, James' office used forensic accounting to follow the money and expose fraud, offering a window into how other prosecutors can pierce private equity's corporate veil.

"It's going to be a model for other attorneys general, and it's certainly a model for the Justice Department, so I think we're going to see litigation get a lot more sophisticated," Harrington said. "But we need the government, the DOJ, to step up and really go after some of these worst owners."

In Massachusetts, the attorney general's office sued former executives of the South Bay Mental Health Center Inc. and its private equity owners, reaching a $25 million settlement. It was the largest publicly disclosed health care fraud settlement in the country, and the $19.95 million paid by the private equity firm, H.I.G. Capital, was the most ever paid to resolve fraud allegations against health care companies in a private equity portfolio.

Kevin Lownds, the deputy chief of the Medicaid fraud division in the Massachusetts Office of the Attorney General, suggested that even though that suit didn't involve a nursing home, prosecutors could apply the same approach—showing that a private equity firm is aware of violations, fails to correct them and exacerbates them—in future nursing home cases.

Rosemary Batt, the Alice Hanson Cook Professor of Women and Work at the Cornell University School of Industrial and Labor Relations, has studied ownership and investment in health care. She called South Bay "an extremely critical, path-breaking case." It helps demonstrate that "private equity is the puppeteer behind the puppet," she said. But, she added, the amount of time and resources that went into pursuing the South Bay case "shows how absolutely difficult it is to enforce these kinds of laws and to seek decent standards in health care."

Some experts argue that the best way to address the harm caused by private equity ownership is to prevent it in the first place. "The number one preference is that they be totally barred from any investment in nursing homes," Harrington said.

If absolute prohibition is unfeasible, less extreme measures could still address many of the most troubling aspects of private equity's participation in the nursing home industry. Direct-care ratios and increased staffing minimums offer two levers to ensure that more helping hands are available for residents; both strategies are

Rosemary Batt is a professor at the Industrial and Labor Relations School at Cornell University. She has written extensively about the impact of private equity investment on health care.

being test-driven around the country. Last year New York established a minimum of 3.5 hours of nursing care per patient-day.

"How many decades do we need to have reports saying staff makes all the difference in the world for quality care before something is done?" Edelman asked, noting that the Biden administration has pledged to develop and enforce staffing ratios for nursing facilities. "Not surprisingly," she continued, "the nursing home industry has already promised a massive campaign to defeat whatever standards the administration proposes."

Care ratios would go a long way toward fixing the misaligned motives that allow profits to dictate how a nursing home is run, said Pam Walz. Public money shouldn't be so easily converted to private gain.

"Resources are scarce enough without operating under a model where much of that money has to go to creating a profit for someone," she said.

Scrutinizing nursing home owners more closely—including by establishing consistent criteria for eligibility to buy into the industry and devising a more meaningful five-star rating system—would allow consumers to steer clear of operators or facilities that don't meet standards, experts say.

Given that it controls the purse strings for the industry, CMS could use its authority to tie reimbursement rates to metrics that would force nursing homes to improve their level of care, Allison Hoffman suggested. Studies have shown that when private equity acquires a nursing home, not only do staffing levels decline, but residents are more likely to be sent to an emergency room. Within the data lies an opportunity for what she calls "technocratic tinkering."

"These things are measurable and tracked, so you could tie reimbursements more closely to the kinds of outcomes that you know private equity is going to fail on," she continued.

Antitrust enforcement offers another avenue for preventing private equity from expanding its stake in long-term care at the expense of patient safety. Antitrust regulators have been "chasing" in the health care space, rather than leading, Allison Hoffman said, but updating laws to prevent private equity purchases from flying under the radar would give regulators more power to limit these firms' share of the market.

"If you step back and look at what's going on, it's exactly the kind of structure, harm to competition and harm to consumers that antitrust law should be concerned about," she said.

Ironically, the complex corporate structures that help private equity firms evade responsibility when things go wrong could be their undoing. Batt's scholarship has focused on REITs, and she contends that there's no reason these trusts should be able to deduct dividends paid to shareholders—one reason their use is attractive to private equity firms and part of why the nursing home industry has been a profit center for them.

But the increased attention to private equity ownership notwithstanding, none of the proposed reforms will matter, advocates argue, unless legislators and regulators are committed to enforcing them.

"If we enforced some laws, maybe these private equity people would say, 'It's not worth it, we can make money somewhere else,' and they'd go away," Edelman said, "because they really just care about extracting profits."

Some critics have pushed back against regulators' focus on private equity. In a joint statement issued March 11, 2022, the American Health Care Association (AHCA) and the National Center for Assisted Living (NCAL) argued that private equity's impact on nursing homes has been exaggerated and its share of the market already declining. In addition, according to the AHCA and NCAL, private equity only got its toehold in the industry in the first place because low government reimbursement rates made it impossible for traditional operators to stay in the business.

"The lack of financial support for the industry from policy makers," the statement reads, "has forced a small number of nursing home providers to sell off their assets and seek other revenue sources in order to keep their doors open for their residents and staff."

Nowhere to Hide

For nursing home employees, the work of caring for residents can be thankless. Underpaid and understaffed, they perform some of the most demanding labor in health care for some of the most vulnerable patients. It is, Furrow said, "a very different, very human industry" compared with those that have more famously attracted private equity dollars. Without enough nurses and aides in place, the risks are not only financial but potentially fatal.

"If you don't have someone there at the bedside to manage the pain, it all falls on the family," said Tara Sklar, faculty director of the health law and policy program at the University of Arizona James E. Rogers College of Law. "It's really traumatizing, instead of something that could otherwise just be a natural stage of life."

Scholars and advocates who have watched private equity firms squeeze profits out of the nursing home industry fear what will happen as their attention extends further into elder care.

Scholars and advocates who have watched private equity firms squeeze profits out of the nursing home industry fear what will happen as their attention extends further into elder care. "The data has shown that private equity has in some ways finished exploiting the nursing home industry and moved onto other health care segments that impact the elderly," David Hoffman said, highlighting hospice and home care as urgent concerns.

In the past decade, the number of hospice companies owned by private equity has quadrupled. In both hospice and home care, Sklar said, private equity ownership is likely to produce the same conditions that put patients at risk in nursing homes.

"These are all things that are happening disproportionately more when nursing homes are owned by private equity, and there's no reason to think that wouldn't be the case as they continue to expand into home health and hospice," she said.

For their part, the AHCA and NCAL worry that private equity's impact on health care will extend even further. According to their joint statement, "Private equity in health care is shifting away from nursing homes and into more lucrative sectors, such as dermatology and orthopedics. The issue is one for the entire health care system, not just nursing homes."

The pressure is now on prosecutors, lawmakers and regulators to both use the tools already at their disposal—and also to design robust new methods—for holding private equity firms accountable for how they operate care-giving institutions.

"They're in the spotlight now," Furrow said, "and they can't hide." ■

Ben Seal is a Philadelphia-based freelance writer whose coverage includes the environment, the law and academic research.