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2024 New York Budget Proposes Wide-Ranging Transaction Approval Requirement That Targets Private Investment in Physician Practices and MSOs, and Permits DOH to Extract Concessions

Health Care Law Brief on **February 6, 2023**

On February 1, 2023, New York Governor Kathy Hochul announced the 2024 Executive Budget. As alluded to in the Governor's State of the State address, and as described in an earlier Proskauer Health Care Law Brief article, the Governor is proposing to adopt a wide-ranging approval requirement for health care transactions that appears to target investor-backed physician practices.

The legislative proposals related to health care, as contained in the Governor's budget, were introduced as Senate Bill 4007 and Assembly Bill A3007. The bills propose to amend the Public Health Law ("PHL") to introduce a new Article 45-A, named "Review and Oversight of Material Transactions." See 2023 New York Senate-Assembly Bill S4007, A3007, Part M § 5.

The Legislative Intent of the Proposed Bill Underscores That Physician Practices Are Under-Regulated As Compared to Other Health Care Facilities, and Faults Investor-Backed Practices for Increasing Costs

The legislative intent section of the proposed law sets forth that "there has been a proliferation of large physician practices being managed by entities that are investor-backed." Id. at PHL § 4550. The bill states that "physician practices are subject to far less oversight than [other facilities]" but that they "remain unregulated by the state outside of the licensure of the individual practitioners who practice at these sites and Medicaid enrollment." Id. Moreover, the bill notes that physician practices are generally not subject to costly change of ownership or control review, and as such, "the state is not able to track or monitor the impact of these transactions on cost, quality, access, equity, and competition." Id.

Importantly, the bill asserts that "the concentration of… investor-backed physician practices is a significant contributor to health care cost inflation," without noting the basis for the allegation, which is likely to be disputed. Id. There is no mention of alternative sources of capital for large physician practices, uptake of electronic and value-oriented care, or patient satisfaction.

The Bill Introduces a Broad Transaction Approval Requirement, Which Would Apply to Material Transactions Involving Physician Practices and Newly-Formed MSOs or MSAs

As a preliminary matter, the bill broadly defines a "health care entity" to include, in part, a management services organization ("MSO"), health insurance plan, or any other type of health care facility, organization or plan providing health care services in the state. Id. at PHL § 4551(2).

The proposed statute would require "health care entities" to report and obtain the state's consent for "material transactions." Id. at PHL § 4552-53. The Department of Health ("DOH") would be required to promulgate regulations establishing a materiality threshold for reporting transactions. Id. at PHL § 4551(4)(a). Such notice must be submitted at least 30 days prior to the anticipated closing date of the material transaction, and the application will be deemed granted if the state does not respond within 30 days of the submission of a complete application package. Id. at PHL § 4553-54.

As expected, a "material transaction" is defined, in part, to include a merger with a health care entity, or an asset conveyance involving a health care entity. Id. at PHL § 4551(4)(a)(i)-(ii). However, a "material transaction" is also drafted in a manner that may result in the reporting of new transactions between MSOs, investments in MSOs, new management service arrangements with existing MSOs, and the formation of new MSOs. Specifically, a "material transaction" also means: (i) an affiliation or contract between a health care entity and another person, except certain clinical affiliations and other transactions presently regulated by the state; or (ii) the formation of a partnership, joint venture, accountable care organization, parent organization, or MSO for the purpose of administering contracts with health plans, third-party administrators, pharmacy benefit managers, or health care providers. Id. at PHL § 4551(4)(a)(iii)-(iv).

As currently drafted, and subject to further rulemaking, the statute requires disclosure of: (i) involved parties; (ii) material contracts and pre-and-post closing conditions; (iii) service locations and revenue information; and (iv) plans to reduce or eliminate services post-closing. Id. In addition, similar to the state's certificate of need process for certain health care facilities, the proposed statute requires the submission of a description of the proposed transaction, including an assessment of the anticipated impact of the transaction on cost, quality, access, health equity, and competition in the impacted markets. Id.

In reviewing transactions, and also subject to further rulemaking, the DOH will consider, in part, the character and competency of the applicant, the impact of the transaction on cost, access, health equity, and health outcomes, and the impact of the transaction on competition. Id. at PHL § 4554. In addition, the bill empowers the DOH to engage contractors (including actuaries or other professionals) to examine the transaction, to be paid for by parties to the material transaction designated by the DOH. Id. at PHL § 4554(3)(c).

The Bill Requires Public Notice of Material Transactions, Permits DOH to Seek Public Comments That May Raise the Risk of Approval Delays, and Allows DOH to Extract Concessions from Applicants

Of note, the bill would require the DOH to post public notices of pending material transactions, inviting public comments. Id. at PHL § 4554(2). In addition to the foregoing public notice period, the DOH is expressly permitted to "seek public input and otherwise engage the public before making a determination" on a material transaction. Id. at PHL § 4554(3)(d).

The foregoing public notice period, coupled with the DOH's ability to seek further public input, raises the specter that transactions may be delayed, or subjected to further scrutiny, as a result of negative public opinion, low community support, or concerns by competitors. For example, the bill's legislative purpose and intent section tends to convey that investor-backed physician practice transactions have the potential to negatively impact existing health care delivery systems, which face greater regulation by the state. That the state is concerned about the competitive impact on existing delivery systems permeates the proposed bill. For example, as drafted, the bill provides DOH the authority to consider a material transaction's impact on "the operations of the existing delivery system." Id. at PHL § 4554(1)(b).

Finally, the bill enables the DOH to seek concessions from applicants in exchange for issuing approval. Id. at PHL § 4554(4)(c). As a condition of approving a transaction, DOH may require, among other items, "investments in the communities affected by such material transaction," "competition protections," and contributions to "state-controlled funds" such as the health care transformation fund, which is a state grant-making program that generally benefits certain licensed facilities. Id. As drafted, the bill provides limited information as to when or why the DOH may require concessions, and absent further rulemaking or sub-regulatory guidance, applicants are faced with a degree of uncertainty and risk. It appears to authorize an uncontrolled "shakedown" as a *quid pro quo* for, and as part of, the approval process.

The Bill Requires Applicants to Disclose Privileged Material When Requested by DOH, Contemplates Potential Referral by DOH to the New York Attorney General, and Does Not Shield Information Disclosed to the State

The proposed bill requires applicants to disclose a variety of information, where so requested by DOH. Id. at PHL § 4554(3). As drafted, a "health care entity shall not refuse to provide documents or other information requested… on the grounds that such information is privileged or confidential." Id.

If the DOH disapproves of a transaction, the bill sets forth that DOH may notify the New York Attorney General of the DOH's findings and analysis so that the Attorney General "may, if appropriate, conduct an investigation into whether the health care entities have engaged in unfair competition of anticompetitive behavior, and if necessary, take steps to protect consumers in the health care services market." Id. at PHL § 4554(4)(b).

The approval process, DOH's broad authority to review records and compel disclosure of information, the explicit authority to take such information and refer DOH findings to an enforcement agency, when coupled with potential and unlimited approval mandates, may have a chilling effect on health care investment in New York.

Moreover, and despite the broad amount of information that may be requested by DOH, including privileged information, the proposed bill does not provide applicants with heightened privacy protections. Absent further amendments to the proposed bill, applicants will likely solely be able to rely upon the existing exceptions to New York's Freedom of Information Law for the purpose of protecting their commercially-sensitive or privileged information, as submitted to DOH. See Public Officer's Law § 87(2).

If passed, and depending upon the materiality threshold adopted by regulation, the above proposals may impact health care investors in New York. Proskauer's Health Care Group will closely monitor the proposals described above and provide continuing updates.

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