



Episode 111: State Regulatory Interventions in Healthcare, With Tim Fry

Episode Summary

“For clients in the healthcare space, having a state-based compliance program has grown in importance,” says [Tim Fry](#), partner in the healthcare group at McGuireWoods. With McGuireWoods colleague and host [Geoff Cockrell](#), Tim unpacks how state-specific legal treatment has changed dramatically in the last several years.

He explains how states such as California and Oregon built hostility to private equity into their premerger notice laws while other states diverge on noncompete enforceability even after federal rulemaking failed.

Tune in for his insights about the shifting regulatory landscape.

Transcript

Voice over (00:00):

This is the Corner Series, a McGuireWoods series exploring business and legal issues prevalent in today's private equity industry. Tune in with McGuireWoods partner, Geoff Cockrell, as he and specialists share real world insight to help enhance your knowledge.

Geoff Cockrell (00:18):

Thank you for joining another episode of the Corner Series. I'm your host, Geoff Cockrell, a partner at McGuireWoods. Here at the Corner Series, we try to bring together deal makers and thought leaders at the corner of healthcare and private equity. Today I'm joined by my good friend and colleague, Tim Fry. He's a partner in the healthcare group here at McGuireWoods. We're going to talk about some of the evolving landscape in kind of state regulatory interventions that we're seeing across the country and talk a bit about how to navigate those. But Tim, if you could give a little introduction of yourself before we jump into some discussion.

Tim Fry (00:50):

Geoff, thanks again for having me on. I am a partner here in the healthcare group as you mentioned. My practice is focused on regulatory support of our deal teams and our clients to implement new initiatives in the healthcare space. Prior to law school, I worked at the Centers for Medicare and Medicaid Services, which influences my push into regulatory world. Now I've been with McGuireWoods and the great team, including Geoff for about a dozen years and look forward to kind of having a further conversation, like you said, about state issues today.

Geoff Cockrell (01:24):

So Tim, for a long time, state issues, there might be different kind of edges to how one state might approach something versus another state, but it was fairly stable. In the last, let's call it three, four years, that has changed pretty dramatically. Before we get into some of the more detailed aspects of it, what are some of the broad categories of how state-specific legal treatment has been changing?

Tim Fry (01:50):

Geoff, I think you said it very well, and I think for clients in the healthcare space, having a state-based compliance program has grown in importance. Not so much defensive, but to be proactive and think through your deals and your structures and where you want to operate. In some of that is in deal making itself. So a number of states have passed what we kind of refer to as pre-merger notification or consent rules. We can talk a little bit more about that, but we are also seeing a lot of increased focus on corporate practice doctrines. So those things in broad brushstrokes would influence a platform.

(02:37):

But then we're also seeing states diverge on things like non-competes, and especially post-FTC rulemaking, last year that failed. We're seeing states become more restrictive, some are becoming more flexible. And then a third big broad brushstroke is for the longest time investigations in the healthcare space, were mainly driven by the federal government and whistleblowers. We're seeing a lot more action at the state level and kind of Medicaid fraud control units and other investigators in the AG's offices of the respective states becoming much more active.

Geoff Cockrell (03:17):

On the pre-merger notification at a federal level, which has antitrust review of things, you need to be a transaction that's north of \$120 million before you're even thinking about whether or not that comes into play. How have states morphed some of those thresholds and interjected themselves at sizes and in places where at a federal level you might not have had to do anything.

Tim Fry (03:44):

States are going much further south of that number, much further south of 100,000,000. So some states have gone to simply based on the number of physicians working for a platform, 10 to 15

physicians might be enough to trigger notice or consent depending on how the state set up the rules. States are also asking about combined economic weight of an enterprise, not just in a target market or the target itself, but maybe nationally, how big is that platform that is doing the acquisition? So Geoff, the short answer to your question is, just because it's a small deal, a deal that you don't think Hart-Scott-Rodino is going to apply, doesn't mean that a healthcare pre-merger notice or consent won't be required. States have come down below that and are really interested in serial roll-ups, and so they want to make sure they're catching a lot more transactions to get visibility into those.

Geoff Cockrell (04:47):

At a federal level, if you cross those thresholds, the FTC who's generally kind of looking at these things is looking at whether or not you through that combination are amassing certain kinds of specific market power. From a state perspective, are they looking at the same thing? Are they looking at other aspects of impact on healthcare delivery? How's it different?

Tim Fry (05:10):

Yes and no. So a number of states have placed their merger program in their attorney general's offices. Those typically are interested in competition impact, but we also see states asking questions about health equity, access. After some of the circumstances in Massachusetts with kind of a for-profit health system. With real estate investment trusts involved going bankrupt and belly-up in the state of Massachusetts, the state has passed rules. They're just looking at who the investors are and their solvency so that they can make sure care access is maintained if anything were to go wrong.

(05:51):

So yes, kind of that federal antitrust thrust is present and a concern for states, but states have their own unique political pressures and those are coming into play as well. And so you have to look state by state in each deal we're doing right now for clients, that's a part of our process is thinking through are there going to be these pre-merger notice or consent requirements, and if so, what's it going to take? How long could it delay the transaction? In some cases, it's up to six months, and so we want to try to get ahead of that, think about that and think about whether that state's going to be a good place for our clients to invest.

Geoff Cockrell (06:29):

For those that listen to this podcast, they've heard many discussions with many people defending the role of private equity in healthcare investing, and that's a role that sometimes gets dragged through the mud in the press. There's been a few high profile bad actors, but in the discussions that we've had in my experience, those are corner cases. Another area where kind of hostility to private equity investing can materialize is exactly here with hostility from state regulators to private equities role in healthcare. What are you seeing out there in different parts of the country and how would you kind of handicap that hostility?

Tim Fry (07:09):

A couple of the western states, California, Oregon, have built that into their pre-merger notice laws. They've also started to look at enhancements to their corporate practice doctrine, Geoff, and that hostility is probably present in the legislative action that the legislature is considering, passing these laws. I think you're right, Geoff, that there are some cases that have led to that kind of legislative activity. I mentioned Massachusetts in a health system that went belly up.

(07:42):

But overall, I think it's ignoring some of the value that investors can bring, the professionalization of platforms. In some cases, last year there was a bill on the governor's desk in California that would've been pretty hostile to investors. That was brought to Governor Newsom's attention. A lot of advocacy efforts were made in California, and ultimately he vetoed a bill that would've made investment pretty difficult in the state of California. California still has other bills and other laws that require notice ahead of time, and that was part of the emphasis to him and to other policymakers across the country is, let's monitor this. We understand your concerns. Let's take a look, but don't throw the baby out with the bath water, so to speak, let's look very intentionally and see if these laws are helpful or if they impact investment.

Geoff Cockrell (08:41):

How are you seeing investors respond to this shifting landscape? Are you seeing reluctance to enter certain markets, say in the Northwest? Are you seeing folks view this as more of a procedural impact but not a substantive block on what they're trying to accomplish? How are you seeing people respond?

Tim Fry (09:01):

I think it's happening, Jeff, at a time of a bit of a general slowdown in investment in physician practice management vehicles. There are a lot great strong platforms out there still in the market, so I don't want to suggest that the deals aren't happening. We're seeing a ton of deals in this space, but compared to the height of COVID when those deals were happening every other week and being announced, we've seen kind of a search in the healthcare space to some other sectors, and so how much of that is trying to avoid some of these laws versus kind of an investor appetite for something different? It's harder for me to unpack.

(09:43):

But absolutely, I think our clients are being very intentional, Geoff. Is this a state that is going to be friendly to investment long-term, or is this something that could hang up and exit in five years? And so the Northwest states are one's people are keeping an eye out. The New England states are probably other areas that people are keeping an eye on and insane, do we want to pay kind of top dollar? Are we sure we're going to be able to exit as cleanly as we would've five years ago or in a different region of the country? And that is entering people's risk calculations.

Geoff Cockrell (10:21):

In application, there's obviously kind of process implications from some of these developing laws. How often are you seeing either a flat no coming from those regulators or a yes, with conditions that are just intolerable?

Tim Fry (10:39):

Really not a lot. Now is that because we're in the early innings of some of these laws? In many cases, the states pass the laws and then the regulators are trying to figure out what to do with them, build processes on the fly. There haven't been a lot of no's though in these states where the notice is or even consents are required. It's more of, I think the what-if's that are kind of asking people and making the entire industry consider this and stand up in these spaces, Geoff.

(11:11):

But we haven't seen a lot of no's. We have not seen a lot of intolerable conditions, making people jump through hoops that they never want to jump through. Some of that's because as you do the applications, you can be thoughtful, you can think through, how do you tell your story, how do you tell your story about access, how you're going to help the populations and the community, how are you going to streamline things? And the states can hopefully latch onto some of that. But we haven't seen a lot of no's or deals fall apart because of the types of conditionality that regulators are putting on things.

Geoff Cockrell (11:47):

You mentioned the Northeast, the Northwest, California, those all pretty bluish kind of states. To what extent is there a red state, blue state overlay on how states are responding to this topic?

Tim Fry (12:02):

I think a year ago, maybe 18 months ago, we would've thought it was just blue states, Geoff, to your point. Indiana has been pretty aggressive here in terms of putting in place pre-merger notification rules and adding to those laws. Nevada, which has both Republicans and Democrats in various leadership positions as well, so I think it's a yes. Texas has looked at these, so yes, I think your traditional, stereotypical, heavily regulated states have been early adopters of things like this. But certainly states that you may have historically considered more business or investment friendly like Indiana or Texas, they're also hearing from whether it's the physician organizations or policymakers in their state that have whatever concerns they're sharing in pushing forward these types of laws as well. So it's not just avoid the blue states.

Geoff Cockrell (13:03):

So if you get drawn into that pre-merger notification process, to what extent is that a one and done episode? You had to get some clearance. It might've been a little bit painful. To what extent is it that versus now you're in the mill with the regulator, you're having to provide regular updates. They're

asking you lots of questions about kind of impact on billing rates with payers, which also might miss some of the benefits that you're bringing of being able to maybe move things, procedures outside of a hospital setting, which we've talked about on this podcast before. But to what extent are you kind of in it with the regulator going forward?

Tim Fry (13:42):

It's a good question, Geoff, and that's something that I think is going to be evolving, and that's some of what we're seeing with secondary add-on laws in some of these states. But for instance, Oregon requires updates to the state regulators over time, and we'll probably see more of that as we go forward. You also may have a situation in some states where your next deal that you do, even if that would otherwise have been below the threshold that the state has established, the fact that you were above it for an earlier deal means you need to now report your additional add-ons. So there is definitely something to that, and depending on where your platform is in maturity, you might see more regulatory overlay and notice to regulators.

Geoff Cockrell (14:27):

You mentioned another area where state differences can emerge, that being in the arena of non-competes, and when I'm talking to clients, I often kind of lead off that discussion with a recognition that there's a general title direction on how the law is evolving, and that title direction is kind of hostility toward enforceability of restricted covenants, non-competes, outside of, in the specific context of a sale of business. What are you seeing in the state evolution on that topic, especially in the context of employment?

Tim Fry (15:08):

I think that's all right, Geoff, and that's certainly what we're seeing. We're seeing states like Texas and Virginia here in the last year, that have tightened their non-compete enforceability regime. Texas takes effect I believe in September where they're going to be a little bit more targeted for physicians and other healthcare professionals on their radius and limiting how far those employment radiuses can extend.

(15:34):

But we are seeing a shift like Florida, where Florida is actually being more beneficial or more pro-enforceability of restrictive covenants, giving more guidance to employers and giving kind of a more statutory framework, if you hit these hoops, the enforceability is going to be enforceable and kind of seen as broadening enforceability in Florida.

(16:03):

So we are seeing kind of a divergence there a little bit in states, and I don't know that it's neat enough to say it's Democratic or Republican states. Certainly Texas and Florida are both seen as conservative states at this point, and they're diverging. So it is an area where we're paying a lot of

attention to see how non-competes in the employment realm will kind of shake out, now that federal policies kind of again cleared it for the states.

Geoff Cockrell (16:30):

I mean a few years ago, there was the palpable sense that a lot of these state differences on enforceability in the employment context at least, were going to get completely washed away by federal rulemaking. Is there any thought in the current administration that we're likely to see anything like that again, or is that ship sailed at least for the time being? I

Tim Fry (16:51):

I believe it's shipped at this point, Geoff. My sense was the FTC commissioners that are Republican appointees that were part of the FTC commission, they were not favorable to the rule. They opposed the rule, but the fact is that I don't think they're going to be going back to the well here in the next couple of years. I also don't think there's a lot of federal excitement around going the opposite direction either. There were definitely some conservatives like candidly, Vice President, JD Vance, that felt like some of the restrictions on non-competes for especially the famous example of the sandwich workers at restaurants, Geoff, that getting paid minimum wage and signing non-compete restrictions that may be in those realms that had gone too far. And so I don't know that there's also a federal desire amongst this administration to go the opposite direction than the Biden team, all subject maybe to the whims of a Twitter post in the next couple of weeks.

Geoff Cockrell (17:52):

I think a sandwich artist is the word you were looking for.

Tim Fry (17:56):

Thank you, Geoff. That's right. You need that extra artiste to get the non-compete to be enforceable.

Geoff Cockrell (18:01):

Yeah, and I'm seeing folks, especially with senior level people still taking fairly consistent approaches to the topic of wanting those non-competes. The damage that especially a senior person can do, is pretty profound, and it continues to be a pretty hotly negotiated topic. So Tim, while we have you maybe diverging from the state treatment, are we starting to get some guidance from the federal government as to kind of what their fraud enforcement priorities are going to be? There was some question early on with Hudson personnel. Was that signaling maybe less interest in aggressively pursuing the edges of some of those cases? Obviously, pursuing fraud is not a red or blue topic. What are we seeing coming out of Washington with respect to some of those enforcement priorities and how do you expect the heat of enforcement to look here in this administration?

Tim Fry (18:55):

That's a good question, and I think enforceability seems to be just as high of a priority if not a higher priority for this administration. So a couple examples of that. One, the DOJ and the Department of Health and Human Services has re-upped a task force that was formed during the first Trump administration to share information and target healthcare fraud. So I think at the federal level, there's a great signal that these are cases that they want to take on. Certainly if you listen to the administration and their backers in Congress with the one big beautiful bill that they passed, the only changes they're making to the Medicaid program is reducing fraud. I'm skeptical that that's what the law actually does, but certainly that emphasis on fighting fraud at the federal level is continuing, even increasing, maybe even seeing some people pulled off other enforcement priorities.

(19:58):

Immigration is obviously a key concern for this administration, but healthcare fraud is up there. And then what we're also seeing, just to tie back to some of the themes of today's conversation about the states, we're seeing the states become more active and then we're seeing cases, false claims act cases, that maybe the feds have declined to intervene on, but the states are taking it up and pushing it through their state False Claims Acts. And we're also seeing the expansion of investigations under state-based Medicaid fraud control units. Those are required by federal law that all states have them, and we're seeing them increasingly become more active and more sophisticated. And so as you think about it holistically in the healthcare space as a provider of service billing for Medicaid, Tricare, enforcement continues, and I don't see that declining under this administration. It's certainly something like you said, Geoff, it's bipartisan not to pay for fraud.

Geoff Cockrell (21:02):

Tim, I think we will call that a wrap. It's always a ton of fun to talk through latest developments and really appreciate you joining me.

Tim Fry (21:11):

Thanks again for having me, Geoff. Appreciate it.

Voice over (21:15):

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