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New State Laws Requiring Notice of Health Care Transactions Will Uniquely Impact Distressed Transactions

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Distressed businesses are often compared to melting ice cubes or an aircraft in rapid descent.

The goal for a distressed business is to get to a transaction before the ice cube melts or the aircraft and ground meet at an unsurvivable speed. New state laws modeled after the federal Hart-Scott-Rodino (HSR) Act now require, or will soon require, parties to provide notice of certain health care transactions to state regulators creating additional hurdles for distressed healthcare businesses.

State Regulation Examples

Illinois

Effective January 1, 2024, Health care facilities and provider organizations must notify the Illinois Attorney General's office of any proposed covered transaction within the state or with any out-of-state entity that generates at least $10 million in annual revenue from Illinois residents. The transaction may not proceed until 30 days after parties submit the requisite notice. If the Attorney General requests additional information, the transaction may not proceed until 30 days after the parties have substantially complied with the request. Any organization that fails to comply is subject to a civil penalty of $500 per day for each day during which the organization is in violation of this requirement. Once the 30 days pass, the Illinois AG's approval is not necessary for the transaction to proceed. However, the AG may open an investigation if the AG determines the transaction is anticompetitive.

Indiana

Effective July 1, 2024, "[a]n Indiana health care entity that is involved in a merger or acquisition with another health care entity with total assets, including combined entities and holdings, of at least ten million dollars ($10,000,000) shall, at least ninety (90) days prior to the merger or acquisition, provide written notice of the merger or acquisition to the office of the attorney general in a manner prescribed by the office of the attorney general." Indiana's definition of "health care entities" includes private equity partnerships and defines "merger" to include any change of ownership including an acquisition or transfer of assets.

Minnesota

On February 22, 2024, legislation was introduced in Minnesota's House of Representatives that, if enacted, would prohibit private equity companies or real estate investment trusts (REITs) from acquiring or increasing any direct or indirect ownership interest those entities have in a health care provider after August 1, 2024.

Oregon

Or. Rev. Stat. Ann. § 415.501 requires health care entities to give the Oregon Health Authority (OHA) 180 days' notice before closing on a material change transaction. OHA must then review and approve the transaction before the transaction can proceed. Transactions are reviewed to make sure they support Oregon's goals related to cost, equity, access, and quality. A material transaction means a transaction in which 1) at least one party to the transaction had an average revenue of $25 million or more in the preceding three years and 2) at least one other party had at least $10 million in revenue in the preceding three years or, if a new entity, is projected to have at least $10 million in revenue the first full year of operation. If these conditions are satisfied, a transaction that is between an Oregon healthcare entity and an out-of-state entity is still subject to notice requirements if the transaction may result in increases in the price of healthcare or limit access to healthcare services in Oregon. Oregon law also includes a provision providing for emergency exemption from the normal review process.

HSR Act

The HSR Act provides for the U.S. Federal Trade Commission to review transactions to determine if the transaction will adversely impact competition. The size-of-transaction threshold set by certain states is much smaller than the HSR Act size-of-transaction threshold and will capture a much larger number of transactions. For example, in Indiana the size-of-transaction threshold is $10 million. The minimum "size-of-transaction" threshold for acquisitions to trigger the notification requirements for the HSR Act is greater than $115 million. In addition, the initial review period set by certain states for state regulators to examine a transaction is longer than the HSR Act's 30-day period. In Oregon the initial review period is 180 days and in Indiana 90 days.

The new state law notice and review requirements will impact distressed health care transactions that were formerly "small" enough to proceed without HSR Act review in several ways.

Operational Challenges During Notice and Review Periods

Ensuring Sufficient Cash Flow

First, where new notice and review laws have been enacted, sellers and buyers of distressed health care businesses will have to ensure that the health care business has sufficient cash flow to maintain operations during the notice and review period. This may require lenders to make additional protective advances to fund operations. This may also require sellers shorten their marketing period and proceed to a transaction more quickly to provide time for the notice and review period. In distressed transactions where there is no source of funding an extended review period may result in more closures of health care entities.

Transaction Risk Assessment

Second, distressed sellers will have to assess whether a potential buyer and transaction will pass the

state's review. Distressed sellers will potentially have to price the transaction risk of proceeding with certain bidders who may not be approved by the state. Creditors may also have to accept a prospective buyer with a lower bid where the diligence demonstrates that the lower bidding prospect will not trigger concerns of state regulators.

Receivership and Bankruptcy Proceedings

Third, in receivership and bankruptcy proceedings the executory period between court-approval of a sale and the closing date may now need to be longer to comply with the new state-level notice and review requirements. This additional time creates transaction risk, may provide additional time for creditors or spurned bidders to challenge sales transactions, and may increase administrative expenses in bankruptcy and receivership proceedings.

Recommendations for Buyers and Sellers

To streamline the process, as soon as possible, parties to a distressed transaction should advise the state agency reviewing the transaction of its distressed nature and prepare notice material that will assist the state agency in its review. To the extent the state agency permits it, parties should engage in information sharing with the individuals responsible for approving the transaction. Parties should also determine whether the state regulators have provisions for expedited review of distressed transactions. Oregon, for example, has a provision permitting emergency exemptions where the financial forecast demonstrates a need to preserve the solvency of an entity. (An exemplar of Oregon's review of a request for emergency exemption can be found here.) Parties should be prepared to share bank statements, payroll information, financial statements, and forecasts with regulators to explain any need for expedited review given the financial condition of the enterprise.

Finally, buyers and sellers should familiarize themselves with the elements of transactions that have required further state regulatory review or have caused previous proposed transactions to be barred from proceeding to help their clients assess transaction risk and formulate notices to the state regulators that address applicable concerns. For example, parties should be prepared to communicate how a transaction impacts the market share in a service area, impacts patients' access to care in a service area, and impacts the cost of care in a service area.

The Broader Impact on the Health Care Industry

Given the number of health care entities that are financially stressed, these new state laws may make for busy regulators. In 2023, U.S. bankruptcies across all sectors were at a 13-year high, with health care filings being the second leading industry at 81 filings in 2023. Hospitals and health systems are not the only segment of the health care market where certain participants are experiencing a liquidity crisis. According to the National Investment Center for Senior Housing & Care (NIC)'s 3Q 2023 Lending Trends Report, delinquent loan balances for senior housing were at an all-time high. Delinquencies in senior housing rose by 50% in the third quarter of 2023. Looking further ahead in 2024, as a sector, health care entities' financial troubles are expected to persist and may worsen compared to prior years. Moody's predicts increased defaults on health care borrowings. This is largely driven by the growing number of healthcare companies appearing on Moody's B3 Negative and Lower List (B3N list), placement on which indicates that the credit of the entity is at least "considered speculative and subject to high credit risk," if not worse. As of November 2023, there were 192 health care companies rated by Moody's, of which 21% appeared on the B3N list, up nearly 18% from December 2022.

EBG continues to monitor efforts at the state level across the U.S. with respect to notice of health care transaction laws.

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