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Major Regulatory Updates from the West Coast: New California and Washington Approaches to Healthcare Private Equity and MSO Regulation

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State legislatures on the West Coast are intensifying their focus on private equity and management service organizations (MSOs) in healthcare, introducing new regulatory measures that could significantly reshape investment strategies, ownership structures, and operational matters in the healthcare space in these states. As state legislatures respond to growing concerns about the role of non-licensed entities in healthcare decision-making, recent proposals reflect a heightened focus on transaction scrutiny, ownership structures, and the autonomy of licensed providers.

California's Senate Bill 351 ("SB 351") and Assembly Bill 1415 ("AB 1415"), introduced in February 2025, seek to reinforce state oversight of healthcare investments, particularly those involving private equity, hedge funds, and MSOs. While SB 351 reinforces existing restrictions on corporate control over clinical decision-making, AB 1415 expands the authority of the California Office of Health Care Affordability (OHCA), extending its pre-transaction notice and clearance requirements to a broader range of entities. Meanwhile, Washington's Senate Bill 5387 ("SB 5387") is moving through committee review and proposes strict regulations that would limit lay ownership of healthcare practices and curb MSO involvement in operational control.

Below provides an overview of the key components and takeaways from these state legislative efforts.

Legislative Developments at a Glance

Legislation	Key Provisions	Status
SB 351 (California, First Read Feb. 12, 2025)	Codifies limits on private equity and hedge fund influence in clinical decision-making; bans non-competes & non-disparagement clauses; grants	Moving through committee review.

Legislation	Key Provisions	Status
	enforcement authority to the Attorney General.	
AB 1415 (California, Feb. 21, 2025)	Expands OHCA oversight and pre-closing transaction filing requirements to private equity, hedge funds, MSOs, health systems and other provider entities.	Assembly-Pending Referral.
SB 5387 (Washington, First Read Jan. 21 2025)	Requires healthcare providers to hold majority ownership of practices; limits roles, ownership and control among individuals and entities involved MSO-professional entity arrangements;	Moving through committee review.

California's SB 351: Focused on Maintaining Clinical Decision-Making Autonomy

SB 351 reinforces California's existing corporate practice of medicine (CPOM) prohibition by specifying certain restrictions on private equity firms and hedge funds in clinical decision-making. The bill enumerates specific restrictions to ensure that key medical and operational decisions remain within the control of licensed providers.

Specifically, SB 351 would codify the following restrictions:

- Prohibiting investors from determining diagnostic tests, treatment options, patient volume, or referral requirements.
- Restricting non-licensed entities from owning or managing patient medical records or influencing billing and coding practices.
- Expanding enforcement authority, allowing the California Attorney General to seek injunctive relief for violations.
- Banning non-compete and non-disparagement clauses in management contracts and asset sale agreements involving medical and dental practices.

While SB 351 strengthens the state's CPOM framework, it does not contain a mandatory state pre-approval process for private equity-backed healthcare transactions, which was a feature of the much publicized Assembly Bill 3129 last year, which was ultimately vetoed by Governor Gavin Newsom.[i] Rather, the core provisions focus on clarifying what are generally recognized legal boundaries surrounding the corporate practice of medicine doctrine and clinical autonomy.

California's AB 1415: Expanded OHCA Authority Over Healthcare Transactions

Concurrently, AB 1415 proposes a significant expansion of OHCA's authority over healthcare transactions. The bill would broaden the scope of entities required to file pre-transaction notices with OHCA, including private equity groups, hedge funds, MSOs, and health system affiliates, all of which were previously outside the agency's direct oversight.

If enacted, AB 1415 would reshape California's healthcare transactional landscape by:

- Requiring private equity firms, hedge funds, and newly formed holding entities involved in

healthcare deals to submit filings to OHCA with respect to their involvement in material transactions.
- Expanding the definition of "provider" to health systems and their affiliates to subject such entities to OHCA review. The definition is also reframed to include "any private or public health care provider", as opposed to the current framework which lists out specific licensure or service line categories constituting a "provider".
- Expressly bringing management services organizations (MSOs) under OHCA authority, which were notably excluded under prior regulations, and consequently more directly impacting physician practice management models.

The proposed expansion of OHCA's jurisdiction under AB 1415 represents a dramatic shift in California's approach to healthcare transaction oversight. By requiring private equity groups, hedge funds, MSOs, and health systems to submit pre-transaction notices, the bill would broaden the regulatory reach of OHCA.

While AB 1415 would not grant OHCA the authority to block transactions outright (unlike the approach taken in last years' AB 3129), its review process could delay closings involving such entities and introduce additional compliance burdens to navigate healthcare deals in California. As seen with prior legislative efforts, this bill signals a continued push for increased scrutiny of non-licensed entities and investors in healthcare. While the measure is likely to face intense lobbying efforts, it is worth reminding our readers that Governor Newsom's veto statement specifically called out the existing OHCA authority and framework as a reason why AB 3129 was not necessary. Here, it will be interesting to see whether carving in private equity stakeholders within the OHCA framework makes this type of legislation more likely to get enacted into law.

Washington's SB 5387: New Restrictions on Healthcare Ownership Structures

Meanwhile, Washington's SB 5387 takes a relatively strict and targeted approach to regulating lay entity arrangements and influence over health care practices. Specifically, the bill includes the following key features:

- Non-licensed individuals, corporations, or entities cannot own or control health care practices or employ licensed healthcare providers unless explicitly permitted under state law.
- Whereas under existing law shareholders, officers and directors of professional service entities do not necessarily have to be licensed in Washington, this bill would require Washington-licensed healthcare providers to retain control of such entities by holding a majority of the voting shares, serving as the majority of directors, and occupying key leadership roles. The bill also adds what appears to be an active practice requirement to be an owner of a professional health care entity.
- Shareholders, directors and officers of professional health care practices would be prevented from owning equity in or serving as an officer, director, employee or contractor of an MSO contracted with such practice, or receiving significant financial compensation from such MSO in return for ownership or management of the professional entity. Such shareholders, directors and officers would also not be able to transfer or relinquish control over the issuing of shares in the practice or the paying of dividends.

The provisions in SB 5387 take an approach similar to the version of California's AB 3129 originally passed by the California State Assembly in May 2024, as well as Oregon's HB 4130 passed by the Oregon House of Representatives in February 2024 (which ultimately failed to be enacted into law). Both prior bills called into question the viability of the "friendly" PC-MSO model commonly used by

private equity and other investors, which typically involve succession agreements and similar arrangements that give certain control rights to MSOs relating to professional entities, among other features. Here, by delineating broad ownership and control requirements and restrictions involving professional entities and MSOs, it could prove to be difficult in practice to utilize such PC-MSO structures in Washington if the bill as currently drafted is enacted into law.

Looking Ahead

California and Washington are advancing significant legislative changes that would reshape the west coast healthcare investment landscape. We will continue tracking the proposed bills as they progress and provide updates on their impact on healthcare transactions in these states. For more information, contact our team for guidance on navigating these proposed changes.

FOOTNOTES

[i] See our previous blog series on California Assembly Bill 3129 pursued by CA state legislators in 2024: Update: Governor Newsom Vetoes California's AB 3129 Targeting Healthcare Private Equity Deals | Healthcare Law Blog (sheppardhealthlaw.com), published October 2, 2024, Update: AB 3129 Passes in California Senate and Nears Finish Line | Healthcare Law Blog (sheppardhealthlaw.com), published September 6, 2024, California's AB 3129: A New Hurdle for Private Equity Health Care Transactions on the Horizon? | Healthcare Law Blog (sheppardhealthlaw.com), published April 18, 2024, and Update: California State Assembly Passes AB 3129 Requiring State Approval of Private Equity Healthcare Deals | Healthcare Law Blog (sheppardhealthlaw.com), published May 30, 2024.

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