

Mergers and Acquisitions

Amazon Deal Brightens Blase January Health Transactions Landscape

The late January announcement that Amazon.com Inc., BerkshireHathaway Inc., and JPMorgan Chase & Co. plan to join forces to meet their employees' health-care needs created a lot of health-care industry deal-making buzz in a month that was otherwise on the quiet side.

The announcement sent shock waves through the health-care industry because the three companies aim to change how health care is provided to their combined 1 million U.S. employees and because the move has the potential to revolutionize health-care delivery and payment in America more broadly. It also helped transform a month that started out a bit dull on the health-care transactions front, but ended with a bang.

The list of transactions announced and closed in January reflects the growth and flexibility in a \$3 trillion industry, where health-care providers are jockeying for positions where they can continue to thrive in the face of lower payments and higher costs. At the same time, some highly publicized deals show there still is a lot of room for, and interest in developing, innovative ideas that may solve some of the problems facing the industry.

Although January did not see any major health-care deals, such as several hospital deals that were announced or closed in December, Bloomberg Law's experts in the health-care mergers and acquisitions space said they are convinced there are multiple deals "in the pipeline." Expect 2018 to be a banner year in terms of the number of consolidation transactions across many sectors throughout the health-care industry, they said.

Direct Contracting The Amazon announcement was scant on details, and no one quite knows what the companies have in mind. Without trying to predict what the three will do, one possibility is direct contracting.

In direct contracting arrangements, self-insured employers cut out the middleman and contract directly with health-care providers. Providers may create clinically integrated networks or accountable care organizations designed to meet the employers' needs, but health insurers, health maintenance organizations (HMOs), and preferred provider organizations (PPOs) are not used as the primary network or administrators, Gary W. Herschman, a member of Epstein, Becker & Green health care and life sciences team, told Bloomberg Law.

Further, if a health system has or acquires sufficient internal claims processing capabilities, there may be no need for a third party administrator, Herschman said.

Large health systems are "gearing up" to be able to offer these arrangements, Herschman said. He is a Bloomberg Law advisory board member whose practice is based in New York and Newark, N.J.

Kevin J. Ryan, also of Epstein, Becker & Green, agreed that the health-care industry will see more direct-to-employer contracting in 2018. Employers are beginning to evaluate which facilities and services their employees use most and how they can efficiently and cost-effectively make the services available more directly and at lower cost.

Ryan, who is in the firm's Chicago office, told Bloomberg Law employers can be expected to use these direct contracting arrangements as a tool for retaining and recruiting employees. Employers "have an incentive to keep employees happy" and to offer perquisites that will attract top-level talent.

Offering potential employees access to high-quality health care is as important as being able to offer them jobs in communities that have good schools or other amenities for which they may be looking, he said.

No Major Transactions, Yet Herschman and Ryan both observed that January's list doesn't contain the same type of big transactions seen at the end of 2017. There were no deals announced that would create 191-hospital health systems or huge payer-provider conglomerates, they noted.

Neither, however, expects that to continue through the coming months. Big hospital systems will continue to consolidate, and small independent hospitals will be "picking sides" and joining larger systems, Herschman said. Stand-alone hospitals will be "few and far between," he said.

The most movement in the hospital space right now seems to be among smaller regional systems consisting of between 10 and 15 hospitals that are major players in their regions but not beyond, Herschman said. These systems are merging or affiliating with similar-sized systems in contiguous geographic areas that aren't in direct competition, thus lessening antitrust law concerns.

The deal between Aurora Health Care, a 15-hospital system based in Milwaukee, and Advocate Health Care, Illinois's largest nonprofit system with 12 acute care hospitals, is a good example. The two recently announced the Federal Trade Commission and state regulators have approved their proposed merger.

Physician Practice Deals Physician practice deals made up the biggest wedge in the health-care deal pie in January, with 23 deals reported or closed over the month.

Among other things, the list shows that health systems still are actively acquiring practices. Lots of attention is being paid to private equity and large national companies, as they continue investing in and consolidating physician practices, Herschman said. It is clear, however, that hospitals haven't left the physician practice market.

The most often targeted practices, as seen over the past few months, still are eye care, dermatology, gastroenterology, and those that involve multiple disciplines. Movement, however, is being seen in the the orthopedic (musculoskeletal), radiology, behavioral health, and health-care staffing spaces.

Behavioral Health/Autism Space Ryan said the behavioral health-care deals are just a "precursor." He expects to see many more deals in this area, especially those involving providers engaged in opioid addiction and autism treatment.

Michael Mahoney and Robert Aprill, of Provident Healthcare Partners, in Los Angeles and Boston, respectively, told Bloomberg Law the strong transactional activity in the behavioral health-care market was particularly focused on the autism treatment segment in January.

"Autism has attracted considerable interest from the private equity community for the past 12 to 18 months," they told Bloomberg Law. "Shore Capital Partners' sale of The Stepping Stones Group exemplifies the investment opportunity within the sector, as the fund reportedly earned a seven-time return on its investment, according to PE Hub's Buyouts newsletter."

"While valuations within behavioral health remain high, private equity firms continue to be drawn to the prospect of achieving above-market returns, and this will remain a fundamental driver of deal flow within the sector in 2018," Mahoney and Aprill said.

Health-Care Staffing Moves Mahoney and Aprill also highlighted the movement in the health-care staffing sector, where four significant transactions closed in January. Activity in this sector "was dominated by strategic consolidators, which are seemingly favoring transactions that provide vertical integration, as opposed to building market share through horizontal acquisitions," they said.

This trend, they said, "is largely a function of health systems and other clients consolidating amongst themselves." The consolidation "is pressuring health-care staffing firms to do the same in order to remain competitive in the marketplace and provide a full suite of services to clients."

Private equity firms also "continue to recognize the value of staffing firms, given the micro-economic drivers supporting growth in overall demand within the sector," Mahoney and Aprill said.

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The list of select transactions involving health-care providers, managed care and services companies for January 2018 was compiled by health-care investment bankers using publicly available information, including articles, websites, and press releases.

The January list is at <http://src.bna.com/wvO>.

Bloomberg BNA would like to thank its Health Care Transactions Editorial Committee for their guidance:

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Epstein, Becker & Green PC did not comment on any particular transaction or party discussed or listed in this article.

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