

# **Provident Perspectives:**

## **An Update on Investment & Consolidation in the Addiction Treatment Sector**

*Examining recent developments and key trends within the addiction treatment space*



**Provident**  
Healthcare Partners

# Introduction

The addiction treatment sector continues to be one of the most active investment areas within the healthcare services universe, as a combination of attractive macro level tailwinds and favorable demand dynamics drive consolidation and outside investor interest.

Substance use disorder (“SUD”) cases increased in recent years due to elevated levels of mental distress, a rise in the prevalence of potent drugs, and the continued lack of recovery support. Concurrently, drug overdose deaths in the United States also increased, soaring from 185K in 2020 to 215K in 2021 (16% year-over-year increase), with nine states realizing a 30% annual increase in substance use-related mortality.<sup>(1)</sup>

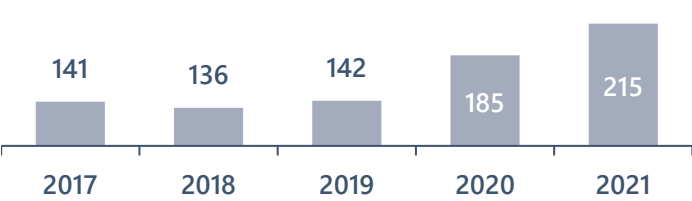
Recent regulatory developments implemented to combat the crisis, such as the Eliminating Kickbacks in Recovery Act (“EKRA”) and amendments to the Mental Health Parity and Addiction Equity Act (“MHPAEA”), prompted industry alignment between patients and payors for comprehensive treatment offerings. As a result, addiction treatment programs focused their efforts to expand operational capabilities and accessibility to treatment options, driving outside investment in the sector.

So much so, that as of Q2 2022, 45+ groups operated across the United States with private equity backing. 27 states currently have a presence of five or more platforms, with 13 states having a presence of 10+. Most consolidation has been fairly recent, with over 75% of transactions occurring since the start of 2016 and approximately 15 organizations moving on to their second or third private equity partner.<sup>(3)</sup>

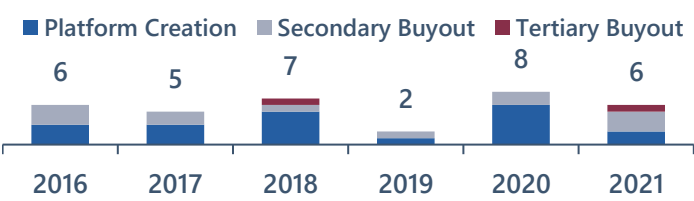
Given the current transaction landscape and rate at which the sector continues to mature, we expect to see increased competition for transactions among sponsors already invested in the space. Further, half of platforms on both their first and second private equity partner are 5+ years into their investment hold period, suggesting an uptick in both secondary and tertiary buyouts, as well as add-on acquisitions.

Provident Healthcare Partners (“Provident”) is an investment banking firm exclusively focused on advising healthcare companies through transactions. In this white paper, we examine the evolution of regulation and investment within the sector, emerging transaction and industry trends, as well as key drivers for premium valuations.

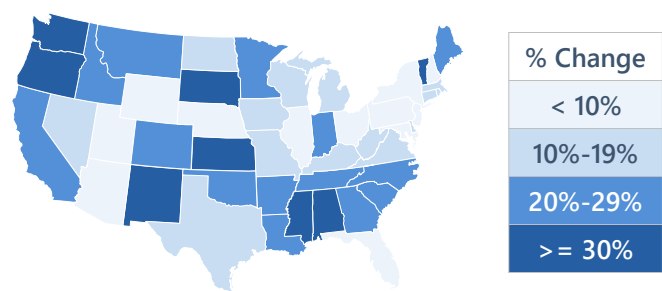
Overdose Deaths by Year (Thousands)<sup>(1)</sup>



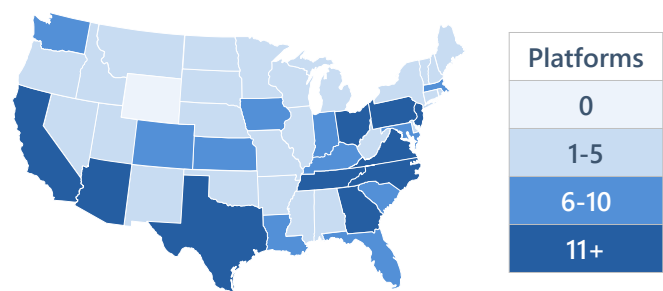
Platform Transaction Timeline<sup>(3)</sup>



Overdose Deaths by State (2021 vs. 2020)<sup>(1)(2)</sup>



Platform Representation by State<sup>(3)(4)</sup>



<sup>(1)</sup> CDC; <sup>(2)</sup> Includes Hawaii (-3.3%), Alaska (74.7%), and the District of Columbia (4.9%); <sup>(3)</sup> Transaction statistics based on research completed by Provident; <sup>(4)</sup> Includes Hawaii (0 platforms), Alaska (2 platforms), and the District of Columbia (4 platforms)

# Evolution of the Addiction Treatment Space

Early History	2005	2006	2008	2010
	<ul style="list-style-type: none"> <li>Limited high-quality treatment options</li> <li>Community-based centers dominate the addiction treatment market</li> </ul>	<ul style="list-style-type: none"> <li>Vantage Capital Partners establishes Behavioral Health Group as a platform</li> </ul>	<ul style="list-style-type: none"> <li>Mental Health Parity and Addiction Equity Act ("MHPAEA") enacted requiring group health plan and insurance coverage for mental health conditions</li> </ul>	<ul style="list-style-type: none"> <li>Affordable Care Act ("ACA") enacted increasing coverage for the uninsured</li> <li>ACA expanded MHPAEA coverage to apply to individual health insurance</li> </ul>
Industry Expansion	2011	2015	2017	
	<ul style="list-style-type: none"> <li>Rapid growth following ACA enactment</li> <li>Frontenac Company acquires Behavioral Health Group from Vantage Capital Partners in a secondary buyout</li> </ul>	<ul style="list-style-type: none"> <li>Flexpoint Ford establishes Summit Behavioral Healthcare as a platform</li> <li>Webster Equity Partners establishes BayMark Health Services as a platform</li> <li>Billing codes established to create quality and standards among practices</li> </ul>	<ul style="list-style-type: none"> <li>FFL Partners and Lee Equity acquire Summit Behavioral Healthcare from Flexpoint Ford in a secondary buyout</li> <li>Rise in profitability due to lack of regulation</li> <li>Quality concerns due to patient-brokering and deceptive marketing tactics</li> </ul>	
Regulatory Response	2018	2020	2021	
	<ul style="list-style-type: none"> <li>Legislation responds to growing awareness of malpractice while increasing accessibility to treatment services</li> <li>Eliminating Kickbacks in Recovery Act ("EKRA") enacted prohibiting kickbacks from patient referrals</li> <li>The Vistria Group acquires Behavioral Health Group from Frontenac Company in a tertiary buyout</li> </ul>	<ul style="list-style-type: none"> <li>MHPAEA amendment requires insurers to disclose non-quantitative treatment limitations for SUD benefits (establishes parity between behavioral health and medical/surgical care)</li> <li>Title 42 changes expand the permissible use of patient consent in disclosures (facilitates better care coordination while maintaining confidentiality)</li> </ul>	<ul style="list-style-type: none"> <li>Landmark EKRA case reduces abusive marketing</li> <li>Reinstated X waiver increases difficulty in receiving MAT</li> <li>Patient Square Capital acquires Summit BHC from FFL Partners and Lee Equity in a tertiary buyout</li> </ul>	

As the stigma surrounding mental health has declined in recent years, legislators continue to place guard-rails to make addiction treatment more affordable and accessible. The 2008 MHPAEA enactment, followed by the ACA in 2010, broadly expanded service coverage and resultingly sparked a period of growth within the sector. Three major players in the space, Behavioral Health Group, BayMark Health Services, and Summit Behavioral Healthcare, led the pack with 90+ combined add-on acquisitions since 2010.<sup>(1)</sup>

However, a lack of established billing codes created an opportunity for high profitability without a focus on maintaining quality care, as industry operators took advantage of flexible pricing and other malpractices such as patient-brokering, flophouses, and aggressive internet marketing. In response, legislators developed quality and billing standards among practices while also ensuring widespread access to care.

<sup>(1)</sup> Transaction statistics based on research completed by Provident

# Emerging Trends in Addiction Treatment

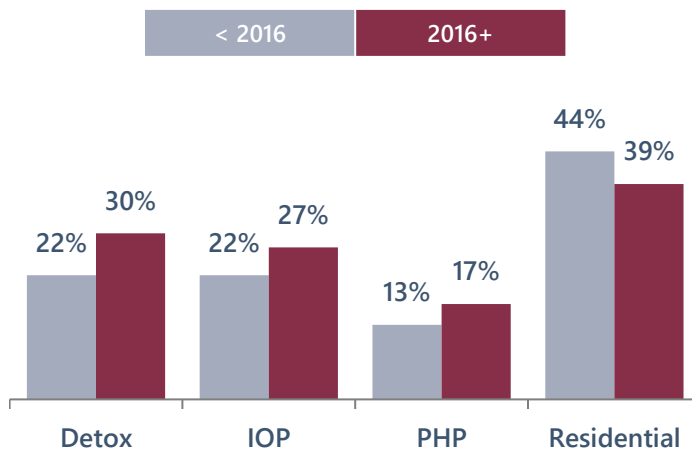
Contrary to other sectors, the COVID-19 pandemic led to an uptick in growth in the addiction treatment space. As compared to pre-pandemic levels, the number of individuals seeking addiction treatment increased 10-20% due to record drug overdose deaths and relapses, heavy drinking, and general stress.<sup>(1)</sup> In June 2020, 13% of Americans reported increased substance use to cope with the ongoing stress and anxiety surrounding the pandemic.<sup>(2)</sup> The surging demand for treatment forced many programs to streamline operations, reassess staffing needs, and augment service offerings, most of which were accomplished with the help of a strategic partner. Resultingly, transaction activity remained steady, represented by 90+ transactions from 2020 to 2021, with 20+ transactions realized through the first quarter of 2022, setting the pace for a record-breaking year.<sup>(3)</sup>

## Integrated Care Models

To increase patient reach and retention, large SUD programs predominantly looked to expand across the continuum of care. A full-service model allows programs to increase patient retention and reduce drop-out rates, all while increasing revenue per patient capture. Webster Equity-backed BayMark Health Service's ("BayMark") shift in investment thesis represents an example of this trend. Initially, an office-based opioid treatment-focused platform, BayMark refined their focus to addiction treatment centers that offered a broader suite of services, executing on transactions across the care continuum to include companies in the detox, intensive outpatient program ("IOP"), partial hospitalization program ("PHP"), and residential spaces.<sup>(3)</sup>

By offering comprehensive treatment services, organizations can capture additional pay points across a patient's care cycle. Vertical integration also provides synergistic capabilities as companies can better manage and coordinate quality care, own part of the referral stream, and achieve economies of scale via the utilization of overlapping providers.

## Add-On Acquisitions by Treatment Service<sup>(3)</sup>



Add-on acquisitions by treatment service further exemplifies investor interest in expanding service offerings via cross segment consolidation.




Prior to 2016, 44% of add-on acquisitions were made in groups that offered residential services, whereas that percent decreased to 39% from 2016 to present. Over that same time period, investors focused on detox, intensive outpatient, and partial hospitalization programs.

## BayMark Health Services Transaction History<sup>(3)</sup>

### 2015-2019: MAT Transactions



### 2020-2021: Comprehensive Model Transactions

			
Detox	✓	✓	✓
IOP	✓	✓	✓
PHP	X	✓	✓
Residential	✓	✓	✓

# Emerging Trends in Addiction Treatment *(Continued)*

## Dual-Diagnosis & Co-Occurring Treatment

Another recent development in the addiction treatment space has been the addition of dual diagnosis and co-occurring treatments. Integrating psychiatric services provides an interesting opportunity for the sector, as SUD platforms expand their capabilities to treat underlying mental illness.

Estimates show that approximately 50% of individuals with a mental illness also suffer from substance use disorder.<sup>(1)</sup> While the links between the two are complex, recent studies show substance use either begins as individuals attempt to cope with a mental illness, or the two start simultaneously in reaction to a traumatic experience. The latest developments in treatment show an integrated approach to be the most effective, where an individual is treated for both SUD and mental illness at the same time by the same provider.

As a result, historically substance use disorder-focused platforms have started to build upon service offerings to include mental health treatment options. As an example, the Center For Discovery acquired Cliffside Malibu in 2018, and together rebranded to Discovery Behavioral Health (“DBH”). The acquisition established DBH as a leading SUD provider with 42 residential treatment centers and 23 outpatient centers across 11 states. Since then, DBH has made several psychiatric acquisitions to establish itself as a leader in co-occurring mental health treatment.

DBH Mental Health Acquisitions<sup>(2)</sup>

2019	• New Life Addiction Counseling & Mental Health Services
2020	• Associated Behavioral Health Care
2021	• Awakenings KC Clinical Neuroscience Institute
2022	• Dan Med TMS Neuro Institute • Anew Era TMS & Psychiatry

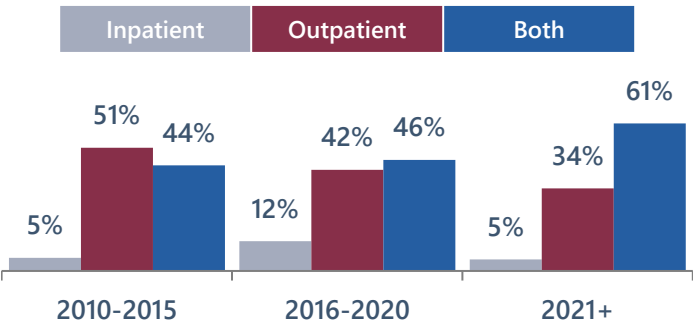
## Treatment Care Settings

The decision to enroll in an addiction treatment program is based on several factors, but for many, it comes down to accessibility and affordability. While it should be noted that patients medically requiring inpatient services should seek inpatient care, there are many outpatient options available to individuals suffering from SUD. Furthermore, studies show that effective treatment starts with inpatient offerings, followed by some form of outpatient care, such as an intensive outpatient or partial hospitalization programs.

As people became more reliant on local treatment options through the pandemic, individuals preferred outpatient and community-based services to the traditional destination treatment model. Transaction activity followed suit, as since the start of 2020, private equity investment into pure outpatient centers outpaced that of pure inpatient centers by 9-1.<sup>(2)</sup>

Additionally, the pandemic led to the rise of solely telehealth-focused companies, with Bicycle Health, an online MAT provider active in 27 states, as one such example of the industry’s shift towards virtual treatment offerings. Online treatment options increase the reach and availability of services, but also add an additional layer of confidentiality. Private equity investment is still in the early stages but will likely accelerate in the coming months and years as telehealth becomes a permanent fixture within treatment modalities.

Transaction Volume by Care Setting<sup>(2)</sup>



<sup>(1)</sup> Integrated Treatment of Substance Use and Psychiatric Disorders by Thomas Kelly and Dennis Daley; <sup>(2)</sup> Transaction statistics based on research completed by Provident

# Emerging Trends in Addiction Treatment *(Continued)*

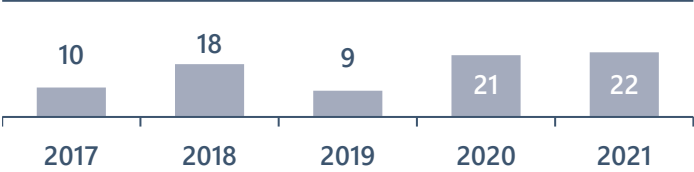
## MAT & OBOT

Similar to trends within the broader addiction treatment space, programs focused on the medication-assisted treatment (“MAT”) and office-based opioid treatment (“OBOT”) spaces realized increases in transaction activity. MAT and OBOT treatment models offer flexible dosing and higher patient retention rates, making the sector a very attractive space for investment.

Furthermore, MAT and OBOT programs are proven to lower costs within the healthcare system as they provide evidence-based treatment plans at accessible rates, largely covered by all insurance plans. As a cost-saving haven, MAT and OBOT organizations are well-positioned for integrated and value-based care models.

Despite the opportunity for improved outcomes and cost savings, value-based care payment models have not gained much traction in the addiction treatment space due to a lack of consensus on quality measures. The most widely accepted model today is the Patient-Centered Opioid Addiction Treatment (“P-COAT”) model designed by the American Society of Addiction Medicine (“ASAM”) and the American Medical Association (“AMA”). Risk-adjusted payments under P-COAT are performance based and tied to the percentage of patients who both fill medications and demonstrate treatment plan compliance. The P-COAT model also tracks drug-testing programs and emergency department visits to measure performance. As industry stakeholders move towards consensus on quality measures, value-based care payment models provide the opportunity to improve outcomes and reduce costs in the addiction treatment space.

MAT Transaction Activity<sup>(1)</sup>



## Primary Care

The implementation of value-based care models also depends on the integration and coordination of care from primary care providers. The majority of addiction treatment is conducted in a specialty setting, where the expansion of services to primary care supports efforts to provide high-quality and accessible treatment options. To be successful, primary care integration will require greater training and resources as policymakers and payors align to expand treatment access.

### Expanding MAT Access through Integrated Programs in Primary Care Practices

#### OUD Treatment Models in Primary Care<sup>(2)</sup>

**Clinician Model** – Several prescribing clinicians supported by one medical assistant; physicians see patients regularly

**Group Model** – Prescribing clinicians are supported by a licensed behavioral health counselor; the prescriber sees patients frequently and patients participate in weekly group therapy sessions

**OBOT Model** – Small number of prescribers see patients at the beginning of treatment and then as needed; patients are managed by RNs

#### Facilitators of Success in Integrated Programs



Provider Champions



Technical Support



OUD Education & Support



Mental Health Services



Group Meetings



Strong Leadership

<sup>(1)</sup> Transaction statistics based on research completed by Provident; <sup>(2)</sup> Massachusetts Health Policy Commission

# Driving Value in an Addiction Treatment Platform

## Key Drivers for Premium Valuations

### Robust Outcome Tracking

- Tracking outcomes can increase team member productivity, organization, and accountability
- Utilization review and quality metrics assist in third-party payor negotiations

### Platform-Quality Leadership Team

- Experienced leadership teams position treatment programs for continued growth
- Business-oriented leaders bring a knowledge base to streamline operations

### Low Patient Drop-Out Rates

- Effective programs demonstrate low patient drop-out levels and high program completion levels
- Favorable measures indicate a high-quality addiction treatment program

### In-Network Contracting

- Out-of-network programs struggle to maintain consistent referral streams
- Well contracted programs mitigate reimbursement risk and demonstrate an improved collection cycle

### Strong Local Presence

- Most successful treatment centers benefit from key relationships built within their local community
- Partnering with local referral sources reduces the costs of acquiring and recruiting patients

### Diversified Revenue Streams

- Treatment programs that offer multiple treatment modalities reduce revenue concentration risk
- Ancillary offerings such as case management and mental health complement core SUD services

### Growing Continuum of Care

- Programs with multiple treatment levels better accommodate patients as their needs develop
- Following up with patients after treatment plan completion reduces the chance of relapse

### Effective Multimedia Marketing

- Contrary to other healthcare verticals, addiction treatment is largely self-directed
- Multimedia marketing strategies create brand equity for addiction treatment platforms

Valuation multiples within the addiction treatment space continue to be quite rich relative to most other sectors in healthcare services. That being said, valuations are ultimately a function of growth and risk; the more attractive the growth profile of the business, the higher the multiple on earnings that one can expect to garner in a sale.

When evaluating a business, investors carefully perform due diligence in several areas, most notably outcome tracking capabilities, in-network contracting, patient drop-out/program completion rates, and levels of care offered. Post-pandemic, easily accessible addiction treatment centers that could accommodate patients'

needs, regardless of the level of care, drew greater interest from outside investors.

One such example of the frothy post-pandemic valuation landscape is Patient Square Capital's ("PSC") tertiary buyout of Summit Behavioral Healthcare ("SBH") from FFL Partners ("FFL") and Lee Equity Partners ("Lee") in 2021. Since FFL and Lee's investment in 2017, SBH opened five additional centers and acquired seven companies across substance use disorder and psychiatric care specialties. At FFL and Lee's exit, SBH commanded an approximate valuation of \$1.3 billion, implying an approximate EBITDA multiple of 15x.<sup>(1)</sup>

<sup>(1)</sup> Estimated, based on research completed by Provident

# Partnership Considerations

There are several partnership options afforded to business owners looking to explore a transaction. With over 45 platforms in the space, not all partnership opportunities are created equal.<sup>(1)</sup> As such, it is important to vet and perform in-depth reverse diligence on potential partners and their respective models to determine the likelihood of go-forward success as well as philosophical and cultural alignment.

	Platform Investment	Add-On Acquisition
<b>Cash Proceeds at Close</b>	<ul style="list-style-type: none"> <li>Lower due to rollover equity requirement</li> </ul>	<ul style="list-style-type: none"> <li>Potential for 100% buyout &amp; succession plan</li> </ul>
<b>Rollover Equity</b>	<ul style="list-style-type: none"> <li>Ability to retain meaningful equity ownership &amp; benefit from value appreciation</li> </ul>	<ul style="list-style-type: none"> <li>Rollover equity is shared across a network of agencies, diversifying risk, but limiting upside potential</li> </ul>
<b>Strategic &amp; Operational Autonomy</b>	<ul style="list-style-type: none"> <li>Allows for the most operational &amp; strategic autonomy to retain key providers/staff</li> </ul>	<ul style="list-style-type: none"> <li>Lower strategic &amp; operational autonomy as compared to a platform investment</li> </ul>
<b>Valuations</b>	<ul style="list-style-type: none"> <li>No synergies factored into initial valuation</li> </ul>	<ul style="list-style-type: none"> <li>Typically, higher valuations than platform investments due to revenue and expense synergies</li> </ul>
<b>Synergies &amp; Best Practice Sharing</b>	<ul style="list-style-type: none"> <li>Best practice sharing not necessarily available at initial phase</li> <li>Platform companies must have the infrastructure and ambition to scale outside of their current markets</li> <li>Existing management team leveraged for growth initiatives</li> </ul>	<ul style="list-style-type: none"> <li>Ability to share operational &amp; clinical best practices</li> <li>Ability to leverage platforms centralized back-office resources and infrastructure</li> <li>Access to experienced management teams</li> <li>Potential to gain leverage with payors or benefit from improved rates due to economies of scale</li> </ul>
<b>Board Representation</b>	<ul style="list-style-type: none"> <li>High likelihood for board level representation &amp; voting power</li> </ul>	<ul style="list-style-type: none"> <li>Limited opportunity for board level representation &amp; voting power</li> </ul>
<b>Risk</b>	<ul style="list-style-type: none"> <li>More risk than joining an existing platform</li> </ul>	<ul style="list-style-type: none"> <li>Economies of scale and revenue diversification limits go-forward risk</li> </ul>
<b>Other Considerations</b>	<ul style="list-style-type: none"> <li>Not an option for all groups due to size and infrastructure parameters</li> </ul>	<ul style="list-style-type: none"> <li>Potential clash of organizational cultures within combined entity</li> </ul>

<sup>(1)</sup> Transaction statistics based on research completed by Provident

# Select Private Equity Transactions

## Select Private Equity Platform Investments (2021 to Present)<sup>(1)</sup>

Date	Acquirer	Target	Transaction Type
Jul-22	The Vistria Group	Sandstone Care	Platform Creation
May-22	Traverse Pointe Partners	The Hope House	Platform Creation
Mar-22	Retro Capital Group	Resurgence Behavioral Health	Platform Creation
Mar-22	Amulet Capital Partners	Lighthouse Behavioral Health	Platform Creation
Feb-22	Webster Equity Partners	Oceans Healthcare	Secondary Buyout
Dec-21	FFL Partners	Community Medical Services	Secondary Buyout
Nov-21	Patient Square Capital	Summit Behavioral Healthcare	Tertiary Buyout
Jul-21	Onex Partners	Newport Academy	Secondary Buyout
May-21	Nautic Partners	Pyramid Healthcare	Secondary Buyout
Apr-21	RiverGlade Capital	2 <sup>nd</sup> Chance Treatment Center	Platform Creation
Apr-21	Myconic Capital	Mindscape Ketamine and Infusion	Platform Creation

## Select Private Equity Add-On Acquisitions (YTD 2022)<sup>(1)</sup>

Date	Acquirer	Target	Financial Sponsor
Jul-22	BayMark Health Services	San Antonio Recovery Center	Webster Equity Partners
Jul-22	Discovery Behavioral Health	Anew Era TMS & Psychiatry	Webster Equity Partners
Jun-22	Pinnacle Treatment Centers	Stepping Stone in North Carolina	Linden Capital Partners
Jun-22	Spero Health	My Turning Point	Heritage Group
Apr-22	Bradford Health Services	The Estate at River Bend	Centre Partners
Apr-22	Mindscape Ketamine and Infusion	Tristar Wellness	Myconic Capital
Mar-22	Mindpath Health	Psychiatric Centers at San Diego	Centerbridge Partners
Mar-22	BayMark Health Services	Emerald Isle Health & Recovery	Webster Equity Partners
Mar-22	BayMark Health Services	Pathfinders Recovery Center	Webster Equity Partners
Mar-22	Behavioral Health Group	Beacon Specialized Livings Services	The Vistria Group
Mar-22	Discovery Behavioral Health	Dan MED TMS Institute	Webster Equity Partners
Feb-22	BayMark Health Services	Mahajan Therapeutics	Webster Equity Partners
Feb-22	BayMark Health Services	Lucina Treatment Centers	Webster Equity Partners
Jan-22	Behavioral Health Group	Center for Behavioral Health	The Vistria Group
Jan-22	Summit Behavioral Healthcare	Strategic Behavioral Health	Patient Square Capital
Jan-22	BayMark Health Services	Kaden Health	Webster Equity Partners

<sup>(1)</sup> Transaction statistics based on research completed by Provident

# Conclusion

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Given the rapid growth of the addiction treatment space and the rate at which the market continues to mature, Provident expects the sector to realize continued consolidation, represented by an uptick in secondary buyouts and increased competition among platforms for add-on acquisitions. As competition escalates across the marketplace, Provident anticipates both financial and strategic investors to pay high valuations for groups that exhibit key value drivers, such as a strong in-network contract base, high patient retention rates, robust data tracking capabilities, and effective marketing strategies.

Furthermore, consolidators will continue to look towards vertically integrated care models that bring a

comprehensive offering to the space. By integrating primary care and psychiatric services to the care platform, organizations can better manage a larger portion of the patient’s treatment program.

For operators considering private equity or strategic partnership, Provident recommends business owners carefully vet available partnership opportunities to ensure post-transaction goals are achieved. As valuations remain at stable levels, addiction treatment operators stand to benefit from the operational and capital resources provided by outside investors, which will hopefully continue to make a meaningful impact on the lives of those suffering from substance use disorder.

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Provident is the leading investment banking firm specializing in merger and acquisition advisory, strategic planning, and capital formation for middle-market and emerging growth healthcare companies.

The firm has a vast network of senior industry relationships, a thorough knowledge of market sectors and specialties, and unsurpassed experience and insight into the investment banking process.

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