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Proposed California Legislation AB 3129 Would Require Attorney General Approval for Private Equity and Hedge Fund Acquisitions of Certain Healthcare Entities

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Private equity is a growing presence in the healthcare sector, but that trend has drawn a backlash from federal and state regulators. Private equity firms have found increasing opportunities in the healthcare sector in recent years. More than 780 private equity deals in the U.S. healthcare sector were announced or closed in 2023, a slight decline from 2022 but still the third-highest on record. *See* Healthcare Dive, *Healthcare PE deals third-highest on record in 2023: Pitchbook*, Feb. 12, 2024. The Private Equity Stakeholder Project lists over 450 U.S. hospitals owned by private equity firms, including 22 in California. Private Equity Stakeholder Project, *Private Equity Hospital Tracker*, updated Jan. 2024. Private equity is a growing presence in nursing homes and hospice agencies. That trend has drawn a backlash from federal and state regulators, however. In the last three months, Congress, antitrust regulators, and the Department of Justice have all announced efforts to target private equity firms in the healthcare industry. In December 2023, the Chair and Ranking Member of the United States Senate Budget Committee announced "a bipartisan investigation into the effects of private equity ownership on our nation's hospitals." U.S. Senate Budget Committee, *Press Release*, Dec. 7, 2023. The White House announced on December 7 that it was taking action to promote competition in healthcare, including greater scrutiny of acquisitions and "a cross-government public inquiry into corporate greed in health care." The White House, *FACT SHEET: Biden-?Harris Administration Announces New Actions to Lower Health Care and Prescription Drug Costs by Promoting Competition*, Dec. 7, 2023. Following up on that announcement, the Federal Trade Commission, on March 5, 2024, convened a workshop "aimed at examining the role of private equity investment in health care markets." And on February 22, 2024, Principal Deputy Attorney General Brian Boynton announced at a conference that the Department of Justice would be using the False Claims Act to target private equity firms that influence healthcare providers to engage in conduct that causes the submission of false claims. Brian M. Boynton, *Remarks at the 2024 Federal Bar Association's Qui Tam Conference*, Feb. 22, 2024. Last year was a record year for new False Claims Act matters, and healthcare cases have constituted the majority of FCA recoveries in recent years. *See* Gibson Dunn's False Claims Act 2023 Year-End Update, March 4, 2024. There can be little doubt that there will be an increase in cases involving private equity-owned healthcare providers. State legislators and regulators in California have also been active in turning up the heat on private equity firms in the healthcare industry. On February 16, 2024, California Attorney General Rob Bonta and Assembly Speaker pro Tempore Jim Wood (D-Healdsburg) introduced a bill that would require private equity groups and hedge funds to obtain the written consent of the California Attorney General before acquiring or effecting a change of control with respect to a healthcare facility or healthcare provider group. *See* Asm. Jim Wood, *Press Release*, Feb. 20, 2024. The bill, AB 3129, would authorize the Attorney General to deny or impose conditions on such a transaction upon a determination that it poses a risk of anticompetitive effects or reduced

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access to healthcare. Under existing law, the California Attorney General may block or impose conditions upon certain sales or transfers of control with respect to *nonprofit* healthcare facilities. *See* Cal. Corp. Code § 5914, *et seq*. This oversight has generated significant controversy, with many asserting that the review process is too stringent and often leads to debilitating conditions on these transactions. *See* Wall Street Journal, *California Nonprofit Hospitals Turn to Bankruptcy for Leverage Against State*, July 30, 2023. AB 3129 would expand upon this framework by creating an attorney general review and consent process for certain sales or transfers of control with respect to *for-profit* healthcare entities. The proposed law would continue the trend of increasing state oversight of the healthcare sector in California. In 2022, the California Legislature passed a bill establishing the Office of Health Care Affordability ("OHCA"), and required written notice to OHCA of certain sales of, or transfers of control with respect to, health care entities. *See* SB-184 (2022). OHCA began accepting these submissions in January 2024. While OHCA cannot prevent or impose conditions on such transactions, it may issue a referral to the Attorney General "for further review of any unfair methods of competition, anticompetitive behavior, or anticompetitive effects." *Id.* § 127507.2(d)(1). AB 3129, by contrast, would directly require Attorney General review—not merely upon referral from OHCA. Additionally, the Attorney General would be granted express powers to deny or impose conditions upon certain transactions. As detailed below, those requirements could be based not only on concerns about the impact of the transaction on competition, but on concerns relating to healthcare access more generally. AB 3129 was introduced with the express backing of the California Attorney General, who, in a statement of support for the bill, accused private equity of "maximizing their profits at the expense of access, quality, and affordability of healthcare for Californians." Attorney General Rob Bonta, *Press Release*, Feb. 20, 2024. The legislation proposes several sections that would be codified in the California Health and Safety Code beginning with a new section 1190. **I. Framework** The bill requires private equity groups and hedge funds to provide written notice to the Attorney General at the same time that any other state or federal agency is legally required to be notified, and "otherwise . . . at least 90 days before the change in control or acquisition[.]" AB 3129, § 1190.10(a). "Hedge fund" is defined broadly as "a pool of funds by investors, including a pool of funds managed or controlled by private limited partnerships, if those investors or the management of that pool or private limited partnership employ investment strategies of any kind to earn a return on that pool of funds." *Id.* § 1190(a)(5). "Private equity group" is also broadly defined as "an investor or group of investors who engage in the raising or returning of capital and who invests, develops, or disposes of specified assets." *Id.* § 1190(a)(9). These expansive definitions could have broad applicability to investors in the healthcare sector. While the current draft of AB 3129 provides no deadline for the Attorney General to issue a decision after receiving notice, it implies that the default deadline for such a decision is 90 days. The Attorney General has broad authority to extend this period for an additional 45 days if, for example, it needs extra time "to obtain additional information[,]" or if the proposed transaction "involves a multifacility or multiprovider health system serving multiple communities." *Id.* § 1190.10(b). The Attorney General may grant itself a further 14-day extension in order to hold a public meeting for the purpose of "hear[ing] comments from interested parties." *Id.* §§ 1190.10(c), 1190.30(b). If a "substantive change or modification" to the transaction is submitted to the Attorney General after that public meeting takes place, the Attorney General may hold a second public meeting. *Id.* 1190.30(b). Importantly, the Attorney General may stay its approval process "pending any review by a state or federal agency that has also been notified as required by federal or state law." *Id.* § 1190.10(e). **II. Criteria for Approval** AB 3129 would grant the Attorney General significant discretion to grant, deny, or impose conditions on these transactions. To deny or impose conditions on the transaction, the Attorney General need only determine that it either (1) "may have a substantial likelihood of anticompetitive effects" or (2) "may create a significant effect on the access or availability of health care services to the affected community." *Id.* § 1190.20(a) (emphasis added). As drafted, the bill arguably only requires the Attorney General to establish the mere possibility of either of these two negative outcomes. In making this determination, the Attorney General must apply a "public interest standard," which looks to whether the transaction is "in the interests of the public in protecting competitive and accessible health care markets for prices, quality,

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choice, accessibility, and availability of all health care services . . . ." *Id.* § 1190.20(b). Additionally, the bill stipulates that "[a]cquisitions or changes of control shall not be presumed to be efficient for the purpose of assessing compliance with the public interest standard." *Id.* Prior to issuing the determination, the Attorney General may convene a public meeting to hear from interested parties. *Id.* § 1190.30(b). The Attorney General may waive these notice and consent requirements where a party to the transaction is at grave risk of immediate business failure and can demonstrate a substantial likelihood that it would have to file for bankruptcy absent a waiver. *Id.* § 1190.10(f). For an acquisition or change of control involving smaller providers—a group of two to nine individuals that provides health-related services and has annual revenue of more than $4 million but less than $10 million—the private equity group or hedge fund is required to notify the Attorney General, but the latter's consent to the transaction is not required. *Id.* § 1190.10(d). **III. Reconsideration and Appeal** After the Attorney General issues its written decision, any party to the transaction may apply for reconsideration—but only "based upon new or different facts, circumstances, or law." *Id.* § 1190.30(c). The Attorney General must issue a decision as to reconsideration within 30 days. *Id.* Additionally, where the Attorney General does not consent to the transaction, or gives only conditional consent, "any of the parties" to the transaction may appeal by writ of mandate to a California superior court. *Id.* § 1190.30(d). Such appeals must be sought within 30 days of the Attorney General's decision. The superior court must issue a decision within 180 days, unless the parties otherwise consent, or there exist "extraordinary circumstances[.]" *Id.* Pursuant to the text of the legislation, however, the court's standard of review is highly deferential: whether the Attorney General's decision was a "gross abuse of discretion." *Id.* **IV. Additional Restrictions on Private Equity** AB 3129 also contains provisions prohibiting private equity groups and hedge funds from controlling or directing physician or psychiatric practices—such as by "influencing or setting rates[,]" influencing or setting patient admission, referral or other policies, or "influencing or entering into contracts on behalf of" such practices. *Id.* § 1190.40(a). The bill would also prohibit physician or psychiatric practices from entering into arrangements in which private equity groups or hedge funds manage "any of" their "affairs" for a fee. *Id.* § 1190.40(b). Finally, the bill prohibits certain non-compete and non-disparagement clauses in contracts that private equity groups and hedge funds enter into related to physician or psychiatric practices. *Id.* § 1190.40(c). If enacted, the Attorney General will be authorized to enforce AB 3129 through actions for injunctive relieve and other remedies, including attorney's fees and costs. *Id.* § 1190.40(d). The earliest date on which AB 3129 may be heard in committee is March 18, 2024. The bill has been referred to the Health and Judiciary committees. In California, at least, private equity firms in the healthcare industry must be cognizant not only of the increased scrutiny from federal regulators and enforcement agencies, but also of the expanding oversight role of the California Attorney General in the sector.

The following Gibson Dunn lawyers prepared this update: Benjamin Wagner, Winston Chan, Jonathan Phillips, and Zachary Gross.

Gibson Dunn's lawyers are available to assist in addressing any questions you may have regarding the issues discussed in this update. Please contact the Gibson Dunn lawyer with whom you usually work, the authors, or any leader or member of the firm's White Collar Defense and Investigations, Private Equity or FDA and Health Care practice groups: **White Collar Defense and Investigations**: Stephanie Brooker (+1 202.887.3502, sbrooker@gibsondunn.com) Winston Y. Chan (+1 415.393.8362, wchan@gibsondunn.com) Nicola T. Hanna (+1 213.229.7269, nhanna@gibsondunn.com) Benjamin Wagner (+1 650.849.5395, bwagner@gibsondunn.com) F. Joseph Warin (+1 202.887.3609, fwarin@gibsondunn.com) **Private Equity**: Richard J. Birns – New York (+1 212.351.4032, rbirns@gibsondunn.com) Ari Lanin – Los Angeles (+1 310.552.8581, alanin@gibsondunn.com) Michael Piazza – Houston (+1 346.718.6670, mpiazza@gibsondunn.com) John M. Pollack – New York (+1 212.351.3903, jpollack@gibsondunn.com) **FDA and Health Care**: Gustav W. Eyler – Washington, D.C. (+1 202.955.8610, geyler@gibsondunn.com) John D. W. Partridge – Denver (+1 303.298.5931, jpartridge@gibsondunn.com) Jonathan M. Phillips – Washington, D.C. (+1 202.887.3546, jphillips@gibsondunn.com) © 2024 Gibson, Dunn & Crutcher LLP. All

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