



AMC Transformation through Consolidation Despite the Pandemic

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The COVID pandemic led to an unprecedented operating and financial environment for hospitals and health systems in the U.S. The spike in COVID cases in multiple major waves, overcapacity of ICUs across the country, pressures on caregivers, shortages of clinical staff members, and a host of related challenges wreaked havoc on our nation's healthcare delivery system. These challenges, along with inflationary pressures, resulted in the three-month period ending March 31, 2022 being the toughest financial performance quarter on record for U.S. not-for-profit hospitals and health systems.¹ During this period of unparalleled pressures, academic medical centers (AMCs) have played a distinctive role. In many communities, AMCs are the most viable mainstay against unprecedented demands in care acuity and volume, and at the same time, AMCs play an essential role in ensuring public confidence in healthcare.² Due to these critical roles, AMCs were forced to step up in ways never seen before. As a result, the pandemic hit AMCs harder than other hospitals due in part to greater challenges with cost-cutting because of distinct teaching and research functions and more complex service offerings.³ Yet, despite these range of hurdles, and potentially accelerated by the effects of COVID, AMCs rapidly expanded their reach and enhanced their relevance through consolidation during the period leading into, and continuing throughout, the pandemic.

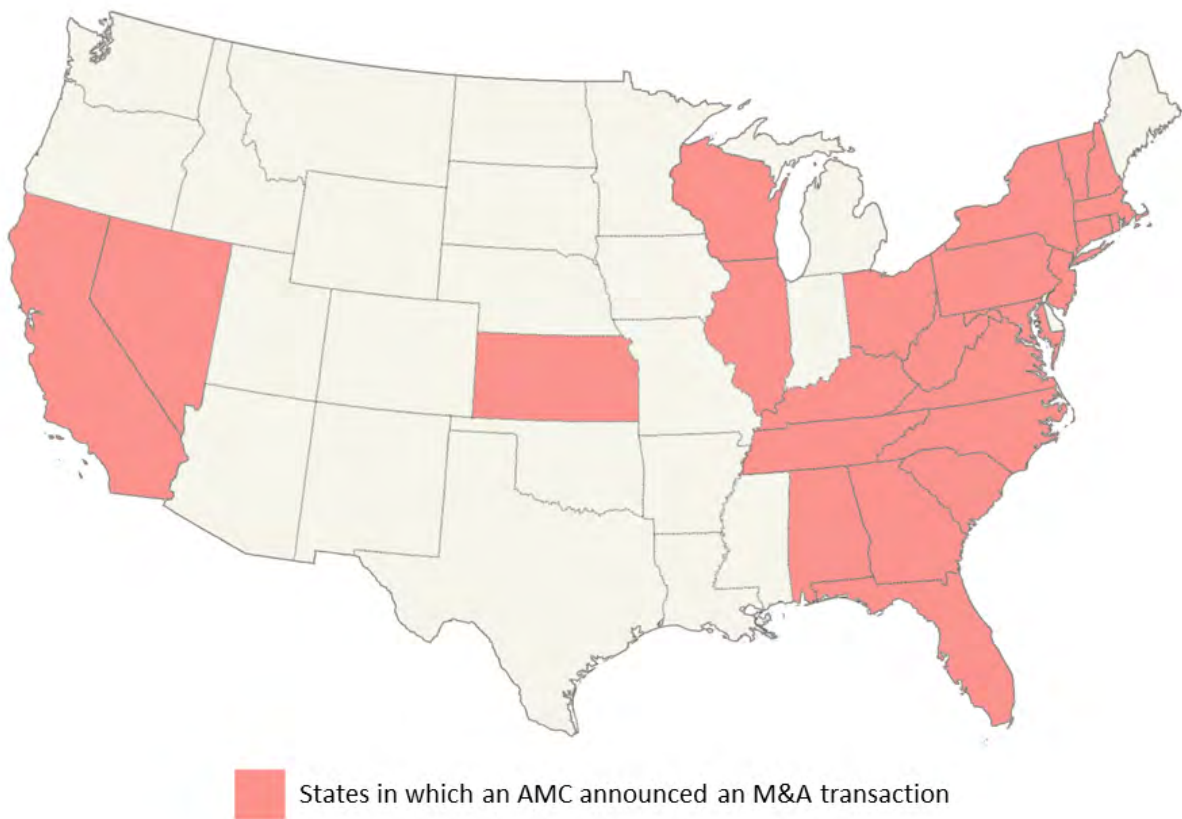
AMC Consolidation

From the third quarter of 2019 through the second quarter of 2022, AMCs announced 42 change-of-control hospital alignments representing 18.6 percent of all announced

- 1 *U.S. Not-for-Profit Acute Health Care Mid-Year 2022 Update: Providers Face Mounting Pressures from Inflation and Labor Costs*, S&P Global Ratings, June 27, 2022.
- 2 Jeffrey R. Balseer, "The COVID-19 Pandemic: A Window into Trust within Academic Medical Centers," *NEJM Catalyst*, August 5, 2021.
- 3 "Not-for-Profit and Public Healthcare—U.S. Medians: Pandemic Hits Academic Medical Centers Harder than Other Hospitals in 2020," Moody's Investors Service, September 29, 2021.

health system M&A over this period.⁴ This included acquisition of for-profit and not-for-profit hospitals, mergers, new joint ventures (JVs) or unwinding of JVs, and new academic affiliation agreement (AAA) alignments. Activity was broad-based geographically spanning 24 states in the U.S. During this 12-quarter period, seven different AMCs announced multiple change-of-control transactions. Despite the challenges of completing transactions during the pandemic, AMCs continued to forge ahead with new alignments that expanded their geographic reach, established new AMC-community hospital combinations, and added needed scale to support their tripartite mission of education, research, and clinical care. These change-of-control alignments followed three major approaches while non-change-of-control alliances proliferated as well.

Announced AMC M&A Activity by State, Q3 2019–Q2 2022



4 Ponder & Co. proprietary database.

Consolidation Approach #1: Acquiring Community Hospitals

Since the third quarter of 2019, AMCs have added numerous community hospitals through membership substitutions with not-for-profit hospitals and also through acquisitions of for-profit hospitals. This wave has continued the trend of transforming single-campus AMCs into metro-wide, statewide, or even regional networks. By expanding in this manner, AMCs focus on providing primary- and secondary-level care closer to patients' homes, at a lower cost than the flagship facility.⁵ For example, MUSC Health in South Carolina transformed from a health system with one flagship medical center to a network of eight hospitals through the acquisition of four hospitals from Community Health Systems in 2019 and three hospitals from LifePoint Health in 2021, as well as a minority equity investment in a not-for-profit health system in 2020. WVU Health System has been the most active AMC announcing six different change-of-control transactions with not-for-profit systems in West Virginia, Ohio, and Maryland. Below is a table of AMCs with more than one transaction announced since the third quarter of 2019.

Academic Health Systems Announcing Multiple M&A Transactions Q3 2019–Q2 2022

| Acquirer | State | Transactions |
|----------------------|--------------|---------------------|
| WVU Health System | WV | 3 |
| | OH | 2 |
| | MD | 1 |
| Geisinger | PA | 2 |
| RWJBarnabas Health | NJ | 3 |
| MUSC Health | SC | 2 |
| UAB Health System | AL | 2 |
| University Hospitals | OH | 2 |
| Vanderbilt Health | TN | 2 |

5 *State of Academic Medical Centers in 2022*, JP Morgan Chase, 2022.

Consolidation Approach #2: New AAA Alignments

Despite the challenges of COVID, two significant academic affiliation agreements were completed. First, in October 2020, Atrium Health and Wake Forest Baptist Health, including Wake Forest School of Medicine, officially joined together as a single enterprise, Atrium Health. The collective vision is to transform medical education, expand patient-centered research and innovation, and define the next generation of clinical excellence.⁶ The combination will lead to a second campus of the school of medicine in Charlotte, which is currently the largest city in the U.S. without a four-year medical school. In June 2021, the University of Nevada, Reno School of Medicine, Nevada's first public AMC, and Renown Health completed a master affiliation agreement designed to enhance Nevada's medical education system, expand clinical research capacity in northern Nevada, and create a world-class integrated health system that improves access to patient care for all and achieves a vision of a healthy Nevada. These two highly complex alignments, which include transfer of certain assets, leases, clinical service agreements, and a range of other related agreements, were completed despite the myriad of COVID challenges.

Approach #3: Creating new JVs and JOAs, as well as Unwinding JVs and Past Mergers

From the third quarter of 2019 through the second quarter of 2022, there were 10 AMC transactions that involved 1) new JVs or joint operating agreements (JOAs) or 2) the unwind of past JVs, JOAs, or mergers. New JVs by AMCs with for-profit partners were completed by Emory Health, University Hospitals, and Vanderbilt Health. These for-profit partners hope to improve their standing in the regions served through the capabilities and halo effect of their AMC partners while the AMCs benefit from the for-profit partners' proficiency at operating community hospitals. Geisinger Health System, Froedtert and the Medical College of Wisconsin, and MUSC Health each completed joint operating companies or minority equity interest transactions with not-for-profit partners. These transactions enable AMCs to establish closer alignments with not-for-profit community health system partners, but without the health system partners having to give up control or management of the systems. However, these transactions are not always a success as reflected by the unwind of JVs or mergers by Geisinger Health System, UVA Health System, and University of Kansas Hospital Authority.

6 "Atrium Health and Wake Forest Baptist Health Combine, Create Next-Generation Academic Health System" (press release), Atrium Health News, October 9, 2020.

→ Key Board Takeaways

- What are the latest trends in community hospital and health system consolidation and alignment activity in our region?
- Which remaining community health systems in our region are critical to our goals and growth plans?
- Are we willing to consider a range of alignment structures that also meet the goals of community health partners?
- Are we ready to move on high-priority opportunities in a timely manner despite the complexities of an AMC and its mission?

Non-Change-of-Control Transactions Continue to Proliferate

In addition to the three trends above, AMCs showed no sign of slowing down in pursuing non-change-of-control alignments during the pandemic. These affiliations included:

- Clinical affiliations such as Nuvance Health in Connecticut becoming a Cleveland Clinic Heart, Vascular affiliate in 2022
- Network affiliations such as Hancock Health and Hendricks Regional Health in Indiana joining Mayo Clinic Care in June 2022
- Non-acute JVs in service lines such as rehabilitation, long-term acute care, and behavioral health such as the new JV between Geisinger and Acadia Healthcare to build two freestanding facilities in Pennsylvania
- Management services agreements such as the new alignment between Southeastern Health and UNC Health

These strategic alignments enable community hospitals to benefit from the expertise, scale, brand, and medical education prowess of its AMC partners without any ownership interest changing hands.

Uncertainty in Regulatory Environment

The recent change-of-control activity has unfolded over a changing regulatory landscape including an executive order highlighting antitrust enforcement in healthcare M&A transactions. Many announced transactions have been abandoned following FTC intervention, including two AMC-related transactions that were

abandoned in the second quarter of 2022 that had been previously announced by Dartmouth Health as well as RWJBarnabas Health. The FTC has challenged six major health system transactions since 2020, and the only transaction that has successfully withstood the intervention involved an AMC via the Jefferson Health-Einstein Healthcare Network merger. Other deals have been materially altered via settlement with the FTC, such as Geisinger Health System’s minority equity investment with Evangelical Community Hospital that was recast following FTC intervention with the settlement limiting the transferred equity position to 7.5 percent and eliminating any Geisinger representation in Evangelical’s governance among other conditions. Although the regulatory environment is becoming increasingly challenging, the mission and imperatives of academic healthcare will continue to lead AMCs to pursue alignments with community hospitals.

Summary

The COVID pandemic created a wide range of challenges and hurdles for hospitals and health systems, and especially for AMCs across the country. But these challenges did not deter AMC’s continued push for expanded networks and transformation of their delivery systems, driven in large part by a pursuit of a wide range of consolidation strategies.

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