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Health System Consolidation Expands to Post-Acute Care

The consolidation of healthcare enterprises has been a consistent trend in the healthcare industry since the 1970s.[1] Generally, consolidation in the healthcare industry was primarily manifested through hospital mergers, which occur in an effort to: (1) decrease administrative costs by creating economies of scale;[2] and, (2) produce efficiencies within healthcare organizations.[3] More recently, consolidation in the healthcare industry has occurred as a reaction to the various provisions of the *Patient Protection and Affordable Care Act* (ACA), which act to: (1) shift the basis of the industry's reimbursement methodologies from volume-driven to value-driven; (2) address the increasing level of healthcare expenditures; and, (3) decrease the high level of wasteful spending in the healthcare delivery system, which accounted for 30% of healthcare expenditures in 2009,[4] as highlighted in an April 2014 Health Capital Topics article.[5]

Between 2005 and 2012, the number of hospital mergers per year increased from approximately 55 mergers to more than 105 mergers.[6] This number continues to rise, as the benefits of creating large health systems become more evident. One of the strengths that hospitals gain when consolidating is the ability to more efficiently purchase and use resources, which is increasingly important in this era of healthcare reform characterized by declining reimbursement rates and high levels of healthcare expenditures.[7] Consolidation also benefits the health system by expanding the range of services that organizations offer their patients and by fostering an environment in which information may be shared easily among providers, e.g., through the utilization of electronic health records.[8] With these advancements, health systems are able to minimize duplicative testing and increase efficiency, resulting in decreased costs for both providers and patients over the long term.

Because of its anticipated benefits, consolidation is occurring across various sectors of the healthcare industry, including post-acute care. [9] The post-acute care sector includes situations in which providers render services at locations other than acute-care hospitals, such as *long-term acute care hospitals* (LTACH), rehabilitation facilities, skilled nursing facilities, and home care.[10]

In May 2014, Kindred Healthcare, the biggest post-acute care provider in the U.S.,[11] presented Gentiva Health Services, a provider of home health and hospice services, with a buyout offer, in hopes of: (1) decreasing its system's emphasis on skilled nursing; and, (2) creating a community focused on providing their patients with a wide range of post-acute care services.[12] Gentiva's board of directors rejected the original takeover proposal, in fear that it undervalued Gentiva's growth potential. Kindred attempted to negotiate the offer with Gentiva, but Gentiva elected to remain independent.[13]

Now, executives at Kindred have expressed concerns that Gentiva may present a buyout offer to Amedisys Inc., another leading home health and hospice care organization,[14] which is having difficulties generating a profit.[15] Kindred executives believe that members of Gentiva will be "*disenfranchis[ing] its shareholders through a value-destroying and highly levered transaction*" if they choose to consolidate with Amedisys. Although Gentiva has rejected Kindred's last two buyout offers, executives at Kindred have reported that they are prepared to raise or withdraw their buyout offer for Gentiva, depending on Gentiva's next course of action.[16]

Kindred's offers to Gentiva, and Gentiva's possible offer to Amedisys, seem to indicate that organizations across various healthcare sectors are attempting to capitalize on the benefits of consolidation. These offers also represent the first merger and acquisition proposals in the post-acute care industry, a sector that healthcare analysts consider "*ripe for consolidation*".[17]

Kindred is one of many organizations that have attempted to consolidate with other healthcare enterprises. In 2012, 3,100 of the 5,723 hospitals in the U.S. were owned by health systems, and the number is expected to continue increasing.[18] Many healthcare executives believe that the independent hospitals are decreasing in prevalence due to: (1) regulatory changes causing a decrease in *reimbursement rates*; (2) difficulties accessing *capital goods*; and, (3) an inability to provide a *continuum of care*.[19] These factors, all of which are addressed through the most recent iteration of healthcare reform, are motivating healthcare organizations to consider consolidation.[20]

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As healthcare organizations continue to consolidate, stakeholders will be impacted in various ways. Consumers may have less choice in the healthcare organizations from which they receive specialty care, as consolidation results in decreased competition in the market.[21] Consumers may also be faced with higher prices, because reimbursement in outpatient departments (within and outside of the hospital) is higher than in independent physician offices.[22] This difference in reimbursement may push organizations to acquire more physician practices and consider them outpatient departments, which will allow the health systems to charge higher prices.[23] Health systems may be wary of potential competition from organizations in which primary care may be provided at lower costs, e.g., drugstores.[24] If the number of acute care providers increases, health systems may be incentivized to find ways to lower prices for services and improve their internal cost structure.[25]

Healthcare industry consolidation is a trend that appears to be continuing. By joining with, or acquiring, other healthcare organizations, hospitals create health systems, which increases access to services than those patients would have had with independent hospitals. Internally, healthcare organizations are often able to run more efficiently and reduce administrative costs. If health systems are able to control prices while providing high quality care, consolidation may have a positive effect on the industry and may accomplish goals established by the ACA.

The next installment of this three-part series will address a potential solution to the current pressures on the healthcare industry – hospitals and health systems becoming insurance providers; and, the third installment will discuss provider concentration and the ways in which antitrust regulations impact healthcare consolidation.

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