AMWINS

Healthcare Firms Confront 'Perfect Storm' of Post-Pandemic Liability Issues

The healthcare management liability market is experiencing rapid growth, fueled by rising healthcare expenditures and higher employee wages. **Health Affairs reports** that healthcare spending hit $4.5 trillion in 2022 and is projected to continue its upward trend annually. Additionally, the depletion of COVID-19 funds and inflationary pressures have led to a surge in directors and officers liability (D&O) and employment practices liability (EPL) claims, even in states that usually see lower activity in these areas.

With significant changes on the horizon, what underlying issues and factors in the healthcare management liability market are causing concern for professionals? What developments can insurers expect in this evolving sector in the coming years?

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Private equity in healthcare

These changes and challenges present a unique opportunity for private equity firms to invest in the healthcare industry. In 2020, the CARES Act was passed – Coronavirus Aid, Relief and Economic Security Act. One of the act's most important provisions was the Provider Relief Fund.

The stimulus money, distributed by the Centers for Medicare and Medicaid Services, had two purposes. First, to provide additional money to cover COVID-19-related expenses. At the time, hospitals and health systems were incurring the cost of PPE, such as masks, gloves and respirators. Second, to cover lost revenue from elective services. For example, plastic surgery procedures were no longer available, causing a drop in revenue and a decrease in patient volume.

Post CARES Act, hospitals and other healthcare providers experienced financial difficulties due to the lack of ongoing financial support from the federal government. These challenges included higher operating expenses due to increased wages and benefits, as well as rising inflation caused by higher interest rates, making it more costly to borrow money. Additionally, there was a decline in investment income, which healthcare providers relied on to support their operations and compensate for decreases in net profits.

The largest expenses for most hospitals are salaries and the benefits they provide to their staff. While some hospitals have great credit and could take out loans, with interest rates increasing, additional debt costs them a lot more. And after stimulus money disappeared, the expenses still remained. Hospitals couldn't borrow any more money, there was no relief fund to tap into, and any investment income was dwindling.

Private equity firms see healthcare as an industry with significant opportunities for growth and profitability, driven by the need for innovation, expansion and tech-enabled healthcare delivery. This interest has been heightened by the financial struggles hospitals have faced post-COVID, despite temporary relief from the CARES Act's Provider Relief Fund. With rising operating costs, inflation and a decline in investment income, many hospitals find it difficult to sustain operations without external financial support. As a result, private equity investors have stepped in, offering capital to help healthcare providers expand, modernize and improve patient care, filling the gap left by dwindling government aid.

Private equity firms have ample capital to invest in healthcare companies and they see the potential in expanding operations, updating technology and improving patient care. Their significant financial resources can be used to support a healthcare company's growth and enhance its services.

The down-side of private equity in healthcare

According to **NBC research**, over **40%** of American hospital emergency departments are overseen by for-profit healthcare staffing companies owned by private equity firms. The draw is there for employees, too, with research from the **Physicians Advocacy Institute** finding that nearly **80%** of physicians now work for hospitals or other corporate entities while private practices continue to dwindle.

In the future, the FTC is likely to conduct thorough investigations and audits, particularly for mergers and acquisitions. The Biden administration's 2021 executive order on promoting competition targets anticompetitive behavior, particularly in the healthcare industry, where a small number of large systems dominate the market. The order encourages the Federal Trade Commission (FTC) and the Department of Justice to enforce antitrust laws, scrutinize mergers and limit practices like non-compete agreements that restrict employee mobility. In the future, the FTC is likely to conduct detailed investigations and audits, focusing on mergers and acquisitions, while healthcare organizations may face audits from the Centers for Medicare and Medicaid Services for compliance and financial misuse. This increased oversight could lead to significant consequences for healthcare providers, including fines for noncompliance.

Private equity investments **could negatively impact** the healthcare industry. Some PE firms might prioritize profit over the quality of patient care. They are more likely to cut costs by reducing staff, replacing physicians with fewer experienced nurse practitioners or physician assistants, or reducing services altogether to increase profits. PE firms invest in various industries, and if they are not familiar with the healthcare industry and the regulatory environment, it can lead to compliance violations, which may lead to more in-depth investigations and, ultimately, costly fines.

High salaries bring high social inflation

Apart from PE firms' role in the healthcare system, another issue insurers are grappling with right now is the impact of high salaries and rising litigation costs.

According to **AMGA**, there has been an overall increase in compensation for medical professionals of **5.3%** in 2024 compared to just **0.1%** in 2021. All industries within the medical field are seeing a rise in total compensation numbers.

When underwriters handle a claim related to a high earner like a CEO, CFO, any C-suite executive or a physician, it's highly probable that the costs of settling these claims will be significantly higher. For example, an insured works with an anesthesiology practice for surgeries. A dispute rises between the hospital's CEO and an anesthesiologist over patient care. Despite ongoing disagreements, the CEO pressured the anesthesiology group to remove the doctor from the hospital. Due to limited opportunities at other facilities, the anesthesiologist's income decreased, which he attributed to the CEO's actions. After complaining to the practice leader, his contract was terminated. He then filed a lawsuit alleging breach of employment agreement and retaliation for reporting patient safety concerns, as well as tortious interference with prospective business opportunities against the hospital and CEO. The D&O insurance coverage defended the hospital, incurring $400,000 in legal expenses, and settled the case for $2 million before the summary judgment motions were heard. To account for this, higher retentions are being emphasized. This is because it's recognized that nuclear verdicts usually don't involve frontline workers.

For those employees, lower deductibles or retentions may be applied. However, it is recognized that higher retentions are needed for individuals in specialized roles with higher salaries and the marketplace seems to be aligning with this need.

Staffing shortages impact more than just care

Due to the impact of COVID-19 on the healthcare workforce, we have noticed the significant effects these challenges have on healthcare workers, particularly in relation to stress.

For many healthcare staff, burnout is very real, which is another challenge and expense for hospital systems. While providing patient care, the healthcare industry didn't anticipate the support their employees would need due to increased patient volumes and longer work hours, leaving many feeling overworked and undervalued. The good news is many hospitals have made efforts to improve employee assistance programs [EAPs] for their employees by offering online behavioral mental health support. Staffing shortages, especially among nurses, have worsened due to the pandemic. Hospitals had to hire contract nurses to address the shortages. Many nurses left their facilities to join staffing agencies for better pay. Salaries have remained high because employers want to retain good employees and have been unable to reduce salaries since the onset of COVID-19.

To combat these staffing issues, hospitals are getting creative with their recruitment strategies. The healthcare industry is having a tough time in recent years attracting a younger generation of employees. Hospitals are reaching out to local high schools and universities, offering internships and even helping to finance a portion of their schooling as a recruitment strategy.

Takeaway

The healthcare management liability market is worried about the increasing presence of private equity firms in the industry, attracted by opportunities for profitability despite regulatory scrutiny and potential impacts on patient care quality. With all of these new issues emerging in the field, underwriters are adapting quickly with new strategies and market dynamics for the healthcare sector.

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You can **learn more about our healthcare management liability program** here.

Insight provided by:

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