



The National

CONSUMER VOICE

_____ for Quality Long-Term Care

Hidden Profits in the Nursing Home Industry

April 10, 2024

About the Consumer Voice

The leading national voice representing consumers in issues related to long-term care

- ▶ **Advocate for public policies** that support quality of care and quality of life responsive to consumers' needs in all long-term care settings.
- ▶ **Empower and educate** consumers and families with the knowledge and tools they need to advocate for themselves.
- ▶ **Train and support** individuals and groups that empower and advocate for consumers of long-term care.
- ▶ **Promote the critical role** of direct-care workers and best practices in quality care delivery.

Welcome

- ▶ The program is being **recorded**
- ▶ Use the **Q&A feature** for questions for the speakers
- ▶ Use the **chat feature** to submit comments or respond to questions from speakers or other attendees
- ▶ Please complete the **evaluation** questionnaire when the webinar is over.
- ▶ Links to **resources** will be posted in the chat box and will be posted to the Consumer Voice website – theconsumervoice.org

Related Party Transactions and CMS's Role in Regulation

What are related parties?

In 2003, an article published in the Journal of Health Law suggested that nursing homes should undergo corporate restructuring to help avoid civil liability for negligent care.¹ The article suggested that by creating separate, single-purpose corporations, owners and operators could protect assets that would otherwise be subject to civil judgment. The article's chief recommendation was that owners separate the operational side of the nursing home from the real estate side. The article stated:

"There is an emphasis on separating the ownership of the real estate from the ownership of the operating entity that holds the license and Medicare and Medicaid provider agreements. This is normally achieved by having the operating entity lease the facility from the real property entity. This can be accomplished even where there is identical ownership and control between and among the real-property entity and the operating entity."

Not mentioned in the article was an additional benefit to owners: they could use the corporation that owned the real estate (which they own) to charge unrestricted rent and lease fees to the nursing home (which they also own). Essentially, owners began charging themselves to rent their own facility through related party transactions.

Since the publication of this article, this practice has proliferated, with some estimating that 75% of nursing homes engage in related party transactions.² However, the practice has evolved to include not only real estate but almost every aspect of nursing home operations. It is now common for nursing homes to have several related party organizations with which they do business, for instance, management companies, physical therapy companies, staffing companies, and others. This practice can often translate into millions of dollars in payments by a single nursing home to companies that are in fact owned by the owners of the facility. For instance, Life Care, a nursing home chain with over 200 nursing homes and 25,000 beds, in 2018 reported over 260 separate related party expenses on its Medicare cost reports. These related parties include management companies, staffing companies, insurance companies, therapy companies and many more. Over the three-year period from 2018 to 2020, Life Care reported \$1.25 billion dollars in payments to related parties (to themselves).³

- ▶ Related party companies are companies that do business with a nursing home and are related to the nursing home through common ownership or control.
- ▶ Protect from liability and can also be used to disguise profits.
- ▶ Related parties make nursing homes look less profitable, while a closer look reveals that profits may be hidden in these transactions.
- ▶ Cost reports do not capture enough information for CMS to fulfill its regulatory obligation of ensuring taxpayer dollars are spent on care.
- ▶ https://theconsumervoice.org/uploads/files/issues/Related_Party_Transactions_CMS_Role_in_Regs.pdf

WHERE DO THE BILLIONS OF DOLLARS GO?

A LOOK AT NURSING HOME RELATED PARTY TRANSACTIONS

- ▶ Despite billions of dollars funneled through related party companies each year, there appears to be little to no scrutiny by the federal government on how this money is spent.
- ▶ Life Care Centers paid related parties over \$1.2 billion dollars from 2018-2020.
- ▶ Roughly 75% of for profit homes use related parties.
- ▶ Even non-profits use them, particularly large non-profits.
- ▶ <https://theconsumervoice.org/uploads/files/issues/2023-Related-Party-Report.pdf>

Speakers



Ashvin Gandhi, PhD

Assistant Professor
UCLA, Anderson School of
Management



Andrew Olenski, PhD

Assistant Professor of Economics
Lehigh University, College of
Business

Tunneling and Hidden Profits in Healthcare

Ashvin Gandhi (UCLA & NBER)

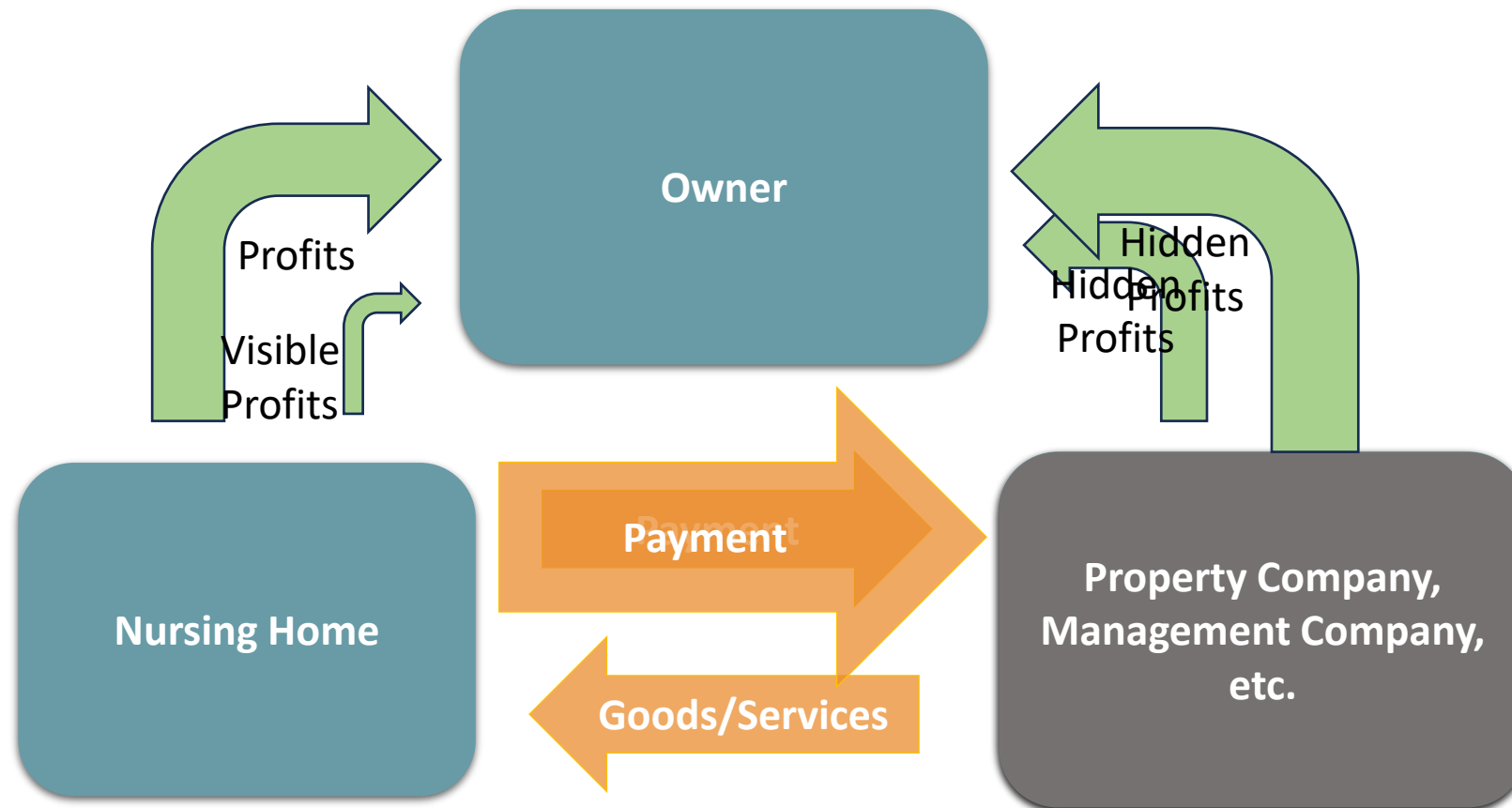
Andrew Olenski (Lehigh)



About us



Hiding Profits through Related Party Transactions



What's a Fair Price to Pay a Related Party?

One Approach: Use the related party's costs.

- Very nice in theory. But do we believe related party's reported costs

Another Extreme: Assume all related party payments are tunneling.

- Probably unfair. (Unless the goal is to stop related party transactions.)

Our Approach: Study cases where the facility *switched* to using a related party.

- Great for statistics, bad for policy implementation.
- 

Key Assumption for Our Approach

The “true cost” of the good/service doesn’t meaningfully change right when the facility starts using a related party.

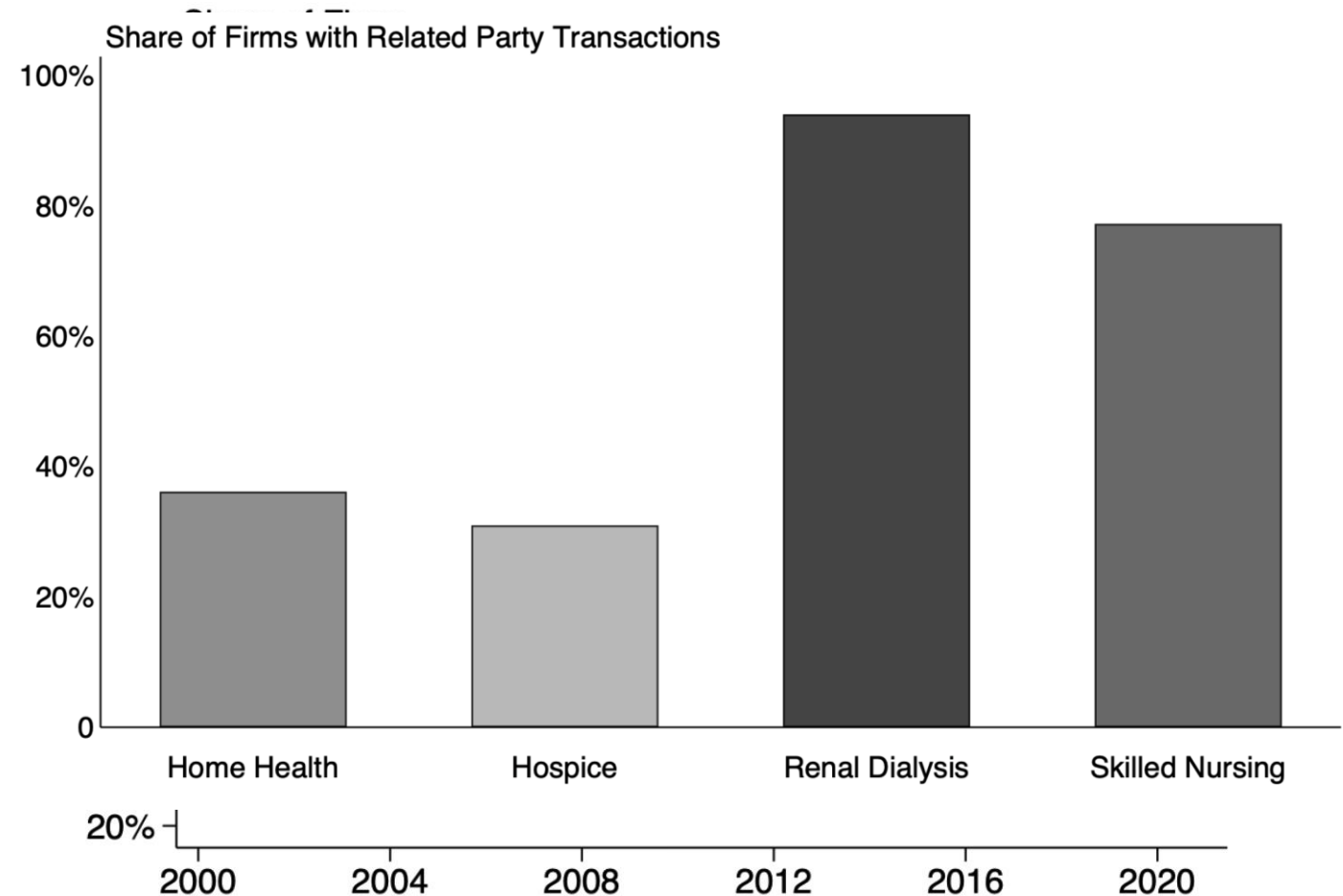
- Same land & buildings, same management team, etc.

Standard statistical methods deal nicely with other issues.

Our Setting

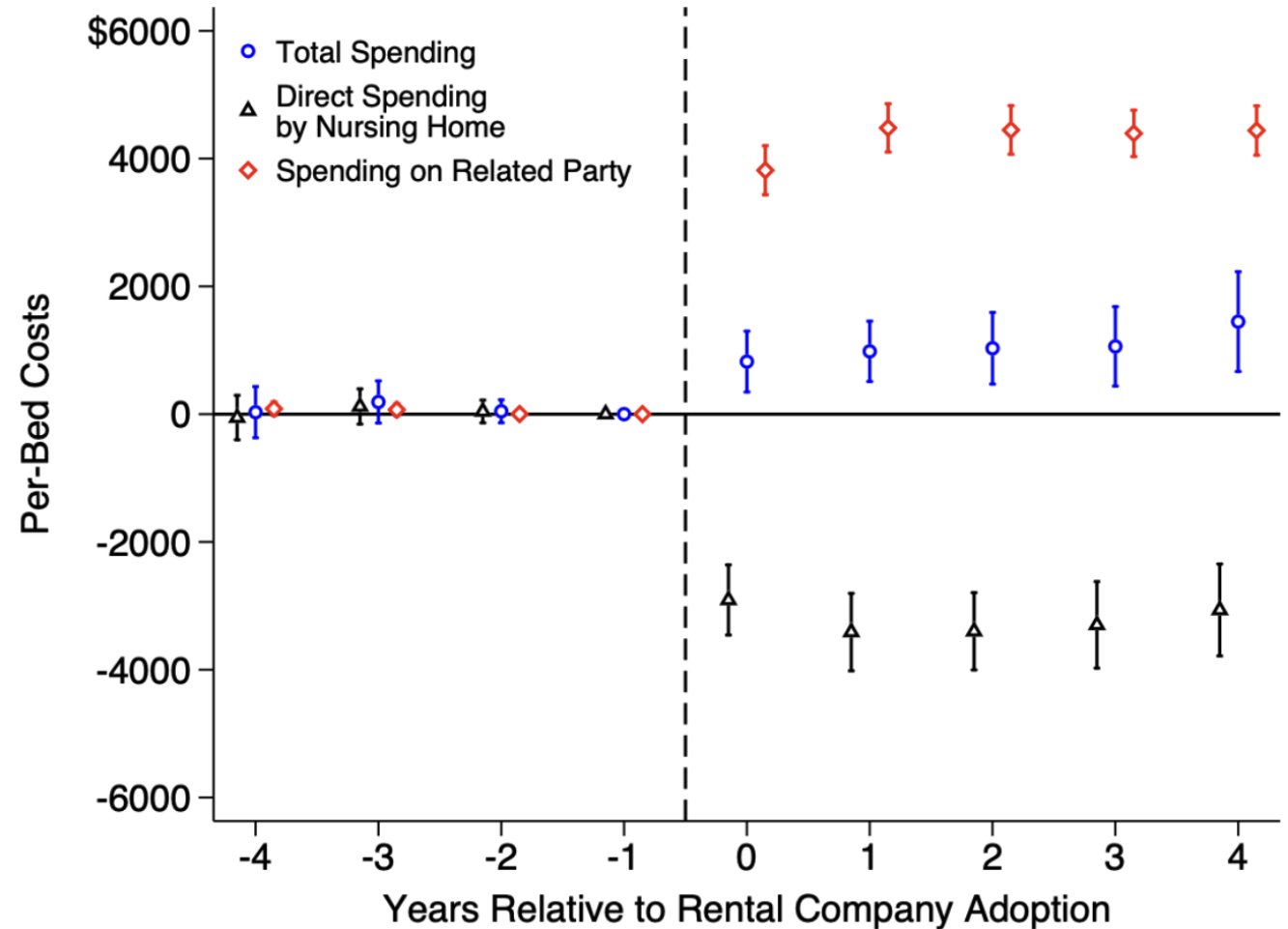
- Nursing homes, where related parties are fairly common.
- Study Illinois, where data are particularly good.
- There's a lot of related party adoption over time.
- Focus primarily on real estate and management, where most of the action is.

(a) Share of Firms Reporting a Related Party Payment



What Happens When You Start Renting from a Related Party?

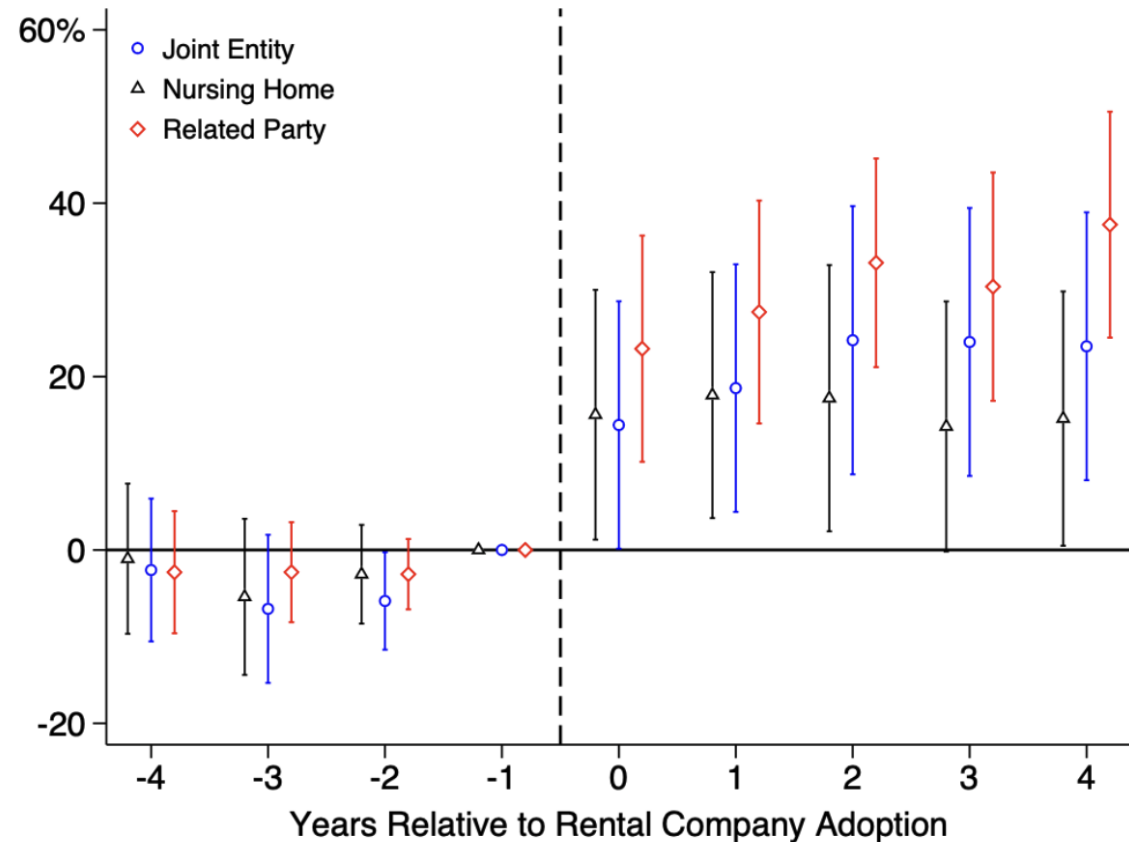
- Stop paying directly for real estate (mortgage, taxes, etc.).
- Pay rent to a related party.
- The amount you pay in rent is greater than the direct cost of ownership. **This gap represents hidden profits.**



Could This be a Fair Transaction?

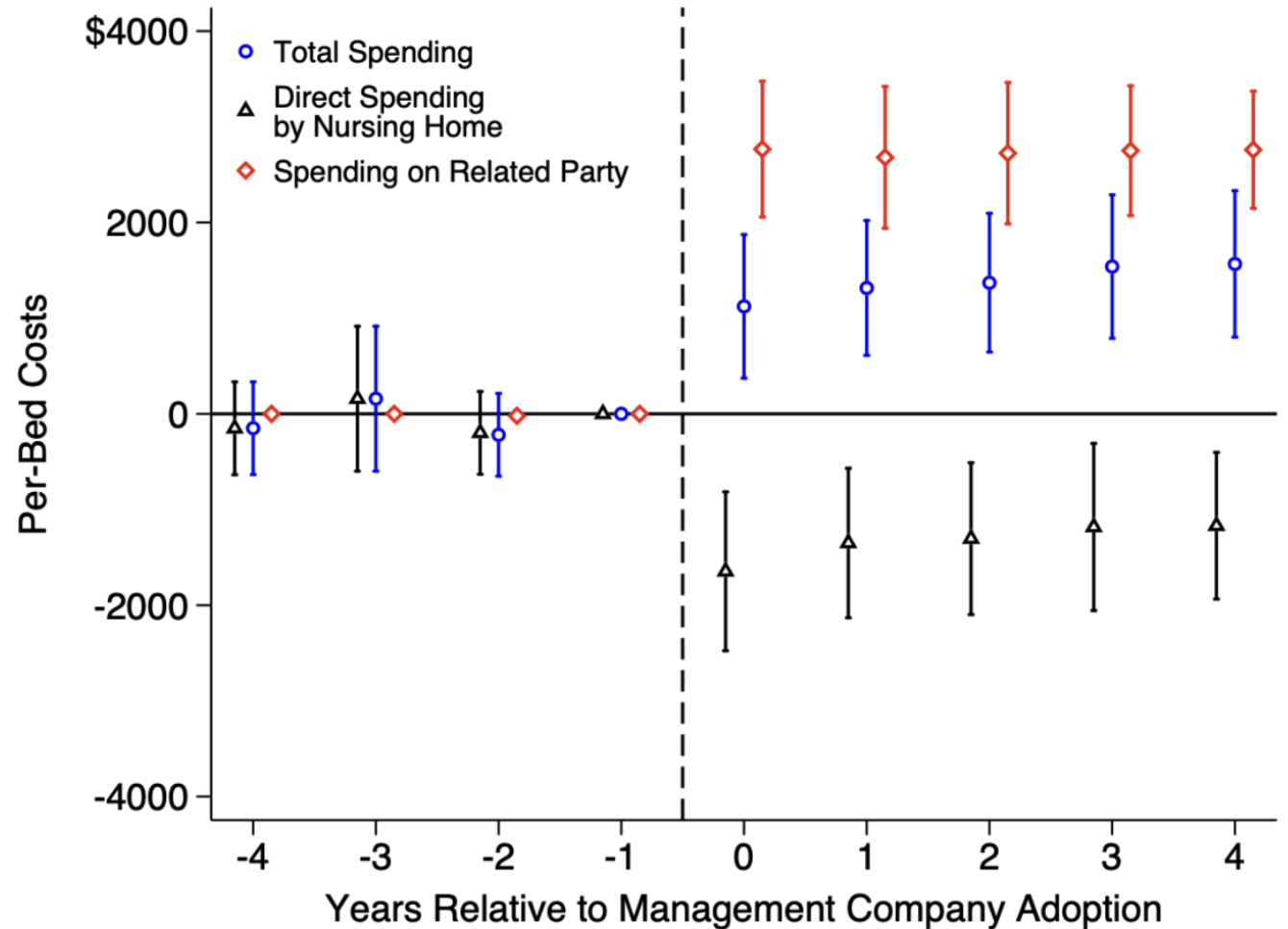
- Could still be OK if nursing home is receiving compensation.
- But nursing home assets decrease!
- This isn't just paying off debts.
- The “book equity” decreases often to the point of being negative!
- Hard to rationalize except as an accounting trick.

(d) Probability of Reporting Negative Equity



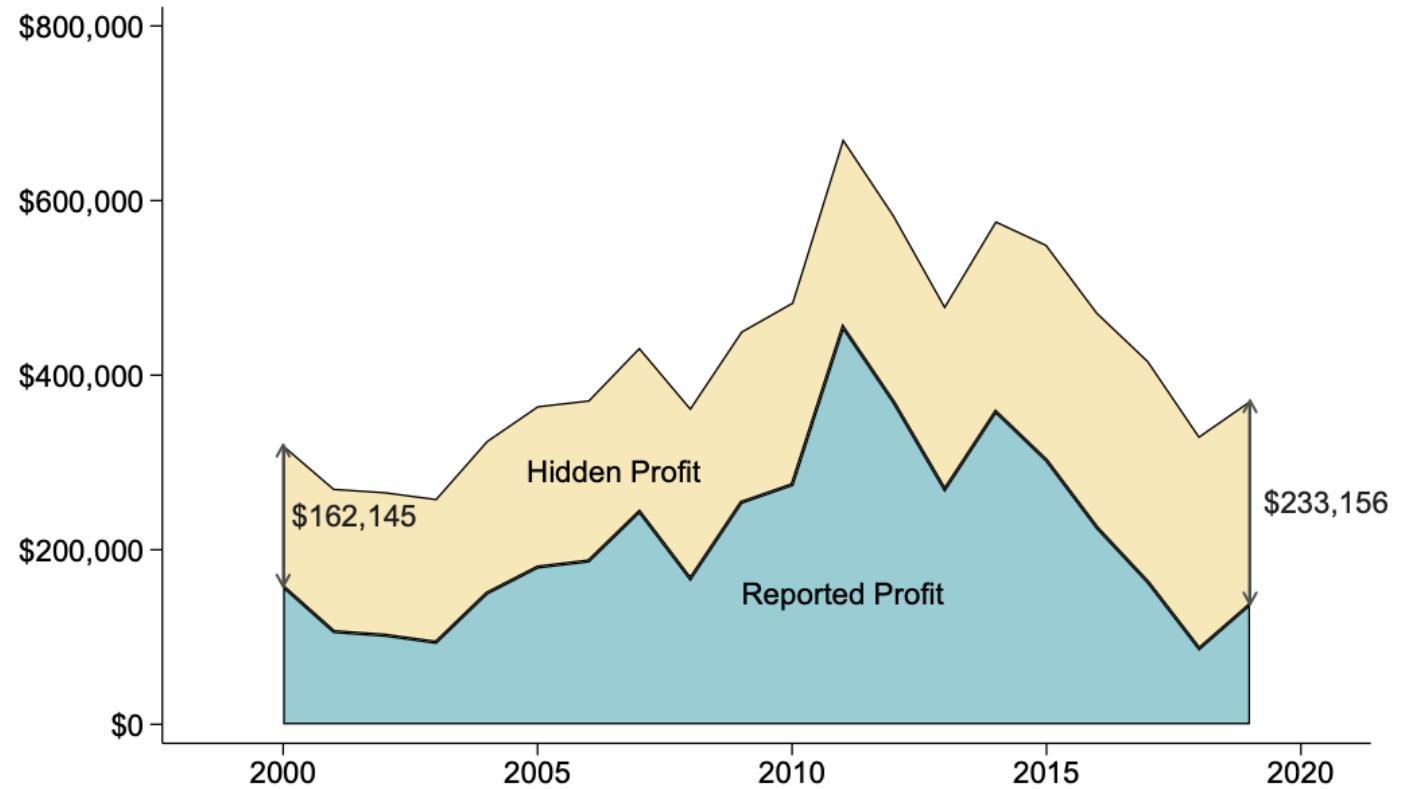
The Same
Holds for
Management

(b) Decomposition of Management Costs



How Much Profit is Being Hidden?

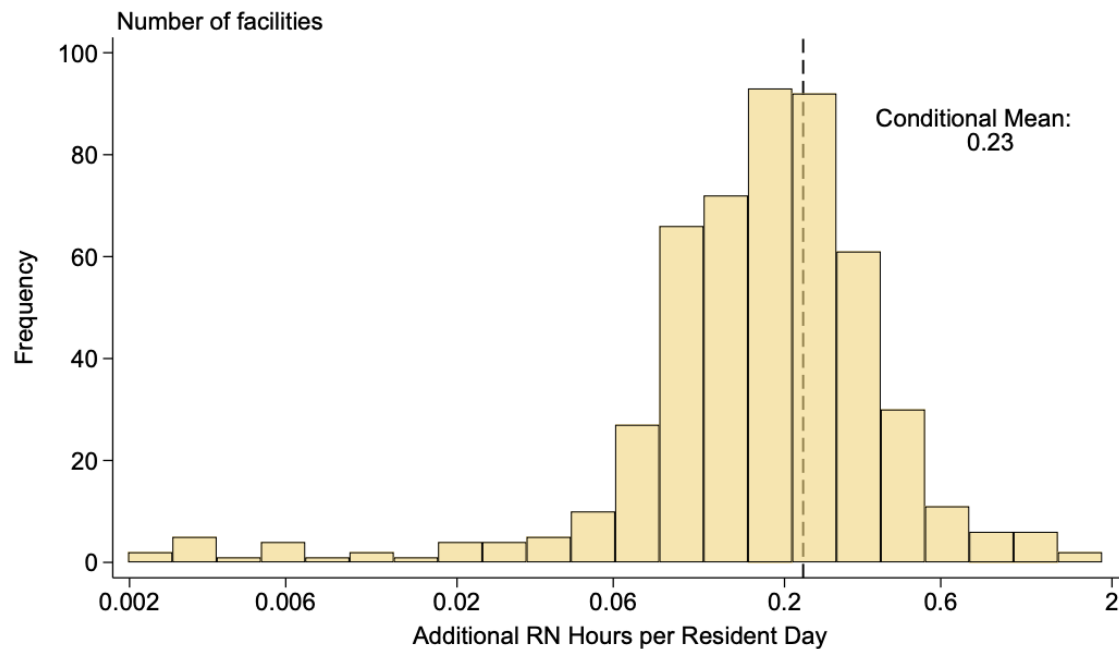
(b) Evolution of Hidden and Reported Profits



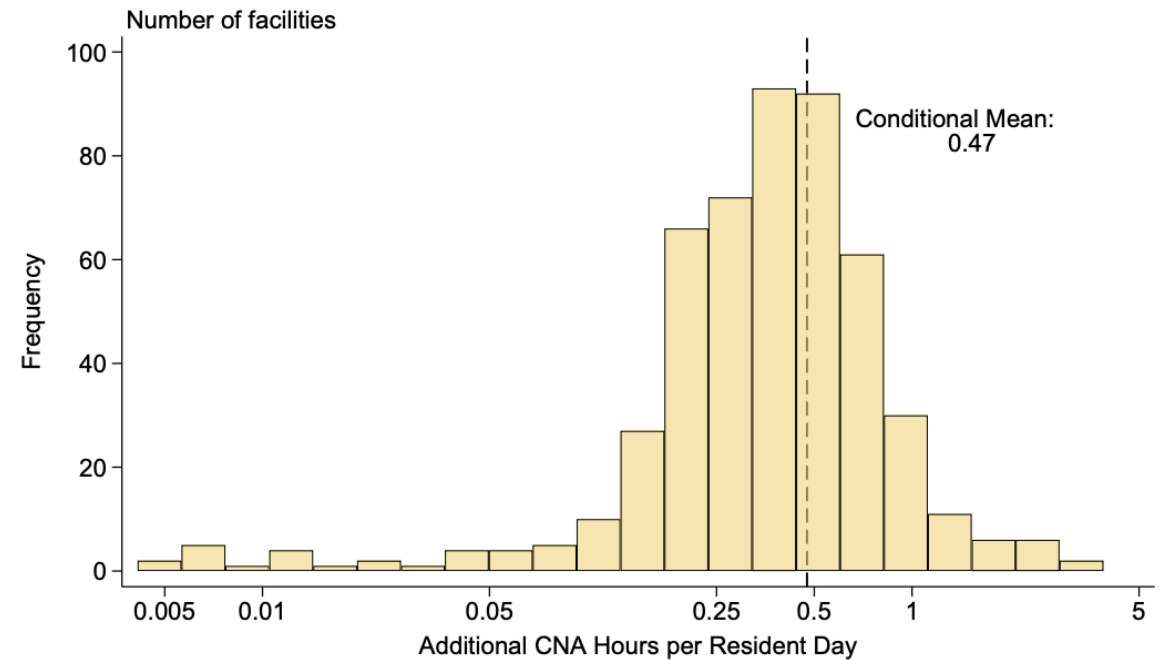
How Much Money Is That?



(a) Distribution of Additional RN Hours



(b) Distribution of Additional CNA Hours





Our Takeaways

Research Finding: There are a lot of hidden profits!

- If anything we suspect we may be underestimating.

Policy/Regulatory Takeaway: We need much better data.

- Audited cost reports. (Audits can be rare and focus on high-risk areas.)
- Full financial accounting for all related parties.
- Require review for certain transactions (e.g. related party sale leaseback).



Thank you!

- Ashvin Gandhi (UCLA & NBER)
 - ashvin.gandhi@anderson.ucla.edu
 - Twitter: @ashdgandhi
- Andrew Olenski (Lehigh)
 - ano223@lehigh.edu
 - Twitter: @andrewolenski



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