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Governor Newsom Embraces Tighter Requirements on Private Equity and Hedge Fund Investments in California Health Care By Signing AB 1415 and SB 351

This month, Governor Newsom signed AB 1415 and SB 351 into law, two bills that will enhance the requirements on investments by private equity groups and hedge funds in California health care. As detailed below, AB 1415 will significantly expand the reach of the Office of Health Care Affordability (OHCA), and SB 351 further codifies restrictions on the role that private equity groups and hedge funds can play in the management of medical and dental practices. Both bills will go into effect on January 1, 2026.

Collectively, these measures add to the burdens and scrutiny faced by private equity and hedge funds that invest in the health care sector, although other health care stakeholders may feel the ripple effects as well. Many stakeholders may need to revisit their ownership and contracting structures — especially those involving management services organizations (MSOs) — to evaluate whether they could fall within OHCA's expanded review authority or implicate SB 351's new restrictions.

Where the Legislation Lands — and Where It Leaves Uncertainty

While the final text of AB 1415 and SB 351 resolves some open questions, much will depend on how regulators implement and enforce the new requirements. Key areas of uncertainty include:

- **More transactions will trigger OHCA review.** AB 1415 expands the parties and scope of transactions subject to OHCA's review process, including MSOs, private equity groups, hedge funds and related affiliates. However, the law leaves many points unclear that must be clarified through further regulation — like defining which transactions with MSOs require notice and setting revenue and materiality thresholds.
- **MSO scope remains unclear.** AB 1415's definition of MSO could be interpreted broadly to include businesses that manage specific aspects of health care practices that are not generally considered health care MSOs, like payroll administrators, accountants, or even software-as-a-service (SAAS) providers. OHCA will need to further define the types of entities that constitute MSOs effected by the notice requirements.

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- **Reporting burdens are coming, but not yet specified.** AB 1415 empowers OHCA to establish requirements "as necessary to carry out the functions of the office." Current regulations generally focus on requiring payor and provider information. But through AB 1415, OHCA may require specific information unique to private equity groups and hedge funds — potentially including their organizational structure, investors, other portfolio companies and financial performance. Similarly, as OHCA is empowered to analyze cost trends, develop policies for lowering health care costs, create strategies for controlling the cost of health care and enforce cost targets, OHCA appears to have broad leeway for the type of information it could require MSOs to report and which MSOs would be subject to such reporting requirements. Without reasonable and tailored regulations and guidance narrowly defining MSOs for OHCA reporting and filing requirements, OHCA may be inundated with more submissions than was intended — and that it can handle. Many health care investors and stakeholders may also face significant filing and reporting burdens that may deter investment and that may not materially serve the purposes of OHCA.
- **SB 351 codifies and sharpens CPOM enforcement.** SB 351 largely reflects existing guidance from the Medical Board of California (MBC) and opinions issued by the California Attorney General's office on the corporate practice of medicine (CPOM). But as detailed below, it codifies them with more precision. However, the passage of both SB 351 and AB 1415 — plus recent prior related legislative efforts — may mean the California health care sector will experience increased litigation or government enforcement actions based on alleged violations of CPOM or other restrictions, particularly when private equity or hedge funds are involved.

Preparing for Compliance and Regulatory Clarity

For now, members of the California health care industry should keep close watch on any regulatory developments from OHCA as it begins to implement AB 1415 and evaluate their current contractual and ownership relationships with private equity groups, hedge funds and MSOs — with a particular focus on transactions that may be subject to notice requirements when the law goes into effect. All health care providers and stakeholders, especially private equity groups and hedge funds, should also evaluate MSO and related contracts with medical and dental practices to ensure that they comply with the restrictions set forth in SB 351.

Statutory Summary: AB 1415 and SB 351

The following sections provide a deeper look at the new statutory requirements, including updated definitions, notice triggers, and operational restrictions introduced by the two laws.

AB 1415:

- A "noticing entity" must provide OHCA with notice of certain transactions between the noticing entity and a health care entity or MSO, or an entity that owns or controls the health care entity or MSO. Transactions requiring notice include transactions that: (1) sell, transfer, lease, exchange, option, encumber, convey, or otherwise dispose of a material amount of the health care entity's or MSO's assets to one or more entities; or (2) transfer control, responsibility, or governance of a material amount of the assets or operations of the health care entity or MSO to one or more entities. In addition, MSOs must notify OHCA of any agreement or transaction described in (1) and (2) above between the MSO and any other entity.
- "Noticing entity" includes (1) a private equity group or hedge fund; (2) a newly created business entity created for the purpose of entering into agreements or transactions with a health care entity; (3) an MSO; and (4) an entity that owns, operates, or controls a provider, regardless of whether the provider is currently operating,

providing health care services, or has a pending or suspended license.

- OHCA shall establish requirements for MSOs to submit data and other information "as necessary to carry out the functions of [OHCA]."
- "Management services organization" is defined as an entity that provides management and administrative support services for a provider (as that term is defined under applicable law) in support of the delivery of health care services, excluding the direct provision of health services. Management and administrative support services shall include provider rate negotiation, revenue cycle management, or both. A management services organization does not include entities that own one or more health facilities, as defined in subdivision (a) or (b) of Section 1250 of the California Health and Safety Code.
- "Hedge fund" is defined as a pool of funds managed by investors for the purpose of earning a return on those funds, regardless of the strategies used to manage the funds, and include, but are not limited to, a pool of funds managed or controlled by private limited partnerships or other types of private corporate or partnership formations. The definition of "hedge fund" does not include the passive investors or lenders to a hedge fund.
- "Private equity group" is defined as an investor or group of investors who primarily engage in the raising or returning of capital and who invest, develop, dispose of, or purchase any equity interest in assets, either as a parent company or through another entity the investor or investors completely or partially own or control. The definition of "private equity group" does not include its passive investors.

SB 351:

- A private equity group or hedge fund may not do either of the following with respect to a physician or dental practice:
    - (1) Interfere with the professional judgment of physicians or dentists in making health care decisions, including: (A) determining what diagnostic tests are appropriate for a particular condition; (B) determining the need for referrals to, or consultation with, another physician, dentist, or licensed health professional; (C) being responsible for the ultimate overall care of the patient, including treatment options available to the patient; and (D) determining how many patients a physician or dentist shall see in a given period of time or how many hours a physician or dentist shall work.
    - (2) Exercise control over, or be delegated the power to do, any of the following: (A) owning or otherwise determining the content of patient medical records; (B) selecting, hiring, or firing physicians, dentists, allied health staff, and medical assistants based, in whole or in part, on clinical competency or proficiency; (C) setting the parameters under which a physician, dentist, or physician or dental practice shall enter into contractual relationships with third-party payers; (D) setting the clinical competency or proficiency parameters under which a physician or dentist shall enter into contractual relationships with other physicians or dentists for the delivery of care; (E) making decisions regarding the coding and billing of procedures for patient care services; and (F) approving the selection of medical equipment and medical supplies for the physician or dental practice.
- Importantly, unlicensed persons or entities, including private equity groups and hedge funds, will continue to be allowed to assist or consult with a physician or dental practice with respect to the decisions and activities described immediately above, provided that the physician or dentist retains the ultimate responsibility for, or approval of, those decisions and activities.
- A private equity group, hedge fund, or an entity controlled by a private equity group or hedge fund may not contract with a physician or dental practice in a way that would enable the unlicensed entity to interfere with the professional judgment of the

physicians or dentists in making health care decisions. Such contracts would be void, unenforceable and against public policy.

- Any contracts involving the management of physician or dental practices, or the sale of real estate or assets owned by a physician or dental practice to a private equity group, hedge fund, or entity controlled by a private equity group or hedge fund may not contain: (1) noncompete clauses that bars any provider from competing with the practice in the event of their termination or resignation or (2) non-disparagement clauses that bar commentary on the practice in relation to issues involving quality of care, utilization of care, ethical or professional challenges in the practice of medicine or dentistry, or revenue-increasing strategies employed by the private equity group or hedge fund. However, a noncompete agreement related to the sale of a business and confidentiality agreements protecting material nonpublic information will remain permissible, so long as such confidentiality agreements do not prohibit the disclosure of information required by law or prohibit disclosures otherwise prohibited by SB 351, as described immediately above.
- SB 351's definitions of hedge fund and private equity group are nearly identical to their definitions in AB 1415, where "Hedge fund" is defined as a pool of funds managed by investors for the purpose of earning a return on those funds, regardless of the strategies used to manage the funds, and include, but are not limited to, a pool of funds managed or controlled by private limited partnerships. "Private equity group" is defined as an investor or group of investors who primarily engage in the raising or returning of capital and who invests, develops, or disposes of specified assets. The definitions of "hedge fund" and "private equity group" exclude passive investors and lenders, as well as hospital or hospital systems that own one or more licensed hospitals, affiliates of a hospital or hospital system, any entity managed or controlled by a hospital or hospital system, and public agencies.
- The California Attorney General would be entitled to seek injunctive relief or other equitable remedies to enforce the prohibitions under SB 351, plus recovery of costs and attorneys' fees.