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Partner Insight Series:

The Rural Healthcare Crisis

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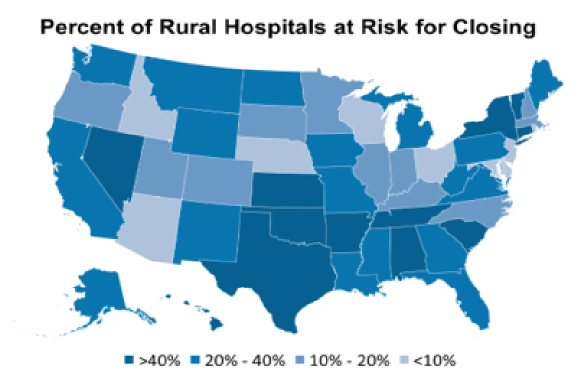
Why are Rural Health Systems Closing and What Can be Done to Ensure Access to Care?

Rural hospitals are an essential component of the healthcare system in rural communities, providing vital medical services to over 60 million Americans. However, in recent years, many rural hospitals across the U.S. have been facing financial difficulties, resulting in a significant number of closures. The closure of rural hospitals can have severe consequences for the surrounding communities, leaving residents with limited access to medical care and resulting in longer travel times to receive necessary treatments. Additionally, the loss of these hospitals can have an adverse impact on the local economy, as many hospitals are major employers in rural areas. There are many factors contributing to the closure of rural hospitals, including declining populations, inadequate reimbursement rates, and rising operational costs. Addressing these challenges will be critical in ensuring that rural communities have access to the healthcare services they need to lead healthy lives.

The Problem

Over the past decade, rural hospitals have become increasingly at risk for financial crises leading to closure. The Chartis Group, a healthcare advisory firm, recently released a study that found nearly 51% of rural hospitals have a negative operating margin. Recent reports commissioned by the Alabama Hospital Association and the Texas Hospital Association paint a similar picture. Half of the rural hospitals in Alabama ended 2022 with negative operating margins, up from 22% in 2019. In Texas, 26% of rural hospitals are at risk of closure as compared to 5% of urban hospitals.

According to the Chartis Group report, the financial problems plaguing rural hospitals are leading many facilities to cut back on services provided, including obstetrics. Between 2005 and 2019, more than 150 rural hospitals closed their doors and about 30% of rural hospitals in America are in danger of closing due to persistent financial losses, low reserves, and rising expenses. A report by the Center for Healthcare Quality and Payment Reform indicates that seventeen states have more than 30% of their rural hospitals at risk of closing as of January 2023.



Derived from information presented in "Rural Hospitals at Risk of Closing." Center for Healthcare Quality and Payment Reform. Data current as of January 2023.

Several factors influence rural hospital closures, including:

1. Financial challenges faced by rural hospitals, including lower patient volume compared to urban hospitals as well as a higher proportion of patients who are either uninsured or covered by governmental insurers. This leads to a lower reimbursement on average, as Medicare and Medicaid generally reimburse lower than commercial payers.
2. Shortages in hiring and challenges retaining healthcare professionals, particularly doctors and nurses. To compete with urban hospitals on the recruiting front, many rural hospitals

must provide higher compensation to those providers, even though the patient volumes and associated reimbursement may not fully support it. In a time where demand for nurses and doctors is already high, rural hospitals are experiencing increasing difficulty recruiting the staff necessary to meet the healthcare needs of the community.

Possible Solutions

Private Equity Investors

Private equity has become increasingly interested in investing in rural healthcare in recent years. According to a survey by the Private Equity Stakeholders Project (PESP), private equity firms own at least 130 rural hospitals today. Private equity firms see the potential for growth in the sector due to the lack of healthcare options available in rural areas, and they aim to fill that gap by providing capital for the expansion and improvement of rural healthcare facilities. Private equity firms may invest in a variety of healthcare services, such as telemedicine, urgent care clinics, or specialty hospitals, with the goal of providing better access to quality healthcare in rural communities. However, some critics argue that some private equity firms have a short-term focus that tries to achieve profitability by cutting costs too deeply or selling off long-term assets, all at the expense of quality patient care. Nonetheless, private equity investments in rural healthcare are expected to increase in the coming years as the demand for healthcare services in rural areas grows. In an industry desperately needing capital, private equity may be the best, and quickest, solution.

Rural Emergency Hospital Designation

Another possible solution is to convert to a Rural Emergency Hospital (REH). This designation was created by Congress in response to the recent increase in rural hospital closures and the resultant reduction of access to care that rural Americans now face. Providers that were enrolled as a critical access hospital (CAH) or rural hospital with 50 or fewer beds when the legislation was enacted on December 27, 2020, are eligible to convert to an REH if they meet certain criteria. REH facilities benefit from a monthly facility payment ($272,866 per month in 2023) and payment at 105% of the Outpatient Prospective Payment System (OPPS) rate for services that qualify as "REH services." Although financial stability is not guaranteed for hospitals that convert to a REH, it may be the best option for some communities. However, this new designation is not without its critics. Hospitals considering the redesignation must maintain 24-hour emergency services, but may not offer inpatient care. In addition, REH's are not able to participate in the 340B drug program, which provides access to pharmaceuticals at a reduced cost. Critics of the REH are concerned that these restrictions will create hardships for patients having to go outside of the local community for inpatient care, and also limit local access to vital drug intensive services due to increased drug costs.

Payment Reform

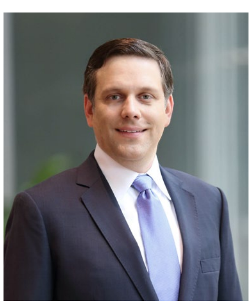
Is the payment system the problem? The Center for Healthcare Quality and Payment Reform (CHQPR) explains that although smaller rural hospitals may get paid less for services when compared to their urban counterparts, the payment system may be more to blame. CHQPR notes that primary care services that help patients stay healthy reduce the amount of emergency or high-acuity cases. This is good for patients, but decreases profitability for hospitals because high-acuity cases and surgeries tend to result in higher reimbursement. CPQHR has proposed a new payment system for rural hospitals that where these facilities would receive “Standby Capacity Payments” that are intended to cover a facility’s fixed operating costs (e.g., the fixed costs required to maintain an emergency department and other essential services.). Service-based fees would then be intended to cover variable costs incurred during the provision of direct patient care. CHQPR states that “a patient-centered approach to payment is designed to support the services that patients need, not to increase profits for either hospitals or health insurance plans,” and “since the payments are specifically designed to support both the fixed and variable costs of delivering services, the hospital would neither lose money when patients are healthier nor make excessive profits when patients need more services.”

Telehealth

Additional solutions for rural hospitals include the expansion of telehealth. While rural providers are losing the ability to staff full-time specialists, they may be able to provide specialist services via telehealth at a fraction of the cost. This may be adequate for some services like behavioral health; however, some specialty services (including obstetrical care) cannot simply be administered via telemedicine, even though capabilities continue to increase.

Final Thoughts

Success in rural hospitals requires balancing the needs of patients and providers within the severe financial constraints experienced today. Opportunities exist to solve these problems with capital and operating expertise provided by private equity, but long-term success ultimately depends on meeting the needs of patients and the community. Success will not only require innovation from private equity and others within the private sector, but will also require federal and state governments to address the Medicare and Medicaid reimbursement challenges.



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