

The Hollowed-Out American Nursing Home

Using Private Law to Police Poor Quality Care and Expand Owner Responsibilities

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21.1 INTRODUCTION

The United States has more than 26,000 nursing homes, caring for more than 1.4 million residents.¹ About 70 percent of nursing homes are now operated by for-profit corporations, 24 percent are not-for-profit, and 7 percent are government-owned, while 58 percent are operated by corporate chains.² Private equity firms own about 11 percent of nursing facilities nationwide. By 2050, up to 30 million people in the Americas will require long-term care services. Most of these nursing home residents are or will become exceptionally vulnerable, but the quality of their daily lives may well be shortchanged by their nursing home owners – particularly private equity (PE) owners. Nursing home care is an industry built on “market” solutions to end-of-life care for the elderly.³ The advent of Medicare and Medicaid was not based on a model of nonprofit nursing homes. As Leslie King writes: “[l]awmakers instead allowed the growth of a system of large, for-profit, chain nursing homes.”⁴ Early advocates of such privatization argued that a private ownership system could be more efficient – providing quality services at a lower cost.⁵ For-profit corporate

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¹ Abby McCain, 25 *Insightful Nursing Home Statistics* [2023]: Residents, Locations, and Long-Term Care, Zippia (Mar. 20, 2023), www.zippia.com/advice/nursing-home-statistics/.

² These Administrative Actions Would Improve Nursing Home Ownership and Financial Transparency in the Post COVID-19 Period, Health Affs. Blog (Feb. 11, 2021), <https://www.healthaffairs.org/content/forefront/these-administrative-actions-would-improve-nursing-home-ownership-and-financial>.

³ Leslie King, *How Government Created and Shaped the U.S. Nursing Home Industry*, 46 *Critical Socio.* 881, 897 (2020).

⁴ *Id.*

⁵ John B. Goodman & Gary W. Loveman, *Does Privatization Serve the Public Interest?*, Harv. Bus. Rev. (Nov.–Dec. 1991), <https://hbr.org/1991/11/does-privatization-serve-the-public-interest>.

entities would strive to maximize their bottom-line goals for shareholders, but the great engine of the “market” in an industrial economy would also deliver benefits for consumers.

The market, however, fails when PE ownership exists: PE owners are a special class of financial entity driven toward intense opportunistic behavior in order to hit high rates of return promised to investors within a short time frame.⁶ PE firms – blessed with captive residents, guaranteed federal reimbursement, and poor regulation – pillage nursing homes with impunity.

Flaws and externalities in for-profit businesses can normally be counteracted by regulation, shifts in consumer shopping, and private litigation. The nursing home industry, however, is poorly regulated for several reasons. First, annual surveys of nursing homes are backlogged, leaving too many homes uninspected and sanctioned.⁷ Second, serious problems are underreported because state inspectors fail to identify quality problems or rate them as less severe than they are.⁸ Third, states fail to act to force institutions to correct violations, rarely imposing financial penalties. And even if corrections are mandated, there is rarely follow-up by state surveyors.⁹

The NAS 2022 report is striking: “[d]espite significant measures to improve the quality of nursing home care in OBRA ‘87, the current system often fails to provide high-quality care and underappreciates and underprepares nursing home staff for their critical responsibilities.”¹⁰ Government enforcement needs a partner – private law litigation – to force transparency of ownership, improve remedies for families of injured residents, and formalize a fiduciary standard of ownership that uses equitable tools to claw back excess profits and constrain bad nursing home management.

My argument is in three steps. First, I examine the unique financial incentives baked into the PE model of profit-maximizing ownership. Second, I examine the development of the corporate negligence doctrine. Third, I develop a model of a robust fiduciary duty, coupled with equitable remedies. My goal is to build a private law doctrinal framework to better police the waste, fraud, and pillaging of assets by PE owners of nursing home systems.

⁶ Eileen O’Grady, *Understaffed, Unlicensed, and Untrained: Behavioral Health under Private Equity*, Private Equity Stakeholder Project 2 (Sept. 2020), <https://pestakeholder.org/reports/understaffed-unlicensed-and-untrained-behavioral-health-under-private-equity/>.

⁷ Letter from Robert Casey, U.S. Senator of Pa., to State Survey Agencies (Sept. 13, 2022) (noting that 71 percent of nursing homes nationally had gone at least sixteen months without a standard survey).

⁸ Nina A. Kohn, *Nursing Homes, COVID-19, and the Consequences of Regulatory Failure*, Geo. L. J. Online 8 (2021), https://www.law.georgetown.edu/georgetown-law-journal/wp-content/uploads/sites/26/2021/04/Kohn_Nursing-Homes-COVID-19-and-the-Consequences-of-Regulatory-Failure.pdf.

⁹ *Id.*

¹⁰ Nat’l Acads. of Sci., Eng’g, and Med., *The National Imperative to Improve Nursing Home Quality: Honoring Our Commitment to Residents, Families, and Staff* 2 (2022).

21.2 PRIVATE EQUITY AS OPPORTUNISTIC FIDUCIARY: PIRATES WITH MBAS¹¹

Private equity investment involves acquisition of a total or partial ownership interest in an entity that is not publicly traded.¹² The playbook of PE is actively antithetical to the operation of a quality nursing facility.¹³ The profits are intended to satisfy investors first, not to provide quality resident care.¹⁴ I will show that the financial playbook of PE risks poor quality for nursing home residents¹⁵ – as well as draining the Medicare and Medicaid budgets through strategies of revenue inflation.¹⁶ Patients suffer from neglect caused by a cost-cutting PE ownership mode of finance.¹⁷ The PE strategies are cumulative and opportunistic, striving to capture and extract excess profits from every aspect of a nursing home system.¹⁸ Consider the playbook of PE firms that acquire nursing homes:

21.2.1 *High Rates of Return in a Short Time Horizon: Fast Bloodletting*

PE demands a rate of return in three to five years of around 20–30 percent, and typically a firm moves on at that point, selling the new consolidated firm after having extracted value from the firm and often leaving it in poor condition.¹⁹

¹¹ For the use of “pirate” to describe private equity owners, see Brendan Ballou, *Plunder: Private Equity’s Plan to Pillage America* (2023).

¹² Lisa Lillioth Rydin, *Private Equity, Venture Capital, and Hedge Funds*, Harv. L. Sch. Libr. (Aug. 17, 2022), https://guides.library.harvard.edu/law/private_equity.

¹³ Private Equity Ownership of Nursing Homes Linked to Lower Quality of Care, Higher Medicare Costs (Nov. 19, 2021), <https://news.weill.cornell.edu/news/2021/11/private-equity-ownership-of-nursing-homes-linked-to-lower-quality-of-care-higher>; Robert Tyler Braun et al., Association of Private Equity Investment in US Nursing Homes with the Quality and Cost of Care for Long-Stay Residents, 2 JAMA Health Forum e213817 (2021).

¹⁴ Richard M. Scheffler et al., Soaring Private Equity Investment in the Healthcare Sector: Consolidation Accelerated, Competition Undermined, and Patients at Risks, Petris Ctr. (May 18, 2021), <https://publichealth.berkeley.edu/wp-content/uploads/2021/05/Private-Equity-I-Healthcare-Report-FINAL.pdf>.

¹⁵ See Eileen Appelbaum & Rosemary Batt, *Financialization in Health Care: The Transformation of US Hospital Systems*, Center for Economic and Policy Research 58 (2021), <https://cepr.net/wp-content/uploads/2021/10/AB-Financialization-In-Healthcare-Spitzer-Rept-09-09-21.pdf>; Commercial Real Estate Investor & Private Equity Liability, First Nat’l Realty Partners (Mar. 2, 2022), <https://fnrpusa.com/blog/commercial-real-estate-investor-private-equity-liability/>.

¹⁶ David C. Grabowski et al., Low-Quality Nursing Homes Were More Likely Than Other Nursing Homes to Be Bought or Sold by Chains in 1993–2001, 35 Health Affs. 907 (2016).

¹⁷ Yasmin Rafiei, When Private Equity Takes over a Nursing Home, *The New Yorker* (Aug. 25, 2022), <https://www.newyorker.com/news/dispatch/when-private-equity-takes-over-a-nursing-home>.

¹⁸ See generally Robert I. Field et al., Private Equity in Health Care: Barbarians at the Gate?, 15 Drexel L. Rev. 821 (2023).

¹⁹ Private Equity Industry Overview, St. of Walls Blog (2013), <https://www.streetofwalls.com/finance-training-courses/private-equity-training/private-equity-industry-overview/>.

21.2.2 *Debt as a Profit Tool: Starving the Nursing Home*

PE loads up acquired firms with high levels of debt and then leverages this debt on the firms acquired in order to pay themselves and other shareholders dividends – in the order of magnitude of billions of dollars.²⁰ The acquired company must then manage these high levels of debt.²¹ The result often is a high number of bankruptcies;²² one study found that nearly 20 percent of PE-owned companies have filed for bankruptcy, ten times the rate of public companies.²³ Nursing homes end up reducing worker wages and cutting other resources, further increasing the risk of bankruptcy.²⁴ Nursing homes end up with little money for resident care improvements²⁵ and the long-term health of the nursing home suffers.²⁶

21.2.3 *High Rates of Churn in Ownership: Instability as Byproduct*

Frequent shifts in nursing home ownership destabilize both residents and staff.²⁷

21.2.4 *Staff Reduction Programs: Blood from a Turnip*

Cost-cutting is a central PE tool, used aggressively to allow firms to hit their rate-of-return metrics. Cutting billing, legal, and human resource departments reduces “wasteful” overhead. The PE ownership toolkit in particular drains nursing home assets and reduces needed spending on nurses and aides.²⁸ For-profit nursing homes routinely determine staffing levels based on census and reimbursement as opposed to resident acuity – for-profit facilities have 16 percent fewer staff than nonprofits after accounting for differences in residents’ needs.²⁹

²⁰ Eileen O’Grady, Dividend Recapitalizations in Healthcare: How Private Equity Raids Critical Health Care Infrastructure for Short Term Profit, Private Equity Stakeholder Project (2020), <https://pestakeholder.org/wp-content/uploads/2020/10/PE-SP-HC-dividends-10-2020.pdf>.

²¹ Id.

²² See Everything Is Private Equity Now, Bloomberg: Businessweek (Oct. 8, 2019, 4:10 PM), <https://www.bloomberg.com/news/features/2019-10-03/how-private-equity-works-and-took-over-everything?embedded-checkout=true>.

²³ See Brian Ayash & Mahdi Rastad, Leveraged Buyouts and Financial Distress, Fin. Rsch. Letters, Forthcoming 4 (July 19, 2019).

²⁴ O’Grady, *supra* note 20.

²⁵ Id.

²⁶ Jordan Rau, Nursing Home Owners Drained Cash While Residents Deteriorated, State Filings Suggest, NPR (Jan. 31, 2023), <https://www.npr.org/sections/health-shots/2023/01/31/1139783599/new-york-nursing-home-owners-drained-cash>.

²⁷ Grabowski et al., *supra* note 16.

²⁸ Robert I. Field et al., When Worlds Collide: The Effects of Private Equity on Health Care, 15 Drexel L. Rev. 101 (2023).

²⁹ Charlene Harrington et al., Time to Ensure Sufficient Nursing Home Staffing and Eliminate Inequities in Care, 7 J. Geontol. Geriatr. Med. 99 (2021).

21.2.5 “Related Party Transactions”: *Skimming the Till*

For-profit nursing facility executives develop new financial streams by creating complex ownership and management structures – this creates tax advantages and allows companies to move capital from one entity to another. Nursing home chain owners often outsource goods and services to multiple entities in which they also have ownership, and these entities then allow ancillary clinical services to be fragmented and spun off under the corporate umbrella.³⁰ Such services may include laboratory, radiology, pharmacy, and specialty medical services.³¹ PE nursing homes may also make referrals to PE-owned home health care, hospice, mental health, emergency room staff services, and specialty clinics.³²

These ownership structures are not a search for market efficiencies and cost-savings: to the contrary, “. . . the owners can establish highly favorable contracts in which their nursing homes pay more than they might in a competitive market. These profits are then siphoned off, not recorded in nursing home accounts, and hidden in affiliated companies.”³³

21.2.6 *Multilevel Corporate Structures: Deceiving and Dodging*

Complex layers of entities also shield the enterprise from liability by making it difficult for plaintiff lawyers to pursue a defendant with assets. Such strategies often involve deception in financial statements to conceal real income and assets among a myriad of subsidiaries.³⁴ Without data and visibility, plaintiff lawyers and regulators are all blinded.³⁵

The cumulative effect of the PE playbook is poor quality care and high mortality rates – PE ownership increases 90-day mortality by 2.4 percentage points, or 15 percent of baseline mortality among Medicare residents, adding up to approximately 20,150 deaths over the course of 12 years according to a recent study.³⁶ Costs to the

³⁰ See Melea Atkins, *The Impact of Private Equity on Nursing Home Care: Recommendations for Policymakers*, Roosevelt Inst. 5–6 (Apr. 2021), https://rooseveltinstitute.org/wp-content/uploads/2021/04/RI_NursingHomesandPE_IssueBrief_202104.pdf.

³¹ See Gary M. Kirsh & Deepak A. Kapoor, *Private Equity and Urology: An Emerging Model for Independent Practice*, 48 *Urologic Clinics N. Am.* 233, 234 (2021).

³² *Id.*

³³ Jordan Rau, *Care Suffers as More Nursing Homes Feed Money into Corporate Webs*, N.Y. Times (Jan. 2, 2018), <https://www.nytimes.com/2018/01/02/business/nursing-homes-care-corporate.html>.

³⁴ Yao O. Dinizulu & Jennifer Matta, *The Multi-Level Nursing Home Corporate Structure: Transparency, Accountability and Common Sense*, 12 *Nursing Home Litig. Rep.* 3 (2009).

³⁵ David E. Kingsley & Charlene Harrington, *Financial and Quality Metrics of a Large, Publicly Traded U.S. Nursing Home Chain in the Age of Covid-19*, 52 *Int'l J. of Health Servs.* 212 (2022).

³⁶ Atul Gupta et al., *Does Private Equity Investment in Healthcare Benefit Patients? Evidence from Nursing Homes*, NBER Working Paper No. 28474 (2021), https://www.nber.org/system/files/working_papers/w28474/w28474.pdf.

federal and state governments of paying for Medicaid and Medicare services are also inflated with no benefit accruing to residents.

21.3 HEALTH CARE AS AN ENTERPRISE: CORPORATE NEGLIGENCE

The origins of corporate negligence in health care settings began with hospitals.³⁷ Courts began to notice that hospitals were big businesses – running aggressive marketing campaigns, managing their medical staff and other professionals, and generally acting like the central provider of health care.³⁸

21.3.1 *Corporate Negligence: Responsibility of the “Enterprise”*

The doctrine of corporate negligence starting in the 1960s noted that the modern hospital as an enterprise is no longer just a shell for physicians to use.³⁹ Hospitals have gone from small not-for-profit religious systems to large systems run on corporate principles of revenue maximization.⁴⁰ More than half of American jurisdictions have now adopted the corporate negligence doctrine in some form.⁴¹

Corporate negligence, in the Pennsylvania case of *Thompson v. Nason Hospital*,⁴² requires a hospital to uphold a standard of care to “ensure the patient’s safety and well-being while at the hospital.” *Thompson’s* corporate negligence doctrine mandates four distinct duties for institutional providers: (1) reasonable care in the maintenance of safe and adequate facilities and equipment; (2) selection and retention of competent physicians; (3) oversight of all persons who practice medicine within its walls as to patient care; and (4) formulation, adoption, and enforcement of adequate rules and policies to ensure quality care for patients. These duties are nondelegable.

Corporate negligence views the modern hospital as a complex corporate management structure with responsibilities to its patients, measured by its own internal practices as well as those of other similar hospitals.⁴³ Hospitals can in fact be just as opportunistic as any business, susceptible to the temptation to engage in self-

³⁷ *Sword v. NKC Hospitals, Inc.*, 714 N.E.2d 142 (Ind. 1999) (and cases cited).

³⁸ *Clark v. Southview Hosp. & Family Health Ctr.*, 628 N.E.2d 46 (Ohio 1994) (promotional and marketing campaign stressed the emergency departments); *Gragg v. Calandra*, 696 N.E.2d 1282 (Ill. App. Ct. 1998) (patients assume that hospital physicians are employees).

³⁹ Alex Stein, *Toward a Theory of Medical Malpractice*, 97 Iowa L. Rev. 1201, 1229 (2012).

⁴⁰ Thomas L. Hafemeister & Joshua Hinckley Porter, *Don’t Let Go of the Rope: Reducing Readmissions by Recognizing Hospitals’ Fiduciary Duties to Their Discharged Patients*, 62 Am. Univ. L. Rev. 513, 546 (2013).

⁴¹ See *Larson v. Wasemiller*, 738 N.W.2d 300 (Minn. 2007) (adopting corporate negligence for Minnesota, the court noted that more than half of the state courts have adopted the tort, and it has support in Restatement (Second) Tort sections such as sections 320 and 411).

⁴² *Thompson v. Nason Hosp.*, 591 A.2d 703 (Pa. 1991).

⁴³ See Barry R. Furrow, *The Limits of Current A.I. in Health Care: Patient Safety Policing in Hospitals*, 12 NE. Univ. L. Rev. 1 (2020).

interested behavior when their financial interests conflict with those of the populations they serve.⁴⁴ The evolution of the corporate negligence doctrine reflects judicial awareness that health care institutions owe enhanced duties to their beneficiary patients.⁴⁵ Corporate negligence has been a large step toward a vigorous fiduciary obligation to care for patients.

21.3.2 *The Corporate Negligence Model Expands*

Thompson, decided in 1991, was at first applied only to hospitals. Next, in *Shannon v. McNulty*,⁴⁶ Health Maintenance Organizations (HMOs), acting as the primary decision-makers with respect to their subscribers' care, were subject to corporate liability. In *Hyrca v. West Penn Allegheny Health*,⁴⁷ medical professional corporations were added, on the basis that such entities, if they take responsibility for their patients' total health care like hospitals, are liable for failing to fulfill institutional duties.⁴⁸ Finally, in 2012, the Pennsylvania Supreme Court applied corporate negligence to nursing homes in *Scampone v. Highland Park Care Center*.⁴⁹ The court held that nursing home facilities and their parent corporations were subject to corporate negligence liability for patient harms. This new duty intensifies nursing home incentives to improve the quality of their care to avoid liability.⁵⁰

21.4 CREATING A PRESUMPTIVE FIDUCIARY DUTY FOR NURSING HOME OWNERS

A second source of private law is fiduciary law. Courts can use fiduciary duties plus equitable powers to constrain nursing home opportunism, creating a presumptive fiduciary duty that eliminates the need for plaintiffs to make a particularized factfinding in each case.⁵¹

This nursing home fiduciary duty is built on three foundations.

⁴⁴ Danielle Ofri, *Why Are Nonprofit Hospitals So Highly Profitable?*, N.Y. Times (Feb. 20, 2020), <https://www.nytimes.com/2020/02/20/opinion/nonprofit-hospitals.html>.

⁴⁵ Barry R. Furrow, *Patient Safety and the Fiduciary Hospital: Sharpening Judicial Remedies*, 1 Drexel L. Rev. 439 (2009).

⁴⁶ *Shannon v. McNulty*, 718 A.2d 828 (Pa. Super. Ct. 1998).

⁴⁷ *Hyrca v. West Penn Allegheny Health*, 978 A.2d 961 (Pa. Super. Ct. 2009).

⁴⁸ *McClure v. Parvis*, 294 F.Supp.3d 318 (E.D. Pa. 2018) (physician practice groups were added, as entities responsible for a patient's health).

⁴⁹ *Scampone v. Highland Park Care Ctr., LLC*, No. 16 WAP 2011.

⁵⁰ R. Tamara Konetzka et al., *Malpractice Litigation and Nursing Home Quality of Care*, 48 Health Serv. Res. 1920 (2013) (finding "... significant increases in registered nurse-to-total staffing ratios in response to rising malpractice threat, and a reduction in pressure sores among highly staffed facilities").

⁵¹ See, e.g., *Zaborowski v. Hosp. Care Ctr. of Hermitage, Inc.*, PA. Dist. And Cty. Ct., 2002 WL 32129508 (2002).

21.4.1 *Medicaid as a Fiduciary*

Medicaid is the primary federal payer of nursing home expenses. Sara Rosenbaum and her coauthors have argued that Medicaid has a fiduciary duty standard, based on statutory state plan requirements for medical assistance requiring "... such safeguards as may be necessary to assure that eligibility for care and services under the plan will be determined and such care and services will be provided in a manner consistent with simplicity of administration and the *'best interests of the recipients.'*" [Italics mine.]⁵² This "best interests of the recipients" standard is analogous to ERISA's fiduciary duty standard.⁵³ Since state programs certify and regulate all owners of nursing home chains, whether nonprofit or for-profit, this "best interests" standard of fiduciary duty obligates states and their nursing home managers and owners.

21.4.2 *The Resident as "Vulnerable"*

Fiduciary law establishes a norm of special obligations, creating higher expectations than we normally allocate to others in contractual relationships.⁵⁴ As Rothman writes, "the fiduciary concept brings law closer to the human condition by anticipating potential problems that exist in certain forms of interaction characterized by power imbalances and vulnerability and prohibiting their development through the entrenchment of strict principles on fiduciaries."⁵⁵ This concept of fiduciary law fits the nursing home relationship between owners/managers and residents perfectly.⁵⁶ The court in *Schenk v. Living Centers-East* emphasized the unique vulnerability of residents in nursing homes:

Residents are in the care and custody of the home on a 24-hour basis, with all their needs necessarily supplied by the facility. Residents are almost invariably in poor physical and/or mental health; they are frequently incompetent and unable to comprehend much less protest any mistreatment or neglect; their families likewise are not in a position to readily know whether injuries are caused by genuine accidents or whether they result from neglect or abuse. [] These various factors make such residents particularly vulnerable to neglect and a variety of possible abuses with detection arguably difficult . . . unlike the situation where a presumably

⁵² Sara Rosenbaum et al., *Medicaid and Health Information: Current and Emerging Legal Issues*, 28 *Health Care Fin. Rev.* 21 (2006–07).

⁵³ *Id.*

⁵⁴ Leonard I. Rotman, *Understanding Fiduciary Duties and Relationship Fiduciarity*, 62 *McGill L. J.* 975, 1003 (2017).

⁵⁵ *Id.* at 46.

⁵⁶ *Petre v. Living Centers-East*, 935 F. Supp. 808 (E.D. La. 1996).

competent person seeks a consultation with a physician for a particular problem or even requires hospitalization for a particular malady.⁵⁷

The *Schenck* court then builds a conceptional foundation for the fiduciary duty count in the plaintiff's complaint:

[M]any if not most nursing home residents are in a vulnerable physical and/or mental state. Placing a loved one in such a facility necessarily entails trust on the part of the family as well as the resident. Since the residents reside in the home, the family has comparatively limited access and opportunity to learn if the resident is neglected or otherwise mistreated. *If entrusting one's money to a receiver or conservator created a business relationship, one would hope at least in principle that entrusting a valued family member to the care of a business entity such as a nursing home would carry similar responsibilities.* [Italics mine.]⁵⁸

The *Schenck* court acknowledges the realities of nursing home care: Most residents are vulnerable physically, lack the cognitive skills in many cases to protect themselves, did not "choose" their home, and need a heightened level of personal attention and care.⁵⁹ The *Petre* court observed that no relationship better fits "the description of the fiduciary capacity than the relationship between a nursing home and its residents."⁶⁰

21.4.3 *Anti-Opportunism: Fiduciary Controls over "Self-Interest Seeking with Guile"*

The third leg of nursing home fiduciary duty is built on the extreme opportunism of PE ownership in health care, as shown in Section 21.4.1. The generally accepted definition of opportunist behavior in fiduciary law is that of Williamson. His definition is as follows:

By opportunism I mean self-interest seeking with guile. This includes but is scarcely limited to more blunt forms, such as lying, stealing and cheating. Opportunism more often involves subtle forms of deceit . . . More generally, opportunism refers to the incomplete or distorted disclosure of information, especially to calculated efforts to mislead, distort obfuscate, or otherwise confuse.⁶¹

Fiduciary law strives to control such opportunistic behavior: Smith defines "opportunism" as "behavior that is undesirable but that cannot be cost-effectively

⁵⁷ *Schenck v. Living Centers-East, Inc.*, 917 F. Supp. 432 (E.D. La. 1996).

⁵⁸ *Id.* at 438.

⁵⁹ See generally Joachim Boldt, The Concept of Vulnerability in Medical Ethics and Philosophy, 14 *Phil., Ethics, and Human. in Med.* 6 (2019); see also D. Gordon Smith, The Critical Resource Theory of Fiduciary Duty, 55 *Vand. L. Rev.* 1399, 1404 (2002).

⁶⁰ *Petre*, *supra* note 56, at 812.

⁶¹ Oliver E. Williamson, *The Economic Institutions of Capitalism: Firms, Markets, Relational Contracting* 47–48 (1985).

captured – defined, detected, and deterred – by explicit ex ante rulemaking . . . It often consists of behavior that is technically legal but is done with a view to securing unintended benefits from the system, and these benefits are usually smaller than the costs they impose on others.”⁶²

Private equity acts knowingly and opportunistically through its financial playbook – deliberate pillaging of nursing home, residents, and government payers. Actions by PE owners of nursing homes are “intentional” – the core strategies discussed in Section 21.4.1 are intended to load nursing homes with debt, build structures to inflate charges to Medicaid and Medicare, and cut staffing and other costs with the predictable results of poor care and fraud on Medicaid.

21.5 EQUITABLE POWERS TO CONSTRAIN PRIVATE EQUITY OWNERSHIP

Fiduciary law, coupled with a court’s equitable tools, provides a far more muscular approach to nursing home bad actors than does either tort or contract law limited to damage remedies.⁶³ Fiduciary law offers future-looking equitable tools to change the PE calculus for those who invest in and run nursing homes.⁶⁴ It identifies opportunistic power used against the vulnerable. It allows vulnerable beneficiaries and their families to demand honesty and selflessness of their fiduciaries.⁶⁵

21.5.1 *Coupling Fiduciary Duties and Equitable Remedies*

Imposing a fiduciary duty on an organization raises the baseline for conduct and the measurement of failure and breach of duty. Fiduciary doctrine can create a presumption of wrongdoing for this class of relationships.⁶⁶ Fiduciary law creates legal rights grounded in equity for those who need protection, allowing tolling of statutes of limitation and easing a plaintiff’s burden of proof. And fiduciary law can draw on a range of equitable remedies. Equity imposes harsh sanctions against fiduciaries for failing to conform to the fiduciary concept’s high standards: These may include *inter alia* the disgorgement of profits or amounts equal to losses avoided, equitable compensation, a constructive trust, an injunction, or an accounting of profits.⁶⁷

⁶² Henry E. Smith, Why Fiduciary Law Is Equitable, in *Philosophical Foundations of Fiduciary Law* 267 (Andrew S. Gold & Paul B. Miller eds., 2014).

⁶³ *Id.*

⁶⁴ Kingsley & Harrington, *supra* note 35.

⁶⁵ O’Grady, *supra* note 20.

⁶⁶ Rotman, *supra* note 54.

⁶⁷ For a full list of fiduciary remedies, see generally David F. Johnson, *Remedies for Breach of Fiduciary Duty Claims* (Aug. 7, 2020).

21.5.2 *Examples of Fiduciary Powers*⁶⁸

21.5.2.1 Disgorgement

In *Rohlfing v. Manor Care, Inc.*,⁶⁹ the executor of a nursing home resident's estate sued Manor Care, the nursing home operator, its parent, and the related pharmaceutical company for antitrust violations, fraud, and breach of fiduciary duty. His goal was to recover excessive fees the resident was forced to pay because of the nursing home's pharmaceutical policies, as well as attorney fees. The court allowed class certification for antitrust and Racketeer Influenced and Corrupt Organizations Act (RICO) claims, the Illinois Consumer Fraud Act (ICFA), and the breach of fiduciary duty.

Manor Care owned a network of 179 facilities in 28 states, offering a spectrum of services to residents – from “high acuity” (intensive) nursing care to custodial care and assisted living arrangements. Manor Care owned an 82.3 percent interest in eighteen of the facilities, which were required to get their pharmaceutical services from Vitalink Pharmacy Services, Inc. (Vitalink). Vitalink also provided consulting services for Manor Care residents, such as monitoring potential drug interaction problems and reviewing patients' drug administration records.

The court expanded on the nature of fiduciary duty: “A fiduciary duty exists in relationships where ‘there is confidence reposed on one side and a resulting superiority and influence on the other.’ [citations omitted] . . . It is certainly true that ‘many, if not most nursing home residents are in a vulnerable physical and/or mental state,’[*Schenk*], which could place their caregivers in a position of confidence and influence.”⁷⁰

The court in *Rohlfing* held that the plaintiff, Rohlfing, had alleged a proper claim for breach of fiduciary duty.⁷¹ The plaintiff in *Rohlfing* alleged that Manor Care charged him excessive prices for pharmaceuticals, thus breaching their fiduciary duties. The court found that Rohlfing had alleged a claim for breach of fiduciary duty, quoting *Quist v. Dorn*: “Courts of Equity will scrutinize with jealous vigilance the transactions between parties occupying fiduciary relations toward each other . . .”⁷²

Manor Care is an example of the abuse of *related-party transactions*, specifically use of a pharmacy service owned by the nursing home system to extract high prices

⁶⁸ Samuel L. Bray, *Fiduciary Remedies*, in *The Oxford Handbook of Fiduciary Law* (Evan J. Criddle et al. eds. 2019).

⁶⁹ *Rohlfing v. Manor Care, Inc.*, 172 F.R.D.330 (N.D. Ill. 1997).

⁷⁰ *Id.*

⁷¹ *Id.* (the court did make a specific finding of several elements that justified imposing a fiduciary duty in the case).

⁷² *Quist v. Dorn*, 301 Ill.App. 264, 22 N.E.2d 729, 732 (1939).

for drugs and drug services. If such a case goes to trial, a plaintiff can seek disgorgement of excess gains – to be returned to nursing home residents.

21.5.2.2 Fiduciary Duties of Corporate Owners

In *Isby Brandon v. Beverly Enterprises, Inc.*,⁷³ defendants were the corporate owners of the nursing home – the administrator was not a defendant. The District Court considered whether a fiduciary breach could be claimed against nondiverse defendants, the corporate owners of the nursing home. The court stated the elements of a fiduciary duty. A contractual relationship may give rise to a fiduciary duty when: “(1) the activities of the parties go beyond their operating on their own behalf, and the activities for the benefit of both; (2) where the parties have a common interest and profit from the activities of the other; (3) where the parties repose trust in one another; and (4) where one party has dominion or control over the other.”⁷⁴

The *Isby Brandon* court held that patients could prove a fiduciary duty at trial as a matter of Mississippi law. It recognized the resident status as “vulnerability” in a nursing home, by analogy to the “ward” of a fiduciary. The patient, says the court, is “usually permanently invalid and subject to the nursing home.” The court continued: “[T]he parties obviously repose trust in one another and has been said above, the nursing home as fiduciary has dominion and control over the nursing home patient.”⁷⁵

This case, drawing on fiduciary law analysis, opens a judicial path to plaintiff’s pursuit of owners who are not the onsite managers but rather the corporate owners of the nursing homes. It offers state courts the power to unravel complex ownership structures created by PE firms, imposing a fiduciary duty through the mechanism of private law.

21.5.2.3 Accounting for Profits

An accounting orders an inquiry into the defendant’s handling of money or property, usually to ascertain the defendant’s gains so they may be paid to the plaintiff. Such an accounting is typically given against a fiduciary. One recent example: New York’s Attorney General has asked a state court to force the owners of a Syracuse nursing home to answer questions about “pocketing” US\$37.6 million in Medicaid funding from related-party transactions.⁷⁶ A private litigant can make the same

⁷³ *Isby Brandon v. Beverly Enters.*, No. 1:06CV280-P-D (N.D. Miss. Apr. 6, 2007).

⁷⁴ *Id.* at 2.

⁷⁵ *Id.* at 3.

⁷⁶ See Jessica R. Towhey, NY Brings Fresh Allegations for a For-Profit Nursing Home “Pocketing” Medicaid Funds, McKnights Long-Term Care News (June 13, 2023), <https://www.mcknights.com/news/ny-brings-fresh-allegations-of-a-for-profit-nursing-home-pocketing-medicaid-funds/>.

demand for an accounting if the state court invokes the equitable powers available to someone victimized by a fiduciary.

21.5.2.4 Unwinding Remedies

One of the specialties of equity is unwinding and undoing. “Equity, one might say, delights in erasing and not by halves.”⁷⁷ Judicial orders may include cancellation of documents, avoidance of contracts, reformation, and equitable rescission.⁷⁸

21.5.2.5 Injunctions

As fiduciary scholars write, fiduciary law offers robust remedies that “... must be more severe than against garden variety actors. One method of conforming to this requirement is to employ injunctions against suspected opportunists, and also to withhold injunctive relief from opportunists.”⁷⁹

21.6 CONCLUSION

Vulnerable nursing home patients can benefit from the use of private law tools to move the regulatory focus back to the nursing resident as the beneficiary of a fiduciary owner.

Fiduciary duties coupled with corporate negligence duties harness private law to force PE owners toward more demanding fiduciary duties toward their nursing home residents. Private law can have a powerful role in expanding the duties owed by PE firms to vulnerable nursing home patients.

⁷⁷ W. Hudson R. Unger, *Equity Delights to Do Justice and Not by Halves*, 33 *Dick. L. Rev.* 248 (1929).

⁷⁸ Bray, *supra* note 68, at 459.

⁷⁹ Kenneth Ayotte et al., *Safety Valve Model of Equity as Anti-Opportunism* 30–31, *Nw. L. & Econ. Rsch. Paper*, Paper No. 13–15 (2013), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2245098.