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# Steward Health Care: A Cautionary Tale

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## Abstract

**What is the message?** The May 2024 bankruptcy of Steward Health Care – the largest physician-owned hospital system in the country and one of the largest U.S. private hospital systems – raises questions about the hospital's private equity funding, debt-financed business model and the future care of its patients.

**What is the evidence?** News reports, court documents, and company announcements.

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In May 2024, Steward Health Care filed for bankruptcy with nearly $9 billion in liabilities, one of the largest hospital bankruptcies in US history.[1] Steward's financial collapse is closely tied to its private equity funding and debt-financed business model, leaving policymakers with questions about care delivery for the former Steward patients and scrutiny of private equity investment in healthcare.

Steward was launched in 2010 after a private equity firm, Cerberus Capital Management, acquired a failing nonprofit Massachusetts hospital system, Caritas Christi Health Care.[2] Ralph

de la Torre, a cardiac surgeon with degrees from Harvard Medical School and Massachusetts Institute of Technology, joined Caritas as CEO in 2008 after being recruited from Beth Israel Deaconess Medical Center, and remained as CEO for the new Steward Health Care.[3] Steward was intended to show how an injection of private capital and the management model of private equity can be used to improve the management capacity and the services of a safety net healthcare system. At the time, de la Torre was quoted, “We are striving to further improve the quality of care our patients receive, attract talented new physicians, upgrade and expand the infrastructure at our facilities, maintain or grow our staffing levels and undertake additional investments to further improve the quality of care we provide. In Cerberus, we found an investor that shares our vision and commitment.” [2] This marked a substantial private investment in a large hospital system that predominantly delivered care to low-income patients on Medicaid or Medicare. The terms of the transaction were later modified, but finally approved, by the Massachusetts Attorney General.[4]

Steward grew from the six Caritas Christi hospitals in 2010 to 33 hospitals at bankruptcy in 2024.[4]

After failing to achieve profitable status or expand outside of Massachusetts, Steward sold its Massachusetts properties to Medical Properties Trust (MPT), a real estate investment trust (REIT), in a $1.25 billion sale-leaseback agreement in 2016.[4] In a sale-leaseback agreement, organizations offload properties for a capital infusion, with an agreement to lease the facilities from the new property manager. Steward’s agreement included a 10-year escalator clause leading to annual rent increases, with each individual hospital responsible for rent, insurance, and taxes.

Steward used the funds it raised to make a payment to Cerberus capital, and then to acquire IASIS Healthcare in 2017 and expand to 36 hospitals across 10 states.[3,5] In 2018, Steward became an international health system with operations in Malta and Columbia.

In 2020, de la Torre led a buyout of the remaining Cerebus interest in Steward, leaving ownership to a physician group (90%) and MPT (10%).[5]

As a result of the sale-leaseback agreement, the Steward system, which already failed to attain profitability by 2016, began experiencing increasing operating costs and worsening budgetary pressures given the large and increasing lease payments. Adding to the financial instability, Steward fell behind in its accounts payable to vendors who repossessed medical equipment needed for patient care. This was linked to adverse patient outcomes, including one patient's death.[6]

The financial model for Steward remained challenging. In late 2023, Steward delayed lease payments to MPT, so MPT publicly announced efforts to recover its overdue payments and limit its exposure to Steward in January 2024.[7] Negotiations to financially restructure Steward were unsuccessful, leading to the bankruptcy filing of Steward and 166 related entities in May 2024.[8] In their filings, Steward reported $1.2 billion in secured debt and $8 billion in unsecured debt.[8] Steward reported the full potential impact of this bankruptcy when they report that they served *"two million patients annually, and employing a workforce of nearly 30,000. Since its inception, Steward has become a national, integrated health care network across 10 states comprised of 31 hospitals and over 400 facility locations (including physician practice offices, ambulatory surgical centres, and diagnostic imaging centres) with over 4,500 primary and specialty care physicians, all committed to serving patients in underinsured and underserved communities."*[8]

This was a stunning turn of events for Steward, leading to significant questions about the financial engineering underlying all of these transactions. Publicly, politicians were screaming about the two yachts and two jets owned by de la Torre.[9] They demanded greater transparency and accountability for Steward's management.[10]

Given the implications of the Steward collapse for patients and government-sponsored insurance, federal and state governments have grounds to scrutinize some of the financial tools used to construct Steward, including its REIT financing model. In 2021, REITs owned over $3.5 trillion in assets, with ownership of 3% of all hospitals nationwide.[11] Medical institutions are particularly attractive for REITs, as these organizations are often willing to enter longer term sale-leaseback agreements that are negotiated for decades-long leases and have a predictable revenue stream.[12] Healthcare organizations have stable cash flows, yet in this instance essential

services were put at risk. From the perspective of investors, investing in these organizations can be risky, with Cereberus capital profiting approximately $800 million over 10 years,[13] while MPT attributed $693 million in losses in Q1 2024 to Steward.[14]

The obvious question remains if sale-leaseback agreements even have a place in healthcare, and whether these institutions have the governance structure required to support these transactions. The short-term fiscal benefits of a sale-leaseback agreement could be very lucrative to hospital executives, but they may not support sustained growth of the underlying institutions. From the data currently available, its unclear if the REIT structure itself was at fault, or the escalation terms built into the REIT payments – presumably to help support operational cash-flow in the short term in exchange for higher payments in the future that might only occur by abandoning the safety-net patient base of the organization in the search for patients with more generous commercial insurance. Safeguards could be required in the terms of a sale-leaseback to prevent capital expenditures without an established plan for the hospital system to maintain its new fiscal responsibilities. In addition, the government could regulate sale-leaseback terms in healthcare to prevent hospitals from entering very long-term agreements or unfavorable escalator clauses. Of course, the Steward bankruptcy is also a cautionary tale for the REIT industry which supported an aggressive growth plan by Steward that ultimately failed.

The bankruptcy of Steward Health Care, the largest physician-owned hospital system in the country and one of the largest U.S. private hospital systems, could serve as a wake-up call for further examining the role of private equity in healthcare, especially in the hospital and safety-net markets. Of course, the investment industry will argue that Steward is a case of management greed and failure and should not serve as the condemnation of all of private equity. The inevitable investigations that will follow will shed further light on these questions.

In the immediate term, the crisis leaves lawmakers with several urgent questions to prevent the loss of care continuity for patients served by this hospital system. With Massachusetts often serving as a trailblazer in healthcare policy, the outcome of the Steward Health bankruptcy may set the tone for national health policy on private equity investment in healthcare.

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