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**Acquisition of a
Physician Practice**

Linda L. Fleming, Esq.
Carlton Fields, P.A.

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Acquisition of a Physician Practice

- I. Letter of Intent/NDA**
- II. Due Diligence**
- III. Structuring the Transaction**
- IV. Key Considerations**
- V. Regulatory Matters**

I. Letter of Intent

- Nondisclosure Agreement is necessary
- LOI is optional: To sign or not to sign?
- If LOI is drafted, key issues:
 - Preliminary Purchase Price (FMV)
 - Transaction/Structure
 - No Shop



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Letter of Intent (cont.)

- Other Matters Important to the Physician
 - Employment Terms
 - Compensation and Benefits
 - Employment of Other Staff
 - Post Closing Practice Location
 - Noncompetition Covenants
- Binding or Nonbinding
 - Usually some provisions are binding (e.g., no shop; governing law; nondisclosure) while others are not (e.g., transaction structure; purchase price)
 - Given most provisions are nonbinding, what justifications are there for entering into Letters of Intent?



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II. Due Diligence

- Compliance Issues
 - Self Disclosure
 - Transferee Liability
- Licensure and Disciplinary Issues
- Practice Locations
- Medical Staff Privileges
- Financial Performance



Due Diligence (cont'd.)

- Managed Care Contracts – do not request or review rates without a signed agreement
- Staffing/Salary/Benefits – again, be mindful of requesting too early
- Ownership of Assets
- Encumbrances on Assets
- Litigation
- Insurance Coverage
- Electronic Medical Records (or lack thereof)
- Need for Indemnity Escrow based on due diligence findings?

III. Transaction Structure

- Asset Purchase/Employment
- Asset Purchase/Professional Services Agreement
- Asset Purchase/Management Support Organization
- Ownership Interest Purchase/Merger

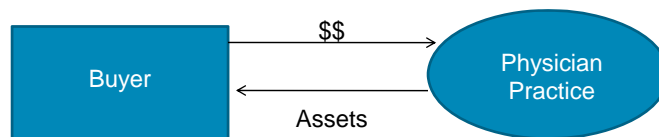


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Typical Transaction Structures *Asset Purchase/Employment*



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Typical Transaction Structures *Asset Purchase/Employment*

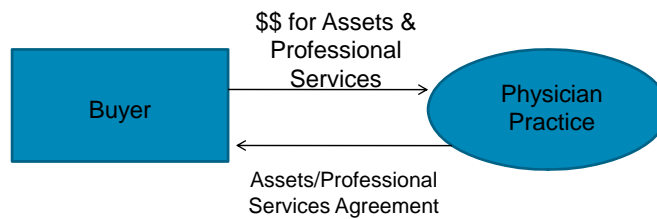
- Assets of Physician Practice are purchased at fair market value
- Physicians, along with clinical and non-clinical staff, become employees of Buyer
- Physician employees are compensated at FMV under Stark Law compliant employment arrangements
- Noncompetition covenants can be included
- Certain liabilities could be assumed

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Typical Transaction Structures *Asset Purchase/Professional Services Agreement*



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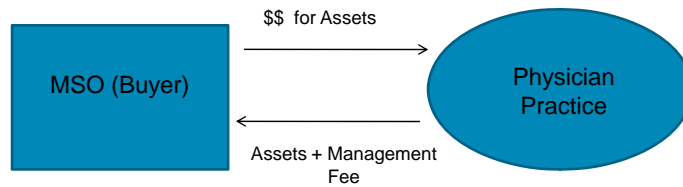
Typical Transaction Structures *Asset Purchase/Professional Services Agreement*

- Assets of Physician Practice are purchased at fair market value
- Staff (other than physicians) become employees of Buyer
- Physicians remain employed by Physician Practice and enter into a long-term professional services agreement with Buyer
- Compensation under PSA must be at fair market value compensation
- Buyer bills and collects for physician services

Typical Transaction Structures *Asset Purchase/Professional Services Agreement*

- Model works best in states where corporate practice of medicine is an issue
- Physicians relieved of burden of capital investment and costs of carrying staff
- Physicians remain responsible for their compensation; funded through utilizing PSA compensation

Management Services Organization



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Typical Transaction Structures Management Services Organization

- MSO acquires tangible assets of the Physician Practice
- Physician Practice remains independent
- MSO provides turn-key management services to Physician Practice, which may include
 - Equipment
 - Personnel Pooling
 - Billing/Collections
 - I.T./EMR
 - Clinical Improvement Initiatives
 - Risk Management
 - Recruiting

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Typical Transaction Structures *Management Services Organization*

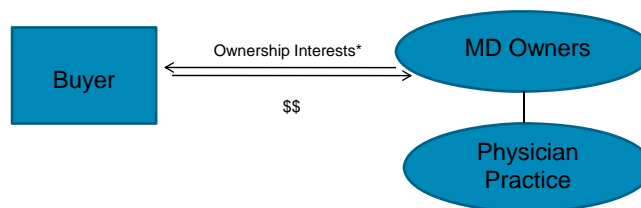
- Purchase price limited to FMV of hard assets
- Physicians relieved of burdens of:
 - Capital investment
 - Administration of practice
- Physician Practice remains at risk for reimbursement and physician compensation
- MSO services must be provided at FMV
- Be cautious of fee splitting restrictions in Florida

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Typical Transaction Structures *Ownership Interest Purchase/Merger*



* Can be structured as a stock purchase, membership interest purchase, or merger

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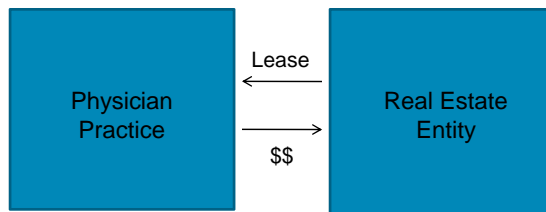
Typical Transaction Structures *Ownership Interest Purchase/Merger*

- If possible, may lessen tax burden on selling physician
- May avoid licensure or anti-assignment clauses
- Only in non-CPM states
- In certain states, physicians practice can be converted from professional corporation (or LLC) to a traditional for profit corporation (or LLC) to allow for ownership by non-physicians

IV. Key Considerations

- Real Estate
- Physician Compensation
- Valuation Matters
- Purchase Price
- Other Concerns

Real Estate Component



Real Estate Component

- Physicians may hold practice real estate in a separate entity
- Transactions often structured to allow physicians to retain real estate and enter into lease with Buyer at fair market value
- Current lease can be assigned to Buyer (with any needed amendments) or new lease directly with Buyer
- Lease valuations are advisable

Physician Compensation – “The wise man learns from the mistakes of others”

- “Guaranteed” salary models are disfavored
- Trend is toward production based models
 - Revenue *minus* expenses
 - Base compensation *plus* incentive compensation (incentive at risk)
 - Work relative value unit production (WRVUs allocated to CPTs)
 - Incentives for quality, good citizenship, patient satisfaction
- Hybrid – one year guaranty then production based

Physician Compensation

- Physician compensation must meet Stark Law bona-fide employment exception
- Anti-Kickback statute is less stringent; only requires that physicians are bona-fide employees
- If Buyer is tax-exempt, excess benefit transactions and private inurement/private benefit issues
- Possible to structure compensation to include ancillaries (DHS) if physician is employed by group practice
- FMV is a critical threshold

Valuation Matters

- All regulatory analyses turn on FMV
- Formal valuations close the gap between perception and reality
- Physician professional component generally has relatively low valuation
- Most value embedded in ancillary businesses that spin off cash flow (imaging, ASC, lab)
- What about goodwill?
- Certain intangible assets have value
 1. Workforce in place
 2. Medical records
 3. Trademarks and trade names
- Use of “stay bonuses” and payments for covenants not to compete

Purchase Price & Other Concerns

- Consider tax consequences to physicians
- Installment payments v. lump sum payment
- Other Concerns
 - Certain percentage of physicians contracts signed as a condition to closing
 - Regulatory approvals
 - Indemnity escrow
 - Noncompetition covenants
 - In Florida, term, geographic area and scope of activities must be reasonable
 - Statutory guidance is available (F.S. §542.335)
 - Courts will redraw if restrictions are overly broad

V. Regulatory Matters

- Federal
 - Anti-Kickback Statute
 - Stark Law
 - False Claims Act
 - Civil Monetary Penalty Laws
 - HIPPA/HITECH
- State
 - Anti-kickback
 - Stark equivalents
 - Corporate Practice of Medicine (California, Illinois, Texas, Others)
 - Fee Splitting
 - Noncompetition
 - Licensure

Conclusion

- Focus on Big Picture
 - Purchase Price
 - Physician Compensation
 - Integration and Post-Closing Performance
 - Exit Strategy
- Regulatory Compliance
 - \$\$ to Physicians = Fraud & Abuse Concerns
- Get the Right Team Involved Early
 - Health Care/Corporate Attorney
 - Accountant
 - Valuation Expert