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Practical Considerations in the Purchase and Sale of Physician Practices

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The purchase and sale of a physician practice is a common transaction, especially as the trends of health care diversification and consolidation continue. While general business and legal knowledge regarding the sale of businesses applies to these transactions, additional health law and practical issues must be addressed in a physician practice sale. Consideration of the issues specific to the sale of physician practices beforehand can save both parties time, trouble, and money. The issues covered in this article include fraud and abuse concerns, licensure, ownership restrictions, medical records, managed care, and government payer issues. The authors are practicing lawyers in Florida with substantial experience in the sale of physician practices, so this article will have a Florida law perspective. Nonetheless, these issues exist, with some differences in laws, in every state. The intent of this article is not to be an exhaustive resource of all legal issues concerning physician practice sales, but to help lawyers and parties to the transaction identify certain potential issues up front so that these issues can be explored further, before they delay or derail a transaction.

Fraud and Abuse Concerns

A variety of state and federal fraud and abuse laws may apply to the sale of a physician practice. For example, in Florida, if a component of the purchase of a practice appears to be in exchange for referrals of health care business, this could implicate both the Federal Anti-Kickback Law ("AKL") for federally paid business, as well as the Florida Patient Brokering Act ("FPBA") for any medical services no matter how paid.[1] These are criminal penalty statutes that generally prohibit the provision of anything of value in exchange for patient referrals.[2] This can become a complex issue because a purchaser of the practice may want to pay for "goodwill," which can mean a lot of things, and/or pay over time for the practice acquisition while the selling physician is still working at the practice or otherwise generating business for the practice. Fortunately, the AKL has a safe harbor for the "sale of practice," which could exempt such payment arrangements from AKL if all the requirements are met.[3] The FPBA provides that if the AKL safe harbor requirements are met, then the arrangement will not violate the FPBA.[4] While the failure to meet a safe harbor does not necessarily mean that the AKL has been violated, a payment arrangement that fails to meet the safe harbor is not shielded from criminal liability.

The sale of practice safe harbor has specific requirements, including that the period from the date of the first agreement pertaining to the sale to the completion of the sale cannot be more than one year. Also, the physician selling the practice cannot be in a professional position to make referrals to, or otherwise generate business for, the purchaser after one year from the date of the first agreement relating to the sale.[5] This safe harbor can be met if all payments are wrapped up in a year. These requirements need to be kept in mind when negotiating potential transition agreements in connection with the sale of a practice, and employment or consulting agreement with the selling physician after the sale. Furthermore, the safe harbor for the sale of a physician practice to a hospital (rather than another type of purchaser) has additional requirements that will need to be met.[6]

Other fraud and abuse concerns that the parties need to consider are whether any physician party (or their immediate family member) involved in the sale of a physician practice refers federally paid business to the other party for "designated health services" as defined under the federal Stark law in any context.[7]

If such is the case, then all of the payment arrangements between the parties related to the sale must meet a pertinent Stark exception. This is because the Stark law is a strict liability civil penalty statute, thus, if it is implicated, all the requirements for an exception must be met in order for there not to be a violation. Depending upon the facts, the Stark Fair Market Value Exception to compensation arrangements may be applicable.[8] This exception, among other things, requires that the compensation be set in advance, consistent with fair market value, and not determined in a manner that takes into account the volume or value of referrals or other business generated by the referring physician.[9] The parties must also consider state fee splitting laws and state self-referral laws, as applicable.[10]

Ownership Restrictions

Another issue to consider is whether any legal restrictions exist on who can own a medical practice. In a majority of the states in the United States, the corporate practice of medicine doctrine places restrictions on persons other than licensed physicians owning medical practices. This doctrine appears in statutes, rules, and opinions and varies from state to state.

In Florida, there are no restrictions on who can own a medical practice. However, a special health care clinic license may be required for owners who are not licensed medical practitioners if the medical practice tenders charge for reimbursement to insurers or government payers and they do not meet one of the statutory exceptions.[11] If a health care clinic license is required but not obtained, it is illegal to operate the medical practice and all charges and reimbursement claims are not compensable.[12]

Accordingly, initial questions that should be addressed in a physician practice transaction are whether the purchaser can legally own a medical practice and whether, in order to purchase the practice, the purchaser must obtain a special license, such as a health care clinic license. If such license is required, the parties need to plan for the time necessary to obtain such license, which could take several months to process. The parties may need to schedule the closing for the date the license is issued to the new owner. Alternatively, if permissible, some parties may enter into an interim management arrangement pending the issuance of the required license. If the parties enter into an interim management agreement, in order to satisfy state regulators and for general health care compliance, it is important that the management arrangement be fair market value, commercially reasonable, and implemented as stated in the agreement.

Licensure

In addition to Florida health care clinic licensure previously discussed, the parties must consider whether the physician practice has other health care licenses that must be transferred or, if not transferrable, must be acquired by the purchaser in order to conduct the business. For example, depending upon the services being provided, a physician's practice could have licenses for its laboratory, dispensing of prescription drugs, radioactive materials, biomedical waste, and laser registrations, as well as other licenses and registrations. Each of these licenses should be examined early in the negotiations of the transaction to determine whether the licenses are transferable and whether transfer or assignment is required, which may depend on whether the sale of the physician practice is a stock or membership interest transfer or whether its assets are being sold to a new purchaser entity. The definition of a change of ownership (commonly called a "CHOW") must be assessed under each licensure law or registration.

Managed Care

Another important consideration in the purchase and sale of a physician practice is whether the practice has any valuable managed care contracts that can be transferred to the purchaser in an asset purchase or maintained by the practice in a stock or membership interest purchase. This is a very fact-specific analysis that depends on the structure of the physician practice sale and the terms of the managed care agreements.

Most parties assume that the managed care contracts will not transfer with the sale of a physician practice. However, in some instances, the purchase of a physician practice can be structured as a stock or membership interest purchase in order to preserve a valuable managed care contract. This may occur, for example, when the managed care contract is in the name of the legal entity whose stock or membership interests are being transferred and the managed care contract is tied to that entity's tax identification number. It is also helpful if the assignment clauses in the managed care contracts do not require payer consent for a change of ownership of the physician practice and do not include a change of ownership within the definition of "assignment" in these agreements.

It is important to note that if the purchaser structures the acquisition of a physician practice as a stock or membership interest purchase in order to attempt to maintain licenses or managed care contracts, then the purchaser should negotiate

for more protections through extensive representations and warranties from the seller and strong indemnification after the closing for breach of the representations and warranties since taking over ownership of the entity (instead of just purchasing the assets through a new entity) creates more potential liability for the new owner.

Government Payer Issues

Purchasers of physician practices should ask the seller whether Medicare, Medicaid, or Tricare liabilities exist. This is especially true if the purchaser plans to take over the Medicare number through, for example, a stock or membership interest purchase, or an assignment of the Medicare number. Successor liability can cause a new and innocent owner of a Medicare number to be required to pay for any Medicare overpayments and penalties of the prior owner of the Medicare number. Also, even if a practice acquisition is structured as a stock or membership interest purchase which may not trigger a new Medicare enrollment, purchasers should make sure that they satisfy any applicable notification requirements. For example, in a stock purchase, the Medicare provider must notify Medicare of the new owners of the practice within 30 days of the closing.

Potential successor liability in a stock or membership interest acquisition is one of the primary reasons an asset purchase is preferred by purchasers in physician practice transactions. If the purchaser of a physician practice intends to form a new entity and purchase the assets of a physician practice, they must obtain a new Medicare or other government payer number. Due to the time involved in obtaining these numbers, the purchaser should start the process early and plan for any interruptions in payments.

Medical Records

Another important issue for the parties to address is how to handle the records of the physician practice. The purchaser of a physician practice may or may not want the records of the prior owners. If the selling physician is retiring, for example, the purchaser of the practice may not want to have to maintain all of the selling physician's voluminous practice records.

The seller, however, may want the purchaser to maintain the records for five years from the last patient contact as required under the Florida rules to the Medical Practice Act,[13] or longer, depending upon the requirements of the selling physician's malpractice insurance. The purchaser may only want the last three years of records because with HIPAA and Florida privacy laws, the maintenance of medical records can be more of a liability than an asset, especially if the records are so old that it is not likely that the patient will return to the practice for medical services after the sale of the practice to purchaser. These are important negotiating points and they can often be addressed in a separate patient records transfer agreement.

The foregoing is not an exhaustive list of the special issues applicable to the purchase and sale of a physician practice. However, it does address some of the issues peculiar to these transactions that the parties commonly have to manage. If the parties keep these issues in mind when contemplating the purchase and sale of a practice, the parties may be able to minimize some of the pitfalls that could derail the closing of their transaction, or a purchaser may be able to more quickly determine whether or not it is in the best interest of the purchaser to close on a particular transaction.

If you have any questions, please contact Erin S. Aebel at eaebel@shumaker.com or 813.227.2357 or Kathleen M. Bickelhaupt at kbickelhaupt@shumaker.com or 813.227.2262.

[1] See, 42 U.S.C.A § 1320a-7b; Fla Stat. § 817.505.
[2] Id.
[3] 42 C.F.R. § 1001.952.(e).
[4] Fla. Stat. § 817.505(3)(a).
[5] 42 C.F.R § 1001.952(e).
[6] Id.
[7] 42 C.F.R § 1395nn.
[8] See, 42 C.F.R § 411.357(l).
[9] Id.
[10] See, e.g. Fla. Stats. § 458.331 (1)(i); 456.053.
[11] See, Florida Statutes Chapter 400 Part X.
[12] Fla Stat. § 400.9935(3).
[13] Fla. Admin Code § 64 B8-10.002(2).

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