



Five Pre-Transaction Considerations for the 21st Century Medical Practice

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Physicians, worried about the changes spurred by healthcare reform, are increasingly shifting from solo / small / independent practices to other practice models and affiliations. Rather than shoulder rising malpractice costs, declining reimbursement rates, and the increased regulatory and administrative burdens of post-reform practice, many private practice physicians are considering selling their practice or affiliating with a hospital or health system or other medical groups as a viable exit option. The trend is pervasive. As of February 2014, approximately 25 percent of surgical subspecialists, 50 percent of surgeons, and 60 percent of internists were employed by hospitals or health systems. In 2013, Merritt Hawkins, the nation's leading physician placement firm, reported that 64 percent of its placements involved hospital employment compared to 11 percent in 2003. The forces driving consolidation are undeniable and the opportunities to sell or affiliate abound.

Yet, physicians should resist the herd mentality and not rush blindly into alternative practice arrangements too quickly. Selling a medical practice, or affiliating with a health system or other medical practice through a joint venture, professional service agreement (PSA), medical directorship, co-management agreement or otherwise, is a significant undertaking that should only be done with careful planning -- including but not limited to internal due diligence by and of the practice.

Below are five action items that the modern medical practice should consider prior to evaluating and entering into a sale or affiliation transaction.

1. The importance of a robust compliance program (not just a plan)

Over the last 15-20 years, most medical practices have heard, read and been told of the importance of a compliance plan -- a specifically designed plan that would assist the medical practice to address privacy, fraud and abuse concerns. In 2000, the HHS OIG published guidelines for individual and small physician practices -- <http://oig.hhs.gov/authorities/docs/physician.pdf> -- yet 14 years later very few medical practices have a written compliance plan and even fewer have a robust, actively engaged compliance program, which includes training, testing and a forward-facing proactive stance regarding compliance. All medical practice purchasers will conduct due diligence to determine the status of the practice's compliance program, but so will other savvy partners. Hospitals and other medical practices considering joint ventures, professional service agreements or even medical directorships place significant value on medical practice partners who place compliance efforts as a demonstrable cornerstone of the business operations.

Action items:

- Establish a robust privacy, fraud and abuse compliance program; or revisit the current compliance program.
- Schedule periodic (at least annual, and part of every new hire orientation) training and updates to the compliance program. In-service / lunch and learn lessons can be easily organized and demonstrate to practice employees the value of compliant operations.

2. Confidence in the Practice's Billing and Collections

Along the integration spectrum, medical practice sales and professional service agreements reflect the highest level of integration. In both instances, the quality of the medical practice's billing and collection efforts drives not only acquisition pricing, but also amounts paid under PSAs for services rendered. If the medical practice can demonstrate superior ability with its own billing and collection efforts, there is a greater likelihood that the practice may be provided with post-transaction billing and collection service options. When considering an integration with another medical practice, it is important to have confidence in the capabilities (and shortcomings) of each partner so that an educated decision can be made with regard to which entity will shoulder those responsibilities going forward.

Action items:

- Schedule a professional review of the practice's billing and collecting efforts (consider conducting such a review under the attorney-client privilege).
- Schedule annual training of billing and collecting personnel.
- Actively review improvement against defined metrics.
- Schedule a professional review of the practice's medical record documentation.
- Schedule annual training for all personnel with medical record documentation responsibility.

3. Running a Marathon, Not a Sprint

Physicians, who have worked for decades to build a medical practice, often rush to finalize a sale or affiliation, neglecting the most important part of the transaction—the timing of when to sell or affiliate. Physicians often force a sale or affiliation at the worst time—after years of declining profits—when the practice is at its lowest value. It's best to sell or explore affiliation options when a practice is at its peak, before profits are expected to decline and while assets are well-maintained. But, if this peak has passed, waiting and retooling a practice for efficiencies may generate a larger purchase price. Simply retaining the status quo is obviously not a winning strategy.

Timing the purchaser's desires helps as well. If a local health system is beginning to evaluate its affiliation options, the medical practice may gain some advantages by willing to partner with the system early, working together to iron out the unknowns rather than waiting until all the unknowns are identified and worked out.

Action items:

- Identify the practice's immediate options in the context of the marketplace's evolution -- including but not limited to meeting with leadership from the other healthcare provider to discuss (within legal confines) the evolving marketplace and the delivery of care under current and future models.
- Identify "Plan B" for the coming 24 months. ("The best laid schemes of mice and men / Often go awry." - John Steinbeck) Despite the practice's best intentions, the Plan A identified at Item 1, above, may be postponed or removed from consideration. In such an instance, it will be important for the practice leadership to be able to pivot quickly to the next alternative -- for example, instead of a PSA arrangement with Health System X, pivot to a merger with Medical Practice B; instead of a medical directorship, pivot to a recruiting agreement; instead of a medical directorship, pivot to a co-management agreement.
- Under each element, consider what the practice's "walk away" requirements are -- either in terms of an affiliation, acquisition, or joint venture.
- Evaluate and repeat quarterly.

4. Don't forget the IT Interface and / or Upgrades

Many medical practices may elect to postpone IT upgrades, citing costs (both direct and indirect) affiliated with such.

If, (after conducting the 2014 Action Items under Section 3, above) the medical practice is not contemplating a sale to a new owner in the next 12 months, then consider upgrading the current IT systems to provide greater operational efficiency. If (after conducting the 2014 Action Items under Section 3, above) the medical practice is contemplating a sale or high level affiliation with another provider, consider whether the respective IT systems will work together (with all features operable) and/or whether the parties will need to explore a new IT system better suited to the subject affiliation.

Action items:

- Evaluate current IT systems; identify systems used by likely partners identified in Item 3, above.
- Review IT service agreements to determine termination options, assignability, modification to add new partners to the current service.
- Review IT service agreements as a party of Items 2 and 3, above -- conduct HIPAA Security Testing Audits; review ICD-10 readiness.

5. Ultimate Value is Derived from Productive Work

Whether a medical practice is considering a sale, a PSA, or a group practice affiliation, the owners must understand that the value accorded to the practice is going to be based upon actual, historical, productive work. Evaluate the use of mid-level providers (applying Sections 1 and 2, above) to increase efficiency; consider participating in an accountable care organization or clinically integrated network in order to expand.

Action items:

- Evaluate the practice's productivity and immediate action available to increase each provider's productivity on a month by month basis.
- Consider locking in current value, while maintaining flexibility by way of a PSA, co-management or joint venture arrangement.

The healthcare industry will continue to evolve in 2014 and beyond. The modern medical practice will proactively position itself to take aggressive advantage of these changes. Committing resources today to the growth and future of the practice will benefit the constituents -- patients, employees and owners.

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