



Legal Considerations for Healthcare Private Equity Firms Entering Into the Healthcare Industry

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Private equity firms continue to target the healthcare industry. In fact, this industry has seen tremendous growth over the past decade. The Centers for Medicare and Medicaid Services believes that national healthcare spending will rise to 20% of GDP by 2026.¹ Moreover, according to a recent report issued by PricewaterhouseCoopers, private equity activity in healthcare has steadily progressed from over two hundred deals in 2009 to over six hundred in 2017.² This trend is projected to increase to over seven hundred deals in 2019. The driving force behind this growth includes factors such as: (1) the realization of economic value in a fragmented healthcare industry/market, (2) the shift from a fee-for-service reimbursement model to a value-based model seeking increased efficiencies, (3) an aging population requiring more healthcare services, (4) healthcare consumerism (*i.e.*, improvement and promotion of patient experience), and (5) opportunities for innovation.

There are a number of areas within the healthcare industry that private equity firms have identified as fiscally lucrative. These areas include, for example, post-acute care (*e.g.*, hospice, home health), physician practice management (*i.e.*, also known as management services organizations), dermatology, veterinary medicine, optometry, physical therapy, and behavioral health. Despite private equity's desire for a considerable return on investment, healthcare creates unique challenges, particularly with respect to regulatory issues. Such regulatory issues may include the corporate practice of medicine prohibition, fraud and abuse implications, and licensure (*e.g.*, change of ownership) limitations. To reduce liability, private equity firms should scrutinize the target entity's compliance program, conduct coding and billing audits of the target entity, review the target entity's relationships with referral sources, identify whether the target entity has been subject to government investigations, determine if the target entity has been the victim of privacy or security breaches, and review the target entity's licenses and third party payor contracts for requisite consents and approvals.

In light of private equity's fervent activity in healthcare, here are 5 tips private equity firms should remember when negotiating a deal in the healthcare industry:

1. It is imperative that both parties understand the goals and objectives of the other party to the transaction prior to entering into any definitive agreements. This mutual understanding will help facilitate a "win-win" for both parties.
2. There is no "standard" Non-Disclosure Agreement ("NDA"). Rather, if you've seen one NDA, then all you've seen is one NDA.
3. Strongly consider including exclusivity language in the Letter of Intent. In this way, the target entity will be restricted from negotiating or soliciting offers from other potential buyers for a certain period of time.
4. Pay attention to "boilerplate" contractual provisions (*e.g.*, governing law, forum, etc.). If these provisions are inadvertently overlooked, you could potentially find yourself in a foreign jurisdiction and searching for unfamiliar legal representation.

¹ Centers for Medicare and Medicaid Services, *CMS Office of the Actuary releases 2017-2026 Projections of National Health Expenditures* (Feb. 14, 2018), <https://www.cms.gov/newsroom/press-releases/cms-office-actuary-releases-2017-2026-projections-national-health-expenditures>.

² PwC, *Private equity: Healthcare's new growth accelerator* (December 2019), https://www.pwc.com/us/en/industries/health-industries/top-health-industry-issues/pe-in-healthcare.html?WT.mc_id=CT3-PL300-DM1-TR1-LS40-ND40-TTA9&eq=CT3-PL300-DM1-CN_HealthServices-Google.

5. In any healthcare transaction, parties typically do not want to contemplate the prospect of “divorce” prior to “marriage.” However, it is vital that the parties consider how to unwind the assets and dissolve the relationship; otherwise, the separation can become quite messy. Think of it as a prenuptial agreement between the parties. Nonetheless, it is an unfortunate reality that some business combinations simply are not meant to be.

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