

The background of the slide is a dark blue gradient with a series of bright, multi-colored streaks (red, orange, yellow, and blue) that appear to be light trails or motion blur, creating a sense of speed and direction. The streaks originate from the top right and fan out towards the bottom left.

Morgan Lewis

HEALTHCARE

Mergers & Acquisitions

**M&A ACADEMY: RED FLAG? GREEN LIGHT? OR JUST
YELLOW ALL THE WAY? NAVIGATING THE TRAFFIC ON
HEALTHCARE TRANSACTIONS**

**Janice Davis
Banee Pachuca**

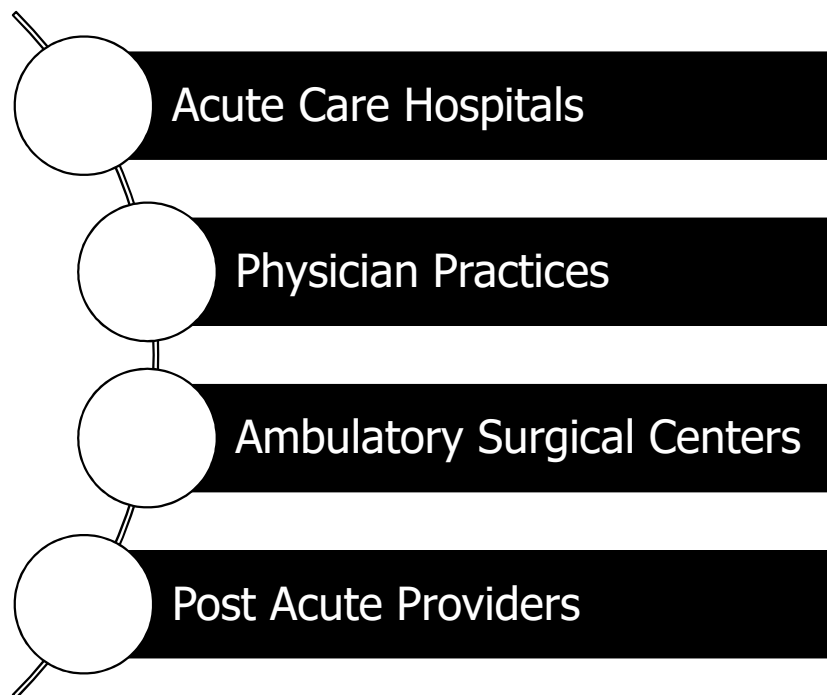
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AGENDA

- Healthcare Transaction Trends
- M&A Transactions-General
- Considerations in Structuring Transactions
- Due Diligence Issues
- Other Select Issues in Healthcare M&A Transactions

SECTORS INVOLVED IN HEALTHCARE M&A INDUSTRY



Deal volume, value, and year-over-year growth, 2019

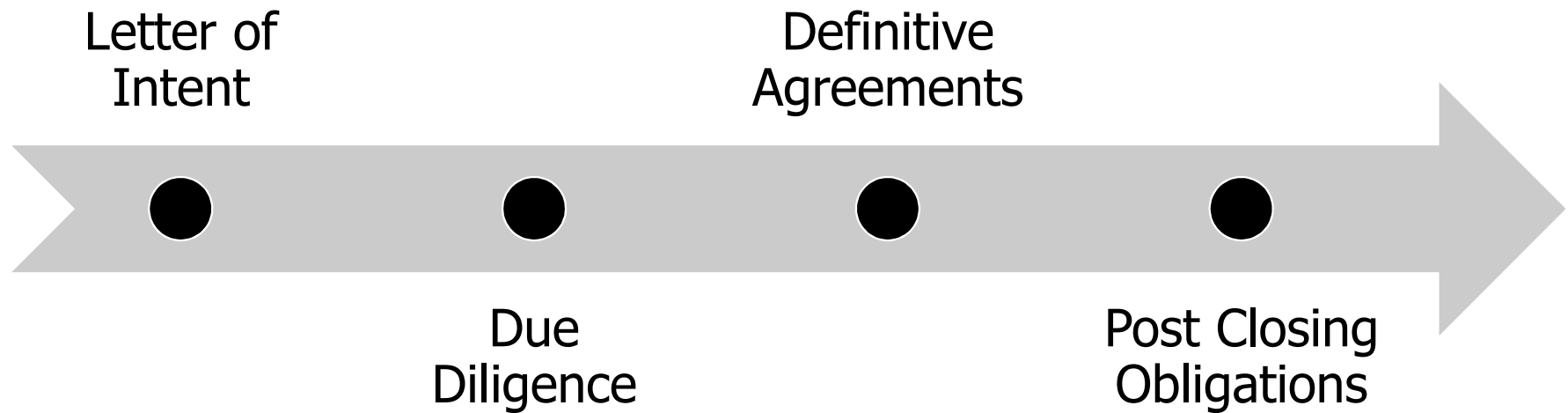
No. of Deals	Deal value (\$ billions)	YoY deal growth, by:	
		Volume	Value
201	Other Services \$21.2	10%	(72%)
27	Managed Care \$19.2	8%	597%
437	Long-Term Care \$16.6	2%	22%
95	Hospitals \$15.8	19%	31%
48	Labs, MRI & Dialysis \$10.1	0%	503%
219	Physician Medical Groups \$6.2	(14%)	(49%)
89	Home Health & Hospice \$1.5	5%	(55%)
74	Behavioral Care \$0.4	(19%)	(82%)
31	Rehabilitation \$0.2	(28%)	82%
1,221	\$91.2	(1.5%)	(27%)

Source: Deal Search Online and Health Care M&A News (January, 2020), www.HealthCareMandA.com

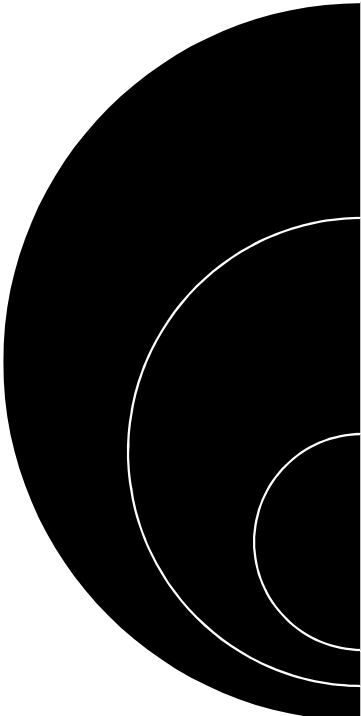
MARKET TRENDS

- 2019 saw continued robust healthcare M&A activity. Not confined to one sector or type of service.
- Buyers are being more selective about which organizations they choose to acquire, both in the for-profit and not-for-profit space. More hospitals and health systems are entering into informal partnerships.
- 2019 brought increased M&A activity in sectors such as behavioral health, healthcare IT, and post-acute. Slowdown in home health M&A but diverted investment in hospice.
- Many of the hospital and health systems activity represented regional alliances or consolidations. Hospital systems continue to use M&A as a tool to better coordinate care, expand the scope of services to patients, and reduce challenging administrative burdens.
- PE firms continue to inject capital into the healthcare industry.
- Impact of COVID-19

KEY STAGES OF AN M&A TRANSACTION

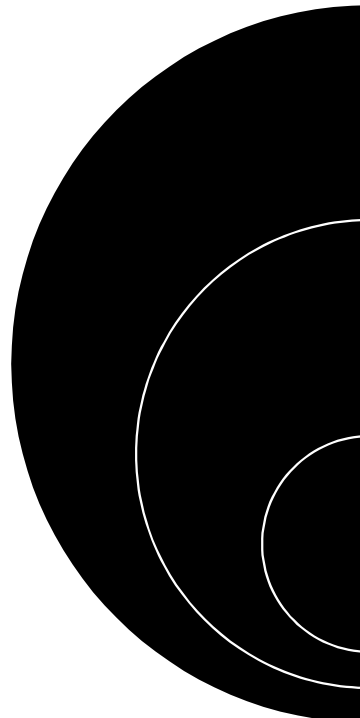


CONSIDERATIONS IN STRUCTURING A TRANSACTION



Tax Considerations	<ul style="list-style-type: none">• Buyer and seller tax considerations• Short and long term issues
Transaction Form	<ul style="list-style-type: none">• Asset v. Equity Transaction• Merger• Member Substitution Transaction
Commercial Issues	<ul style="list-style-type: none">• Third Party and Corporate Consents• Deal Process and Timing

SPECIAL CONSIDERATIONS IN HEALTHCARE TRANSACTIONS



Corporate Practice of Medicine (CPOM)	<ul style="list-style-type: none">• Friendly Physician Model• Foundation Model
Fraud & Abuse	<ul style="list-style-type: none">• Earnouts• Stark Law / AKS
Licensing and Enrollment	<ul style="list-style-type: none">• Change of Ownership (CHOW)• Certificate of Need (CON)

EARNOUTS AND CONTINGENT PAYMENTS

- Common in non-healthcare transactions
- Portion of the purchase price is contingent on the future financial performance of the target business
- Payment is contingent on a future event, such as exceeding a specified gross revenue, net income, or EBITDA
- Incentives to increase revenues or earnings can present risk under fraud and abuse laws
 - Prohibited in some circumstances
 - May create material risk if not prohibited
- Must ensure that earn-out structure is permissible under applicable fraud and abuse laws.

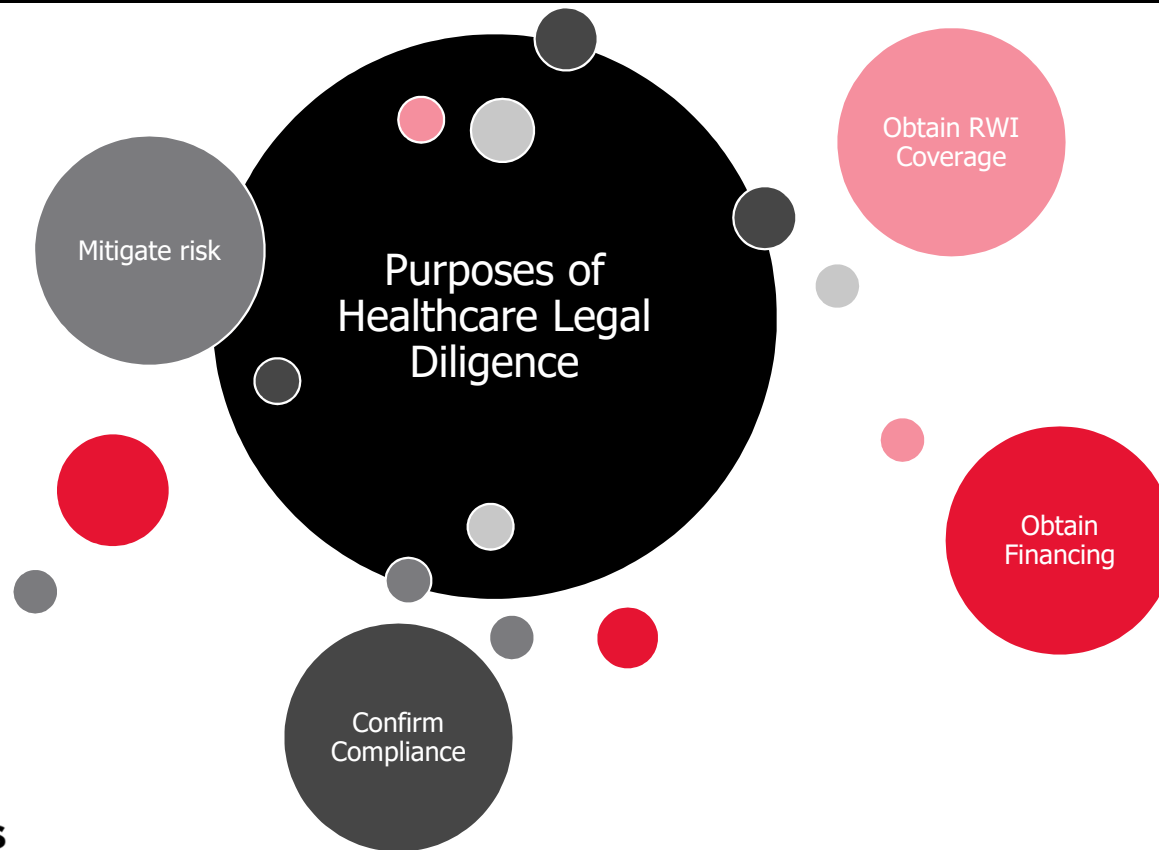
ANTI-TRUST CONSIDERATIONS

- The FTC and DOJ have placed increased scrutiny on healthcare transactions that involve consolidations or affiliations.
- Analyze early whether the transaction may adversely affect competition.
- State laws that require pre-transaction notification.
- DOJ Antitrust Division issued a business review letter that underscores the flexibility of US antitrust regulators towards competitor collaborations aimed at increasing supply and distribution of medical equipment to fight COVID-19.

CHANGE OF OWNERSHIP (CHOW) CONSIDERATIONS

- Medicare program is a health insurance program administered by the federal government benefitting the elderly and disabled, and Medicaid program is a health insurance program administered by states benefitting low-income individuals
- Many providers and suppliers are dependent on payments from governmental programs
- Providers that furnish services reimbursed under Medicare Part A (e.g. inpatient care furnished by hospitals, care in SNFs, hospice care, and home health services), and Medicare Part B, such as hospitals furnishing outpatient services, ASCs, durable medical equipment companies, clinical laboratories, and outpatient rehabilitation clinics
- The classification of an M&A transaction determines:
 - timing and process for regulatory notices and approvals
 - whether there will be an interruption in Medicare billing and payment for the provider's services
 - whether successor liability for pre-closing overpayments and penalties will attach

HEALTHCARE DILIGENCE



COMMON AREAS OF HEALTHCARE DILIGENCE



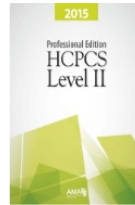
Compliance Program



Payor Agreements



Fraud and Abuse



Billing and Coding



Licensure / CPOM



Privacy

COMPLIANCE PROGRAM

- Seven elements of an effective compliance program:
 - 1. Written policies and procedures
 - 2. Compliance professionals
 - 3. Effective training
 - 4. Effective communication
 - 5. Enforcement of standards
 - 6. Internal monitoring
 - 7. Prompt response

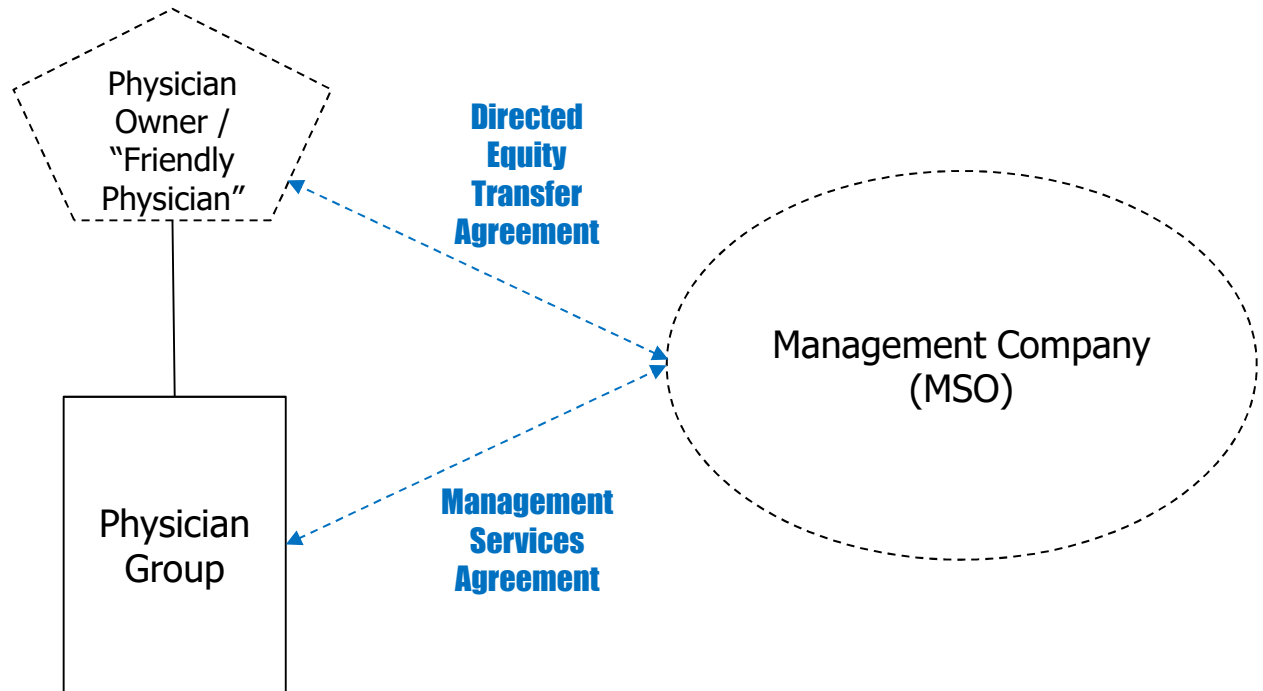


FRAUD AND ABUSE: STARK LAW / ANTI-KICKBACK STATUTE

- Stark Law:
 - Physician may not refer Medicare/Medicaid patients to a DHS entity if the physician or immediate family member of the physician has a financial relationship with the entity
 - DHS entity cannot bill for the services
 - Unless the financial relationship qualifies for an exception
 - Strict liability statute; intent is irrelevant
- Anti-Kickback Statute:
 - Prohibits the willful and knowing offer, solicitation, payment, or receipt of any remuneration, directly or indirectly for:
 - Referring an individual covered by a government health program or arranging for such a referral; or
 - Purchasing, leasing, ordering, arranging for, or recommending the purchase, lease, or order of any good, facility, service, or item covered by a government health program
 - Criminal statute; intent is a key element of liability

LICENSURE / CORPORATE PRACTICE OF MEDICINE

- CPOM prohibits certain relationships between physicians and non-physician owned entities, including:
- CPOM is a state law licensure issue



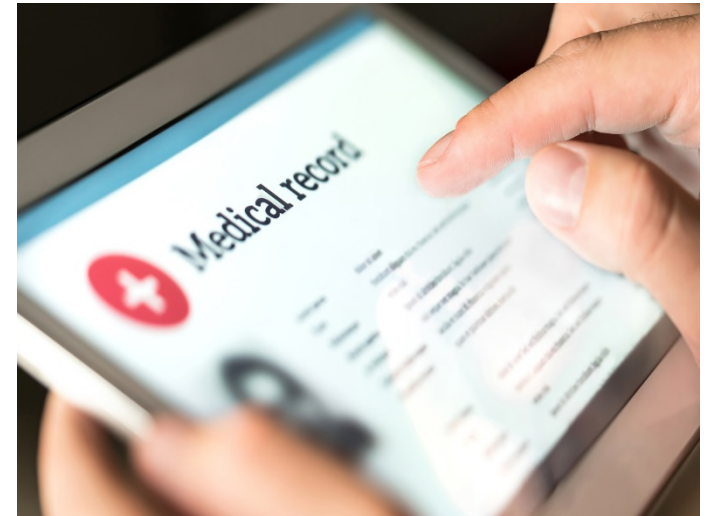
PAYOR AGREEMENTS / BILLING & CODING

- Notice / consents required by commercial payors
- Confirmation of historical audits
- Review a sample of claims for compliance with Medicare billing rules



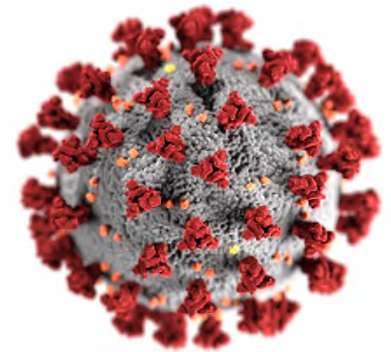
PRIVACY COMPLIANCE

- Health Insurance Portability and Accountability Act of 1996 (HIPAA) and its implementing regulations govern the use of patient health information
- Part 2 Regulations apply to certain substance abuse records
- State privacy laws



DUE DILIGENCE – COVID'S IMPACT ON APPLICABLE LAWS

- Stark Law
 - [Blanket Waivers](#)
- Federal Anti-Kickback Statute
 - [OIG Policy Statement](#)
- Licensure
 - Waiver of licensure requirements for providers and facilities
 - Prohibition on the provision of elective, non-urgent procedures
- Reimbursement
 - Requirements for telehealth services

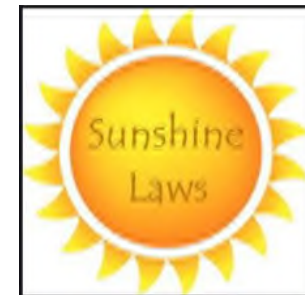


TRANSACTIONS INVOLVING NONPROFIT ENTITIES

- Attorney General (AG)-General Review of Transactions Involving Nonprofit Entities
 - Rules differ greatly among the 50 states
 - Formal review process, and even post-transaction monitoring
 - AG Review of Nonprofit Transactions Involving For-Profit Entities
- General Focus of AG Review
 - Valuation
 - Private Benefit
 - Charitable Use of Proceeds
- Determine appropriate time to notify the AG

TRANSACTIONS INVOLVING GOVERNMENT HEALTH CARE ENTITIES

- Government Entities have their own set of issues
- Subject to state open meetings and open records statutes – Sunshine Laws
 - ❑ Texas: Texas Public Information Act (PIA)
 - ❑ Texas: Open Meetings Act
 - ❑ Exceptions:
 - Trade secrets
 - Confidential commercial or financial information-disclosure would cause competitive harm to the business
 - Information that, if released, would give advantage to a competitor or bidder
- Political aspects as Board members are sometimes elected by the public



REPRESENTATIONS AND WARRANTIES INSURANCE FOR HEALTHCARE M&A

Historically, obtaining R&W coverage for transactions involving healthcare providers was challenging.

Carriers did not want to assume risks for violations of U.S. and state healthcare regulatory laws, primarily risk associated with Medicare and Medicaid billing and reimbursement practices (False Claims Act violations), Anti-Kickback and Stark laws.

2014

In 2014, Aon introduced R&W coverage for healthcare transactions using a unique underwriting process involving primary healthcare diligence.

- Market largely limited to one carrier providing a side-car R&W policy for healthcare coverage (underwritten via a primary diligence process) to a standard R&W policy (i.e., two RWI policies)
- Other carriers more selective on healthcare
- Only 2 carriers (Concord Specialty and Ironshore)

NOTE: Slides 21, 22 and 23 are provided with the permission of AON.

2020

Current market much deeper with more carriers (more than 13) providing RWI for healthcare transactions.

Carrier interest influenced by:

- Provider type
- Government payor exposure
- Availability of audited financials
- Size of provider and scope of operations
- Compliance history and operation

HEALTHCARE REGULATORY DILIGENCE FOR RWI

Carriers expect fulsome diligence on healthcare regulatory matters

- Federal False Claims Act, Stark Law, Anti-Kickback Statute, HIPAA
- Billing / coding compliance and medical necessity – claims sample review (75-100 records)
 - Focused on government payor reimbursement (Medicare, Medicaid, etc.)
 - Understand error rate compared to industry
- Determining overall effectiveness of compliance infrastructure and program (compliance culture)
 - OIG’s Compliance Program Guideline for the 7 essential elements of an effective Compliance Program

Scope of Diligence

- Financial arrangements and referral sources
- Employment, physician and independent contractor arrangements
- Real estate leases
- FMV analysis as applicable
- Sales and marketing activities
- Internal / external compliance audits
- Compliance program – policies, procedures, Chief Compliance Officer
- HIPAA – policies, security assessment, prior breaches, BAAs, training
- Licenses, permits and excluded provider testing
- Payor contracts – commercial,
 - governmental, fee-for-service, capitated rate

COMMON RISKS IN HEALTHCARE SERVICE/PROVIDER TRANSACTIONS AND AVAILABILITY OF RWI COVERAGE

Exposure	Availability of RWI coverage
Government-payor reimbursement	Yes, from certain markets, and subject to diligence, including a clean third-party billing/coding audit of claims sample
Private-payor reimbursement risk	Yes, subject to standard diligence
Regulatory risk (e.g. Stark, AKS)	Yes, subject to standard diligence
Data Privacy/Cyber/HIPAA	Yes, subject to standard diligence; may attach excess of (and no broader than) underlying cyber coverage depending on carrier
Corporate practice of medicine	Yes, subject to standard diligence
Medical malpractice/ bodily injury	Typically excluded, with limited exceptions (presumed to be covered by other insurance); if covered, will attached excess of (and no broader than) underlying medical malpractice coverage

POST CLOSING OBLIGATIONS

- Updates to CMS / Medicaid
- Notifications to licensing agencies
- Commercial payor notifications
- Restructuring of any problematic arrangements identified during diligence
- Implementation of compliance program

KEY TAKEAWAYS FROM THIS SESSION

- Businesses in the healthcare industry are regulated by a wide array of federal and state laws enforced by various specialized regulatory agencies. Violation of these laws can subject parties to these healthcare transactions to onerous sanctions, including criminal penalties.
- Not all healthcare targets are the same. It is very important that the team understands the business of the target.
- Assemble a team of lawyers who are familiar with healthcare transactions, particularly a healthcare regulatory attorney as well as a corporate transactional attorney who is familiar with healthcare transactions. Because healthcare is such a highly regulated industry, all aspects of a transaction should be evaluated from a healthcare regulatory perspective.
- Diligence in a healthcare transaction is very important. It helps mitigate risk for a buyer, and it will be necessary for a buyer to obtain financing or RWI coverage.
- Certain healthcare transactions result in successor liability, regardless of how the transaction is structured.

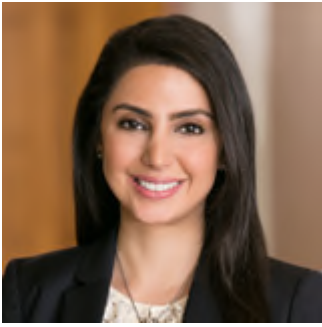
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Janice Davis has a broad-based corporate practice with an emphasis on mergers and acquisitions, corporate and securities law, and private equity and venture capital transactions. In the healthcare area, Janice represents hospitals and health systems, academic medical centers, managed care companies, and other health care and life science companies in implementing innovative integration and alignment strategies. She has extensive experience in leading significant transactions, including mergers, acquisitions, distressed acquisitions and dispositions, joint ventures, affiliations, private placements, and asset and stock purchases and sales for clients throughout the healthcare industry.

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Banee Pachuca focuses her practice on healthcare law, including transactional, regulatory, and compliance matters. She represents hospitals, health systems, academic medical centers, large physician groups, and private equity and financial investor clients in mergers, acquisitions, divestitures, joint ventures, and other collaborative and alignment strategies. Additionally, Banee frequently advises clients with respect to fraud and abuse laws, including the Stark Law and state and federal anti-kickback laws, billing compliance, as well as state and federal privacy laws. She assists healthcare clients with internal investigations, analyzing potential self-disclosures, responding to government subpoenas, and developing compliance programs.

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