New Jersey Law Journal

VOL. 206 - NO 1 OCTOBER 3, 2011 ESTABLISHED 1878

IN PRACTICE

HEALTH CARE

Navigating a Health-Care M&A Transaction

When a corporate lawyer needs a health-care lawyer

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Attorneys involved in transactions concerning mergers, acquisitions and disposition of business interests (M&A transactions) frequently represent businesses across a range of industries. When an M&A transaction involves an entity in the healthcare industry, there are a number of issues that need to be considered which are outside of, or different from, the normal scope of an M&A transaction. Whether the subject business is a provider of health-care services, like a hospital or a magnetic resonance imaging facility, or simply provides goods or services to a health-care provider, an attorney advising clients with health-care M&A transactions needs to be aware of the implication and effect of health-care laws and regulations. This article highlights some of the health-care-specific issues that may arise in connection with a health-care M&A transaction.

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M&A transactions often require the input of an attorney who is well-versed in specialty areas such as tax, securities and ERISA. When handling a transaction involving a health-care provider or supplier, the transaction will also benefit from the input of an attorney with knowledge of health laws and regulations. At the outset of a health-care M&A transaction, it is important to understand the potential effect on the transaction of the Health Insurance Portability and Accountability Act of 1996, as amended (HIPAA). HIPAA is a federal law that addresses the use and disclosure of individuals' health information by organizations subject to the act.

Generally speaking, most M&A transactions begin with a confidentiality agreement among the key parties to the potential transaction. During a potential buyer's due diligence examination of a health-care provider or supplier's business, the buyer may receive and have access to health information protected under HIPAA. The typical nondisclosure agreement used in a nonhealth-care related M&A transaction may not comply with the requirements of HIPAA and may not sufficiently protect the parties from the risks of a HIPAA violation. Depending on the circumstances, the seller may want to utilize a separate business associate agreement with the potential buyer, or incorporate HIPAA-specific provisions into the standard nondisclosure agreement. For example, the recipient of the protected health information should agree to report to the seller any use or disclosure of the information of which it becomes aware. In turn, the seller may want to make clear that, to the extent any unauthorized use, disclosure or access is caused by the recipient or someone acting on his behalf, the recipient will be responsible for the payment of any expenses associated with the HIPAA Breach Notification Rule, as well as any fines or civil monetary penalties imposed on the seller as a result of such unauthorized use, disclosure or access.

In the early stages of a transaction, special attention needs to be given to the structure of the transaction and the consideration to be paid to the seller. While private parties in an M&A transaction in a nonregulated industry are generally free to negotiate the structure and terms of their deal, health-care providers and suppliers need to be careful not to run afoul of any applicable federal or state antikickback and similar laws. These laws are intended to protect patients and the federal health-care programs (e.g. Medicare) from fraud and abuse. The federal Anti-Kickback Statute (42 U.S.C. § 1320a-7b) (AKS) generally prohibits a person or entity from paying for a referral concerning a health-care product or service for which payment is to be made by any federal health program, including Medicare or Medicaid. Violations of the law include monetary

and also criminal penalties.

Not all violations of antikickback laws are clear-cut, as the laws could be implicated in subtle ways in an M&A transaction. For example, it is not uncommon to see an "earn-out" provision in an M&A transaction in which the seller may be paid additional consideration based on the success of the business post-closing. An earn-out structure in an M&A transaction involving the sale of a physician practice, however, could easily run afoul of antikickback and other related laws. Also, M&A transactions are occasionally accompanied by separate real estate transactions because the principals of the seller may hold the real estate directly. Any such separate transactions (e.g., sale of real property, or lease transactions) must be scrutinized to evaluate their impact on any antikickback analysis of the deal.

In addition to AKS, other applicable laws to consider when structuring the transaction include the Stark Law (42 U.S.C. § 1395nn) and Regulations (42 C.F.R. § 411.350, et seq.); the AKS Safe Harbor Regulations (42 C.F.R. § 952.1001); New Jersey's Codey Law (N.J.S.A. 45:9-22.5) (prohibiting self-referrals by health-care practitioners) and its implementing regulation, N.J.A.C. 13:35-6.17; and the New Jersey Anti-Kickback Law (N.J.S.A. 30:4D-17(a)-(d)). These laws may not apply in each case, and various exceptions and recognized safe harbors do exist.

Another concern arising in the early stages of a health-care M&A transaction is the health-law-specific due diligence that needs to be considered by the buy side of the transaction. The business of providing health-care services is a highly regulated industry. The buyer's counsel will want to add a number of health-care-specific items to its standard due diligence request list. Some of these items will include obtaining copies of the target's HIPAA policies and procedures, business associate agreements, compliance policies and a description of marketing practices, and getting a list of accreditations of the business and its employees. When reviewing material contracts, the buyer will want to pay particular attention to agreements with third-party payors, including private insurers and HMOs, and identify whether the target holds an interest in or participates in any associations, such as an independent practice association. Such agreements and arrangements may affect the rates that the target receives for its services, and may not be assignable to the buyer.

A major focus of due diligence relates to the licenses that may be required for the operation of the business, and the regulatory approvals necessary for closing the transaction. The State of New Jersey generally requires an entity providing health-care services to be licensed, with the licensing requirements varying by the type of services being provided. Some licenses are only valid for specific geographical locations (e.g., a license to provide home health services). Transfers and assignments of licenses, to the extent permitted, typically require the approval of — or at least notice to — one of the New Jersey regulatory authorities, such as the Department of Health and Senior Services. Counsel will need to be familiar with the licensing requirements specific to the business involved in the M&A transaction.

For businesses participating in a federal health program, such as Medicare or Medicaid, the parties will need to provide notification to, and possibly obtain approval from, the Centers for Medicare & Medicaid Services (CMS). Failure to comply could impact an organization's ability to receive reimbursement for services from Medicare and Medicaid. A threshold question in these transactions is whether or not the buyer intends to acquire the seller's Medicare provider agreement and provider number. A buyer who acquires a provider agreement and number, even as part of an asset sale, typically inherits any liability associated with that provider number. For example, if the seller received Medicare overpayments prior to the time the transaction closed, CMS may assert the liability against the new owner and may withhold future reimbursements until the liability is satisfied. Accordingly, evaluating the need to acquire the existing provider number is a critical piece of the due diligence and structuring process.

When applicable, the additional requirement of licensing notification and approval will impact the timetable of the transaction. Unlike nonregulated M&A transactions, which can often be signed-up and closed on the same day, most health-care deals will be subject to a gap between signing and closing while the licensing process is underway. Depending on the type of health-care provider and the applicable licensing requirements, the gap can be lengthy and indeterminable. Counsel needs to factor in these issues when preparing the purchase agreement and setting up a timetable for the transaction.

The foregoing highlights some of the structuring, due diligence and closing issues that may be unique to M&A transactions involving health-care businesses. Not all of the possible issues are addressed. The key item to remember is that when handling an M&A transaction involving a health-care business, an attorney should take care to review the health law rules and regulations that apply in the particular circumstances and consult a specialist in the area, if necessary. ■