In-Network

Healthcare Industry News from Investors Bank

Issue 2 | June 2018

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Private Equity Knocking? What to know before you invite them in.

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A recent trend on the rise within the healthcare industry is Wall Street private equity firms buying out Main Street medical practices for substantial amounts of money. These offers have prompted doctors to sell their practices. Two things need to be kept in mind before accepting:
1. Will double taxation apply?
2. How will the sale of goodwill be taxed?
Those who need to proceed with caution are C corporations. When a private equity firm purchases the assets of a C corporation, the proceeds are received by the corporation. Corporate tax is paid on the net gain of the asset sale, and the remaining proceeds are distributed to the shareholder physicians as a dividend. Personal income taxes are imposed on the dividends received by the physicians. Since the corporation cannot deduct the dividends paid to the physicians, and the physicians pay personal taxes on the dividends received, the same money is taxed twice, hence the term "double taxation". Without proper planning the results can be disappointing when the tax bite is larger than expected. Taking steps now may avoid the double taxation trap.

When private equity firms purchase medical practices the sales price is allocated among hard assets, such as furniture and equipment, and intangible assets such as goodwill. Goodwill results when one company acquires another for a premium value. In many instances, the goodwill of the practice can be a large piece of the purchase price. Goodwill is classified as a capital asset. Goodwill is taxed at preferential rates, when it is a personal asset. However, if goodwill is a corporate asset, there are no preferential rates. The ownership of goodwill has a long history of debate in tax law. Is it owned by the corporation? Or the shareholders? The answers can be complex. The goal is to structure the deal so preferential capital gains treatment of the goodwill results.
To avoid the double taxation, you should focus on how the offer is structured:
1. Structure the sale so that the buyer has a post-purchase consulting/non-compete agreement with the shareholder who claims the personal goodwill.
2. Document that the shareholder selling the goodwill has a strong history or expertise with the customers and key-suppliers.
3. The selling shareholder should never sign a non-compete or post sale employee agreement with the selling company.
4. Obtain independent appraisals on the value of personal goodwill and any noncompete agreement.
Other solutions I have offered my clients is consider practicing as a S corporations or a limited liability company. Again, these solutions are long-term, so early planning is key to successful implementation.

Deirdre Hartmann specializes in healthcare advisory services and personal and business income tax planning. She is a frequent lecturer, writer and advisor for medical practices and facilities on a wide range of topics including practice efficiency, revenue cycle analysis, analyzing physician contracts, year-end tax tips, and information systems for physician practices. Reach her at 973.328.1825 or dhartmann@nisivoccia.com

Our team can help busy physicians and healthcare professionals get solutions to fit the needs of their practice.

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An Action Plan for Plugging Profit Leaks in Your Practice

By Marc H. Lion, CPA, CFP

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The current healthcare environment has created an increasing need for the traditional and specialty medical practice to strive toward improving its operational efficiencies in an effort to enhance the bottom line. The end result for a medical practice's physician owners and employees is to improve their income and quality of life. This can be an uphill battle as most physician owners, although highly intelligent and educated, enter the business of medicine without any formal business training and are often unprepared to manage the practice they have started. To begin improving operational efficiencies, the first order of business is to better understand your practice from your own perspective. I know this sounds simple, but it is harder than one would think. You need to ask yourself: What were the reasons that you started your practice? What are your goals and ambitions? Most importantly, what are the sources of your frustrations, obstacles and profit "leaks"? During this process, it is imperative that you incorporate two key elements: One, write down your conclusions, so that you can reference them and start developing your Strategic Action Plan (SAP); and two, develop your team with a focus on accountability.

Developing a Strategic Action Plan

How do you start to develop your SAP? Begin with the end: Define your quality-of-life and income goals, and then work your way backwards. Once you've defined these goals, you can create a plan -- and set a timeline -- to achieve them. Next, you'll need to complete an assessment of your practice, where you'll no doubt uncover multiple inefficiencies and profit leaks. You'll soon become aware that to "fix" your business, you'll need to implement "change." Change must be embraced not only by yourself, but by other members of your team -- and it is human nature to resist change. Another obstacle you may encounter will be the amount of time it will take to implement change. If you have been in practice for many years, it is likely that it took time to develop the inefficiencies within the practice. Accordingly, it will take time to fix them. After you've identified the inefficiencies, you will need to develop a system to correct them and them develop accountability by creating a form of measurement that can be monitored.

Plugging Up "Profit Leaks"

Fixing a so-called profit leak doesn't necessarily mean simply cutting staff or expenses. Profit leaks most commonly occur in billing and collections, fiscal management, human resource and practice growth. Let's look at specific areas that warrant a review during the assessment of your practice.   Billing and Collection. This is a primary area of opportunity for income optimization. Proper coding practices, documentation, charge capture and efficient utilization of technology, such as patient management systems or electronic medical records, should be analyzed for accuracy and consistency. The ability of your front desk to properly capture information and translate this information with precision to your internal or external billing department is imperative. Errors occurring at the front desk -- or shall I term it the "front lines" -- tend to go unnoticed or unaddressed until a patient's billing has already made its way through the collection process. A system of denial management should also be incorporated: After a claim is denied, you must track why it was denied and look for patterns rather than just resubmit the claim. Monitoring accounts receivables will enable you to keep track of your aged receivables in order to reduce the number of days an outstanding claim remains unpaid. Fiscal Management. Establishing a financial budget for your practice will help you manage your cash flow, and set parameters for your ability to make future investments in new equipment and technology. Tracking and monitoring your financial statements can improve your ability to measure profit centers -- and profit leaks -- that exist in your practice. Accurate financial reporting will help you to establish benchmarking to compare your practices' financial health to that of similar practices, or compare your practice's revenue and expenses with the prior year's performance to help identify areas of concern.

Marc H. Lion CPA, Marc provides tax, estate, financial, and retirement planning services to high-net-worth individuals and business owners in the health care, investment banking, real estate, and professional services industries. Marc's more than 25 years of public accounting experience span a range of tax, personal finance, business advisory, and practice management expertise. Often invited to speak to medical societies and health care groups, he has served as an adjunct Healthcare Economics professor in Hofstra University's Master of Healthcare Administration program. Contact him at 516.620.8722 or marc.lion@MazarsUSA.com

Consolidating Purchased Services in Healthcare Transactions

By Jeanna Palmer Gunville, Associate
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Is your health care organization undergoing a strategic transaction? Are you wondering how to best focus your current legal and operational resources during the information-gathering phase (i.e., diligence) to understand the target hospital or health system's current purchased services vendor relationships?

Most strategic transactions are made with the goal of identifying synergies that can lead to cost savings. As you are conducting your due diligence, you should begin evaluating where consolidation of purchased services could lead to post-closing cost savings. Prioritizing review of your soon-to-be partner's vendor relationships and identifying key operational and performance issues during diligence can ease the burden of integrating or renegotiating those arrangements with current or new vendors after the transaction closes.

Leaders of supply chain operations should consider tasking legal resources or vendor management consultants with assessing and summarizing aggregate or annual costs, the services in question, and the vendors' overall performances.[1]

During your next strategic transaction, use the diligence phase to do the following prior to closing:

1. Bring your internal business leaders and legal counsel up to speed on your organization's current purchased services vendor relationships. Develop a list comparing what is outsourced in your organization against what is outsourced by the target hospital. Identify any overlapping service areas.
2. Ask for aggregated information that demonstrates the performance of the target hospital's vendors under its current agreements. Consider including the following in your diligence request:
   - Ask for data regarding annual expenses. Assess what the target spends on categories of products and whether there are aggregate discounts. Where applicable, assess labor staffing and aggregate labor expenses. Compare that data against data related to your current vendors or in-house team to identify savings opportunities.
   - How is communication with the vendor team? Accessibility? Responsiveness? Does the vendor monitor the relationship and anticipate and address issues? Is the target hospital's vendor performing at a higher level than your in-house team or vendor?
3. Be proactive, not reactive, when it comes to contract expiration dates. Ask for a chart summarizing key terms within the purchased services arrangements related to termination and renewal. This will aid in understanding potential expiration dates and windows of opportunity for renegotiation, or consolidation into a single RFP post-closing. Do the dates align with windows for expiration at your current organization? What are the conditions for breach of the agreement? If you want to consolidate vendors but the contracts and circumstances do not permit termination of the vendor contracts, can you convince the vendors to mutually agree to a termination date in order to offer both vendors the opportunity to become the sole vendor of all of your post-closing facilities?
4. Request information regarding existing vendor capital commitments. Identify the penalties and losses applicable if the target pursues early termination of any existing agreements. If you are considering service consolidation between vendors, determine whether your preferred vendor is willing and capable of assuming any capital commitment obligations that may result from termination of the other vendor's contract.
5. Many contracts prohibit a hospital from hiring a member of a contractor's management team after termination. You need to determine what impact termination of an existing vendor contract will have on management staffing subsequent to the termination.

Consolidating purchased services vendor relationships in a health care transaction can be challenging. Your organization's efforts in the diligence phase to gain insight into current relationships will support your ability to efficiently evaluate potential savings opportunities, evaluate potential impediments to consolidation, and be better prepared to address those relationships post-closing.

For further information, contact the author below or any member of our Outsourcing and Cost Management Team.

1 The pre-closing exchange of cost information can raise antitrust considerations and should be done in consultation with legal counsel.

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Out-of-Network Bill: The Law of the Land

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On April 12, 2018, both houses of the New Jersey Legislature passed the "Out-of-Network Consumer Protection, Transparency, Cost Containment and Accountability Act." Some of the major provisions of the bill include:

Disclosures:
The bill would impose significant new disclosure obligations on all carriers, health care facilities (primarily hospitals and surgery centers), and health care professionals regarding network participation status. Further disclosures are required to be made by out-of-network providers prior to scheduling a procedure, including that the provider is out-of-network, that the patient will have additional liability, and that the patient will be provided, on request, with applicable CPT codes and estimated professional fees.

Arbitration:
The bill contains binding "baseball" arbitration provisions applicable to out-of-network charges for emergency services and charges for "inadvertent out-of-network services," the latter being defined as out-of-network services provided at an in-network facility where in-network services are unavailable at the facility.

Waiver Prohibition:
The bill would prohibit an out-of-network provider from waiving deductibles, copayments, or coinsurance as an inducement to the patient to utilize the out-of-network provider, and would consider "a pattern" of such waivers to constitute an inducement.

Penalties:
Penalties under the bill would be up to $1,000 per violation per day up to $25,000 per occurrence for facilities, and $100 per violation per day up to $2,500 per occurrence for professionals, with the possibility of further sanctions by the applicable licensing authority.

Although the baseball arbitration provisions are limited to emergency and inadvertent out-of-network services, the disclosure requirements and waiver prohibitions have the potential to impact a far broader range of out-of-network services.

The Health Care Practice Group at Sills Cummis & Gross will continue to monitor this legislation and any implementing regulations and will issue updates from time to time to our clients and industry colleagues.

Charles H. Newman has more than 30 years of experience in a broad range of transactional matters primarily focusing on the health care industry. Mr. Newman's health care practice includes the representation of a diverse group of clients, including health systems, hospitals, medical groups, ambulatory surgical centers and other provider entities. Reach him at 973.643.4776 or cnewman@sillscummis.com

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