INTRODUCTION

- As the Affordable Care Act enters its fifth year, the pace at which health care transactions occur continues to increase.

- To ensure a solid foundation throughout this process, certain fundamental issues must be addressed at the outset.

- With a strict interpretation pertaining to the prohibition of the corporate practice of medicine, California still affords a number of exceptions to certain providers.
HEALTH CARE TRENDS
NUMBER OF HEALTH CARE PROVIDERS

- In 2012, there were an estimated 45,686 physicians in California, compared to 397,130 in the United States.

- In 2011, there were an estimated 345 hospitals in California, compared to 4,973 in the United States.

- Over the past decade, the average number of hospitals in a health system has been 60%.

- A hospital system averages 3.2 hospitals.
INCREASE IN MERGERS/ACQUISITIONS

- Between 2007 and 2012, 432 hospital mergers and acquisitions included 835 hospitals.

- In 1999, there were 4,956 hospitals in the United States and 395 in California.

- In 2011, there were 4,973 hospitals in the United States and 345 in California.
HOSPITALS AND HOSPITAL SYSTEMS

Hospitals By Ownership Type (1999-2011)

United States

- State/Local Government: 21%
- For-Profit: 20.6%
- Non-Profit: 58.4%

California

- State/Local Government: 20%
- For-Profit: 21.4%
- Non-Profit: 58.6%
HOSPITALS AND HOSPITAL SYSTEMS continued

Number of Hospitals (California)
HOSPITALS AND HOSPITAL SYSTEMS continued

Number of Hospitals (United States)
STRUCTURE
ENTITIES AVAILABLE FOR USE IN CALIFORNIA

- **Corporations** (for profit/non-profit, professional and flexible purpose/benefit)

- **Limited Liability Companies**

- **Partnerships** (general and limited)

- **Unincorporated Associations**

Does not include District Hospitals or other quasi-governmental or governmental entities.
CORPORATIONS

- **For profit corporations** have shareholders, board of directors and officers. These corporations either face double taxation or choose S corporation status and are treated like partnerships (flow through taxation).

- **Professional corporations** engage in the practice of professions, such as medicine or law.

- **Non-profit corporations** can have members, but do not have shareholders. These corporations have a board of directors and officers.
CORPORATIONS continued

- **Flexible Purpose corporations** must provide in their articles of incorporation, in part, that they are organized for charitable or public benefit purposes or to promote the positive effects or minimize any adverse effects on employees, suppliers, customers and creditors, the community and society, or the environment.

- **Benefit corporations** must provide in their articles of incorporation that they have a purpose of creating general public benefit and may have specific purposes related to public benefit.

- Both require shareholders, a board of directors and officers.
LIMITED LIABILITY COMPANIES

- The owners are called members and the LLC can be member-managed or be manager-managed by a manager who may or may not be a member.

- Are taxed like a partnership unless LLC makes an election to be taxed as a corporation.

- Cannot practice medicine through an LLC.
Compared to corporations, LLCs have more flexibility regarding economic aspects (contributions, allocations and distributions), ownership, and voting/control.

Can be non-profit but only tax exempt if owned by government or tax exempt entity.
NEW LIMITED LIABILITY COMPANY LAWS

- Effective 2014

- Fiduciary duties (17704.09): Duties of care and loyalty set out, others possible. Cannot eliminate fiduciary duties, but can eliminate liability of manager for duty of care or other fiduciary duties.

- Tax allocations: No default in rule, should put in operating agreement.
NEW LIMITED LIABILITY COMPANY LAWS continued

- Voting (17704.07): Default for matters outside the ordinary course is unanimous consent of the members.

- Dissociation (17706.01 et. seq.): Sets out default reasons that a member can be expelled, including unanimous consent of members when a member transfers its entire interest, death of an individual member, bankruptcy. Provides for judicial dissociation.

- Applicability of RULLCA (17713.04)
PARTNERSHIPS

- **General partnerships** have general partners who have liability for the partnership’s activities and liabilities. There is inherent flexibility as to management.

- **Limited partnerships** must have one general partner who assumes liability for the partnership’s activities and liabilities. Other partners may be limited partners with limited liability.
UNINCORPORATED ASSOCIATIONS

- Can be non-profit or for profit.
- Offer some liability protection to their members.
- Provide more liability protection, including for directors and officers, if the unincorporated association is non-profit.
- Specific liability rules for medical associations apply for property.
AVAILABLE ENTITIES IN HEALTH CARE

Corporations

- Hospitals*
- Physician Practices
- Surgery Centers*
- ACOs*
- Home Health Agencies*
- Management Companies
- Real Estate Holding Companies

*Certain limitations may apply
AVAILABLE ENTITIES IN HEALTH CARE continued

Limited Liability Companies

- Hospitals*
- Surgery Centers*
- ACOs*
- Home Health Agencies*
- Management Companies
- Real Estate Holding Companies

No Physician Practices

*Certain limitations may apply
AVAILABLE ENTITIES IN HEALTH CARE continued

Partnerships

- Hospitals*
- Physician Practices (general partnerships only*)
- Surgery Centers*
- ACOs*
- Home Health Agencies*
- Management Companies
- Real Estate Holding Companies

*Certain limitations and/or exceptions may apply
PROHIBITION OF THE CORPORATE PRACTICE OF MEDICINE
CORPORATE PRACTICE OF MEDICINE

California prohibits the corporate practice of medicine.

- Laypersons or lay entities may not own any part of a medical practice. (Cal. Bus. & Prof. Code § 2400)

- Physicians must either own the practice, or must be employed or contracted by a physician-owned practice or medical corporation.

- The majority of stock must be owned by California licensed physicians, with no more than 49% owned by other licensed health care professionals (nurses, physician assistants, nurse practitioners, etc.).
CORPORATE PRACTICE OF MEDICINE continued

Possible Exceptions

- Management Services Organizations: An MSO may provide administrative services to a physician or medical group.

- Medical Foundation: California Health & Safety Code Section 1206(l) provides for a non-profit corporation to contract with a medical group of 40 or more physicians which does research and includes at least 10 specialties.

- Friendly Professional Corporation (“Captive PC”) may be problematic.
CORPORATE PRACTICE OF MEDICINE continued

- Businesses that provide management services, franchises or other similar models **must not** result in an unlicensed person or entity influencing or making medical decisions.

- Management service organizations arranging for advertising, or providing medical services instead of administrative staff and services for a physician’s medical practice are prohibited.

- A physician who acts as a medical director of a lay-owned business may be “aiding and abetting” the unlicensed practice of medicine.
HEALTH CARE TRANSACTIONS
HOSPITALS AND HOSPITAL SYSTEMS

- Non-profit corporations and for profit corporations
- LLCs
- General and limited partnerships
- District Hospitals
HOSPITALS AND HOSPITAL SYSTEMS continued

- Tax implications
- Management and control
- Ownership
- Capitalization
- Liability concerns
- November ballot initiatives regarding CEO compensation
OTHER HEALTH CARE ENTITIES

- Physician Practices
- Surgery Centers
- Other categories of health care services (e.g., ACOs, home health agencies)
- Management Companies
- Real Estate Holding Companies
- Equipment Leasing Companies
Types of Mergers/Acquisitions

- Asset/Stock Purchase
- Merger
- Joint Venture
- Management Agreements
- Joint Operating Agreements
- Affiliations
TYPES OF MERGERS/ACQUISITIONS continued

Additional transactions to consider include:

- Real estate loans
- Working capital extensions
- Employee stock ownership plans
- Other
NON-PROFIT TO FOR PROFIT

➢ Authority pursuant to section 999.5, Title 11, Division 1, Chapter 15, of the California Code of Regulations.

➢ California law requires the review and consent by the Office of the Attorney General for any sale or transfer of a health care facility owned or operated by a non-profit corporation whose assets are held in public trust.

➢ This requirement covers health care facilities that are licensed to provide 24-hour care, such as hospitals and skilled nursing facilities.
NON-PROFIT TO FOR PROFIT continued

- The review process includes public meetings and, when necessary, preparation of expert reports.

- The Attorney General’s decision often requires the continuation of existing levels of charity care, continued operation of emergency rooms and other essential services, and other actions necessary to avoid adverse effects on healthcare in the local community.

- Proposed amendments to Section 999.5 were published April 18, 2014, with a public hearing scheduled in early June.
MEDICARE LIABILITY

- There may be no corporate veil.
- A CHOW may not protect you. Medicare provider agreements are automatically assigned to a new owner. This includes exposure to past liabilities. (42 C.F.R. § 489.18(c)).
- Bankruptcy may not protect you (11 U.S.C. § 523).
- Providers have Medicare liability, irrespective of the transaction.
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Craig is an attorney and health care consultant, specializing in issues pertaining to modern American health care and the ways it should be managed in its current climate of reform.

Craig’s law practice focuses on health care mergers and acquisitions, regulatory compliance and counseling for providers. Craig is also an adjunct professor of law at Pepperdine University School of Law, where he teaches courses on Hospital Law and the Affordable Care Act.

Between 2002 and 2011, Craig was the Chief Executive Officer of Coast Plaza Hospital in Norwalk, California. Craig is also a Fellow Designate with the American College of Healthcare Executives, a Member of the State Bar of California, Business Law Section, Health Law Committee and a Vice Chair of the Healthcare Reform Educational Task Force of the American Health Lawyers Association.

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Rachelle is an attorney with Kehr, Schiff & Crane LLP, in Los Angeles. Her practice focuses on assisting clients with their business transactions, including forming entities, acquiring and selling business units or entities, obtaining funding, and negotiating contracts and buy-outs.

Previously, Rachelle worked in the state and local tax and investment management groups at Dechert LLP. Rachelle is the Vice Chair of the California State Bar's Partnerships and Limited Liability Companies Committee. She speaks frequently about limited liability company and partnership issues. She assisted in drafting the technical corrections bill for RULLCA. She currently is involved in the revision of the Guide to Organizing and Operating a Limited Liability Company in California, a publication of the Business Law Section of the State Bar of California. She also is involved in updating the CEB books Advising California Partnerships and Forming and Operating California Limited Liability Companies.

Rachelle attended the UCLA School of Law and received a B.S. in Marketing and Management from Cornell University.
Thank You

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