



## legal matters

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**Details of the Deal** Without adequate preparation, buying or selling a medical practice can become a nightmare. Double checking this list can help your exchange go smoothly.

BY JOHN ALLEVATO



Thinking of buying a practice or selling the one you have?

Conducting these negotiations can be exciting and nerve wracking. By reviewing a checklist of some of the most common issues addressed in the sale of a practice in advance, both parties can avoid wasting time.

We will examine, from the perspectives of both a buyer and a seller, some of the issues

involved in this process. This should shed some light on solutions to common issues and provide guidance for embarking on such a transaction.

### General considerations

The best overall advice for anyone, whether they are buying or selling, is to seek competent, experienced professional help to assist in the process. Find someone—a lawyer, consultant, or other professional—who is familiar with the sale of professional medical practices. There are issues peculiar to physicians

not present with, say, selling a manufacturing business or a grocery store.

There are what I will refer to as “business” points, and there are “legal” or more technical issues surrounding the details of the arrangement and other matters affected by the law. The business issues are ones that the physician would most often be involved with and would most affect the decision-making process.

One of the main legal issues to be considered is how the transaction could affect your

tax bill or expose you to unnecessary tax liability. Your adviser should be able to help you structure your arrangement in a manner that provides the most benefits to you.

### Following are the most commonly negotiated issues.

- **Purchase agreements.** It may seem obvious, but it is important to only conduct purchase and sale agreements in writing (and with the supervision of an attorney.)

Often a letter of intent is used. A letter of intent is a

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(usually) non-binding agreement between the buyer and seller which sets forth the highlights of the business points surrounding the deal. It is a starting point for the preparation of a more formal and detailed purchase agreement which contains all the terms and provisions of the arrangement between the parties.

Letters of intent are not necessary however, and often are not recommended. Why? Because getting the parties to sign a letter of intent often entails negotiating over points which then are renegotiated when the purchase agreement is prepared. Depending on the size and complexity of the arrangement, it may be just as well to go straight to the preparation of the final and definitive purchase agreement. On the other hand, long, drawn-out negotiations over a letter of intent often indicate problems with the deal which may make it impossible to complete—and it's better to learn that early in the process rather than later.

- **Non-compete provisions.** Covenants not to compete are provisions commonly seen in physician agreements. Under these agreements the buyer requests that the selling physician not practice in the same marketplace after the sale, competing with the buyer for patients. The buyer who requests this covenant should be willing to compensate the selling physician for such a restriction.

Courts will and do honor non-compete provisions, but they are not to be taken lightly. Sellers, be sure that the inclusion of a non-compete provision is in your best interest, and that the one proposed by the buyer is appropriate for your deal.

Non-compete provisions restrict the selling physician from practicing medicine for a set period of time within a limited geographical area. The geographical area should be the market area of the practice being purchased. What happens

on too many occasions, unfortunately, is that the geographical parameters or the period of time for which the physician is restricted from practicing is too broad. In some states, courts can fix that by “rewriting” the restrictions to a period of time or geographical area that the court finds reasonable. Other states will just throw out the offending provisions of the agreement. This is one provision for which your local counsel will be able to provide guidance on the particular law in your jurisdiction.

- **Asset valuations.** Getting the assets which are to be purchased and sold appraised for fair market value is an important consideration, both from the standpoint of fraud and abuse and Internal Revenue Service concerns. If a purchaser or a seller is a tax-exempt organization, then obtaining appraisals for all the assets to be sold is critical.

The tax laws now provide that the parties to a sale of a business (your practice is a business) provide, on a separate tax schedule, a breakdown of the sale price of the business and an allocation of the sale price among the various classes of assets which were sold. These assets include equipment, patient records, goodwill, office furniture, supplies, etc. Since the allocation of the purchase price among the assets sold has significant tax consequences (to both the buyer and seller), a valuation of assets is important to support the valuation placed on each of those assets in the sale of the business. A failure to justify the allocation of the purchase price among the assets could result in the IRS reallocating the amount paid for the assets, probably in a manner which provides less tax benefits to either or both parties.

From the perspective of fraud and abuse, especially if a tax-exempt organization is a buyer or seller, valuations of all the assets sold or bought must be done.

This is to comply with the rule that fair market value, and no more or less, must be paid for assets when a tax-exempt organization is part of the equation.

### Considerations for Buyers

From the buyer's perspective, the following is a short list of considerations that may be important:

- **Form of entity.** How does the buyer wish to own the business she is purchasing? The options are considerable, and that makes the decision more complex than ever. The choices include a C corporation (a regular corporation for tax purposes), an S corporation, (which taxes the owner or owners as partners), a sole proprietorship, a partnership with another physician, or a limited liability company. The latter alternative is a relatively new possibility, and combines the best of an entity that traditionally has limited the liability of its shareholders (like a corporation), with tax advantages not found in a corporation (like a partnership). No form of entity will protect you and your assets from your own malpractice, but the right form of entity can go a long way in limiting your exposure for the malpractice of a partner. This decision is another one which may be peculiar to your local jurisdiction, as state laws differ substantially on which of these forms are suitable for physicians and what levels of liability protection are available.

- **Adequate investigation.** No one wants to buy a “pig in a poke,” and that is doubly true with a medical practice. With the specter of governmental fines and penalties for billing errors, such as under the False Claims Act, and with potential Stark and fraud and abuse violations seemingly around every corner, it is critical to perform adequate due diligence and investigation before the acquisition. Know the professional reputation of the seller and

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the practice you are buying. Check with state medical societies in every state in which the practice operates and is licensed. Check with local hospitals to determine if the physician's privileges are in force, or have ever been suspended or limited. Have your professional advisers assess the financials and the tax returns of the business. Finally, if tangible assets are a big part of the purchase, see that the equipment and other assets are checked out ahead of time, and note any needed repairs or maintenance that has been deferred.

### **Considerations for sellers**

**Cash is king.** It is common for sellers to "finance" a sale of a business; that is, to act as a bank. I would not recommend that approach when selling a medical practice, as issues surrounding the fraud and abuse laws are brought into play any time a contract extends for more than a year. Get paid in cash up front—there is no reason for you to act as a bank.

**Stay on and work?** Buyers will frequently wish for physician-sellers to stay on for a while and assist them in the transition of the practice. Be prepared for your buyer to ask you to do this. Before you agree to work in the practice however, ask yourself if you will be comfortable working for someone in the practice you just sold. Can you stay out of running the business and just show up and work?

**Representations and warranties.** Buyers will ask sellers to make various and sometimes extensive representations about the business and assets that are being sold. Read these provisions carefully, because you may find yourself in a lawsuit later if some of the representations turn out to be untrue. For example, you may be asked to represent that the equipment is in working order, or that you have disclosed all contracts of the business to the buyer. If something turns out not to be true or if ade-

quate disclosure was not made, the buyer may seek redress for any loss she suffers as a result of what she believes was a breach of a representation you made.

Physician acquisition transactions, from the side of either the buyer or seller, are fraught with peril. You should seek competent professional assistance every step of the way in these arrangements. A dollar spent now could save you countless dollars and headaches later. But with the proper research and preparation, your dream of owning a practice (or shedding that responsibility) can come true. ■

*John Allevato is a member in the Charleston, WV, law firm of Spilman Thomas & Battle, PLLC, where he practices business and tax law. He is a member of American Health Lawyers Association and can be reached via e-mail at [jallevato@spilman-law.com](mailto:jallevato@spilman-law.com)*