10 Things I Wish I Knew Before Our Acquisition
~and~
What We Learned Looking Back

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Learning Objective

This session will provide you with the knowledge to:

• Understand what to expect from an acquisition process
• Make better decisions throughout the acquisition process
• Transition to the new corporate structure with minimal conflict
• Achieve strong working relationships within the new organizational chart
But first ... My Story
My Group Story

In 2012, we decided to explore selling the practice.

- Hospital
- Payer

Overview of the group, at that time

- 100 physicians
- 300,000 unique patients
- Profitable each year
- Owned 6 medical offices and one admin building (billing)
We decided to narrow our investigation to hospitals to protect our culture and independence.

In 2012, we engaged in acquisition discussions with:
- Florida Hospital (now AdventHealth)
- Orlando Health

In January 2012, we signed a non-disclosure agreement.

In November 2012, a letter of intent was signed.

Deal closed on December 31, 2012.
Why We Sold

1. To access additional working capital
   - For the past several years, we had to have “capital calls” for
     - Electronic health records
     - IT equipment
     - Telephone equipment, etc.

2. We saw the need to expand to new locations, open new medical offices and hire additional physicians.
   - New leases (build-out)
   - Funding new physicians through break-even
Why We Sold

3. We saw the need to begin “Population Health” or care coordination strategies (new employees) to help physicians manage the care of complex and sick patients (required by many new payer contracts that paid incentives for quality and cost of care).

4. We saw a future where contracting required the physician group to join an ACO.
Why We Sold

5. To avoid Medicare reimbursement reductions (MIPS/PIPS), we needed to join a Medicare ACO that could assume a greater degree of financial risk.

6. We saw the Orlando market developing “narrow networks,” and we needed greater medical alignment with a hospital and key specialists.
10 Lessons Learned
What you think the practice is worth may differ from an outside valuation.
Purchase Price

- By law, hospitals (non-profit organizations) acquiring a physician practice can only pay "fair market value" for the practice.

- What determines "fair market value"?
  - Fair market value of equipment (appraisal)
  - Fair market value of real estate and buildings (appraisal)
  - A value attributed to an assembled work force (valuation firm)

Note: In most physician practices, all profits are distributed back to the owners; however, if annum profits exist year after year and it is expected after the acquisition, these profits will still exist. Then, these earnings times a multiplier can be paid as a part of the acquisition price. (This could be a business residing within the practice.)
Purchase Price (continued)

- Selling to an entity which is not a non-profit, for example United Healthcare, Humana, etc.
  - The acquisition price is based on a negotiated price (based on other acquisitions).
The process of arriving at a “fair market value”: 
- A hospital will hire an outside valuation firm to arrive at a fair market value of the practice.
- The practice should also hire someone to provide a valuation.
  - The cost could be a flat fee or a percentage of the firm purchase price.
    - The percentage depends on the scope or work the valuation firm will perform (helping to negotiate the final price would increase the percentage).
Purchase Price (continued)

- The valuation process can be long and time consuming and will require a lot of information:
  - 5 years of financials
  - Cash flow statements
  - Copies of **ALL** contracts (payer and office)
  - Accounts receivable history
  - Employment history of physicians and employees
  - Malpractice insurance
  - Any outstanding litigations
  - And much more...
# 2
Not everyone on either side is going to like this.
The Selling Practice

- The practice partners (depending upon their age) may have different expectations from the sale.
- Reaching a consensus will be important on critical issues.
- Forming a relationship early on in the process will help build trust.

**Staff**

- You will need to get them involved in this process, early on, as with any big change, they may tend to think the worst.
  - We’re going to lose our jobs.
- Where consolidation is likely to occur
  - Billing and collections
  - IT
  - Human Resources
  - Finance and Accounting
- Clinical staff should be fine, so long as they can pass a drug screening and criminal background check.
Partners should try to keep their eyes on the end strategy (life after the practice is sold).

Key elements to consider:

- Acquisition agreement
- New employment contract
- New physician compensation agreement (multiple years)
- Governance of the practice
- If separation occurs:
  - Re-payment of a partial percentage of the buy-out proceeds
  - Non-compete provision
  - If real estate is involved, negotiating a long-term lease is important
- Negotiate the new name of the practice.
# 3
Money isn’t everything!
Values, culture, mission, and vision are more important.
For Physicians ~
Love of their patients is critical!

During the negotiations, discussions need to be established on how the practice will be run post-acquisition.

- Who has the authority to hire and fire?
- Who determines and controls the physician’s scheduling template?
- Who determines the operating hours of the practice?
- Who determines if patients who have outstanding payment balances will be seen?
- Who determines how the office will function -- from patient check-in to patient check-out?

Some physicians tend to forget they sold their practice and find it difficult to give up control and decision making.

What are the rules for closing a physician’s panel to patients?
Be careful what you ask for – you just might get it.

It may be great short term, but you might pay a price later.
Know Why You Are Selling Your Practice

- Contracting leverage/higher reimbursement
- Access to working capital (electronic medical record, expansion, etc.)
- Access to new contracts (ACO, narrow networks, etc.)
- Sale of real estate or lease of building
Know Why You Are Selling Your Practice (continued)

- When selling your practice, you give up some independence and decision making.
  - During the negotiations, try to discuss changes that will occur after the acquisition:
    - Contracting – Will you have to accept new patients from new payers?
      - Medicaid
      - Advantage Medicare
      - ACOs
    - Will quality metrics be imposed on the physicians?
    - Will the practice hours change?
    - Know how “call” coverage will work.
Healthcare in Its Present Form is Unstable

- Total healthcare spending continues to increase and will only get worse with the Baby Boomers.
- Expect changes in the delivery of healthcare:
  - Moving away from “fee for service”
  - Moving toward “fee for quality” and full risk
  - Payers developing “narrow networks” based on quality scores and total patient cost of care
  - Practices required to provide care coordination services to very sick patients
  - Physician incentivized on closing medical care gaps
- The goal will be to make medicine available to more people and at an affordable cost.
Understanding What is Critical

- It is critical to understand what the acquiring entity is looking for and to understand their mission, culture and strategic plan.
- Early in the process, get names and contact information from others who have joined the acquiring entity.
  - What did they like?
  - Where were the sticking points?
  - Are they happy as employees of the new entity?
  - How did the staff fare?
  - What didn’t work?
- The values of the two organizations must match.
- Expectations, on both sides, need to be discussed and agreed upon.
# 5
Due diligence on both sides means more than just looking at finances.

“You know, I never properly vetted you.”
Due Diligence = Opportunity for Analysis

- Provider Analysis – discovery process receiving key information on the nature of the practice and performance

- Practice Analysis – discovery process receiving key information on the nature of the practice and performance.

- Provides opportunity to learn about each other
Due Diligence List

Company Data:
- Company Articles of Incorporation
- Company Fictitious Filing Report
- List of Location(s) and Operating Hours
- Office Location(s) – Owned or Leased
- Copy of Lease Agreement(s) for each location or
- Copy of Ownership Documents for each location
- List of Physicians and Providers
- State Licenses of Physicians and Other Providers
- Copy of Physician Board Certification(s)
- Physician and Provider Hospital Privileges/Which Hospital(s)?
- Summary of Core Services Provided and Ancillary Services
- Malpractice Insurance Carrier
- Copy of Malpractice Insurance Coverage Document
- Malpractice Claims History Report
- Business License (copy)
- CLIA License, if applicable (copy)
Due Diligence List

Financials:
- Tax Returns for Last Two Years
- Last Year’s Financial Statements
- Year-to-Date Financial Statements
- Payroll Report(s)
- AR Summary Report(s)
- Payer Mix Report
- Current Payer Insurance Contracts
- List of Any Insurances Not Accepted
- Billing & Coding – Internal or Outsourced
  - If outsourced, provide vendor information and copy of agreement
- Collections – Internal or Outsourced
  - If outsourced, provide vendor information and copy of agreement
- List of Contracted Vendors for Any and All Services and Copy of Agreement(s)
Due Diligence List

Technology:
- Current EMR/EHR Program and Copy of Agreement(s)
- Current Practice Management System and Copy of Agreement(s)
- Current Claims Submission Vendor or Software Utilized and Copy of Agreement(s)
- List of Any Other Licensed Software Utilized and Copy of Agreement(s)
- Telephone System Utilized and related Software and Copy of Agreement(s)

Assets Inventory
- Hardware Equipment Inventory
  - If any Equipment is leased or financed, provide copy of Agreement(s)
- Clinical Equipment Inventory
  - If any Equipment is leased or financed, provide copy of Agreement(s)
- Office Furnishing Inventory
  - If any Equipment is leased or financed, provide copy of Agreement(s)
- Other Assets Inventory
  - If any Equipment is leased or financed, provide copy of Agreement(s)
Due Diligence List

**Staffing:**
- Number of Employees
- Title of All Employees
- Payroll Internal or Outsourced
  - If service is outsourced, provide copy of Agreement(s)
- Payroll Report(s)
- Benefits Provided with Detail
- Benefits Summary
- After Hours On-Call Coverage Provider, Internal or Outsourced
  - If service is outsourced, provide copy of Agreement(s)
Key Factors Reviewed

Importance of Due Diligence
- This process can take up to six (6) months to complete.

Agreement Considerations
- Is our interest in a Physician Partnership or Physician Employment Agreement?
- Is there also an interest to acquire the Practice Assets & Property?
- These are two different aspects and not mutually inclusive.

Asset Strategy & Space Management
Due Diligence Process

Introduction

It is vital to the acquiring entity that every effort is made to ensure that practices acquired bring strength to the organization:

- That the physicians and team members fit into the new culture
- That the assets brought with the acquisition are sound and do not financially drain the organization
- That the acquired practice comes financially healthy prior to the acquisition
- That the acquired practice does not come into the company with any legal or compliance issues

To assure all of this, a thorough investigation of the potential acquisition must be done. This is not a process that can be done in days or weeks but will take months. All parties should be prepared in advance for this process and realistic expectations set.
Due Diligence Process (cont.)

Process
A non-disclosure agreement is normally prepared and sent to the physician(s) for signature.
# 6
Really evaluate what you want long term and focus on getting that during negotiations.

“Early retirement is an OK long-term goal, Kevin, but most folks need to get a job first.”
Negotiating

In negotiating a physician new employment contract, you want to protect physician compensation from being decreased.

- Higher hospital expense allocations (especially IT, billing and collections)
- Try negotiating a collections guarantee on expected revenue
- Negotiate performance incentives:
  - Quality
  - Cost of Care
  - Patient Satisfaction

Guaranteed salaries at the transition due to collection delays, from changing Tax ID number
- This protection needs to be in a long-term contract.
# 7
Start “living together” as soon as possible.

And when we see each other in the morning, it will be a nice surprise!
Very Important to Form Relationships

- The goal is to develop:
  - Mutual respect in both organizations
  - Trust comes from getting to know one another
  - Communication of expectations
  - Concerns

- How would you handle a sudden major disagreement?
  - Effective communication is critical.
    - Listen to their side/concerns and understand where the buyer is coming from.
    - Communicate why this is a concern for the seller.
  - Negotiations are an attempt to meet in the middle, unless compliance/law dictate otherwise.
  - Consider bringing in others who can support your concerns and help to provide new ideas to be considered by both parties.
# 8

Remember that compromise takes both sides giving up something. This is as important after the acquisition as it is during negotiations.

“If you are willing to take a 25% pay cut, I’m willing to give you a 10% raise!”
After the Marriage

- With the rapid changes occurring in medicine, it is undeniable that a surprise is going to arise.
- Both the buyer and the seller should have a person responsible for a successful negotiation.
- These two persons should continue to meet periodically after the transactions have been completed.
- These two persons have the responsibility to work together to solve problems that arise, post transaction – expect these to occur.
  - This is where good relationships, trust, transparency, and genuine concern for a win-win are critical.
# 9
It is very difficult for those who have been owners and in charge to suddenly become employees.

“"I appreciate the effort, but need you to be more flexible.""
In the six years since the sale and purchase of our old medical practice, I’ve heard the following several times:

- “What your proposing is un-acceptable; I'm the physician."
- “This is my practice, and I decide how things are to be done.”
- “This is how we’ve always done things around here.....”

No, you sold your practice, and now you have agreed to be employees.

Take away thoughts:

- During negotiations, things that are important to the doctors have to be laid aside and negotiated separately. Anything agreed upon **MUST BE IN WRITING**. Our Board had agreements related to the deal structure that were “sealed” with a hand-shake. The problem: everybody that was party to the original agreement is no longer present; and agreements not in writing **WILL NOT COUNT**.
Key Items for Consideration

- How physician compensation will be calculated and for how long. Exact methodologies must be documented and agreed upon.
- Practice governance
- Treatment and retention of employees
- Bonuses and calculations
- Contracts, Payers, treatment of risk contracts, capitation agreements, acceptance of Medicare and Medicaid
- Malpractice limits
Key Items for Consideration (cont.)

- How new Physicians will be hired
- Expense allocations of practice expenses to physicians
- Billing and collection costs to be passed on to the physicians (make sure there is a good history of the buyers ability to bill and collect)
- IT expenses to be pushed down to the physicians
- Care coordination expenses

In summary, know the critical things you want in the practice and have this discussed and agreed upon in writing and included as part of the acquisition agreement.
Charts (patients) are not necessarily an asset that has monetary value.
Chart Considerations

- Old paper charts have little to no value (maybe $10 to $25/chart).
- Electronic patient charts have more value, and this varies widely. Estimated value $100 to $135/chart.
- The more patients you have, the more negotiating room you have. If the sale gets in the newspaper, it’s important for the physician to explain to their patients why they sold their practice:
  - To join an integrated delivery system that provided them more access to Payer contracts
  - Reimbursement did not keep up with medical inflation, and as a small provider, you did not have any leverage on the Payer.
  - Access to Electronic Medical Records
  - Access to care-coordination services for very sick patients
  - Improved billing and collections
  - Better benefits
  - Etc.
- You need to sell this to your patients -- you don’t want them to think this was for greed.
In Closing

- Pursuing a sale with two different organizations, at the same time, is ideal. Fair market value is recognized if another company offers a higher acquisition price. If this strategy is pursued, make sure this is spelled out in the non-disclosure agreement.

- This is a long process.

- You will need two key positions throughout this process:
  - A skilled negotiator
  - An excellent lawyer who has experience developing these documents (also beneficial if they have experience working with acquisitions)

- Have frequent partner meetings.

- Keep the staff well informed.
In Closing

An acquiring entity is looking for physicians who:

- Are highly qualified
- Will be a good fit into their culture
- Will bring their patients
- Can effectively manage their patients’ overall cost of care
- Improve their provider network
- Pull other physicians away from their competitor(s)
- Help them grow
  - ACOs
  - Advantage Medicare Networks
  - Narrow Network

For a hospital it could mean:

- New retention for its employed specialists
- New downstream revenue
- A defensive move
Community Reaction

In general, the community did not favor market consolidation because they feared it limits competition and raises the overall cost of medicine.

In our case, our reimbursement rates increased (hospital had better contracts); but, our overall total cost of healthcare decreased.
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