

HEALTHCARE TRANSACTIONS

Special Healthcare Legal Issues
for Attorneys

November 9, 2011
Pittsburgh

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Special Role of Attorney in Healthcare Transactions

- Identify scope of healthcare regulatory issues
- Assess reimbursement issues
- Assess timing of requirements for transaction

**Attorney General and Orphans’
Court Review of Non-Profit
Transactions**

- Under Pennsylvania law, the assets of a charitable nonprofit corporation must be dedicated to charitable purposes, and prior to any fundamental change that results in any diversion of the assets away from the original purpose, the court must determine a disposition of the property that furthers a charitable purpose.

- The Pennsylvania nonprofit corporation law (“NCL”) provisions concerning the sale by a nonprofit corporation of all or substantially all of its assets make specific reference to the statute’s restrictions on diversion of charitable assets.

Fundamental Transactions
(see 15 Pa. C.S.A. 5901 – 5997)

- Merger or consolidation
- Sale of all or substantially all assets
- Dissolution

AG Review Protocol

- Background. In the wake of the bankruptcy of AHERF, which had grown rapidly in the 1990's through numerous acquisitions of hospitals in Pittsburgh and Philadelphia, in 1997 the Pennsylvania Office of Attorney General ("OAG") developed a "Review Protocol for Fundamental Change Transactions." The Review Protocol is available on the OAG website at <http://www.attorneygeneral.gov/consumers.aspx?id=229>.

- Applicability. The Review Protocol applies [w]henever a nonprofit, charitable health care entity enters into a transaction effecting a fundamental corporate change which involves a transfer of ownership or control of charitable assets.

- The Review Protocol is applicable regardless of the form of the transaction contemplated (*i.e.*, sale, merger, consolidation, lease, option, conveyance, exchange, transfer, joint venture, affiliation, management agreement or collaboration arrangement, or other method of disposition).

- It does not apply if the transaction is in the usual and regular course of the nonprofit's activities.

Example: Purchase of assets of a physician's practice

- It applies "regardless of whether the other party or parties to the transaction are a nonprofit, mutual benefit or for-profit organization."

Submission to OAG

- Notice to OAG must be furnished "at least 90 days prior to the contemplated date of its consummation."

• The Review Protocol requires that, with the notice, a long list of documents must be submitted to OAG with the notice “as the Attorney General may determine to be necessary.”

Confidentiality

• The Review Protocol states that confidential information submitted to OAG will be held in confidence as a part of its investigative files. Such information may be made public if OAG objects to a transaction or if a court orders its dissemination. OAG will notify all transaction parties of any formal or informal request seeking access to the information provided.

Review of Transaction

• The Review Protocol says that OAG’s review will include, “among other components”:

- information gathering.
- review of fiduciary responsibilities of directors, particularly relative to the exercise of due diligence, the assessment of self-dealing and whether or not the transaction is at arms length.
- fair market valuation analysis.

- inurement inquiry, including stock options, pension plans and perquisites, performance bonuses, consulting contracts or other post-transaction employment agreements, corporate loans, golden parachute provisions and severance packages, salaries, and related party transactions.

- public interest review to evaluate the transaction's effect upon the availability and accessibility of health care in the affected community, to include community involvement and antitrust review.

- appropriate *cy pres* determination, to ensure that all restricted funds remain segregated and used for their restricted purposes; and that the remaining or successor charitable organization competently and efficiently utilizes the assets for a like charitable purpose benefitting the same class of beneficiaries.

Example: Existence of an independent foundation

No Objection Determination

- According to the Review Protocol, “[u]pon completion of its review of the transaction, the Office of Attorney General may: issue a letter indicating that it has no objection to the transaction; bring judicial proceedings to enjoin consummation of any disputed transaction; seek to void any transaction consummated as being in derogation of the law or contrary to public policy; or take any other action it deems appropriate.” In practice, if Orphans’ Court approval is sought, OAG may simply state its lack of objection on the record in the court proceeding.

Orphans’ Court

- The Orphans’ Court has jurisdiction over the disposition of assets of a nonprofit corporation.

Specific Issues

- Among the features that have been identified as relevant in OAG and Orphans’ Court consideration of nonprofit healthcare transactions are the following:
 - Decisionmaking Process
 - Conflicts of Interest
 - Adequacy of Consideration
 - Purchaser Contractual Commitments
 - Donor Restricted Funds

Intervention/Standing

- Transaction parties are often concerned that, even though OAG does not object to a transaction, a third party may seek to intervene in the Orphans' Court process to disrupt the sale. Private parties generally lack standing to participate in proceedings involving charitable organizations.

- Generally, the only persons who may participate in such proceedings are the Attorney General, a member of the charitable organization or someone having a special interest.

Duties of Boards and Executives

- **Fiduciary Duties of Directors and Officers**

- Standards of Care

- Trustees/Directors. "A director of a nonprofit corporation shall stand in a fiduciary relation to the corporation and shall perform his duties as a director, including his duties as a member of any committee of the board upon which he may serve, in good faith, in a manner he reasonably believes to be in the best interests of the corporation and with such care, including reasonable inquiry, skill and diligence, as a person of ordinary prudence would use under similar circumstances."

• Officers. "Except as otherwise provided in the bylaws, an officer shall perform his duties as an officer in good faith, in a manner he reasonably believes to be in the best interests of the corporation and with such care, including reasonable inquiry, skill and diligence, as a person of ordinary prudence would use under similar circumstances."

– Permitted Factors for Board Consideration
– Business Judgment Rule
– Duty of Loyalty

Limitations on Liability

- Limitations in Organic Documents
- Indemnification
- Limited Immunity for Uncompensated Charitable Board/Officers

Regulatory Approvals

- **Medicare**

– Generally, a transaction involving a Medicare provider can be classified as alternatively involving a change of ownership (“CHOW”), requiring a new Medicare enrollment, or having no impact on the provider’s continued Medicare enrollment

– CHOW. The principal guidance on whether a transaction constitutes a CHOW is set forth in Medicare regulations at 42 C.F.R. § 489.18 and the Medicare State Operations Manual (“SOM”), Chapter 3, §§ 3210 et seq.

New Enrollment

– A new Medicare enrollment is involved if the Medicare provider enrollment is not or cannot be transferred to the new owner, or if, in the case of transaction that would otherwise constitute a CHOW, the new owner rejects assignment of the provider agreement

No CHOW

– If the transaction does not require new enrollment and does not constitute a CHOW, the Medicare provider’s enrollment continues unaffected by the transaction. For example, the transfer of all of the stock of a corporation that owns a Medicare provider is not a CHOW or new enrollment

Pennsylvania Licensed Health Care Facilities

• Health Care Facilities Act

– Certain types of health care facilities and providers are licensed by the Pennsylvania Department of Health (“DOH”) under the Pennsylvania Health Care Facilities Act, 35 P.S. §§ 448.801 *et seq.* These include hospitals, home health care agencies, home care agencies, hospices, long-term care nursing facilities, cancer treatment centers using radiation therapy on an ambulatory basis, ambulatory surgical facilities, and birth centers.

• Notice Requirements under Health Care Facilities Act

– A transfer involving 5% or more of the stock or equity of the health care facility: 30 days prior notice. 28 Pa. Code § 51.4(a).

- A change in ownership or a change in the form of ownership or name of the facility: 30 days prior notice. A change in ownership shall mean any transfer of the controlling interest in a health care facility. 28 Pa. Code §51.4(b).

- A change of management of a health care facility: notice within 30 days after change. A change in management occurs when the person responsible for the day to day operation of the health care facility changes. 28 Pa. Code § 51.4(c).

• DOH’s provisions applicable to hospitals require a hospital to “advise the Department no later than 90 days prior to an intended change of ownership or control of the hospital. No license shall be transferable to new owners or controlling parties except upon a finding by the Department that they are responsible persons.” 28 Pa. Code § 101.52

Pennsylvania Medical Assistance

- Notification Requirements

- General. A change in ownership or control interest of 5% or more of a provider enrolled in the Medical Assistance program must be reported to the Department of Public Welfare (“DPW”) within 30 days of the date the change occurs.

- Nursing Facilities. In addition to the general provisions, DPW regulations require that, “[i]f a provider enters into an agreement of sale that will result in a change of ownership of its nursing facility, the provider shall notify [DPW] of the sale no less than 30 days prior to the effective date of the sale.” The notice must include the effective date of the sale and a copy of the sales agreement. If a provider operating a nursing facility fails to provide the general and specific notices that are required, “the provider forfeits all reimbursement for nursing care services for each day that the notice is overdue.”

Other State and Federal Agencies

- May be multiple licenses within a transaction

Example: nuclear license

Other Issues/Considerations

- Due Diligence
- Representations and Warranties/Indemnification

- **Antitrust.**
 - A healthcare transaction may be subject to review from an antitrust perspective.

– Depending on the size of the transaction and the parties, pre-merger notification to the Federal Trade Commission and the Department of Justice may be required under the Hart-Scott-Rodino Antitrust Improvements Act

- In 1996, the Federal Trade Commission ("FTC") and Department of Justice ("DOJ") issued "Statements of Antitrust Enforcement Policy in Health Care," which, among other things, set forth an "antitrust safety zone" for certain hospital merger transactions.

- In 2010, FTC and DOJ issued revised horizontal merger guidelines, which outline analytical techniques, practices, and enforcement policies the agencies use to evaluate mergers and acquisitions involving competitors.

- The Pennsylvania OAG also reviews healthcare transactions from an antitrust perspective. In some transactions, OAG has resolved antitrust concerns by obtaining commitments addressing the conduct going forward.

Examples of Antitrust Actions and Final Orders

- Commonwealth of Pennsylvania vs. Urology of Central Pennsylvania, et al. August 30, 2011
- Commonwealth of Pennsylvania vs. Catholic Health East, Pittsburgh Mercy Health System, et al. May 2007

Tax Exempt Organizations

- Private Benefit
- Private Inurement
- Intermediate Sanctions

Conclusion

- Importance of attorney with healthcare expertise in healthcare transactions
