

# “To Be or Not to Be” Affiliated with a Radiology Practice Management Company (PPMC)

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**DISCLOSURE**

**NONE**

# Introduction

- Why do we care about this subject?
- The history of physician practice management companies (“PPMCs”), particularly in radiology.

# Introduction (cont'd)

- “To Be or Not to Be” affiliated:
  - Strategic objectives of today’s radiology PPMCs.
  - How radiology PPMCs tactically do what they do.
  - Threshold and document issues that will have to be worked through in any transaction with a radiology PPMC.

# Why Do We Care?

- Perhaps at no other time in history has health care, especially radiology, experienced the recent volume and velocity of change.
- The drivers:
  - Health care "reform."
  - Federal scrutiny of diagnostic imaging.
  - Reimbursement pressure from all governmental and non-governmental payors.
  - More and more (expensive) technology.
  - Heightened tension with hospitals and their efforts to acquire (or consolidate) physician practices (even radiology groups).
  - Accountable care organizations, as well as other integrative efforts, most often being driven by hospitals.
  - "Big" teleradiology businesses and PPMCs are changing the competitive landscape for professional radiology services.
- Radiology groups are left asking "What should we do?"

# History of PPMCs

- Over the past 5-10 years, there's been a resurgence of PPMCs.
  - In virtually all specialties.
- As far back as 20 years ago, most of the early PPMCs were struggling operationally and financially, and eventually most of them went into bankruptcy.
  - They tended to be purely financially-driven plays, with few plans for how they were going to create value and achieve growth.
  - They would buy an EBITDA stream (out of the pockets of the physicians) at “x” multiple with equity, debt and/or cash, and then go public or sell to a strategic buyer at “x plus” multiple, with the PPMC benefitting from the “plus” part of the multiple.
  - Usually the equity and the debt was, or quickly became, worthless.
  - They wanted total control.
  - They often demonstrated an acute ignorance of how to work with physicians, and . . .
  - They were often willing to take significant regulatory compliance risks.

# History of PPMCs (cont'd)

- Despite this ignominious history, a second (and perhaps even a third) generation of PPMCs have begun to proliferate throughout medicine.
  - Most recently, PPMCs (and companies that want to behave like PPMCs) have begun to move much more aggressively into the practice of radiology.
  - They are still often investor-owned.
  - Some base themselves around technical facilities.
  - Others are focusing on teleradiology and tout themselves as being tantamount to “supergroups.”
- These “new” PPMCs tend to have different strategic objectives than their ancestors.
- And although their tactics for achieving these objectives have some components in common with the old way of doing things, . . .
- They also have some new twists.

# Strategic Objectives of Today's Radiology PPMCs

- Today's Radiology PPMCs want so-called "high value" groups, with capacity.
- The PPMCs can then use "their" radiology groups to:
  - Compete for business using teleradiology and/or
  - Staff their technical facilities.
- The PPMCs also believe that they are better positioned than the typical radiology group to participate in accountable care organizations ("ACOs") and clinically integrated networks (CINs").



# Strategic Objectives of Today's Radiology PPMCs (cont'd)

- Today's radiology PPMCs usually still want to “own” the radiology group, and “buy” an income stream.
  - However, they tend to be less interested in buying a “significant” stream than in the past, and . . .
  - The upfront payment tends to be smaller (you're probably not going to retire on the payment), and. . .
  - The payment tends to mostly cash (possibly with a relatively small equity sliver of the PPMC).
  - Bottom line: the PPMC generally still views the transaction as them “buying” the practice.

# Strategic Objectives of Today's Radiology PPMCs (cont'd)

- On the one hand, the PPMCs usually want a very high level of control, right to the edge of violating any corporate practice of medicine prohibition (“CPOM”).
- On the other hand, the new PPMCs have learned from the mistakes of the past, *i.e.*, that it is usually beneficial to leave some control in the hands of the physicians, and to exert whatever control that the PPMC does retain in a less heavy-handed, and more selective, fashion.

# Tactics: How Radiology PPMCs Do What They Do

- Identify “high value” groups.
  - What does this mean?
  - It’s all in the eyes of the beholder.
- Engage in dialogue.
  - Emphasize the PPMC’s value proposition for the radiology group.
    - Today the “sell” by the PPMC is less about current monetization for the physicians of future earnings, rather . . .
    - The PPMC tends to focus on the additional revenue that the PPMC believes it can help generate for the radiology group.
    - Beware of simply accepting the PPMC’s propositions: challenge the assumptions.
  - Emphasize the level and types of control that the radiologists will retain.
    - Beware: the devil’s in the details.
  - To a certain extent, play to the insecurities, if not outright paranoia, of the radiology group.
    - The radiology group must have a realistic sense for its strengths and weaknesses, and for its relative position in the market served by the radiology group.
    - Beware of starting down the path to a deal with a PPMC, because it can be very difficult to turn around.
  - Connect the target with other radiology groups who are affiliated with the PPMC.
    - Beware of groups who have financial incentives to “gild the lily” (such as “founding groups”).

# Tactics: How Radiology PPMCs Do What They Do (cont'd)

- Determine a value for the practice (a “price”) and for the ongoing relationship (the “compensation”).
  - Beware of the “bait and switch.”
- Develop preliminary structure for the transaction.
  - **TAX, TAX, TAX (more in a later slide)!**
  - Don’t assume that certain structures won’t work.
- Persuade (co-opt?) the radiology group’s key leadership.
- Enter into a letter of intent (“LOI”) with a binding “no shop” provision.
  - Query how much effort should be put into the LOI?

# Tactics: How Radiology PPMCs Do What They Do (cont'd)

- Prepare documents.
  - Beware of “these are our documents, and we can’t move off of them.”
  - Beware of “trust us, that’s never going to happen.”
  - And beware of signing anything that’s:
    - Incomprehensible,
    - Just doesn’t make sense, or . . .
    - Potentially illegal.
  - If it’s important or needs more clarity, then put it in the documents.
- Negotiate the deal.
  - Beware of artificial pressure.
  - At the same time, remember that today’s world of radiology is much different from what it was 20, 10 or even 5 years ago.
- Close.

# Threshold Issues

- What's the deal that's on the table?
  - Purchase price and then ongoing compensation?
  - Carefully analyze any earnout because they are generally disfavored under the law.
  - Form of consideration, *i.e.*, cash, equity and/or debt?
- **TAX CONSIDERATIONS, PARTICULARLY AS THEY PERTAIN TO THE INITIAL “SALE,” MUST BE ADDRESSED AT THE OUTSET OF THE STRUCTURING PART OF THE DIALOGUE.**
  - **AND REMEMBER ANY TAX/ACCOUNTING “SKELETONS IN THE CLOSET” THE RADIOLOGY GROUP MIGHT HAVE.**

# Threshold Issues (cont'd)

- Critically important to “connect the dots.”
  - The interplay of all of the documents and all of the moving parts of the arrangement, on a going forward basis, can disguise somewhat insidious consequences for the radiologists.
  - So, put it all together and understand exactly what the radiology group is agreeing to and what the potential consequences are.

# Threshold Issues (cont'd)

- Impact on radiology group's relationship with its hospital(s).
  - When a radiology group does a deal with a PPMC, the radiologists likely, in effect, give up any meaningful control of the radiology group, and . . .
  - The PPMC's interest may not align with the interest of the group's hospital(s), so . . .
  - What happens if a conflict develops between the radiology group's hospital(s) and the PPMC?
- How much commitment is the PPMC making to the radiology group?
  - Are they willing to put it in writing?
  - Restrictive covenants?
  - Exclusivity and/or rights of first refusal?



# Document Issues

- Purchase Agreement.
  - Likely will be transacted as an asset purchase.
  - In certain states, might be able to transact as an equity acquisition.
  - Form of consideration , *i.e.*, cash, equity and/or debt.
  - Earnout (if any).
  - Reps and warranties.
  - Indemnification.
  - Escrow (if any).
  - Restrictive covenants.

# Document Issues (cont'd)

- Management Services Agreement.
  - Why it's used?
  - And when it might not be as important?
  - What is the PPMC supposed to do?
    - What does it control?
  - What is the radiology group supposed to do?
    - What does it control?
  - How does the PPMC get paid?
    - Need a “waterfall” provision describing order of priority for payments.
    - Should clearly state (not subject to amendment) that the radiologists get paid first, under their respective employment agreements, before the PPMC gets paid.
  - Restrictive covenants?
    - For radiology group?
    - For PPMC?
  - Amendments?
    - Beware if the PPMC has deployed a “friendly physician model” (see subsequent slide).

# Document Issues (cont'd)

- Employment Agreements.
  - What they require of each radiologist?
  - What does the group retain control over and what does the PPMC have control over?
  - How is compensation calculated and paid?
    - Base?
    - Incentive?
    - Draw plus bonus?
    - Regulatory compliance?
  - Expenses?
  - Professional liability insurance?
    - Obligation upon termination of the employment agreement?
  - Restrictive covenants?
  - Ability of radiologists to “talk among themselves.”
  - Term and termination?
    - Are they terminable without cause, and if so, is that desirable?
  - Amendments?
    - What if a single radiologist wants to terminate and/or amend her/his employment agreement?

# Document Issues (cont'd)

- Option Agreement.
  - Implements the “friendly physician model.”
    - What is this?
  - Why and how it accomplishes this?
  - When it might not be necessary.
  - Beware of how this agreement interacts with all of the other “going forward” agreements.
    - Management Services Agreement.
    - Employment Agreements.

Thank you!

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