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Buying and Selling Equity in Ambulatory Surgery Centers – 2023

AAO Instruction Course

San Francisco, November 4, 2023

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Financial Disclosures

Ms. Bibet-Kalinyak, Ms. Patterson, and Mr. Kothari have no financial interests or relationships to disclose.

Ms. Bibet-Kalinyak is legal counsel for the New Jersey Association of Ophthalmology (NJAO) and the New Jersey Association of Ambulatory Surgery Centers (NJAASC) however, she is not representing the NJAO or the NJAASC for purposes of this instruction course and is here solely in her capacity as Partner at the law firm of Brach Eichler L.L.C.

Objectives

- Investments in ambulatory surgery centers (ASCs) are both complex and financially beneficial for ophthalmologists. It is important, however, to understand both the financial and regulatory risks associated with such investments. Key objectives of this presentation include:
  - Understanding the financial aspects involved in investing in ASCs.
  - Understanding the key legal and regulatory requirements pertaining to ASC investments.

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ISABELLE BIBET-KALINYAK, ESQ., VICE CHAIR HEALTHCARE PRACTICE GROUP

Isabelle Bibet-Kalinyak is an experienced and creative healthcare attorney and proven deal maker representing "brick-and-mortar" and virtual multi-state healthcare clients in complex business transactions including private equity deals, hospitals and ambulatory surgery centers acquisitions and joint ventures, MSO structuring, strategic partnerships and compliance.

As Vice Chair of the Brach Eichler's Healthcare Practice Group, she counsels physicians, healthcare providers, hospitals, associations, Boards and management teams on the legal and strategic implications associated with various forms of corporate entities, healthcare integration models, compliance, payers, credentialing and emerging trends, laws, and regulations. The depth of Isabelle's experience enables her to assist clients in evaluating both the legal and business ramifications of transactions, contracts, agreements, negotiations, and compliance issues.

Her legal, business and operational acumen is keenly aligned with her role as legal counsel to six New Jersey medical societies:

- NJ Association of Ambulatory Surgery Centers (NJAASC)
- NJ Academy of Ophthalmology (NJAO)
- NJ American College of Obstetricians and Gynecologists (ACOG) Section
- NJ Obstetrical & Gynecological Society (NJOGS)
- NJ Orthopaedic Society (NJOS)
- NJ Society of Pathologists (NJSP)

Bar and Court Admissions

- New Jersey
- Ohio
- New York (pending)

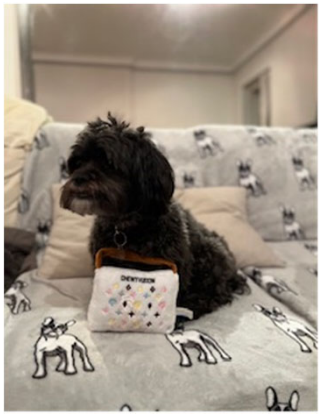
Education

- University of Akron School of Law, J.D., *magna cum laude*
- Kent State University, MBA
- Temple University, B.B.A. in Finance, *summa cum laude*
- Centre d'Etudes Franco-Américain de Management, B.B.A. in Finance

ISABELLE BIBET-KALINYAK, ESQ., VICE CHAIR HEALTHCARE PRACTICE GROUP *(continued)*

As one of the few French business attorneys in the U.S. and a first-generation immigrant herself, Isabelle's healthcare practice has over time organically expanded to trans-national business transactions and immigration. Isabelle brings vast knowledge and experience advising U.S. clients with operations in French-speaking countries as well as companies based in French-speaking countries seeking to expand in the U.S. Her expertise also spans immigration law, representing clients in employment-based immigration matters in healthcare, biotech, and manufacturing.

She frequently speaks at the national conferences of organizations such as the American Academy of Ophthalmology (AAO/AAOE), ASCRS/AAOE, the Medical Group Management Association (MGMA) and the American Health Lawyers Association (AHLA) and lectures on advanced topics related to healthcare, mergers and acquisitions, private equity and business immigration. A French native and former French Honorary Consul in Ohio for the French Government, Isabelle now resides in Connecticut with her furry son, Louie.



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CAROLINE J. PATTERSON, ESQ., PARTNER, HEALTHCARE PRACTICE GROUP

Caroline Patterson is a prominent healthcare and business attorney with a reputation for sound judgment, responsiveness, and a creative approach to achieving her client's legal and business objectives. Caroline concentrates her practice on a wide variety of transactional, corporate, and regulatory matters, including mergers, acquisitions, sales, strategic partnerships, joint ventures, private equity investments, HIPAA compliance, federal and state laws fraud and abuse laws, ownership and compensation arrangements, and employment negotiations. Caroline also has extensive experience advising investigators and clinical institutions on clinical trial agreements and clinical research law.

Caroline's clients include physician practices, hospitals, health systems, management service organizations, life science and other healthcare consulting companies, dental practices, physical therapists, ambulatory care facilities, and individual healthcare professionals. Caroline is a frequent lecturer and contributor to the American Academy of Ophthalmology (AAO) on advanced legal topics related to healthcare, including mergers, acquisitions, private equity, fraud and abuse, clinical research, and employment law matters.

Bar and Court Admissions

- New Jersey
- Pennsylvania
- U.S. District Court, Eastern District of Pennsylvania

Education

- Villanova University Charles Widger School of Law, J.D., cum laude
- Managing Editor, Villanova Law Review
- Cabrini University, B.A., magna cum laude

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CASCADE PARTNERS

RAJESH U. KOTHARI, CFA
MANAGING DIRECTOR, CASCADE PARTNERS

Rajesh U. Kothari (Raj) draws over thirty years of experience as an investor, a financial advisor, and an entrepreneur. He is the founder and a Managing Director of Cascade Partners, a private investment and investment banking firm where he assists companies with mergers, acquisitions, divestitures, and other corporate finance activities. In addition, Cascade Partners makes a variety of control and non-control investments in companies in the business service, high value manufacturing, technology, and healthcare sectors.

Prior to forming Cascade Partners, he was a co-founder of Seneca Partners, Inc., a similar investment banking and private investment firm where he completed nearly 50 transactions or investments. He also co-managed a healthcare focused private equity fund, Seneca Health Partners.

Prior to establishing, Seneca Partners, Raj was a Director at Beringea (formerly GMA Capital), a boutique investment-banking and venture capital firm. While there, he led numerous divestitures, recapitalizations, acquisitions, and other strategic transactions for clients across industries. In addition, he co-managed the firm's $70 million healthcare private equity fund, InvestCare Partners where he was responsible for identifying, evaluating, structuring, and providing on-going development of investment opportunities for the fund. He represented InvestCare as the Board representative for several of the Fund's investments. He has also served as an Investment Officer for ProVen Private Equity in London, England, a venture capital affiliate of Beringea. Raj began his investment career as a money manager, most prominently for Masco Corporation where he helped manage over $750 million in in pension assets. He left Masco to found Cranbrook Capital Management, a $650 million money management firm, where he was Treasurer and Director of International Investing.

Education

- University of Michigan, B.A., Masters of Business Administration

CASCADE PARTNERS

RAJESH U. KOTHARI, CFA
MANAGING DIRECTOR, CASCADE PARTNERS *(continued)*

He has extensive board service including current service at Celtic Bank (Board and Audit Committee), Crecera Brands, Northstar Bank, OHM Advisor (Board and Finance – Chair), CAP Foundation (Chair), Ascension – Michigan Market and the Foundation for Leaders Dogs for the Blind. Prior Board service includes Priority Health (Board & Chair Audit & Finance Committee), Micro Machine Company, LLC (Chair), MedBio, Inc., HR Certificates Institute, Amicas, Computer Dynamics, Active Health Management, VerNova, Critical Signal Technologies and RedPath Integrated Pathology.

In addition to his professional endeavors, Raj has helped establish several not-for-profit professional organizations which promote the investment community in Michigan. He was a founder of the Detroit chapters of both the National Association of Securities Professionals and The Indus Entrepreneur Association (TiE), for which he is a Charter Member. He served on the Boards of the Michigan Venture Capital Association and Great Lakes Entrepreneurs Quest (Chair) and as an elected Councilperson for the Village of Wolverine Lake, Michigan.

He has served as an Adjunct Professor at the University of Michigan Ross School of Business and served as the University of Notre Dame at the Gigot Center for Entrepreneurial Studies, the later for over 12 years. He was honored as one of Crain's Detroit Business's 40 Under 40. His other community interests include the Civil Air Patrol ("CAP"), a volunteer auxiliary of the United States Air Force where he has served for over 40 years. He is a Colonel in the CAP and most recently served as the Commander of Michigan Wing.

Raj, a Chartered Financial Analyst, earned both a Bachelors of Arts and a Masters of Business Administration from the University of Michigan. He currently holds the Series 7, 79, 24, and 28 licenses from FINRA.

ASC Investments

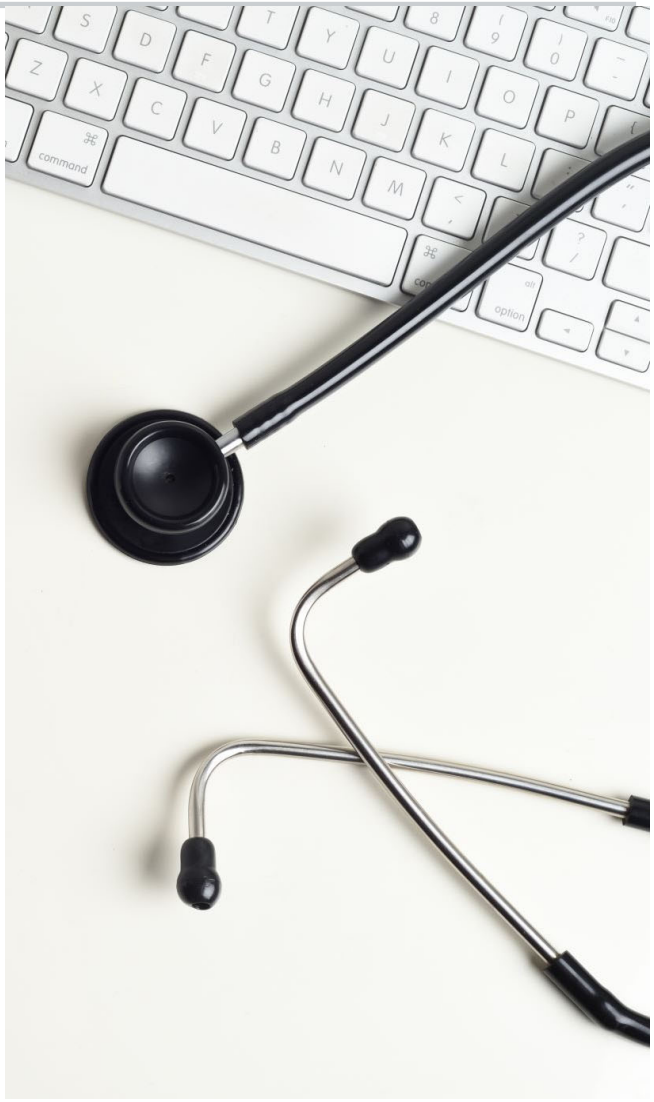
Positive Factors

- Ophthalmology generally remains independent as a medical specialty.
- More ophthalmologist owners than any other surgical specialty.
- Emergence of value-based care.
- Derive some return on investment from own cases.
- Ownership enables surgeons to tailor surgical environment and scheduling.
- CMS and commercial payers continue to allow more procedures to be performed in ASCs.
- Widely viewed as high quality and low cost.

ASC Investments

Negative Factors

- Proliferation of ASCs leads to competition to recruit surgical cases.
- Moratorium in certain states (NJ).
- Decline in number of “independent” physicians.
- Emergence of in-office surgery.
- High cost and scarcity of CRNAs.
- No Surprises Act and increased transparency requirements overall.



ASC Investments

Additional Considerations

- Single versus multi-specialty ASCs.
- Mix of ownership:
  - Most beneficial: Ophthalmology, orthopedics, gastroenterology, pain management.
  - Ownership by non-surgeon physicians (i.e., primary care physicians).
  - Ownership by non-surgeons (i.e., businesspeople, hospitals, retired physicians).
- Equipment.

Financial Implications

De Novo

- Up front cost to build out.
- Ability to finance.
- Certificate of Need (CON) states: Significant legal hurdles.
- Capacity utilization.
- Heavy overhead and operating expenses until surgical volume increases.
- Limited value if need to sell quickly.

Buying In Existing ASC

- Valuation of buy-in.
- Payback period.
- Fewer financing options than de novo projects.
- If limited operating history: Matching contributions and typically purchase from the ASC entity.
- Significant operating history: Multiple of EBITDA (earnings before interests, taxes, depreciation and amortization) and from hospital or physician owners

ASC – Potential Revenue Sources for Providers

- Professional fee for services personally performed.
- As owner of ASC, share of profits from facility fee revenue stream.
- As owner of Management Services Organization (MSO) managing the non-clinical services of ASC, share of profits from Management Services Agreement fees billed by MSO to ASC.
- As owner of real estate, share of revenue from lease.
- As owner of equipment (lasers), share of revenues from equipment leases.
- Some specialties can also derive revenue from lab services (if structured properly).

Evaluating the Opportunity

- Finances and legal.
- Governance documents:
  - Operating Agreement (LLC)
  - Shareholder Agreement (Corporation).
- What class of stock are you buying?
- Financial Statements
  - Federal income tax returns – 3 most recent years.
  - Financial statements and reports.
    - Balance Sheets
    - Profit and Loss Statements
- Capitalization table evidencing historical ownership.

Evaluating the Opportunity *(Continued)*

- Personal guarantees.
- Long-term debt or major contractual commitments:
    - Loans
    - Equipment leases
    - Real estate lease
- Real estate ownership:
    - Third-party landlord
    - ASC owners
- Historical liabilities: Medical malpractice lawsuits, Labor and Employment claims, HIPAA breaches…
- Legal due diligence

Partners/Buyers

- Hospitals.
- Public acquirers.
- Private-equity funds.
- Private ASC companies.
- Other physicians and providers.

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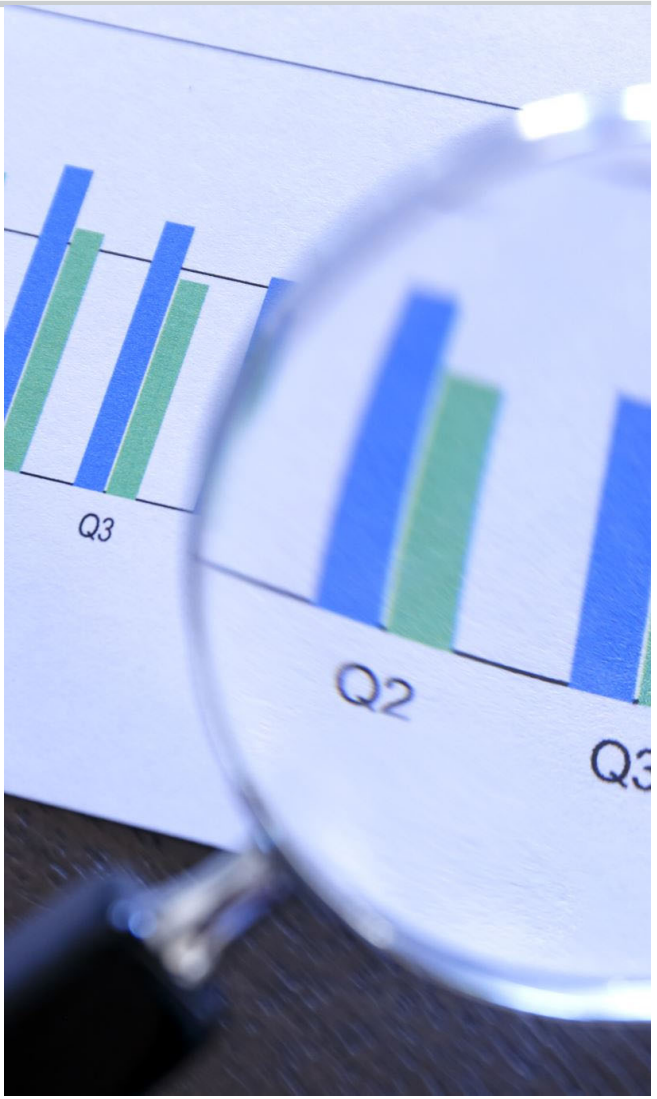
Fraud & Abuse Laws

State and Federal

- Anti-referral laws
- Quantity of equity interest and price of equity interest cannot be based upon case volume referred to ASC (past, present or future).



Payment Terms

ASC Fraud & Abuse Safe Harbors

- Payment in cash at time of sale.
- Financing OK but no seller financing or other form of direct or indirect financial support from seller or seller's affiliates.

Key Operating Agreement Terms

Case Volume Requirements

- Minimum requirement for staff privileges.
- ASC Fraud & Abuse Safe Harbors.
- Failure to fit 100% within safe harbor does not render structure illegal *per se*.

Key Operating Agreement Terms

ASC Safe Harbor

- Key Common Requirements to All ASC Safe Harbors:
    - Protects only return on investment.
    - Patients are informed of investment interests.
    - Terms of investment interests not related to referrals.
    - No loans or guarantees to purchase ASC interest.
    - Return on investment proportional to capital investment.
    - All ancillary services directly and integrally related to ASC procedures and not separately billed.

Key Operating Agreement Terms

ASC Safe Harbor - Single Specialty ASCs

- Physicians in same specialty or group practices comprised of such specialists.
- At least 1/3 of each physician investor's practice income for previous 12-month period must come from the physician's performance of procedures.
- Non-physician investors must not be employed by ASC or any investor, must not be in a position to refer to the ASC or any investor, and must not provide items or services to the ASC or any investor.

Key Operating Agreement Terms

ASC Safe Harbor - Multi-Specialty ASCs

- Mix of physician and group practice types.
- At least 1/3 of each physician investor's practice income for previous 12-month period must come from the physician's performance of procedures.
- At least 1/3 of each physician investor's procedures for previous 12-month period must be performed at the ASC.
- Non-physician investors must not be employed by ASC or any investor, must not be in a position to refer to the ASC or any investor, and must not provide items or services to the ASC or any investor.

Key Operating Agreement Terms

Ownership Non-Compete Restrictions

- Watch for conflict with employment-related restrictive covenants.
- During ownership and after divestiture.
- Geographic and time limitations: X years and X miles from ASC.
- Disclosure requirements.
- Legality?

Key Operating Agreement Terms

Restrictions on Transferability

- Who can you sell your interest to?
- What happens when you want to exit?
- Does the ASC entity *have* to buy you out or is it a mere *may* buy you out?
- Who has a first right of refusal?
- Is buy-out price set?

ASC Equity Interest Buy-Out Terms

Mandatory or optional?

How is price determined?

Events causing discounted buy-back price

Payment usually on a deferred basis

Ownership and corporate structure

Case Study

- Eyecare practice owned by ophthalmologists and optometrists.
- ASC is owned by practice (not a separate entity).
- Optometrists do not invest/fund the ASC; only the ophthalmologists do.
- Profits from the ASC are distributed among ophthalmologists only since they fund the ASC and bring all the cases.

QUESTIONS?

THANK YOU! MERCI BEAUCOUP!

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*No aspect of this advertisement has been approved by the Supreme Court of New Jersey.

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