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Newsletter, November 2014

Avoid Successor Liability when Buying a Medical Practice, including Provider Numbers and Taxes

In this article, I explain how to avoid successor liability when buying a medical practice, specifically as regards provider numbers and taxes. It's a nasty surprise to discover, after you've paid the purchase price for the practice, that you must pay the seller's debts and liabilities from before the closing.

Rule of Thumb: Buyer Assumes Liabilities in a Stock Deal, not an Asset Deal

The structure of the purchase initially determines whether the buyer will assume the liabilities of the seller. As a rule of thumb, the buyer assumes liabilities in a stock deal, but not an asset deal.

- In a stock deal, you buy the stock of the target corporation. The corporation does not change, other than getting you as the new owner. The corporation and all its assets and liabilities remain in place. This means the corporation keeps all liabilities that it had before you purchased it. In sum, you become the shareholder of the target corporation, which keeps its assets and liabilities in place.
- In an asset deal, your shell corporation buys the assets of the target company, and your shell only assume the liabilities and debts that you want. The buyer can pick and choose among the assets and liabilities of the seller. Hence you do not buy the target corporation; instead your shell corporation buys its assets, and leaves unwanted liabilities behind in the target company. After the deal, the seller still owns the target corporation, which keeps its debts and liabilities.

Most deals are structured as asset purchases to avoid the automatic assumption of unwanted debt. Usually you only do a stock deal if you need the target corporation itself. For example, the target might have contracts in place that you can't have assigned over to your shell corporation, or you need its tax ID number or provider number to keep a steady flow of Medicare or insurance reimbursements.

Provider Numbers

As I mentioned, sometimes a buyer wants to take assignment of the seller's provider number to ensure continuity in Medicare payments. I do not advise this. When you take a seller's provider number, legally you are assuming the seller's Provider Agreement. This means you assume the seller's obligation to repay all Medicare overpayments that were previously made to the seller, and you become liable for all other damages and penalties that the seller may owe to Medicare.

Get Your Own Number. I prefer that you get your own provider number before the purchase. I understand that the application process can take over a year, and that you might not be able to satisfy all conditions for issuance of the provider number before the purchase. Starting early will reduce your wait time to receive Medicare reimbursements, however. A short gap in reimbursements is worth the avoidance of liability. Start early.

In the alternative, if you feel you must take assignment of a provider number, then perform due diligence on the seller's Medicare liabilities, and holdback a portion of the purchase price to cover you for unexpected liabilities that flow to you through the seller.

Automatic Assignment of Provider Number. On the sale of certain defined providers, Medicare law automatically assigns the provider number and Provider Agreement to the buyer. The benefits of automatic assignment are (1) buyer receives uninterrupted Medicare payments; and (2) buyer is generally not required to undergo a survey by the accrediting organization. The cost is that the buyer automatically assumes the seller's outstanding Medicare debt and liabilities.

Automatic assignment usually does not apply to physician practices. It applies to rehabilitation facilities and agencies, home health agencies, clinics, and physical therapy facilities, among others.

Taxes

Taxes are a big exception to the general rule that, in an asset purchase, the buyer does not automatically assume the seller's debts. The buyer corporation (and even you, its shareholder, personally) can be liable, by operation of law, for a number of the target practice's tax obligations. Remember that the king writes the law, and the king gets paid his taxes no matter what, even by making the buyer responsible for the seller's taxes. Here is a list of the primary taxes for which successor liability applies:

- Federal income and social security taxes.
- CA sales and transfer taxes.
- CA payroll taxes including unemployment insurance contributions.

Conclusion: Protect Yourself

How does the buyer protect itself from the liabilities of the seller (in an asset deal)? In all cases, the buyer should perform an extensive due diligence on the purchased practice, and demand representations in the purchase agreement for problem areas. For tax liabilities, consider getting tax clearances. Lastly, the buyer can require that the seller leave a portion of the purchase price in escrow, or the buyer can pay a portion of the price via promissory note, in both cases to ensure that funds are available to cover any undisclosed liability flowing through seller.

Call me if you want to talk more.



Thanks to Dan Kiser for this one.