



# BUYING AND SELLING A DME SUPPLIER

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# INTRODUCTION



# INTRODUCTION

- From a purchaser's standpoint, acquiring a DME supplier has challenges that are not normally associated with non-health care industries.
- For example:
  - Being dependent on Medicare is a mixed blessing. Medicare may, pursuant to a post-payment audit, recover revenue it has previously paid. Further, if a large portion of the supplier's gross revenue is dependent on a competitive bidding contract, then there is a risk that the competitive bidding income will disappear if the supplier's re-bid for the contract is not accepted. As a result, from a purchaser's standpoint, financial statements (balance sheet and profit/loss statement) that initially look attractive might end up becoming less attractive.

# INTRODUCTION

- From the government's standpoint, the ability of a supplier to successfully collect revenue is dependent on the supplier's documentation. If the documentation is sloppy or non-compliant with reimbursement rules, then even though services or products may have been provided, the supplier will not be able to collect its revenue. Likewise, non-compliant documentation can lead to an unfavorable post-payment audit.
- If a supplier has engaged in past fraudulent practices (e.g., payment of kickbacks or billing fraud), then it can be liable to the government for a great deal of money.

# INTRODUCTION

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- When acquiring a supplier through a stock purchase, the acquired company carries with it the liabilities that arose prior to the purchase. When acquiring a supplier through an asset purchase, the purchasing entity is usually not liable for prior acts of the selling entity.



# WHAT A PURCHASER LOOKS FOR IN ACQUIRING A SUPPLIER



# WHAT A PURCHASER LOOKS FOR . . .

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- Product Mix

- How much of the seller's business is related to
  - (i) Medicare-covered products that fall under competitive bidding,
  - (ii) Medicare-covered products that do not fall under competitive bidding,
  - (iii) Medicaid-covered products,
  - (iv) products covered by commercial insurance,
  - (v) products that are cash only,
  - (vi) products that require a physician's order, and/or
  - (vii) products that do not require a physician's order?

# WHAT A PURCHASER LOOKS FOR . . .

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- Provider and Supplier Number Issues
  - How many physical locations does the selling supplier have?
  - Does the selling supplier have a DMEPOS supplier number and-or a Medicaid provider number for each location?
- Payer Mix
- Competitive Bidding Contract
  - Is the selling supplier a party to a competitive bidding contract?
- Medicaid Issues
  - Is the selling supplier a qualified provider to one or more state Medicaid programs?



# WHAT A PURCHASER LOOKS FOR . . .

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- Employment and Independent Contractor Issues
- Referral Source Issues
  - Does the supplier have any written or verbal relationship with health care referral sources such as physicians, hospitals, home health agencies or respiratory therapists?
  - Do these arrangements comply with applicable safe harbors and Stark exceptions?

# WHAT A PURCHASER LOOKS FOR . . .

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- Documentation Issues
  - Does the selling supplier have appropriate documentation in the patients' files?
- Numbers, Licensure, and Sanction Issues
  - Have any numbers, licenses, permits, registrations, or certificates of authority to operate any part of the selling supplier ever been revoked, suspended, investigated, or voluntarily surrendered?

# WHAT A PURCHASER LOOKS FOR . . .

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- Litigation, Audits, and Reviews
- Legal
- Financial
  - A purchaser will carefully examine a seller's financial statements and related documents.
- Understanding Day-to-Day Operations



# HOW A SUPPLIER CAN MAKE ITSELF ATTRACTIVE TO A PURCHASER



# MAKING SUPPLIER ATTRACTIVE . . .

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- Financial Statements
  - The selling supplier should have a CPA prepare a current balance sheet (statement of assets and liabilities) and a year-to-date profit and loss statement (statement of income and expenses).
- Income Tax Returns
  - The selling supplier should have copies of federal and state tax returns for the last three calendar or fiscal years.

# MAKING SUPPLIER ATTRACTIVE . . .

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- Billing Audit
  - The selling supplier should contract with an outside billing consultant for an on-site visit to conduct a mock audit of the supplier's documentation and billing procedures.
- Medicare Supplier Numbers
  - The selling supplier needs to verify that it has an active Medicare supplier number for each of its locations from which it services Medicare beneficiaries.

# MAKING SUPPLIER ATTRACTIVE . . .

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- Medicaid Provider Numbers
- Employees and Independent Contractors
  - The selling supplier needs to examine its relationship with each individual who is involved in marketing on behalf of the supplier (“marketing rep”).
  - If the selling supplier designates a marketing rep as an employee, then the supplier must assure itself that the marketing rep will be classified by the IRS as a bona fide employee.

# MAKING SUPPLIER ATTRACTIVE . . .

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- Referral Sources
  - The selling supplier needs to verify that it is not paying any remuneration to any referral source in exchange for referrals and/or arranging for referrals.
  - Additionally, the selling supplier needs to be able to assure the purchaser that the referral sources are loyal to the supplier because of the excellent service the selling supplier has given over the years to its customers.



# MAKING SUPPLIER ATTRACTIVE . . .

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- Documentation
  - The selling supplier needs to verify that it has the appropriate documentation in the patients' files.
- Numbers, Licenses, and Permits
- Audits, Reviews, and Investigations
- Litigation
- Customer Satisfaction

# MAKING SUPPLIER ATTRACTIVE . . .

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- Often, the purchaser will attempt to reduce the purchase price if the purchaser concludes there are uncertainties that might affect the value of the acquired supplier subsequent to closing.
- By addressing these issues prior to entering into negotiations with the purchaser, the selling supplier will be in the position to insist on the best purchase price possible.



# STOCK VERSUS ASSET ACQUISITION



# STOCK VS. ASSET ACQUISITION

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- In an asset acquisition, as a general rule, the purchaser does not assume any liabilities of the seller except for the liabilities that the purchaser expressly agrees to assume.
- Most importantly, if the seller has engaged in prior fraudulent activities, then generally speaking, the government will not attempt to impose successor liability on the purchaser.
- Medicare Part B supplier numbers (PTANs) are tied to tax identification numbers. In an asset acquisition of a DME supplier, the acquired DME operation will be continued under a new tax ID number (the purchaser's tax ID number).

# STOCK VS. ASSET ACQUISITION

- If the purchaser moves the acquired DME operation to an existing DME location owned by the purchaser (for which the purchaser already has a supplier number), then there will be no requirement for the purchaser to apply for a new supplier number.
- However, as is often the case, if the acquired DME operation will be continued at the seller's old location, or at a different location, then the purchaser will need to apply for a new supplier number for that location.

# STOCK VS. ASSET ACQUISITION

- Before submitting an application for a new supplier number, the purchaser must
  - (i) be accredited for the new location and
  - (ii) have a state DME license for the new location. In addition, the purchaser must have a surety bond for each location that has a supplier number issued to it.
- It takes months to obtain a new supplier number from the National Supplier Clearinghouse (“NSC”).

# STOCK VS. ASSET ACQUISITION

- Normally, during the interim period, the purchaser can sell products and services out of the new location, can accrue the claims to be submitted at a later date, but cannot actually bill for the claims until the new supplier number is received. In short, the purchaser will experience a cash flow crunch.
- On the other hand, in a stock acquisition, the DME operation remains with the same corporation (the entity whose stock is sold) and the supplier number remains attached to the same tax ID number (the corporation whose stock is sold to the purchaser).

# STOCK VS. ASSET ACQUISITION

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- Therefore, there is no break in billing and the purchaser does not experience a cash flow interruption.
- The downside is that if the selling corporation engaged in prior activities that result in an overpayment or a recoupment demand or in an allegation of fraud, then the selling corporation remains liable for the prior activities.





# STEPS TO BRING AN ACQUISITION TO FRUITION



# BRING ACQUISITION TO FRUITION

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- The purchaser and seller should each employ an experienced transactional attorney and an experienced health care regulatory attorney.
- The purchaser and seller will initially execute a confidentiality/non-disclosure agreement.
- This will allow the seller to forward financial and other confidential data to the purchaser so that the purchaser can make a preliminary determination as to whether it wishes to follow through with the acquisition. Once the purchaser decides that it wishes to follow through with the acquisition, then the parties will sign a non-binding letter of intent.

# BRING ACQUISITION TO FRUITION

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- When executing the letter of intent, the purchaser and the seller will have decided whether the acquisition is an asset acquisition or a stock acquisition.

# BRING ACQUISITION TO FRUITION

- Between the time of execution of the letter of intent and the time of execution of the definitive agreement, the purchaser will conduct due diligence.
  - Financial Due Diligence entails the review of bank statements, cash flow statements, tax returns, and financial statements.
  - Corporate Due Diligence entails reviewing documents to confirm that the seller is a legal entity in good standing.
  - Regulatory Due Diligence entails reviewing documents to confirm that the seller is compliant with health care statutes and regulations.

# BRING ACQUISITION TO FRUITION

- The seller and purchaser will then execute the definitive agreement.
- The purchaser will desire to pay as little cash up front as possible and to pay as much of the purchase price on the back end as possible.
- If problems do arise following closing, then the definitive agreement will give the purchaser the right to offset a portion of the purchase price (to be paid on the back end) against the damages to be sustained by the purchaser as a result of the unanticipated problems following closing.
- On the other hand, the seller will desire to be paid as much cash up front as possible and to receive as little of the purchase price on the back end as possible.

# BRING ACQUISITION TO FRUITION

- At closing, the parties will execute the appropriate documents necessary to transfer assets or assign stock, assign leases or sublet premises, assign contracts and other documents necessary to transfer the business.
- Also, prior to closing, the purchaser will ascertain which employees of the seller that the purchaser wishes to retain.
- As a condition of closing, the purchaser may require that the principals of the seller remain as employees of the purchaser for a period of time (e.g., six to twelve months).

# BRING ACQUISITION TO FRUITION

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- As a condition of their employment, the principals of the seller will introduce the purchaser and the purchaser's management and employees to key referral sources.
- Principals of the seller will have to execute reasonable non-compete/non-disclosure agreements.



# ROLE OF A BROKER





# INTRODUCTION

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- Often, a selling DME supplier will hire a broker to (i) locate prospective buyers and (ii) facilitate the sale.
- But what is it, exactly, that the broker does?

# INITIAL BROKER CONTACT

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- The selling supplier will have an initial conversation with the broker about the seller's goals and objectives.
- If the selling supplier is interested in further discussion, the broker will furnish a Mutual Non-Disclosure Agreement (“NDA”) to the selling supplier so that the broker and selling supplier can discuss the selling supplier's interests confidentially.
- Once the NDA is signed, the broker will forward a request for more detailed information, including financials.

# REVIEW OF OPTIONS

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- The broker will review the selling supplier's performance and its responses to the broker's Preliminary Client Review.
- Following the review, the broker and supplier will discuss the supplier's options.
- This discussion will lead to one of these outcomes:
  - A decision to proceed with a potential transaction,
  - A decision not to proceed, or
  - A decision to delay moving forward.
- In this latter case, the broker will discuss the next steps with the selling supplier.

# FEE AGREEMENT

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- If the selling supplier decides to proceed, the broker will forward a Fee Agreement (“FA”) for the supplier’s review.
- The FA includes the broker’s fees, terms, exclusions, and a copy of the selling supplier’s Confidentiality Agreement (“CA”) that all prospective buyers must sign prior to receiving information about the selling supplier.

# MARKETING BOOK DEVELOPMENT

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- A Confidential Information Memorandum (“CIM”) will be developed to market the selling supplier to potential buyers.
- The broker will request further information it will use in developing the selling supplier’s CIM.
- This phase is often demanding for sellers as the broker requests considerable detailed information on the selling supplier and marketplace.
- The CIM will be approved by the selling supplier prior to finalization.

# MARKETING

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- The broker utilizes a variety of marketing approaches to attract qualified buyers and the broker will review these with the selling supplier in advance, as well as during the marketing process.
- Often, potential buyers will request a conference call, or even a visit with the selling supplier.
- Potential buyers may also request additional information.
- The broker will be involved in the calls and will document and track information requests.
- The broker will update the selling supplier regularly during this process.

# LETTER OF INTENT & NEGOTIATION

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- When a potential buyers is sufficiently interested in the purchase of the selling supplier, the buyer will present a Letter of Intent (“LOI”) to the selling supplier and its broker.
- The LOI briefly outlines the transaction terms, including sales price, non-compete agreement, and other similar conditions.
- A LOI can be terminated relatively easily, but a seller has to abide by the confidentiality and exclusivity or “no shop” clauses, which means that the selling supplier cannot talk to other potential buyers after it signs the LOI.

# DUE DILIGENCE

- Upon signing a LOI, the selling supplier will begin providing more detailed information to the potential buyer, including: copies of leases, contracts, employee information, etc.
- During this process, the selling supplier, its accountant, and its attorney will begin the review of the proposed final contract documents (“Definitive Agreement,” “Purchase Agreement,” or “Sales Agreement”).
- A checklist is developed to help make the process more transparent.
- The broker may provide a virtual data room to securely store all data for review by all parties.
- The broker will continue to provide support throughout this process.



# DEFINITIVE AGREEMENT

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- As the selling supplier approaches the closing of the transaction, it will be negotiating the final points in the agreement, notifying parties (regulatory boards, employees, and others) about the transaction and proposed timelines, and determining the activities necessary for a closing.

# CLOSING & POST CLOSING

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- At closing, the final documents are completed and the electronic transfer of funds takes place to complete the transaction.
- After closing, there may be certain activities that must be performed. These could be the collection of accounts receivable, criteria for escrow accounts, or earn-outs. The broker will be available to assist the selling supplier post-closing.



# ASSET PURCHASE: POTENTIAL SUCCESSOR LIABILITY



# ASSET PURCHASE: POTENTIAL . . .

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- As previously discussed, an upside for engaging in an asset acquisition is that, as a general rule, the purchasing entity is not liable for any of the selling entity's liabilities.
- Over the years, the Department of Justice has taken the position that the purchaser of assets *might* be responsible for the seller's pre-closing fraudulent acts if the asset purchase is a “de facto merger.”
- A recent federal appellate court decision illustrates how such a de facto merger might arise.

# ASSET PURCHASE: POTENTIAL . . .

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- Eriem Surgical, Inc. (“ESI”) purchased the assets of Micrins Surgical, Inc. (“MSI”) shortly after it closed its doors.
- In so doing, ESI (i) hired MSI’s former employees, (ii) took over the MSI facilities, and (iii) took over usage of MSI’s trademark, website, phone number, and e-mail address. ESI is owned by the wife of a large stockholder of MSI.
- The IRS took \$400,000 from ESI’s account to pay \$400,000 owed by MSI to the IRS.

# ASSET PURCHASE: POTENTIAL . . .

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- The federal district court (trial court) upheld the IRS's treatment of ESI as a "continuation of MSI."
- The 7<sup>th</sup> Circuit Court of Appeals upheld the trial court's decision.



# QUESTIONS?





# THANK YOU

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