

K&L|GATES

WAYPOINT
HEALTH CARE ADVISORS

FULBRIGHT
& Jaworski L.L.P.

“Deal Risk” Management Strategies

Third Annual

Southwest Healthcare Transactions Conference

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Dallas

Introduction of Panel Members

Mike Austin, Managing Director

WayPoint Health Care Advisors

Jon Henderson, Partner

K&L Gates LLP

Todd Kelly, Partner

Fulbright & Jaworski L.L.P.

Jim McCoy, Managing Director

WayPoint Health Care Advisors

Mergers and Acquisitions Gone Wrong



Looks like UPS wins!



... must have been the FedEx driver ...

Can you get there from here?



Deal Risk Management

Types of Deal Risk

- ◆ Pre-signing - negotiation and letter of intent stage
- ◆ From signing to closing
- ◆ Post-closing
- ◆ Structural risks
- ◆ Financial risks
- ◆ Regulatory compliance risks
- ◆ Operational risks

Deal Risk Management

High Risk Deal Issues

- ◆ Changes in law
- ◆ Compliance with law
- ◆ Changes in coverage
- ◆ Changes in reimbursement
- ◆ Changes in financial condition
- ◆ Provider enrollment
- ◆ Third-party claims
- ◆ Undisclosed liabilities
- ◆ Personnel
- ◆ Anti-trust
- ◆ Accreditation
- ◆ Excluded persons
- ◆ Licensure and certification
- ◆ Radioactive materials, radiation machines
- ◆ Tax-exempt status

Deal Risk Management

High Risk Assets

- ◆ Physician contracts (employment, service, medical director, JV)
- ◆ Managed care contracts
- ◆ Real property
- ◆ Deferred tax assets
- ◆ Governmental provider/supplier agreements and provider numbers
- ◆ Controlled substances and radioactive materials
- ◆ Personnel and non-compete agreements
- ◆ Medical records
- ◆ Licensure and certification

Deal Risk Management

Real Life Post-Closing Claims

- ◆ Successor liability (e.g. recoupment, false claims, cost report settlements)
- ◆ Malpractice liabilities
- ◆ Tax liabilities
- ◆ Employment liabilities
- ◆ Environmental liabilities
- ◆ Pre-closing contracts and payables
- ◆ Pre-closing claims/unripe lawsuits

Due Diligence and Risk Management

Due Diligence Prioritization and Coordination

Due Diligence

- Durability – Business model strengths and weaknesses
- Vulnerability – Potential failures in core business functions
- Exposure - Post closing claims

Deal Structure

- Apply risk mitigation techniques and tools
- Assess the prospective ability to address risk through deal terms
- Deal Terms Study
- Experience
- Develop transition and integration plan

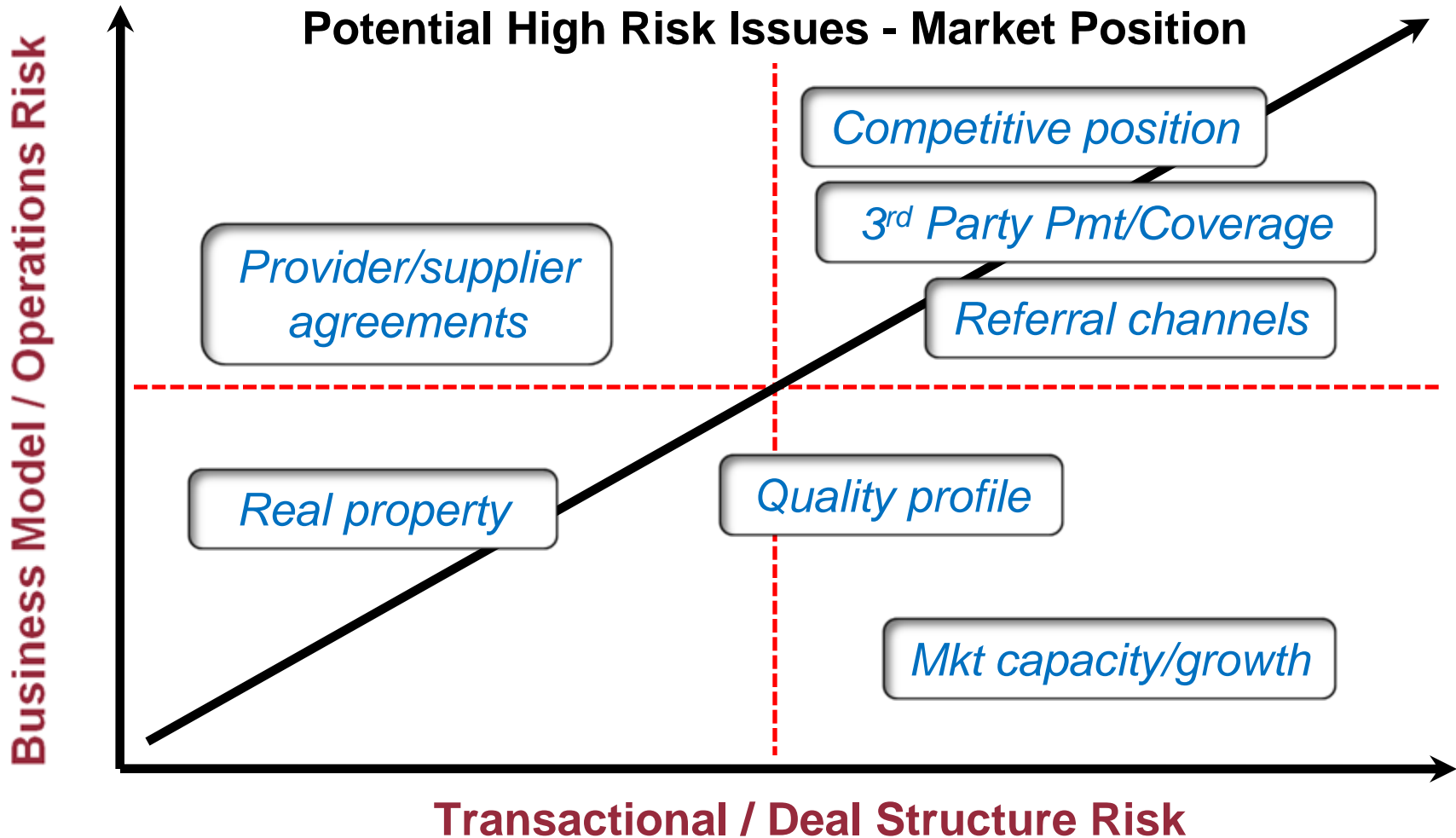
Post Closing

- Execute transition / integration plan
- Post closing claim risk management

Due Diligence and Risk Management

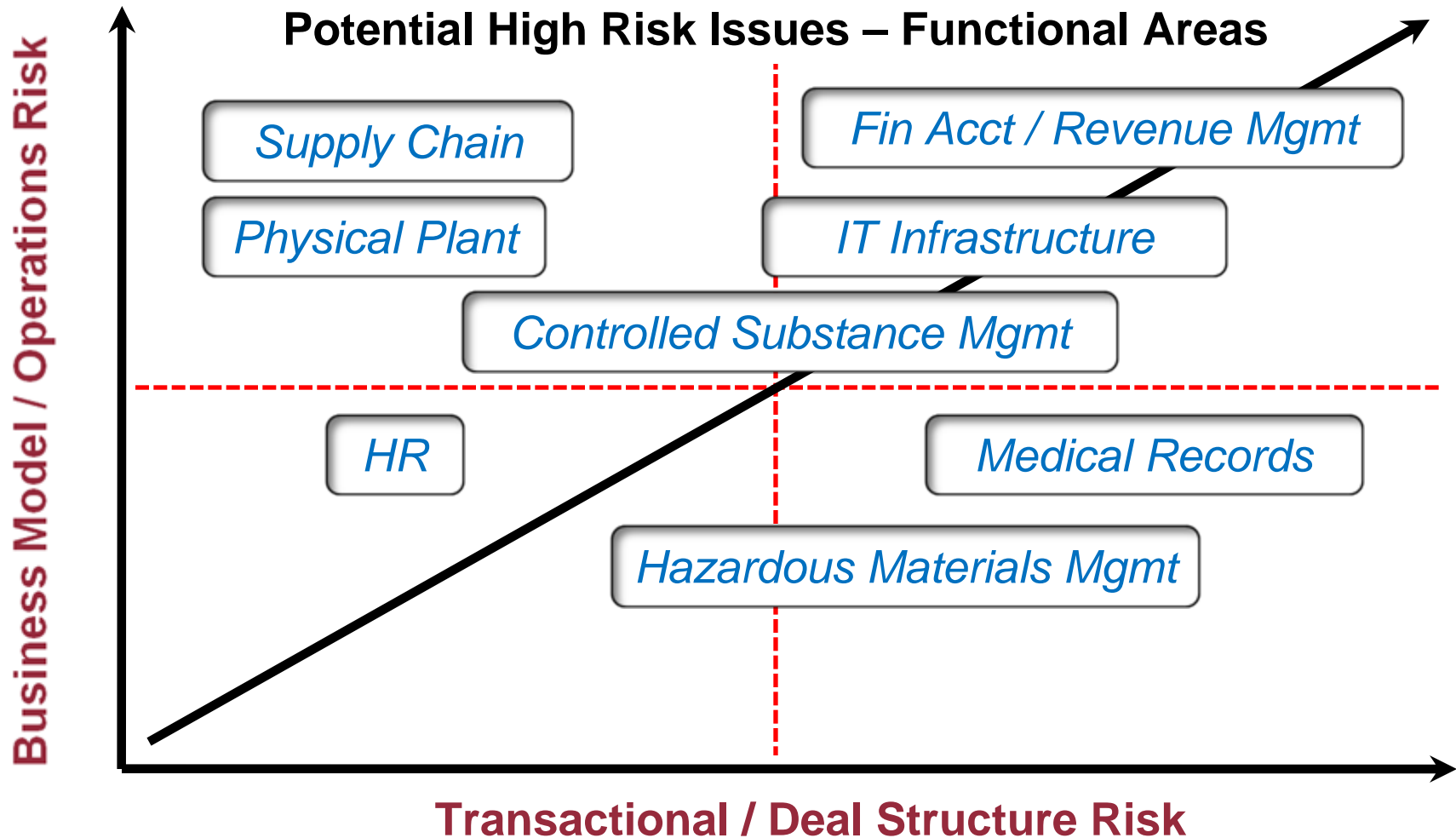
Due Diligence Prioritization and Coordination

Potential High Risk Issues - Market Position



Due Diligence and Risk Management

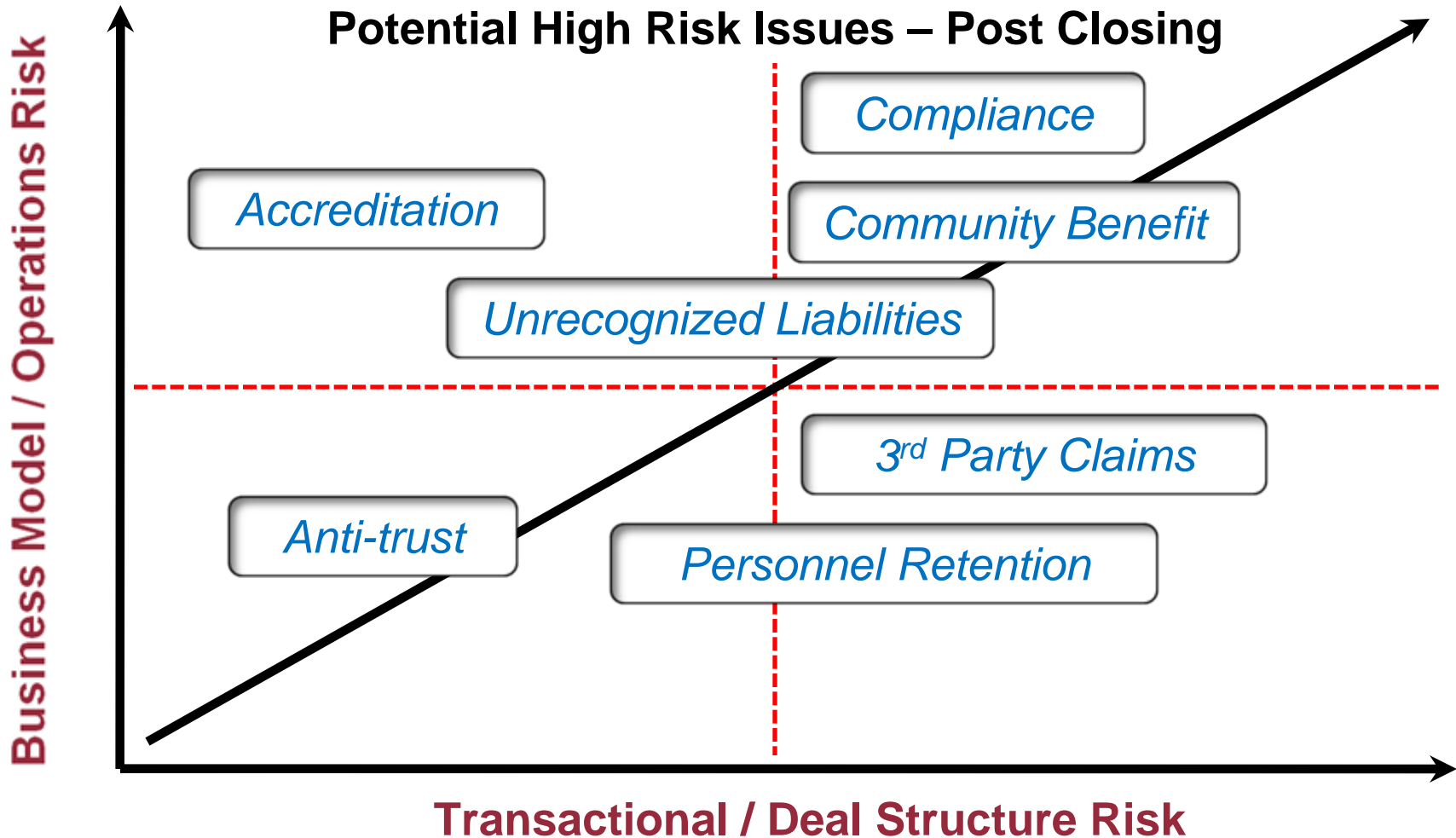
Due Diligence Prioritization and Coordination



Due Diligence and Risk Management

Due Diligence Prioritization and Coordination

Potential High Risk Issues – Post Closing



Deal Structure and Terms

Risk Mitigation Techniques and Tools

- Asset vs. stock purchase
- Simultaneous vs. delayed sign and close
- Representations and warranties
- Material adverse change clause
- Indemnities
- Guarantees
- Escrows/Holdbacks
- Continued existence of seller
- Restrictive covenants

Deal Structure and Terms

Representations and Warranties - Concepts

- ◆ Qualifiers to reps and warranties
 - Materiality
 - Knowledge
 - Due diligence and reliance
 - As-is, where-is
 - Sandbagging/Anti-sandbagging

Deal Structure and Terms

Indemnities - Concepts

- ◆ Survival
- ◆ Baskets and deductibles
- ◆ Caps
- ◆ Carve-outs
- ◆ Limitations
- ◆ Rights and obligations to defend
- ◆ Exclusive remedies

Deal Risk Management – What’s Market

Risk Mitigation Statistics ^[1]

Material Adverse Effect

	<u>Public Target</u>	<u>Private Target</u>
◆ Defined/Included	97%	92%
◆ Forward looking (“could reasonably be expected to have”)	n/r	74%
◆ Buyer’s ability to operate	n/r	6%
◆ Carve-outs included	98%	79%
	n/r (not reported)	

^[1] See Mergers & Acquisitions Market Trends Subcommittee, American Bar Association, 2009 Private Target Mergers & Acquisitions Deal Points Study (2009).

Mergers & Acquisitions Market Trends Subcommittee, American Bar Association, 2009 Strategic Buyer/Public Target Mergers & Acquisitions Deal Points Study (2009).

Deal Risk Management – What’s Market

Risk Mitigation Statistics

“Knowledge”

- Defined

- Actual
- Constructive

Public Target

n/r

Private Target

93%

25%

68%↑

n/r (not reported)

Deal Risk Management – What's Market

Risk Mitigation Statistics

Compliance with Law

	<u>Public Target</u>	<u>Private Target</u>
■ Included	99%	100%
● Covers past and present	22%	71%↓
● Covers past to specified date	35%	n/r
● Covers current compliance only	43%	n/r

n/r (not reported)

Deal Risk Management – What's Market

Risk Mitigation Statistics

“10 b-5”/Full Disclosure Rep

	<u>Public Target</u>	<u>Private Target</u>
■ Included	2%↓	68%↑
● No untrue statement or omission of a material fact (“10 b-5”)		
● Seller has no knowledge of adverse facts not set forth (“Full Disclosure”)		

Deal Risk Management – What's Market

Risk Mitigation Statistics

Indemnity

	<u>Public Target</u>	<u>Private Target</u>
■ Escrow/Holdback	n/r	81%
■ Sandbagging	n/r	
● Pro-sandbagging included		39%↓
● Anti-sandbagging included		8%↓
● Silent		53%↑
■ Survival of reps	n/r	
● <12 mos.		0% [2]
● 12-24 mos.		88%
● >24 mos.		6%

[2] 4% expressed no survival period

n/r (not reported)

Deal Risk Management – What's Market

Risk Mitigation Statistics

Indemnity

	<u>Public Target</u>	<u>Private Target</u>
■ Baskets	n/r	
● Deductible – type		47%↓
● 1st dollar – type		36%
● ≤.5% threshold		44%
● .5% – 1.0% threshold		45%
■ Caps	n/r	
● Mean		21.72%
● Median		11.2%
● Biggest grouping – less than 25%; majority of those: 10% or less		

not reported (n/r)

For more information, please contact:

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THANK YOU!