Why Should My Medical Group Explore Strategic Options:

Top Three Reasons To Consider A Transaction

Why My Medical Group Should at Least "*Explore*" Strategic Options

In light of various factors (see next 3 pages), a strategic transaction or partnership may be beneficial to certain physician groups ***– but it's not right for every group, and some groups will decide that staying independent is right for them***.

But, before making the decision to "stay the course" and remain independent, medical groups should at least explore different strategic options by "dipping their toes in the water" via obtaining and reviewing the terms of various potential partnership opportunities, and assessing the pros and cons of each. This will enable groups to make truly informed decisions regarding whether a strategic transaction may position their physicians most optimally for both short- and long-term survival and profitability, or if staying independent is their best option.

Different options to consider in this "exploration/assessment" process include potential arrangements with local hospitals, with large/mega physician groups in the region (single or multi-specialty), with national health care companies, or with private equity funded specialty platforms.

Over the last 2-3 years, many physician practices have pursued strategic partnerships with private equity platforms more than with hospitals and others, and the next several pages set forth the top reasons why this is happening.

Physicians rarely recommend a surgical procedure to their patients without assessing different options. Physicians rarely buy a new home without visiting different houses for sale in their general price range.

Officers, leaders and boards of physician groups likewise should be exploring the terms, pros and cons of different strategic options before potentially deciding that it's in the best interest of their group to remain independent. This is not only common sense, but also consistent with their fiduciary duty as leaders of their practice.

Top Three Reasons to Consider a Private Equity Transaction

1. Monetizing "True Value" of Your Practice.

a. Right now, medical practices are at (or near) the ***height of their market value***

b. If a practice doesn't transact, then it won't be able to ***lock-in its current high value*** for the benefit of all of its physician owners

   I. Instead, upon their retirement, disability or other departure from the practice, each physician's ownership interest will be redeemed based on the financial terms of their Shareholder/Operating Agreement, ***which usually results in a very small buyout price***.

   II. Thus, it makes sense for all owners of a medical practice – late career, mid-career and early career – to pursue a transaction while the market is at (or close to) its height.

c. Also, there are many risks in the healthcare industry (see Item 2 below), which causes there to be future uncertainty in many respects (e.g., reimbursement, competitive landscape, etc.) – and which may result in lower practice profitability and lower practice value in the future.

   I. Due to such future uncertainty/risks, many practices are ***transacting to "take some chips off the table" now*** (at the height of the market), with each physician receiving very large ***multi-million dollar checks,*** and investing such proceeds how they see fit (nest egg, etc.).

d. Importantly, most of these multi-million checks are received at ***advantageous long-term capital gain tax rates*** – versus 18-20% higher "ordinary income" rates.

   I. ***Benefit from tax arbitrage*** *on normalization/reduction in compensation in exchange for double digit multiple of lower rates.*

   II. ***BUT, the Biden administration is proposing to increase tax rates*** for long-term capital gains, and if enacted into law, the existing lower tax rates may disappear.

e. Moreover, investor platforms that partner with medical groups in these transactions likely will be "exiting" their investment within 3-6 years (aka "second bite" transactions). Over this time such investor's equity – ***as well as the physicians' rollover equity -- will increase (generally 2-4 times), and result in a second-bite "liquidity" event for physicians, who generally will cash out 50-75% of such greatly increased value,*** to be invested thereafter as such physicians see fit.

   I. Not only is this beneficial for physician owners at all stages of their careers, but additional "exit" transactions may occur every 4-6 years thereafter, in each case resulting in additional liquidity (cash out payments) for physicians with rollover equity, ***which makes these transactions especially beneficial for early and mid-career physicians*** (as opposed to physicians who retire within 3-5 years of the initial transaction and will not be able to participate in these potential additional exit/liquidity transactions).

2. Future Risks & Uncertainties: Market Share, Reimbursement & Regulations

a. There are local and regional market risks impacting practices, such as changing reimbursement and regulatory programs, and therefore increasing uncertainty and risks in the future

b. Continued consolidation by new market entrants (i.e., Optum, health systems, private equity) results in larger and ***more well-capitalized competitors that may erode a practice's market share***

c. Acquisitions of independent primary care referral sources by local hospitals, regional multi-specialty groups and national companies (e.g., Optum) may change existing referral sources and patterns

d. There is uncertainty in light of future reimbursement changes that likely will impact Medicare and commercial payors rates and payment methodologies.

e. There is a slow but ongoing shift from fee-for-service to ***value-based payment structure, population health and risk*** programs (benefiting larger organizations such as health systems, Optum, HopCo, etc.)

f. Expertise in direct contracting with self-insured employers will become more important, as that model of healthcare delivery and reimbursement continues to grow

Physician practices that are part of larger organizations with extensive corporate infrastructure (see Item 3 below) will be best positioned to adapt to these future uncertainties, changes and risks in a manner that continues successful operations and profitability.

3. Benefits of Larger Corporate Infrastructure for Growth and Continued Success

a. ***Greater access to capital*** to fund ongoing clinical and non-clinical practice operations, including new offices, recruiting new physician, and ancillary service expansion, as well as to fund the economic impact of the next pandemic or other market interruption – all ***without reducing physician compensation.***

b. ***Experienced/sophisticated corporate executives*** to successfully guide the practice through many competitive challenges and industry changes: CEO, CFO, COO, CIO, VP of HR, VP of Managed Care, Finance Director, Billing Director, Credentialing Director, Compliance Officer

c. ***Substantial investment in the latest information technology, advanced data analytics, EMR and virtual care platforms to best compete and succeed in the changing environment***

d. ***Cost savings through the consolidation*** of back-office functions (e.g., mid-level management, revenue cycle function, IT systems, call centers, etc.)

e. ***Lowering costs ("economies of scale")*** via group purchasing of health benefits, malpractice insurance, expensive equipment and supplies, etc.