



Healthcare Buyouts 101

Virtual Event

October 8, 2020

October 9, 2020

Sponsored by:





Healthcare Buyouts 101: New Analyst Training

October 2020

AGENDA

Day 1 – Thursday, October 8th (afternoon)

Noon -	12:15	Welcome - HCPEA Overview	Melissa Gardiner – Executive Director, HCPEA
12:15 -	1:00	Healthcare Industry Overview & Trends	Anirudh Goel, Vice President – EY-Parthenon
1:00	2:00	Legal considerations	Rob Goldstein, Partner – McDermott Will & Emery LLP
2:00	2:15	Break	
2:15	3:15	Washington Council	Heather E. Meade, Principal – Washington Council Ernst & Young
3:15 -	4:15	Keynote	Tom Flynn, Managing Partner – SV Health Investors
4:15	5:00	Virtual Networking Break	HCPEA YL members (by geography)

Day 2 – Friday, October 9th (morning)

9:00	10:30	Foundational deal considerations	Financial including: <u>Quality of earnings, Debt and debt-Like items, and Net Working Capital</u> – Brian Mabry, Senior Manager; Will Bailey, Manager; Austin Berning, Manager – EY Strategy and Transactions <u>Analytics</u> – Rob Del Vicario, Senior Manager – EY Strategy and Transactions
10:30	10:45	Break	
10:45 -	Noon	Other Deal considerations	Tax: <u>changes, diligence, and structuring considerations</u> – Chris Wheeler, Managing Director – EY Strategy and Transactions <u>Integration</u> – Lauryl Campbell, Director – EY Strategy and Transactions

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Perspectives on the U.S. Healthcare System

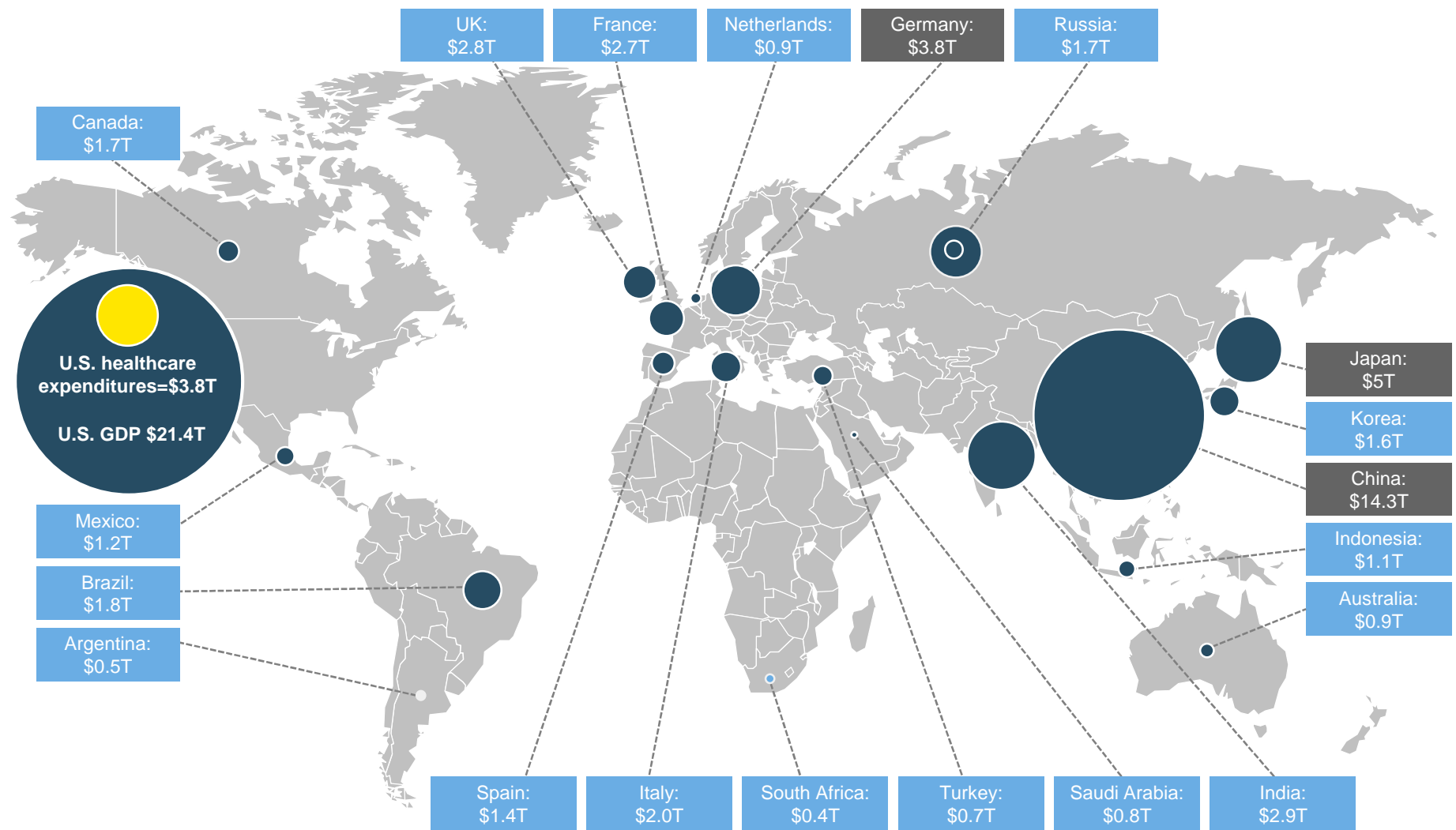
Anirudh Goel, EY-Parthenon
October 2020

Agenda

- ▶ **Macro Context**
- ▶ Investment Themes
- ▶ Appendix

Macro Context

U.S. spending on healthcare exceeds the total GDP of all but three countries

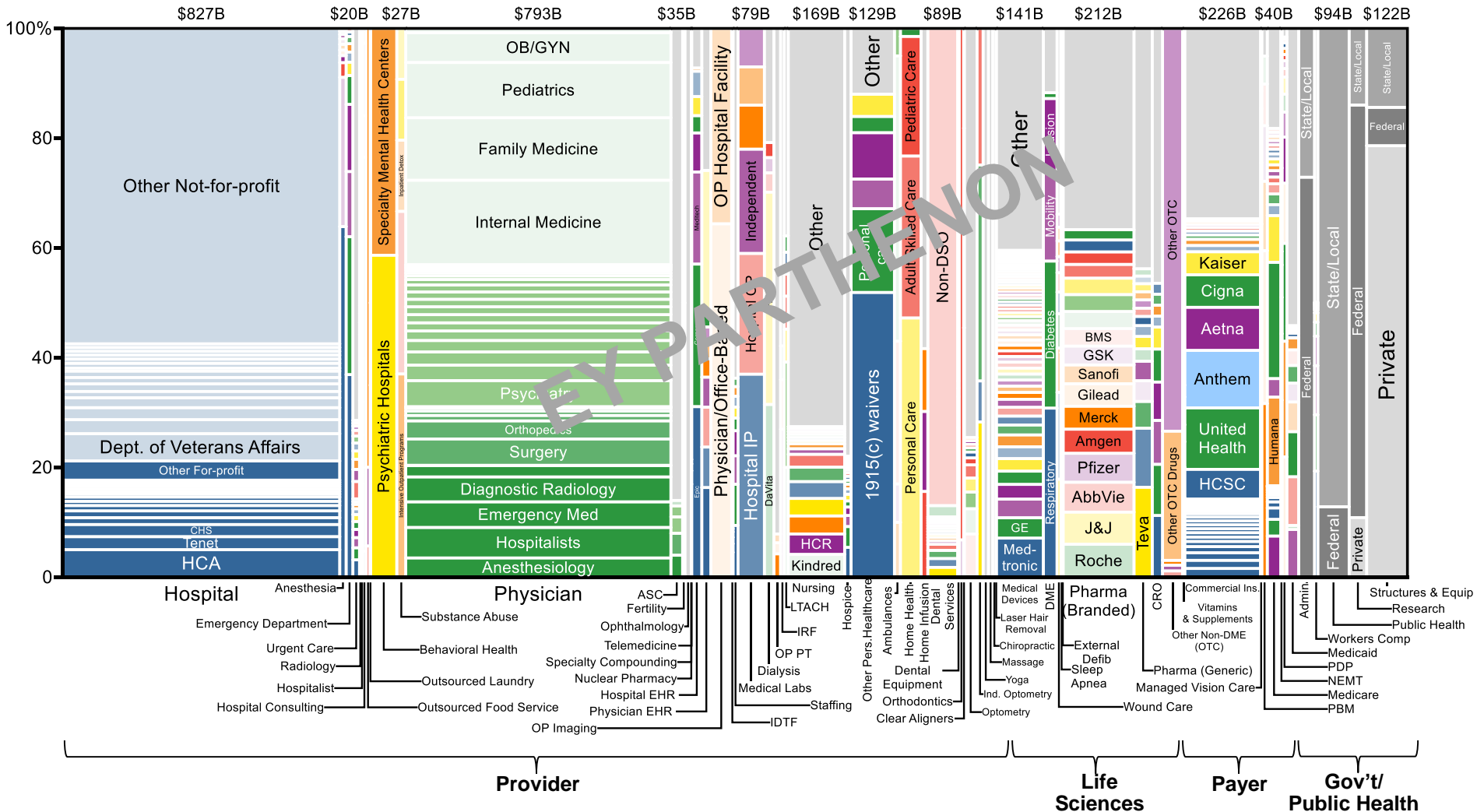


Macro Context

U.S. Healthcare Spending: \$3.8T ~~and growing~~

U.S. Health Expenditures, 2019

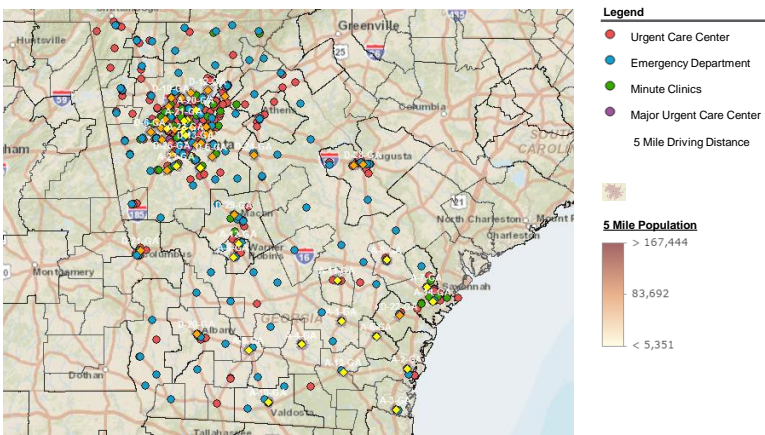
Total = \$3.8T



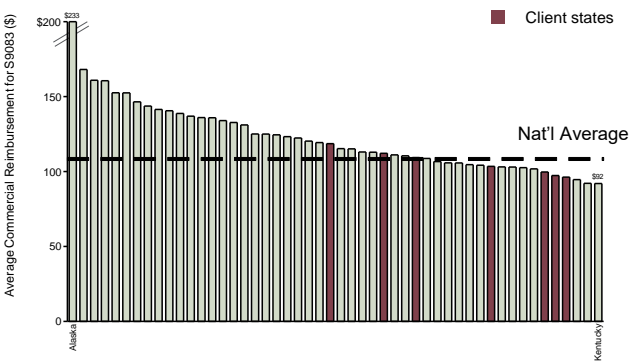
Macro Context

Healthcare is local and variation is a constant theme in diligence

Urgent Care/ ED Density



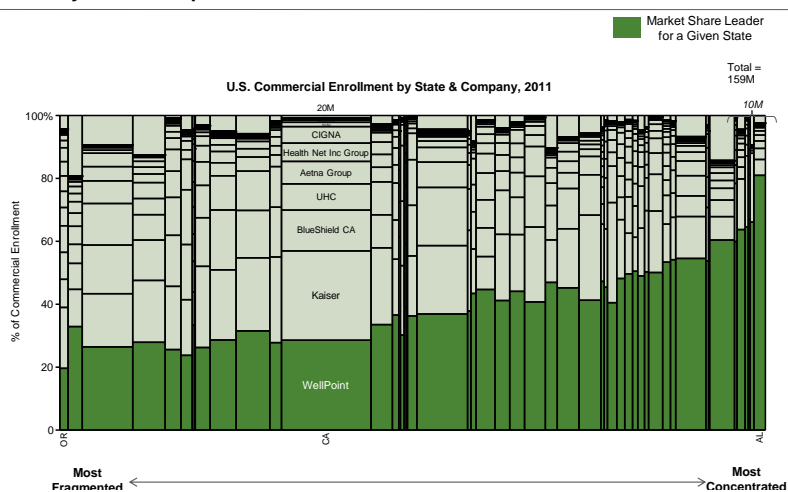
Commercial Reimbursement Rates by State



Market Characteristics of High-Performing Centers

			Population / All Competitors (K)			Population / Sig. Competitors (K)					
Center Name	MSA	Perf.	2 mile	5 mile	10 mile	2 mile	5 mile	10 mile	% Uninsured	Payer Conc.	
Center #1	MSA #1	BEST	26	73	97				19%	4,121	
Center #2	MSA #1		51	64					15%	4,884	
Center #3	MSA #1		21	25	31				13%	4,884	
Center #4	MSA #1		10	19	25				13%	4,884	
Center #5	MSA #1		6	15	16	12	60	38	16%	4,195	
Center #6	MSA #1		11	41	26				16%	2,972	
Center #7	MSA #1		8	11	25				14%	3,270	
Center #8	MSA #2			40	35				15%	3,013	
Center #9	MSA #2			160	36						
Center #10	MSA #2			28	27	29					
Center #11	MSA #2			54	18				96	18%	
Center #12	MSA #2			57	50				199	16%	
Center #13	MSA #2		24	44	38				120	16%	
Center #14	MSA #3		44	19	23	44	35	47	16%	1,903	
Center #15	MSA #3			29	50		86	175	16%	1,903	
Center #16	MSA #3			104	37			111	16%	1,903	
Center #17	MSA #4		16	24	21			77	15%	2,306	
Center #18	MSA #4			60	38			132	16%	1,903	
Center #19	MSA #4			83	39		83	77	16%	1,903	
Center #20	MSA #4		18	16	23	53	34	48	16%	1,903	
Center #21	MSA #4		17	22	23	35	89	45	16%	1,903	
Center #22	MSA #4				40			150	16%	1,903	
Center #23	MSA #4		17	52	41	17	52	76	16%	1,903	
Center #24	MSA #5			87	21			56	16%	1,903	
Center #25	MSA #5			76	30		76	53	16%	1,903	
Center #26	MSA #5										
		AVG	15	31	19	44	43	33	16%	1,903	

U.S. Payer Landscape: Commercial insurance market



Macro Context

Key Impacts of COVID-19

1

The COVID-19 impact on the broader economy will be worse than the U.S. experienced in 2009 with the Great Recession

2

The unemployment rate will skew payer mix towards Medicaid and the uninsured

3

Healthcare spending will respond differently in this recession relative to prior ones, with a negative impact of \$400-\$500B on our national healthcare expenditures (NHE)

- NHE will be negative for the first time in 60 years
- The cycle will be shorter in duration, greater in magnitude and without the time lag observed in other recessions

4

Almost all subsectors of healthcare have been negatively impacted by COVID-19, but these impacts are not uniform

5

Opportunities and challenges arise for specific subsectors and their potential recovery

Agenda

- ▶ Macro Context
- ▶ **Investment Themes**
- ▶ Appendix

Investment Themes

What we presented at JPM 2020 (January 2020)... some of them remain true despite COVID others have changed dramatically

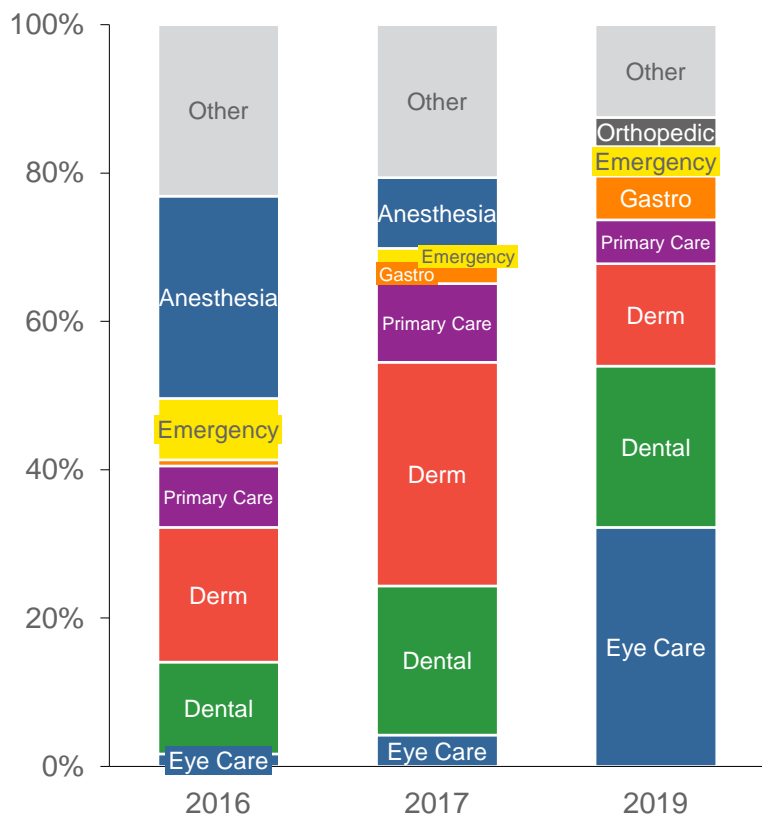
Key themes that impact healthcare investing...

Providers	1	Vision 2020: A big year for eye-care investing	COVID Impact
	2	PPM Report Card: Lessons learned over the past 3-years	
	3	Behavior Health Maturation: Where are investors going next?	
	4	Sector Favorites: “The Bookends”: IVF and Hospice	
	5	Peak Demographics (2032): Capitalizing on another decade of aging tailwinds	
Technology	6	HCIT: Maneuvering in an Epic / Cerner-dominated landscape	COVID Impact
	7	Telemedicine: Still early for healthcare’s game-changer	
	8	Digital Health: Big bets, but still venture	
Payers/ Employers	9	Employers still trying to make a dent	
	10	What the heck is a pay-vider?	
Pharma / Services	11	Proliferation of investment opportunities in pharmacy services	
	12	Outsourcing across Pharma & MedTech enabling diverse strategies	
	13	Gene and cell therapy: The centers of attention	
	14	Graying of lines between PE and VC in drug development	
	15	Surgical robotics: Changing ORs and business models	

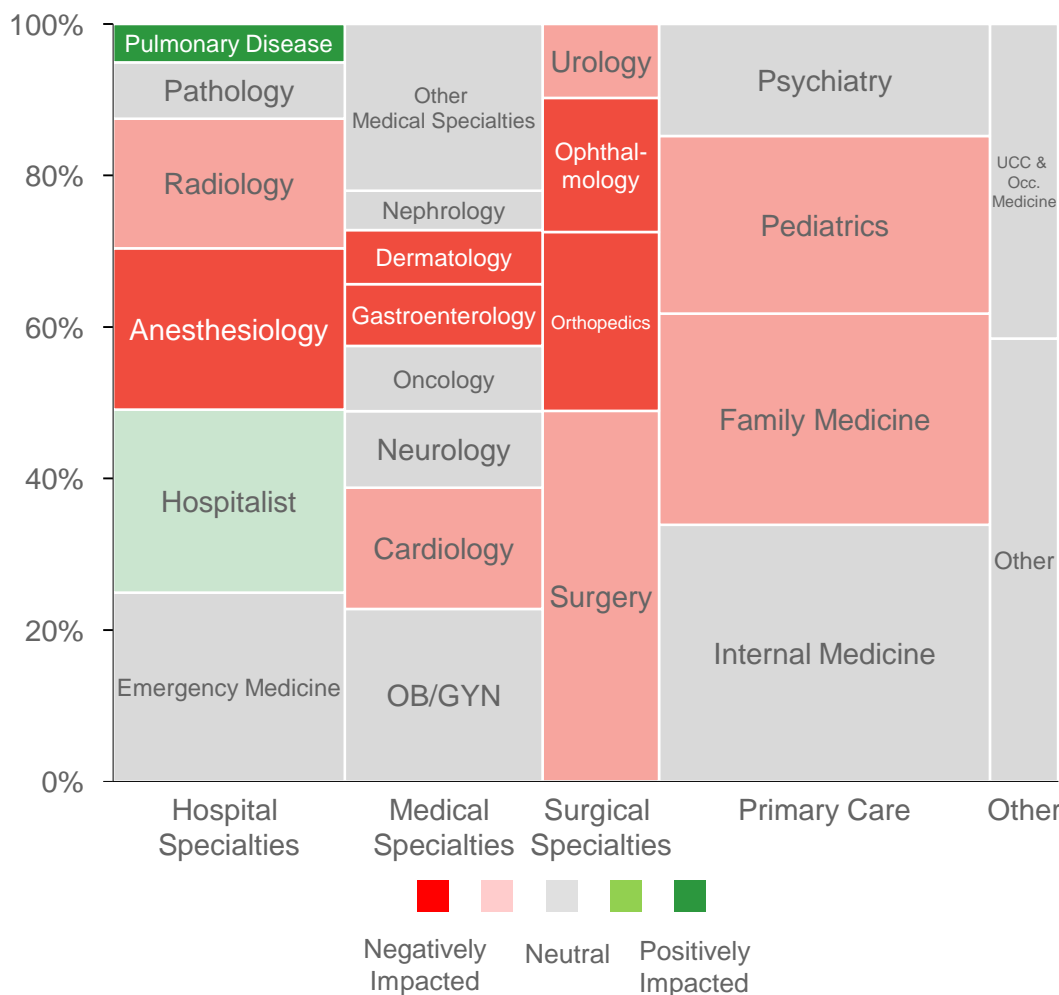
PPM Report Card

PPM deals continued to be very active in 2019 and while new specialties are emerging, COVID effectively paused provider deals for two quarters

U.S. physician practice management deals
2016-2019



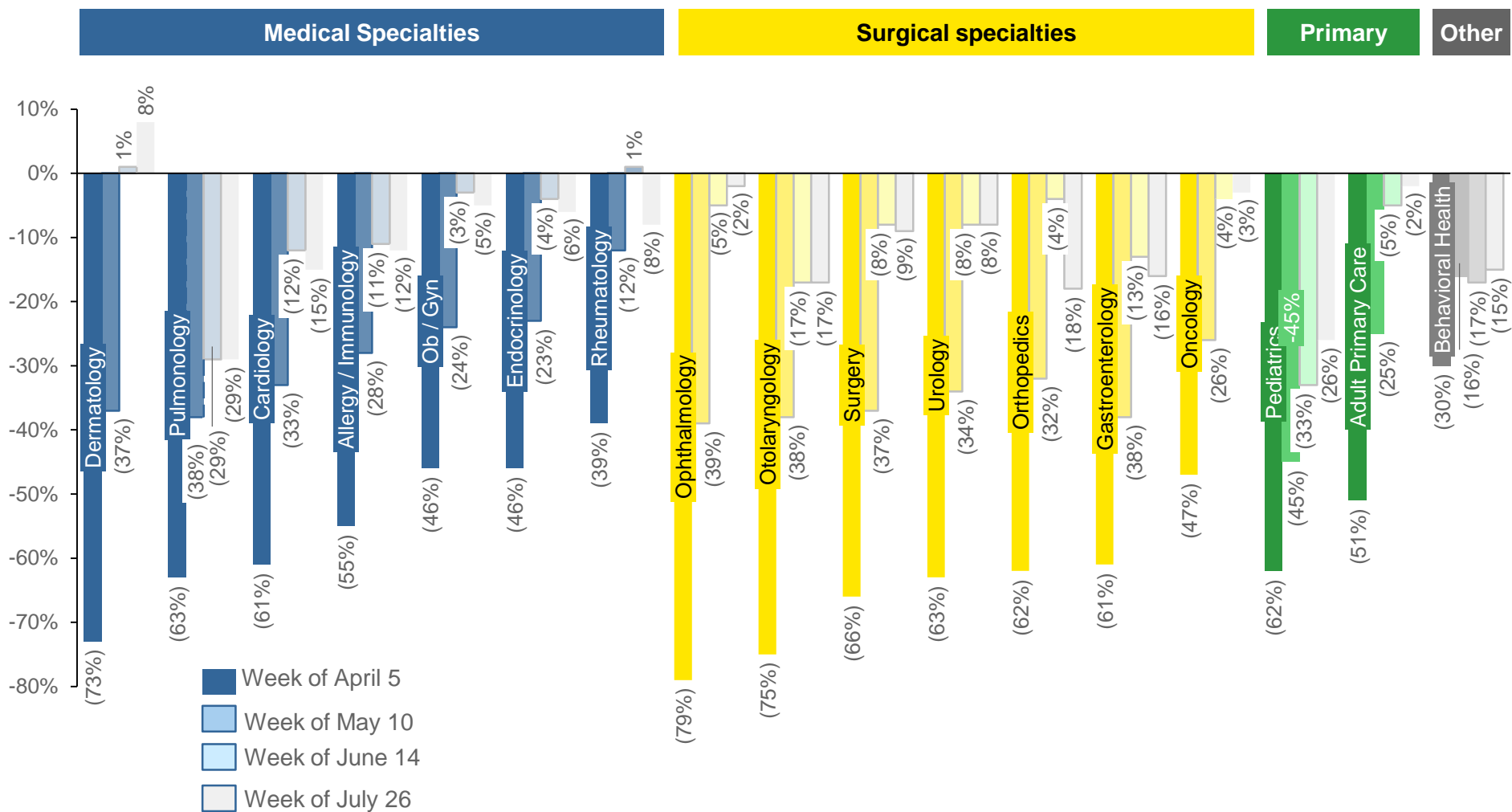
Impact on U.S. physicians by specialty
during COVID-19 pandemic



PPM Report Card

After facing 30-80% patient volume declines across most specialties in April, outpatient volumes started to return to pre-COVID levels by July

Percent change in outpatient visits from baseline by specialty,
Comparison to week of March 1 for the week of April 5, May 10, June 14, and July 26, 2020



When PPM deals return investors will likely still have the some concerns around value-creation that emerged pre-COVID

1 Misaligned compensation expectations and incentives

- ▶ Difficulty calibrating across younger vs experienced physicians
- ▶ Even with attractive up-front economics, MDs frustrated if post-deal compensation is not at market rate
- ▶ Importance of non-compensation motivators often neglected, but may be critical for MD retention
- ▶ Compensation and culture are also important for non-MD staff – high turnover can harm the business

2 Unrealistic projections for ancillary service growth

- ▶ Forecasts on penetration and patient unit economics are often aggressive
- ▶ Need to consider investments required, local competition, and time to scale

3 Aggressive assumptions on ease of recruitment / acquisition within a market

- ▶ Target actionability and valuation impacts ability to drive scale
- ▶ Interest in selling (and strength of value proposition to independent MDs) is often over-estimated
- ▶ Recruitment of physicians in under-penetrated markets may be challenging

4 Lack of understanding for local market dynamics in expansion geographies

- ▶ Supply/demand balance may look attractive, but not reflect the target payer or population mix
- ▶ Hospitals can influence referral patterns in ways that may not be reflected in first-pass market analysis
- ▶ Fragmented and disperse market footprints are challenging to manage and remove the benefits to scale

5 Insufficient operational integration across practices

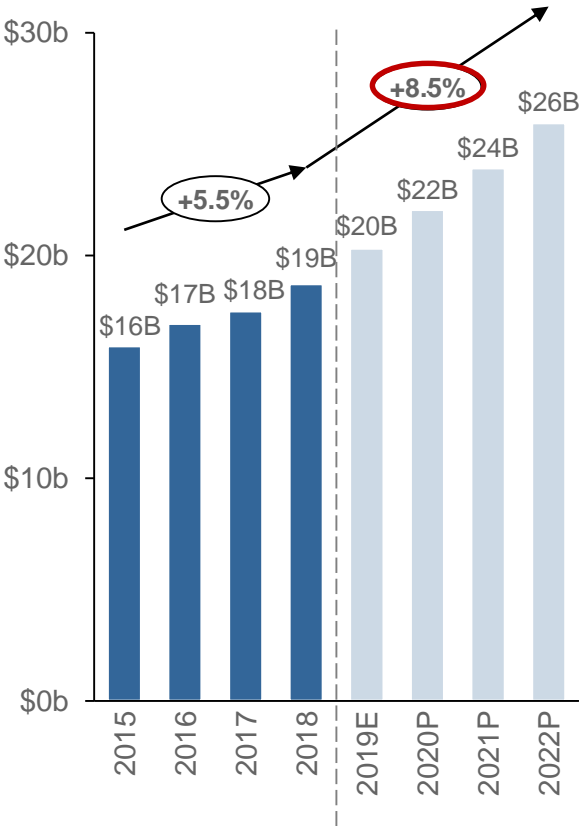
- ▶ IT systems in particular can be challenging which impacts the ability to track metrics and performance
- ▶ Infrastructure may not be equipped to support larger scale; Need for shared compliance culture

6 Incomplete understanding of reimbursement dynamics

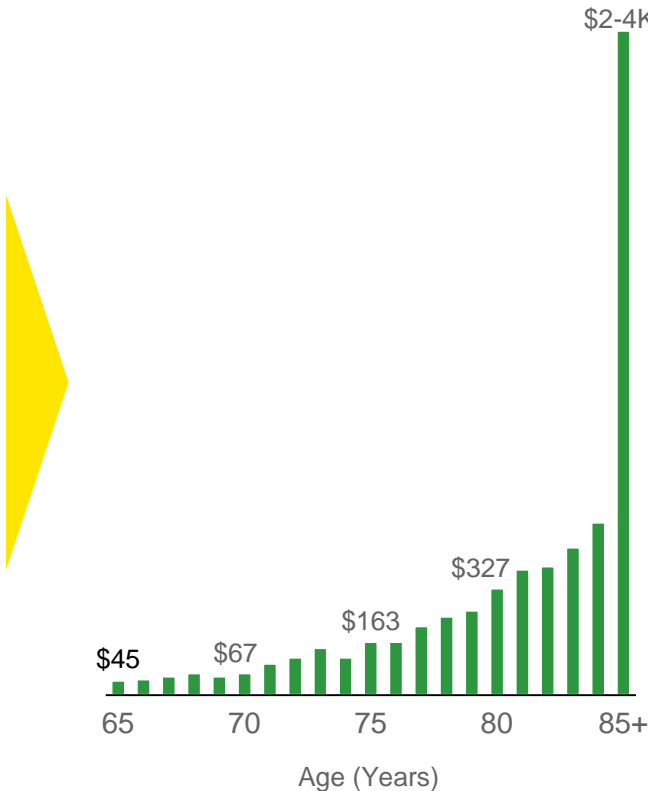
- ▶ Commercial rate variation can lead to over-estimation of contracting benefits to scale
- ▶ Out-of-network strategies can be viable, but present specific risks

Hospice market tailwinds are numerous and show little signs of slowing

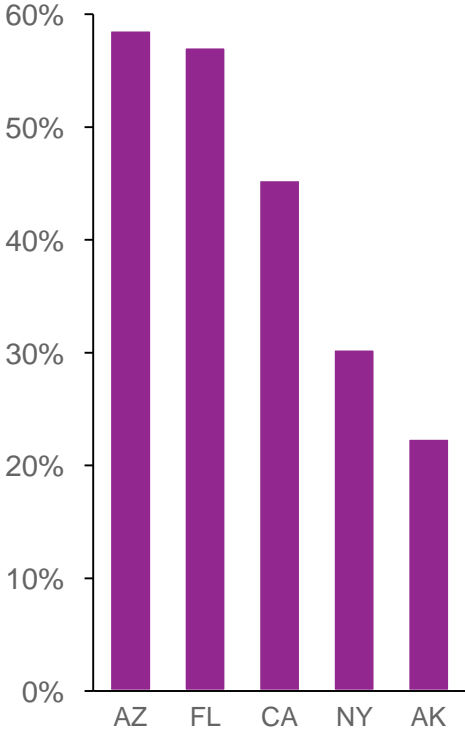
To U.S. Medicare hospice spending, 2000-2022P



Per capita spending on hospice by age (65 + year old)



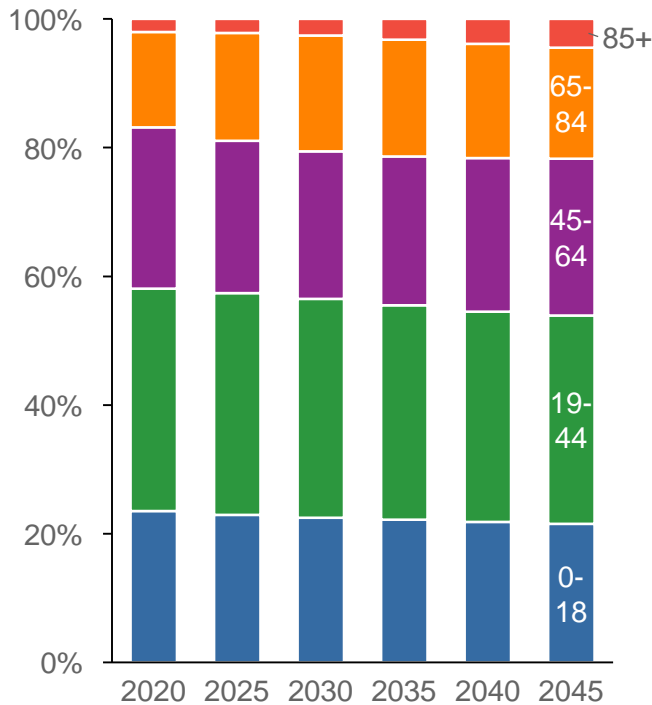
Hospice Utilization Rate, (Select States, 2017)



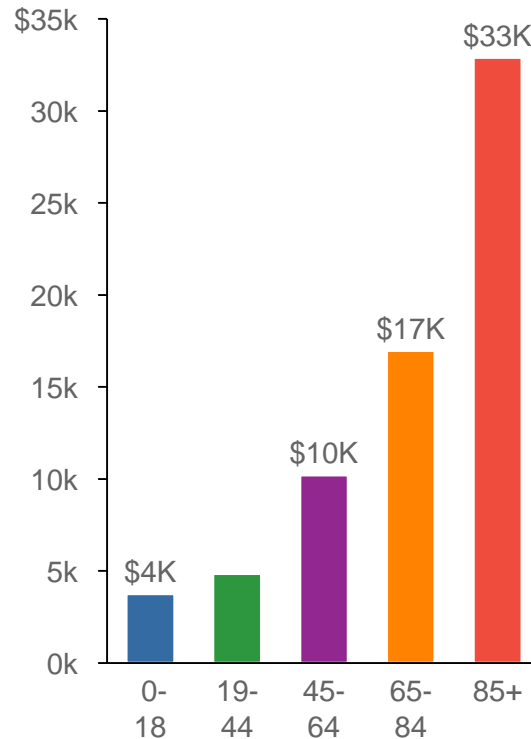
Peak Demographics – 2032

Aging demographics will continue to provide a tailwind to health care spending for another decade

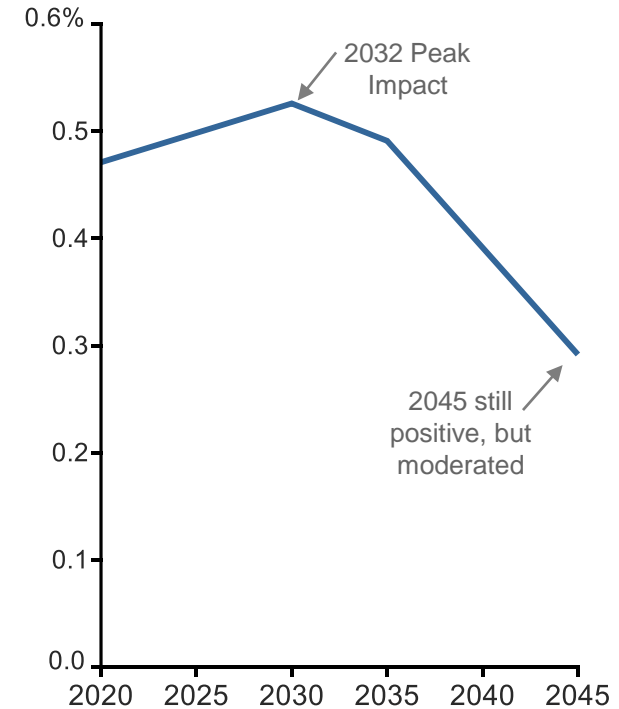
**U.S. Population by Age Cohort
2020-2045**



**Personal Health Care
Per-capita Spending, 2014**



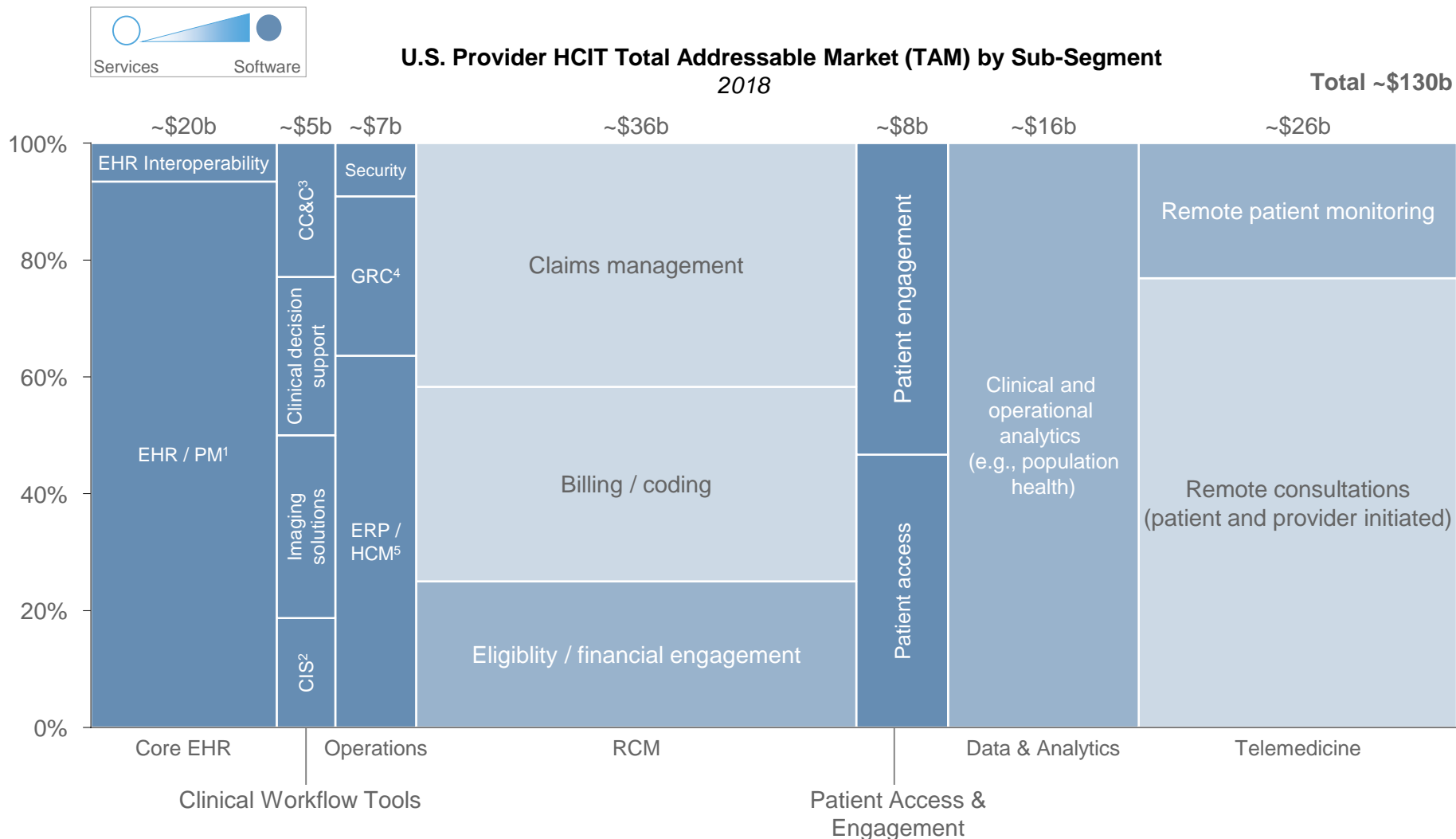
**Real Health Expenditure Growth
from Demographic Effects, 2020-2045**



Sectors experiencing differential population tailwind:

Post-acute - Home Health, Hospice
Ophthalmology and Optometry
Medicare Advantage and related services

U.S. provider HCIT market opportunity is ~\$100b+; significant whitespace exists in more services-heavy categories, such as RCM and telemedicine

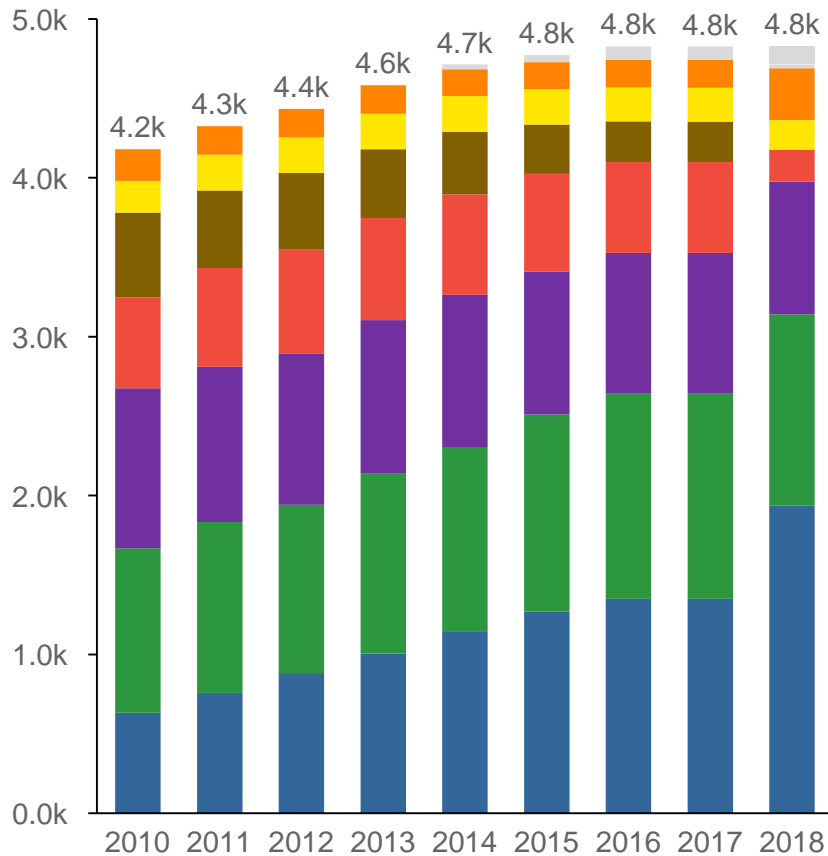


Note: TAM includes spend on software + services; ¹EHR/PM includes medical and dental providers; ²Clinical Information Systems; ³Clinical Communications & Collaboration; ⁴Governance, Risk, and Compliance; ⁵Enterprise Resource Planning and Human Capital Management;

Source: Company Public Filings; Barclays; JP Morgan; Cantor; Cowen; Mizuho; Leerink; Allied Research; Frost & Sullivan; Zack's Investment Research; EY-Parthenon Interviews & Analysis

Epic and Cerner continue to take share in the acute care EHR market

Total U.S. Acute Care Hospitals EHR Market Share, by Hospital Count 2010-2018

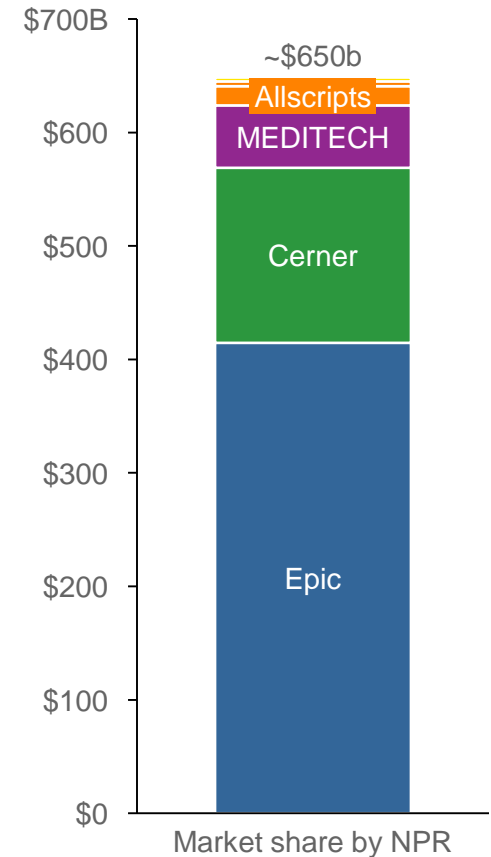


% Epic 15% 18% 20% 22% 24% 27% 28% 28% 40%

CAGR ('10-'18)

Total	2%
All Other	-5%
MEDHOST	-1%
CPSI	-12%
MEDITECH	-2%
Cerner	2%
Epic	15%

EHR Vendor Market Share within Medium and Large Health Systems, by NPR⁽¹⁾ 2018

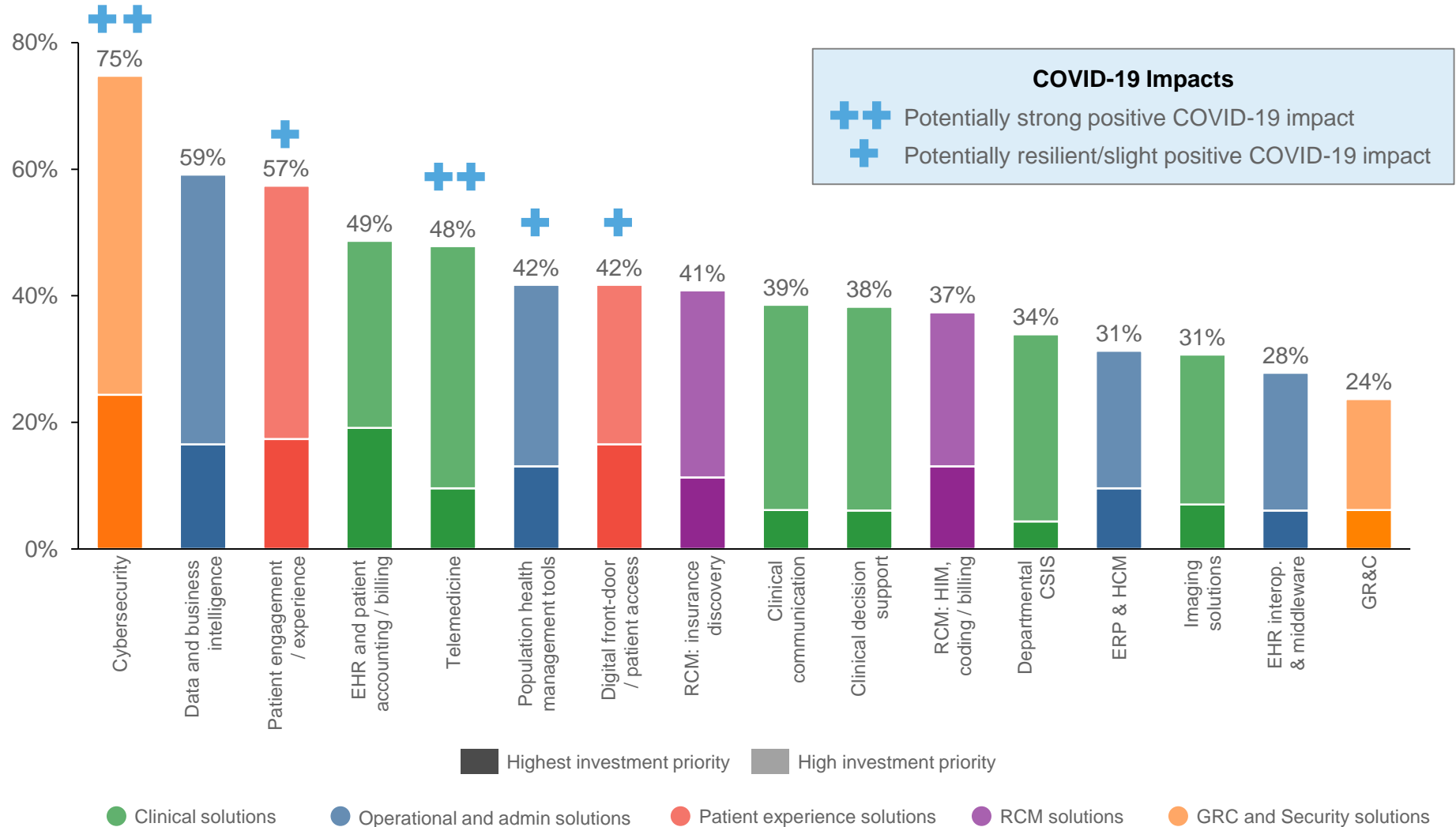


% Epic 64%

Cybersecurity, data/BI, and patient engagement are the highest priorities; post COVID-19, patient-facing and mission-critical technologies will prove resilient

Top investment priorities for health systems

Q: How significant an investment priority is each of the following types of technology solutions for your organization over the next 3 years?*

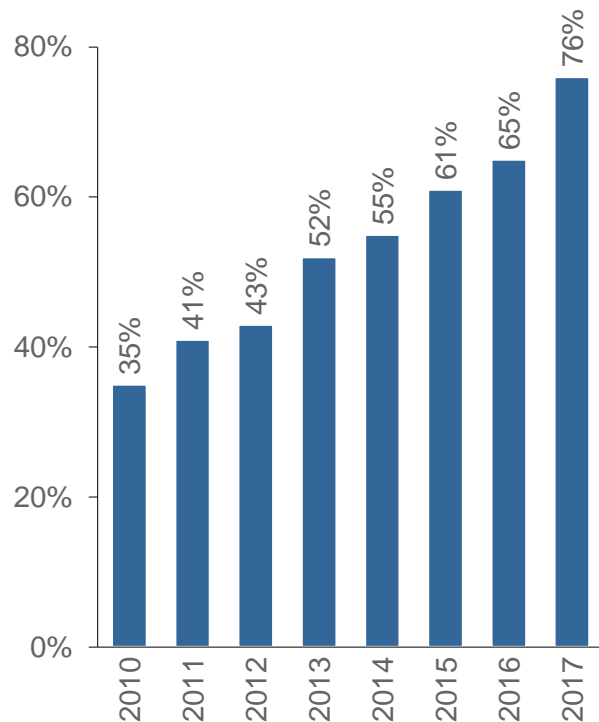


Note(*): Response "I don't know" excluded from analysis; cybersecurity, data and business intelligence, ERP/HCM, and GRC are typically served by non-HC focused horizontal vendors
Source: EY-Parthenon HCIT Decision Maker Survey (n=115)

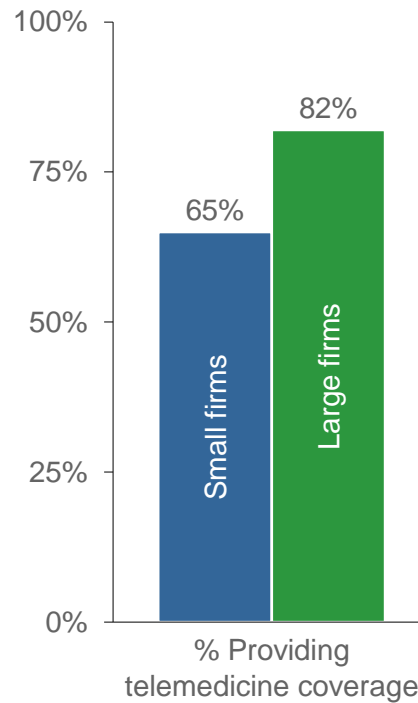
Telemedicine

Prior to COVID-19, vendor and plan adoption of telemedicine capabilities was high, while utilization was exceedingly low (1-2%)

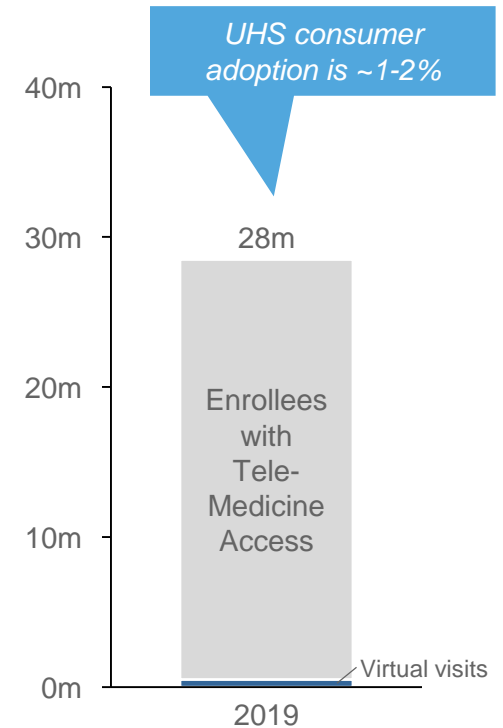
Percentage of hospitals using full or partial telemedicine systems, (2010-2017)



Telemedicine coverage by firms that offer health benefits, (2019)



Usage of Telemedicine services, UnitedHealth Group's covered lives (2019)



Regular customer usage of telemedicine services will be a key component of future growth

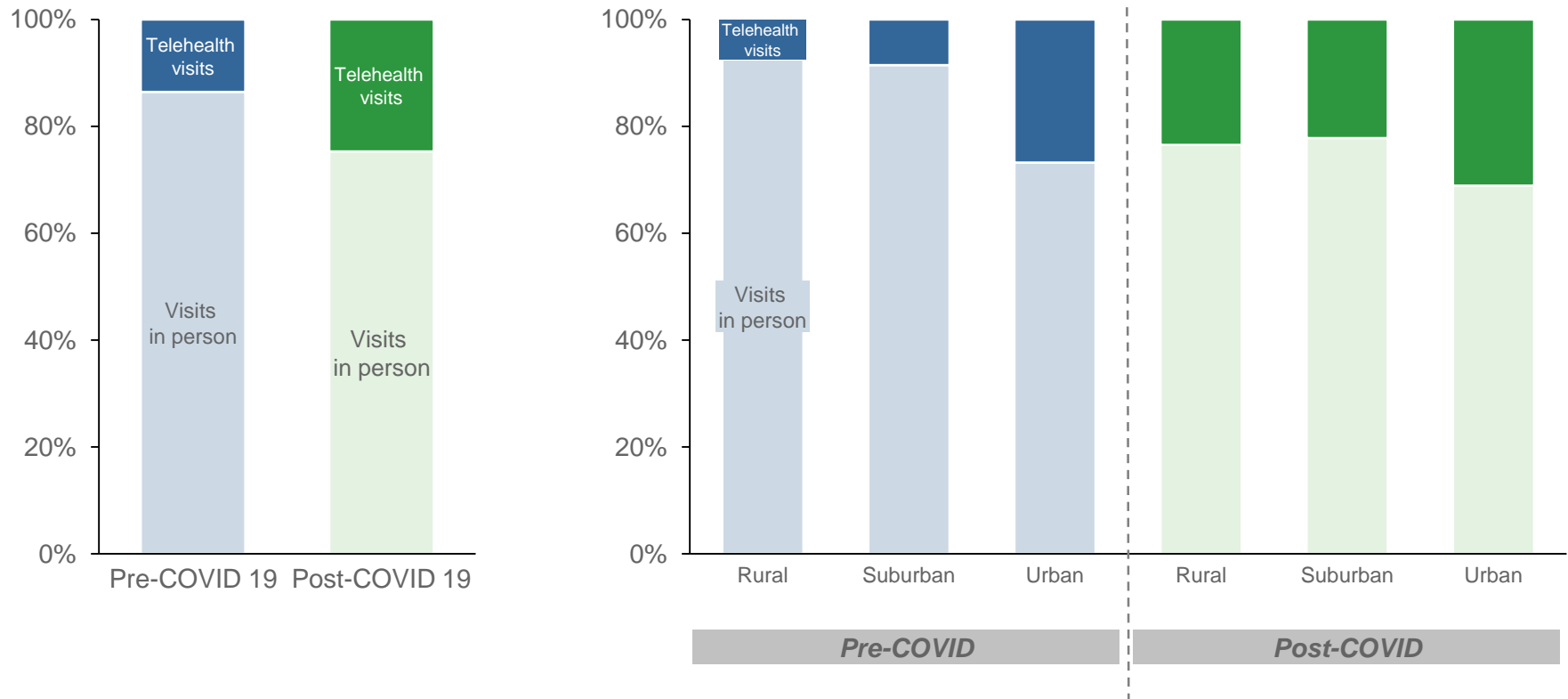
Patients expect to increase their level of telehealth visits in a post COVID-19 environment making telemedicine a new reality for all providers

Healthcare setting, in person vs. telehealth,

[All respondents]

Q: Prior to COVID-19, how many times did you go to the doctor last year (e.g., in-person, telehealth, etc.)? (n=769)

Q. After COVID-19 (12+ months from now), how many times will you book each of the following types of appointments to go to the doctor in a year (e.g., in-person, telehealth, etc.)? (n=769)

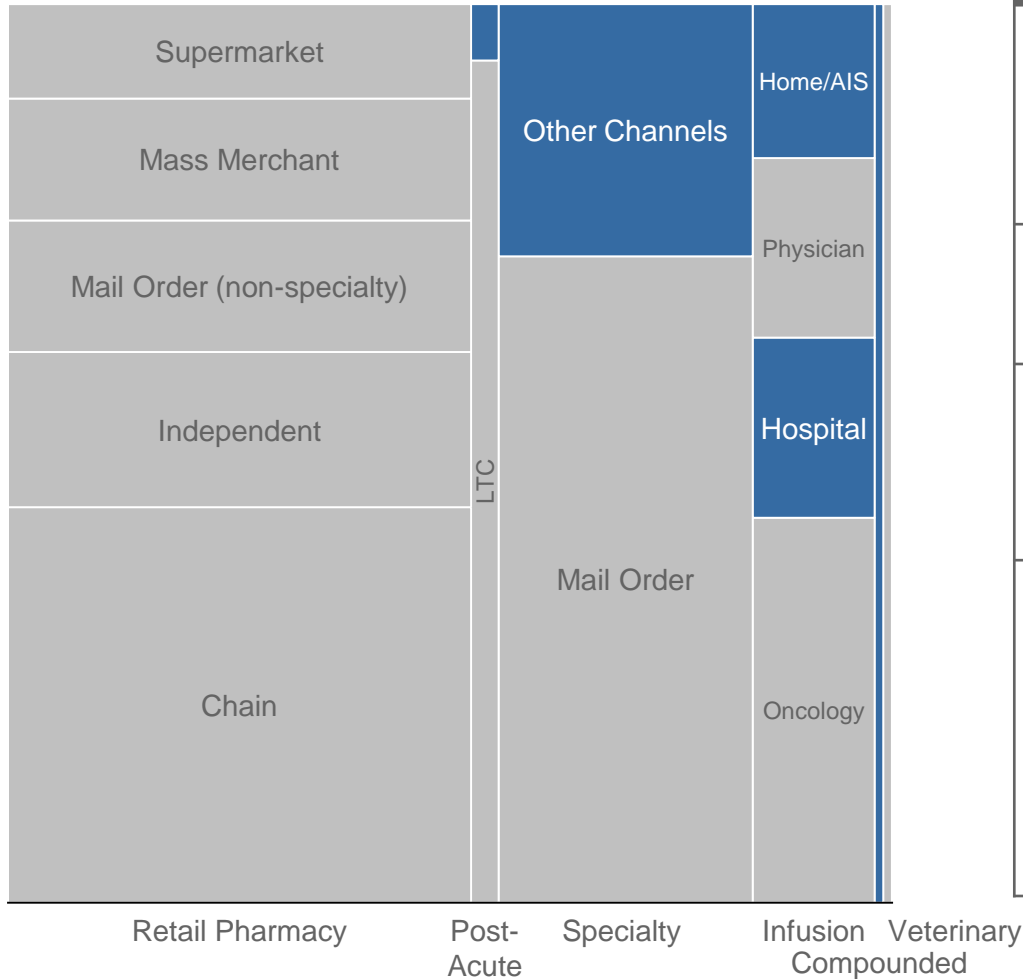


Pharmacy Services

Investors see an opportunity to differentiate within service-focused pharmacy categories

Pharmacy Landscape
Drug Revenue by Channel

Active Investment Area



Representative 2019 Deals

Hospital Pharmacy Services	
Compounding	
Special Populations	
Home and Ambulatory Infusion	

Agenda

- ▶ Macro Trends
- ▶ Investment Themes
- ▶ **Appendix**

Overview

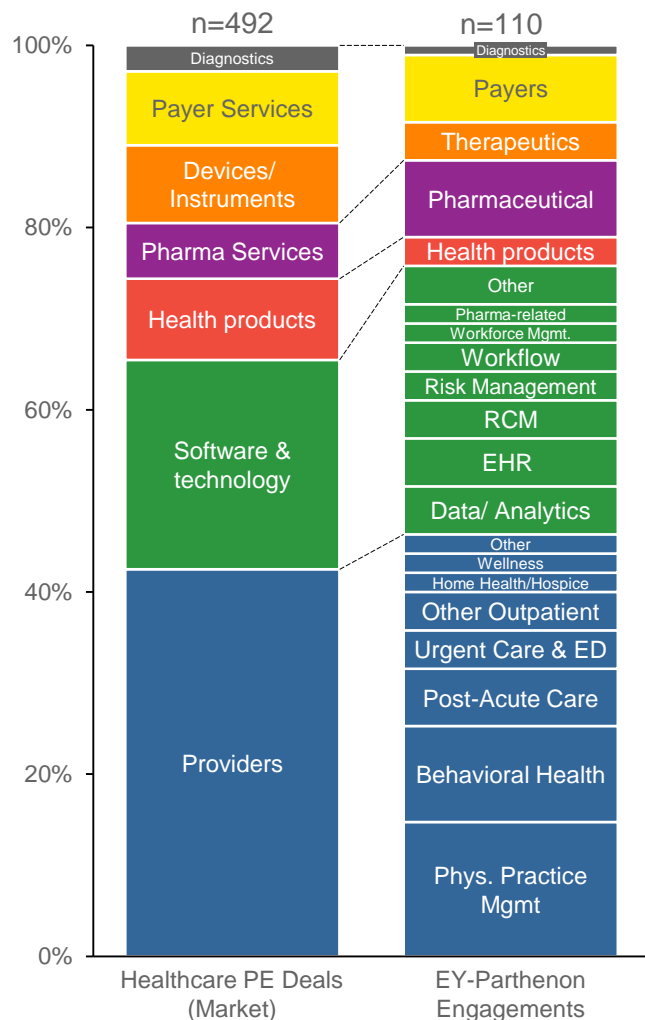
EY-Parthenon's healthcare and life sciences experience

Providers	HCIT	Payers	Life Sciences	Private Equity
Physician Practice Mgmt 	EHR/ Practice Management MEDHOST KINNSER RCM 	Managed Care 	Devices & Therapeutics 	Private Equity
Multi-site providers 	Telemedicine/ Workflow 	Workers Comp 	Diagnostics & Lab Services Distributors 	PBM & Pharma Services
Behavioral health 	Data/ Analytics CROSSIX	Wellness/Employee Benefits 	Other 	Staffing, Post-Acute, Other

Overview

2019 healthcare deal volume increased relative to 2018, with providers accounting for ~50% of activity

Healthcare PE Deals by Subsector, 2019



HistoGeneX Buyside Arsenal Capital July 2019 Oncology Diagnostics	Confidential Buyside Riverside Company Dec 2019 Life Sciences Learning Solutions	medicalknowledgegroup Sellside Windrose Health Investors Dec 2019 Pharma Analytics/ Marketing	CAPRION Buyside Arsenal Capital Jul 2019 CRO	BELMAR PHARMACY Buyside Webster Mar 2019 Compounding Pharmacy	AskBio Buyside TPG Capital Apr 2019 Gene Therapy
FSAstore Buyside BPOC Feb 2019 Medical Products Distribution	NATIONAL SEATING & MOBILITY Buyside Cinven Sep 2019 DME/ Accessibility	SPECTRUM SOLUTIONS Buyside DW Healthcare Partners June 2019 Packaging Solutions/ Logistics	Tri-Imaging SOLUTIONS Buyside Quilvest Aug 2019 Diagnostic Equipment Services	Med Tech Solutions Buyside Sunstone Partners Apr 2019 Medical Equipment Distributor	Longs DRUGS Sell-Side Tailwind Capital Jan 2019 Pharmacy
LEARN Behavioral Buyside Gryphon Jan 2019 Autism Provider	Censis Sellside Riverside portco Jun 2019 Surgical Asset Management	DEFINITIVE HEALTHCARE Sellside Spectrum Equity May 2019 Provider Data	iContracts Buyside TA Associates May 2019 Contract Mgmt. Software	jvion Buyside JMI Equity Jan 2019 AI-Based Hospital Analytics Platform	cpi Sellside FFL Jun 2019 Behavioural Health/ Crisis Prevention
EPTAM PLASTICS Sellside New Heritage October 2019 Medical CMO	Santa Monica FERTILITY Buyside Webster October 2019 Fertility Clinics	Compassus Buyside Towerbrook Sep 2019 Hospice	centria HEALTHCARE Buyside Thomas H. Lee Partners Sep 2019 Autism Provider	CENTER FOR SIGHT Buyside Pamlico Jun 2019 Ophthalmology	THE CHARTIS GROUP Buyside Audax Apr 2019 Hospital Consulting
SUMMIT MEDICAL GROUP Buyside Warburg Mar 2019 Multispecialty Physician Group	Confluent HEALTH Buyside Partners Group Mar 2019 Physical Therapy	SPG Buyside Ridgemont Feb 2019 Autism Provider	KureSmart Pain Management Sell-Side New Harbor Capital Jan 2019 Pain Management	HealthPlus Management LLC Buyside Investcorp Jan 2019 Physiatry Group	Radiology Ltd Buyside U.S. Radiology Specialists (WCAS) Jan 2019 Radiology Group

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A low-angle, upward-looking photograph of several modern skyscrapers in a city, likely New York City. The buildings are made of glass and steel, reflecting the sky. The perspective creates a sense of height and architectural grandeur. The sky is a clear, pale blue.

McDermott
Will & Emery

Healthcare Private Equity Association
October 8, 2020 – New York, New York
HCPEA New Analyst Training

Healthcare Private Equity Association
New Analyst Training
October 8, 2020 – New York, New York

Principal Transaction Agreements



Rob Goldstein
Partner - McDermott Will & Emery

Principal Transaction Agreements – Basic Objectives

- Reflect the **business deal and commercial terms** to which the parties have agreed
- Create a **road map** to govern the parties' conduct pre- and post-closing
- Establish the conditions governing when the transaction **must close**, the situations in which the parties may **walk away** from a deal and the **consequences**, if any, for walking away
- Protect the **benefit of the bargaining** the parties have negotiated for
- **Allocate risk** among the parties

Principal Transaction Agreements: *Agenda and Training Goals*

- Understanding Principal Transaction Agreements
 - Parts of an Agreement
 - Basic Function
- Working Capital Adjustments
 - Common Tensions between Buyers and Sellers
 - How Working Capital is Addressed in Principal Transaction Documents to Reflect the Business Deal and Avoid Costly Disputes
- Indemnification Matters
 - Typical Formulations
 - How to Achieve Specific Objectives
 - Common Pitfalls to Avoid
 - Role of Rep & Warranty Insurance
- Addressing Extra-Contractual Claims/Liability
- Closing Conditions, Termination Provisions and Remedies for Failure to Close
 - When must the deal close, when may a party walk away and what happens if they do

Part I:

Understanding Principal Transaction Agreements

Understanding Principal Transaction Agreements

	Representations & Warranties	Covenants	Conditions to Closing	Indemnification
Definition	A statement of fact as of a specified time	A promise to take (or refrain) from a specified action	A condition precedent to a party's obligation to perform/close	A contractual obligation to compensate a party for losses arising from certain breaches or the occurrence of specified events
Function	<ul style="list-style-type: none"> • Allocate risk • Gather Information • Basis to exit from deal (through rep "bring-down" condition) • Basis for indemnification (through indemnity) 	<ul style="list-style-type: none"> • Ensure specified actions are taken ("affirmative covenants") or not taken ("negative covenants" or "restrictive covenants") following signing, either before or after Closing • Provide basis for indemnification (and possibly specific performance) if breached 	<ul style="list-style-type: none"> • Basis to exit from deal if condition is not met • Allocate risk and allow parties to provide for actions or events that may or may not be within either party's control that are deemed necessary for the transaction to close 	<ul style="list-style-type: none"> • Provide procedures and parameters to govern claims by a party for specified breaches of representations and warranties, covenants or other specified circumstances • Protects parties and other related persons (e.g., officers, directors, affiliates) from certain specified losses

Understanding Principal Transaction Agreements

	Representations & Warranties	Covenants	Conditions to Closing	Indemnification
Relevant Time	A specified point in time (e.g., when made, at signing, at Closing, at signing and again at Closing)	At any time after entering into the agreement	Period between signing and closing	Typically, for a specified period following the Closing
Remedy for Breach	<ul style="list-style-type: none"> Damages Potentially rescission Remedies often contractually limited by indemnification provisions 	<ul style="list-style-type: none"> Damages Potentially specific performance Remedies often contractually limited by indemnification provisions 	<ul style="list-style-type: none"> None Means for a party to elect not to close (generally without liability; but not always) 	<ul style="list-style-type: none"> Damages
Qualifiers & Limitations	<ul style="list-style-type: none"> Scheduled exceptions Knowledge Materiality Ordinary course of business 	<ul style="list-style-type: none"> Scheduled exceptions Degree of obligation (e.g., best efforts, commercially reasonable efforts) Materiality Ordinary course of business 	<ul style="list-style-type: none"> Scheduled exceptions Knowledge Materiality 	<ul style="list-style-type: none"> Scheduled exceptions Baskets (true deductible vs. threshold or "tipping basket") Caps Contractually limited survival period (statute of limitations)

Part II:

Working Capital Adjustments

Purchase Price Adjustments – Typical Formulation

The “Closing Purchase Price” shall be equal to:

- i. the Base Purchase Price;
- ii. plus, the Closing Cash;
- iii. plus, if the Net Working Capital Estimate exceeds the Target Net Working Capital, the amount of such excess;
- iv. minus, if the Target Net Working Capital exceeds the Net Working Capital Estimate, the amount of such excess;
- v. minus, the Escrow Amount;
- vi. minus, the Closing Debt; and
- vii. minus, the Company Expenses.

Net Working Capital – Key Definitions

- "Current Assets" means, as of the **Effective Time**, the consolidated current assets of the Company and its Subsidiaries, ***which current assets shall include only the line items set forth in Annex A under the heading "Current Assets" and no other assets.***
- "Current Liabilities" means, as of the **Effective Time**, the consolidated current liabilities of the Company and its Subsidiaries, ***which current liabilities shall include only the line items set forth in Annex A under the heading "Current Liabilities" and no other liabilities.***

Net Working Capital – Key Definitions

"*Net Working Capital*" means, the Current Assets minus the Current Liabilities, as of the Effective Time, calculated *in accordance with the Balance Sheet Rules.*

Net Working Capital – Key Definitions

- GAAP is a set of accounting principles, standards and procedures not hard and fast rules
 - GAAP recognizes multiple acceptable methods for accounting for items:
 - Ex. AR – flexibility in how to reserve for doubtful accounts
 - Ex. Inventory – flexibility in the manner in which obsolete/non-saleable inventory is addressed
 - Under GAAP an event that occurs during a subsequent-events-period that provides additional evidence about conditions existing at the balance sheet date may result in an adjustment to the financial statements

RELYING ON A GAAP STANDARD ALONE MAY OPEN THE DOOR TO POST-CLOSING DISPUTES

Net Working Capital – Key Definitions

- "Net Working Capital" means, the Current Assets minus the Current Liabilities, as of the Effective Time, calculated **in accordance with the Balance Sheet Rules**.
- "Balance Sheet Rules" means, collectively, the accounting principles, methods and practices used in preparing the [Audited Financial Statements for the year ended December 31, 2016] to the extent in accordance with GAAP, applied on a consistent basis, and the rules set forth in [Annex A (the "Balance Sheet Rules")]; provided, that in the event of any conflict between GAAP and the Balance Sheet Rules, the Balance Sheet Rules shall apply.

Net Working Capital – Key Definitions

- **Specific Accounting Rules:**

- *Ex. Accounts Receivable:* The reserve for doubtful accounts for accounts receivable over ninety days old as of the Effective Date will be 20%.
- *Ex. Inventory:* Buyer may require, upon at least twenty (20) Business Days advanced written notice to the Seller, that the Seller cause the Company to perform a physical count of all inventory prior to Closing. The results of any physical inventory counts will be incorporated into the calculation of Net Working Capital. Representatives of the Buyer, including but not limited to its auditors, shall have the right to be present at and observe the physical inventory count as well as review the results of the physical inventory count and all subsequent adjustments due to the physical inventory count.

- **General Rules:**

- *Ex.* For the avoidance of doubt, Net Working Capital shall be calculated without giving effect to the closing of the transactions contemplated by [this Agreement] and shall be based exclusively on the facts and circumstances as they are known to exist by the Company as of the Closing and shall exclude the effect of any event, act, change in circumstance or similar development arising or occurring thereafter (including the Company acquiring knowledge after the Closing (for the first time) of any fact or circumstance existing as of the Closing).

Part III:

Indemnification Matters

Indemnification Matters: Key Terms

- Indemnification is about:
 - Allocation of Risk
 - Monetary Compensation
- Who is Liable
 - May Impact Deal Structure
 - Joint & Several Liability vs. Joint Liability vs. Several Liability
- For What – Scope of Indemnity
 - Breaches of Representations and Warranties/Covenants
 - Special Indemnities
 - Fees and Expenses
 - Third Party Claims
 - Measure of Damages
 - Between Signing and Closing

Indemnification Matters: Key Terms

- Limitations on Indemnification:
 - Baskets: Threshold/“Tipping Basket” vs. True-Deductible
 - DeMinimis Losses/“Mini-Basket”
 - “Materiality Scrape”
 - Caps
 - Survival and Appropriate Carve-outs
- Other Significant Issues:
 - Measure of Damages (e.g., consequential, punitive, multiple of damages)
 - Control over Third Party Claims
 - Tax Benefits and other Third Party Payments
 - Equitable Relief (as opposed to monetary relief)
- Effect of Knowledge on Indemnity Claims
 - Anti-Sandbagging vs. Affirmative-Sandbagging
 - Key Distinctions in Certain Legal Jurisdictions

Impact of Rep & Warranty Insurance

- Reduced Liability Exposure to Seller
 - Shorter Survival of Claims
 - Smaller Financial Exposure

Recourse	General Cap on Exposure
Standard (Seller Only)	Cap on Most Claims* generally = 5% - 10% EV <i>*Fundamental Reps, taxes and specified other reps often have a higher cap (purchase price or in some instances no cap at all)</i>
R&W Policy	Loss Retention Under Policy (e.g., 2% EV) <u>less</u> Deductible (e.g., 0.5% EV) = 1.5% EV* <i>* Policy Exclusions may be handled separately</i>

- Less Contentious Negotiation of Reps
- Buyer Generally Receives Enhanced Rep Coverage
 - Broader Scope of Rep Coverage
 - Longer Survival Under Rep & Warranty Policy
- Addressing Exclusions

Part IV: Addressing Extra-Contractual Claims/Liability

Addressing Extra-Contractual Claims/Liability

- Certain highly-negotiated “lawyers points” affect the ability of a party to go beyond the “four corners” of the document
 - Disclaimers of Reliance
 - Integration Clauses
 - Exclusive Remedy Provisions
 - Non-Recourse Provisions
 - Defining “Fraud”

- Forum/Choice of Law Provisions
 - Differing Default Governing Law Provisions
 - Alternative Approaches/Interpretations of Law

Part V: Closing Conditions, Termination Provisions and Remedies for Failure to Close

Closing Conditions, Termination Provisions and Remedies for Failure to Close

- Common Conditions to Closing
 - Rep Bring Down
 - No MAE
 - Antitrust Clearance/Expiration of HSR Waiting Period
- Additional Conditions to Closing
 - Employment Agreements
 - Material Third-Party Consents
 - Regulatory Approvals
 - Other material events without the occurrence of which one party (or the other) would not want to proceed with the transaction
- Effect of Satisfaction/Failure of Closing Conditions
 - Obligation to Close
 - Right to Terminate
- Effect of Termination/Remedies for Failure to Close
 - Specific Performance
 - Termination Fee/Reverse Termination Fee (e.g., Liquidated Damages)
 - Expense Reimbursement

Part VI: COVID Considerations

COVID Considerations in M&A Agreements

- Pricing Considerations
 - Earnouts/Seller Financing
- Supplements to Reps and Warranties
- Interim Operating Covenants
- Closing Conditions/MAE

Questions?

A wide-angle photograph of the U.S. Capitol building in Washington, D.C. The building's iconic white marble facade, featuring a large portico with columns and a massive dome topped with a gold leaf, is the central focus. An American flag flies from a tall pole in front of the dome. The foreground is a large, paved plaza with a brick pattern. A person is riding a bicycle across the plaza in the lower center. The sky is bright blue with scattered white clouds.

Health care in Washington

October 2020

Election update

Key dates

October	<ul style="list-style-type: none"> ▶ October 7 - Vice presidential debate ▶ October 15 - Second presidential debate ▶ October 22 - Third presidential debate
November	<ul style="list-style-type: none"> ▶ November 2 - Presidential mail-in ballots due in Louisiana, Vermont ▶ November 3 - Election Day Presidential mail-in ballots due in Alabama, Arizona, Arkansas, Colorado, Connecticut, Delaware, Florida, Hawaii, Idaho, Indiana, Maine, Missouri, Montana, Nebraska, New Hampshire, New Mexico, Oklahoma, Oregon, Rhode Island, South Carolina, South Dakota, Tennessee, Wyoming ▶ November 4 - Presidential mail-in ballots due in Texas ▶ November 6 - Presidential mail-in ballots due in Georgia, Kansas, Kentucky, Massachusetts, North Carolina, Pennsylvania, Virginia ▶ November 9 - Presidential mail-in ballots due in Iowa, North Dakota, West Virginia, Wisconsin ▶ November 10 - Supreme Court oral arguments on ACA Presidential mail-in ballots due in Minnesota, Mississippi, Nevada, New Jersey, New York, Utah ▶ November 13 - Presidential mail-in ballots due in Alaska, DC, Maryland, Ohio ▶ November 17 - Presidential mail-in ballots due in California ▶ November 18 - Presidential mail-in ballots due in Illinois ▶ November 23 - Presidential mail-in ballots due in Washington
December	<ul style="list-style-type: none"> ▶ December 8 - Deadline for states to make determinations of controversies/contests as to appointment of electors ▶ December 14 - Electors meet in their respective States to select the President and Vice President ▶ December 23 - Deadline for receipt of electoral votes ▶ December 31 - Expiration of tax extender provisions
January 2021	<ul style="list-style-type: none"> ▶ January 3 - Transfer of Certificates to Congress ▶ January 5 - Georgia special Senate election runoff (if necessary) ▶ January 6 - Congress meets to count electoral votes. The President and Vice President must achieve a majority of electoral votes (270) to be elected. In the absence of a majority, the House selects the President (voting by delegation), and the Senate selects the Vice President. ▶ January 20 - Presidential Inauguration

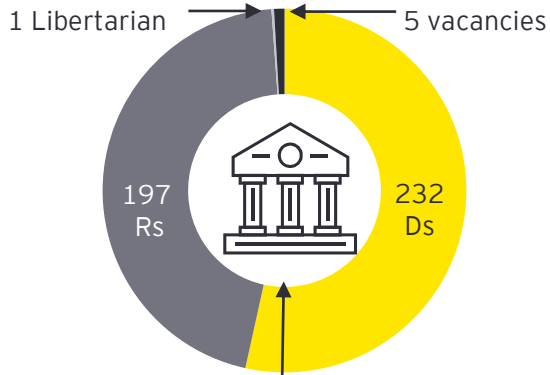
Election notes

- ▶ Source for presidential mail-in ballot deadlines is the New York Times; deadlines subject to postmark date requirements
- ▶ Florida allows counties to begin verifying signatures on and scanning mail ballots 22 days before election day
- ▶ Arizona, Colorado, North Carolina allow for mail-in ballots to begin to be counted 2 weeks or more prior to Election Day
- ▶ Other states have unspecified allowances for mail-in ballots to begin to be counted before Election Day

Congress and the presidency

Now and election outlook

House

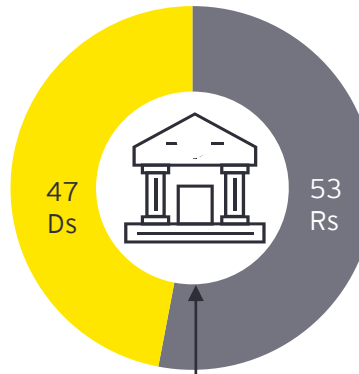


218 needed for control

- ▶ 232 Democrats
- ▶ 197 Republicans
- ▶ 1 Libertarian (Amash)
- ▶ 5 vacancies: CA (Hunter), NC (Meadows), TX (Ratcliffe), GA (Lewis, Graves)

- ▶ If vacant seats remain same-party, 17-seat gain needed by Republicans to regain control of House
- ▶ 31 Democrats are from districts President Trump won in 2016
 - ▶ 21 are freshmen
- ▶ 3 Republicans are from districts won by Clinton
- ▶ 32 Republicans, 11 Democrats, 1 Libertarian not seeking re-election or lost primary
- ▶ No party has gone from the minority to the majority in the House in a presidential election year since 1952

Senate

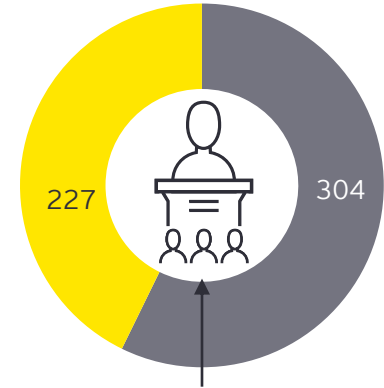


50 needed for control*

- ▶ 53 Republicans
- ▶ 47 Democrats

- ▶ Up for re-election in 2020:
 - ▶ 23 Republican seats, 12 Democratic seats
- ▶ Most vulnerable GOP senators include:
 - ▶ Martha McSally (R-AZ)
 - ▶ Thom Tillis (R-NC)
 - ▶ Susan Collins (R-ME)
 - ▶ Cory Gardner (R-CO)
 - ▶ Steve Daines (R-MT)
 - ▶ Joni Ernst (R-IA)
 - ▶ David Perdue (R-GA)
- ▶ Democrat Doug Jones (D-AL) in tough race

White House



270 electoral votes to win presidency

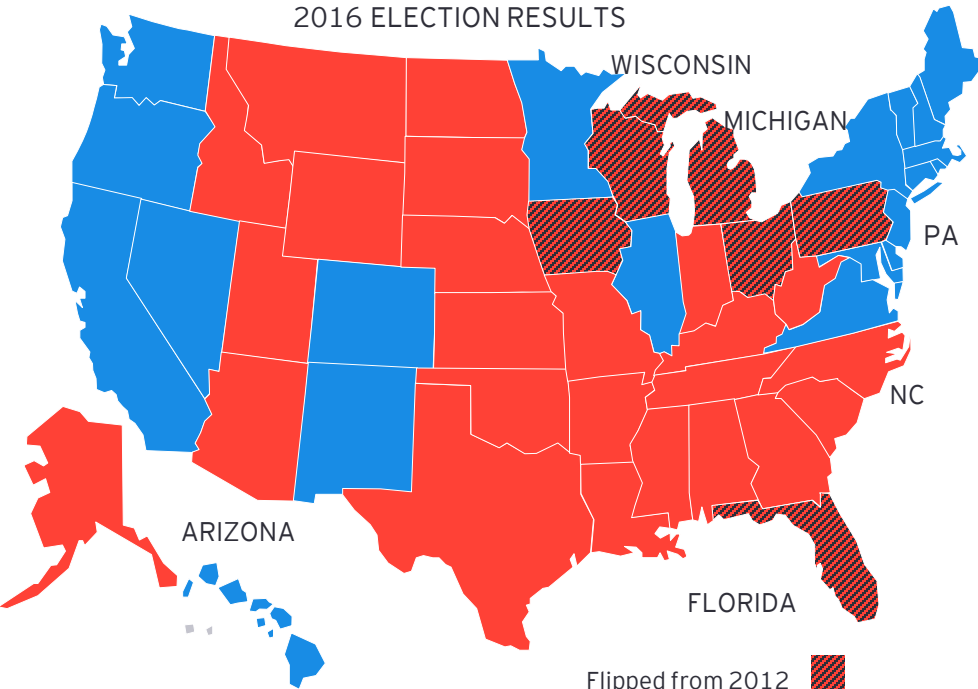
- ▶ President Trump won with 304 electoral votes in 2016; 232 pledged to Clinton, who received 227
- ▶ Four states were/are key: MI (16 votes), WI (10), PA (20), FL (29) = 75 total

- ▶ AZ, NC are also now considered battlegrounds
- ▶ Biden campaign also sees opportunities in Georgia, Texas, Iowa, Ohio
- ▶ Trump campaign eyeing MN, NH
- ▶ Battleground electoral votes:
 - ▶ Florida: 29
 - ▶ Pennsylvania: 20
 - ▶ Michigan: 16
 - ▶ North Carolina: 15
 - ▶ Arizona: 11
 - ▶ Wisconsin: 10

*If same-party President; VP becomes 51st vote

Presidential battleground states

2016 ELECTION RESULTS



State, electoral votes	2012 result	2016 result	Currently*
Michigan - 16	Obama +9.5%	Trump +.2%	Biden +5.2%
Pennsylvania - 20	Obama +5.2%	Trump +.7%	Biden +6.5%
Wisconsin - 10	Obama +6.7%	Trump +.8%	Biden +5.5%
Florida - 29	Obama +.9%	Trump +1.2%	Biden +2%
Arizona - 11	Romney +10.1	Trump +3.5%	Biden +3.1%
North Carolina -15	Romney +1.8	Trump +3.7%	Biden +.5%
Ohio - 18	Obama +1.9%	Trump +7.9%	Biden +2.5%
Georgia - 16	Romney +8%	Trump +5.1%	Biden +.3%
Texas - 38	Romney +15.8%	Trump +9%	Trump +3.2%
Minnesota - 10	Obama +6.7%	Clinton +1.5%	Biden +9.4%

*Source: Real Clear Politics average

Election notes

- ▶ 232 electoral votes were pledged to Clinton in 2016. 270 electoral votes needed to win presidency. Battleground states # of electoral votes:

FL - 29

PA - 20

WI - 10

MI - 16

AZ - 11

NC - 15
- ▶ If Trump wins FL, Biden must win MI, WI and PA (or other Trump states) + all states Clinton won
- ▶ If Biden wins FL and all states Clinton won, victory could be had with a win in any of MI, WI or PA (since only 9 more electoral votes could be needed)
- ▶ CNN: Biden's easiest path to victory is MI, PA, AZ - "He can ... lose Wisconsin, Florida and North Carolina and still be elected president"
- ▶ Biden could also win (assuming he gets the 232 votes pledged to Clinton) with: just FL & AZ; just FL & PA; MI, PA, & AZ; MI, PA, & NC
- ▶ Trump won with 306 electoral votes. Could win again if he lost: PA & MI; PA & AZ; AZ & MI

It's the economy ...

No recession in two years before re-election bid

Recession	President (year)	Re-election?
No	Obama (2012)	Yes
No	Bush43 (2004)	Yes
No	Clinton (1996)	Yes
No	Reagan (1984)	Yes
No	Nixon (1972)	Yes
No	LBJ (1964)	Yes
No	Ike (1956)	Yes
No	Truman (1948)	Yes
No	FDR (1944)	Yes
No	FDR (1940)	Yes
No	FDR (1936)	Yes
No	Wilson (1916)	Yes

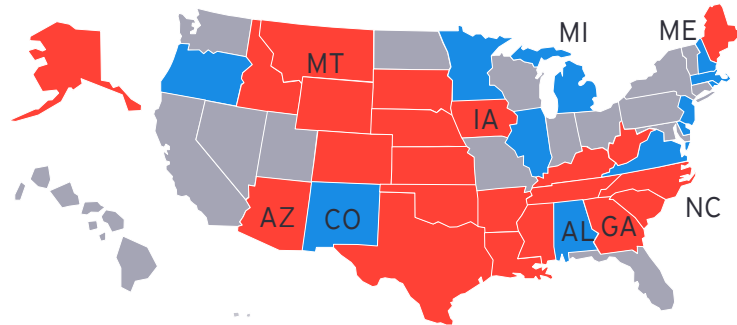
Recession in two years before bid

Recession	President (year)	Re-election?
Yes	Bush41 (1992)	No
Yes	Carter (1980)	No
Yes	Ford (1976)	No
Yes	Hoover (1932)	No
Yes	Coolidge (1924)*	Yes
Yes	Taft (1912)	No

*Coolidge was not technically running for re-election as president, since he had come to the presidency after the death of President Harding in 1923.

Source: Adrian Gray, AGC Research, and Mehlman Castagnetti.

Senate



Republican seat(s) up in 2020
Democratic seat(s) up in 2020
No Senate election in 2020

Category	Senator	Rating ¹	Opponent	
2 Republicans in states Trump won by <5 percentage points	Martha McSally (R-AZ)	Lean D	Mark Kelly	<ul style="list-style-type: none"> ▶ McSally appointed to Sen. Jon Kyl's seat after losing the election for the other AZ Senate seat to Sen. Sinema ▶ Kelly is the astronaut husband of former Rep. Gabrielle Giffords (D-AZ) ▶ Kelly led 48%-42% in a Fox News poll released September 23 ▶ Kelly could take office as soon as November 30 because McSally appointed
	Thom Tillis (R-NC)	Toss-up	Cal Cunningham	<ul style="list-style-type: none"> ▶ Tillis on Senate Judiciary Committee
2 Republicans running in states Clinton won	Susan Collins (R-ME)	Toss-up	Sara Gideon	<ul style="list-style-type: none"> ▶ A Quinnipiac University poll released August 6⁴ has Gideon ahead 47%-43% ▶ Collins no longer perceived as a moderate after voting for 2017 tax reform bill, Kavanaugh Supreme Court nomination
	Cory Gardner (R-CO)	Toss-up	John Hickenlooper	<ul style="list-style-type: none"> ▶ Gardner trailing Hickenlooper 48%-42% in poll released July 28² ▶ Efforts to dismantle ACA working against Gardner and other Republicans
2 Democrats running in states Trump won	Doug Jones (D-AL)	Lean R	Tommy Tuberville	<ul style="list-style-type: none"> ▶ Jones was elected in a 2017 special election ▶ Tuberville led Jones 52%-35% in poll released July 28²
	Gary Peters (D-MI)	Lean D	John James	<ul style="list-style-type: none"> ▶ Peters ahead 49%-44.3% in Real Clear Politics average of polls
Other competitive races	Steve Daines (R-MT)	Toss-up	Gov. Steve Bullock	<ul style="list-style-type: none"> ▶ Gov. Bullock term-limited; won high approval ratings for COVID handling ▶ Daines affected by views of President's handling of coronavirus
	David Perdue (R-GA)	Toss-up	Jon Ossoff	<ul style="list-style-type: none"> ▶ CBS poll reported September 27 shows Perdue up 47%-42%⁵ ▶ Traditionally conservative Georgia has increasingly become competitive
	Joni Ernst (R-IA)	Toss-up	Theresa Greenfield	<ul style="list-style-type: none"> ▶ Ernst was the only vulnerable GOP senator to make a prime-time convention appearance; a main campaign message is supporting Trump

¹ Cook Political Report

² <https://morningconsult.com/2020/07/28/senate-presidential-polling-political-intelligence/>

³ <https://www.foxnews.com/official-polls/fox-news-poll-biden-tops-trump-among-likely-voters-in-key-states>

⁴ <https://poll.qu.edu/2020-presidential-swing-state-polls/release-detail?ReleaseID=3670>

⁵ <https://www.cbsnews.com/news/trump-biden-opinion-poll-georgia-north-carolina-supreme-court-09-27-2020/>

House

Retiring members – parenthetical denotes running/ran for other office

22 Republicans retiring, 5 running for other office, 5 lost primary

1 Libertarian retiring

6 Democrats retiring, 3 running for other office, 2 lost primary

Bishop (R-UT)	King (R-IA) (lost primary)
Woodall (R-GA)	Riggleman (R-VA) (lost primary)
Brooks (R-IN)	Tipton (R-CO) (lost primary)
Mitchell (R-MI)	Watkins (R-KS) (lost primary)
Olson (R-TX)	Spano (R-MI) (lost primary)
Roby (R-AL)	Gianforte (R-MT) (gov.)
Conaway (R-TX)	Byrne (R-AL) (Senate)
Hurd (R-TX)	Marshall (R-KS) (Senate)
Marchant (R-TX)	Cook (R-CA) (county brd.)
Shimkus (R-IL)	Collins (R-GA) (Senate)
Flores (R-TX)	Amash (I-MI)
Sensenbrenner (R-WI)	Loebsack (D-IA)
Thornberry (R-TX)	Serrano (D-NY)
Rooney (R-FL)	Davis (D-CA)
Walden (R-OR)	Lowey (D-NY)
King (R-NY)	Visclosky (D-IN)
Graves (R-GA)	Heck (D-WA)
Holding (R-NC)	Lujan (D-NM) (Senate)
Yoho (R-FL)	Kennedy (D-MA) (Senate)
Walker (R-NC)	Gabbard (D-HI) (President)
Roe (R-TN)	Lipinski (D-IL) (lost primary)
Abraham (R-LA)	Engel (D-NY) (lost primary)

25 House races rated toss-up: 15 D, 10 R

Freshman Democrats in Trump 2016 districts

NY-22, Brindisi <i>toss-up</i>	VA-2, Luria <i>toss-up</i>
OK-5, Horn <i>toss-up</i>	GA-6, McBath <i>toss-up</i>
SC-1, Cunningham <i>toss-up</i>	IA-1, Finkenauer <i>toss-up</i>
ME-2, Golden <i>toss-up</i>	IA-3, Axne <i>toss-up</i>
NM-2, Torres Small <i>toss-up</i>	IL-14, Underwood
UT-4, McAdams	MI-11, Stevens
VA-7, Spanberger <i>toss-up</i>	MN-2, Craig
NJ-3, Kim <i>toss up</i>	NJ-2, Van Drew
MI-8, Slotkin	NJ-11, Sherrill
NY-19, Delgado	PA-17, Lamb
NY-11, Rose <i>toss-up</i>	

D toss-ups not in Trump 2016 districts

IA-02, Open (Loebsack)	CA-21, Cox
MN-07, Peterson	

R toss-ups

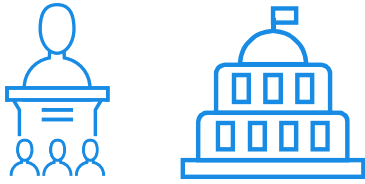
CA-25, Garcia	OH-01, Chabot
GA-07, Open (Woodall)	PA-10, Perry
IL-13, Davis	TX-21, Roy
IN-05, Open (Brooks)	TX-22, Open (Olson)
NE-02, Bacon	TX-24, Open (Marchant)

In a closely watched primary, Ways & Means Chairman Neal (D-MA) defeated a progressive challenger September 1.

Sources: House press gallery, Cook Political Report, Ballotpedia

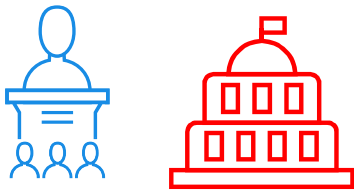
Acting on agenda largely requires same-party control

The House is expected to remain under Democratic control. Joe Biden's ability to act on his agenda would likely hinge on whether Democrats also control the Senate. (Note: If 50-50 in Senate, Vice President breaks the tie.)



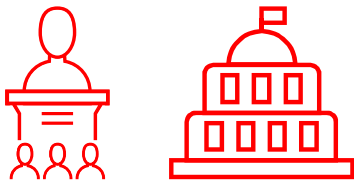
If Biden wins and Democrats take control of the Senate

- ▶ Major priorities like climate change, health care, education, & housing financed with tax increases could be proposed and brought up for votes in the House and Senate
- ▶ Democrats will certainly be well short of 60 votes in the Senate, meaning Democrats would likely turn to the budget reconciliation process, which allows simple-majority passage in the Senate or eliminate or modify the filibuster; or pursue proposals with bipartisan appeal



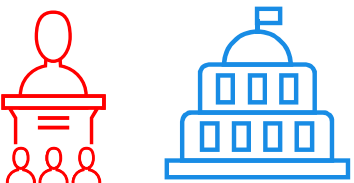
If Biden wins and Republicans retain control of the Senate

- ▶ Majority Leader Mitch McConnell (R-KY) will decide which bills are brought up in the Senate and can block consideration of Democratic priority bills financed with tax increases
- ▶ Some areas of potential bipartisan cooperation: infrastructure, retirement savings, addressing changes scheduled under the TCJA (e.g., interest deduction, R&D amortization, expiration of provisions for individuals)



If Trump wins and Republicans retain control of the Senate

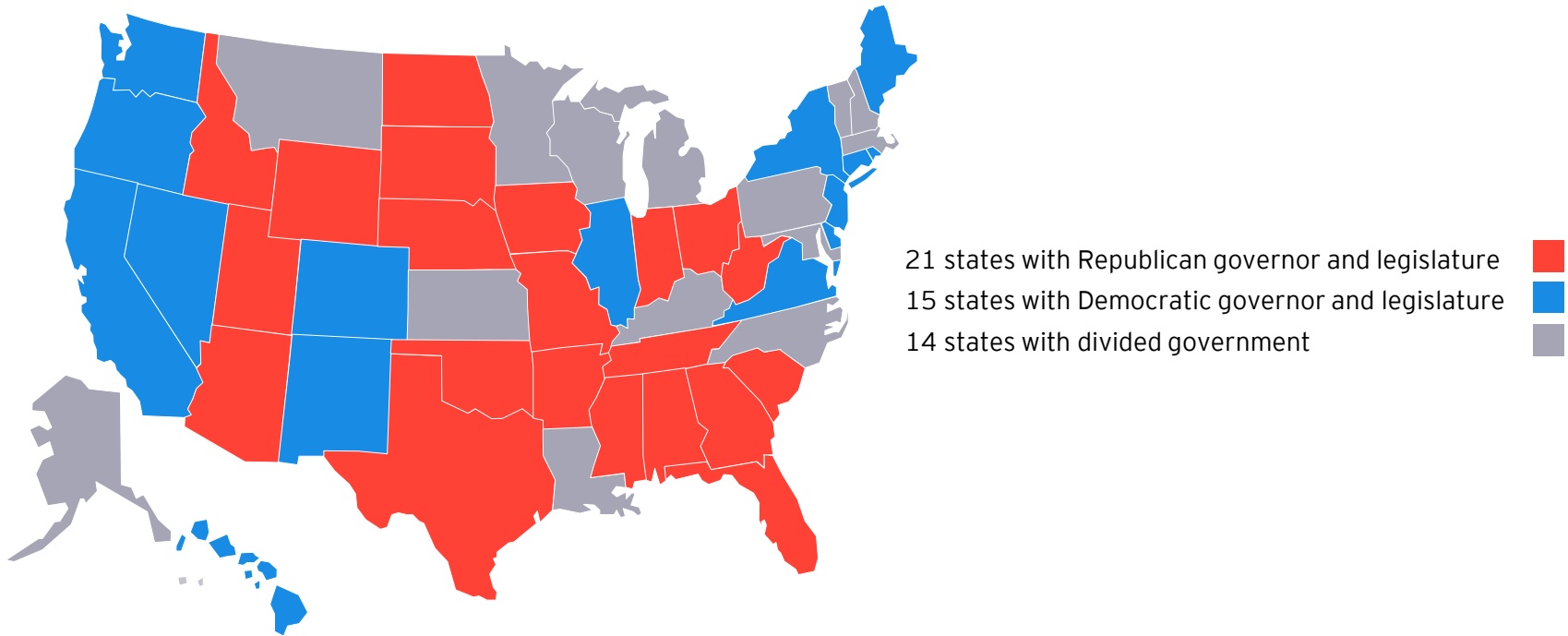
- ▶ The Senate could consider Trump priorities like a middle-class tax cut or capital gains cut but the Democratic House would be a backstop
- ▶ The parties would be required to compromise on must-pass legislation, but there could be significant gridlock as we have seen with next coronavirus bill



If Trump wins and Democrats take control of the Senate

- ▶ An all-Democratic Congress would consider priority bills and force the President to veto them
- ▶ The President would be under greater pressure to compromise to get anything done

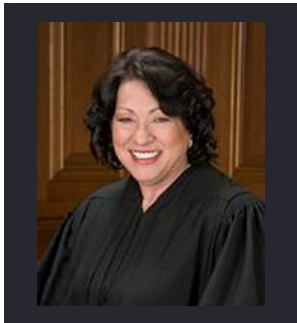
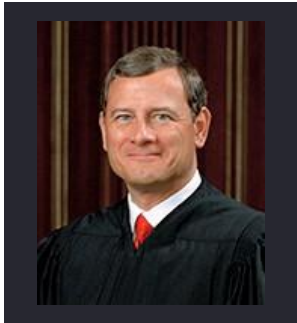
State government 'trifectas'



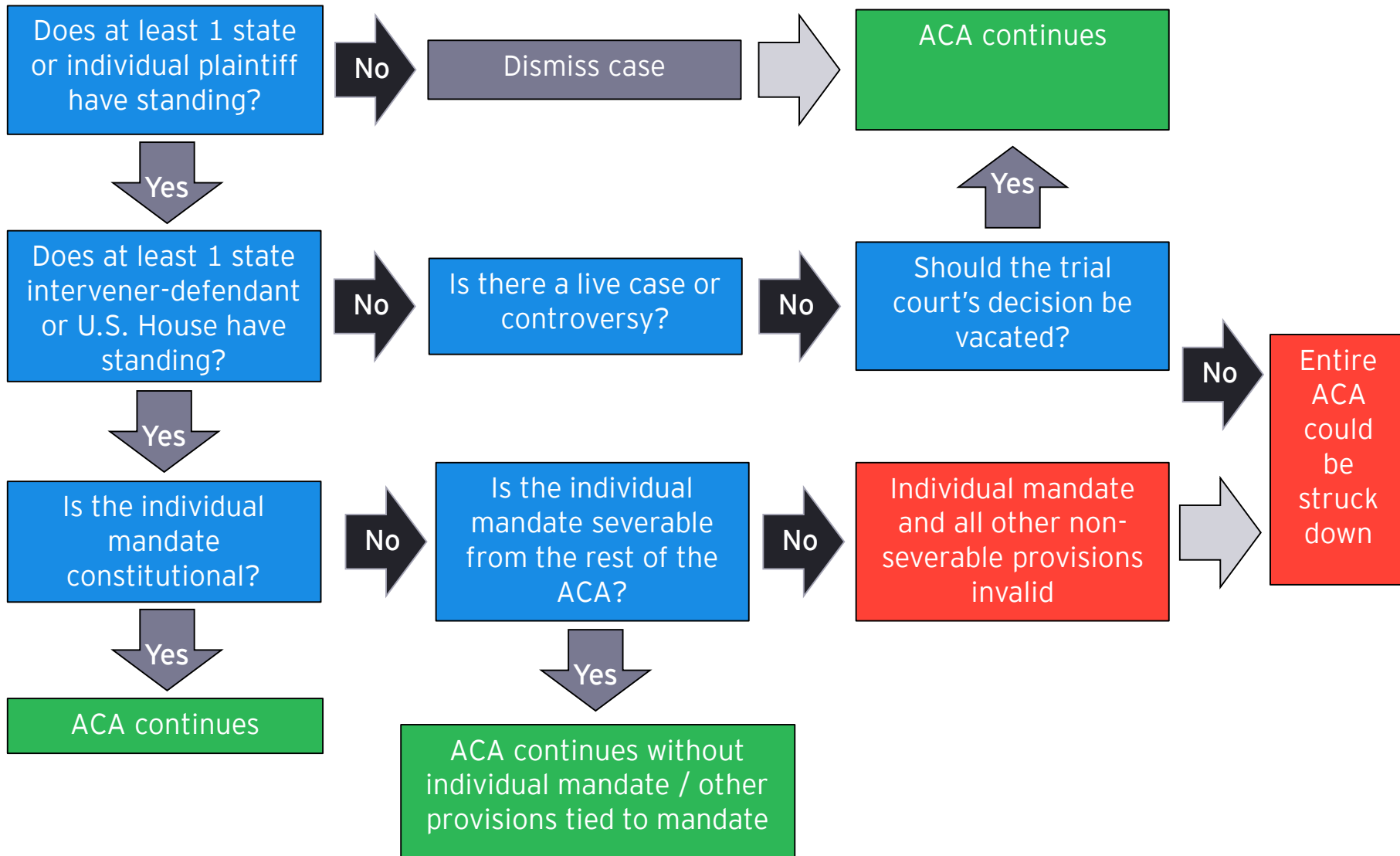
Election notes

- ▶ Of 99 chambers nationally, Republicans control 61 (Nebraska's legislature is unicameral)
- ▶ States that Democrats eye for pickups include: Arizona, Minnesota, Iowa, Michigan (according to Wall Street Journal)
- ▶ In 2020, most states will hold legislative elections, except for: AL, LA, MD, MS, NJ, and VA (Michigan will hold elections in their lower house, North Dakota in their upper house)

California v. Texas



Legal questions and potential outcomes in California v. Texas



Health care: the candidates at a glance



**President
Donald J. Trump**



**Former Vice President
Joe Biden**

Affordable Care Act	Supported repeal and backing lawsuit overturning ACA	Strengthen ACA, create public option, enhance subsidies
Coronavirus	Delegated primary responsibility to states	Prefers federal response and emergency relief
Medicare and Medicaid	Proposed cap to federal funding, work requirements and “public charge” for immigrants	Supports Medicaid expansion, Medicare at age 60, enhanced funding for long-term care
Drug pricing	Reduced insulin costs in Medicare, proposals for importation, “favored nations” pricing, rebate restrictions	Government negotiation of drug prices, drug importation, capping out-of-pocket costs in Medicare
Reproductive health	Restricted access to reproductive health services	Restored and expanded women’s health services

Biden's public option proposal

How would a public option differ from Medicare-for-all?

A public option would be offered as an option for eligible individuals rather than replacing current sources of coverage

Who would be eligible for the public option?

Biden's public option would be offered to everyone, including those currently covered through their employer

Would people be automatically enrolled in the public option?

Only people making below 138% of the federal poverty level will be automatically enrolled, if not currently covered through Medicaid expansion

How much will it cost?

The public option would negotiate prices with providers like Medicare, aiming to provide a more affordable option. Biden's plan would also increase premium tax credits and premiums will be capped at 8.5% of their income.

How many people currently covered by their employers would switch?

Estimates vary, but Kaiser Family Foundation estimates 12.3 million people would potentially switch to the public option due to affordability

Coronavirus response

COVID-19 dashboard

~\$2.8t spent across three congressional bills on:

Health care and social
Services \$450b

Small businesses \$750b

Tax provisions \$540b

Specific industries \$525b

UI benefits, state funding,
supplemental
appropriations \$600b

Outlook for a next bill (CARES 2/COVID 4)

Timing

- ▶ House approved Democratic bill May 15
- ▶ President Trump signed exec. actions Aug. 8
- ▶ Senate GOP narrow bill blocked Sept. 10
- ▶ House approved v2 of Democratic bill Oct. 1
- ▶ Deal could happen before or after election

Size

- ▶ Democrats insist on at least \$2.2t-\$2.4t
- ▶ Administration offered \$1.62t
- ▶ Senate Republicans back \$500b bill, resist very large bill sought by Democrats

Major sticking points

- ▶ Overall size of package
- ▶ Unemployment add-on at \$600 or lesser amount
- ▶ Funding for state and local governments
- ▶ Expansion of Child Tax Credit, Earned Income Tax Credit
- ▶ Expansion of eligibility for ACA exchanges, tax subsidies

The latest

- ▶ Relief sought for wide-scale airline furloughs
- ▶ President Trump pulled out of bipartisan talks October 6 but urged action on discrete issues: airlines, stimulus checks, Paycheck Protection Program
- ▶ WH officials say talks still on in some fashion

Other issues



Economy: real GDP decreased at an annual rate of 32.9% in 2nd quarter of 2020



Budget (CBO)

- ▶ FY20 deficit: \$3.3t
- ▶ Federal debt held by the public near 100%/GDP, highest since 1945



Election

- ▶ Trump/Pence vs. Biden/Harris
- ▶ Close Senate races

COVID-19 relief: reported Trump administration offer vs. updated House HEROES Act

Size

House Democrats:
\$2.2t-\$2.4t

Administration:
\$1.62t

State & local funding

House Democrats:
\$436b

Administration:
\$250b

Tax credits

House Democrats: make CTC fully refundable for 2020 and expand the eligibility and amount of the EITC for those with no qualifying children, repeal CARES Act NOL, excess business loss provisions

Administration: unlikely to support

ACA subsidies

House Democrats:
Expansion of eligibility for ACA exchanges, tax subsidies

Administration:
unlikely to support

\$ for health care

House Democrats:
~\$400b

Administration:
\$175b

Food, rental assistance

House Democrats: \$70b+ for housing needs; \$10b for Supplemental Nutrition Assistance Program

Administration: \$60b housing assistance

COVID 4: Health care items on the negotiating table



Testing, tracing, & coverage



Mandatory coverage provisions



More provider funds



Advanced Medicare Payments



Infrastructure



Telehealth



Liability protections



Regulatory extensions



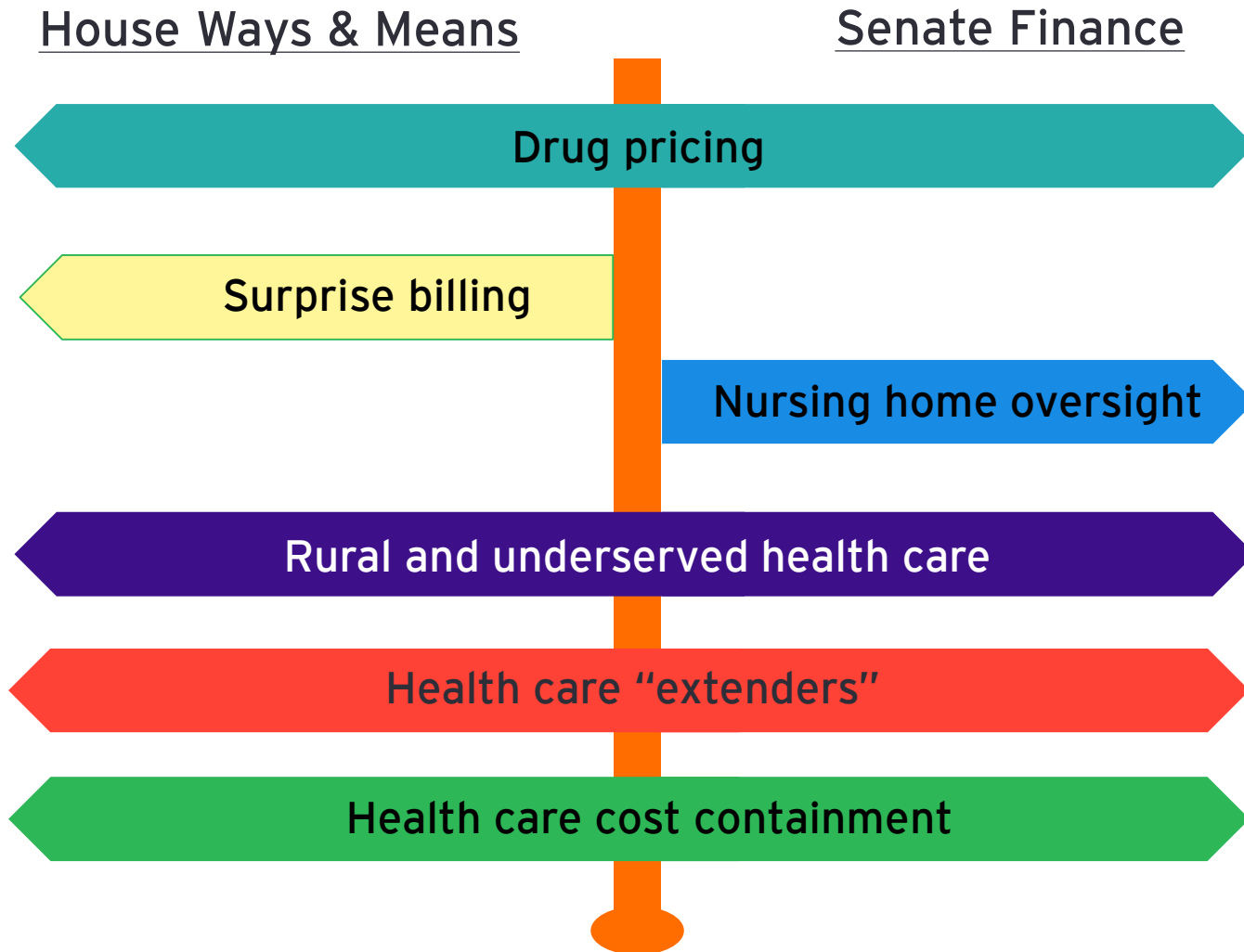
COBRA coverage

Other Congressional and administration priorities

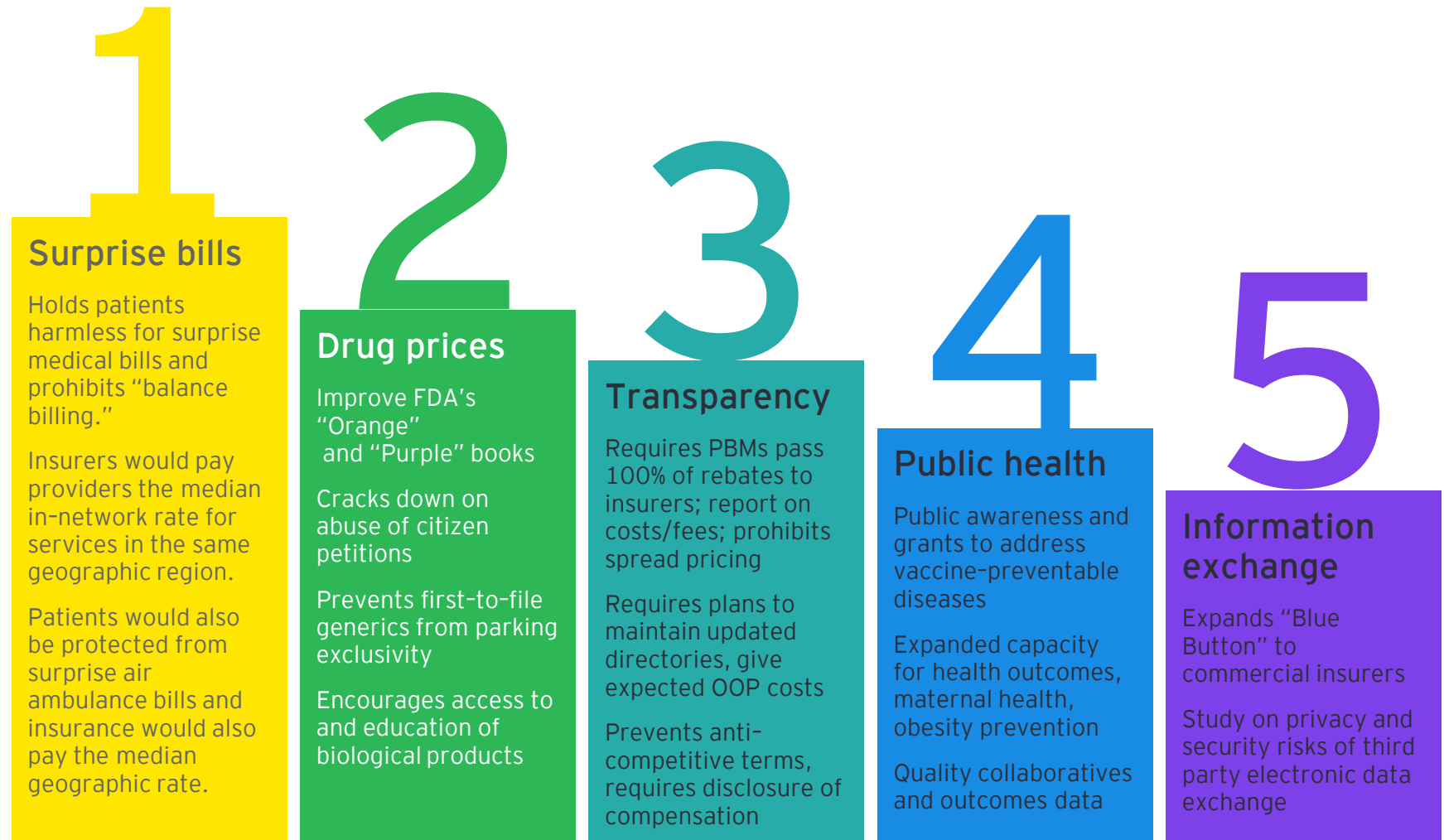
2020 key legislative health care issues



Priorities for key committees

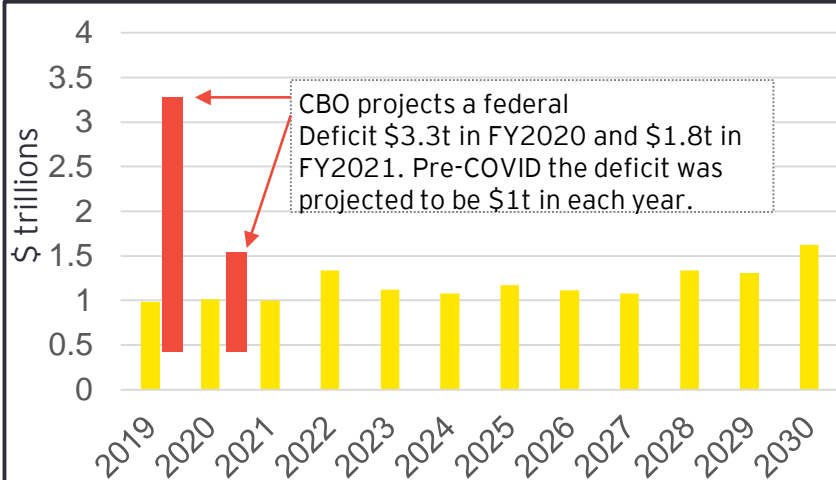


Senate HELP committee focused on cost containment, including surprise bills, drug pricing, transparency



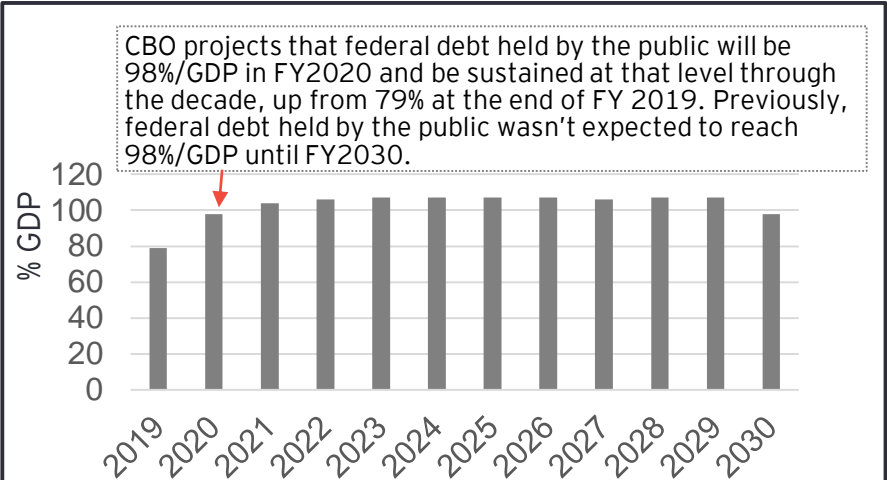
Deficit, debt could put pressure on future health care changes

Federal deficit increase resulting from coronavirus



Source: Congressional Budget Office, An Update to the Budget and Economic Outlook : 2020-2030, September 2020.

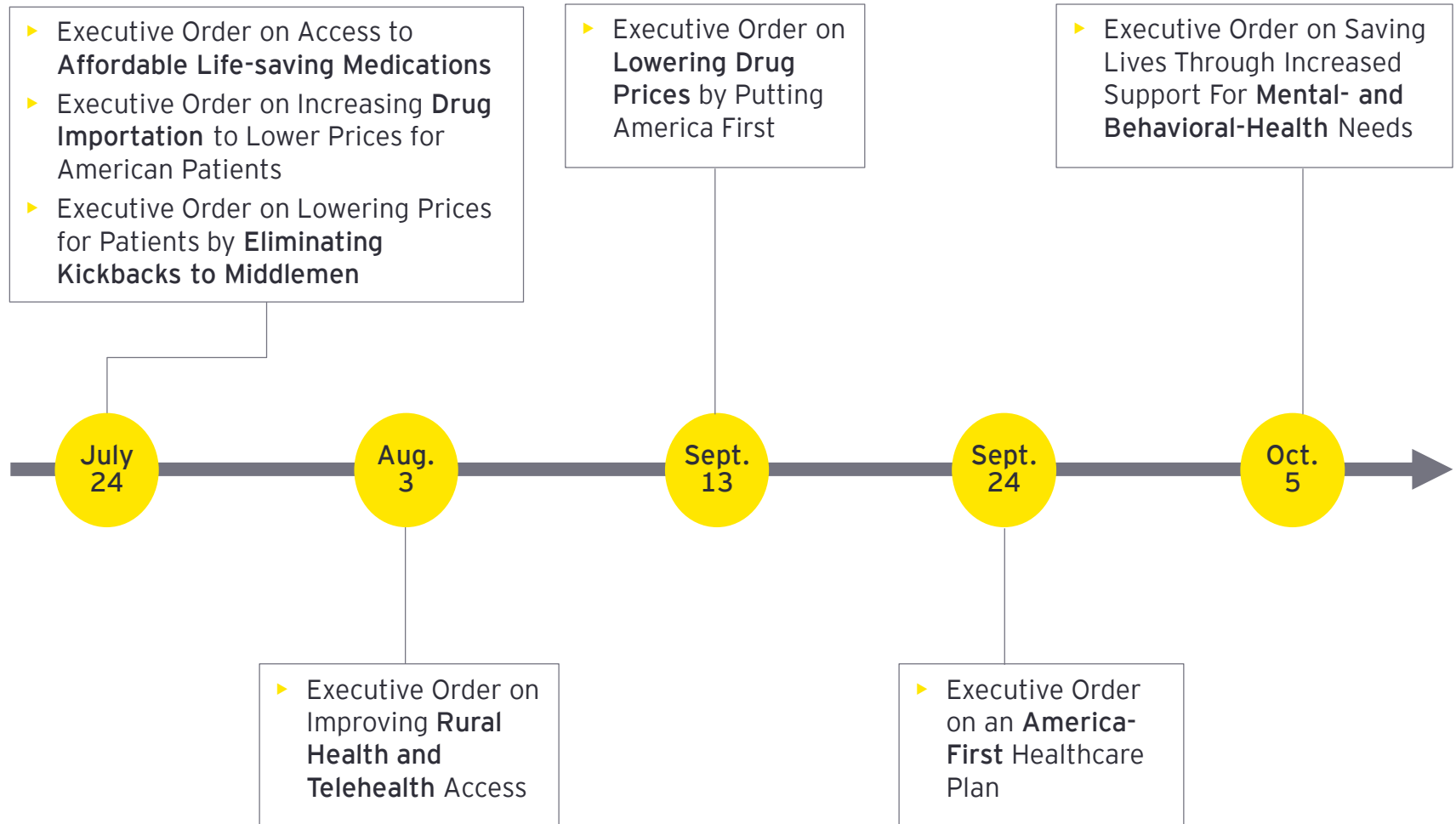
Federal debt as % of GDP to top 100% much sooner than previously projected



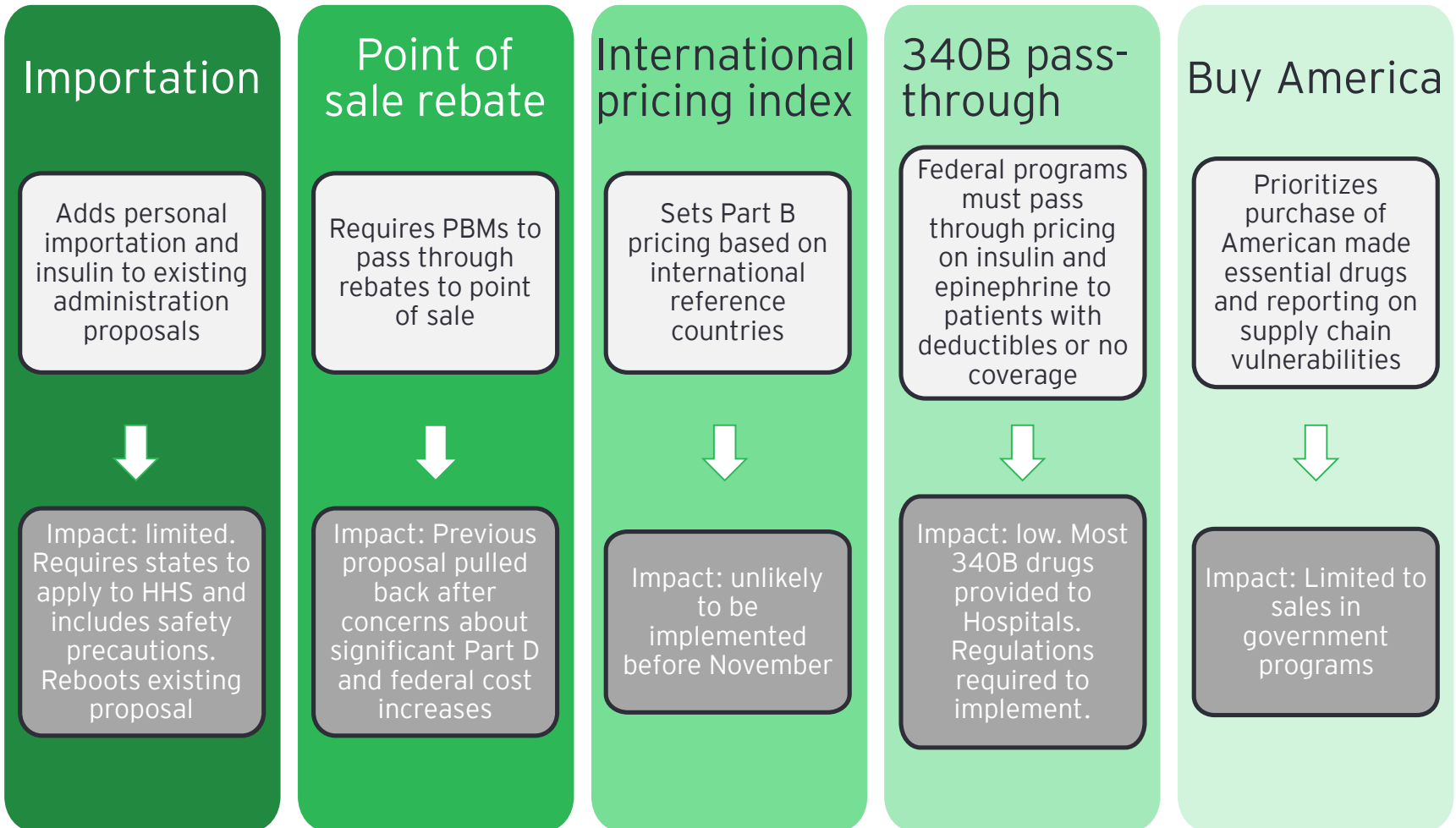
Source: Congressional Budget Office, An Update to the Budget and Economic Outlook : 2020-2030, September 2020.

- Democrats say if they have new power in the presidency and/or Senate majority in 2021, they will first act to repair coronavirus economic damage before increasing taxes.
- Steep deficits and debt will put pressure on finding new revenues. There is speculation about tax increases and a renewed focus on offsets or cuts to the health care sector.

Executive orders outline President's health care priorities ahead of election



Executive orders on drug pricing reboot existing policies



Administration hospital price transparency rule and proposed out-of-pocket cost requirements for insurers

Hospital transparency final rule

Posting of standard charges

- ▶ Hospitals must post standard charges in a “machine-readable” format for all items and services on a public website, updated annually. Standard charges that must be listed are:
 - ▶ Gross charges; Payer-specific rates; Discounted cash prices; Deidentified minimum and maximum rates

Requirements for “shoppable services”

- ▶ Hospitals must post standard charges for 300 “shoppable services” in a consumer friendly way:
 - ▶ 70 CMS-specified services (e.g. x-ray, CT)
 - ▶ 230 hospitals selected services
- ▶ CMS will deem this met if operating a price estimator tool for as many services providing real-time estimates without barriers to access

Enforcement

- ▶ Monitoring, auditing, corrective action plans, and civil monetary penalties of up to \$300 per day.

Burden

- ▶ CMS estimates it would take each hospital 150 hours and ~\$12k to implement in the first year.

Timeline

- ▶ Policies would be effective January 1, 2021.

Insurer transparency proposed rule

Online self-service tool for out-of-pocket costs

- ▶ Plans/issuers must make available personalized out-of-pocket costs information including:
 - ▶ Estimated cost-sharing liability
 - ▶ Accumulated amounts
 - ▶ Negotiated rates
 - ▶ Out-of-network allowed amounts
 - ▶ Items and services content list
 - ▶ Prerequisites for coverage and disclosures
- ▶ Information must be searchable by item/service, provider, billing code, and cost sharing tier.

Public disclosure of rates and payments

- ▶ Two files must be made public that include:
 - ▶ Negotiated rates by provider
 - ▶ Historic out-of-network amounts for 90 days

Inclusion of “shared savings” in MLR

- ▶ Allow plans/issuers who incentivize consumers through shared savings when selecting lower-cost, higher-value providers to include saving in MLR

Timeline and Comment

- ▶ All provisions except MLR take effect one year post finalization. MLR takes effect in 2020 plan year.
- ▶ Comments open until 60 days after rule release.

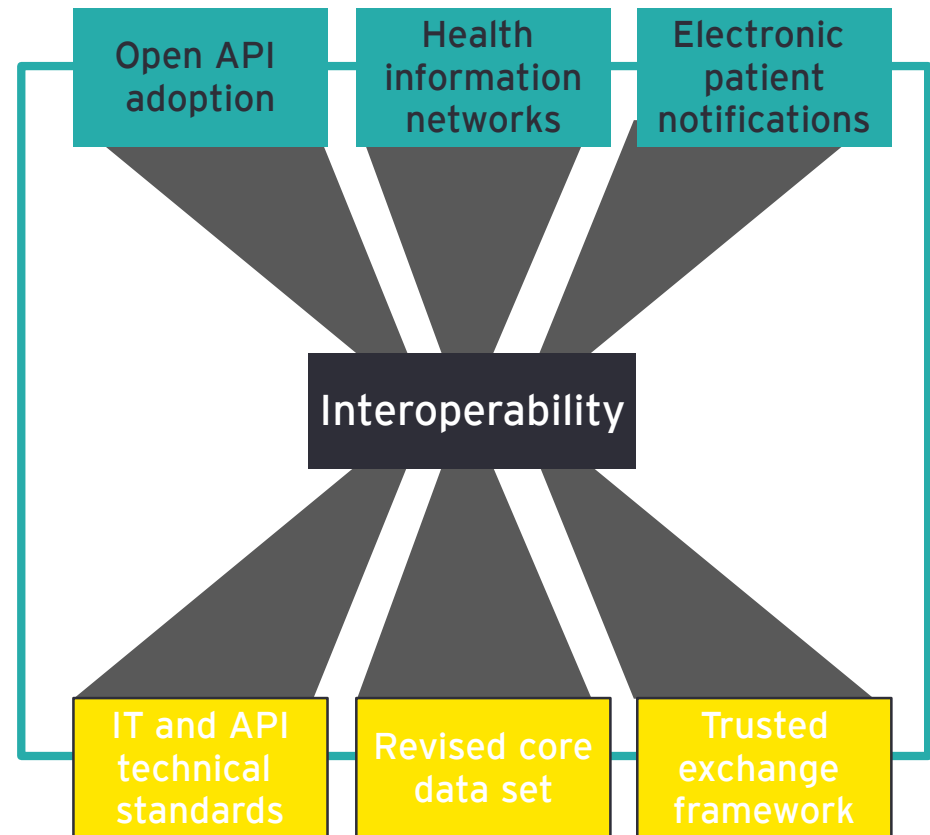
CMS/ONC interoperability and information blocking rules

CMS Interoperability Rule

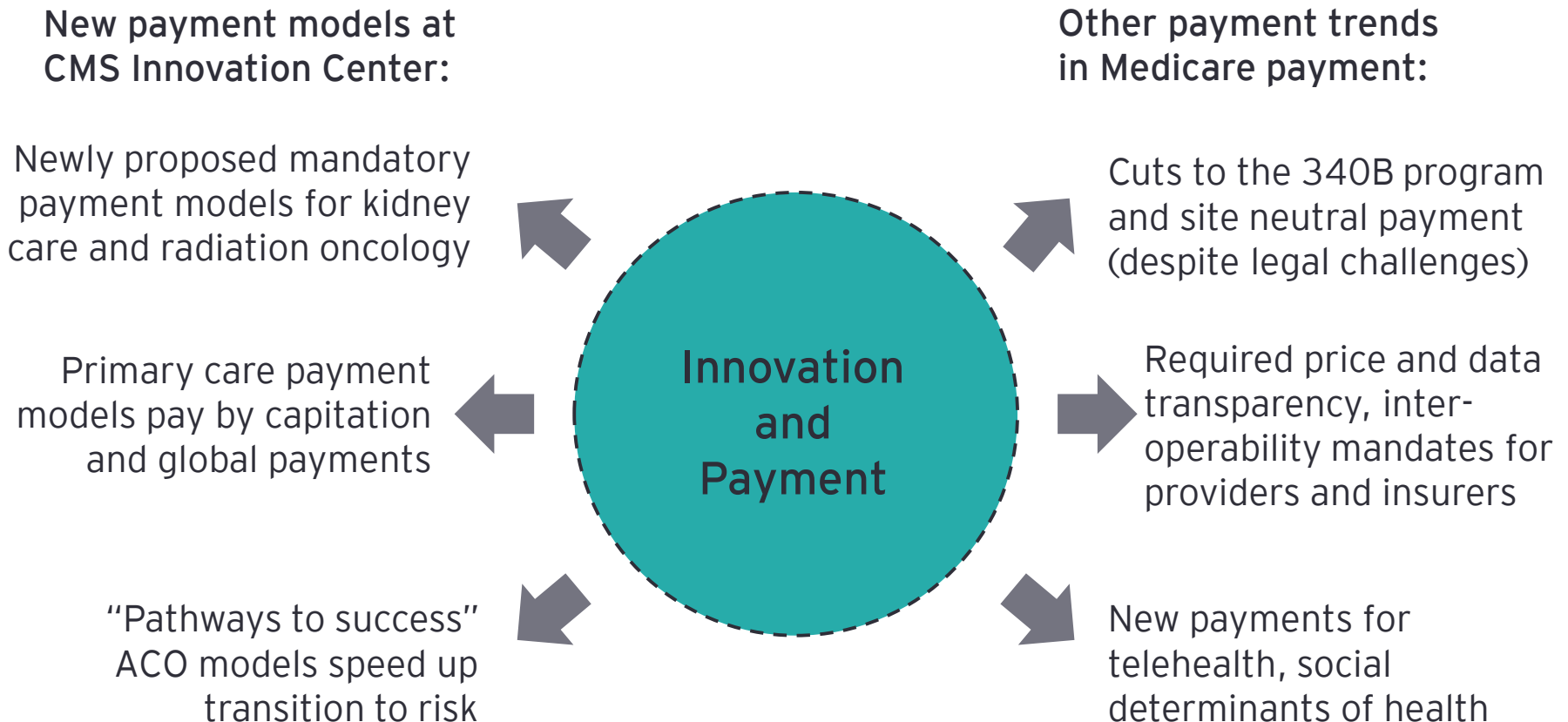
- ▶ **Payers:** Required to adopt open APIs, support electronic data exchange, and engage in health information networks to increase patient access to data and overall interoperability of the system
 - ▶ Those offering QHPs, MA plans, Medicaid/CHIP MCOs and fee-for-service programs are impacted by the rule
- ▶ **Providers:** must adopt technologies to allow patients easier access to their data, comply with electronic event notification requirements and disclose if they engage in information blocking

ONC Information Blocking Rule

- ▶ Sets standards for health IT developers and API certification criterion
- ▶ Proposes removal of 2015 Edition of “Common Clinical Data Set” in favor of the USDI
- ▶ Clarifies what information blocking is and seven “reasonably and necessary” exceptions
- ▶ Requests information on ONC’s draft Trusted Exchange Framework and Common Agreement



New Medicare payment models and trends from HHS



Appendix (Other things you might want to know)

Highlights of COVID-19 relief packages

1

"Coronavirus Preparedness and Reponses Supplemental Appropriations Act"

- ▶ \$3.1b to develop and purchase vaccines and medical supplies
- ▶ \$2.2b for the CDC for preparedness, response, and detection
- ▶ \$826m to support R&D of vaccines, therapeutics and diagnostics
- ▶ \$1.2b for global health programs, humanitarian assistance

2

"Families First Coronavirus Response Act"

- ▶ Requires two weeks of paid sick leave for private sector employers (<500 workers)
- ▶ Up to 12 weeks of family and medical leave for private sector employers (<500 employees and public sector)
- ▶ 100% refundable payroll tax credit on required wages and additional health benefits
- ▶ \$1 billion to states for unemployment insurance
- ▶ 6.2% Medicaid FMAP increase and funding for uninsured
- ▶ \$500m in food and nutrition assistance programs
- ▶ Requires free COVID-19 testing without prior authorization, allocates associated funding

3

"Coronavirus Aid, Relief, and Economic Security (CARES) Act"

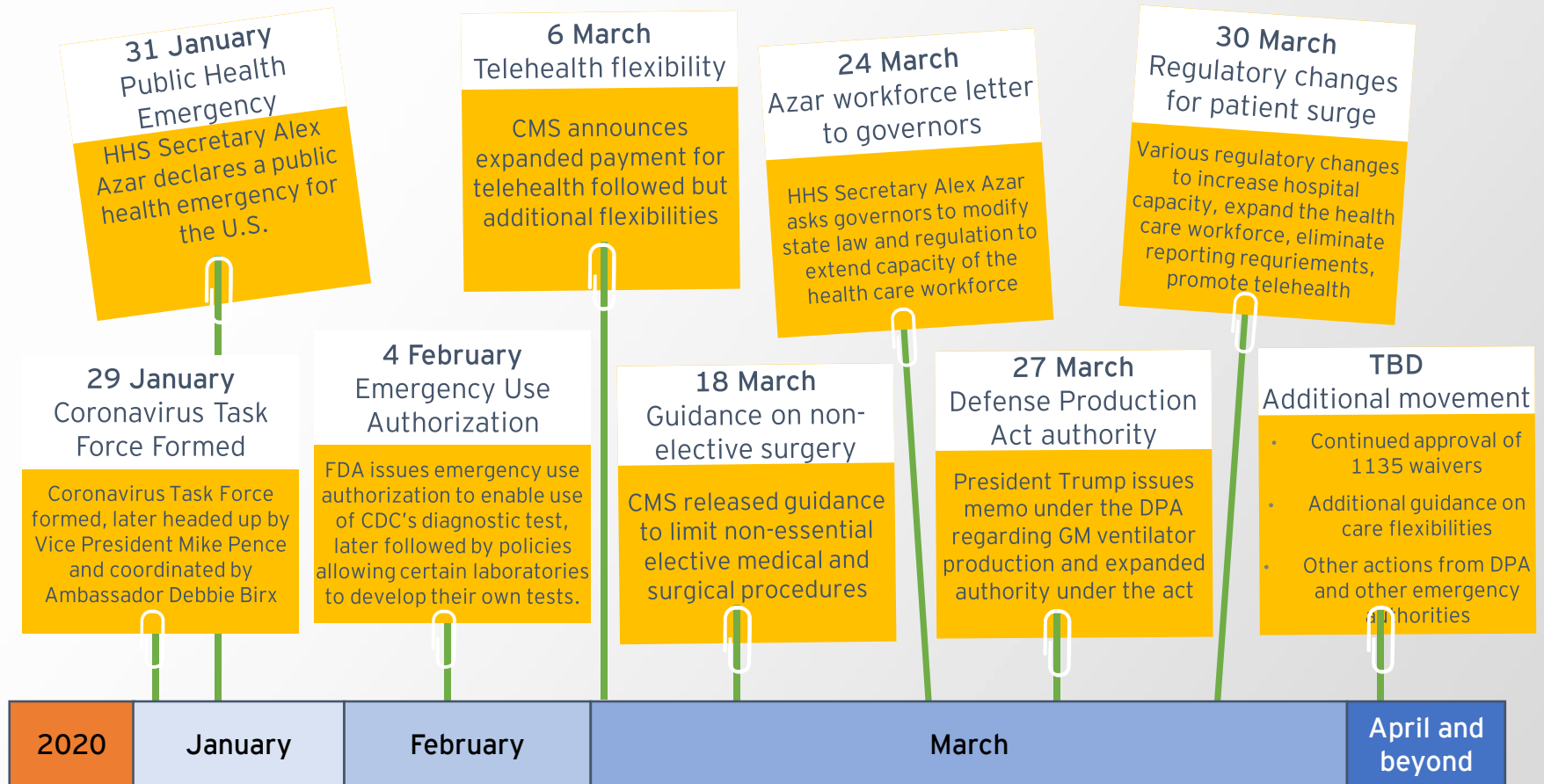
- ▶ \$292b in individual payments
- ▶ \$500b in economic stabilization
- ▶ \$377b for small businesses
- ▶ \$150b in aid to states
- ▶ \$260b in expanded unemployment benefits
- ▶ \$276b in business tax items
- ▶ \$140b in health care funding
- ▶ \$1.23b health center funding
- ▶ Requires free coverage of COVID-19 vaccines
- ▶ Boost in COVID-19 Medicare payments, delayed cuts
- ▶ Medicare telehealth flexibility
- ▶ Drug and device reporting
- ▶ Extension of Medicare, Medicaid, health programs

4

TBD: Ideas for the next bill under discussion

- ▶ More funding for state and local governments
- ▶ OSHA regulations to protect first responders
- ▶ Hazard pay for federal workers treating COVID-19 patients, or who have frequent public contact
- ▶ Free treatment for COVID-19 patients
- ▶ Expanded family and medical leave
- ▶ More money for food stamps (SNAP)
- ▶ Shoring up pension funds
- ▶ Possible 2nd round of direct payments to people

Highlights of federal action



Highlights of state movements actions

Stay at home, gathering, business closures and travel restrictions

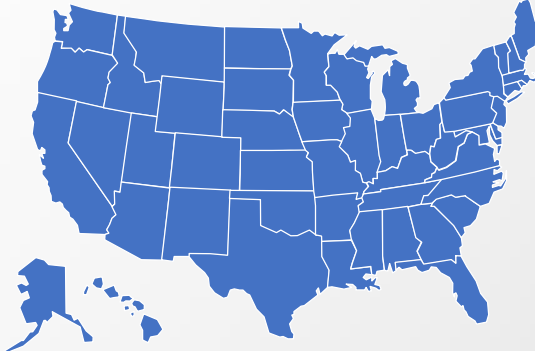
As of late March:

- 33 states issued stay at home orders,
- 15 have mandatory travel quarantine
- 35 closed non-essential business
- 46 have some gatherings ban
- 49 have state-mandated school closure
- 50 have bar/restaurant limits
- 51 have declared emergencies

State legislative action

As of late March, at least 35 states have introduced legislation to support state action related to COVID-19. This includes on issues such as:

- Appropriation of funds
- Insurance coverage, medical costs, or telehealth services
- Paid leave
- Unemployment benefits
- Workforce protections
- Eligibility for public services



Providers



Public and private payers



Individuals



State agencies and businesses

Health policy actions

As of late March:

- 3 states have waived COVID-19 cost sharing for treatment
- 9 states require free vaccine when available
- 10 states have waived prior authorization
- 16 states require early prescription refills
- 12 have marketplace special enrollment periods

Medicaid emergency authority

As of late March, 35 states have submitted and gotten approved Section 1135 waivers to waive or modify certain Medicare, Medicaid, and CHIP requirements during the emergency

Elective procedures

As of late March, 32 states have released statements addressing the issue of elective procedures during the ongoing COVID-19 outbreak

Bipartisan focus on addressing “surprise” medical bills, but disagreement on payment solution

LEADING LEGISLATION	Patient protections	Payment resolution	Ambulance provisions
E&C: No Surprises Act (H.R. 3630)	<ul style="list-style-type: none"> • Holds patients harmless by limiting cost-sharing to the in-network rate • Prohibits balance bills • Up-to-date provider directories 	Set at median in-network rate; arbitration option if over \$1,250	Transparency for air ambulance bills
HELP: Lower Health Care Costs Act (S. 1895)	<ul style="list-style-type: none"> • Holds patients harmless by limiting cost-sharing to the in-network rate • Prohibits balance bills • Up-to-date provider directories 	Set at median in-network rate; no arbitration	Out-of-network air ambulances set at median in-network rate
Ed & Labor: Ban Surprise Billing Act (H.R. 5800)	<ul style="list-style-type: none"> • Holds patients harmless by limiting cost-sharing to the in-network rate • Prohibits balance bills • Up-to-date provider directories • Access to expected cost-sharing 	Set at median in-network rate; arbitration option if over \$750	Out-of-network air ambulances set at median in-network rate; arbitration if over \$25,000. Increases ground ambulances transparency
W&M: Consumer Protections Against Surprise Medical Bills Act (H.R. 5826)	<ul style="list-style-type: none"> • Holds patients harmless by limiting cost-sharing to the in-network rate • Prohibits balance bills • Up-to-date provider directories • Detailed explanation of benefits before scheduled care 	Relies on mediation and arbitration for disputes	Transparency for air ambulance bills

Dec. '19 E&C/HELP Compromise:

- Sets payment at median in-network rate
- Arbitration for bills >\$750
- Includes air ambulance bills >\$25k

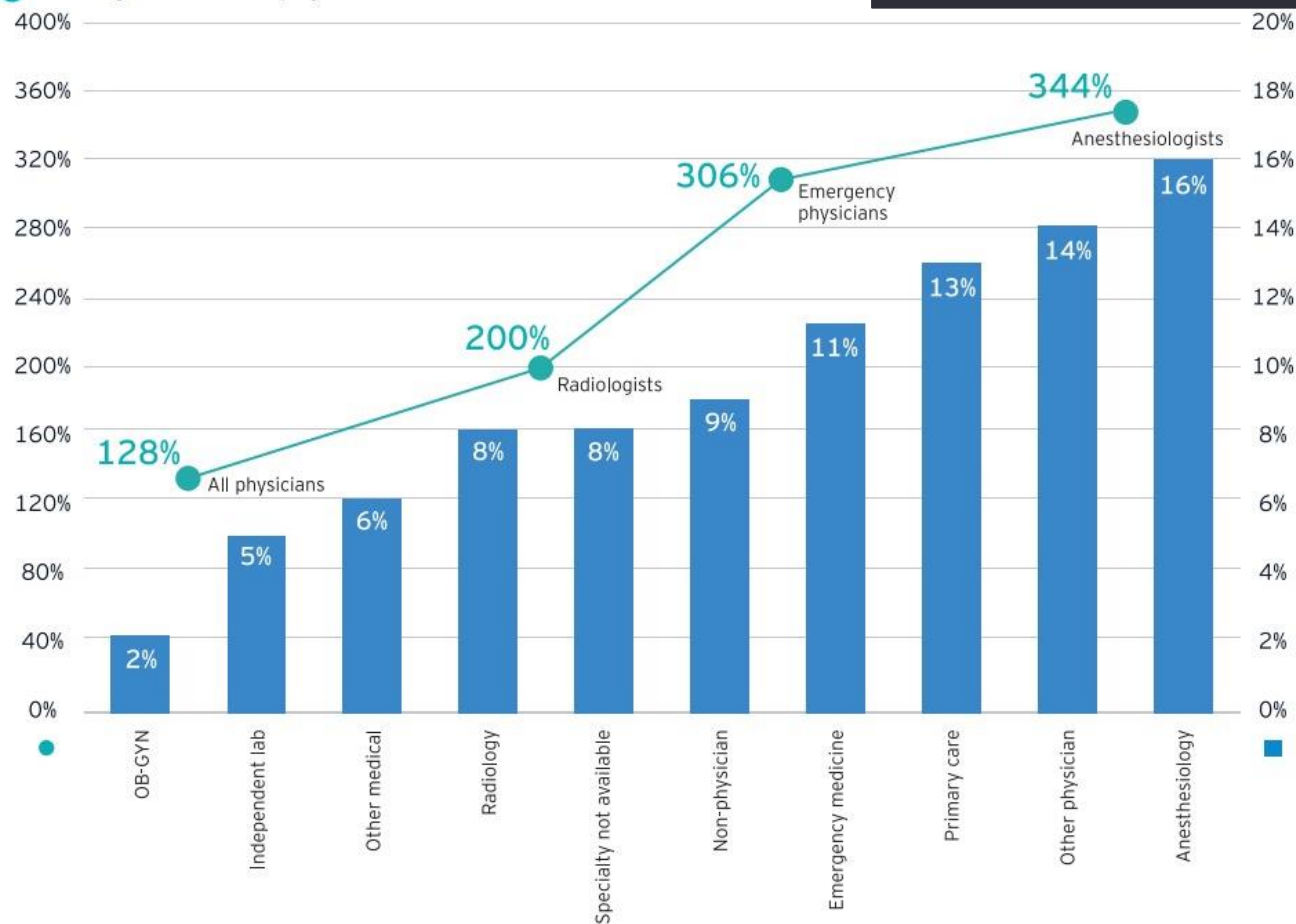
Similar to above

Certain providers would be more impacted by changes to out-of-network billing rates

Out-of-network claims and in-network rates, by specialty

■ Share of out-of-network professional claims by specialty
Percent of all OON claims associated with in-network admissions by specialty, 2016

● Average contracted payment relative to Medicare rates



Percentage of out-of-network ambulance transports for privately insured patients

51%

Ground ambulance transport

69%

Air ambulance transport

Overlap between Speaker Pelosi's Medicare negotiation bill and Senate Finance bi-partisan drug package

Speaker Pelosi's bill (H.R. 3)

Senate Finance bill (S. 2543)

HHS negotiation for certain drugs capped at 1.2x of six countries			Improvement of Medicare average sales price methodology
Steep penalties for drug companies that do not reach agreement			Reduces WAC-based payment and caps add-on for certain drugs
Medicare Part B and D rebates for prices rising faster than inflation	Part D based on AMP + 2016 benchmark	Part D based on WAC + use 2019 benchmark	Medicare Part B and D rebates for prices rising faster than inflation
Medicare Part D redesign	\$2k OOP cap + higher manufacturer responsibility	\$3k OOP cap + higher drug plan responsibility	Medicare Part D redesign
Price reporting for drug cost increases	Reporting for >10% in 12-mo or >35% in 36-mo period	Reporting for >100% in 12-mo period	Price reporting for drug cost increases

Potential areas for compromise:

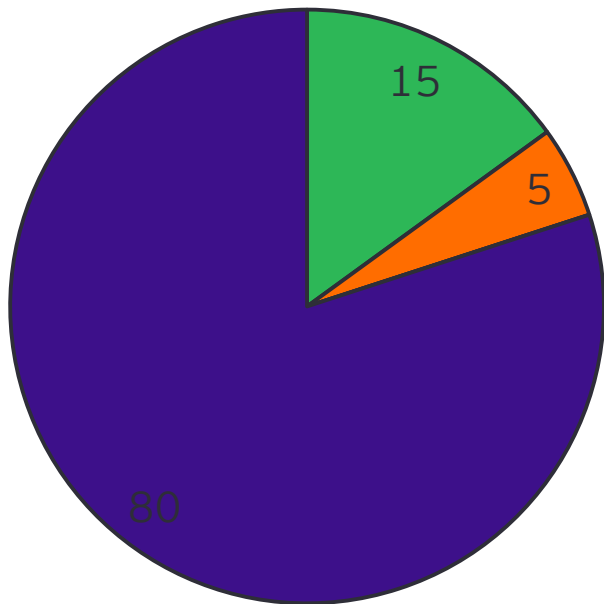
* Areas with broad bipartisan support

Part D redesign proposals vary in burden of costs in the catastrophic benefit phase and out-of-pocket limits

Share of costs in catastrophic coverage period paid by:

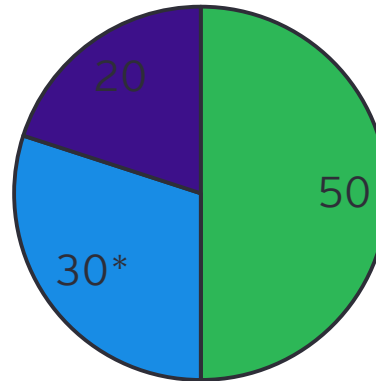


Current Law



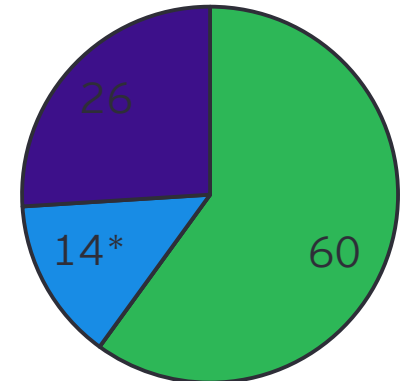
No out-of-pocket cap

House Democrats (H.R. 3)



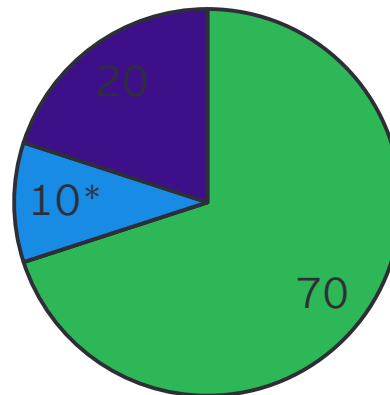
\$2,000 out-of-pocket cap

Senate Finance (S. 2543)



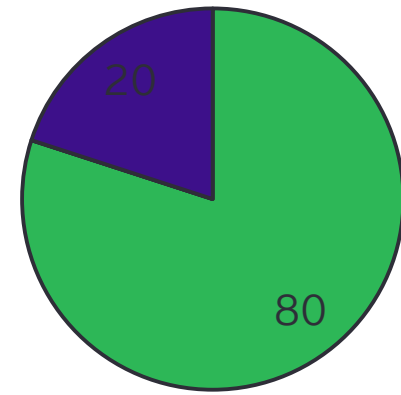
\$3,100 out-of-pocket cap

Crapo bill (S. 3129/H.R. 19)



\$3,100 out-of-pocket cap

Administration's plan



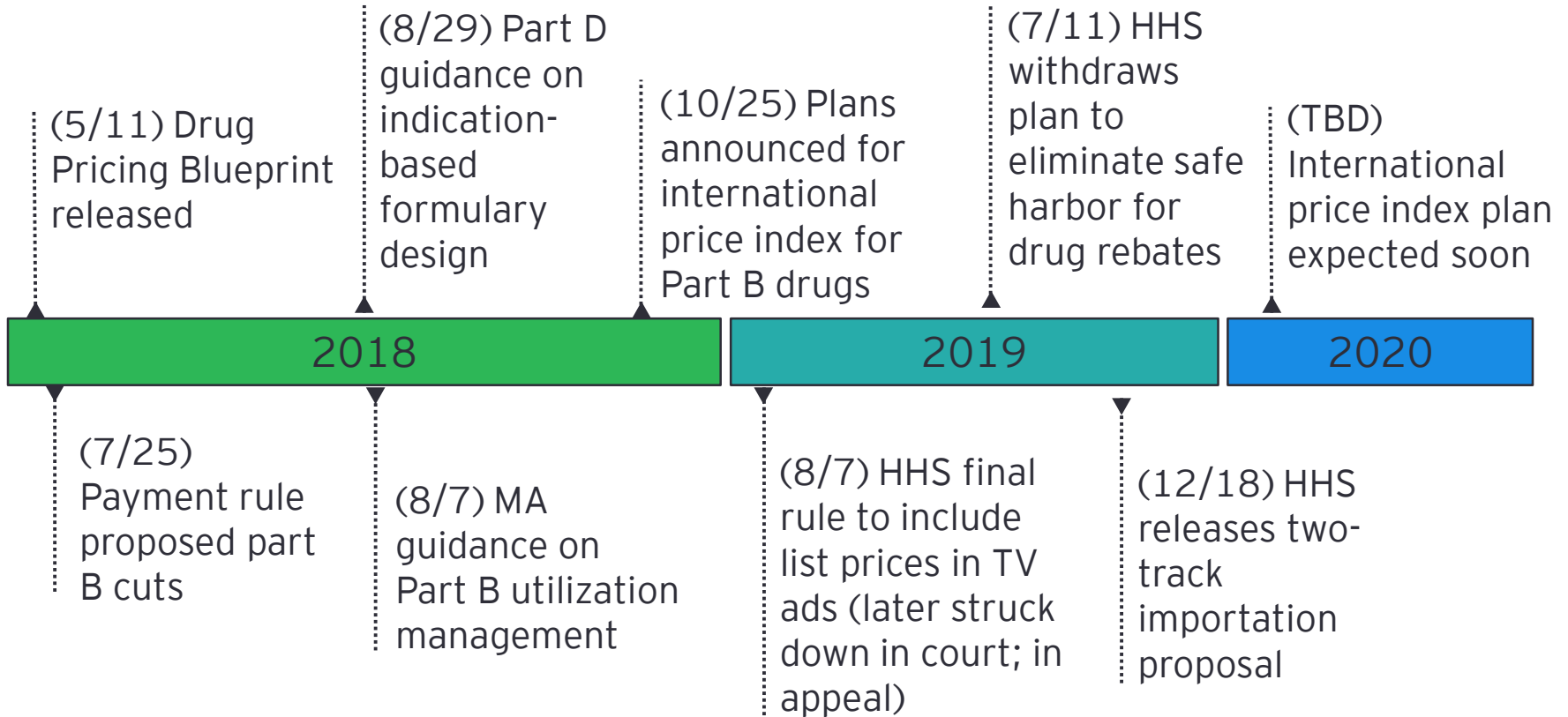
Out-of-pocket cap not specified

*Plans would also require manufacturers to cover a share of the costs in the initial coverage period (7% for S. 2543 and 10% for H.R. 19 and H.R. 3).

Other areas for drug pricing compromises on the margins

Topic	Committee approval	Floor action
'Pay for delay' in patent settlements	<ul style="list-style-type: none"> ▶ House E&C (H.R. 1499) ▶ House Judiciary (H.R. 2375) 	<ul style="list-style-type: none"> ▶ House passed H.R. 1499 under H.R. 987
Generic exclusivity 'parking'	<ul style="list-style-type: none"> ▶ House E&C (H.R. 938) ▶ Senate HELP (S. 1895) 	<ul style="list-style-type: none"> ▶ House passed H.R. 938 under H.R. 987
'Sham' citizen petitions	<ul style="list-style-type: none"> ▶ House Judiciary (H.R. 2374) ▶ Senate Judiciary (S. 1224) ▶ Senate HELP (S. 1895) 	<ul style="list-style-type: none"> ▶ N/A
'Product hopping' and 'patent thickets'	<ul style="list-style-type: none"> ▶ Senate Judiciary (S. 1416) 	<ul style="list-style-type: none"> ▶ N/A
Drugmaker reports on price increases	<ul style="list-style-type: none"> ▶ House W&M (H.R. 2113) ▶ House E&C (H.R. 2296) ▶ Senate HELP (S. 1895) ▶ Senate Finance (S. 2543) 	<ul style="list-style-type: none"> ▶ N/A
Various PBM proposals, including on spread pricing, FTC reports, and pricing and rebate disclosures	<ul style="list-style-type: none"> ▶ House Judiciary (H.R. 2376) ▶ House E&C (H.R. 2296) ▶ House W&M (H.R. 2113) ▶ Senate Judiciary (S. 1227) ▶ Senate HELP (S. 1895) ▶ Senate Finance (S. 2543) 	<ul style="list-style-type: none"> ▶ House passed H.R. 2115, H.R. 1781, and H.R. 3415 (PBM pricing and rebate disclosures and access)

Administration action on drug pricing continues, along with state movement



State are increasingly passing their own drug pricing laws focused on, for example:

- ▶ Price transparency and price gouging
- ▶ Spending and rebate practices
- ▶ Utilization management guidelines
- ▶ Limits for out-of-pocket beneficiary spending
- ▶ Easing biosimilar drug substitution
- ▶ Importation, group purchasing, etc.

Two-track importation plan proposed; International pricing index demonstration program expected soon

Two-track importation proposal

- ▶ **Two-track drug importation plan unveiled in December:**
 - ▶ Track 1: Allows states, wholesalers and pharmacists to import drugs from Canada if HHS certifies them safe and it will save consumers money (through demonstration plans approved by HHS).
 - ▶ Track 2: Allow drug makers to import their own drugs intended for distribution abroad and create new NDCs to sell at a lower price point
- ▶ **Administration already working with states:**
 - ▶ The administration has indicated they are close to allowing Florida to import drugs, who has already submitted a plan outline to HHS
 - ▶ Wholesalers are open to importing Canadian drugs for Vermont as well

Int'l Pricing Index (IPI) demonstration

- ▶ **International reference pricing demonstration (under NPRM) expected soon:**
 - ▶ Replace Part B pay rates with rates based on international prices (move from 180% to 126% of international rates)
 - ▶ 50% of the country would be part of demonstration, potentially moving to whole
 - ▶ Start with sole-source Part B, move to others
 - ▶ Vendors would have to negotiate lower prices each year to maintain profits
- ▶ **Unanswered questions/potential changes in upcoming rule:**
 - ▶ Lower target price to <126%?
 - ▶ Addition of Part D drugs?
 - ▶ Impact on foreign markets?

President Trump executive order on price and quality transparency for providers and insurers

1

Transparency of “actual prices”

HHS should propose regulations to require hospitals to post standard charges and negotiated rates, and to require providers and insurers to provide access to expected out-of-pocket costs before patients receive care

2

Quality measure roadmap

HHS should develop a roadmap to align and improve on data and quality measures across programs

3

Patient access to claims data

HHS and other agencies should increase access to de-identified claims data to empower patients

4

Expanded use of HSAs

Directs Treasury to expand ability to use HSAs and treat arrangements like direct primary care as eligible medical expenses, increase FSA carry-overs

5

HHS surprise billing report

Requires HHS to submit a report on additional ways for the administration to address surprise billing

Increased ACA marketplace competition and state flexibilities, loosened “guardrails” from HHS

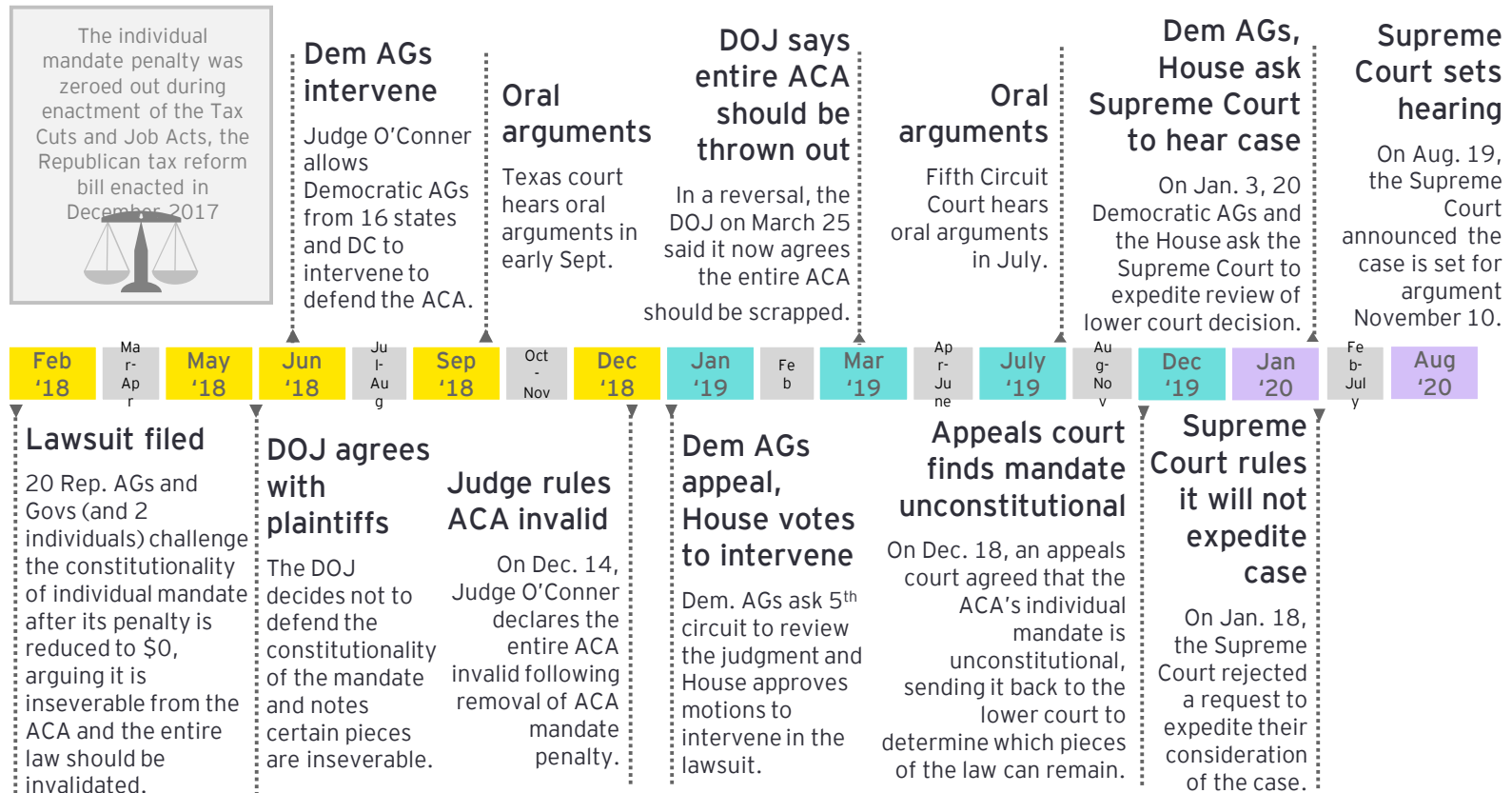
Obama-era ACA

- ▶ 10 essential health benefits (EHBs)
- ▶ Pre-existing condition protections and rating limits
- ▶ “Guardrails” for coverage, affordability, and plan comprehensiveness
- ▶ Medicaid expansion

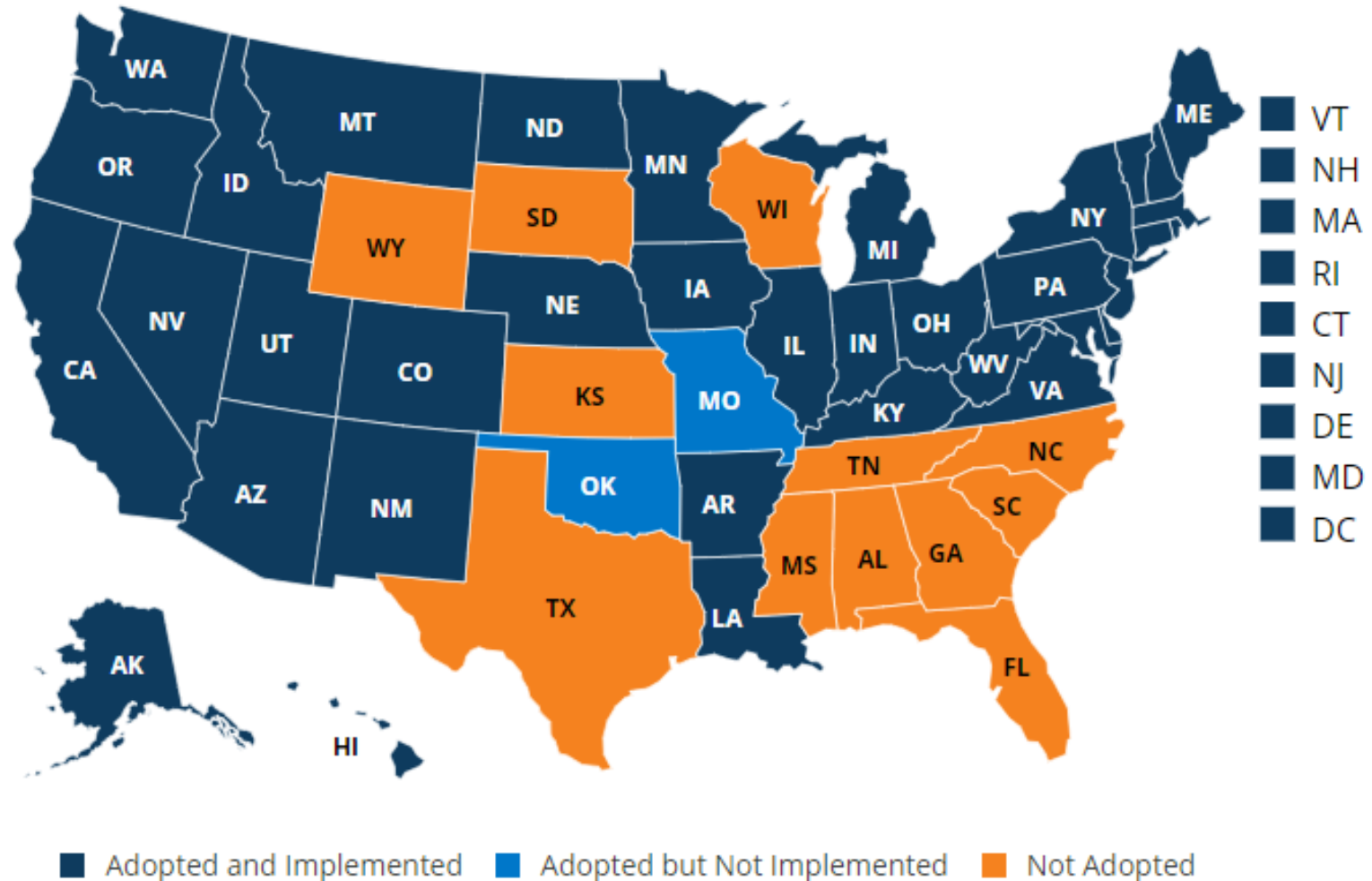
Trump-era ACA

- ▶ Increased state flexibility for EHBs and loosening of other consumer “guardrails”
- ▶ Medicaid work requirements, block grants, other flexibilities
- ▶ Rules to expand access to AHPs¹ and short-term “skinny” plans being litigated
- ▶ Rule permitting use of HRA dollars to purchase market coverage effective 2020

Texas v. Azar lawsuit challenges ACA constitutionality, with Trump Administration siding with Republican states



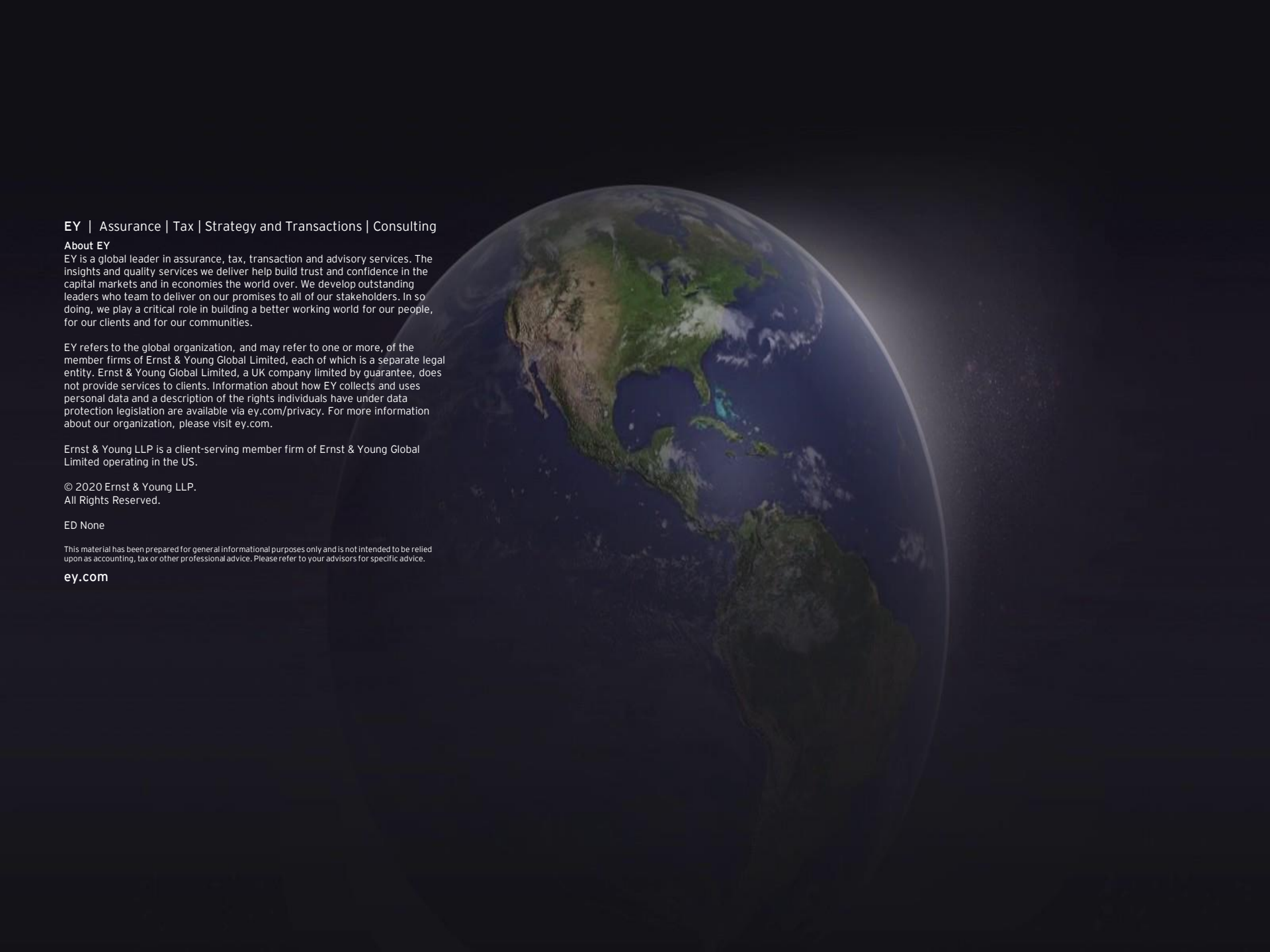
Status of state action on Medicaid Expansion



Source: <https://www.kff.org/medicaid/issue-brief/status-of-state-medicaid-expansion-decisions-interactive-map/>

Questions

Heather Meade, Principal
heather.meade@ey.com



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Financial Due Diligence Overview

Quality of Earnings, Net Debt and Net Working Capital



The better the question. The better the answer.
The better the world works.



Agenda

1. Financial due diligence overview
2. Quality of Earnings
3. Net debt
4. Net working capital

Key takeaways

This presentation will give you a high-level overview of the financial due diligence process, focusing on key topics and considerations for the Quality of Earnings, Net Debt and Net Working Capital analyses.



Brian Mabry

Transactions and Corporate Finance - Senior Manager



Will Bailey

Transactions and Corporate Finance - Manager



Austin Berning

Transactions and Corporate Finance - Manager

Financial due diligence overview

Typical Purchase Price Calculation

Component	Due Diligence Output
Enterprise Value (Adjusted Earnings X Multiple)	Quality of Earnings
+/- Difference in Working Capital as defined and working capital target/peg	Quality of Net Assets / Working Capital
- Indebtedness and Non-Operating Liabilities	Debt and debt-like items / Commitments and Contingencies
- Postponed CAPEX	CAPEX Analysis
+ Transaction Expenses	
+ Cash (if applicable)	
Equals Purchase Price	

How Financial Due Diligence Provides Value

Financial due diligence plays an important role in presenting a clearer picture of the Target's historical operations.

The below schedule shows how different the purchase price can be between the reported numbers, Sell-side CIM and the Buy-side diligence. In the following pages, we will discuss the analyses and considerations that go into the financial due diligence process.

<i>Currency: \$ 000</i>	Reported	Sell-side CIM	Buy-side
EBITDA	20,000	25,000	18,000
Multiple	10x	10x	10x
Enterprise Value (Adjusted Earnings X Multiple)	200,000	250,000	180,000
+/- Difference in Working Capital as defined and working capital target/peg	-	-	-
- Indebtedness and Non-Operating Liabilities	(20,000)	(25,000)	(30,000)
- Postponed CAPEX	-	-	(1,000)
+ Transaction Expenses	-	-	-
+ Cash (if applicable)	1,000	1,000	1,000
Equals Purchase Price	181,000	226,000	150,000

Key Deal Considerations

What is the contemplated deal structure?

- Asset or Stock purchase – “tail risk” contingencies in healthcare stock transactions
- Is the buyer purchasing working capital (specifically AR)?
- Understand the basis of valuation – EBITDA, EBIT, Revenue multiple
- Will the deal involve investors or lenders other than our client?

Other considerations

- Is accounting accrual or cash basis?
- Has the business been audited and will we be able to review the audit workpapers?
- Does the business have a sell-side or buy-side diligence report?
- Acquisitions or discontinued operations?
- Are there multiple participating shareholders taking equity draws (esp. physician practices)?
- How many provider entities and different lines of business?
- Are there significant capitated or risk-sharing reimbursement arrangements?
- Have there been any significant billing or clinical IT system conversions?
- Will they be able to produce the data files necessary to perform revenue testing?

Quality of Earnings

Overview

The importance of EBITDA for buyer and lender:

- Serves as proxy for free cash flow....debt service
- Definitional items (interest, income taxes, depreciation & amortization) addressed separately in model

“Not simply black or white”

- Normalize results to help better depict underlying trends / drivers
- “Quality” and “normalization” requires evaluation and judgment
 - Is Seller's view of normalized earnings over-sanitized?
 - Are “anomalies” an indication of reality?
- Typical EBITDA adjustment categories (details on next page)
 - Out-of-period
 - Non-cash transactions
 - One-time, unusual, non-recurring
 - Pro forma items

EBITDA adjustment categories

1) One-time, unusual, non-recurring

- ▶ Restructuring charges
- ▶ Legal settlements
- ▶ Transaction-related costs
- ▶ System implementation costs
- ▶ Loss of a significant customer
- ▶ Significant change in contractual terms
- ▶ Payroll savings from vacant positions
- ▶ Non-core sources of revenue
- ▶ ACA tax
- ▶ MLR rebates

2) "Non-cash" transactions

Potentially only adjust for cash vs. book difference

- ▶ Deferred rent
- ▶ Stock comp
- ▶ Capitalized internal costs
- ▶ Impairment charges
- ▶ Unrealized gains / losses
- ▶ Amortization
- ▶ Minority interest or equity income
- ▶ Pension and OPEB charges
- ▶ PDR reserves

3) Out-of-period

- ▶ Changes in estimate (benefit of hindsight)
 - ▶ Bad debt, inventory reserves, allowances
 - ▶ Warranty, self-insurance, compensation
- ▶ Timing related
 - ▶ Year-end true-up or audit adjustments
 - ▶ Revenue recognition
 - ▶ Improper cut-off
- ▶ IBNR development
- ▶ Medicare risk scores

4) "Pro forma" items

- ▶ Acquisitions or divestitures run-rate
- ▶ Discontinued operations or product lines
- ▶ Stand-alone or TSA costs ("carve outs")
- ▶ Cost saving initiatives

Provider diligence considerations

- Several financial considerations should be taken into account when evaluating the investment thesis of M&A activity in the healthcare sector

Business or model risks

Revenue recognition and collectability of A/R

- ▶ Does the PL reflect the net realizable value of revenue?
- ▶ Does the company have an established compliance function?
- ▶ Do historical trends indicate current accounts receivable may be collectible?

Reimbursement environment

- ▶ How does reimbursement strategy (i.e. in-network/out-of-network) impact the deal?
- ▶ Are there anticipated legislative changes that may impact future earnings potential of the post-transaction entity?

Acquisitions, de novos and immature providers

- ▶ What is the mature contribution of recent acquisitions, de novos and/or immature providers?

Provider compensation and other physician costs

- ▶ What is the impact of the aforementioned matters on providers' compensation?

Key diligence considerations

- ▶ Assess whether historical accounts receivable estimates have been realized through subsequent cash receipts.
- ▶ Analyze third-party settlement balances.
- ▶ Perform a billing and coding analysis to assess the appropriateness of historical claims. (FIDS)
- ▶ Analyze historical same store and provider performance (including utilization) to determine whether forecasted growth is (i) consistent with historical experience and (ii) achievable with current capacity and macro trends.
- ▶ Analyze provider compensation models to quantify the impact of diligence and pro forma adjustments.
- ▶ Analyze labor metrics and costs.
- ▶ Analyze malpractice and other self-insurance reserves. (Risk)

Provider diligence considerations

- An inadequate reserve methodology could result in net revenue and associated accounts receivable in an excess/deficit position as compared to the net realizable value.

Gross-to-net accounting

Methodology

- Gross revenue is typically recognized in conjunction with the company's chargemaster which stipulates per procedure rates.
- Contractual adjustments represent the difference between the chargemaster and the agreed-upon reimbursement rate to be paid by third parties.
 - Insurance plans reimburse at different rates based on negotiated contracts.

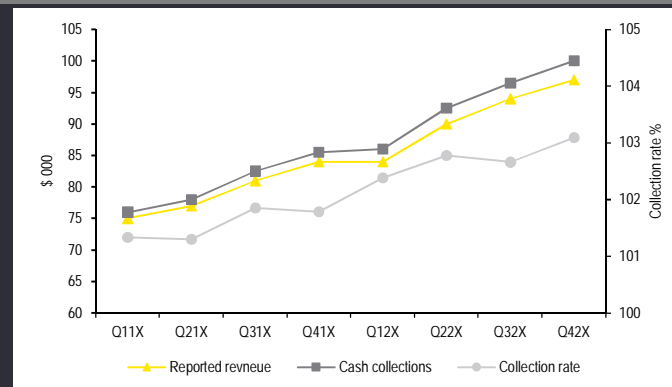
Risk factors

- Changes in reimbursement rates may not be reflected in contractual adjustments and bad debt percentages applied to gross revenue and accounts receivable.
- Historical revenue trends may not be consistent with forecast revenues due to changes in service and payor mix.

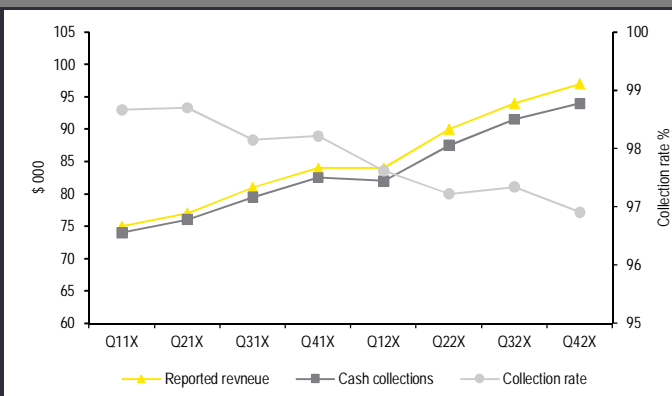
Diligence procedures

- Historical look-back analysis comparing actual cash collections to net reported revenue including an estimate of future collections for immature claims based on historical collection percentages.

Scenario 1 – Increasing reimbursement



Scenario 2 – Declining reimbursement



Revenue recognition considerations

- Estimating revenue is difficult
 - Not all payors reimburse the same amount for the same service
 - Governmental payors - Medicare, Medicaid, and other
 - Managed Care payors - distinguished by types of plans and types of contracts
 - Other payors - commercial insurers, private pay, and others
 - Many providers don't have contracts loaded into patient accounting systems
 - Even when contracts are loaded, patient bad debt, denials and out of network cases complicate the process
- Approaches used by providers to record revenue
 - Percentage of gross charges
 - Unit-based: Volume * historical rate per unit
 - Cash basis
- Gross-to-net presentation of revenue

<i>Currency: \$ 000</i>	FY18	FY19	TTM Aug20
Gross charges	6,569	7,161	7,022
Less: contractual allowances	(1,969)	(2,127)	(2,128)
Less: bad debt	(14)	(33)	(29)
Net collectible revenue	4,587	5,001	4,864
Other adjustments	(217)	(361)	(371)
Net recorded revenue	4,369	4,640	4,494

Payer diligence considerations

- Several financial considerations should be taken into account when evaluating the investment thesis of M&A activity in the healthcare sector

Business or model risks

Claims expenses and incurred-but-not-reported reserves

- ▶ Does the plan utilized fixed capitation payments, fee-for-service models or a blend?
- ▶ Has the plan utilized consistent reserving practices or experienced large out-of-period reserve adjustments?
- ▶ Does the plan have material risk-sharing arrangements or complex gain share calculations?

Regulatory / legislative environment

- ▶ Are there anticipated legislative changes that may impact future earnings potential of the post-transaction entity?
- ▶ What are the potential impacts to the plan's business under different political scenarios?

Revenue recognition and collectability of A/R

- ▶ Does the PL reflect the net realizable value of revenue?
- ▶ Does the company have strong controls over the enrollment and member reconciliation process?

Sustainable operating cost model

- ▶ Does the Company's headcount model balance between efficiency and achieving projected growth?

Key diligence considerations

- ▶ Analyze plan's different provider contract models and understand financial implications of such.
- ▶ Coordinate with independent actuaries to perform a review of key reserve accounts and stress-test methods and assumptions employed by Target.
- ▶ Analyze third-party settlement balances.
- ▶ Analyze historical product-type performance (e.g. trended medical loss ratio) to determine whether forecasted growth is consistent with historical experience.
- ▶ Assess plan's mix of business (managed care vs. governmental business) to gain understanding of risk / exposures to regulatory implications.
- ▶ Assess whether historical accounts receivable estimates have been realized through subsequent cash receipts.
- ▶ Analyze labor metrics and costs.
- ▶ Analyze outsourced services and contractual implications of a potential transaction

Prior-period reserve development example

- Out-of-period earnings impacts can be large if the Company is inaccurate or inconsistent with its reserve estimation process.

Multi-year reserve example

Methodology

- As claims experience emerges in the following period due to receipt and payment, actuarial estimates are able to be adjusted and often result in meaningful adjustments to prior period liabilities.
- If prior-period reserve development is favorable in one year and unfavorable in the next year, this can lead to large swings to earnings trends when activity is placed in the correct year.

Diligence procedures

- Coordinate with actuarial specialist to perform independent assessment of reserves. Review disclosures and underlying reserve support to determine out of period or other areas of management judgement.

In \$000s	FY20	FY19	FY18
Reserve, beginning of year (A)	15,300	11,600	8,700
Claims incurred			
Current year	220,000	179,000	149,000
Prior year	1,000	(2,000)	(1,000)
Net claims incurred (B)	221,000	177,000	148,000
Claims paid			
Current year	200,000	163,000	138,000
Prior year	16,000	10,300	7,100
Net claims paid (C)	216,000	173,300	145,100
Reserve, end of year (A+B-C)	20,300	18,300	10,600
Reported EBITDA	11,000	9,000	7,000
Adjustments:			
Impact of out-of-period	1,000	(3,000)	1,000
Adjusted EBITDA	12,000	6,000	8,000

Net debt

Overview

The importance of net debt for buyer and lender:

- Identifies on- and off-balance sheet obligations that need to be either settled upon the transaction close or by the buyer subsequent to close.
- Agreed upon net debt items are direct reductions to the purchase price (i.e., the Seller is responsible to settle the net debt items with the proceeds from the sale and the Seller's cash on-hand upon close).
- Different points of view: The Seller wants limited net debt items, resulting in a higher net purchase price. The Buyer seeks for more net debt items so they do not have to cover the future cash outflow.

Gross Purchase Price:
\$200m paid to Seller

Net Debt:
\$25m is paid by
Seller with proceeds

Net Purchase Price:
\$175m

Examples

The identified net debt items are a negotiation between the sellers and buyers. The agreed upon net debt items are generally included within the purchase agreement within the definition of indebtedness.

Example #1: Annual bonuses vs. quarterly/monthly bonuses

- Estimated closing date: March 1, 2021
- Due diligence net debt period: January 31, 2021
- Negotiation:
 - Annual bonuses: If the Target paid annual bonuses each March for the services in the prior year, the Seller should be responsible for paying the accrued bonuses (e.g., included within the purchase agreement's definition of indebtedness) as they received the benefits of the employee's work during that period. The accrued bonuses for January through March of the 2021 could also be negotiated.
 - Quarterly/monthly bonuses: This is similar to the January through March 2021 bonus above, in that it is an item that could be negotiated, so the time period in which the Seller received a benefit is less than a full year's benefit.

Example #2: COVID liabilities

- Due to the COVID-19 pandemic, Sellers have numerous liabilities (i.e., deferred employer payroll taxes due in FY20 and FY21 and potential payback of PPP loans) that need to be considered for net debt. Payroll taxes are generally not included within net debt but since the deferred taxes are in a form of extended liquidity, the Seller should be responsible to cover the liability.

Example of net debt and debt-like items

Net debt:

- Short & long term borrowings
- Accrued interest payable
- Less: cash and cash equivalents

Debt-like items:

- Past-due accounts payable
- Taxation / escheatment
- Deferred revenue / gift cards
- Commitments and contingencies
- Long term provisions that will translate into cash outflows
- Capital leases
- Long term level of fixed assets creditors
- Rationalization/ restructuring costs/ provisions
- Transaction costs / bonuses
- Overdue patient refunds
- Shortfall in risk-based capital

Examples of off-balance sheet items:

- Factored, securitized and discounted trade receivables
- Pension funding shortfall and other long-term benefit obligations
- Financial instruments valued at fair market value
- Certain capital leases that under local GAAP are not capitalized
- Operating leases
- Deferred capital expenditure
- Breakage costs on financial instruments
- Letters of credit / other credit commitments (e.g. surety bonds)

Example of Sell-side versus Buy-side net debt

	Sell-side			Buy-side		
Currency: \$ 000	On BS	Off BS	Total	On BS	Off BS	Total
Financial indebtedness:						
Term loans	2,862	-	2,862	2,862	1,500	4,362
Accrued interest	n.q	n.q	-	n.q	n.q	-
Total financial indebtedness	2,862	-	2,862	2,862	1,500	4,362
Cash and cash equivalents	16	-	16	16	-	16
Net financial indebtedness	2,846	-	2,846	2,846	1,500	4,346
Other items that may be considered as indebtedness:						
Management bonuses	-	-	-	314	473	787
Tax provisions	348	-	348	348	-	348
Committed capital expenditures	-	-	-	58	240	298
Provisions for anniversary bonuses	228	-	228	228	-	228
Provision for severance payments	263	-	263	263	-	263
Provision for impending losses	-	-	-	40	n.q	40
USD bank account valuation	n.q	n.q	n.q	n.q	n.q	n.q
Acquisition-related contingencies	-	-	n.q	n.q	n.q	n.q
Legal matters	-	-	n.q	n.q	n.q	n.q
Tax matters	-	-	n.q	n.q	n.q	n.q
Total other items that may be considered as indebtedness	838	-	838	1,249	713	1,962
Net debt and debt-like items	3,684	-	3,684	4,095	2,213	6,308
Other considerations:						
Operating leases	n/a	2,360	2,360	n/a	2,360	2,360
COVID-19 funding	-	-	-	n/a	250	250
Trade A/R due from affiliated companies	54	-	54	54	-	54
Trade A/P due to affiliated companies	31	-	31	31	-	31
Warranty	-	-	-	30	n.q	30
Holding company guarantees	-	-	-	n.q	n.q	-
Total other considerations	85	2,360	2,445	116	2,610	2,726

Net working capital

Overview

What is Net Working Capital (“NWC”)?

- Generally - current assets, less current liabilities, excluding cash, indebtedness and income taxes
- All items identified in the net debt analysis, which are within current assets and liabilities, need to be removed from net working capital

Why is NWC important?

- Modeling importance – Change in NWC is a key component to derive free cash flow and, in turn, debt pay down
- Financing importance – Understanding “peak to trough” inter and intra months NWC trends to revolver facility size
- Valuation importance – Calculated EV for a business typically contemplates a “normal level” of delivered NWC. Absent this concept, sellers could plunder corporate coffers between signing and closing through asset monetization and liability deferrals

NWC PEG Overview

- Many SPA’s include an adjustment for the difference between a predetermined target NWC and a closing NWC, which is called the NWC PEG.
- Makes buyer whole, dollar for dollar, for any deviation in delivered NWC versus “normal” level of NWC (contemplated in EV of target)

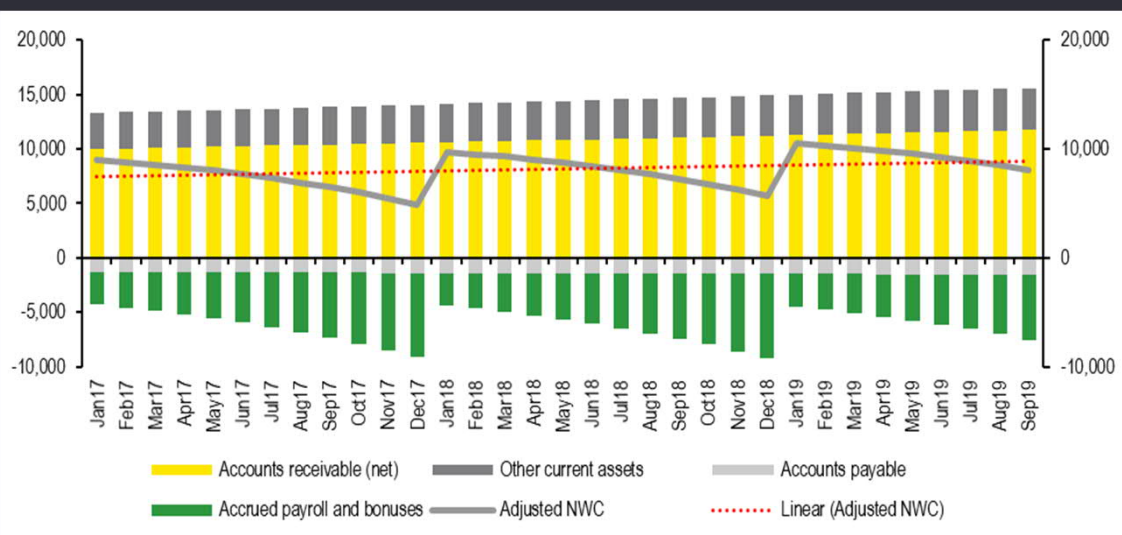
PEG Example

Key considerations

Setting the SPA PEG amount is a key consideration as the difference between the delivered NWC and the SPA PEG results in a direct adjustment to the purchase price.

For provider-focused deals, the main driver in NWC is accounts receivable and accrued payroll/bonuses, so it is important to understand the items such as the timing of payroll and bonuses payouts. The presented schedules show an example at how the timing of close (e.g., the NWC PEG true-up date) can impact how the SPA PEG is set and the corresponding purchase price true-up.

Currency: \$ 000	Dec18	T3M avg	T6M avg	TTM Sep19 avg
NWC PEG based on the applicable dates	5,712	8,503	9,025	8,657
Closing NWC at December 31, 2019	6,000	6,000	6,000	6,000
True-up payment/(receipt)	288	(2,503)	(3,025)	(2,657)



Currency: \$ 000	Oct18	Nov18	Dec18	Jan19	Feb19	Mar19	Apr19	May19	Jun19	Jul19	Aug19	Sep19	T3M avg	T6M avg	TTM Sep19 avg
Accounts receivable (net)	11,104	11,160	11,216	11,272	11,328	11,385	11,442	11,499	11,556	11,614	11,672	11,730	11,672	11,585	11,415
Other current assets	3,663	3,682	3,700	3,718	3,737	3,756	3,774	3,793	3,812	3,831	3,851	3,870	3,851	3,822	3,766
Total current assets	14,767	14,841	14,915	14,990	15,065	15,140	15,216	15,292	15,369	15,445	15,523	15,600	15,523	15,407	15,180
Accounts payable	(1,448)	(1,455)	(1,462)	(1,470)	(1,477)	(1,484)	(1,492)	(1,499)	(1,507)	(1,514)	(1,522)	(1,530)	(1,522)	(1,511)	(1,488)
Accrued payroll and bonuses	(6,516)	(7,102)	(7,741)	(3,000)	(3,270)	(3,564)	(3,885)	(4,235)	(4,616)	(5,031)	(5,484)	(5,978)	(5,498)	(4,871)	(5,035)
Total current liabilities	(7,964)	(8,557)	(9,204)	(4,470)	(4,747)	(5,049)	(5,377)	(5,734)	(6,123)	(6,546)	(7,006)	(7,507)	(7,020)	(6,382)	(6,524)
Adjusted NWC	6,804	6,284	5,712	10,520	10,318	10,092	9,839	9,558	9,246	8,900	8,517	8,093	8,503	9,025	8,657



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Applying transaction analytics to diligence provides greater value, increases speed, creates efficiencies and reduces risk

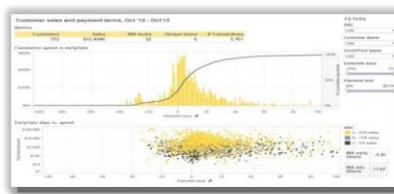
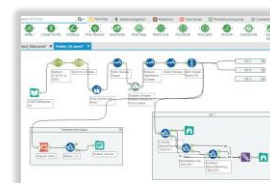
Transaction analytics enhances traditional due diligence by giving you interactive access to enriched information to drive faster and more decisive portfolio and transaction decisions



Data confidence



Dynamic analyses of multiple permutations for key deal value drivers – based on software-enabled, approach to complex datasets.



Interactive data exploration



Platform agnostic use of visualization tools (i.e., Power BI, Tableau, etc.) enables real-time collaboration and interactive interrogation of data.

Incremental insights



Enriched datasets (third-party information and/or connecting disparate target datasets) increases context surrounding key analyses.



Health Analytics Examples: Diligence & Post Diligence



Business imperatives

Synthesize large volumes of claims data to drive decision making

Deploy digital health to increase quality

Optimize costs and improve clinical effectiveness

Increase patient satisfaction



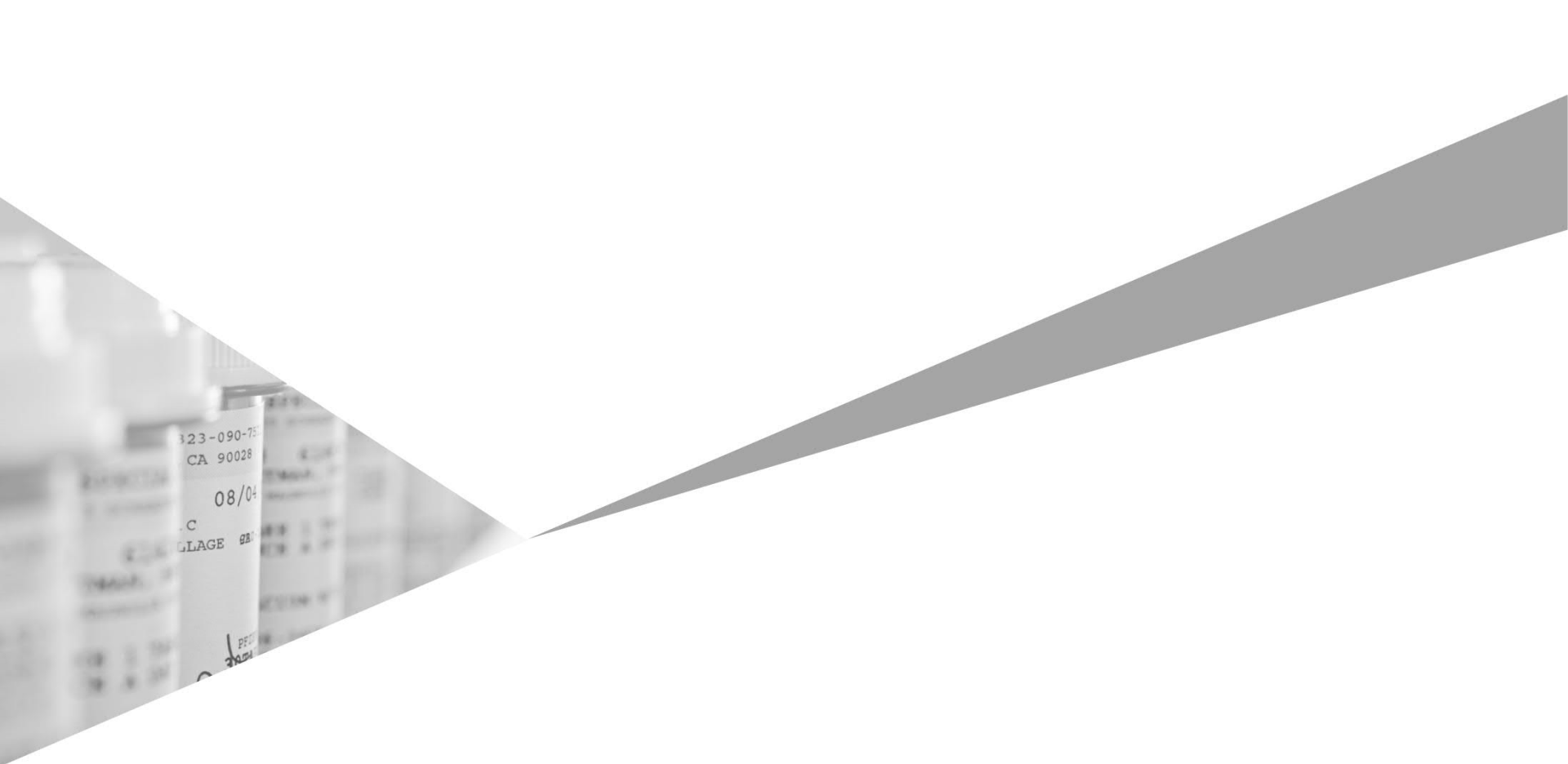
Related interactive data analytics

Diligence Analyses

- ▶ Rate/volume analysis
- ▶ Cash collections analysis (by payor and geographic area)
- ▶ Payor mix
- ▶ Procedure/Acuity Mix
- ▶ Claims data analysis (e.g., CPT/DRG, referral source, payor and provider-level trend analytics)
- ▶ Provider productivity analysis

Post Diligence Analyses

- ▶ Revenue cycle analysis (e.g., denial/re-bill frequency, unbilled charges, charge lag, collections compared to fee schedule by payor)
- ▶ Staffing analysis (clinical and non-clinical costs/ratio per provider)
- ▶ Comprehensive spend analysis
- ▶ Patient engagement
- ▶ Service area and demographics analysis



Tax considerations

Presented by: Chris Wheeler

Tax considerations




- 1) Why tax matters in transactions
- 2) Tax structuring alternatives
- 3) Tax savings from net operating losses (NOLs) and cash tax modeling
- 4) Impact of evolving tax landscape

Question

- Why would a potential buyer want to undertake due diligence for taxes?

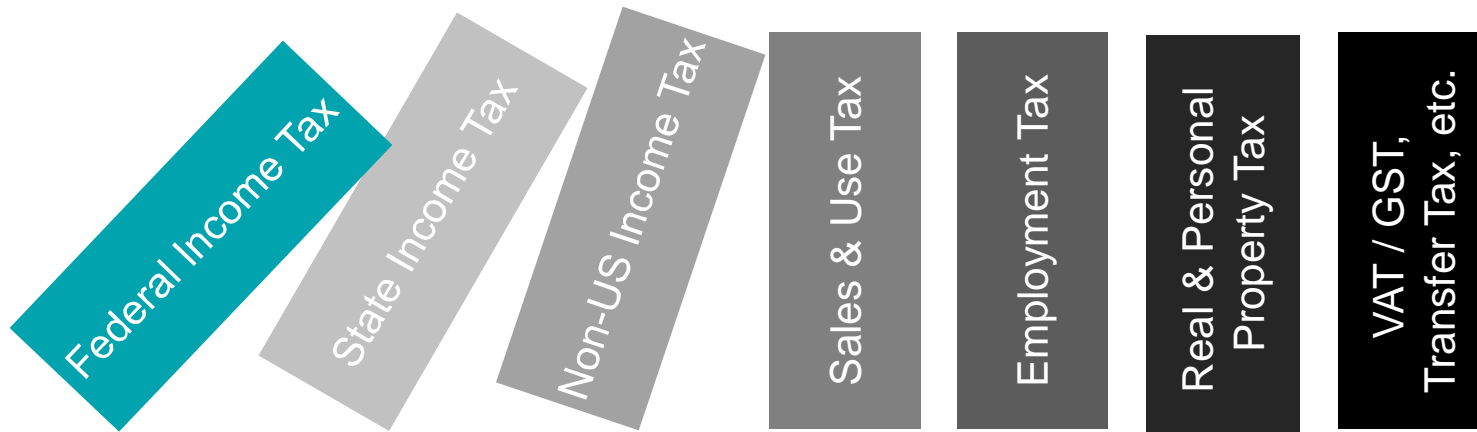
Why tax matters in M&A transactions

- ▶ Taxes are one of the largest cash costs of a business 
 - ▶ Corporate: 21% US federal income tax plus state tax
 - ▶ Pass-through entities: based on partners' individual income tax rates (e.g., could be up to ~54% federal & state for certain high-net worth individuals)
- ▶ Significant risk item and value driver in a transaction:

Past	Present	Future
<ul style="list-style-type: none">▶ Due diligence to identify and quantify potential material tax exposures that may still be relevant to buyer post-close	<ul style="list-style-type: none">▶ Structuring to implement tax-efficient combined legal entity structure, integrate IP, supply chain planning	<ul style="list-style-type: none">▶ Model cash tax requirements post-close, availability of NOLs, and toll charges on moving assets or legal entities

- ▶ Taxes that a Seller will pay can have a significant impact on whether seller wants to sell stock or assets.

Tax due diligence objectives



Purpose of tax due diligence is to:

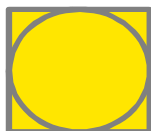
- Understand and quantify the risk of any potential material historical tax issues that may be inherited by a Buyer.
- Protect the Buyer through contracted indemnification or a deal price adjustment based on findings of tax due diligence.
- Gain an understanding of Target tax profile and past tax exam activity (whether pending, current, or closed) to enable more efficient integration into Acquirer's business and tax reporting/accounting functions effectively post-close.

Level of tax due diligence is determined by



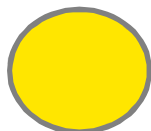
▶ Target's legal entity structure

- ▶ Is the Target a corporation or flow-through partnership, S corp? (i.e., taxable acquisition stock or assets?)
- ▶ Is this a carve-out, and will any legal liability carry over post-close?
- ▶ How complex of legal entity organizational chart, number of entities?

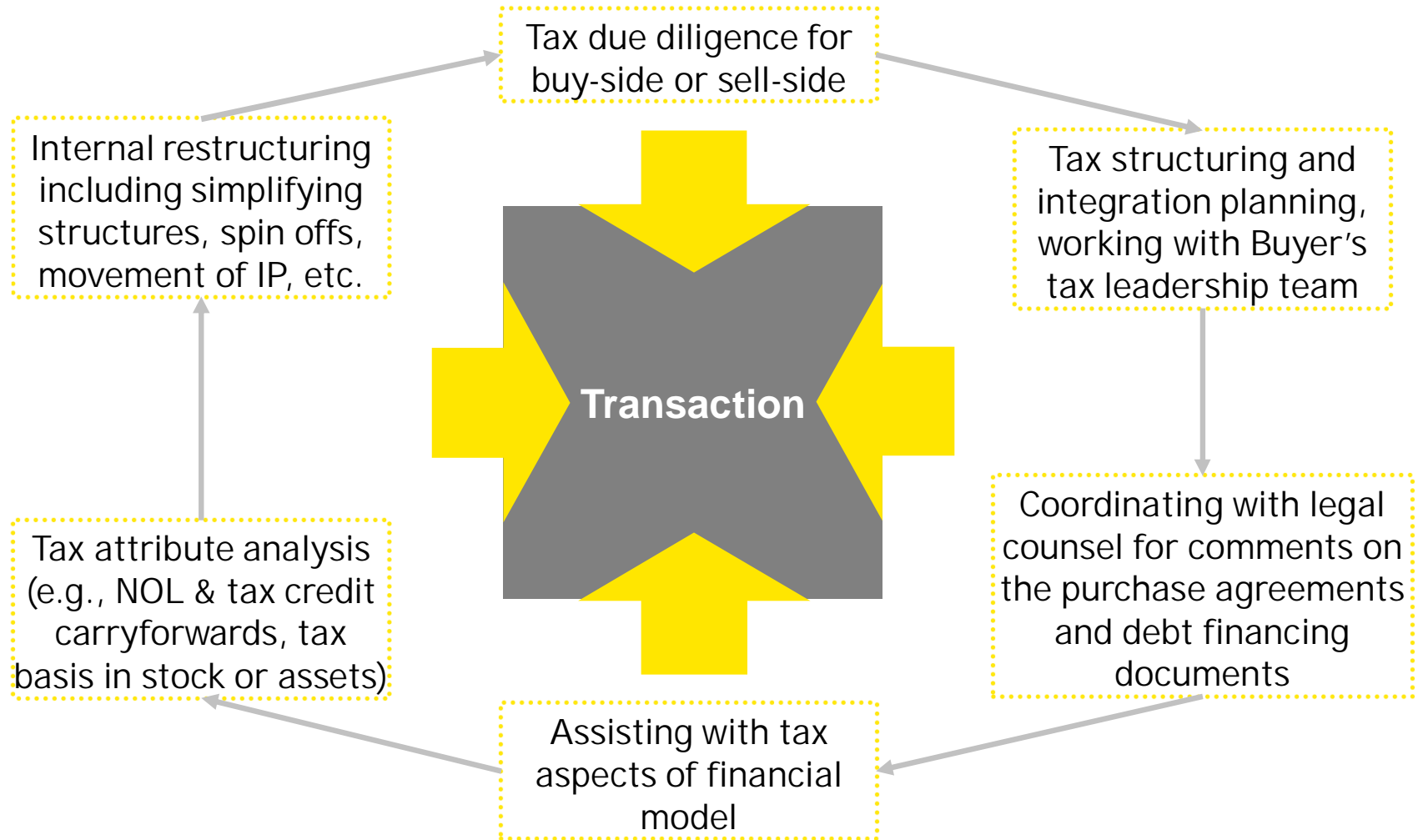


▶ Target's tax profile

- ▶ Tax audit history, reserves, and Uncertain Tax Positions
- ▶ Location of operations, IP, transfer pricing, and does it include significant offshore activities?
- ▶ Reorganization / acquisition history and whether sufficient planning / due diligence was performed and external advice was given
- ▶ Tax attributes – expiration and limitations on use

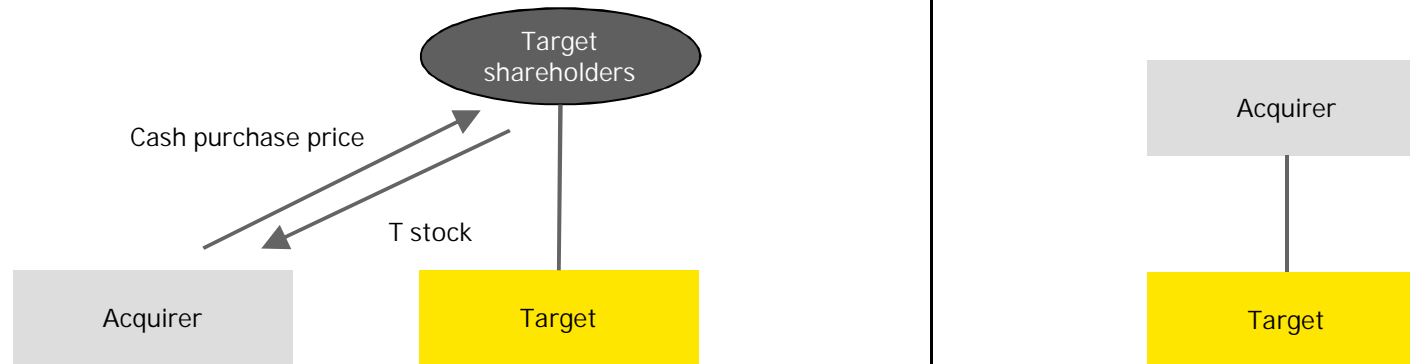


Tax focus areas in a transaction



Basic taxable acquisition structures

Taxable stock purchase

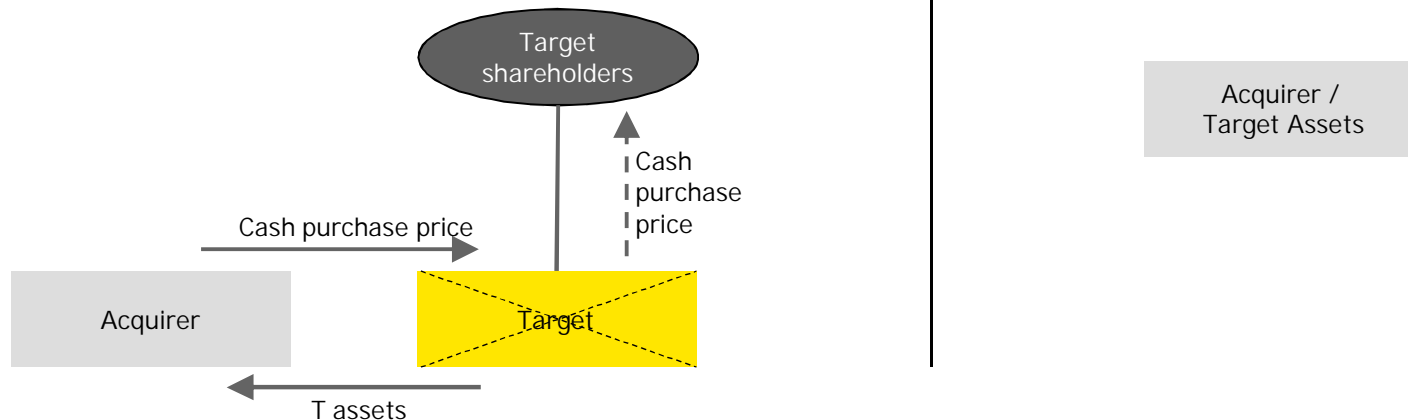


Considerations

- Cost basis in purchased stock, but generally no step-up in assets
 - Contrast to GAAP step-up in target's assets under purchase accounting
- Carryover of NOLs, but use of NOLs may be limited going forward
- Buyer inherits historical tax liabilities of target (whether disclosed, undisclosed, or contingent)
- Sellers pay tax based on their gain in their stock (i.e., purchase price minus tax basis)

Basic taxable acquisition structures

Taxable asset purchase

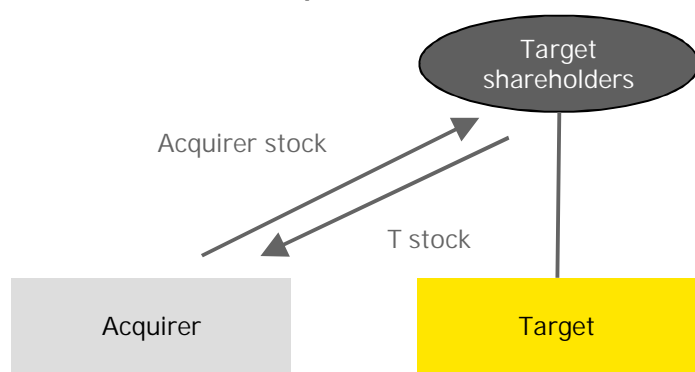


Considerations

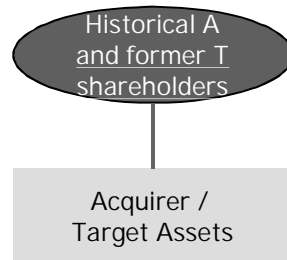
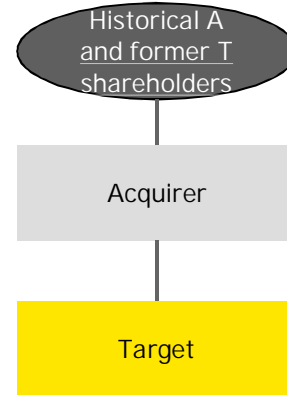
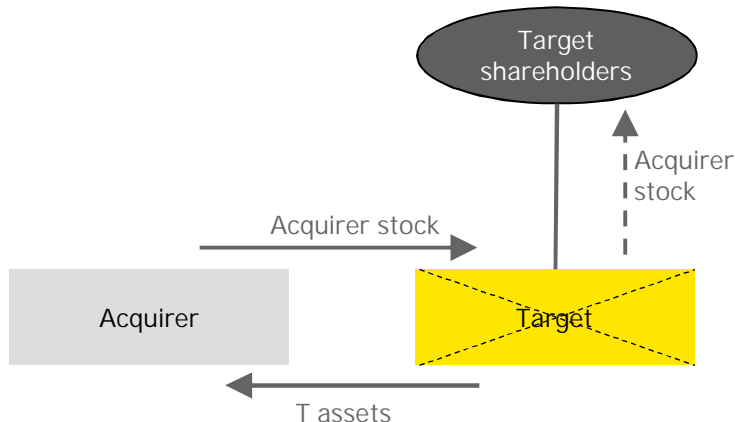
- Double taxation (corporate and shareholder level) often makes a sale of all assets cost prohibitive for a Seller
 - Target pays tax on asset sale gain (21% US federal income tax plus state income tax)
 - Seller receives cash in liquidation of target and has additional capital gain (20% US federal income tax plus state income tax)
- Buyer may get step-up in assets' tax basis (often a real value driver)
- No carryover of NOL or tax credit carryforwards

Basic non-taxable acquisition structure

Non-taxable stock purchase



Non-taxable asset purchase



Why are these transactions tax deferred?

After the reorganization, Target shareholders maintain a direct or indirect interest in Target's business (e.g., through ownership of Acquirer stock).

Deferral is achieved through:

- Substituted basis rule for Acquirer stock received in the exchange
- Carryover basis rule for property received (i.e., no step-up in basis of Target assets). Generally, in order to get a "step-up" in basis, gain must be recognized on the transaction.

Tax attributes (NOLs) and income events

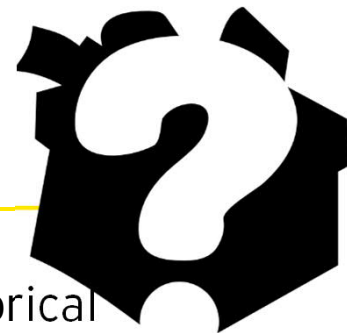
- ▶ Corporations that spend significantly on R&D over years often generate tax attributes (e.g., NOL, R&D credit, orphan drug credit, foreign tax credit and capital loss carryforwards) and may have a significant amounts pre-acquisition.
- ▶ These “tax attributes” allow for a future benefit to the taxpayer to offset against taxable income.
 - ▶ NOL limitations for post-2017 losses. For NOLs generated after tax years beginning after December 31, 2017, NOLs in the amount of 80% of the taxable income may be utilized. The NOL may be carried forward indefinitely, but not carried back.
 - ▶ However, note that the CARES Act made changes to the NOL provisions including: (1) changing the carryback period to five years for any NOLs arising in 2018, 2019, or 2020; (2) temporarily removed the 80% limitation on the use of NOLs; and (3) pass-through business owners may use NOLs to offset their non-business income above the previous limit of \$250,000 (single) or \$500,000 (married, filing jointly) for 2018, 2019, and 2020.
 - ▶ NOL limitations for pre-2018 losses. For NOLs generated prior to tax years beginning prior to December 31, 2017, NOLs are not limited by a percentage of taxable income. The NOL may be carried back 2 years, but carried forward only 20 years.
- ▶ Examples of income events that may create a need to use NOLs

Collaboration upfront payments	• Received upon signing of the collaboration agreement or closing of sale of an asset
Milestones	• Contingent on research or commercialization achieving certain goals
Royalties	• Due based on future monetization or use of certain assets.

Section 382 limitations and impact on value

- ▶ “Section 382 limitations” arise when a company with NOLs experiences an “ownership change,” defined per tax rules as a greater-than-50% cumulative owner shift, in terms of value, over a rolling three-year period.
 - ▶ Limitations may be restrictive such that some NOLs/credits may expire unutilized
 - ▶ It may be that these tax attributes are available over time, subject to an annual Section 382 limitation, which may mismatch with significant income events from collaborative arrangements.
- ▶ Annual limit based on FMV of equity multiplied by a ~2-4% monthly AFR.
 - ▶ Reduction for debt-funding of transaction if debt is placed on books of Target or serviced by Target operations.
 - ▶ Potential increase for certain built-in gains at the time of the ownership change
- ▶ In general, a buyer should assume \$0 value for the tax attributes of Target unless Target can prove that such tax attributes have value
 - ▶ **A Section 382 analysis or study on the other hand might support significant potential NOL/cost savings available to a potential Buyer.**

Due diligence questions around NOLs



- ▶ First question to ask is whether Target has undergone any historical ownership changes (which place Section 382 limitations on the availability to use such attributes).
 - ▶ Have they ever prepared an owner shift calculation?
 - ▶ Is the information available to prepare an owner shift calculation?
- ▶ If there have been historical ownership changes, which tax attributes are limited and to what extent?
- ▶ What will the base limitation be in the current transaction?
- ▶ Additionally, consider if the tax attributes are valid in the first place
 - ▶ Were NOLs generated by valid deductions, or were any such deductions improperly taken (e.g., disallowance of interest expense, non-deductible transaction costs, etc.)?
 - ▶ Have they undertaken a detailed R&D tax credit study to justify the validity of tax credits?

Example: If \$300M of NOLs were limited by a \$40M annual Section 382 limitation

- ▶ The Company would have cash taxes due in Years 2 and 3 because the Target may have more taxable income than available Section 382 limitation.
- ▶ Target can only use \$60M in Year 2 (e.g., \$40M annual limitation plus \$20M unused excess limitation from Year 1) and \$40M in Year 3 (e.g., \$40M of limitation that became available in Year 3).

Cash tax calculation (assuming no restrictions on NOLs)						
	2019	2020	2021	2022	2023	Total
US cash taxes						
US taxable income	25	100	75	20	100	320
NOL utilization	(20)	(80)	(60)	(16)	(80)	(256)
US taxable income after NOL	5	20	15	4	20	64
Tax rate	26%					
US cash taxes	1.3	5.2	3.9	1.04	5.2	16.64

Cash tax calculation (assuming NOLs restricted to 40M annually)						
	2019	2020	2021	2022	2023	Total
US cash taxes						
US taxable income	25	100	75	20	100	320
NOL utilization	(20)	(60)	(40)	(16)	(64)	(200)
US taxable income after NOL	5	40	35	4	36	120
Tax rate	26%					
US cash taxes	1.3	10.4	9.1	1.04	9.36	31.2

Interest deductibility limitations

- ▶ Applicable high yield discount obligation (“AHYDO”) –
 - ▶ Defers tax deductions for original issue discount (“OID”), including payment in kind (“PIK”) interest, until interest is actually paid in cash if the yield-to-maturity (“YTM”) of the debenture exceeds the applicable federal rate (“AFR”) + 5%
 - ▶ Permanently disallows OID deductions to the extent YTM exceeds the AFR + 6%
 - ▶ Planning surrounding terms may help avoid limitation (i.e., bullet payment of interest in year five)
- ▶ Corporate acquisition indebtedness rules – § 279
 - ▶ Disallows interest deduction for the lesser of:
 - ▶ Total acquisition interest greater than \$5M in such year, or
 - ▶ Interest for such year on tainted acquisition debt
 - ▶ Test is applied cumulatively to multiple acquisitions
- ▶ Disqualified interest rules – § 163(j)
 - ▶ For tax years ended prior to December 31, 2017, § 163(j) may disallow interest expense based on debt/equity ratio (1.5:1) of corporation
 - ▶ Generally applies on interest paid to or guaranteed by certain related parties (tax-exempts, or foreign)
 - ▶ For tax years beginning on or after January 1, 2018, § 163(j) limits the interest expense deduction to 30% of adjusted taxable income (i.e., the taxable income computed without regard to any NOL deduction, any item of gain, income, deduction or loss which is not properly allocable to a trade or business, etc.).
 - ▶ Note that the CARES Act increased the limitation from 30% to 50%. However, the change is limited to the 2019 and 2020 tax years.
 - ▶ For tax years beginning on or after January 1, 2022, § 163(j) limits the interest expense deduction to 30% of adjusted taxable income (in addition to the above, adjusted taxable income is computed without regard to any deduction allowable for depreciation, amortization and depletion).

Flow-through deduction generally not available for the Medical Practice

- ▶ As a result of tax reform, Congress provided a tax benefit to individuals with qualified business income from a partnership, limited liability company, S corporation or a sole proprietorship. Section 199A provides a deduction of up to 20% of the US federal taxable income of a domestic business operated in flow-through form.
- ▶ The amount determined to be deductible is based on the qualified business income from a qualified trade or business.
 - ▶ Qualified trade or business does not include a trade or business that involves the performance of services in the health fields.

Carried Interest

- ▶ As a result of tax reform, certain partnership interests held by the taxpayer or a related person in connection with the performance of services (i.e., carried interest) is subject to a three year holding period to obtain long term capital gain treatment.
- ▶ Limited exceptions –
 - ▶ An applicable partnership interest does not include a partnership interest held by a corporation.
 - ▶ An applicable partnership interest does not include a capital interest that provides the partner with a right to share in partnership capital commensurate with: (1) the amount of capital contributed (determined at the time of receipt of the partnership interest); or (2) the value of the interest included in income under section 83 upon receipt or vesting.

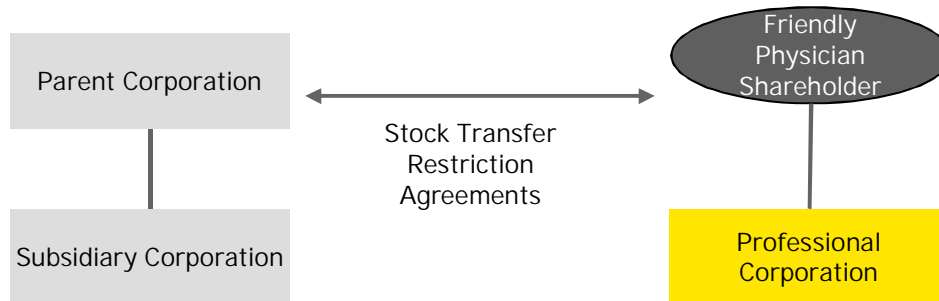
CARES Act Considerations

- ▶ Paycheck Protection Program (“PPP”) Loans
 - ▶ Eligibility for a PPP Loan generally depends on the number of employees. Post-acquisition, Targets should generally not be eligible because the employee numbers are aggregated across the portfolio companies.
 - ▶ Generally, the CARES Act excludes PPP Loan forgiveness from income; however, the IRS disallows any otherwise available deductions to the extent the cost was reimbursed by a PPP Loan amount that was forgiven. For example, to the extent wages are funded by a PPP Loan, the wage expenses (normally deductible) are a disallowed deduction
- ▶ Payroll deferral or employee retention credit are also available. Generally, if a Target uses an employee retention credit, then they are ineligible for a PPP Loan.
 - ▶ Payroll deferral is available so the employer share of Social Security tax on wages paid from March 27, 2020, through Dec. 31, 2020, is deferred, with 50% due at the end of 2021, and 50% due at the end of 2022. A similar rule applies to 50% of self-employment tax liability of partners and sole proprietors.
 - ▶ Employee retention credit is a refundable payroll tax credit equal to 50% of qualified wages (wages, including qualified health plan expenses allocable to the wages) paid by eligible employers from March 13, 2020, to Dec. 31, 2020.
- ▶ Currently, we recommend asset deals to cleanse the taint of Target's historical PPP Loans.

US international income tax considerations

- ▶ Passive foreign investment company (“PFIC”) Rules
 - ▶ Anti-deferral Rules – result in immediate taxation to US taxable investors or interest charge on deferred tax on PFIC income
 - ▶ PFIC is any foreign corporation if either:
 - ▶ Passive income is 75% or more of total
 - ▶ Passive assets are 50% or more of total
- ▶ Subpart F Income
 - ▶ Anti-deferral provisions – result in immediate taxation to US taxable investors on certain types of income of a controlled foreign corporation (“CFC”), including:
 - ▶ Investment Income
 - ▶ Foreign base company sales, service, and oil-related income
 - ▶ Investment in US property
 - ▶ Certain exceptions may apply (e.g., same country activity, manufacturing)
 - ▶ CFC includes: any foreign corporation that is more than 50% owned by US shareholders (vote or value test, does not have to be direct ownership – indirect and constructive ownership taken into account)
- ▶ Global intangible low-taxed income (“GILTI”)
 - ▶ Newly enacted anti-deferral provisions – causes the US Shareholder to include its proportionate share of any income earned by various non-US subsidiaries (i.e., CFCs) that earn a return in excess of a return on capital invested in tangible assets of 10% of such tangible investment.
 - ▶ GILTI will apply to most multinational companies where there is significant value and earnings in CFCs attributable to intangible assets.
 - ▶ A US shareholder that is a corporate entity is generally entitled to a deduction of 50% of the GILTI inclusion (the deduction goes down to 37.5% in tax years beginning after December 31, 2025)

Consolidation in the Medical Practice



- ▶ The Professional Corporation may be permitted to join in the filing of the Parent Corporation's consolidated US federal income tax return
 - ▶ Generally, under applicable state law, the stock of the professional corporation must be owned by a licensed physician. The Friendly Physician Shareholder ("Shareholder") and Parent Corporation have entered into a Directors Agreement and Stock Transfer Agreement (PLR 2014-51009).
 - ▶ The Shareholder is named Director of the Professional Corporation, but the Directors Agreement can be terminated at any time by Parent Corporation.
 - ▶ The Stock Transfer Agreement prohibits Shareholder from transferring or disposing of the stock of Professional Corporation or paying a dividend or consenting to the liquidation of Professional Corporation. Parent Corporation can terminate the agreement and liquidate Professional Corporation.

Common tax modeling misconceptions to watch out for in estimating after-tax cash flow:

Tax should equal book...

Interest is always deductible...

Cash can be moved around from country to country or entity to entity tax-free...

I can use NOLs, to offset EBT, no problem...

Transaction costs can all be expensed...

2020 Election – Key tax considerations

- ▶ A change of administration could have significant impact on future taxes and tax planning
 - ▶ Democratic presidential candidate Joe Biden pledged to raise the tax rate that corporations pay on “day one” of his presidency, regardless of the nation’s unemployment rate.
 - ▶ Proposals also include items such as:
 - ▶ Increasing the tax rate on income earned by non-US subsidiaries.
 - ▶ “Repealing” the Trump tax cuts in some form.
 - ▶ Raising individual income taxes, on high-income individuals with income above \$400,000 from 37% to 39.6%.
 - ▶ Adding social security payroll tax on income earned above \$400,000 (current phase out is at \$137,700).
 - ▶ Taxing long-term capital gains at the ordinary income rate (i.e., 39.6%) on income over \$1 million.
- ▶ More tax news to come!

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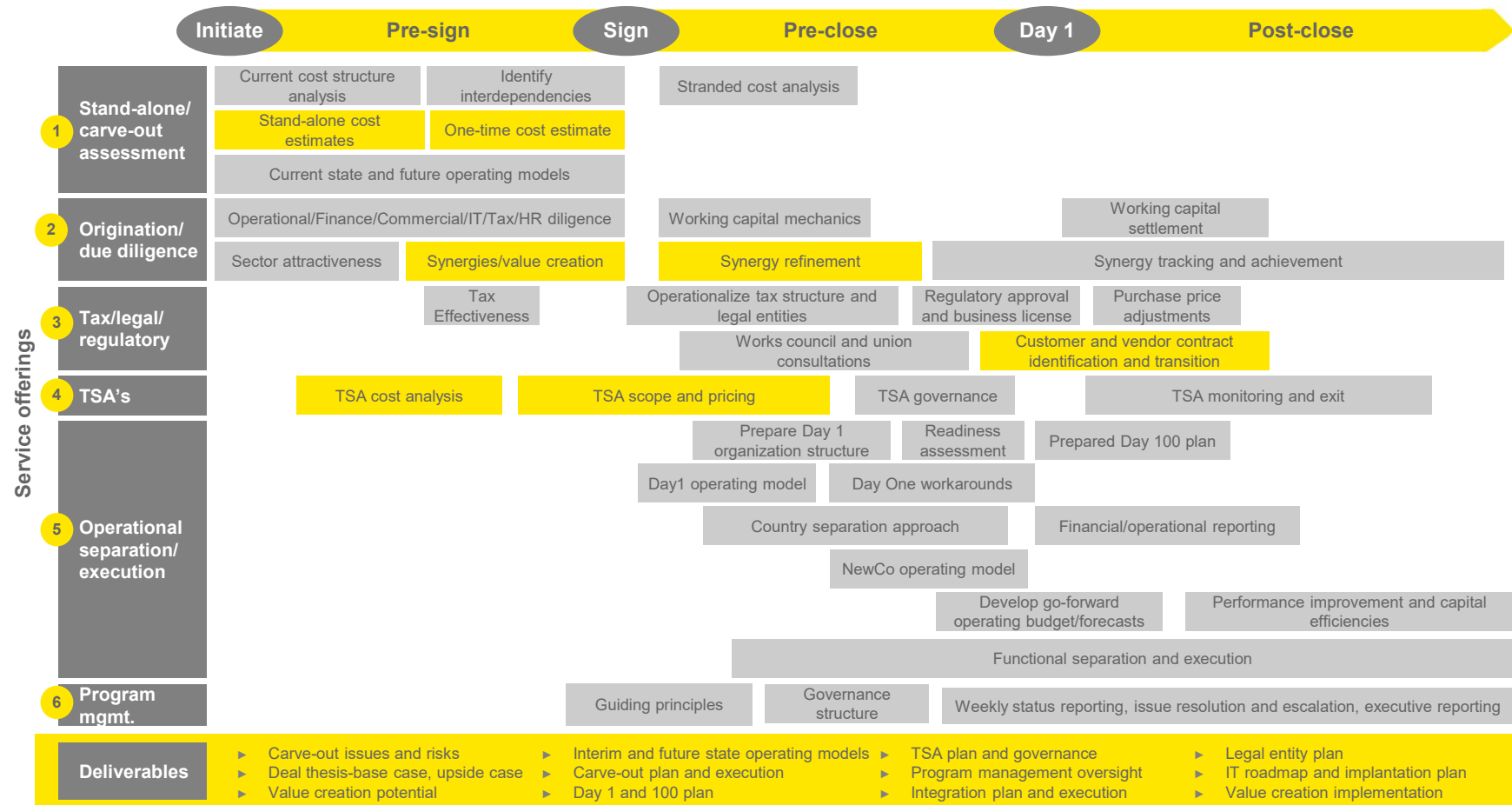
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Deal Consideration -- Integration

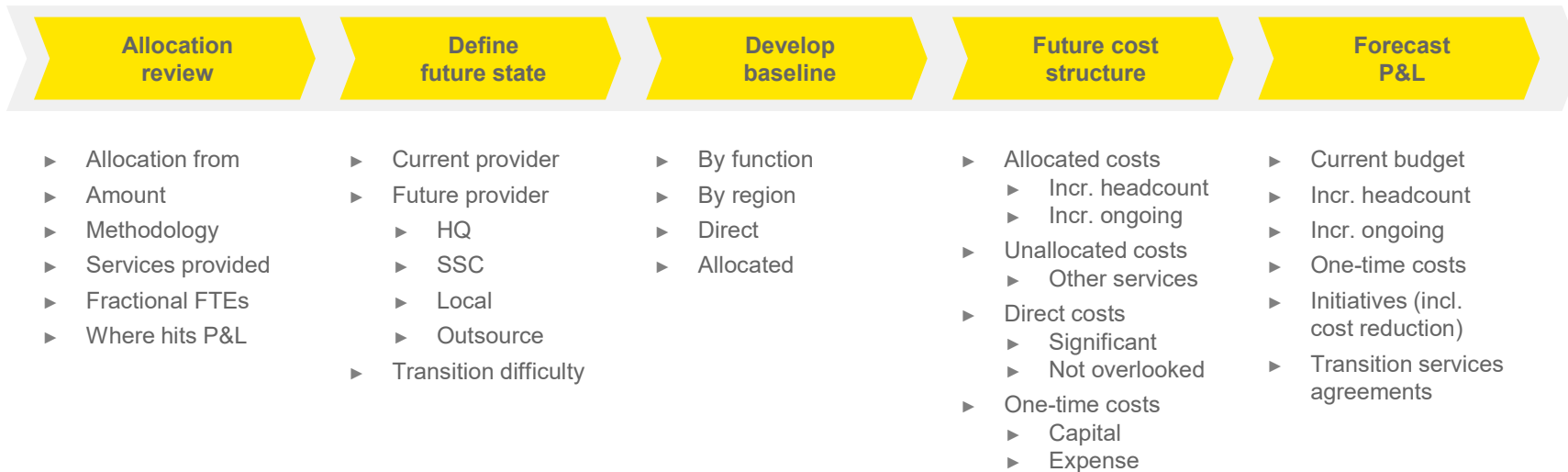


A deal lifecycle proceeds in three phases – key activities need to be performed along each – we will discuss just a few today



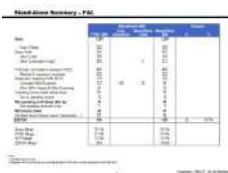
1 Stand Alone Cost Assessment helps define what the cost structure of the entity being purchased would be in your environment

Standalone costing methodology



Example output:

P&L



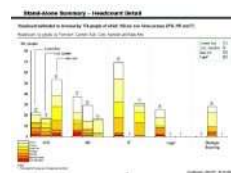
EBITDA impact



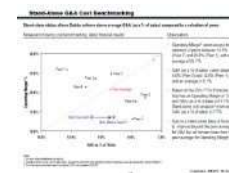
G&A On-going and headcount



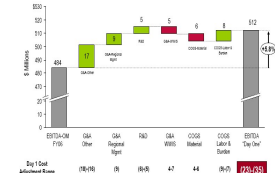
Headcount detail



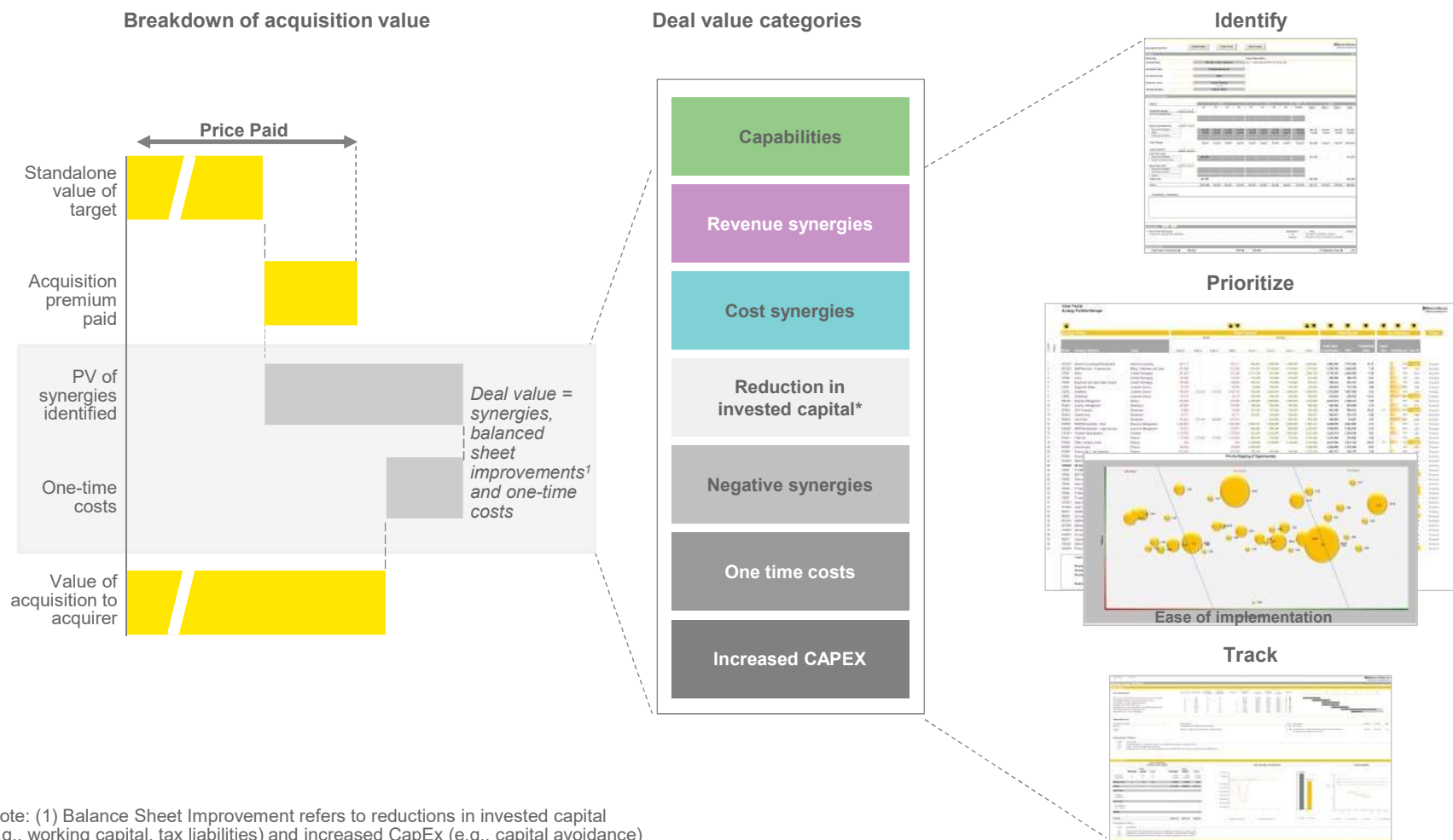
G&A cost benchmark



Stand-alone cost model



2 Synergy identification and capture helps capture the value of the transaction



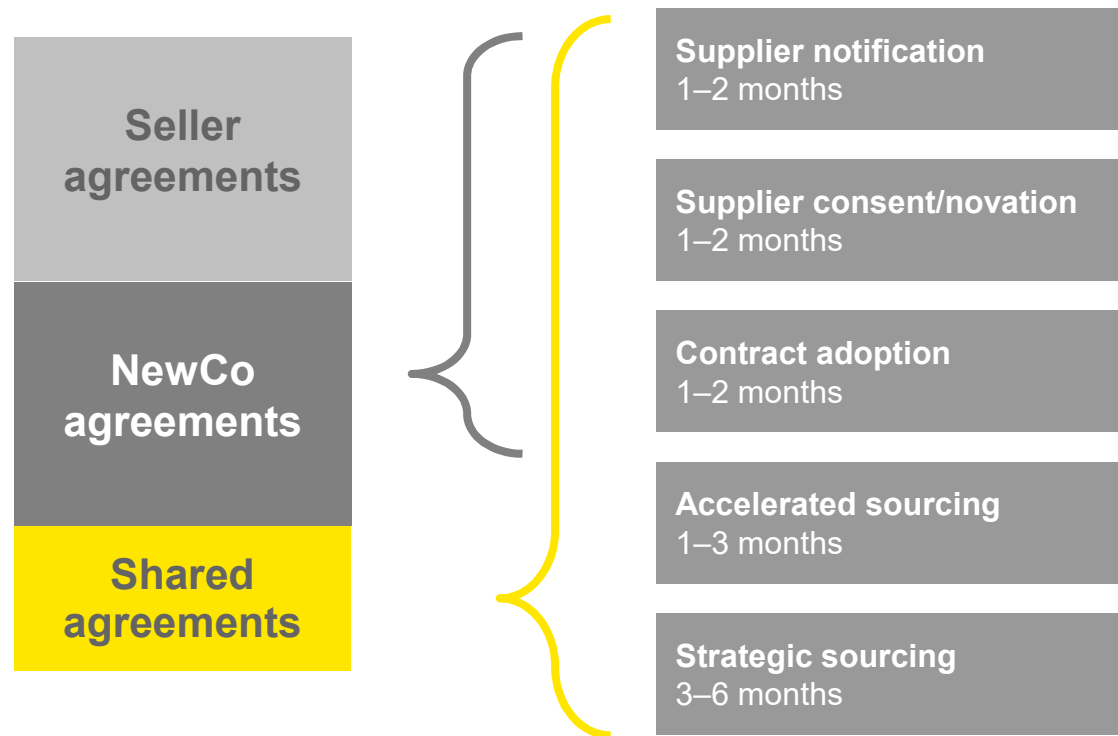
2

Synergies can be both Revenue and Cost

Illustration of Synergy levers for a Provider Practice Acquisition

Revenue Opportunities	Volume	<ul style="list-style-type: none"> Improve referral conversion rate and patient experience Expand referral network Improve IOL upsell conversion 	
	Capacity	<ul style="list-style-type: none"> Optimize capacity across geographies 	
	RCM	<ul style="list-style-type: none"> Optimize revenue cycle management (rates, collections) 	
Cost Opportunities		Admin	Clinical
	Operating Model	<ul style="list-style-type: none"> Rationalized org Standard admin model 	<ul style="list-style-type: none"> Standardized staffing model Clinical/Data governance
	Best Practice Propagation	<ul style="list-style-type: none"> Productivity Automation/IT Regulatory compliance 	<ul style="list-style-type: none"> Utilization/Scheduling Quality best practices
	Scalability	<ul style="list-style-type: none"> Indirect procurement Shared Services 	<ul style="list-style-type: none"> Medical supplies contracts

3 Contractual separation of shared agreements can create significant lead time and also can have synergy impacts



Considerations

- ▶ The time required to develop and implement a transition strategy for contracts is often underestimated
- ▶ A communication plan for vendors and customers should be developed as part of the strategy
- ▶ The potential actions required on a contract vary from notification or assignment to complete renegotiation to temporary coverage under a TSA
- ▶ A strategy to address potential loss of leverage due to changes in the contract's scope and/or volume should be developed

4 Transition Services Agreements (TSAs) are essential to ensure that the operations continue post-close

	Assessment	TSA gap closure	TSA day 1 readiness
Objective	<ul style="list-style-type: none"> ▶ Identify capability gaps in the TSA portfolio presented by PARENT ▶ Understand the scope and detail of carve out (separation assessment) 	<ul style="list-style-type: none"> ▶ Develop TSAs requirements to close identified gaps in the TSAs presented by PARENT 	<ul style="list-style-type: none"> ▶ Prepare for Day 1 TSA Readiness ▶ Advise on TSA considerations and preliminary TSA exit plans, one-time TSA costs and business risks
Project work	<ul style="list-style-type: none"> ▶ Understand the scope and detail of the TSAs presented by PARENT ▶ Assess the structure and progress of the CLIENT TSA gap identification effort in progress ▶ Analyze adequacy of TSA coverage across all functions and countries ▶ Conduct high level assessment of TSA costing/pricing methodology 	<ul style="list-style-type: none"> ▶ Plan and facilitate confirmation workshops ▶ Develop gap closing TSAs to ensure coverage across all functions and countries <ul style="list-style-type: none"> ▶ Aligned with people, processes, systems and assets ▶ Identify gaps after mapping out key end-to-end processes (order-to-cash) ▶ Identify areas where CLIENT will have to build capabilities before Day One (not covered by TSA and critical for Day One operations) 	<ul style="list-style-type: none"> ▶ Work in conjunction with the integration team focusing on TSA Day 1 Readiness ▶ Advise on TSA considerations, and requirements such as: <ul style="list-style-type: none"> ▶ Pricing/costs vs. "market rates" or typical costs we see on similar transactions, compared with what's in the allocations ▶ One off items, duration vs. typical exit plans ▶ PARENT service levels vs. CLIENT's expectations ▶ Alignment with CLIENT tax structure
Deliverables	<ul style="list-style-type: none"> ▶ High level assessment of TSA scope, costing and pricing ▶ TSA Gap Analysis 	<ul style="list-style-type: none"> ▶ Confirmation workshops ▶ Gap closing TSAs 	<ul style="list-style-type: none"> ▶ TSA Day 1 Readiness Sessions ▶ TSA Day 1 Readiness Checklist ▶ Recommendations on TSA considerations

This image shows a single sheet of white paper with horizontal ruling lines. The lines are evenly spaced and run across the width of the page. There are no margins, text, or other markings on the paper.



