WHITE PAPER

MSOs: What You Need to Know

Are you considering partnering with a Management Services Organization (MSO) vice, merging your practice with another, or selling to a hospital? Recently, more private practice physicians approach us about “selling” to private equity or “joining” an MSO. There is often confusion about how these two are related and what it means to join a MSO. The structures of MSOs vary greatly, as well as the management services they offer; laws that vary by state may further complicate the design structure.

This article will attempt to give a high-level overview of two common structures: a MSO that takes ownership (partial or full) of a medical practice, and a MSO that provides business services without taking any ownership.

The Acquisition

For starters, most MSOs are very particular about the practices they purchase. Aside from being specialty-specific, they have specific parameters when it comes to size, revenues, location, number of offices, and so forth. If your practice meets what they are looking for, you may be in a position to entertain offers from an MSO as well as independent buyers (i.e. other practices or hospitals). You can expect a sale to an MSO to be different from a traditional sale in these main areas: time frame, due diligence, financing (or payment of the purchase price), and transition structure.

Established MSOs will have a team of individuals dedicated to acquiring practices. Their primary job will be to dissect all of your practice data to determine if your practice represents a sound investment for them. This process is often very time consuming and demanding on the seller and his or her advisors (consultant, attorney, and accountant).

In a traditional sale, it is common for the seller to be completely cashed out for the purchase price at closing. A full cash payment is less common in an MSO acquisition. Often, the MSO will make a portion of the purchase price contingent on either the seller staying on as a practicing physician in the practice for a period of time after the sale (an earn-out), or on the performance of the practice for a period of time after the sale (a performance-based buyout). If so, it would be prudent for you to learn as much as possible about the company, its principals, its private equity investors, history, performance, etc. You should also speak with current and former selling physicians.

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In most MSO acquisitions, the MSO will require the seller to stay on and work at the practice for two to three years or longer. These work-back requirements may be tied to a purchase price payout or cash penalty if the seller exits early.

Post-Sale Working Arrangement

One of the first things you should consider is: do you want to keep working after the sale? If so, for how long? Another consideration of selling to an MSO vs a hospital or merger with another practice is: how well you deal with loss of control? Some of these transactions may convert you to an employee, not an owner, may set your work hours and vacation schedule, and may decide who will be on your staff. You may be required to change referral patterns or change a number of outside vendors. For some physicians this does not matter. For others it will cause endless aggravation. Before you sell to a MSO, find out what will change, and do some honest self–reflection.

Risk Assessment

Finally, assess your risk tolerance and when you need the money from the sale of your practice. MSO deals are often different. Find out how much will be paid at closing, how much will be held in escrow, and how much may be held back pursuant to some future earn-out. There is also another consideration for those MSOs that do have a hold back of some of the purchase price, which is paid later pursuant to a non-guaranteed earn-out that pays you a percentage of future profits or revenue. If revenue drops, earn-out drops and you may not receive your full anticipated sale price. If you are risk-averse, then that particular MSO may not be right for you.

If you are considering a sale of your practice to a MSO, consider the requirements they make of you as terms of the sale, make sure the numbers add up, do your due diligence on the MSO, measure your expectations and values against what they have to offer, and finally, seek professional advice.

Another Type of MSO

And then there is the other type of MSO which may provide business services without taking ownership in your practice. In this type of relationship, you would enter into a long-term contract with the MSO without giving up any ownership. Your practice would receive similar management benefits, but you would not receive any cash payments in lieu of shares in your practice. Consequently, while this arrangement can deliver outstanding assistance to your practice (depending, of course, on how the MSO is structured) it is in no way a form of succession planning nor an exit strategy because you are not taking on an ownership partner.

Nonetheless, these arrangements can help your practice run better and thus be more appealing to physicians looking to join your practice. Furthermore, without giving up any ownership stake, it allows for partnership paths for physician employees. One of the downsides to the other types of MSOs is that their buy-in at a certain point in time may prohibit or limit those physician employees who were on a path to partnership and partners who may not have yet become owners.

Consideration of a MSO (either partnering with or selling to) is certainly nothing that should be taken lightly. When you begin contemplating this initiative, it is highly advisable to contact a consultant who has a lot of experience working with MSOs as that individual will be able to answer your questions as to the pros and cons and help you weigh whether or not this endeavor is a good fit for your practice.

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