

Questions or Assistance?

If you have further questions about the Medical Foundations Act, please feel free to contact one of the following members of our Health Law Practice Group.

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Recent Law Establishes Medical Foundation Option for Hospitals and Health Systems

I. The Act.

Connecticut Public Act Number 09-212, An Act Concerning Medical Foundations and Medical Group Clinic Corporations (the "Act"), was signed into law by Governor Rell on July 8, 2009. The Act permits a hospital or health care system to organize and become a member of a medical foundation for the purpose of providing professional medical, chiropractic, or podiatric services. While the captive or "friendly private practice" models are still available to hospitals, the medical foundation model now offers hospitals a choice for operating professional practices with greater control and flexibility. The Act became effective July 1, 2009.

II. Organizing a Medical Foundation.

A medical foundation must be organized as a not-for-profit nonstock corporation and may operate at any location(s) its members designate. The foundation's name must include the word "corporation" or the abbreviations "Inc." or "Corp." and must contain either a word or words descriptive of the professional service to be provided.

III. Role of the Office of Health Care Access.

While a medical foundation is not subject to the CON laws, the Act does provide that:

- A medical foundation organized on or after July 1, 2009 must file its certificate of incorporation and amendments, if any, with OHCA within 10 business days after it files them with the Secretary of State;
- Upon written request of OHCA, the medical foundation must, within 10 business days,

provide a statement of its mission, a description of the services it provides, and a description of any significant change in its services during the preceding year, as reported on the foundation's IRS Form 990; and

- Upon a vote by the medical foundation's board or members to liquidate, terminate, cease operations, or dissolve, the medical foundation must file notice with OHCA.

IV. Converting to a Medical Foundation.

A medical group clinic in existence on September 30, 1995, and continuing to operate as such until July 1, 2009, must convert to a medical foundation by July 10, 2010 in order to remain duly organized. A medical group clinic is typically a for-profit, non-stock corporation formed by three or more physicians to study, diagnose, and treat illnesses and injuries and to promote medical, surgical, and scientific research and learning. The act permitting formation of such entities was repealed in 1995.

Other health care corporations may, but are not required to, convert to a medical foundation. The procedure for conversion is as follows:

- The corporation must amend its certificate of incorporation to be consistent with the Act; and
- The corporation must affirmatively state in the amended certificate that its members or shareholders have elected to bring the corporation within the Act's provisions. To the extent that such corporation has



a current provider agreement with the Department of Social Services, the provider agreement will remain in effect regardless of the conversion.

V. Powers, Limitation, and Governance of Medical Foundations.

A medical foundation is governed pursuant to the Connecticut nonstock corporations law. However, the Act provides additional governance rules for medical foundations, as follows:

- The foundation must be governed by a board of directors consisting of an equal or greater number of providers than non-provider member employees, in addition to any other directors elected by the members;
- The foundation may merge with another medical foundation, professional corporation, LLC, or limited liability partnership only if the other entity provides the same specific professional services as the foundation; and
- The foundation may not engage in any business other than the provision of health care services.

VI. Federal Tax Exemption.

In order to qualify for exemption from federal income taxation under §§ 501(a) and 501(c)(3) of the Internal Revenue Code of 1986, as amended, a medical foundation must be organized and operated exclusively for charitable purposes. Because there is no precedent regarding the application of § 501(c)(3) to a medical foundation, the medical foundation will need to rely upon earlier published guidance that recognizes that a captive or friendly private physician practice that is part of an integrated delivery system may qualify as a tax-exempt organization.

This guidance suggests that a medical foundation may obtain exemption from federal income taxation if, among other things:

- The medical foundation is organized and operated exclusively for charitable purposes within the meaning of § 501(c)(3);
- The medical foundation's organizational documents and physician employment agreements are consistent with its charitable endeavors. Internal IRS memoranda suggest the IRS will closely scrutinize the language of these documents;
- A community board of directors exercises control over the entity's activities; and
- The medical foundation demonstrates that it promotes health in a manner that benefits the community, for example, through the implementation of its own charity care policy and/or through such activities as medical education, training or research.

VII. Transfer of Assets.

Taxpayers must take care in how they structure transactions involving the liquidation of a taxable private practice and the transfer of assets to minimize the recognition of taxable gain. It may be prudent, therefore, for taxpayers, to obtain independent appraisals using approved IRS valuation methods. Given the recent passage of the Act, we encourage taxpayers to seek counsel from their tax advisors in order to best take advantage of the business opportunities involved in organizing a new medical foundation under the Act.

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