SEYFARTH SHAW

Senior Living and Long-Term Care Blog

Perspectives on the legal trends, regulatory policy and other issues facing the senior living and long-term care industry

Three Important Considerations when Purchasing a Property Improved with a Skilled Nursing Facility

By Cynthia J. Mitchell and Elizabeth H. Dahill

The acquisition of a property improved with a long-term care facility, in particular a skilled nursing facility ("SNF"), presents certain unique issues for a potential purchaser, which should be addressed early on in the closing process. In addition to traditional legal and financial due diligence considerations involved in a traditional real estate acquisition, a purchaser should also consider the feasibility of the property from a health care perspective. This includes local regulatory and licensure requirements and, potentially, additional financing considerations. While there are many different factors and variables that are specific to every new deal, below are three considerations that any potential purchaser should address with counsel when considering the purchase of a SNF property.

1. Use Restrictions

In reviewing the due diligence materials provided in connection with the acquisition, the purchaser should take special care to spot any potential use restrictions that would prohibit operating the property as a SNF, and/or any customary related uses (e.g., beauty salons, therapy gyms located in the facility). In addition to use restrictions against services, there are real property restrictions that are quite often an issue. An example of this is parking. Depending on the jurisdiction, the way the number of required parking spots is calculated will vary. For instance, in some locales, the required number is calculated by taking into consideration the number of patient beds and the number of employees at the busiest shift. Use restrictions can appear in the title exception documents (including, without limitation, declarations, easements and/or covenants, conditions and restrictions agreements), deed restrictions set forth in prior vesting deeds, use restrictions in the purchase contract and/or local law or municipal ordinance restrictions identified in the zoning report. Each of these documents should be carefully reviewed by counsel to confirm that the purchaser can legally operate the property in accordance with the client's intended use. If use restrictions are recorded against the property, then the purchaser must consider whether these restrictions will limit the types of medical services that can be provided at the property and, if so, if the purchase is still economically viable with the recorded restrictions in place.

2. License Requirements

A SNF real property purchaser also will need to consider whether there is an existing operator (i.e. tenant) in place or if a new operator will take over operations. If there is an operator in place, is the operator duly licensed to operate the property as a nursing home? What are the terms of the lease? Is there a management agreement? Is this a private pay facility or is the operator certified to receive funds through government reimbursement programs (e.g. Medicare and/or Medicaid)? Alternatively, if a new operator will operate the SNF, the purchaser will need to understand from regulatory counsel the timeline for which the new operator can become duly licensed and the steps involved. Local regulatory counsel can advise the purchaser regarding the specific requirements, disclosures and timing of applying for and obtaining a license to operate the SNF in that particular jurisdiction, as well as, becoming certified under any applicable reimbursement programs. In many cases, if a license cannot be obtained before the real estate acquisition must close, a prior operator will cooperate (by their agreement or because they are contractually obligated to do so) by either (a) continuing to operate the property until the new license is issued, or (b) permitting the new operator to operate under its license pursuant to a management agreement until a license is issued to the new operator. Each of these potential scenarios should be reviewed and approved by local regulatory counsel - and will require additional time for negotiations with the prior operator. It is important to note that even if the operations are not being transferred, depending on the state the property is located in, there may be notification requirements or other requirements in effect by the state licensing agency as to the transfer of the real estate.

3. Financing

If the purchaser is obtaining acquisition financing, then the purchaser should also consider the role of the operator in the underwriting due diligence process. Typically, a loan for the acquisition or refinance of a SNF property is underwritten by an operator's performance. As a result, the underwriting due diligence process will rely heavily on the cooperation of the operator. In addition, the purchaser should be aware that many SNF operators obtain an accounts receivable line of credit to cover the costs of the day-to-day management of the property. Therefore, in addition to negotiating the loan for the real property, the purchaser's lender will likely request to review the tenant's accounts receivable loan documents and negotiate an inter-creditor agreement with the tenant's lender. While this inter-creditor negotiation is a common practice in this type of deal, the delineation of lender priority and property subject to each loan can add additional layers of complication and time to the closing timeline.

This article is intended to highlight three of the larger points for discussion and consideration by a potential purchaser of a real property improved with a SNF, but is by no means an exhaustive list. However, by investigating each of the above issues at the beginning of the acquisition process, the proposed purchaser should be in a better position to determine the anticipated timeframe for the closing and potentially, to troubleshoot the feasibility of the deal.

If you would like further information on this topic, please contact Cynthia Mitchell at *cmitchell@seyfarth.com*, Elizabeth Dahill at *edahill@seyfarth.com*, your Seyfarth attorney, or any member of the Senior Living & Long-Term Care Team.

www.seyfarth.com