Mitigating Deal Risk for Sellers of Skilled Nursing Facilities (Checklist Included)

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Despite the financial headwinds that skilled nursing facility (SNF) operators and owners currently face, buyers and operators remain interested in acquiring skilled nursing facilities and operations. In assessing a buyer?s offer to purchase a SNF, a seller should focus on timing and transactional certainty, in addition to price. These concepts are not unique to the long-term care industry. However, there are nuances in the transactional practice of buying and selling SNFs that can greatly impact timing and transactional certainty. The following are steps a seller can take at the outset and throughout the transaction process to retain more control over the timing and to have greater certainty of closing.

First, it is important for the seller to identify who the buyer and new operator are at the outset of the transaction. If the buyer at the early stages of a transaction is a sponsor, the sponsor may enter into a purchase agreement to acquire the property and then arrange its equity syndicate, operators and debt financing. The sponsor, through one or more shell entities, also may execute an operations transfer agreement with the existing operator that provides for a delayed closing on the operations transfer that corresponds to the closing under the real estate purchase agreement. This type of purchaser arrangement creates timing and certainty issues for the seller.

The sponsor will push for a long delay between signing the purchase agreement and the outside date for the transaction to close to allow the sponsor time to arrange its debt and equity financing and leasing structure and to obtain regulatory approvals. While SNF transactions typically have significant delays between signing the purchase agreement and closing to allow the buyer and new operator to obtain requisite regulatory approvals, any additional delays expose the seller to transaction risks such as property damage or destruction and adverse healthcare regulatory surveys. These events may have a material adverse impact on the financial condition of the operations at the facilities and give the buyer the ability to walk away from the transaction. Moreover, the seller in this arrangement will also be exposed to the risk that the sponsor is unable ultimately to arrange its debt and equity financing or engage an operator group to operate the SNF.

If the new operator and buyer ownership structure are not available at the outset of the transaction, the sponsor also may be unable to make the required filings with the applicable regulatory agencies quickly. This inability to make the necessary regulatory filings quickly will delay the closing of the transaction further.

Second, the seller should identify the buyer?s lender. With the current downturn in the skilled nursing industry, some lenders that traditionally financed the acquisition of SNFs may be retreating from the sector. A result of this retreat is that new lenders who may have limited industry knowledge or expertise may be stepping up to finance acquisitions, based on past performance of the SNF industry. Buyers may have more difficulty getting these lenders comfortable with the transaction and structure from an underwriting and execution perspective. In addition, some buyers may be relying on bridge-to-HUD financing to finance their SNF acquisitions. Since the lender in a bridge-to-HUD financing does not want to finance a property that will not qualify for a HUD-insured loan, these lenders typically use HUD?s more stringent underwriting criteria for environmental and other diligence matters. Even where the purchase agreement has no financing contingency for the buyer, these lenders ultimately may delay the closing.

Given the potential pitfalls raised by the foregoing issues, what can a seller do to mitigate its transaction risk? The following checklist contains specific actions that a seller of a SNF can take.

Category	**Actions**
Diligence of the Buyer and Proposed Operator	• Request structure charts of the proposed buyer and operator group to un buyer is. This step will inform the seller of any potential transaction risk r new operator?s structure (or lack of structure). If a buyer is unable to del indicates that it is in the process of putting its equity and operator syndic pursuing a transaction with another more established buyer. • Inquire about the buyer?s proposed financing sources and the status of t that is relying on non-traditional lenders or bridge-to-HUD financing or wh in determining lender interest in the transaction may require more time to buyers. In addition, a buyer with no defined source of equity capital for th greater deal risk than a buyer with a large cash balance sheet or existing • Research the operating history of a buyer?s proposed operator. An oper background will be more likely to have issues obtaining regulatory appro and delay the closing of the sale.
Deposit	• Require the buyer to post a material, non-refundable deposit when the p executed. A buyer with material financial risk in the transaction is more li to close the acquisition quickly. In addition, this requirement will help det buyers from pursuing the transaction.

Outside Date and Regulatory Approvals	• Negotiate an outside date for closing that corresponds with the timing of applicable state and include strict covenants in the purchase agreement filings. These steps will help prevent a buyer from delaying the closing be periods required to obtain regulatory approvals.
Commitment Letters	• Require the buyer to provide debt and equity commitment letters upon ex agreement, as is standard practice outside the long-term care industry in buyer is a private equity fund. If the buyer is unable to deliver commitmen include a financing covenant in the purchase agreement that requires the equity commitment letters by a certain date. If the buyer fails to deliver th ensure that the seller has the right to terminate the purchase agreement liquidated damages. These measures will force the buyer to come to the existing equity syndicate and work expeditiously to organize its debt finan

A seller cannot eliminate all deal risk in the sale of a SNF. However, the foregoing measures will help a seller of a SNF to control the timing of the transaction and to mitigate certain deal risks by decreasing the delay between signing and closing, minimizing loopholes through which a buyer can delay a transaction and forcing a buyer to work expeditiously to obtain debt and equity financing early in the process.

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