

What Physicians and Investors Must Know About California Medical Corporations

November 8, 2019

By Michael H. Cohen

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Physicians can operate their practice as a sole proprietorship or as a partnership with other doctors. While these business structures have some advantages, doctors should understand the many advantages of forming a medical corporation. A medical corporation can help to limit liability, provide a vehicle for tax savings, make control and success of the practice easier, and create other opportunities and risk management benefits.

Unlike many other states, California does not give physicians the option of forming a standard C-Corporation or other common professional corporations such as an S-Corporation or an LLC (Limited Liability Corporation). Physicians who incorporate must create a California professional medical corporation. The medical corporation must be formed pursuant to the Moscone-Knox Professional Corporation Act.

Benefits of a Professional Medical Corporation

Some of the many benefits of a professional medical corporation are:

- **Limitation of liability.** One of the key reasons for professionals to incorporate is to limit their liability if debts can't be paid. Debts can include office rental, equipment leasing, and a full range of business obligations. Sole proprietors are personally liable for all debts the proprietor/doctor incurs. Partners are "jointly and severally liable" for their debts in accordance with the written partnership agreement. Medical corporations are separate entities therefore if the physician did not personally guarantee or sign contracts personally, only the medical corporation is liable for the business debts. If the Professional Medical Corporation is forced to close because it can't pay the debts, the creditors normally can't collect from the individual doctors – provided specific formalities are met such as the doctor didn't personally guarantee any contracts.

One major exception is that physicians in California can't use the cover of a professional medical corporation to protect the negligent doctor from medical malpractice lawsuits. The corporation status can be used, however, to protect the other doctors if they didn't contribute to the malpractice. The corporate benefit is an advantage over partnerships. If three doctors operate a partnership and one doctor commits medical malpractice, the other doctors will likely be held jointly liable

- **Tax benefits.** A second major benefit of a Professional Medical Corporation is that it can help the physicians save on taxes. A Professional Medical Corporation can elect to be taxed the same way as an S-Corporation is taxed. Taxes in S-Corporations can be passed through to the shareholders so that there isn't a double taxation like there normally is with a C corporation. An experienced medical corporate attorney can explain what other tax benefits are available to professional medical corporations. Medical corporations typically allow for higher contributions to 401(K)s than physicians could make on an individual basis

There is a counter tax concern though. Corporations normally pay a higher tax rate than individuals. This means corporations need to work with their accountants and tax professionals to pass the income down to the physicians instead of keeping the income in the practice. California medical corporations also do have to pay different state income taxes, fees, and other taxes such as a franchise tax.

- **Continuity.** A Professional Medical Corporation also helps with the continuity of the medical practice. If a doctor who practices on his/her own dies, the practice ends. If the doctor works with a partner, the partner must look for a new partner. With a professional medical corporation, the practice continues. The corporate by-laws dictate how much the spouse or family receives. Control issues are spelled out which should make the transition much smoother.

California Professional Medical Corporations can also be used to provide tax deductible health insurance, life insurance, and

disability insurance. Physicians can also generally use the Professional Medical Corporation for retirement plans and benefits.

Key terms and provisions of the Professional Corporation Act

Some important definitions found in the Moscone-Knox Professional Corporation Act are:

- **Professional services.** These are professional services that generally require a “license, certification, or registration authorized by the Business and Professions Code, the Chiropractic Act, or the Osteopathic Act.”
- **Who can own shares in the Professional Medical Corporation?** California professional medical corporations (Professional Medical Corporations) must have one or more physician owners. While non-physicians can have a partial ownership interest, the majority interest in the Professional Medical Corporation must be held by licensed doctors. The Act also regulates the number of non-physicians that are allowed. Permissible non-physicians in a medical corporation (provided they don’t have a majority interest) include:
 - “Licensed doctors of podiatric medicine.
 - Licensed psychologists
 - Registered nurses
 - Licensed optometrists
 - Licensed marriage and family therapists
 - Licensed clinical social workers
 - Licensed physician assistants
 - Licensed chiropractors
 - Licensed acupuncturists
 - Naturopathic doctors
 - Licensed professional clinical counselors
 - Licensed physical therapists
 - Licensed pharmacists
 - Licensed midwives

There are separate permitted non-physician interests for podiatrist medical corporations, psychological corporations, and many other licensed health professionals.

All non-physicians must be licensed to practice their profession in California.

Concerns and Restrictions

There are some issues for anyone considering a professional medical corporation must evaluate:

The Corporate Practice of Medicine. When physicians contract with non-physicians or allow non-physicians to invest in their practice (through the purchase of stock for example), an immediate red flag arises. Contracts, investments, and other transactions with non-physicians may be considered a corporate practice of medicine.

In California, the Medical Board of California directly warns doctors that the corporate practice of medicine is a violation of

state law. Specifically,

"The Medical Practice Act, Business and Professions Code section 2052, provides: 'Any person who practices or attempts to practice, or who holds himself or herself out as practicing...[medicine] without having at the time of so doing a valid, unrevoked, or unsuspended certificate...is guilty of a public offense.'

Business and Professions Code section 2400, within the Medical Practice Act, provides in pertinent part: "Corporations and other artificial entities shall have no professional rights, privileges, or powers."

One of the key reasons California prohibits the corporate practice of medicine "is to separate medical from business decision-making." The prohibition includes non-physicians and "lay corporations (corporations that are not medical professional corporations), and limited liability companies. In short, in California, a non-physician can't own (have a majority interest in) a medical corporation. Non-physicians also cannot hire physicians as either an employee or independent contractor.

CORPORATE PRACTICE OF MEDICINE: MEDICAL MANAGEMENT ORGANIZATIONS AND PROFESSIONAL MEDICAL CORPORATION—WHO CONTROLS WHAT?

The Corporate Practice of Medicine (CPM) doctrine continues to befuddle, beleaguer, and bewilder healthcare companies seeking to venture with physicians and non-physician entrepreneurs.

The MSO alternative. One possible alternative to reduce the risk of corporate practice of medicine complaints is that non-physicians can own a management service organization (MSO) which is specifically designed to run the administrative and non-medical parts of the medical practice.

- **Transfer of corporate shares.** There are restrictions on who a shareholder can sell his/her interest to and how proxies or other stock arrangements can be handled. The transfer, sale, or arrangement must not violate the Moscone-Knox ownership requirements. The transaction also can't result in corporate practice of medicine. Generally, the shares can only be transferred to an existing shareholder or to someone who is licensed in California to practice the same profession as the shareholder who is making the transfer.
- **Unlicensed professionals.** The California professional medical corporation must buy back the shares of any health provider who loses his/her license, certification, or is otherwise disqualified from the further practice of medicine or from providing licensed healthcare services. An experienced California medical corporation lawyer will explain the time limits for buy-backs. The lawyer will also explain why the terms of buy-sell agreements should be negotiated before any disqualification occurs.
- **Deceased Professionals.** The California Professional Medical Corporation must buy back the deceased provider's shares in accordance with any buy-sell agreements.
- **Compliance with federal and state laws.** Professional medical corporations and the physicians who work for or have an ownership interest in the Professional Medical Corporation cannot violate Stark Law, the Anti-Kickback Statutes, HIPAA, professional codes, and any other federal or state laws that regulate their practice, billing, marketing, services, or operations. The officers and directors of the professional medical corporation must also comply with all applicable federal and state laws.
- **Fictitious name approval.** The California Professional Medical Corporation should also review whether any pre-approvals are needed before the practice uses a fictitious name to run the medical practices.

An experienced corporate practice of medicine lawyer in California can explain how an MSO can also be used to help protect against Stark, Anti-Kickback, and state fee-splitting laws – in addition to using the MSO to protect against corporate practice of medicine complaints.

A Managed Service Organization can be used to provide an exception to Stark Law, a safe harbor to the Anti-Kickback

Statute, and a defense to California's fee splitting lawyer. A skilled MSO and medical corporation lawyer will explain how the MSO must be formed and operate to qualify for these exceptions, safe harbors, and defenses. For example, the fee the MSO charges must be the fair market value for these services.

MSOs can be used for "a conventional medical practice, a medical spa, an aesthetic medicine practice, integrative medicine, functional medicine, concierge medicine ... or even a psychology practice or behavioral medicine group."

Doctors should review what other restrictions and duties may apply when forming a professional medical corporation – with their California Professional Medical Corporation lawyer.

CORPORATE PRACTICE OF MEDICINE ON STEROIDS: HOW YOUR MSO AND PROFESSIONAL MEDICAL CORPORATION COULD WORK TOGETHER WITHOUT COURTING LEGAL DISASTER

You, MSO is my own variation on I Claudius. Poor Uncle Claudius, everyone said. Ended up becoming Emperor of Rome. Through craft and careful strategy. So you have an MSO and want to operate [...]

Additional concerns and requirements

Generally, the physicians will employ an experienced healthcare Professional Medical Corporation lawyer to form the medical corporation. The articles of corporation must comply with California law and with the rules and regulations of the particular practice area professional boards. The attorney will also prepare the bylaws which set forth how the corporation will function, how disputes are handled, and how the corporation can be dissolved.

Speak with an experienced healthcare lawyer to understand when, how, and why to form a California medical corporation. Some of the key considerations the lawyer will review are:

- The requirements for physician ownership and control.
- The advantages to using a Professional Medical Corporation including liability benefits, tax benefits, retirement benefits, and the ability to control the Professional Medical Corporation when physicians leave the practice or when disputes arise.
- How to protect against the risk of being charged with the corporate practice of medicine, fee-splitting and other federal and state laws, transfer of ownership issues, fictitious name registration, and many other legal concerns.

Before starting a new medical practice or agreeing to participate in an existing practice, physicians in California and elsewhere need to review the pros and cons of forming a professional medical corporation. [Contact](#) Cohen Healthcare Law Group, PC. to review when you must form a professional medical corporation and how you can use the Professional Medical Corporation to benefit your practice and the doctors in the practice. Understand the professional and legal obligations as well as the financial issues. We have helped many physicians form professional medical corporations and work with managed service organizations (MSO), so they can focus on helping their patients and growing their healthcare venture.

[Contact](#) our [healthcare law](#) and [FDA attorneys](#) for legal advice relevant to your healthcare venture.