



The Legal Facelift: How to Build, Run, and Transition a Compliant Med Spa – Part I

In recent years, medical spas – commonly known as med spas – have surged in popularity, blending the clinical precision of medical procedures with the relaxing environment of traditional day spas. The demand for non-invasive medical aesthetic treatments like Botox, laser hair removal, and skin rejuvenation continues to grow creating an opportunity for health care professionals to capitalize on their expertise as well as an invitation for investors to enter a new field. However, before diving into the med spa world too quickly, these entrepreneurs should take a moment to understand the legal landscape and consider how to navigate it.

This blog post is the first in series of three posts, where we will highlight several critical legal considerations related to the formation, operation, and exit of a med spa. First, we start with the formation.

The initial step is to understand who the stakeholders in the business venture are and where the med spa will be operated. Ownership of med spas depends on state laws and can vary widely. In many states, corporate practice of medicine (CPOM) laws prohibit non-physicians from owning entities that provide medical services. This means only licensed physicians (or physician-owned professional entities) can legally own a med spa in those states. These CPOM laws apply to med spas and depending on state law, can prevent non-physicians from owning or controlling med spas. Even though non-physicians (e.g., entrepreneurs, investors, etc.) cannot own the clinical portion of the business in states with CPOM laws, they may operate a management services organization (MSO) that handles non-medical functions (marketing, staffing, billing, etc.).

Depending on the state, the following are common ownership models:

1. Physician ownership: A licensed physician (M.D./D.O.) or professional entity owned by physicians owns the med spa.
2. Management services organization (MSO) model: MSO is a separate business entity that handles all the non-medical operations of the med spa. A non-physician owns the business side and contracts with a physician or physician group for clinical services.
3. Nurse practitioner or physician assistant ownership: In some states, nurse practitioners or physician assistants with full practice authority may be able to own or co-own med spas but still must comply with strict regulations.

Other health care requirements to consider when starting a med spa include, but are not limited to, the following:

- Medical oversight: Depending on applicable state laws, all medical treatments (injectables, lasers, etc.) must be performed by or under the supervision of certain licensed providers.
- Licensing and scope of practice: Providers must be properly licensed, and procedures performed must fall within the individual's scope of practice.
- Patient safety and compliance: Proper patient records, informed consent, and malpractice insurance should be maintained, applicable HIPAA regulations should be followed for patient privacy, and FDA-approved devices and products should be used.
- Facility regulations: The med spa must meet health and safety codes and, in some states, must be registered with the state medical board.

Second, once you know who will be involved and where you will operate, you will need to determine what type of entity and structure work. When choosing a business entity, the owners need to consider both state and federal tax filing requirements. Generally, state-level entity options include partnerships, limited liability companies (LLCs), and corporations. In CPOM states, where a medical professional must own the practice entity, there are professional counterparts to these types of entities. The creation of a separate business serves to limit liability for the business owners and offers a vehicle through the entities' governing documents to define the owners' business relationship.

In addition to choosing a state-level entity type, a tax entity will need to be considered. There are three primary types of tax entities. These include: C-corporation, S-corporation, or partnership. C-corporations are separate taxable entities and distributions made by C-corporations to their shareholders are also taxable; this second level of tax at the shareholder level makes C-corporation tax inefficient. In contrast, S-corporations and partnerships do not pay tax at the entity level. Rather taxation occurs only at the owner level. Income is determined at the entity level and then allocated to the owners, who then report the income on their individual income tax returns. Pass-through tax serves to create tax efficiency because there is only one level of tax. Although both S-corporations and partnerships provide pass-through taxation, the requirements to be an S-corporation are more rigid particularly with respect to who is eligible to be owner and how profits from the entity can be distributed. In contrast, partnerships have tremendous flexibility.

The entity that you choose at the state level will impact the entity's tax status. A state-level corporation must be taxed as either a C-corporation or an S-corporation, and a state-level partnership (limited, general, or limited liability), must be taxed as a partnership. A multi-member LLC, by default is taxed as a partnership, and a single member LLC by default is considered a disregarded entity for income tax purposes; however, as previously mentioned an LLC has flexibility in its tax structure and can make an election to be taxed as a corporation (C-corporation or S-corporation). An LLC, or PLLC where required, is the most common entity created due to the vast flexibility that LLCs offer both in terms of business and governance structure as well as their tax structure.

Third, after determining your entity type, you will need to implement the structure through preparing and filing the proper documents. Not only do these documents establish the existence of the business with the state and IRS, but they also establish the rules of the relationship among the owners. The key documents to consider include:

1. Articles of organization or articles of incorporation;
2. State regulatory board filings;
3. EIN application;
4. Tax election, if required;

5. Operating agreement or bylaws; and
6. Agreements between the MSO and practice entity.

Forming your legal entity is only the first step toward capitalizing on the booming med spa industry. In the next blog post of this series, we will highlight several key operational considerations.

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