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

The medical aesthetics industry, once dominated by independent practitioners, has become a hotbed for private equity and other entrepreneurial investments. The allure is clear: a fragmented market with high-profit margins, a cash-pay business model, and the potential for rapid scalability through consolidation. However, this influx of capital has not gone unnoticed by regulators, and the intersection of med spas and private equity presents a complex and evolving legal landscape.

For investors, the med spa industry offers a compelling investment thesis. They seek to acquire and consolidate "mom-and-pop" operators, creating larger platforms that benefit from economies of scale, professional management, and centralized business functions like marketing, human resources, and billing. This strategy, often referred to as a "roll-up," aims to increase efficiency and profitability, ultimately leading to a lucrative exit.

For med spa owners, a partnership with a private equity firm or other experienced investors can provide a significant infusion of capital, allowing them to expand, invest in new technologies, and offload the administrative burdens of running a business. It can be a path to both financial security and continued professional growth, as they can focus more on patient care and less on business operations.

However, beneath this seemingly harmonious arrangement lie significant legal and regulatory risks that both parties must carefully navigate. Med spa owners seeking to sell and investors seeking to acquire a med spa will want to be confident that the med spa is both structurally and operationally sound.

The first two blog posts in this series address many of the critical aspects of legal structure and operational regulatory compliance. When it comes time to transition a

med spa to achieve a successful transaction closing, several key legal aspects must be addressed.

1. Due Diligence and Pre-Sale Preparation

Prior to closing, buyers will scrutinize every aspect of the med spa business, and thus sellers will want to have their legal and financial house in order to make the process more efficient and instill confidence in potential buyers.

- **Corporate and Regulatory Compliance:** Ensure all corporate records are up-to-date, including articles of incorporation, bylaws, and board meeting minutes. The med spa must be in full compliance with all relevant state and federal regulations, such as those from the state medical board, U.S. Department of Health, and the Drug Enforcement Administration (if applicable). This includes confirming proper delegation agreements, physician supervision protocols, and the licensure of all medical professionals.
- **Employment Agreements:** Review all employment contracts for physicians, nurses, aestheticians, and other staff. Pay close attention to non-compete clauses, non-solicitation agreements, and change-of-control provisions. A buyer will want to know if key personnel are likely to stay on after the sale.
- **Leases and Contracts:** Organize and review all commercial leases, equipment leases, and vendor contracts. Understand the terms of assignability and whether the landlord's consent is required for a new tenant. Identify any contracts that may need to be renegotiated or terminated.
- **Intellectual Property:** Catalog all trademarks, service marks, and copyrighted materials associated with your med spa's brand. Ensure you have clear ownership of the business name, logo, and website content.

2. Structuring the Transaction: Asset Sale vs. Equity Sale

The most critical decision in the sale is whether it will be an asset sale or an equity sale. The choice has significant implications for both parties, particularly regarding liability and tax consequences.

- **Asset Sale:** In an asset sale, the buyer purchases specific assets of the med spa (e.g., equipment, client list, brand name, contracts) but does not acquire the legal

entity itself. This is often the preferred method for buyers because they can "cherry-pick" the assets they want and, most importantly, avoid assuming the seller's liabilities (e.g., past lawsuits, unpaid taxes, etc.). For the seller, an asset sale may result in more complex tax reporting and a potential for a higher tax burden, as different assets are taxed at different rates.

- **Equity Sale:** In an equity sale, the buyer purchases the seller's ownership interest (stock or membership units), thereby acquiring the entire legal entity. This is often simpler from an administrative perspective but carries a higher risk for the buyer, who inherits all of the med spa's liabilities – known and unknown. Sellers often prefer equity sales because they are typically taxed at a more favorable capital gains rate and can provide a cleaner exit.

The choice between an asset and equity sale should be made in consultation with both your attorney and your CPA.

3. Key Legal Provisions in the Purchase Agreement

The Purchase Agreement is the central legal document governing the sale. It must be meticulously drafted to protect your interests. Key provisions include:

- **Purchase Price and Payment Terms:** Clearly define the total purchase price, how it will be paid (e.g., cash, a promissory note, earn-outs), and the timing of the payments.
- **Representations and Warranties:** This is a critical section where the seller makes a series of factual statements about the business. These warranties cover everything from the med spa's financial health and regulatory compliance to the condition of its equipment and the status of its contracts. A buyer will rely on these statements, and a breach could lead to a post-closing lawsuit.
- **Indemnification:** This clause dictates who is responsible for losses or damages that arise after the closing, particularly those related to a breach of the representations and warranties.
- **Non-Compete and Non-Solicitation:** The buyer will almost certainly require the seller to sign a non-compete agreement, preventing you from opening a competing med spa in a defined geographical area for a specific period. Buyers also typically require that seller agree to not solicit former employees or clients. The enforceability of these clauses varies by state, and it is crucial to ensure they

are reasonable in scope.

4. The Importance of a Physician Practice Management Arrangement

For med spas that are not owned by a physician, the sale can be more complicated. Many states prohibit the "corporate practice of medicine," meaning a non-physician-owned entity cannot directly employ a physician or control the medical aspects of the practice. To comply, med spas often operate under a "Medical Director" or "Physician Practice Management" agreement. When selling, you must ensure this arrangement is properly transferred or restructured to comply with state law and protect the buyer.

5. Transition and Closing

The closing process involves a final check of all documents, the transfer of funds, and the execution of all agreements.

Conclusion

The convergence of private equity and other outside investment with the med spa industry is a leading trend, but it is not without significant legal peril. To successfully navigate this landscape, all parties must prioritize compliance, carefully structure transactions to adhere to state and federal laws and ensure that the ultimate focus remains on delivering safe, high-quality patient care. By engaging an attorney with experience in healthcare and business transactions, buyers and sellers alike can protect their interests, streamline the process, and secure the most favorable outcome for a sustainable partnership going forward.

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