

## **Bureau of Audit, Reimbursement, and Quality Assurance**

### **Nursing Facility Acquisition Financing – Non Related Parties**

- The rate of interest on a loan must not be in excess of what a prudent borrower would have had to pay in the market place at the time the loan was made.
- Interest expense, to be allowable, must be paid to a lender/lending institution that is at arms-length with the borrowing organization and not related through control, ownership, or personal relationship. Interest paid by the provider to partners, stockholders, or related organizations of the provider is, therefore, not allowable. Control or influence does not need to be exercised its presence will deem the interest unallowable.
- In order for interest expense to be allowable, the lender cannot have ownership in either the real estate company that holds the facility's assets or the nursing facility operating company.
- As part of the sales transaction, only an individual or corporation that does not have ownership interest in either the realty company that holds the nursing facility assets or the nursing facility operating company, may extend financing to the realty company to acquire the real estate.
- After the sales transaction an individual or corporation that has 5% or more ownership in either the realty company that holds the nursing facility assets or the nursing facility operating company, cannot also extend financing to either company, if the loan's principle balance is more than 5% of the total borrowings of the facility.
- Interest on loans in excess of asset value acquisitions (after July 1970) is not an allowable cost. In a situation where the purchase price exceeds the historical cost or the cost basis, the interest expense on that portion of the loan used to finance the excess is not allowable. All principle payments and loan forgiveness amounts are to reduce the allowable portion of a loan first.
- Interest expense applicable to borrowings principle balance for a nursing facility acquisition must be separately identified and reported from interest expense applicable to working capital or miscellaneous capital asset acquisitions.
- The dollar amount of facility acquisition financing is limited to the lesser of:
  - the purchase price of the nursing facility,
  - the current reproduction cost adjusted for straight-line depreciation over the life of the asset to the time of purchase, or
  - fair market value at the time of purchase; minus the purchase down payment.
- Interest expense on the dollar amount of a facility acquisition loan principle in excess of the financing limit is not allowable.

Reference: Medicaid Provider Manual, Nursing Facility Chapter, Cost Reporting and Reimbursement Appendix, Section 3 and Section 8.8

CMS, Provider Reimbursement Manual (PRM) 15 – 1, Section 2, Interest Expense

CMS, Provider Reimbursement Manual (PRM) 15 – 1, Section 10, Cost to Related Organizations

## **Bureau of Audit, Reimbursement, and Quality Assurance**

### **Nursing Facility Acquisition Financing – Sale Between Family Members**

- A purchase contract or agreement must be present. The transaction must terminate the seller's interest in the business. The seller must not have any recourse or ownership protection to retain or have a security interest in obtaining future ownership of that nursing facility in the event of the termination of the new ownership (purchaser) at a later date.
- Borrowing or financing for the sale transaction must be between the purchaser and a non-related third party (i.e., a financial institution). Financial loans from the family-related seller individual or entity to the family-related purchaser are not allowable for reimbursement. The finance instrument must not be a land contract from the seller.
- Total dollar amount of allowable borrowings cannot exceed the purchase price (allowable asset value). The Capital Asset Value (CAV) limit applicable to the nursing facility immediately prior to the sale, appropriately adjusted for nursing facility asset items that are excluded from the sale transaction, is the maximum reimbursable borrowing balance applicable to the asset transaction.
- The nursing facility property appraisal must be obtained. The facility appraisal value must support the purchase price negotiated between the sales parties.
- The new ownership operation must be a different legal entity in which the family-related seller is not an officer or board member exercising control over the new operation. The nursing facility entity may remain as an ongoing business entity in a situation where the real estate sale does not involve the licensed nursing facility operator. This occurs where a related party lease exists between the nursing facility entity prior to the real estate transaction, and the real estate transaction of the leased nursing facility is between the family-related parties. The requirement that the family-related lessor/seller cannot exercise active interest or control in the management of the nursing facility after the sale must be met.