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Legal Consideration on Transfer of Medical Corporation in South Korea

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Abstract**—** *The Korean medical law prohibits M&As of medical corporations. Currently, many medical corporations are secretly transferring medical corporations to third parties, ignoring the prohibition of the Medical Act. The Medical Law, which prohibits M&A by medical corporations, is resulting in medical corporations that are in a loss of management. Allowing M&A by medical corporations will help the healthy operation of medical corporations by inducing the integration of medical corporations with overlapping treatment items. At the same time, the integration between professional and medical corporations will create synergies and provide better medical services to local patients.*

Keywords**—** *Medical Corporation, The Medical Law, M&A (mergers or acquisitions).*

I. INTRODUCTION

Hospitals in the form of corporations seeking profit are not permitted in Korea. However, private hospitals run by one or more doctors are permitted to pursue profit. A representative examples are plastic surgery hospitals located in downtown Seoul. The first for-profit corporation in Jeju-do was attempted to be established, but in the end, it failed. In South Korea, Mega hospitals can be divided into those operated by school corporations and those operated by national Universities (Changsun Hwang, 2001). The majority of regional hospitals that treat only a portion of all medical departments are established by doctors or by welfare corporations. According to the South Korean medical law, corporations established for the purpose of treating patients must pursue non-profit only (Changsun Hwang, 2001). However, in reality, the transfer of hospitals operated by non-profit corporations to individuals or corporations occurs very frequently. Various legal obstacles are occurring in the process of selling a hospital in the form of a non-profit corporation. The purpose of this study is to find out the legal problems that arise in the process of selling a hospital in the form of a non-profit corporation in South Korea and to suggest alternatives.

II. LEGAL STATUS OF MEDICAL CORPORATIONS

A medical corporation is a representative of non-profit corporation, and the provisions of the civil law foundation are applied to its establishment and operation. (Article 50 of the Medical Law). If an individual or corporation intends to establish a medical corporation, preparing documents certifying that they have contributed certain assets and write articles of association on rules for operating medical corporation and it must obtain permission from the administrative agency (Article 50 of the Medical Law). Therefore, after a medical corporation is established with the permission of the administrative agency, if the medical corporation disposes of all of its assets or changes the articles of incorporation, it must also obtain permission from the administrative agency (Article 50 of the Medical Law)

A medical corporation is a type of foundation. A foundation, like a non-profit association, has no employees. At the same time, no one has shareholder status in corporation. A medical corporation is regarded as having the right to property (i.e., a foundation) contributed for the purpose of treating patients. According to the commercial law, the owners of a corporation are the shareholders. However, in medical corporations, there is no one who has the status equivalent to a shareholder. Therefore, since there are no members to whom the profits will be shared, there is no equity stake or a general meeting of members in the medical corporation. However, human resources are needed to run a medical corporation. They need directors and auditors. They are responsible for ensuring that there is no damage to the corporation without negligence in the course of business. Just as there are the operating rules of a corporation, that is, the employee rules, the operating rules and articles of incorporation of a medical corporation are necessary. The articles of incorporation contain all the operating regulations of medical corporations. In particular, if a medical corporation ceases operation and decides to dissolve, residual assets remain. The remaining property does not belong to the founder of the medical corporation (Hyunhee Jeon, 2004). First, it belongs to the person designated in the articles of incorporation, and unless otherwise stipulated in the articles of incorporation, it reverts to the national treasury and becomes state property. After all, even if the founder of a medical corporation establishes a corporation by donating all of his assets, the medical corporation becomes a legal subject and it separate from the founder at the moment of establishment (Changsun Hwang, 2001). Since the founder is not the owner of the medical corporation, he cannot be involved in the management. However, if the founder takes office as an executive of a medical corporation, he or she may be involved in the management of the medical corporation (Changsun Hwang, 2001).

III. REGARDING QUALIFICATIONS FOR MEMBERS OF THE BOARD OF DIRECTORS OF MEDICAL CORPORATIONS

All matters pertaining to the operating rules of a medical corporation are contained in the articles of incorporation. The purpose of the medical corporation's activities is to provide

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treatment services. In medical corporations, all decisions are made by a majority vote of the board of directors. The people who make up the board are called directors. The chairman of the board is called the chairman. Due to the nature of the majority vote, the board of directors must consist of at least three members. Doctors, dentists and oriental medical doctors are not the only members of the board of directors. Ordinary individuals without a medical license may also be members of the board. This is because the Medical Law does not specifically stipulate the qualification for the member of board in medical corporations (Jungmok Kwon, 2007). When an individual without a medical license becomes the chairman of the board of directors of a medical corporation, it can have a significant influence on the management of the medical corporation. If the number of board members is small and friendly for the chairman, the chairman may arbitrarily operate the medical corporation and reduce the quality of treatment services (Jungmok Kwon, 2007). In particular, the board of directors of medical corporations has a strong authority to hire and fire doctors of litigation hospitals (Supreme Court of Korea, Decision of 13 September 2012, 2012Da46244).

The doctors who actually treat patients and the board of directors who run the hospital can conflict with each other. In particular, doctors treating hospitals can ask the board of directors to improve the treatment environment from the patient's point of view. However, the board, which always puts hospital profits first, may turn down doctors' demands. Non-physicians on board members may not consider the positions of doctors in charge of patient care. In the future, the revision of the Medical Law, which states that more than half of the members of the board of directors of medical corporations must have medical qualifications, can be sufficiently considered.

IV. Legal Issues Regarding M&A of Medical Corporations

There is no provision for transfer of medical corporations in the Medical Law. This means that the transfer of medical corporations is not allowed. In other words, the Medical Law does not provide for mergers or acquisitions of medical corporations. Even if the medical corporation is dissolved, the founder of the corporation cannot recover the remaining assets (Jungmok Kwon, 2007). The means for the founder of a medical corporation to legally recover the property he contributed is blocked (Jungmok Kwon, 2007). As a result, in reality, it is often the case that the founder of a medical corporation transfers his/her position as a board member, that is, an executive, to a third party and receives compensation for it. Such mergers and acquisitions of anomalous medical corporations do not conform to the public interest nature of medical corporations (Jungmok Kwon, 2007, Supreme Court of Korea, Decision of 10 May 1991, 1991Nu4327).

If so, at this moment, it is legally impossible to transfer the management rights (i.e., the position of an executive) of a medical corporation to a third party for a fee. In August 27, 2019 in amended Article 51-2 of the Medical Act, a new regulation was added that

"No one shall exchange or promise to give or receive money, valuables, entertainment, or other property benefits in connection with the appointment of an executive of a medical corporation."

A person who gives or promises to give or receive money or valuables in connection with the appointment of an executive of a medical corporation in violation of this may be punished by imprisonment with labor for not more than one year or by a fine not exceeding 10 million won (Article 89, Paragraph 3 of the Medical Act). And the above regulations are in effect from the date of promulgation. Therefore, after August 27, 2019, the transfer of management rights of a medical corporation for a fee is punishable as a violation of the Medical Law. In addition, a contract with such contents is an anti-social legal act and is invalid, so it cannot be legally protected.

V. Attitude of the Supreme Court on the Paid Transfer of a Medical Corporation

Bobath Hospital, a medical corporation located in Bundang-gu, Seongnam-si, Gyeonggi-do, filed a rehabilitation application to the bankruptcy court to adjust the existing debt due to poor management. The Seoul bankruptcy court issued a decision to authorize the rehabilitation so that the right to form the board of directors of Bobath Hospital, a medical corporation, could be sold to a third party (Seoul Bankruptcy Court, Decision of 21 September, 2016, 2016Hoehap100116).

A Korean conglomerate, Hotel Lotte Co., Ltd., applied to purchase the right to form the board of directors, and the bankruptcy court granted it. As a result, Hotel Lotte Co., Ltd. became the new owner of Bobath Hospital, a medical corporation. Criticism was raised that the bankruptcy court's permission to sell members of the board of directors could provide a clue to the commercialization of the medical corporation. However, even if a large corporation took over the management rights, Bobath Hospital, a medical corporation, is not a non-profit corporation, so it cannot recover the hospital profits. In other words, it is difficult to agree with the claim that a medical corporation will become a profit hospital by acquiring the right to form a board of directors (Young chan Kim and Eunjung Kim, 2016). Before the amendment of the Medical Act, Supreme Court ruled as below

"*The act of an executive of a medical corporation transferring their position and receiving money in return, that is, the de facto M&A of a medical corporation, was interpreted as legally valid and the transfer of management rights of a medical corporation was not subject to criminal punishment. In other words, unless there is a decision by the legislator to prohibit or punish the transfer of the operating right of a medical corporation for a fee (Supreme Court, Decision of 26 December of 2010, 2010Do16681).*"

The Supreme Court stipulated the following specific reasons why criminal punishment could not be imposed on the paid transfer of membership to the board of directors of medical corporations.

"Criminal punishment just only based on the abstract risk of which the transfer of the medical corporation's operating

right and receipt of the transfer price may adversely affect the basic property of the medical corporation in the future causing disruption to the operation was unacceptable as it was against nullum crimen sine lege (no crime without law) and the principle of clarity of criminal laws and ordinance (Supreme Court, Decision of 26 December of 2010, 2010Do16681)".

However, the current medical law amendment does not allow the transfer of the executive status of a medical corporation for a fee.

VI. Legal Basis for Prohibition of M&A by Medical Corporations

The Medical Act strictly regulates the establishment of a medical institution without a doctor. Nevertheless, exceptions are permitted only to medical corporations for medical purposes, that is, medical corporations. Currently, one-third of hospitals opened in South Korea are medical corporations. General hospital operation by medical corporation is positioned in a way. The Medical Law stipulates that a medical corporation is a non-profit corporation. However, there are opposing views in favor of and against the fact that medical corporations have public interest. Currently, most medical corporations are located in urban areas. A medical corporation established in a rural area where there is an absolute shortage of doctors can be interpreted as having the characteristics of public interest based on public health. Currently, the central government does not support subsidies by means of recognizing the public nature of medical corporations (Hyunhee Jeon, 2004).

There is no tax reduction or preferential treatment for medical corporations compared to other for-profit corporations (Supreme Court, Decision of 13 April of 2010, 2010Da101060)

According to the interpretation of the Medical Law, a medical corporation has a non-profit, but it is difficult to say that it has a public interest. For reference, In April 13th 2012 Supreme Court made precident,

*"A medical corporation is merely a non-profit corporation that pursues research and development related to health and medical care incidentally for the purpose of establishing and operating a hospital, and does not fall under the public interest corporation stipulated in Article 2 of the Public Interest Corporation Act (*Supreme Court, Decision of 13 April of 2010, 2010Da101060)*."*

In other words, medical corporations are not relate to the Public Interest Corporation Act and are being apply of the General Civil Act. In the end, there is lots space in interpretation of the Medical Law, which prohibits mergers and acquisitions for medical corporations that are not in the public interest, excessively infringes on the freedom of business granted to all individuals by the Constitution.

In the end, the medical law that prohibits the transfer of management rights to medical corporations is unconstitutional. Currently, the chairman of the board of directors of the medical corporation transfers the management rights of the medical corporation by an anomalous method of transferring the position of the director in exchange for a certain amount of money to a person who wishes to take over the medical corporation. In reality, the transfer of medical corporations is already take place, so the logic of allowing mergers and acquisitions by medical corporations falls into the same contradiction as the argument that drugs should be legalized by people who inhale drugs in reality. In reality, in most cases, the founder of a medical corporation participates in hospital management with the initiative of the medical corporation's board of directors. In a structure where the price of medical services is determined by the government as in Korea, managing a profit is not an easy task. Most medical corporations in Korea are medium-sized regional hospitals and are facing difficulties in management. If M&As of medical corporations are prohibited, hospitals must continue to operate until bankruptcy, even if operating losses continue (Jungmok Kwon, 2007). This is contributing to the deterioration of the quality of medical services. When a local hospital is shut down due to a sudden bankruptcy, the loss goes to the local patients. Consideration should be given to allowing the M&A of medical corporations as a condition of permission from the administrative agency.

VII. Legal Review on Allowance of Transfer of Medical Corporations

The problem of M&A ban: from the perspective of the founder of a medical corporation, after running a hospital for a certain period of time, he or she is faced with a situation in which he has to suspend the operation of the hospital for personal reasons. At this time, the Medical Law prohibits receive transferring fee to disposition of medical corporations, so the founder is blocked from recovering the funds invested in establishing the medical corporation. Therefore, it is often the case that anomalous transfer of the position of a director and receiving the invested money in return. In this situation, it is happening that a businessman who forgets his original purpose of treating patients and pursues only money participates in the acquisition of a medical corporation. It is a profit-seeking behavior that aimed at the blind spot of the law. Currently, doctors over the age of 65 who run medical corporations have virtually no other way to succeed in operating hospitals unless their children have a doctor's license. After all, there are frequent anomalous cases of transferring the position of a director to a third party other than a doctor and handing over the management of the hospital. Hospitals operated by medical corporations, like other companies, must maintain a surplus budget by importing hospital expenses paid by patients and disbursing expenses necessary for patient treatment. However, even if a doctor who is not a professional manager takes office as a director of a medical corporation, the financial compensation for management performance is blocked (Hyunhee Jeon, 2004). Therefore, competent professional managers avoid participating in the management of medical corporations on the grounds of low remuneration (Hyunhee Jeon, 2004).

Advantages of allowing M&A: If the medical corporation that operates the hospital opens the way for a third party to take over mergers and acquisitions, the illegal act of transferring the director's position prohibited by the Medical Act and

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receiving money in return will disappear. It is very difficult to maintain a surplus by operating a medical corporation in Korea, which pursues a public health system in which medical fees are determined by the government. Therefore, the reality of Korean hospitals is that patients have strong distrust of hospital treatment due to hospitals that repeat duplicate treatment and excessive treatment. If hospital M&A is allowed, the participation of professional managers is guaranteed. If hospital management is entrusted to them and doctors focus on patient care, they can provide high-quality medical services, which will increase hospital sales and increase patient satisfaction at the same time (Matt Schmitt, 2017). The establishment of medical corporations will increase. In a situation where M&A was prohibited, the founders of the medical corporation had no way of recovering their investment. In the end, it was possible to transfer the medical law expediently only by accepting the violation of the medical law. However, if hospital M&A is allowed, the number of establishments of medical corporations will increase. This is because the return on investment is guaranteed. Regional hospitals, not high-level hospitals at the level of university hospitals, can have competitiveness only when they specialize in the treatment field. For example, if M&A is allowed between specializes in ophthalmology Hospitals A and specialized in dermatology Hospital B than there will be a synergistic effect will occur and the combined hospital's sales will increase than the combined sales of the two existing hospitals (Monica Noether and Sean May, 2017).

Hospital M&A tolerance limits: Even if hospital M&A is allowed, it cannot be allowed without any restrictions. Administrative offices have the authority to direct and supervise the operation of medical corporations under the Medical Act. It is necessary to make regulations on the administrative agency's permission for M&A of medical corporations. Currently, changes to the directors of medical corporations and changes to the articles of incorporation are permitted by the administrative agency. Similarly, M&A of medical corporations must also be subject to administrative approval conditions. Through the medical amendment, detailed regulations regarding hospital M&A licensing conditions should be in placed. In particular, it is the limit on the sale price. The sale price should be limited to the amount invested by the founder of the medical corporation. Then, the non-profit nature of the medical corporation is maintained. However, only when the performance of a medical corporation in which the management performance of the medical corporation has significantly improved compared to the initial period is verified by a fair evaluation by an external accounting firm, there may be sufficient circumstances in which a transfer is desired at an amount higher than the investment amount. This can be addressed by providing incentives to the management of medical corporations(ED Gunes and H Yaman, 2009). The side effects of receiving excessive incentives can be reduced if the management of the medical corporation provides incentives and the calculation of the amount of incentives are all approved by the administrative agency.

VIII. Conclusion

Currently in South Korea, medical corporations are more focused on non-profit compare to public interest. In the process of operating a hospital, prohibition of profit-seeking is a necessary item because it is directly related to the deterioration of the quality of life caused by the surge in medical expenses. If the provision of better medical services is ensured and a path of return of investment is provided for the founders of medical corporations, more medical corporations will be established than now, and patients will enjoy easier access to medical care than now (Nancy D. Beaulieu and Leemore S. Dafny et al., 2020). The approval of M&A by medical corporations will lead to the emergence of regional hospitals specializing in specialized treatment, which will have a side effect of improving the structural problem of excessive concentration of patients in university hospitals.

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