



Health Care Reform:

How will it affect the value of your center?

BY JONATHAN C. VICK

PHYSICIAN-OWNERS OF GI ENDOSCOPY CENTERS ARE FACING AN UNCERTAIN FUTURE WITH THE CHANGES IN HEALTH CARE BEING DEBATED IN WASHINGTON. NO ONE KNOWS THE LONG-TERM EFFECTS OF THE HEALTH CARE PLAN THAT WILL EVENTUALLY BE LEGISLATED. THIS UNCERTAINTY PROVIDES NEW INCENTIVES TO FORM STRATEGIC PARTNERSHIPS WHILE TAKING SOME MONEY OFF THE TABLE BY PARTNERING WITH AN ASC MANAGEMENT COMPANY WITH PROVEN OPERATIONAL EXPERTISE AND CAPITAL SPECIFICALLY EARMARKED FOR INVESTING IN GI CENTERS. THIS ARTICLE WILL DESCRIBE THE CURRENT HEALTH CARE ENVIRONMENT, THE POTENTIAL IMPACT ON YOUR CENTER, AND STRATEGIC PARTNERSHIP OPPORTUNITIES THAT WILL ENABLE YOUR CENTER TO CONTINUE TO PROSPER.



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Current health care environment: In a word, uncertain! The several competing bills pending in Congress would guarantee all Americans access to health coverage, addressing the plight of the 47 million people who are now uninsured. Congress plans to achieve this by expanding Medicaid, requiring insurers to accept all applicants regardless of their health, and mandating that everyone purchase coverage. Government subsidies would make the obligatory coverage more affordable. The goal of reform is to broaden coverage, improve outcomes and reduce waste—an ambitious goal that will be extremely hard to achieve and that is certain to increase health care costs and taxes.

If Congress includes a “public” or government sponsored option, facility fees will almost certainly be affected, most likely shifting in the direction of Medicare reimbursements. So the bad news is that average facility fee reimbursements for GI procedures are likely to decline. What would happen to your center’s revenue, profits and value if your government (i.e. Medicare) population doubled without any increase in volume? Table 1 provides an example. Bottom line: if your revenues and profits decline without an offsetting increase in volume, the EBITDA* and value of your center will decrease significantly. In the example, the value of the center declined by 25% from \$12.8 million to \$9.6 million. To make this up, this center would have to generate \$540,000 in new revenue (plus all associated variable costs), just to return to a “pre-reform” value.

Impact on endoscopy centers: The good news, however, is that ASCs and endoscopy centers are very efficient and cost-effective facilities that are uniquely positioned to cut waste and improve efficiency—two critical elements to achieving the goals of health care reform. With a potential 47 million additional insured patients seeking services, your facility could benefit significantly if you position yourself strategically to take advantage of approaching changes and opportunities with strategies that will increase volume and maximize earning potential from each patient.

What is the “opportunity”? The “opportunity” will be conditioned by how Congress, the government and the major health insurers agree to pay for achieving the health care reform goals. The health insurers have been deftly maneuvering behind the scenes in Washington and, judging from industry reports, have succeeded in redefining terms of the reform debate

Table 1: Example of increasing public or government (“Medicare”) patients from 25% to 50% of payor mix

	Payor mix: 25% Medicare	Payor mix: 50% Medicare	Changes with 50% Medicare
Procedures	7,200	7,200	
Ave. Medicare fee	\$400	\$400	
Ave. other fee	\$700	\$700	
Ave. rev. per proc.	\$625	\$550	(\$75)
Medicare revenue	\$720,000	\$1,440,000	
Other revenue	\$3,780,000	\$2,520,000	
Total revenue	\$4,500,000	\$3,960,000	(\$540,000)
Total expense	\$2,500,000	\$2,500,000	
Net income	\$2,000,000	\$1,460,000	(\$540,000)
Interest	\$50,000	\$50,000	
Taxes	–		
Deprec. & Amort.	\$100,000	\$100,000	
EBITDA/Cash flow	\$2,150,000	\$1,610,000	(\$540,000)
Valuation			
Multiple of EBITDA	6***	6***	
EBITDA X multiple	\$12,900,000	\$9,660,000	(\$3,240,000)
Less long-term debt	\$600,000	\$600,000	
Plus cash	\$500,000	\$500,000	
Valuation	\$12,800,000	\$9,560,000	(\$3,240,000)
Value of 51%	\$6,528,000	\$4,875,600	(\$1,653,000)
Change in value			(25%)

*EBITDA: Earnings Before Interest, Taxes, Depreciation and Amortization

** TTM: Trailing-12 months

***2009 prevailing multiple for majority interests in single-specialty GI centers

to such a degree that no matter what specifics are included in the final bill, the insurance companies will emerge more profitable (*Why Health Insurers are Winning*, Business Week, August 17, 2009). For insurers, the key to their success with health care reform will be the level of average reimbursements and the minimum standards detailing how much deductible patients would be required to pay, which is projected to range from 24% to 35%.

The key to your success: So with 47 million newly insured patients with significant deductibles on the horizon and insurers trying to protect their profits, how can your endoscopy center benefit, and what must you do to position your center to take advantage of pending opportunities and become more profitable?

Regardless of what shape the final health care reform takes, the key to continued success of a GI center in the coming environment will be professional expertise in business disciplines that will **maximize reimbursements, increase volume, improve efficiency and reduce costs.**

Maximize reimbursements: If 50% of your future patients are government (i.e. Medicare, Medicaid, Public Option, etc.) patients, the remaining 50% will be paid for through your payor contracts. For your center to remain successful, professional expertise in payor contracting will be critically important. If you don’t already have one on your staff, you will need access to contract specialists if you want to win at contracting.

Increase volume: With decreased revenue from your current patient

population, you will have to increase volume to maintain profitability and your center’s value. This means more intense patient acquisition efforts to gain access to your share of the 47 million newly insured, recruitment of more physicians using your facility and educational efforts toward your referral base to increase patient referrals.

Improve efficiency, cash flow, expense control and profitability: Most centers are already relatively efficient when compared with a hospital. However, to continue the profitability of your center in the new environment will require even more efficient operations, expertise in scheduling, coding, case costing, negotiations with suppliers, expense control and personal management. Benchmarking and incorporating “Best Practices” from other centers will become extremely important.

Strategic partnerships: To prepare for the coming changes, many successful centers are forming strategic partnerships with ASC management companies that have the experience, track record, financial resources and expertise in the business disciplines needed to accomplish significant operational improvements. In addition, a corporate partner can negotiate a minority partnership with your hospital and potentially gain access to additional hospital referrals, contracts and higher reimbursements.

Selling to a corporate partner: There are currently over 40 ASC management companies that have an interest in investing in ASCs and endoscopy centers, and they come in all shapes, sizes, levels of expertise and capital. Each has a different model, a unique track record, varying levels of financing and other resources, and different levels of interest and success with GI centers. In most cases, there will be three to six companies that should be considered as a prospective partner for each center,

depending on the goals of the owners, location of the center, level of profitability, needs of the center and related growth opportunities. The goal of corporate partners is to develop and execute strategies that will result in profit growth—thus benefiting all owners.

How centers are valued: GI centers are valued by taking the trailing 12-months (TTM) cash flow (EBITDA) and applying a multiple (6 to 6.5 times for a majority interest, somewhat less for a minority interest), then deducting long-term debt and adding cash to determine fair market value. If your future reimbursements will be less than your TTM reimbursements and your expenses stay the same, the value of your center will decline. Thus, it is to your advantage to establish a value with a buyer before health care reform is enacted while reimbursements are highest and let your corporate partner help develop your growth strategies.

Next step: If you are interested in developing a strategic relationship and selling an interest in your center to a corporate partner that will help you to achieve your goals, here are some important questions and considerations to discuss with your partners and advisors:

- What are the owner's goals?
- What expertise does your center need?
- How much of your center are you willing to sell?
- What are the growth opportunities for your center?
- How can you make your center more attractive to a buyer?
- What can you do to increase the value of your center prior to the sale?
- How can you create competitive leverage to get the best price and the best deal?
- What will happen to your profits if

50% of your patients are government patients?

- Which ASC management companies should you solicit partnership proposals from?

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