

VALUE

EXPERIENCE

RESULTS



Physician Practice Acquisition Analysis & Valuation

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IMA Consulting

VALUE ♦ EXPERIENCE ♦ RESULTS

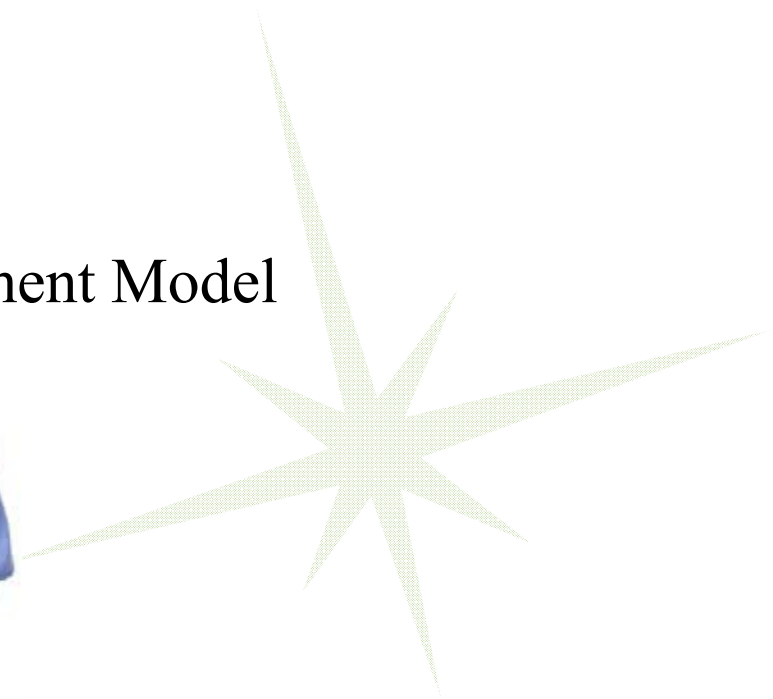
Webinar Objectives

- ◆ Understanding the Underlying Reasons for Enhanced Activity in the Physician Practice Acquisition Marketplace
- ◆ Reviewing the Acquisition Due Diligence Process
- ◆ Discussing the Various Physician Practice Valuation Methodologies
- ◆ Reviewing the Post-Acquisition Integration Process

Underlying Reasons for Acquisition

Physician Perspective

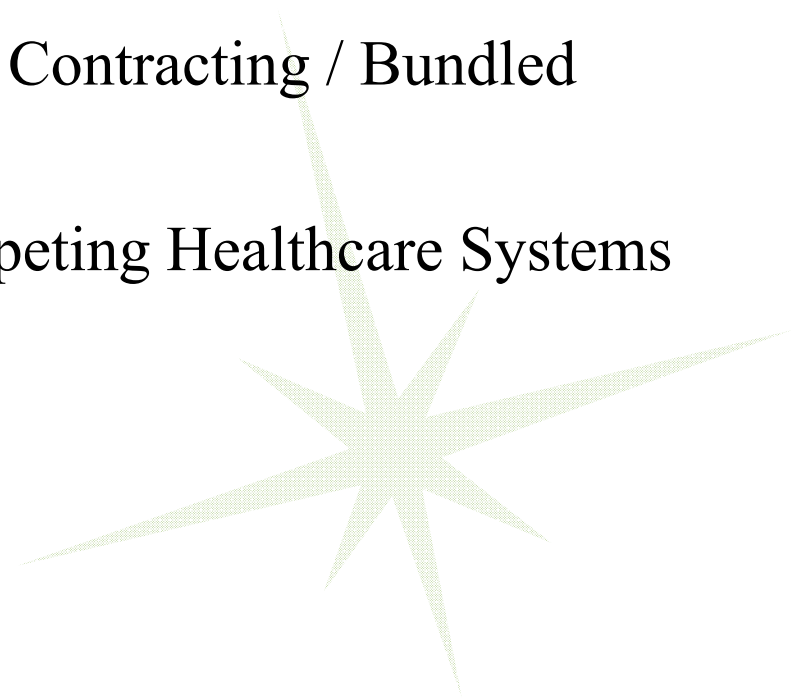
- ◆ Uncertainty with Healthcare Reform
- ◆ Administrative Burden of Running a Private Practice
- ◆ Access to Capital
- ◆ Work / Life Balance
- ◆ Overall Market Shift to Employment Model



Underlying Reasons for Acquisition

Health System Perspective

- ◆ “Lock up” Covered Lives in ACO-type Model
- ◆ Establish Centers of Excellence
- ◆ Gain Leverage with Insurers for Contracting / Bundled Payment Purposes
- ◆ Defensive Posture Against Competing Healthcare Systems

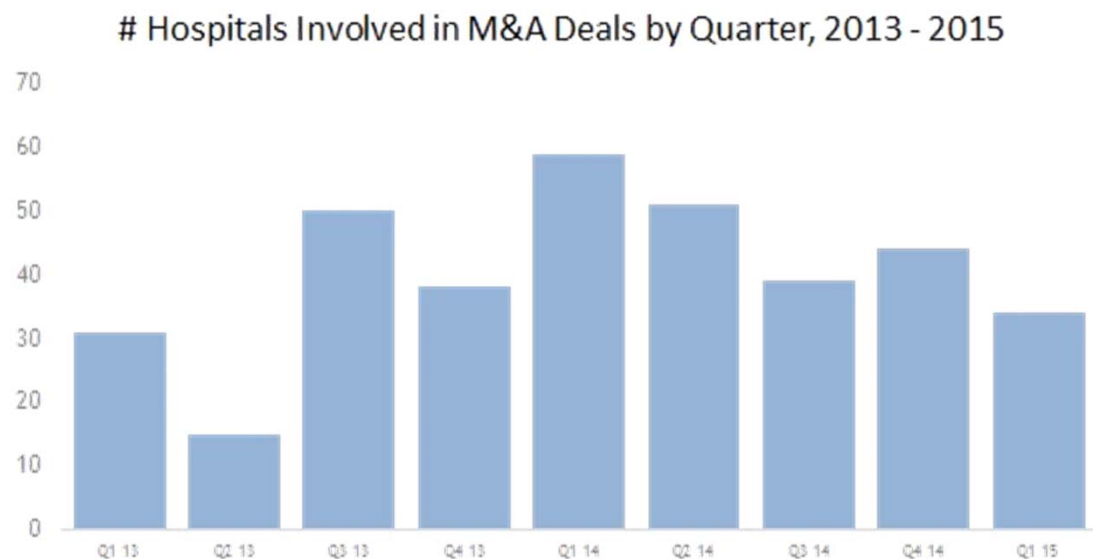


Underlying Reasons for Acquisition Marketplace Trends

- ◆ Healthcare M&A in the U.S. Reached \$241B by May 2015
 - Highest YTD Volume Ever Recorded
 - Gain Economies of Scale
 - Shift from Volume to Value
 - Enhance Consumer Appeal
- ◆ Shift from Horizontal to Vertical M&A
- ◆ Expanding Digital & e-Health Capabilities



Underlying Reasons for Acquisition Marketplace Trends



Source: www.billianshealthdata.com

Underlying Reasons for Acquisition

Legal Considerations

- ◆ Stark Law
- ◆ Anti-Kickback Statute
- ◆ Tax Issues



Underlying Reasons for Acquisition

Other Drivers

- ◆ Office-Based Procedures – Specialty Practice Reimbursement & Volume Reductions
- ◆ Retail Marketplace Changes
 - Influx of “Pop-Up” Clinics
 - Rise of Physician Extenders
- ◆ Pressures on Specialty Practice Margins
 - Cardiology
 - Orthopedic Surgery



Underlying Reasons for Acquisition

Typical Phases of Practice Acquisition



- ◆ Discovery
- ◆ Transaction Itself
 - Lengthy Process
 - Mismatched Resources
- ◆ Day One Integration
- ◆ Long-Term Plan / Vision



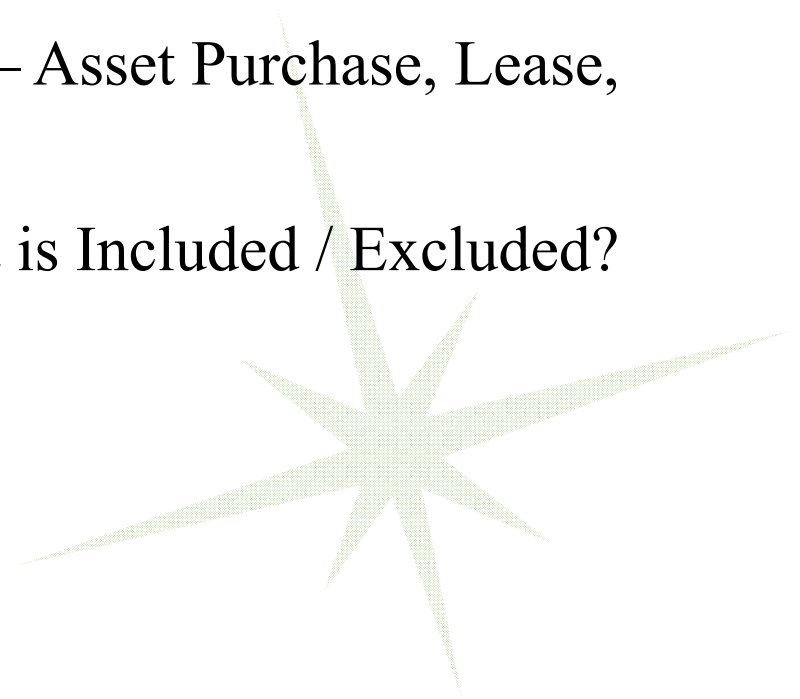
REVIEWING THE ACQUISITION DUE DILIGENCE PROCESS



Acquisition Due Diligence Process

Preliminary Steps

- ◆ Is there a Defined Physician Practice Acquisition Strategy?
- ◆ Does Target Practice Meet Strategic Goals / Objectives?
- ◆ Method of Practice Acquisition – Asset Purchase, Lease, Employment Agreement
- ◆ “Define” the Transaction - What is Included / Excluded?



Acquisition Due Diligence Process

Kicking the Tires to Determine What You're Really Buying

- ◆ Organizational / Legal Review
- ◆ Contracts Analysis
- ◆ Medical Staff / Physician Extenders
- ◆ Financial Analysis



Acquisition Due Diligence Process

Kicking the Tires to Determine What You're Really Buying

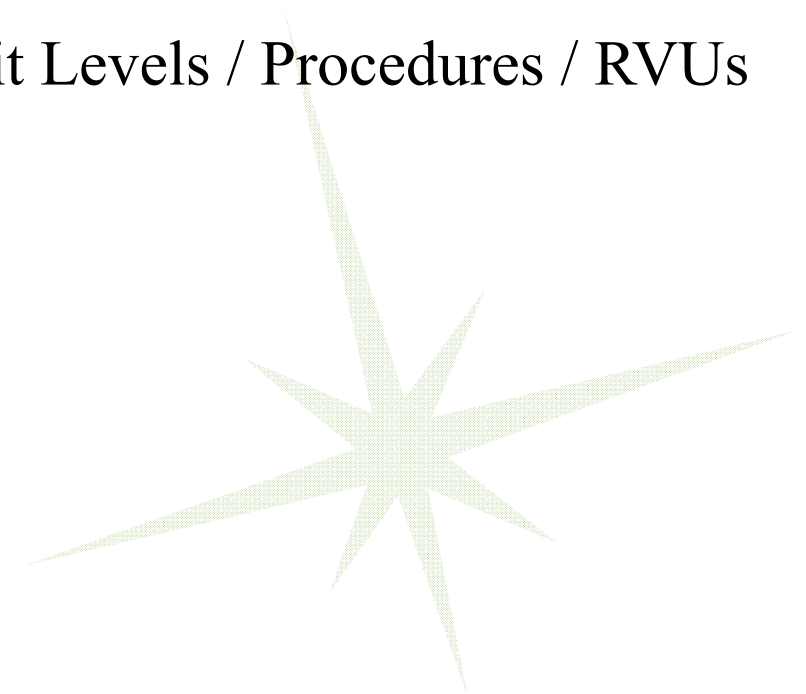
- ◆ Physical Office / Equipment / Environmental Assessment
- ◆ Regulatory Review
- ◆ Insurance Review Including Medical Malpractice
- ◆ Information Systems / EHR



Acquisition Due Diligence Process

Billing / Coding / Clinical Documentation Compliance Review

- ◆ Consider Conducting Review Under Privilege
- ◆ Sample Selection Strategies for Adequate Coverage
- ◆ Identify Practice Volumes / Visit Levels / Procedures / RVUs



Acquisition Due Diligence Process

Predicting Post Acquisition Operating Results

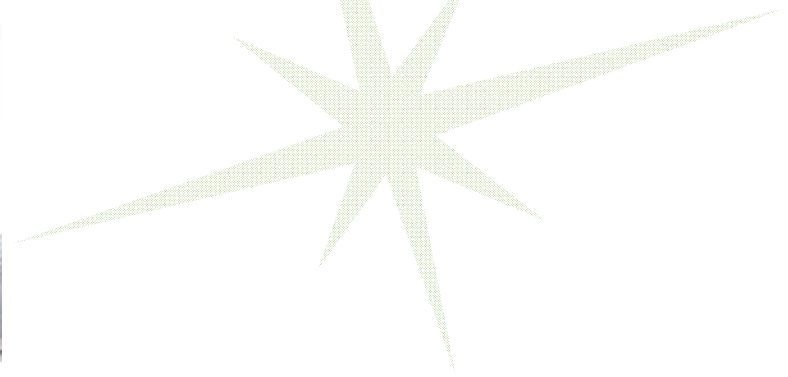
- ◆ Revenue Projection Under a “Black Box” Concept
- ◆ Modeling Potential “Site of Service” Impacts
- ◆ Determination of Transferability of Contracts / Payor Rate Renegotiation



Acquisition Due Diligence Process

Revenue Cycle Assessment

- ◆ Accuracy of Net Accounts Receivable Balances
- ◆ Determination of Days in A/R / Days Cash on Hand
- ◆ Determination of Bad Debt Write Off Trends
- ◆ Assessment of Authorizations Process / Coverage Denials / Related Appeals Process / Scheduling / Billing / Collections



Acquisition Due Diligence Process

Elements of the Purchase Price

- ◆ Working Capital of the Practice?
- ◆ Delineation of Pre versus Post Liabilities
- ◆ Malpractice “Tail”
- ◆ Physician Compensation Contracts / Signing Bonuses





DISCUSSING THE VARIOUS PHYSICIAN PRACTICE VALUATION METHODOLOGIES



Physician Practice Valuation

- ◆ Standard of Value
- ◆ Regulatory Requirement for FMV Determination
- ◆ 3 Conventional Valuation Approaches
 - Income Approach
 - Market Approach
 - Cost Approach
- ◆ IRS Guidance



Valuation Methodologies

Income Approach



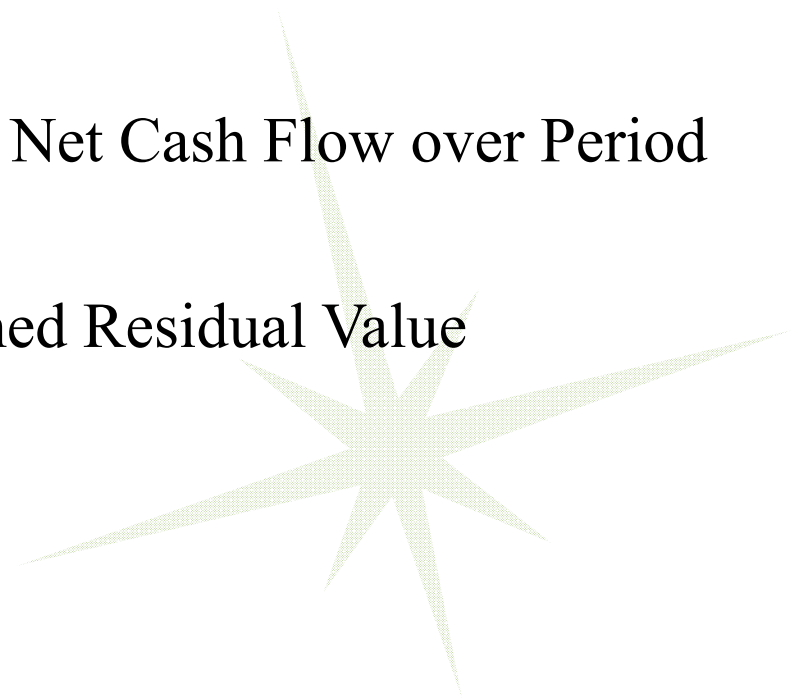
- ◆ Present Value of Expected Future Economic Benefits
 - Direct Capitalization Methodology
 - Discounted Cash Flow Methodology
- ◆ Commonly Utilized when Sales or Services Provided are Main Drivers of Value
- ◆ Direct Capitalization Method
 - Results “Normalized” and Expected Growth is Stable
 - Net Income, Debt-Free Cash Flow or EBIT can be Capitalized

Valuation Methodologies

Income Approach



- ◆ Discounted Cash Flow Method
 - Results “Normalized,” but Allows for Variable Expected Future Growth
 - Measures Value on Expected Net Cash Flow over Period of Time
 - PV of Cash Flow + Determined Residual Value



Valuation Methodologies

Market Approach



- ◆ Transaction Methodology
- ◆ FMV = Prices Paid in Marketplace for Similar Assets
- ◆ “Comps” by Practice Specialty – S&P Capital IQ, Pratt’s Stats, Goodwill Registry
- ◆ Transaction Review Period Typically 24 Months
- ◆ Price-to-Revenue Multiple Derived

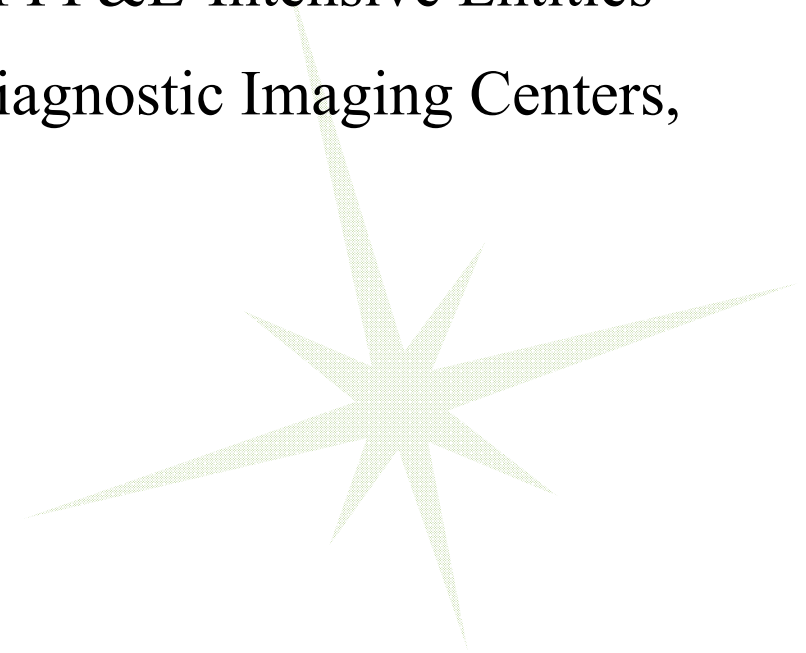


Valuation Methodologies

Cost Approach

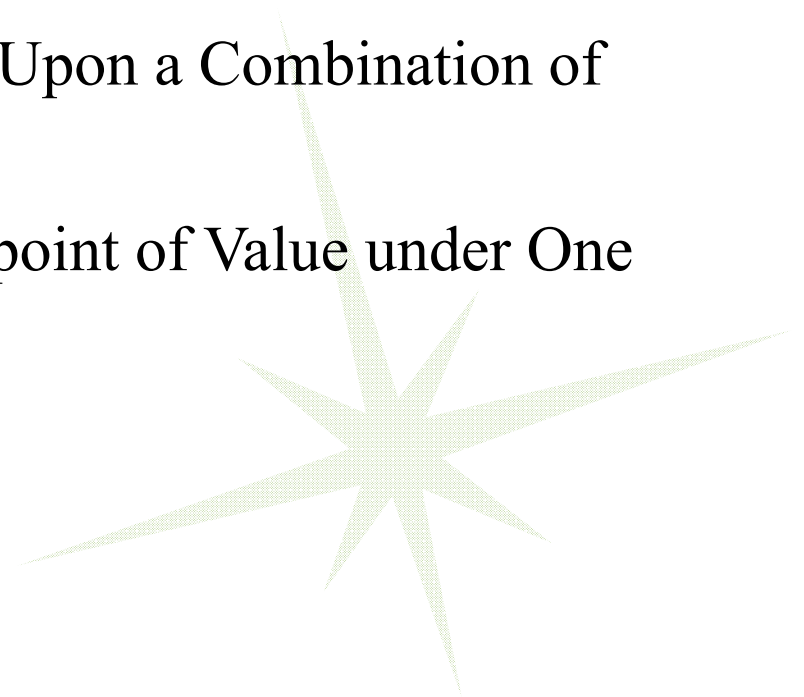


- ◆ Measures Value on a Replacement or Reconstruction Cost Basis
- ◆ Typically Used for Valuations of PP&E-Intensive Entities
- ◆ Ambulatory Surgery Centers, Diagnostic Imaging Centers, etc.



Summary of Value

- ◆ Correlation of Enterprise Value
- ◆ Also Referred to as Findings & Conclusions of Value
- ◆ Determined FMV can be Based Upon a Combination of Methods
- ◆ FMV can be Based Upon a Midpoint of Value under One Methodology



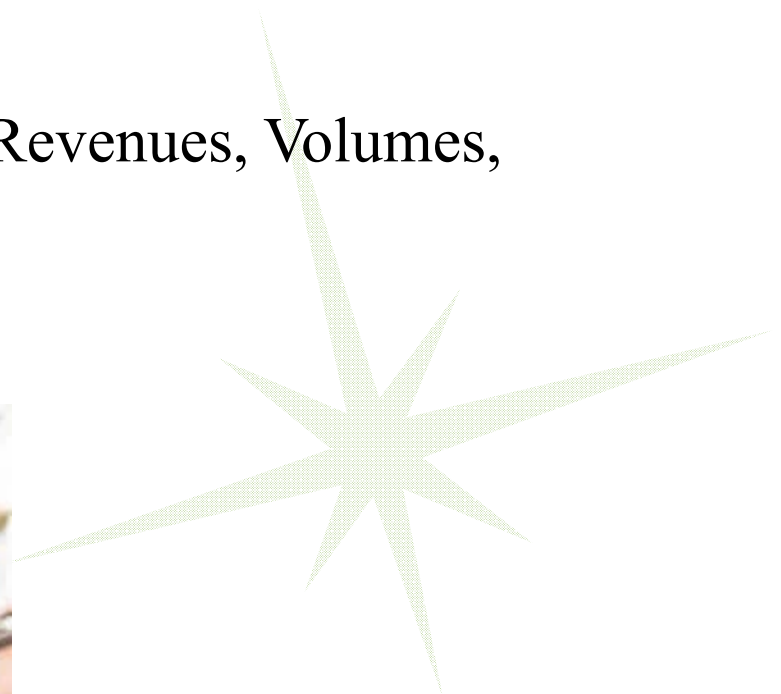
Components of a Valuation Report

- ◆ Background of the Practice being Valued
 - Listing and Background of Physicians and Physician Extenders
 - Related Work RVUs and Weekly Scheduled Office Hours by Clinician
 - General Office Hours Info, Room Make-Up and Practice Profile



Components of a Valuation Report

- ◆ Inventory of Practice Equipment
- ◆ Patient Profile, Health Insurance Plans Accepted, Number of Active Charts
- ◆ Financial Performance – 3-Year Revenues, Volumes, Expenses, Compensation
- ◆ Determination of Value





REVIEWING THE POST- ACQUISITION INTEGRATION PROCESS



Post-Acquisition Practice Integration

Practical Issues / Challenges

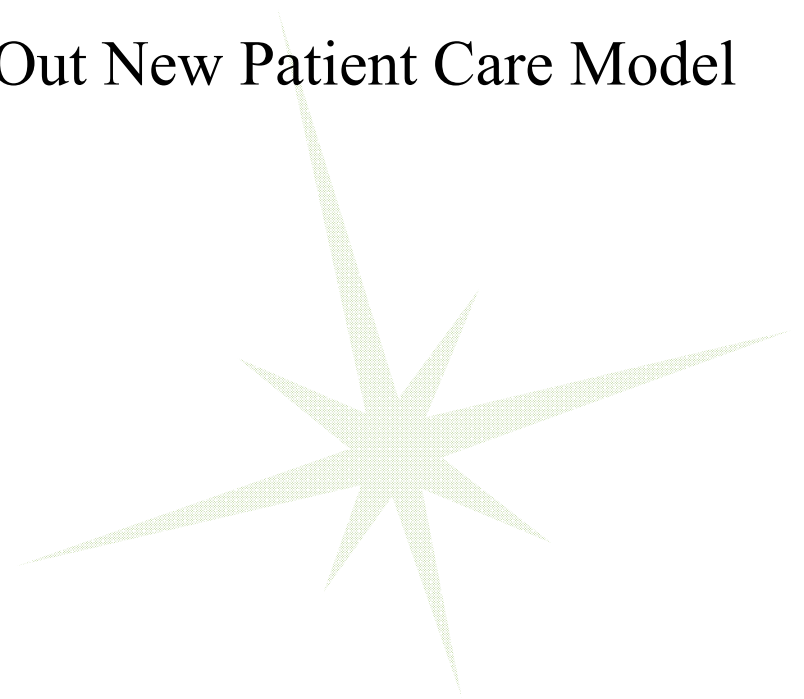
- ◆ Day One Onboarding
 - Practice Hours
 - Billing / Coding Training
 - Arranging for Ancillary Services
 - Requisitioning Medical & Office Supplies
- ◆ Physician Leadership / Culture
- ◆ Non-Physician Employees



Post-Acquisition Practice Integration

Realization of Transaction Realities

- ◆ True Full Cost of Acquisition Transaction
- ◆ Need to Add Physician Extenders
- ◆ Related Efforts / Costs to Build Out New Patient Care Model



Post-Acquisition Practice Integration Risks for Health Systems

- ◆ Fall into the “Monkey See / Monkey Do” Trap
- ◆ Not Having a Well-Thought Out Physician Practice Strategy
- ◆ “Responding” Rather than “Initiating”



Post-Acquisition Practice Integration

Common Difficulties Encountered

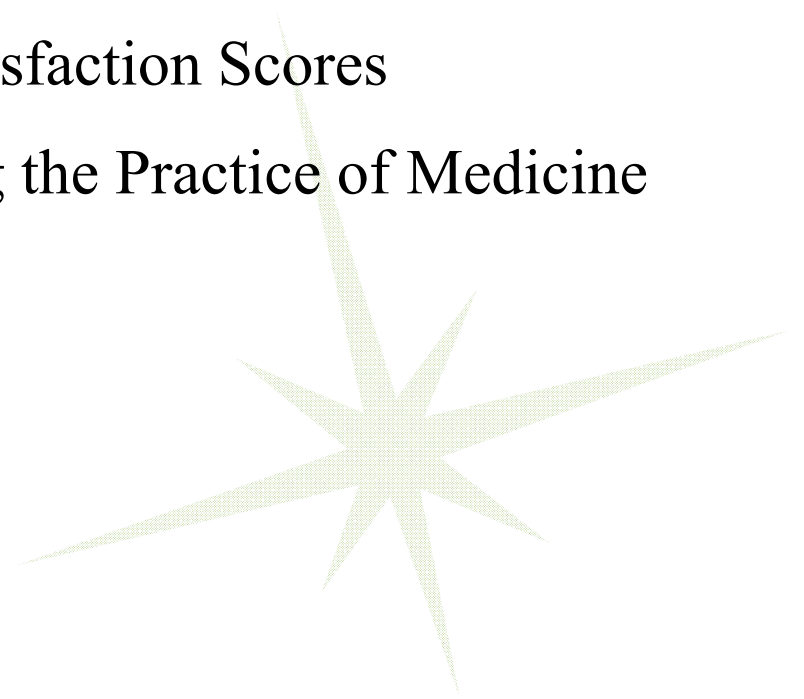
- ◆ Significant Losses Generated
- ◆ Lack of Bandwidth to Effectively Manage Multiple Practices
- ◆ Use of a “Productivity-Only” Model to Monitor Physician Efforts
- ◆ Disconnect Between Pre and Post Acquisition Financial Modeling



Post-Acquisition Practice Integration

Success Stories

- ◆ Gaining Meaningful Physician “Citizenship” Participation
- ◆ Development of Clinical Boards
- ◆ Effective Patient & Nursing Satisfaction Scores
- ◆ Team Approach to Transforming the Practice of Medicine



Post-Acquisition Practice Integration

Top 10 List... How to Make a Good Practice Look Bad

1. Remove Credit for Office Ancillaries
2. Move Practice Billing under Hospital CBO
3. Sacrifice Practice as a “Lost Leader” in Managed Care Contracts
4. Require Practice to Assume Hospital Department Standards
5. Relocate Practice to Vacant Hospital Space



Post-Acquisition Practice Integration

Top 10 List... How to Make a Good Practice Look Bad

6. Focus Practice Managers on Referrals & CM Instead of Quality & Throughput
7. Reduce FTEs / Right-Size Practice to Reduce Operating Losses
8. Allocate Health System Overhead or Dean's Tax as Quasi-Management Fee
9. Ignore Downstream Revenue
10. Have Negative CM Influence Capital Needs

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