

2013

ADVANCED BUSINESS VALUATION CONFERENCE

Healthcare Reform and the Impact on Appraisal Practice

Overview and Key Observations

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Session Objectives

- Provide an Overview of the Patient Protection and Affordable Care Act
- Discuss Impact on the Healthcare Industry
- Discuss Possible Impacts to Industry sectors, business owners and employees
- Provide practical suggestions for appraisers

*****DISCLAIMER*****

Overview and Timeline

PATIENT PROTECTION AND AFFORDABLE CARE ACT

The Affordable Care Act

- The Patient Protection and Affordable Care Act (PPACA or “Obamacare”) was signed into law on March 23, 2010
- The Health Care and Education Reconciliation Act was signed into law on March 30, 2010, making several changes to PPACA
- According to the Dept. of HHS, the goals of PPACA are:
 - To provide new consumer protections
 - Improve the quality and lower the costs of healthcare
 - And to increase access to affordable care

PPACA has been (and continues to be) subject to fierce public debate, legal challenges, modifications, delays, political posturing, and vows of repeal

- On June 28, 2012 the Supreme Court upheld the law in a 5-4 opinion, citing congressional authority to levy taxes.
- There have been 44 lawsuits against the Obama administration filed in federal courts in 18 states. (AL, CO, DC, FL, GA, IL, IN, LA, NE, MI, MN, MO, MS, NY, OH, PA, TN, TX.)
- House Republicans have voted 41 times to repeal the law, a futile effort with Democratic control of the Senate and the Oval Office.
- The President has already signed 14 laws to amend, retract or change the Affordable Care Act, and he has also taken 5 steps to delay the federal law

Timeline - 2010

- Start of changes to pre-existing condition rules and options
- Elimination of lifetime limits and regulation of annual limits (phase out through 2014)
- Free preventative care
- Donut hole rebate checks for seniors
- Incentives for Primary Care
- State matching funds for low-income individuals (optional)
- Small business become eligible for tax credit up to 35% of contribution (with phase out based on # of employees and wage levels)
- 10% excise tax levied on tanning salons

Timeline - 2011

- Additional benefits to Seniors, including 50% discount on drugs for those reaching coverage gap, free preventative care, and post-acute care
- Independent Payment Advisory Committee established to find ways to target waste and reduce cost
- Changes in payment mechanism for Medicare Advantage Plans
- Pharma companies begin paying tax on brand name drugs
- Elimination of tax-free OTC drug purchases through HAS
- Insurers required to spend 85% of premiums on providers or rebate difference to consumers

Timeline - 2012

- Incentives for physicians to join Accountable Care Organizations (ACOs)
- Financials incentives for Hospitals linking payment to Quality outcomes
- Start of series of changes to encourage Electronic Health Records, including standardized billing and information exchange

Timeline - 2013

- Pilot program to “bundle” payments for episode of care
- Additional incentives to primary care doctors, states required to pay no less than 100% of Medicare allowable (federally funded)
- Planned start for open enrollment in Health Insurance Exchanges (HIX)
- FSA contribution limits begin (\$2,500 per year)
- 2.3% excise tax on medical devices
- Pass-through businesses subject to “Medicare” surtax of 0.9% for earners making more than \$200,000 / \$250,000 joint filers (tax does not go to Medicare fund)
- Pass-through businesses owners pay new 3.8% tax on investment income for earners making more than \$200,000 / \$250,000 joint filers

Timeline - 2014

- Individual Mandate begins requiring nearly all individuals to buy insurance or pay a penalty
- Employers must calculate size to determine applicability of Employer mandate
- Small business and individual policies must cover a list of “essential benefits”
- Health Benefit Exchanges open for Individuals
- Small Business Health Option Plans (SHOP) open for businesses
- Insurance reform takes full effect – no pre-existing condition exclusions
- Deductibles capped at \$2,000 individual / \$4,000 family
- Tax implemented for plans purchased in fully-insured market (does not apply to self insured plans – mostly big companies, unions, gov’t)

2014 (continued)

- Individuals can qualify for premium credits under the following criteria:
 1. Household income less than 400% of federal poverty level
 2. Employee share of employer-sponsored health insurance exceeds 9.5% of household income (and)
 3. Employer sponsored coverage does not meet actuarial requirements
- Increase small business tax credit to a level of up to 50% of the employer contribution to private health insurance

2015 and beyond

- 2015 – Businesses with more than 50 FTEs face penalty if one employee qualifies for subsidies
- Planned payment mechanism to pay physicians for Quality
- 2016 – SHOP exchanges open to business with up to 100 FTEs
- Insurers allowed for form choice compacts across state lines
- 2017 – SHOP exchanges open to many larger businesses
- 2018 – Excise tax imposed on employers offering plans with aggregate expenses exceeding \$10,200 for an individual and \$27,500 for a family (Cadillac Tax)

Impact on the

HEALTHCARE INDUSTRY

Healthcare Industry Trends

- Mass migration of physicians from independent practice to Hospital Employment
- Significant acquisition activity by hospitals and health systems
- Consolidation among major systems
 - Tenet buys Vanguard for \$4.3B
 - CHS offer to buy HMA for \$3.9B
- Shift in payment models away from fee for service

Healthcare Industry Trends

- Reimbursement
 - HIX payment models and rates are evolving/uncertain
 - Expansion of Medicaid eligibility will account for 50% of new insured population (18.4M)
 - Medicare reimbursement will face continued cuts (\$716B in planned cuts), also reductions in Medicare Advantage plans
 - Friendly to PCPs, Harder on Specialists
 - Volume vs. Quality
- Pricing Transparency

Healthcare Industry Trends

- Health Information
 - Significant investment will be required on health information systems
 - Meeting new standards could cost as much as \$50M per hospital
 - There will also be significant reporting and compliance costs
 - Access to better information may lead to better outcomes, cost savings and more efficient care
- Patient volumes
 - Projected 30M additional covered lives
 - Changes to insurance coverage for existing population
 - Likely to further exacerbate physician shortages

Healthcare Industry Trends

- Life Sciences
 - Medical device and drug companies subject to new wave of taxes
 - Some or all of this may be passed through to the consumer
 - Additional reporting rules required for life sciences companies will add costs to compliance (Sunshine Act)

Healthcare Industry Trends

HealthCare Valuation Considerations

- Uncertainty should result in higher risk/discount rates
- Changes in reimbursement will vary based on location and service type
- Costs of regulatory compliance will likely be higher
- Models for evaluating FMV may need to change
- Modifications to Stark, etc., could exempt certain entities or transaction types from FMV requirement

Impact on the

OTHER INDUSTRIES

Overview

- New Business Opportunities
- Business Costs
- Taxes
- Impact on Consumers
- Impact on the Economy
- Other Impacts

New Business Opportunities

- Information Technology
 - Electronic Health Records
 - Reporting and monitoring software/apps
 - Information security
- Consulting
 - Integration strategies
 - Tax, M&A, Operational
- New Types of Businesses
 - Accountable Care Organizations
 - Health Information Exchanges

Impact on Business

Size Matters

- Most significantly impacted will be companies with 50-199 workers
- Tax credits for smaller companies will expire after 2016

Higher Costs

- Higher insurance premiums on existing plans
- Possible penalties for “Cadillac plans”
- Higher labor costs for those not currently offering insurance
- Additional cost for reporting / compliance

Staffing Concerns

- Managing hours to <30 per week
- Passing costs to employees

New Taxes

New taxes under Healthcare Reform are anticipated to raise \$700B over the next 10 years

- 2.3% Tax on Medical Device Manufacturers
- 10% Tax on Indoor Tanning Services
- Blue Cross/Blue Shield Tax Hike
- Elimination of tax credit for “black liquor” biofuel
- Excise Tax on Charitable Hospitals which fail to comply with the requirements of the law (\$50,000)
- Tax on Brand Name Drugs
- Tax on Health Insurers
- Elimination of tax deduction for employer-provided retirement Rx drug coverage in coordination with Medicare Part D

New Taxes

- Employer Mandate on business with over 50 full-time employees to provide health insurance. \$2,000 per employee \$3,000 if employee uses tax credits to buy insurance on the exchange.
- Medicare Tax on Investment Income 3.8% over \$200k/\$250k
- Medicare Part A Tax increase of .9% over \$200k/\$250k
- 40% Excise Tax "Cadillac" on Premium Health Insurance Plans 2018
- An annual \$63 fee levied on all insurance plans (decreased each year until 2017 when pre-existing conditions are eliminated) to help pay for insurance companies covering the costs of high-risk pools.
- Over the counter medicines no longer qualified as medical expenses for flexible spending accounts (FSAs), health reimbursement arrangements (HRAs), health savings accounts (HSAs), and Archer Medical Saving accounts (MSAs).

New Taxes

- Health savings account or an Archer medical savings account, penalties for spending money on non-qualified medical expenses.
- Flexible Spending Account Cap 2013
Contributions to FSAs are reduced to \$2,500 from \$5,000.
- Medical Deduction Threshold tax increase 2013
Threshold to deduct medical expenses as an itemized deduction increases to 10% from 7.5%.
- Individual Mandate
Starting in 2014, anyone not buying "qualifying" health insurance must pay an income tax surtax at a rate of 1% or \$95 in 2014 to 2.5% in 2016 on profitable income above the tax threshold.

Economic Impact

National Economy

Significant argument and rhetoric regarding actual cost of reform and impacts to the National Economy

- Conservative groups argue that the law will actually increase the deficit, discourage investment and penalize “job creators”, increase interest rates, and reduce wages.
- Proponents argue that the law will reduce the overall cost of healthcare and decrease the deficit.

State Economies

- Significant budgetary issues for states, notably the expansion of Medicaid
- Federal funding for expansion declines in 2017-2020, leaving State tax payers responsible for 10% of the expansion costs
- Additional enrollees possible for those dropped from employer plans or for those who previously qualified but did not enroll (and now must)
- Federal funding also does not cover the costs of administration

Valuation Considerations

Forecasting

- Expense structure should reflect changes resulting from healthcare reform
- Prior performance may be less indicative of future performance, with certain business types more heavily impacted than others
 - Service industries
 - Firms with 50-199 employees
 - Insurance agencies
 - Insurance companies
 - Medical Device and Drug Manufacturers
 - Healthcare Companies

Valuation Considerations

Economic Analysis

- Appraisers will need to pay closer attention to the overall National and local economy as Healthcare reform is implemented

Cost of Capital

- Interest rates may experience higher volatility or increases
- Company specific risk factors will need to be more closely considered
- General uncertainty should result in additional risk in models

Taxes

- Effective tax rates in our models may need to be higher
- Pass-through entity adjustments may need to change

QUESTIONS?