

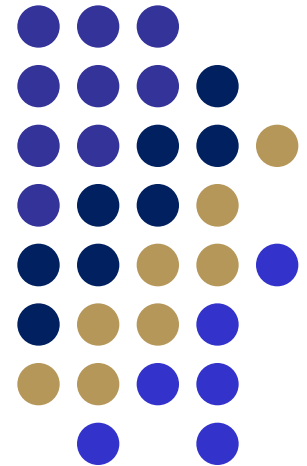
Valuing ASCs and Recent Trends in ASC Transactions

Presented By

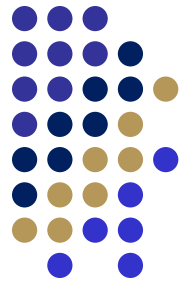
Todd J. Mello, ASA, CVA, MBA, Founding Partner

June 12, 2015


HealthCare Appraisers
INCORPORATED

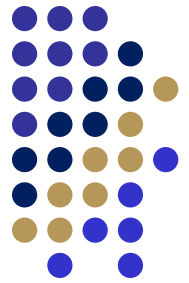


Presentation Outline



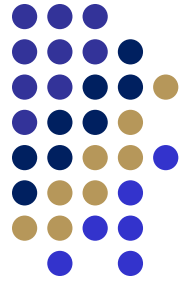
- Valuation 101: Approaches and Methods and other 411
- Do's and Don'ts
- Value Enhancers and Value Detractors
- Minority vs. Majority/Control
- History, Purpose and Limitations of the Survey
- What are Valuation Multiples?
- Reported Earnings Multiples
- Other Survey Observations (time permitting)

Valuation 101



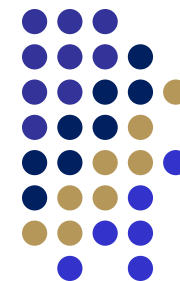
- Valuation is *forward* looking
- Why get a valuation?
- Standard of value in most healthcare transactions is *Fair Market Value*. The definition of **fair market value** in healthcare is slightly different than the standard valuation definition.
 - the price at which property would change hands between a hypothetical willing and able buyer and a hypothetical willing and able seller, acting at arm's length in an open and unrestricted market, when neither is under compulsion to buy or sell ... *between well informed parties who are not otherwise in a position to generate business for the other party...*
 - *Implications of "hypothetical"*

Valuation 101



- **Income Approach** – A general way of determining a value indication of a business, business ownership interest, security, or intangible asset using one or more methods that convert anticipated future economic benefits into a single present amount.
- Most common methods: Discounted Cash Flow Method and Capitalization of Earnings Method
- When and why?
- Example: next slide

Valuation 101

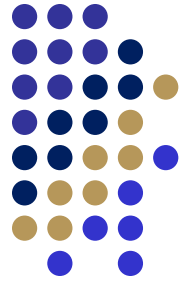


	Low Weighted Average Cost of Capital ("WACC")					Terminal
	2013	2014	2015	2016	2017	Year
-						
Free Cash Flow	\$716,731	\$689,381	\$819,707	\$916,550	\$1,014,428	\$1,076,696
Partial Period Factor	0.25					
Discounting Periods (mid-point)	0.13	0.75	1.75	2.75	3.75	
Present Value Factor @ 14.0%	0.9838	0.9064	0.7951	0.6974	0.6118	
Present Value of Cash Flow	134,776	624,855	651,749	639,202	620,627	

Present Value of Projected Cash Flows	2,671,209	
Present Value of Terminal Value Calculation	<u>5,489,355</u>	
Indicated Market Value of Total Capital	<u>\$8,160,564</u>	
Less: Debt	(1,529,861)	Exhibit B.2
Plus: Surplus Cash	<u>601,000</u>	Exhibit C.5
Indicated Market Value of Equity (Rounded)	<u><u>\$7,232,000</u></u>	
(control, marketable)		

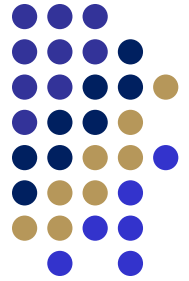
Terminal Value Calculation	
Free Cash Flow in Terminal Year	1,076,696
Divided by Capitalization Rate (WACC - LTGR of 2.00%)	<u>12.00%</u>
Equals Terminal Value in 2017	8,972,466
Present Value Factor for 2017	<u>0.6118</u>
Present Value of Terminal Value	<u><u>\$5,489,355</u></u>

Valuation 101



- **Market Approach** – A general way of determining a value indication of a business, business ownership interest, security, or intangible asset using one or more methods that compare the subject to similar businesses, business ownership interests, securities, or intangible assets that have been sold.
- Most common methods: Guideline Publicly Traded Method and Comparative Transactions Method
- When and why?

What are Valuation Multiples?



The Meaning Behind the Numbers

The Finance Definition (a.k.a. Appraiser speak)

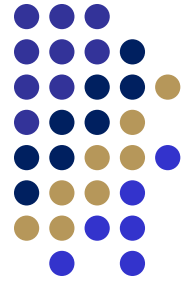
“A mathematical expression of risk and growth, which when applied to a perpetually recurring earnings stream results in an indication of value”

A multiple is mathematically expressed as follows:

$$\frac{1}{(K - g)}$$

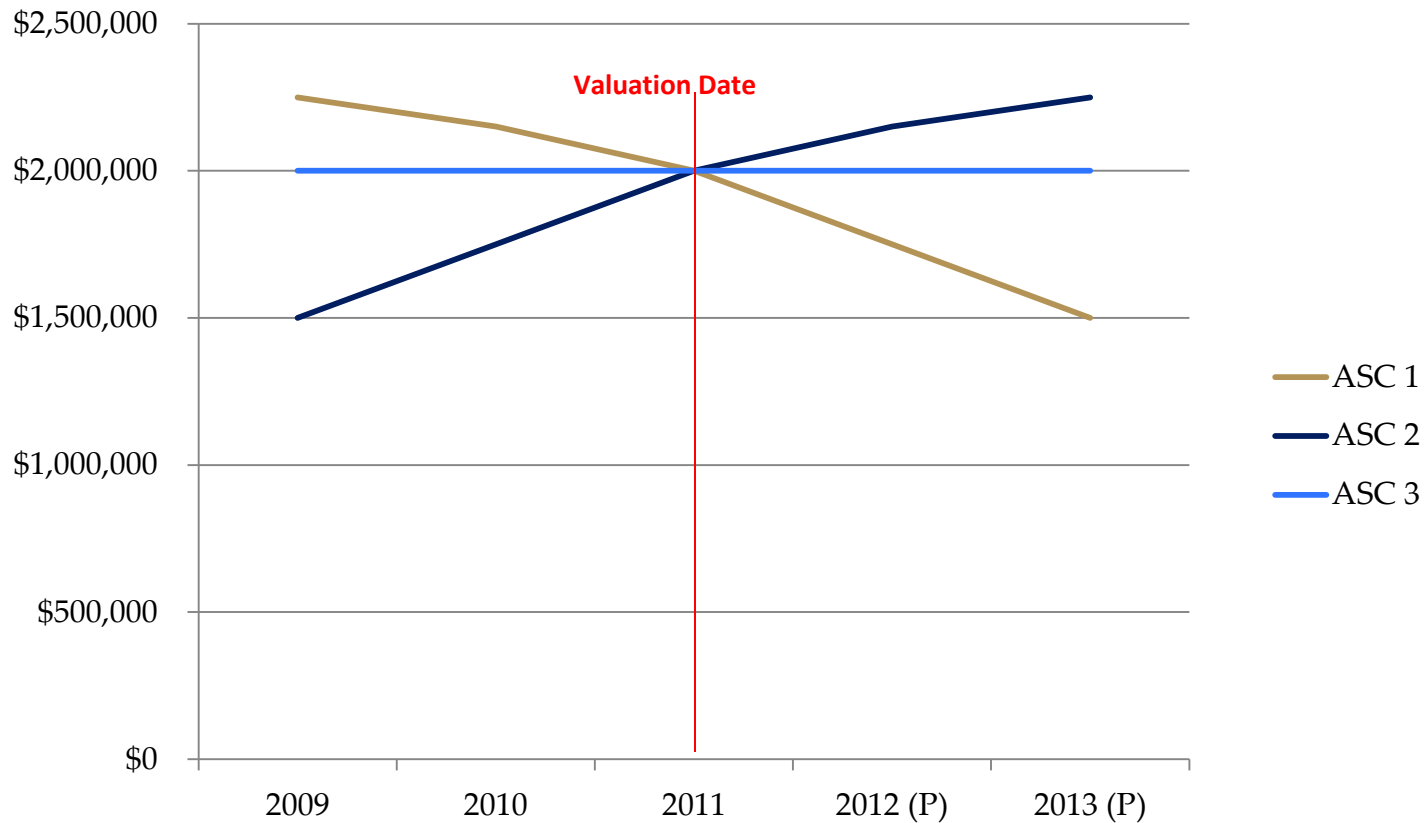
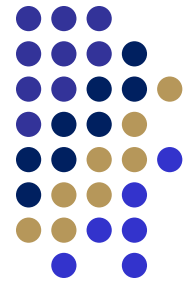
- Where, (K) represents the rate of return (risk), and
- (G) represents the growth rate of the earnings stream

What are Valuation Multiples?

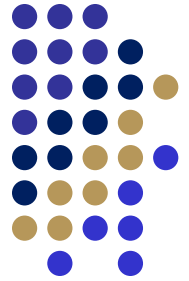


	<u>Varying Growth</u>			<u>Varying Risk</u>		
	<u>Scen 1</u>	<u>Scen 2</u>	<u>Scen 3</u>	<u>Scen 1</u>	<u>Scen 2</u>	<u>Scen 3</u>
k	17.0%	17.0%	17.0%	17.0%	19.0%	22.0%
g	2.0%	3.0%	4.0%	2.0%	2.0%	2.0%
Multiple	6.67	7.14	7.69	6.67	5.88	5.00

Three ASC's with \$2.0M EBITDA

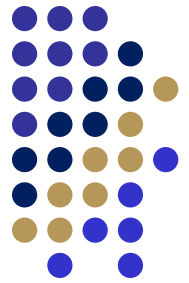


Valuation 101



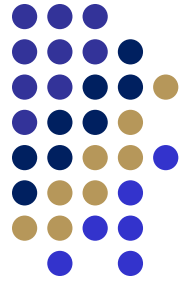
- **Asset or Cost Approach** – A general way of determining a value indication of a business, business ownership interest, or security using one or more methods based on the value of the assets net of liabilities.
- When and why?

Minority vs. Majority Control



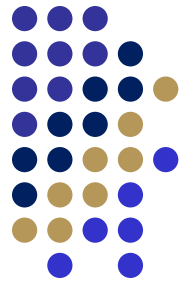
- Interests providing absolute control (*e.g.*, greater than a 50% interest) are worth more than interests which do not have the same control rights.
- Control granted by the governing documents. Examples include:
 - Major equipment purchases and investments
 - Debt signing authority
 - Admitting new owners
 - Granting physician privileges

Do's and Don'ts



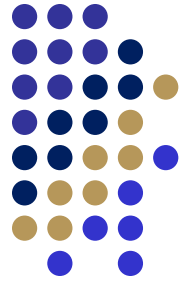
- In connection with a hospital's 100% acquisition of an ASC, can we consider overlaying hospital's fee structure onto valuation?
- If a new surgeon who has not done any (or a material amount) of cases is looking to buy in, should you include his/her cases in connection with valuing the interest?
- An ASC has done a poor job on collecting from Medicare; can we factor billing improvements into our valuation?
- An ASC experienced a one-time material adverse event in the most recently completed year. Can we ignore for purposes of valuation?
- An ASC is looking to buy out one investor at \$X and sell an interest to a new investor at 75% of \$X.
- Assume a hospital want to buy an ASC for purposes of shutting it down. Impact to value?
- Others?

Value Enhancers/Detractors



- Enhancers
 - Multispecialty (diversification of case types)
 - Diversification of surgeons – majority of cases not done by a single surgeon
 - High % of cases performed by owners who are “motivated” to continue working
 - An established history of continually seeking new owners
 - History and expectation of continued distributions
 - Growth in cases and earnings; reimbursement growth less certain
 - Little debt over time
 - Barriers to entry (*e.g.*, CON)
 - Predominantly in network with Commercial payors
 - Others

Value Enhancers/Detractors



- Detractors (opposite of previous slide)
 - Reliance on single specialty (not always)
 - Lack of diversification of surgeons – majority of cases done by a single surgeon
 - High % of cases performed by non-owners
 - Little vision on extending center life cycle
 - Lack of distributions or lack of consistency in distributing cash flow
 - No growth or loss in volume, revenue
 - Excessive debt
 - Predominantly out-of-network with Commercial payors
 - Others?

History, Purpose & Limitations of the Survey

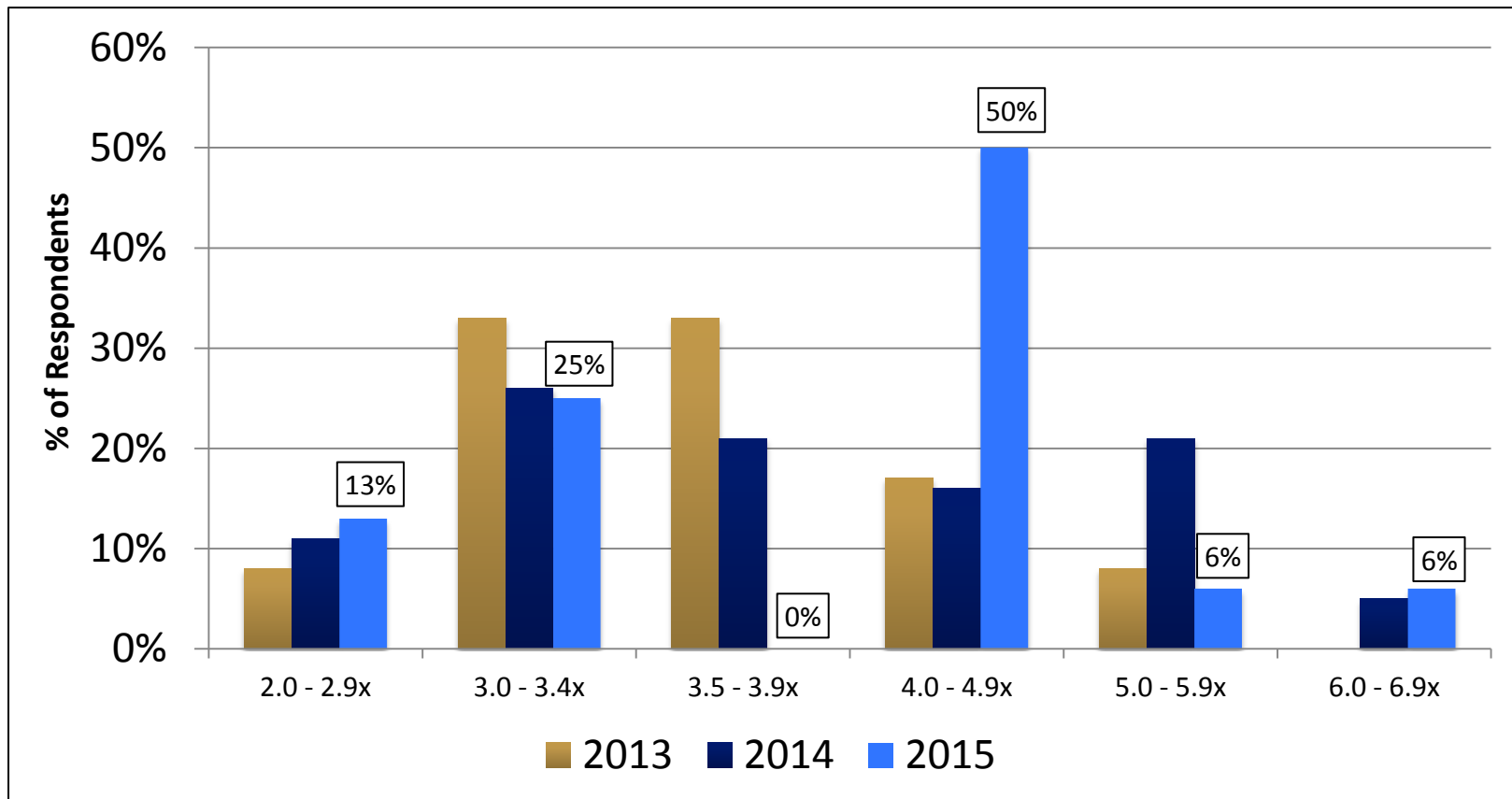


- Since 2003, HAI has published 11 annual ASC surveys
- Why? To provide a centralized source of market intelligence on valuation trends within the ASC industry.
- 2015 - 21 companies/industry players responding
- *Disclaimer: Survey should not be used in lieu of a formal valuation.*

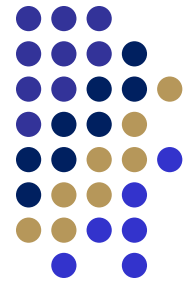
Observed Multiples for Minority Interests



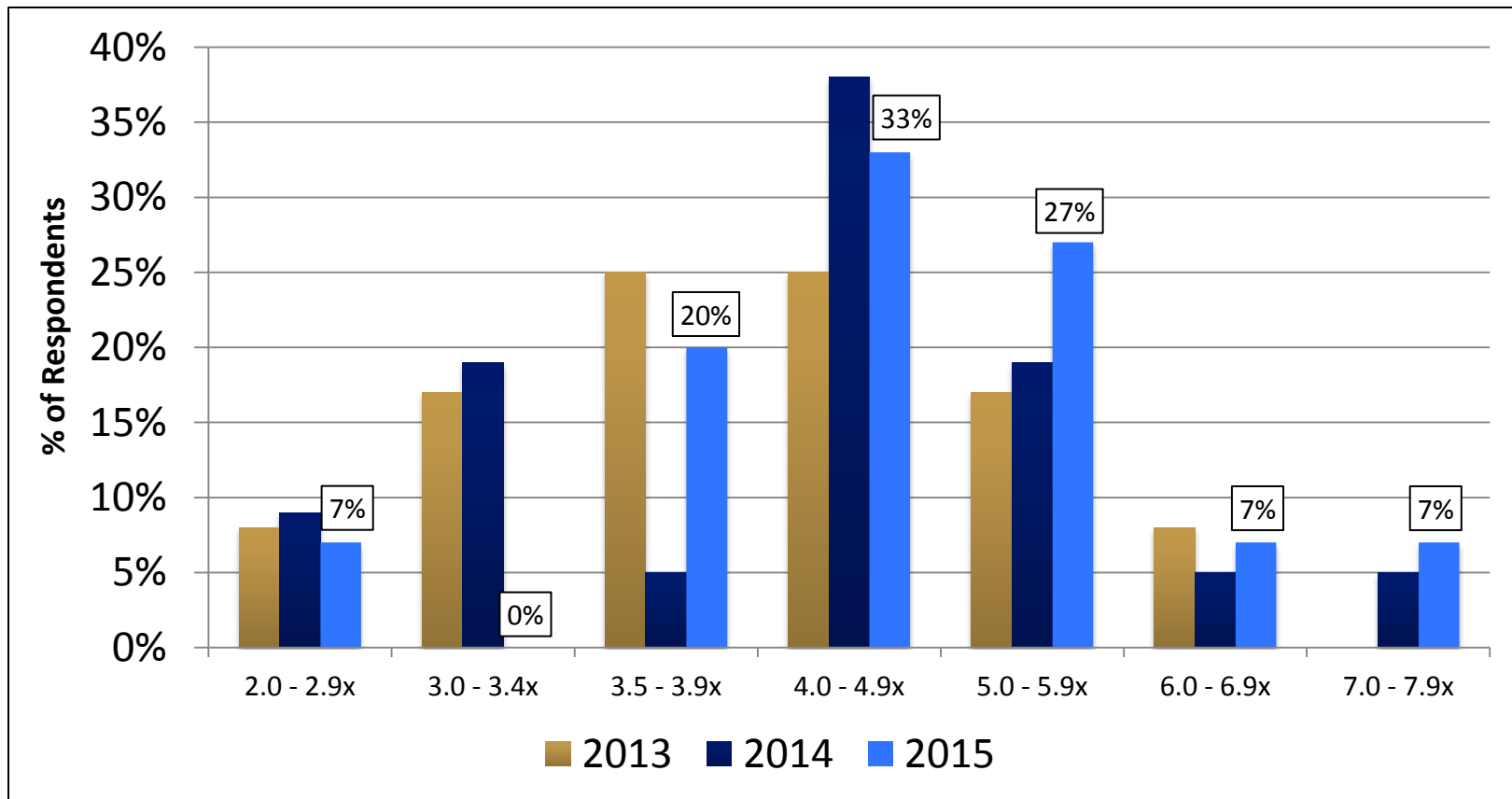
Single-Specialty Centers



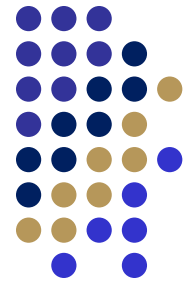
Observed Multiples for Minority Interests



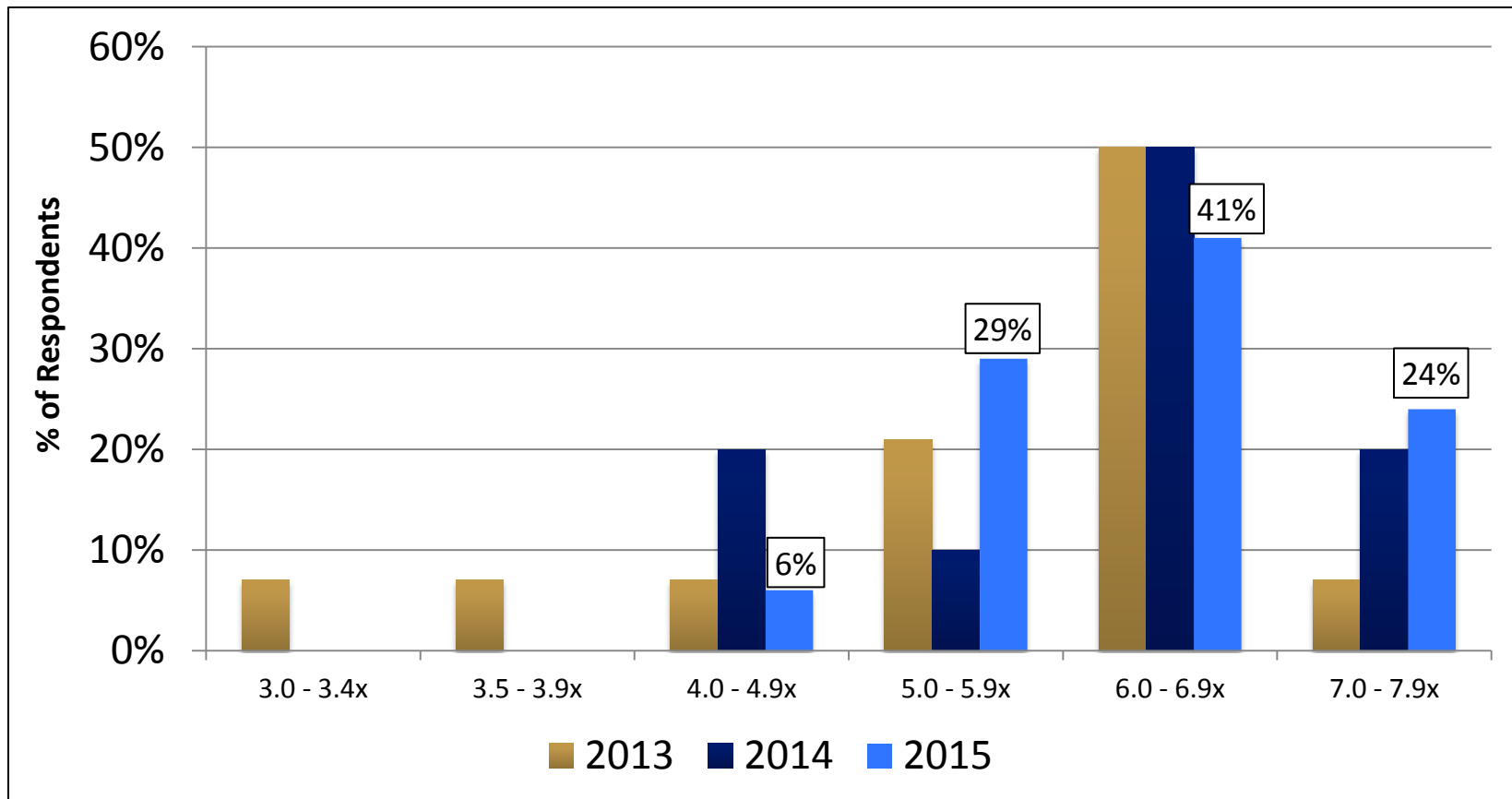
Multi-Specialty Centers



Observed Multiples for Controlling Interests



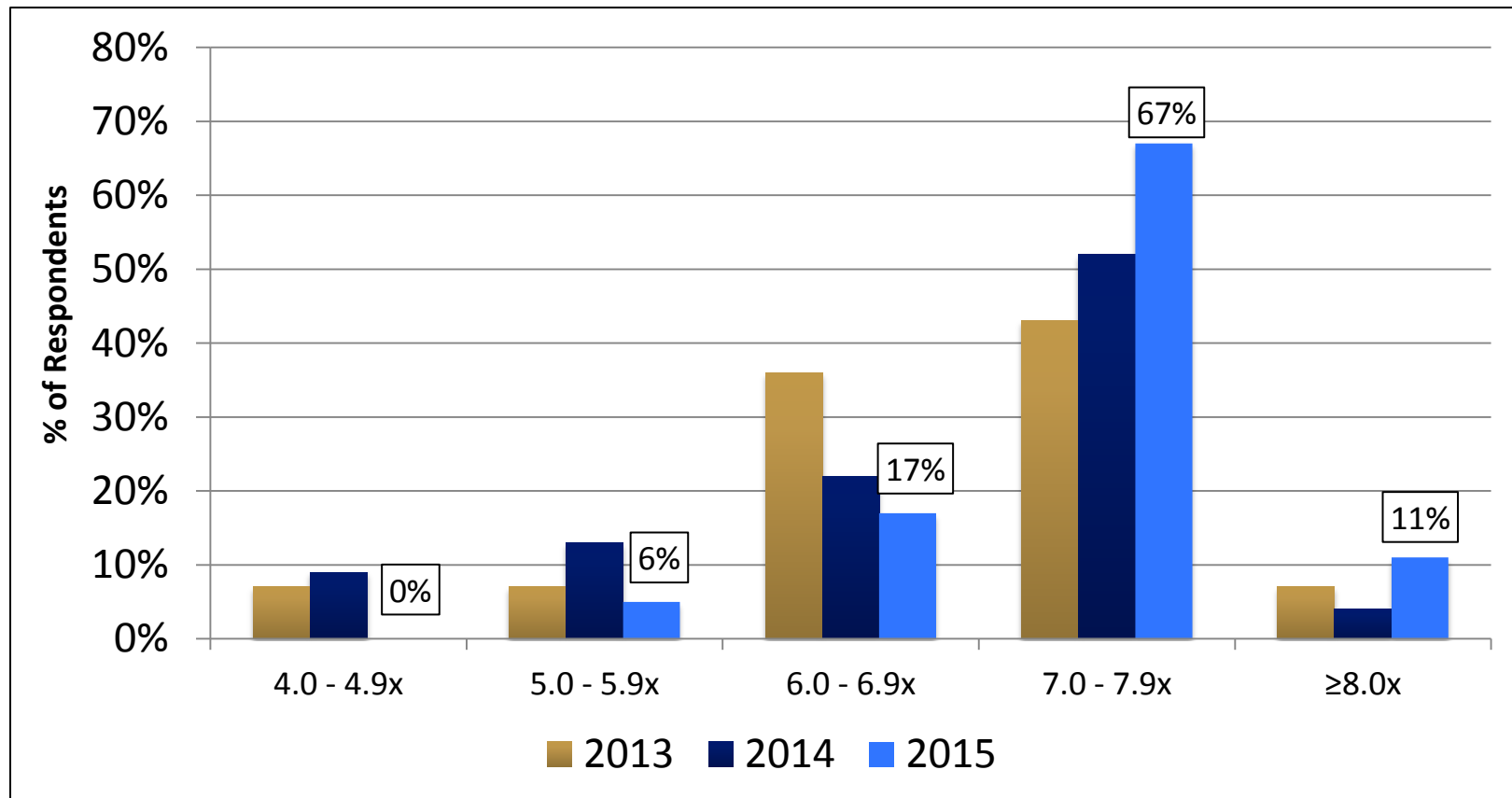
Single-Specialty Centers



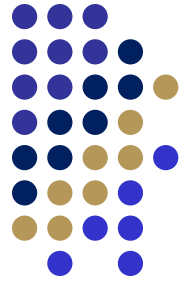
Observed Multiples for Controlling Interests



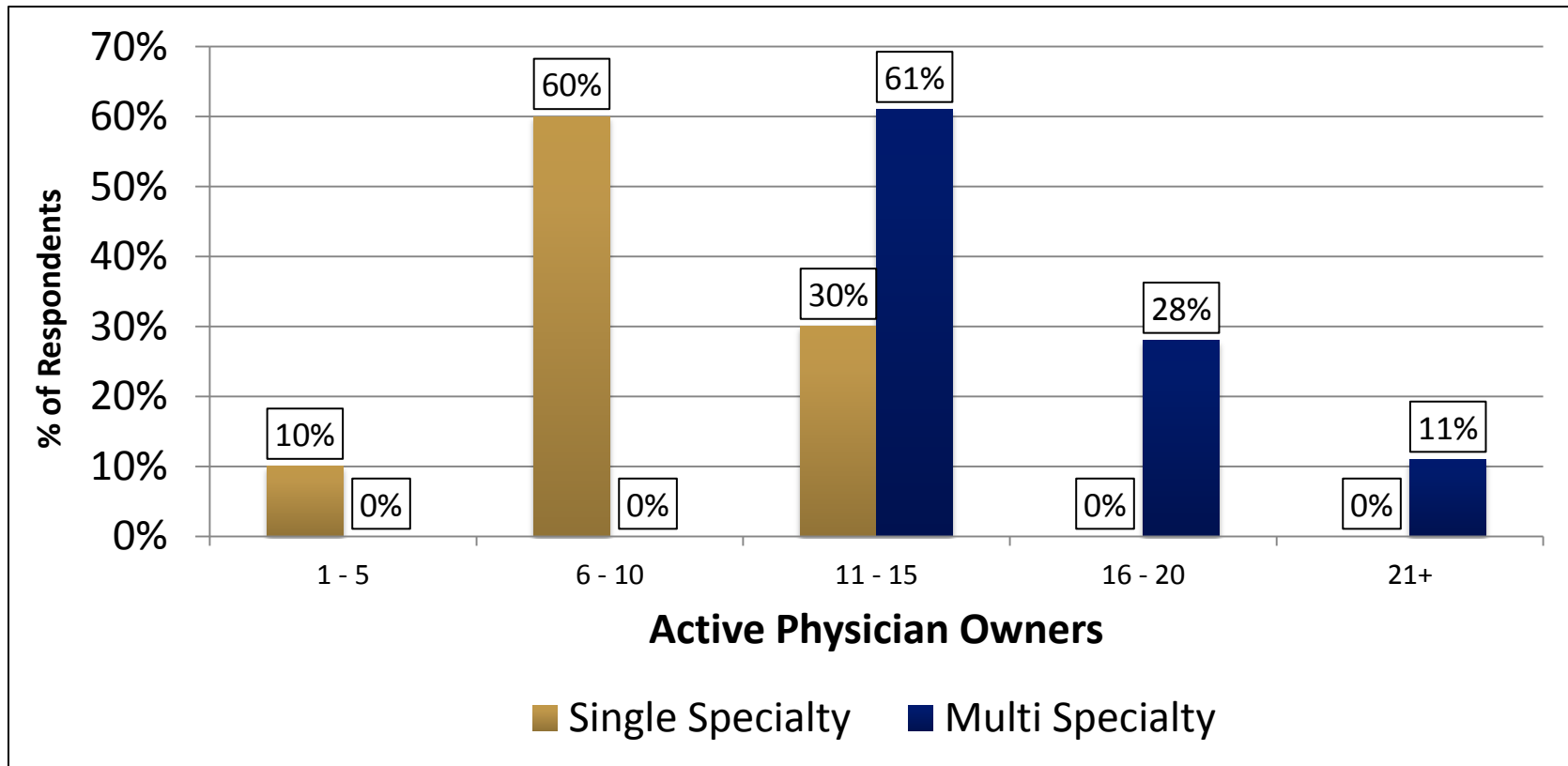
Multi-Specialty Centers



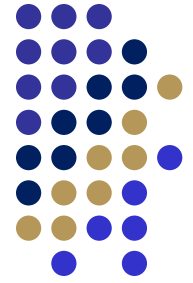
Buyer Expectations



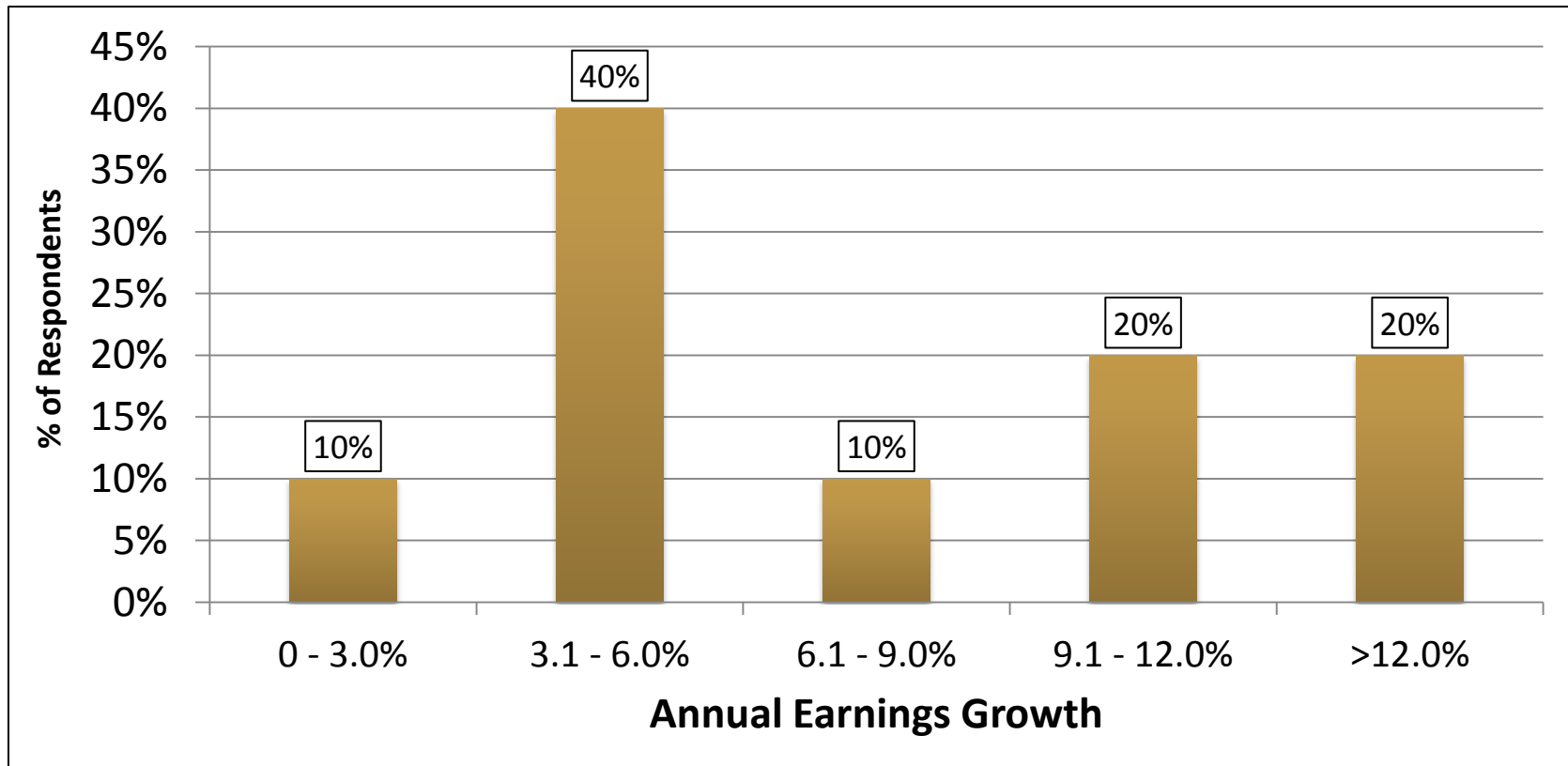
Preferred Number of Active Physician Owners



Buyer Expectations



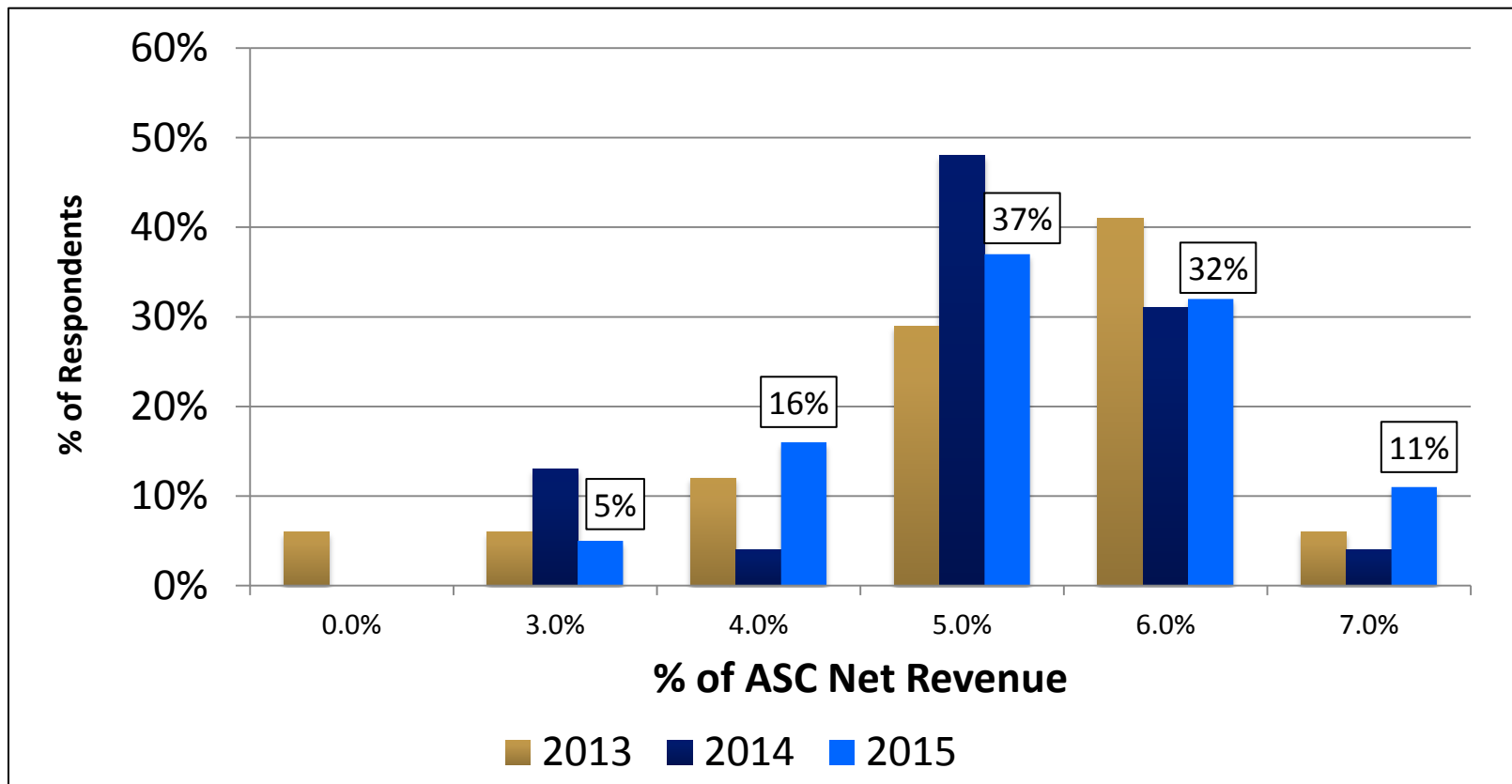
Initial Earnings Growth Expectations Post-Transaction



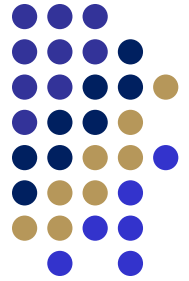
ASC Management Services



ASC Management Fee Rates



ASC Management Services



ASC Management Fee Rates

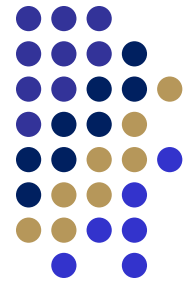
- Competitive trends
- 50% have *minimum* management fees
 - 72% of those report minimum fee of \$100K to \$300K
- 40% have sliding scale management fees whereby fees decline after a predetermined threshold
 - 50% of those report declining management fee rates between \$5.0M and \$9.9M in ASC net revenues

ASC Management Services

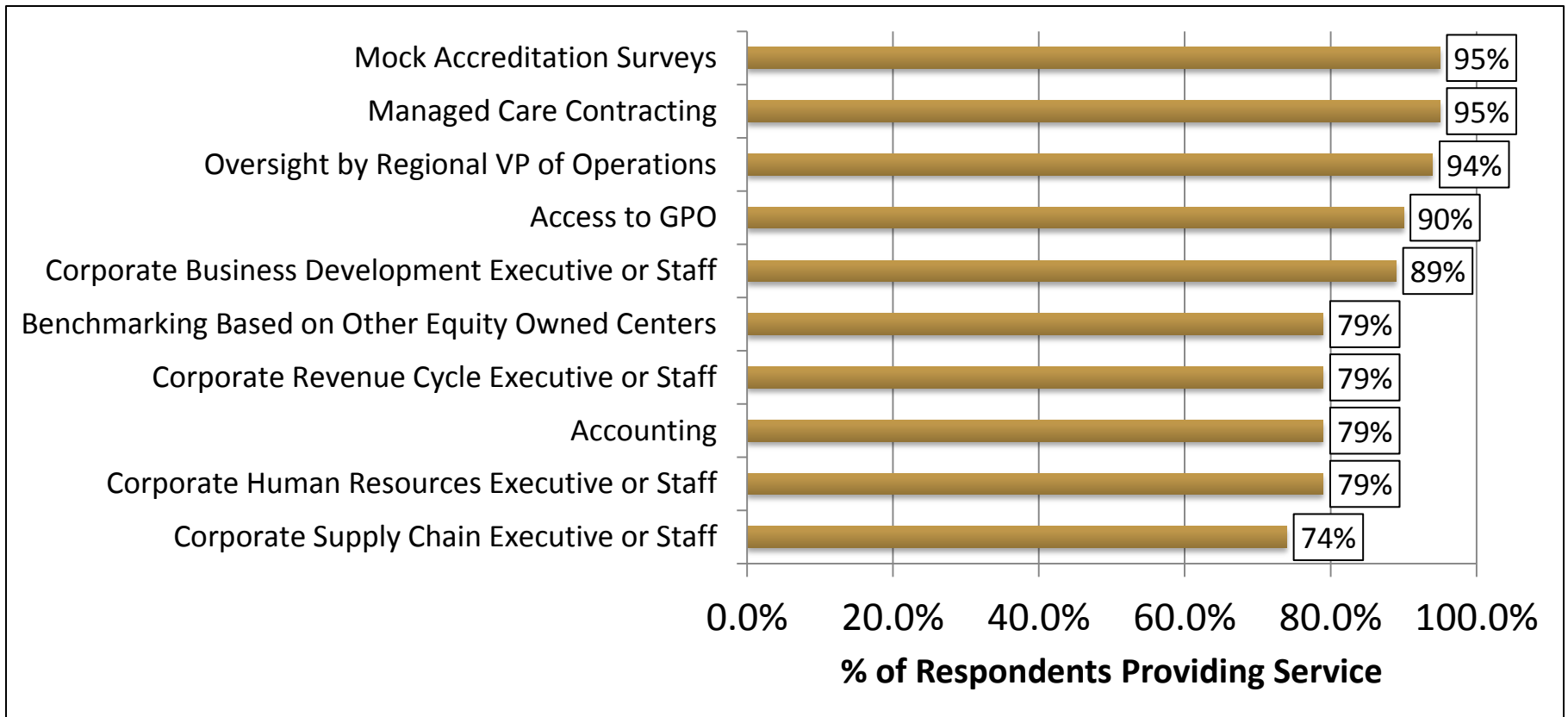


- 85% report no management arrangements with fees at risk for performance
- 68% report holding ownership in all managed ASCs

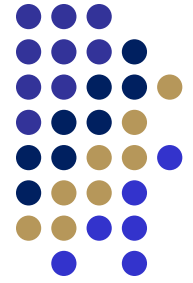
ASC Management Services



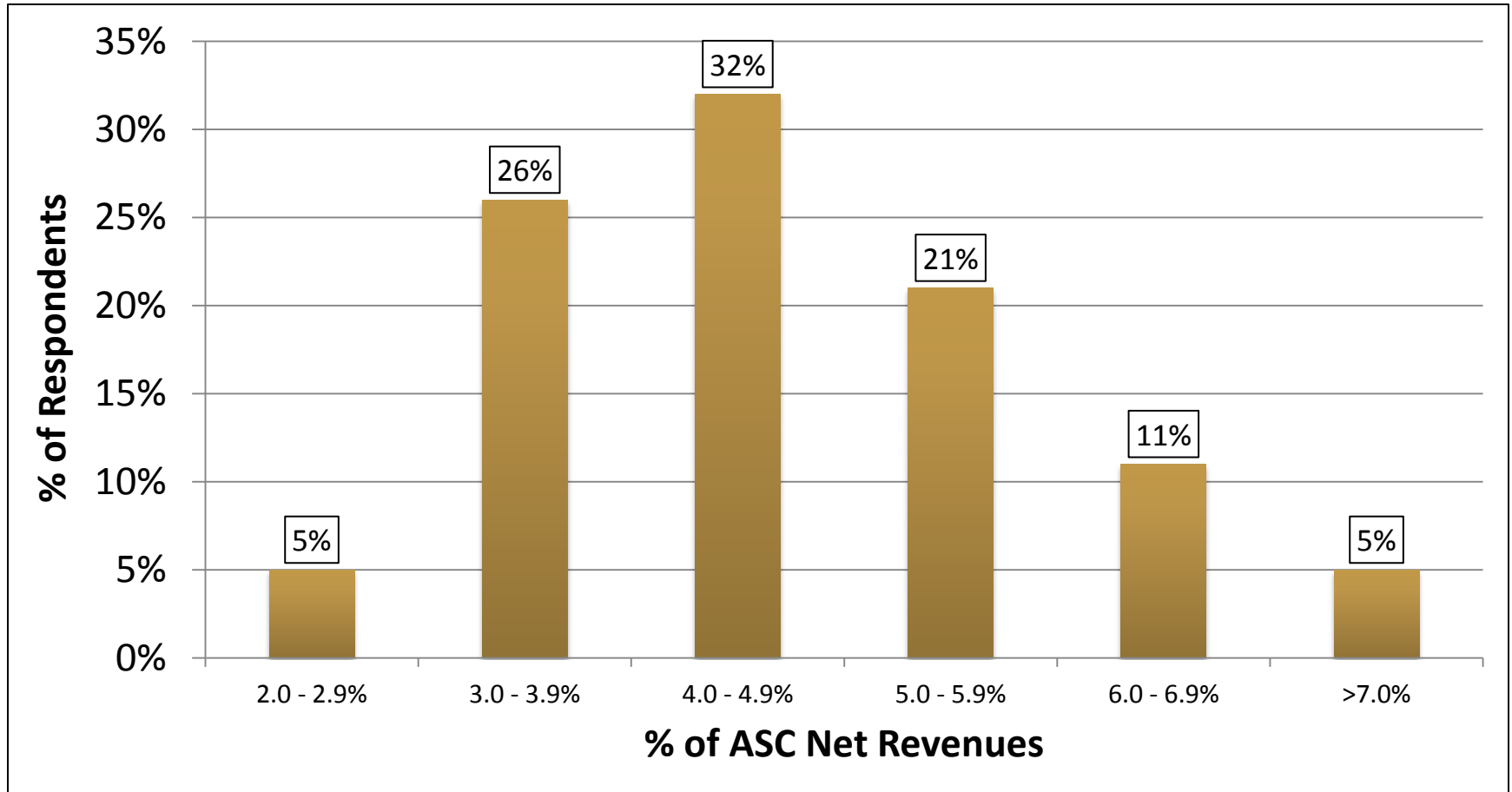
Services Often or Always Provided as Part of ASC Management Fee

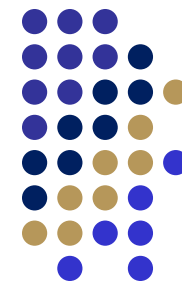


ASC Billing



ASC Billing Fees





QUESTIONS?

Valuing ASCs and Recent Trends in ASC Transactions

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