

How Do You Value Your ASC For Sale?

Vincent M. Kicodrillo, CFA, AVA
Partner – VMG Health

Jon O' Sullivan
Senior Partner – VMG Health

2515 McKinney Avenue, Suite 1500 • Dallas, Texas 75201 • Telephone: 214.369.4888 • Fax: 214.369.0541
3100 West End Avenue, Suite 940 • Nashville, Tennessee 37203 • Telephone: 615.777.7300 • Fax: 615.777.7301
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Presentation Overview

- I. Current Market Observations
- II. ASC Transaction Market
- III. Valuation Issues

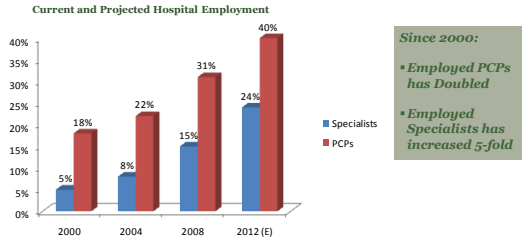
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Current Market Analysis

- Observing a Maturation of the ASC Industry
- Economic Downturn / Sluggish Recovery Continues to Impact ASC Volumes
- Significant Managed Care & Medicare Reimbursement Pressure
- Uncertainty Regarding Healthcare Reform's Long-Term Impact on ASCs

Current Market Analysis

New Competition: Growth in Hospital Employment



Current Market Analysis

What to Expect in a Mature Industry Environment?

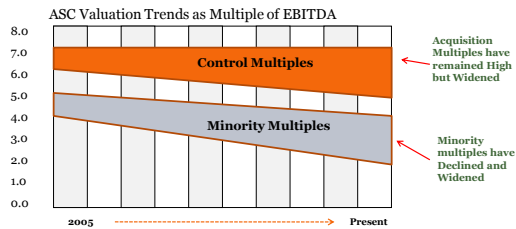


ASC Transaction Market

ASC Acquisition Market – Who are the Buyers?

- ASC Management Companies – Expanding Market Presence
- Acute Care Hospitals – On the rise
- Other ASCs – Consolidation Strategies
- Physician Owned Hospitals – Niche Expansion Strategy

ASC Transaction Market



❖ Key Takeaway - All ASCs are Not Created Equal with Respect to Valuation Multiples

ASC Transaction Market

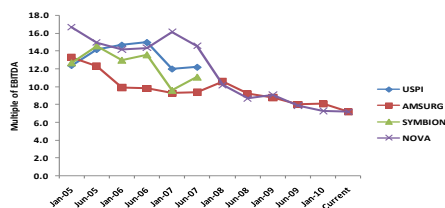
➤ Demand for Acquisitions is High

- Need for ASC Management Companies to Exhibit Growth
- Diminished Ability to do Pursue Growth through De Novo Development
- Market Consolidation Strategies are being Pursued Aggressively
- Hospitals are Joining Management Companies in the Buyers Market

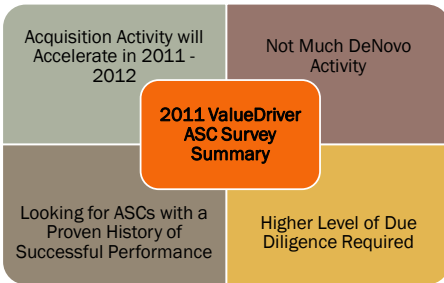
ASC Transaction Market

➤ However Buyers are Cautious

- Buyers are Keenly Aware of the Challenges facing ASCs
- Diminished Value from the Public Market



ASC Transaction Market



A Valuation Primer

How Do You Value an ASC For Sale?

Three Methods of Valuation:

- Discounted Cash Flow Analysis (Income Approach)
- Market Multiple Analysis (Market Approach)
- Asset Analysis (Cost Approach)

Two Primary Drivers of ASC Value:

- Future Cash Flow (Distributions)
- Volatility or Risk related to Future Cash Flow
 - Revenue and Expense Analysis

Risk Factors and Value

The value of minority shares is lower than control value

Risk factors usually decrease equity share values

Measure "Risk" and "Value" the right way

Maximize the value of shares by managing out Risk

Risk Factors and Value

Market Characteristics

- Health system competition
- Freestanding surgery center competition
- Potential for new centers
- Market demographic growth
- Percentage of physicians with no ASC Investment
- Existence of certificate of need ("CON")
- Managed care barriers
- Facility costs or availability

Risk Factors and Value

Payor Profile

- Revenue contraction by payor
- Percentage of out of network business
- Commercial reimbursement relative to Medicare
- Pending legislation impacting reimbursement

Risk Factors and Value

Physician Utilization

- Specialty mix
- Age dispersion
- Growth history
- Ownership by utilizers in competing centers
- Volume concentration by specialty
- Revenue concentration by specialty

Risk Factors and Value

Physician Ownership

- Percent of revenue produced by owners
- Number of physician owners
- Number of non-physician owners
- Revenue dispersion among owners
- Revenue dispersion among non-owners
- Physician ownership growth and retention

Risk Factors and Value

Facility Attributes

- Location in relation to acute care hospital
- Age and condition of facility
- Facility location sustainability
- Capital equipment obsolescence

Risk Factors and Value

Efficiency

- Relative staff efficiency
- Relative supply cost efficiency
- Existence of labor unions
- Geographic cost index

Definitions

Control Interest

- o Generally, greater than 50% interest in the ASC
- o The right to manage the facility
- o The right to make decisions on many issues
- o Not subject to repurchase provisions

Minority Interest

- o Generally, less than 50% interest in the ASC
- o No management authority
- o No decision making authority
- o Subject to repurchase provisions

Standards of Value...

Control or Majority Equity Level Value:

- o Typical for Hospital or Management Company Buy-in
- o Higher Valuation (think 5.0X – 7.0X)
- o Premium value related to rights and privileges of majority owner (management control, distributing level & timing, capital structure decisions, admission of new investors, etc.)
- o Buyer establishes new operating agreement with terms desired by the buyer

Minority Equity Level Value:

- o Typical for Physician Buy-in
- o Lower valuation, typically <4.5x EBITDA
- o Discounted value due to lack of specific control, rights and privileges that are available to the majority owner

Determining Physician Buy-in Price

How is physician buy-in calculated?

- o Pre-determined valuation multiple (stipulated in partnership operating agreement)
- o Independent Fair Market Value Opinion

A pre-determined multiple can be dangerous!

- o Pre-determined multiple often based on trailing financial performance
- o Future growth or risk factors must be considered
- o In today's ASC environment, future performance will not likely mirror past performance

Victims of Their Own Success

- Successful Past Performance = Expensive Buy-in
 - Valuations based solely on past performance may overstate ASC value
 - Self-fulfilling prophecy – Inability to attract new investment will result in deteriorating performance
 - ASC Partnerships have life cycles which mirror the physician investors
- What's the Solution?
 - Buy-in value must be forward looking
 - Buy-in value must consider all risks inherent in that ASC
 - Valuation must consider the actual terms related to the security interest

Summary

- Increased Hospital involvement in the ASC Industry
- Industry Participants should Expect Reduced Reimbursement
- Completely Independent ASCs will have Greater Risk Exposure
- As a Low Cost Provider, ASCs will Have a Place at the Table

QUESTIONS

Vincent M. Kickirillo, CFA, AVA
Partner

Jon O'Sullivan
Senior Partner

