Healthcare industry update.

Current Trends in Mergers & Acquisitions
HFMA Kentucky Chapter – January 23, 2014
Introductions

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M&A Transaction Advisory Services
Our Healthcare Service Capabilities

AUDIT & ACCOUNTING
- Audits, reviews, & compilations
- Single audit federal programs/HUD
- Benefit plan audits & consulting

BUSINESS ADVISORY SERVICES
- Enterprise risk services
- Market studies
- Financial feasibility studies
- Financial modeling
- Debt capacity analysis
- Certificate of need
- Valuation
- Due diligence
- Fraud investigations
- Strategic & business planning
- Commercial real estate advisory*
  - Owner representation; site search/evaluation/real estate transactions/
    M&A; existing facility assessment; project planning/implementation;
    occupancy/move-in logistics

REGENCY & ACCOUNTING
- Audits, reviews, & compilations
- Single audit federal programs/HUD
- Benefit plan audits & consulting

SENIOR CARE CLINICAL CONSULTING
- Clinical reimbursement — RUG IV optimization
- Certification/compliance strategies
- Quality assurance programs
- Mock surveys
- Continuing education programs
- Survey turnaround projects
- MDS 3.0 accuracy & compliance
- RAC readiness reviews

OPERATIONS EFFECTIVENESS
- Operations assessments
- Continuous process improvement
- Medicare management reports
- Organization design
- Labor productivity analysis
- Budget analysis by department

FINANCIAL ADVISORY SERVICES
- Wealth management
- Institutional investment consulting*
- Insurance services*
- Trust services*
- Business transition planning

REIMBURSEMENT SERVICES
- Reimbursement analysis
- Rate-setting projections
- Cost reporting
- Benchmarking analysis

TAX
- Entity structure consulting
- Tax planning, preparation, & review
- State & local tax reviews
- Cost segregation studies
- Individual tax planning or compliance

TECHNOLOGY
- Security assurance
- ERP system implementation
- Internal controls review
- Decision support software, installation, & consulting
- Infrastructure assessment, planning, selection, & design
- Software assessment, planning, & selection
- Communications & networking
- Contract negotiations

* These services are provided by Plante Moran affiliates.
Today’s Learning Objectives

This presentation will focus on the following:

✓ Update on Current National and Regional M&A Activity
✓ Key Drivers Behind Recent M&A Activity
✓ How to Identify and Respond to Key Risks and Opportunities
✓ How to Identify and Quantify Potential Costs and Cost Savings
✓ Post Transaction – External Auditor Key Considerations
✓ Case Studies in Managed Care
Recent Hospital Merger News

Community Health Systems of Tennessee and Health Management Associates of Florida will combine – *The New York Times*

Tenet Healthcare Corp. acquires Vanguard Health Systems – *Modern Healthcare*

Highmark and West Penn Allegheny Health System – *Becker Hospital Review*

Trinity Health and Catholic Health East complete merger – *Crain’s Detroit Business*

Baylor Health Care System and Scott & White Healthcare form largest non-profit in Texas – *Becker Hospital Review*

Mount Sinai and Continuum Health Partners – *Becker Hospital Review*
Recent Hospital Merger News in Kentucky

KentuckyOne Health to Manage All But Reproductive Care at University of Louisville Hospital – *Becker Hospital Review*

Jewish Hospital, St Mary’s HealthCare and Saint Joseph Health System merge – *www.chausa.org*

Clark Memorial, Norton merger still in works – *www.newsandtribune.com*

Baptist Health acquires Trover Health System – *www.modernhealthcare.com*

Hospital chains keep getting bigger – *The Washington Post*
Healthcare Services


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What Do You Think is Driving Hospital M&A?
Drivers Behind Mergers and Acquisitions

- Affordable Care Act
- Economies of Scale
- Access to Physicians
- Sustaining Growth
- Declining Net Revenue per Patient
- Payor Transparency
- Access to Capital
- Increased Regulation
- EHR Pooling of Resources
- Increased Bargaining Power with Suppliers
- Increased Competition
Drivers Behind Mergers and Acquisitions

**AFFORDABLE CARE ACT**
- Where Does Organization Fit in the Care Continuum?
- Sophistication of Executive Team and Core Service Leaders
- Impact on Strategy and Ability to Execute Strategy
- How Do You Plan to Transition to the New System of Delivery?
- Population Management
- Meaningful Use
- ICD-10
- Triple Aim – Increase Access to Care, Improve Quality, and Decrease Costs
- Bundled Payments
- Consumer Driven Healthcare
- Sequester/Changes in Reimbursement
- Readmissions
Drivers Behind Mergers and Acquisitions

**ECONOMIES OF SCALE**
- Commercial Contract Negotiation
- Impact on Employers and Patients with Insurance
- Revenue Cycle
- Cost Savings Synergies
- Labor Productivity
- Supply Chain/GPOs
- Blood Bank
- Malpractice Insurance
- Information Technology

MERGERS and ACQUISITIONS
Drivers Behind Mergers and Acquisitions

ACCESS TO PHYSICIANS

- Expand Service Capabilities
- Referral Flow
- Population Management
- Leadership Capabilities
- Physician Alignment
- Community Needs Assessment
Drivers Behind Mergers and Acquisitions

SUSTAINING GROWTH

- Out-Migration
- Referral Flow
- Population Management
- Medicaid Expansion
- Community Needs Assessment
- Number of Baby Boomers reaching Medicare eligible or dual eligible status

MERGERS and ACQUISITIONS
Drivers Behind Mergers and Acquisitions

DECLINING NET REVENUE PER PATIENT

- Shift from Inpatient Setting to Outpatient Setting
- Reimbursement Cuts/Sequestration
- Health Insurance Exchanges
- Payor Mix
- Downstream Revenue
- RAC
- Readmissions
- Not All Declines Are Bad (Service/Value)

MERGERS and ACQUISITIONS
Drivers Behind Mergers and Acquisitions

ACCESS TO CAPITAL

• Key Performance Indicators
• Days Cash on Hand
• Leverage Ratios
• Age of Plant
• Facility Cap Ex Spend
• IT Cap Ex Spend
• Historical Financial Results
• 3 to 5 Year Forecast
Drivers Behind Mergers and Acquisitions

INCREASED REGULATION

- Accountable Care Organizations
- Health Insurance Exchanges
- Reimbursement Cuts
- Penalties for Non-Compliance or Poor Performance
- Critical Access Hospital Designation
- Need to Increase Lobbying Efforts
Drivers Behind Mergers and Acquisitions

EHR POOLING OF RESOURCES

- Software and Equipment Costs
- Access to Appropriately Trained Technical Resources
- Future Lease/Maintenance Commitments
- Staff Required to Support EHR
- Staff Required to Support IT Function Overall
- Ability to Reinvest Capital
Drivers Behind Mergers and Acquisitions

**INCREASED BARGAINING POWER WITH SUPPLIERS**

- Blood Bank
- Medical Supplies
- Nutrition Services
- Equipment Vendors

MERGERS and ACQUISITIONS
Drivers Behind Mergers and Acquisitions

- Outpatient Clinics
- Population Management
- Kroger/Walmart “Little Clinics”
- Push for Transparency
- Board Pressure
Areas of Opportunity & Risk

- Access to Care/Ability to Adjust Referral Patterns
- Volume/Productivity
- Downstream Revenue
- Payer Mix
- Payer Contract Analysis
- Market Knowledge
- Operational/Clinical Compliance
- Revenue Cycle
- Cost Reporting/RAC
- Service Line Profitability
- Compensation and Benefits
- Supply Chain
- Malpractice Coverage
Consider Taking a Deeper Dive

Managed Care Contracts Deserve a Closer Look

✓ Engage a trusted advisor
✓ Identify common significant payers and high volume procedures
✓ Compare gross charges and net payments at DRG and CPT code level for similar facilities
✓ Compare fee schedules at the CPT code level
✓ Consider how long it will take to negotiate new rates
✓ Determine potential impact managed care contracts will have on your system post-transaction
✓ Downstream revenue impact
Consider Taking a Deeper Dive

Nail Down Compensation Plans

✓ Physician productivity (before and after)
✓ Fee schedules (before and after)
✓ Payer mix (before and after)
✓ Figure out special compensation packages in advance – what does the financial picture look like under lower than expected volume and reimbursement?
✓ Do staff compensation models align?
✓ Is there a gap between the target’s physician and staff benefits and your benefits?
✓ Physician alignment is key
Consider Taking a Deeper Dive

Identify Cost Synergies

- Labor productivity
- FTE needs
- Professional services
- Malpractice insurance
- Purchasing power for blood products, general supplies, nutrition services, information technology
Consider Taking a Deeper Dive

Will Future Cap Ex Be Required?
✓ Electronic Health Records
✓ Computers and Servers
✓ Telephone Systems
✓ New Facility or Additional Space
Other Areas For Consideration

• Culture
• Joint Venture, Partnerships, Affiliations, and Collaborations of Target Entity
• Waste in System
• Domestic Utilization
• Valuation
• Financial Forecasts
• Taxation
• Legal
Post Transaction – External Auditor Key Considerations

✓ Valuation/Appraisal
✓ Purchase Price Allocation
✓ Accounting Guidance
✓ Timely Communication
Managed Care Case Study – Potential Health System Acquisition

Target Background

☑ Large Rural Health System/Lightly Affiliated with Large Regional Competitor of Potential Buyer

☑ Medicare/Medicaid Leaning Patient Mix with Declining Net Revenue and Income from Operations

☑ Limited Access to Physicians and C-Suite Turnover

☑ Limited Access to Capital/Delayed Capital Expenditures

☑ 3 Payers Make Up 80 Percent of Commercial Payments
Managed Care Case Study – Potential Health System Acquisition

Key Considerations/Observations

- Expected Managed Care Gain (Loss)
- Incremental Impact on Downstream Revenue
- Business Risk Related to Lightly Affiliated Competing Health System
- Ability to Negotiate with Payers
- Local Employer and Community Response
Managed Care Case Study – Potential Physician Practice Acquisition

**Target Background**

- Large Primary Care Leaning Physician Practice
- Clinical and Academic Responsibilities
- Commercial Leaning Patient Mix
- Cash-basis Financial Statements
- Limited Access to Capital
- Option to Merge/Affiliate with other Health System which competes directly with Potential Buyer
- 3 Payers Make Up 90 Percent of Commercial Payments
Managed Care Case Study – Potential Physician Practice Acquisition

Key Considerations/Observations

✓ Expected Managed Care Gain (Loss)
✓ Provider-based Ancillary Revenue Impact
✓ Incremental Impact on Downstream Revenue
✓ Ability to Negotiate with Payers
✓ University Response
Things to Consider for the Future

✓ Taking on More Risk
✓ Decrease in Volume Due to High Deductible Plans
✓ Increased Co-Payment Issues
✓ Quality Payments
✓ Reduced Network (Physician and Hospital) Sizes
✓ Price Transparency
Questions?

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