

HOW DO ASC COMPANIES ASSESS VALUE?

# 2017

ASC  
VALUATION  
SURVEY

HealthCare Appraisers  
INCORPORATED



# EXECUTIVE SUMMARY

We are pleased to announce the results of HealthCare Appraisers' 2017 ASC Valuation Survey. Since 2003, HealthCare Appraisers, Inc. has surveyed the ambulatory surgery center (ASC) industry to determine trends in the value and characteristics of ASC ownership interests and management fees charged to ASCs. Twenty-four respondents, representing well over 700 surgery centers throughout the country, responded to this year's survey. The following summarizes highlights of the 2017 ASC Valuation Survey.

## TRANSACTION ACTIVITY

During 2016, our respondents were actively searching for potential acquisitions to grow the amount of ASCs under ownership. 17% of respondents have 11 to 30 ASCs under ownership, and 26% of respondents have 31 or more ASCs under ownership.

Respondents indicated significant levels of acquisition activity in the ASC space, with 41% reporting the acquisition of between one and five centers, 9% reporting the acquisition of between six and 10 centers, and 10% reporting the acquisition of 11 or more centers in 2016. 41% of respondents did not acquire an ASC in 2016.

For 2017, acquisition activity is expected to remain high, as 43% of our respondents plan to purchase between one and five ASCs, 26% plan to purchase between six and ten ASCs, and 9% plan to purchase 16 or more ASCs. 22% of respondents are not planning to purchase over the next 12 months.

## VALUATION MULTIPLES AND METHODOLOGIES

When purchasing a minority interest in a single-specialty ASC, 50% of the respondents reported prevailing valuation multiples of 4.0 to 4.9 times EBITDA, while 22% reported higher valuation multiples ranging from 5.0 to 6.9 times EBITDA, and 28% reported lower valuation multiples ranging from 2.0 to 3.9 times EBITDA.

When purchasing a controlling interest in a single-specialty ASC, 78% of the respondents reported prevailing valuation multiples of 6.0 to 7.9 times EBITDA, while 23% reported lower valuation multiples ranging from 4.0 to 5.9 times EBITDA.

**These valuation multiples are reasonably consistent with the 2016 survey in which 73% of respondents reported valuation multiples of 6.0 to 7.9 times EBITDA when purchasing controlling interests in single-specialty ASCs, while 27% reported lower valuation multiples ranging from 4.0 to 5.9 times EBITDA.**

When purchasing a minority interest in a multi-specialty ASC, 63% of the respondents reported prevailing valuation multiples of 4.0 to 5.9 times EBITDA, while 12% reported higher valuation multiples ranging from 6.0 to 7.9 times EBITDA, and 25% reported lower valuation multiples ranging from 2.0 to 3.9 times EBITDA.

When purchasing a controlling interest in a multi-specialty ASC, 75% of the respondents reported prevailing valuation multiples of 7.0 to 7.9 times EBITDA, while 25% reported lower valuation multiples ranging from 4.0 to 5.9 times EBITDA.

**These valuation multiples are consistent with the 2016 survey in which 72% of respondents also reported valuation multiples of 7.0 to 7.9 times EBITDA when purchasing controlling interests in multi-specialty ASCs, while 23% reported lower valuation multiples ranging from 4.0 to 6.9 times EBITDA.**

A majority of respondents are willing to pay a premium for an ASC with a certificate of need (CON). 69% of respondents would pay a premium of 0.26 to 1.0 to the typical multiple. For 71% of respondents, out-of-network revenue at 20% of the ASC's total revenue would exceed the risk tolerance as a viable investment. However, we note that 10% of respondents do not have a risk threshold with respect to out-of-network ASCs. In valuing out-of-network ASCs, of those respondents who would reduce the valuation multiple, 57% of respondents would reduce the typical multiple by greater than 2.0. 68% of respondents report they utilize an adjusted pricing model by converting revenue to reflect in-network rates and then modeling the ASC's adjusted EBITDA multiplied by unadjusted market multiples.

## ASC CHARACTERISTICS

70% of respondents prefer between six and fifteen physician owners for a single-specialty ASC. 81% of respondents prefer between 11 and 20 physician owners for a multispecialty ASC.

From an equity standpoint, our respondents' preferred ownership varied, with 14% of respondents reporting they prefer less than 10% ownership, 43% of respondents reporting they preferred between 11% and 50% ownership, and 43% of respondents reporting they preferred between 51% and 75% ownership.

When determining purchase price for minority interest transactions with new or existing physician investors, 50% of respondents use a formula, and 32% of respondents obtain an independent FMV appraisal to determine value.

When selling a minority interest to new physician investors, 55% of respondents reported an average period of three to six months to consummate a sale. When selling a controlling interest in an ASC, 56% of respondents reported an average period of six months to one year to consummate a sale. 50% of respondents report they have sold a controlling ASC interest to a hospital/health system.

48% of respondents expect 3.1% to 6.0% earnings growth per year during the first several years post transaction, while 19% of respondents expect greater than 12% earnings growth per year in the first several years post acquisition.

## MANAGEMENT FEES

67% of respondents report that their typical management fees range from 5% to 6% of net revenue, while 20% report typical management fees of 3% to 4% of net revenue. 10% of respondents had other types of management fee arrangements.

**These management fees are reasonably consistent with the 2016 survey, in which 61% of management fees ranged between 5% and 6%, and 28% ranged between 3% and 4% of net revenue.**

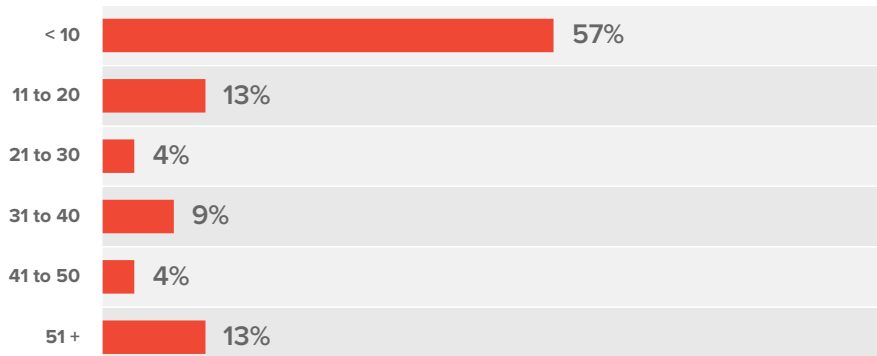
Of the 38% of respondents who reported charging a minimum management fee, 50% indicate that their typical minimum management fee ranges from \$100,000 to \$199,999 per year. Furthermore, 41% of respondents have arrangements whereby the management fee rate varies based on the revenue generated by the ASC (i.e., a sliding scale).

14% of respondents indicated they have management fee arrangements wherein part of their fee is "at risk" for performance metrics, while 86% of respondents indicated they have no "at-risk" management fee arrangements.

57% of respondents observe typical fees for ASC billing and collection services ranging from 4.0% to 5.9% of collections.

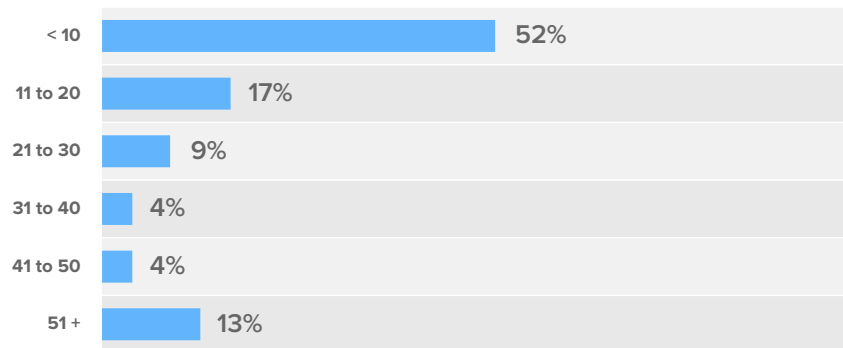
## 01

How many ASCs do you have under ownership?



## 02

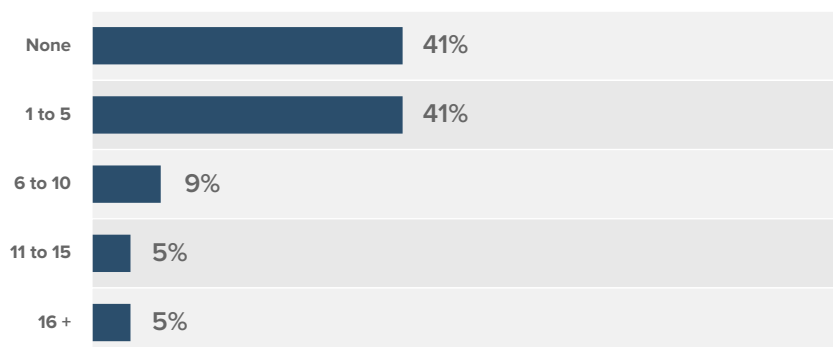
How many ASCs do you have under management?



\* Does not total 100% due to rounding.

## 03

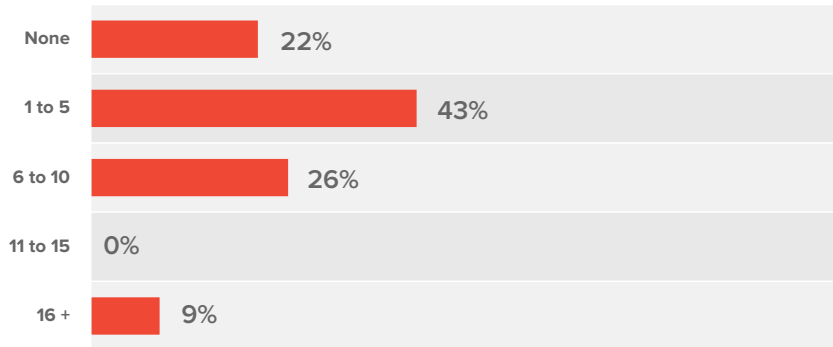
How many ASCs (or ASC interests) did you purchase in the last 12 months?



\* Does not total 100% due to rounding.

## 04

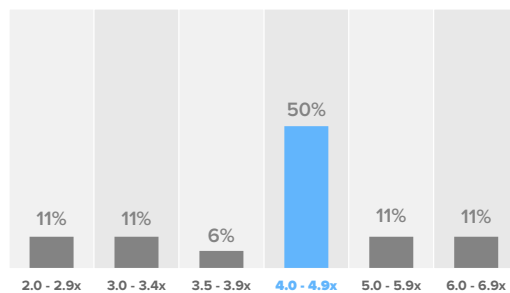
How many ASCs (or ASC interests) do you plan to purchase over the next 12 months?



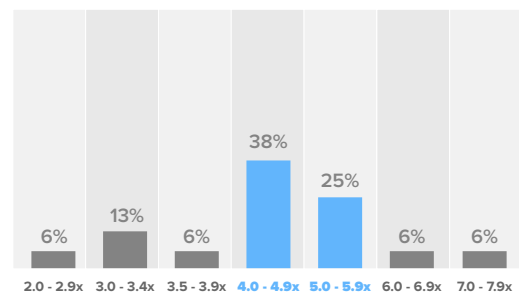
## 05

What valuation multiples have you most typically observed in the marketplace during the past 12 months for predominantly in-network centers?

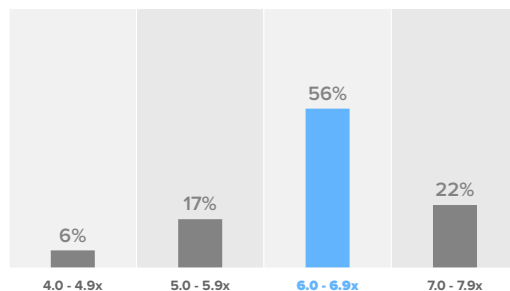
Minority Interest Single Specialty



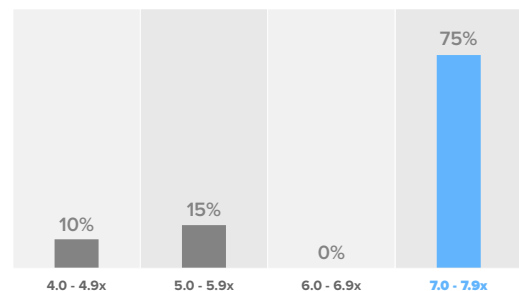
Minority Interest Multi-Specialty



Controlling Interest Single Specialty



Controlling Interest Multi-Specialty

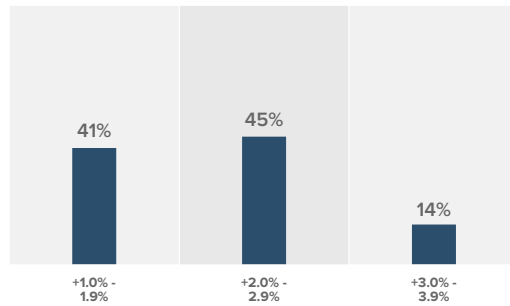


\* Does not total 100% due to rounding.

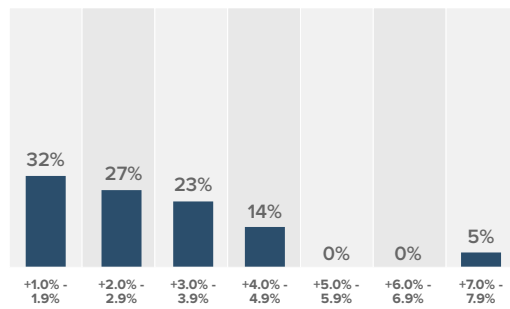
# 06

What is the typical annual change you observe in the ASC market for each of the following items?

### Commercial Payor Rates

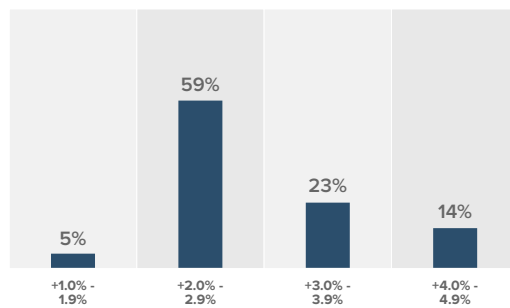


### Medical Supplies and Implantable Device Costs

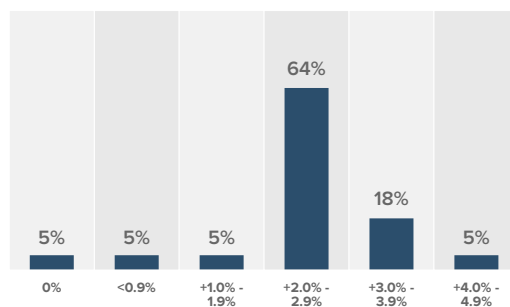


\* Does not total 100% due to rounding.

### ASC Staff Raises



### All Other ASC Expenses

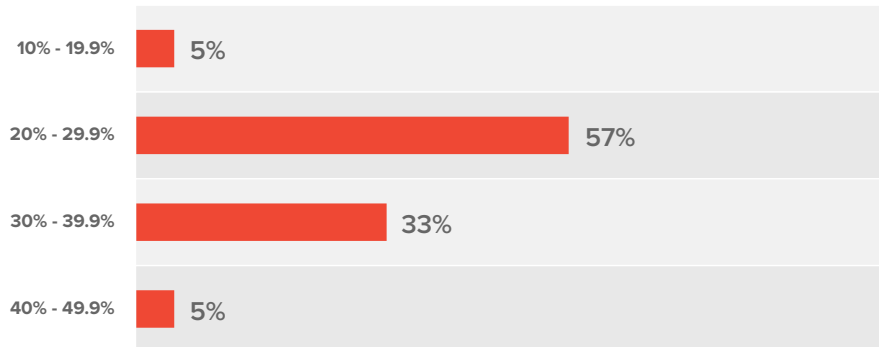




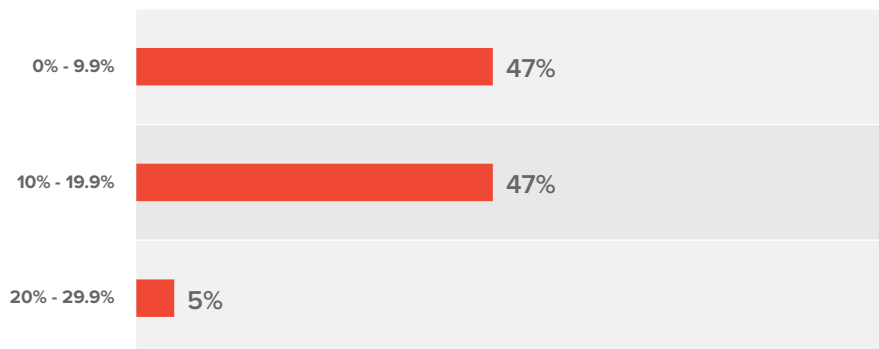
## 07

What percentage of revenue do you observe for the following ASC operating expenses (in-network centers only)?

### Salary and Benefits

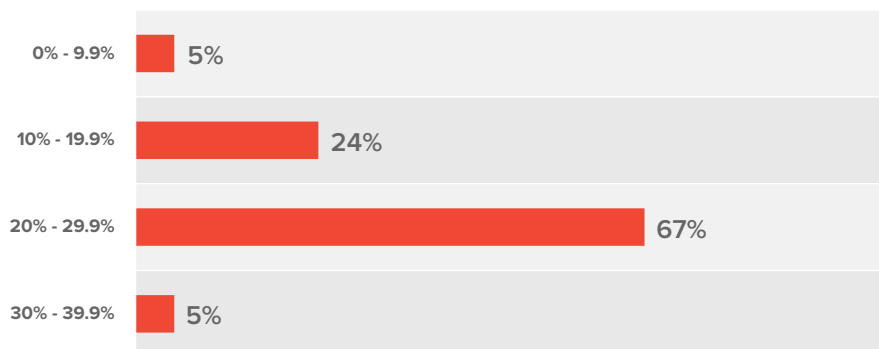


### Occupancy



\* Does not total 100% due to rounding.

### Drugs, Medical Supplies and Implantables

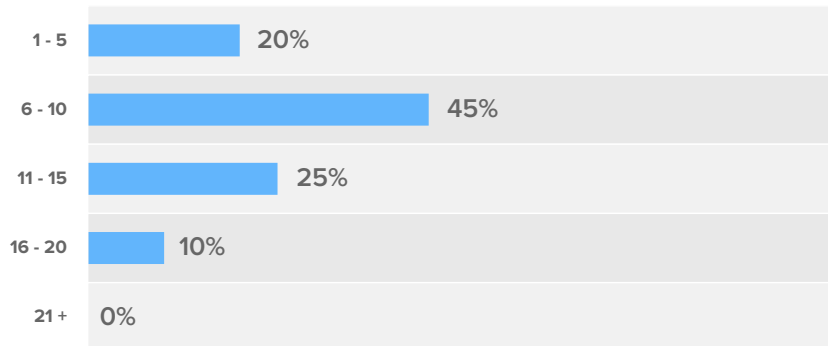


\* Does not total 100% due to rounding.

08

For single-specialty centers, your company generally prefers how many active physician owners?

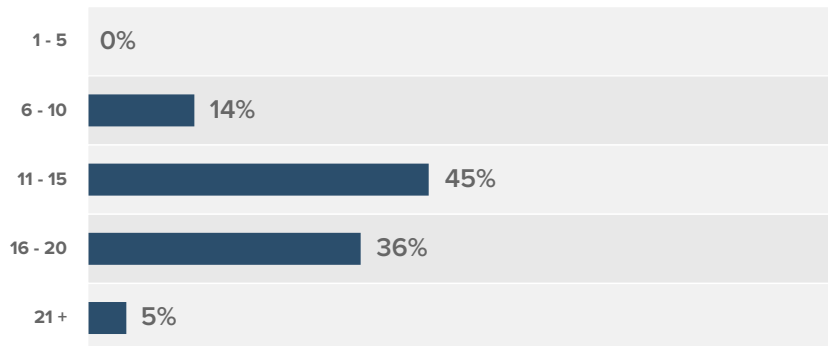
#### Number of Physicians



09

For multi-specialty centers, your company generally prefers how many active physician owners?

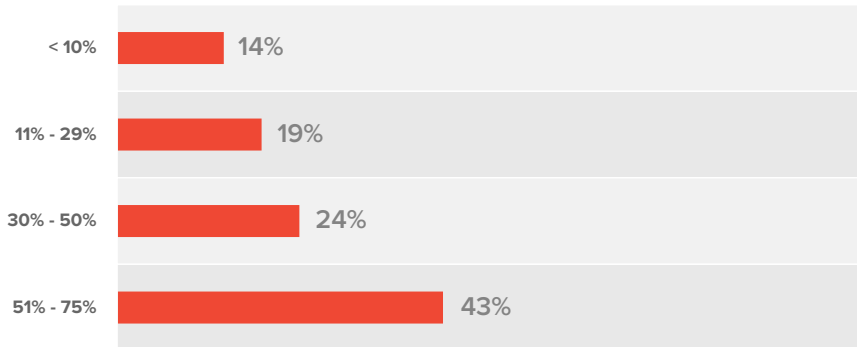
#### Number of Physicians



## 10

From an equity standpoint, your company's preferred ownership is:

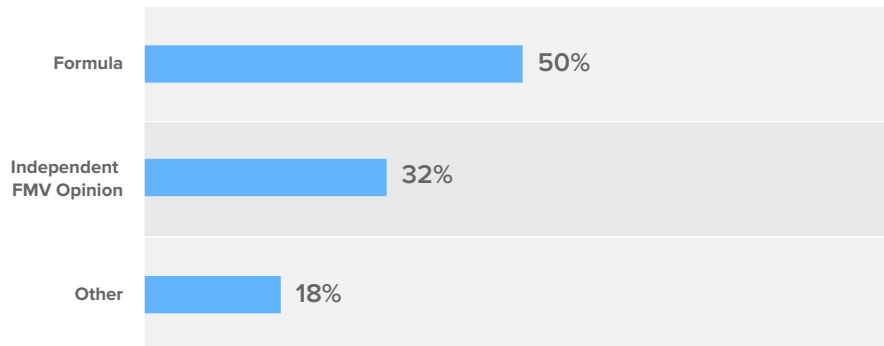
## Ownership



## 11

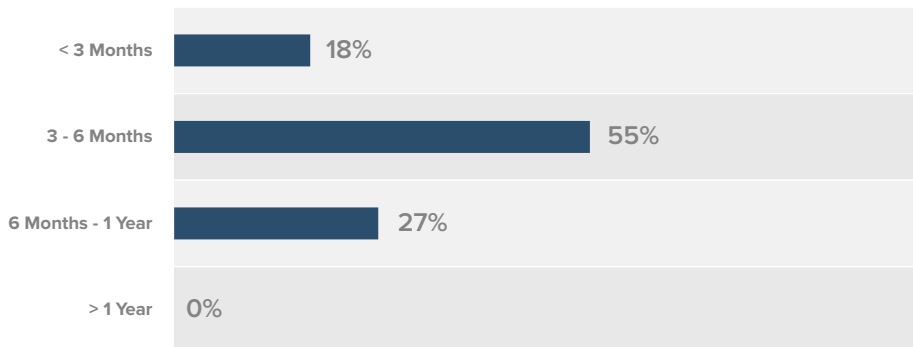
How do you determine the purchase price for minority interest transactions (e.g., new or existing physician investors)?

## Minority Interest Valuation Method



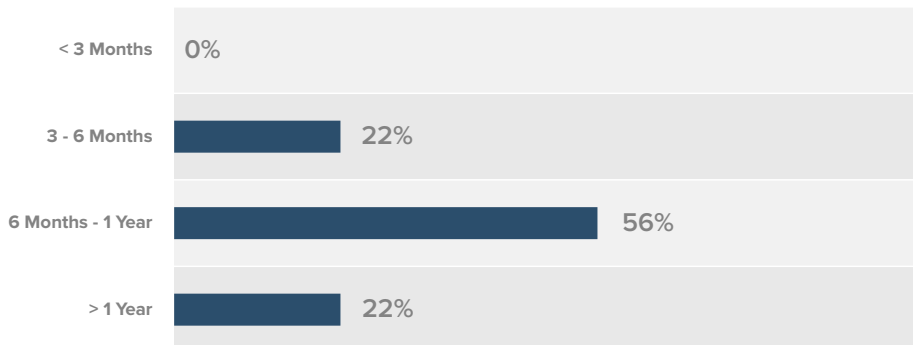
## 12A

When selling minority interests to new physician investors, on average, how long does it take to identify the buyer and consummate the sale?



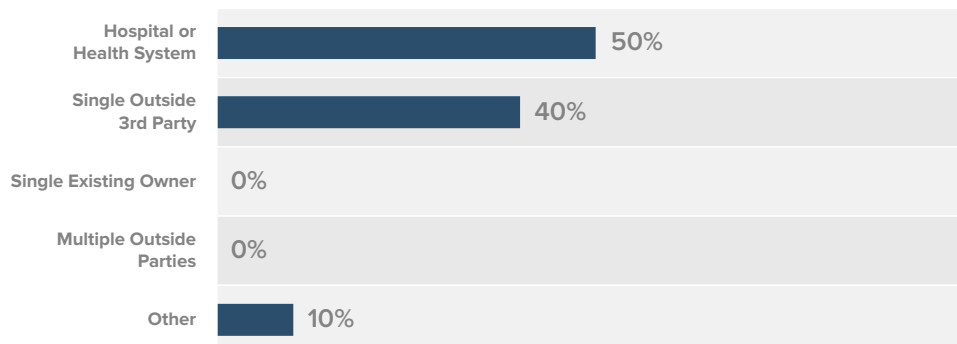
## 12B

If you have sold a controlling interest in a center during the last year, approximately how long did it take to identify the buyer and consummate the sale?



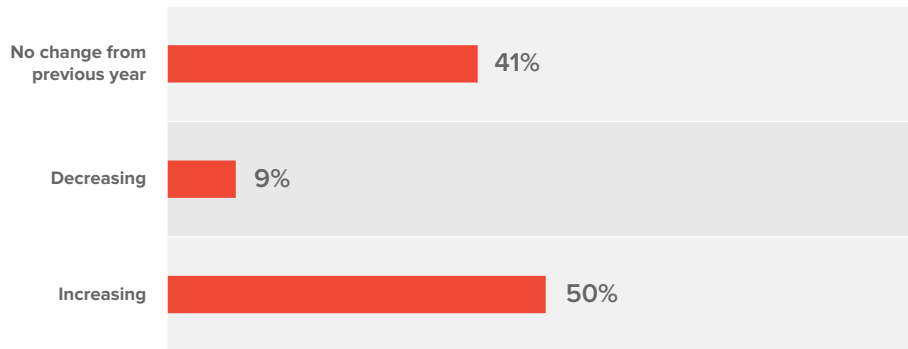
## 12c

If you have sold a controlling interest was the buyer of your interest?



## 13

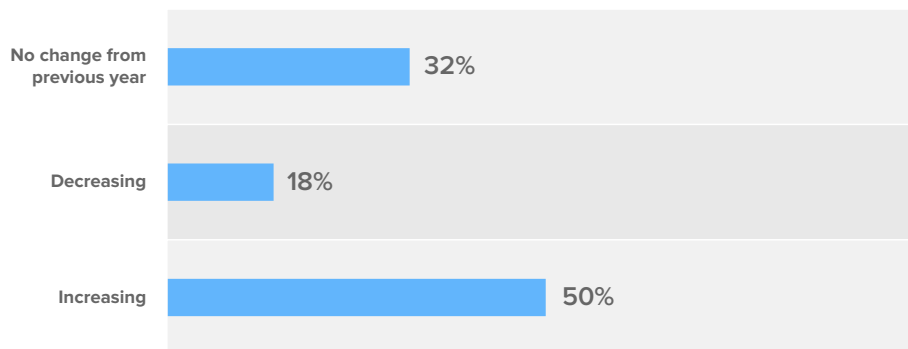
In the past year, what best describes the multiples paid (or considered) by your company?



## 14

In the past year, what best describes your observations in the ASC marketplace related to acquisition activity?

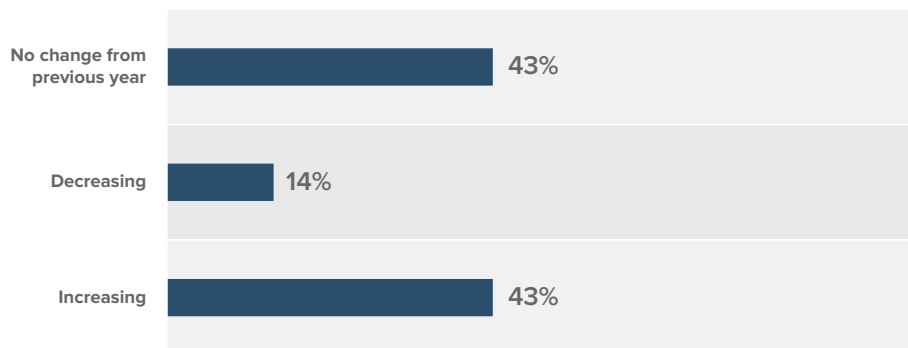
#### Observed Acquisition Activity



## 15

In the past year, what best describes your observations related to competition for acquisitions?

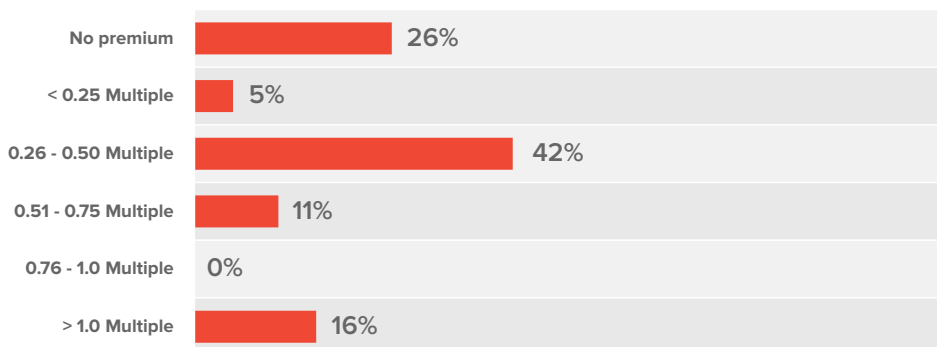
#### Observed Acquisition Competition



## 16

What is the magnitude of the premium paid by your company for a surgery center with a CON?

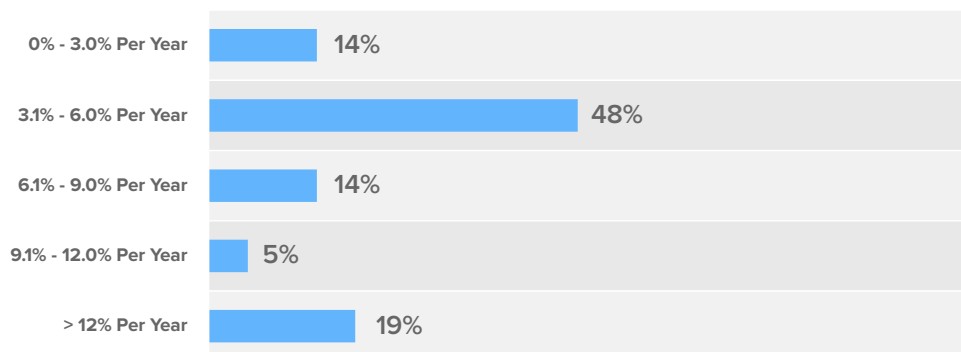
## CON Valuation Multiple Premium



## 17

When evaluating an acquisition target, what level of earnings growth is typically expected in the first several years post acquisition?

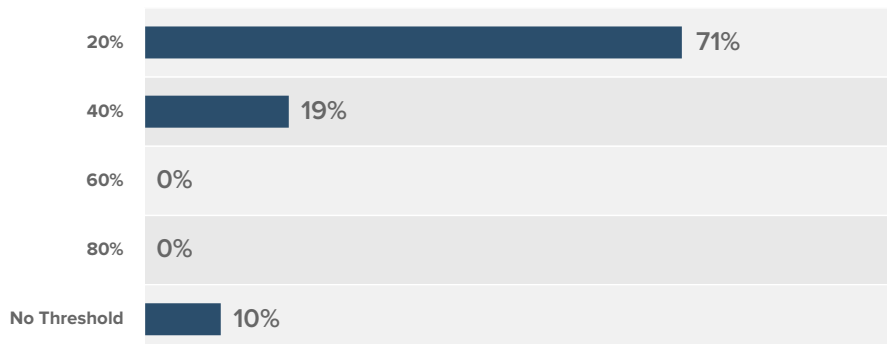
## Initial Growth Expectations Post-Transaction



## 18

At what percentage of total revenue does out-of-network volume exceed your risk tolerance?

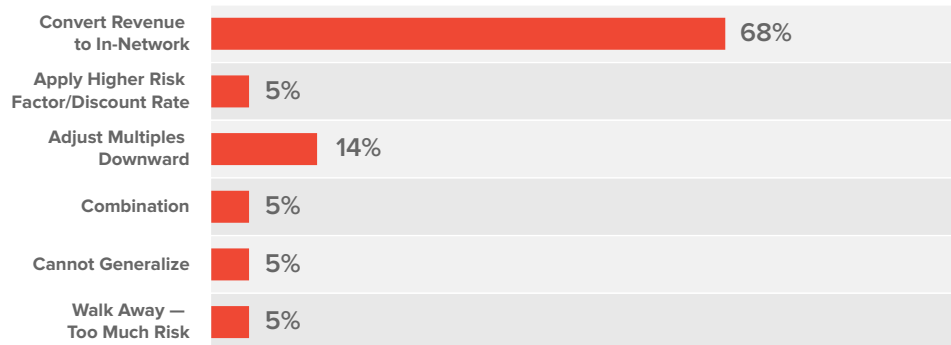
## Out-of-Network Risk Threshold



## 19

How does your company adjust valuation models/pricing for out-of-network centers?

#### Out-of-Network Adjustment Approach

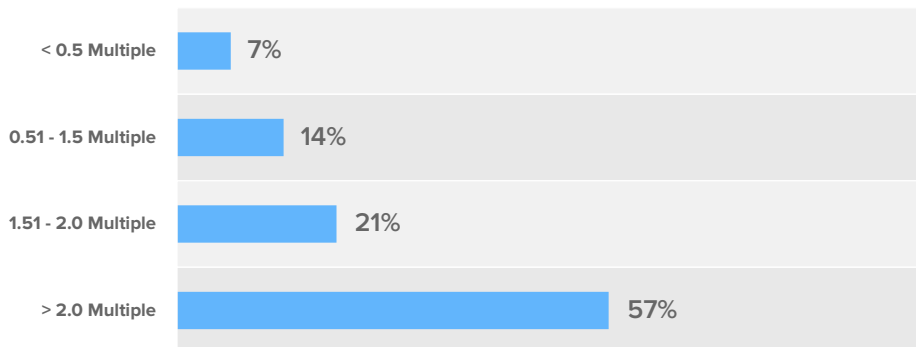


\* Does not total 100% due to rounding.

## 20

If applicable, what is the magnitude of the reduction to the multiple for a center with an out-of-network strategy (i.e. the center generally is not contracted with any commercial payors)?

#### Out-of-Network Multiple Adjustment

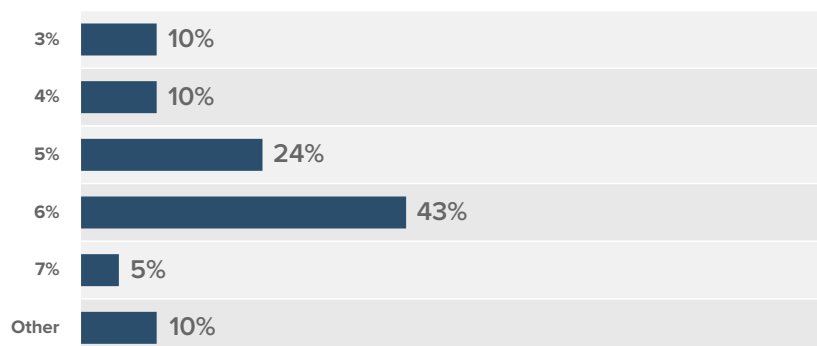


\* Does not total 100% due to rounding.

## 21A

What is the typical management fee rate your company charges for ASCs (% of net revenue)?

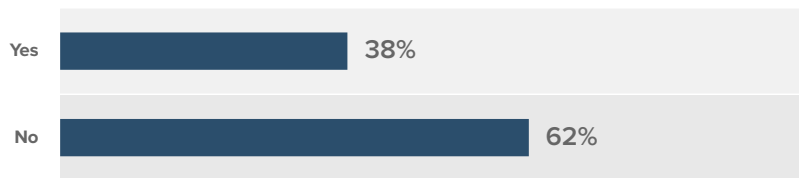
#### Typical ASC Management Fee



\* Does not total 100% due to rounding.

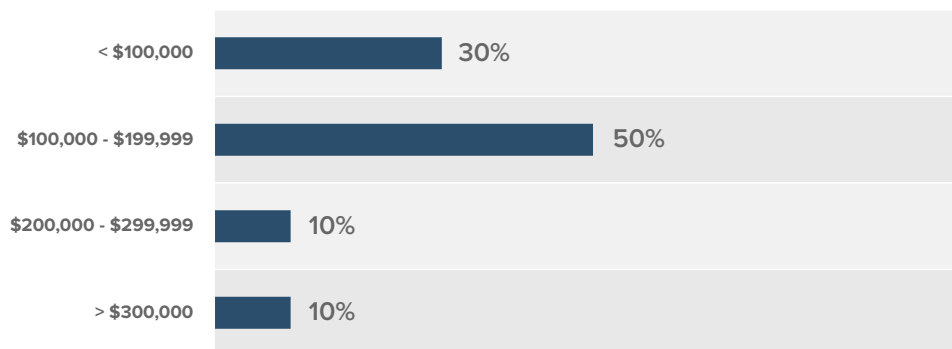
## 21B

Do you have a minimum annual management fee?



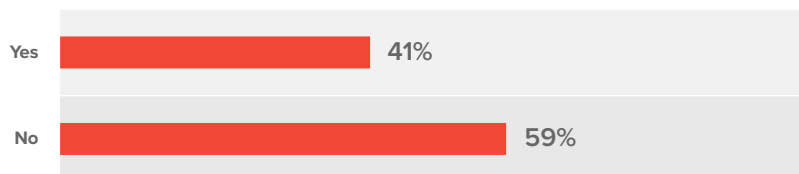
## 21c

If “yes”, what is the typical annual minimum management fee that you charge?



## 22A

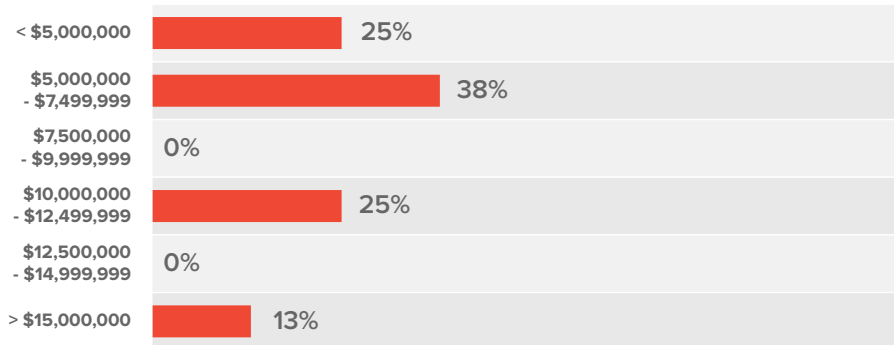
Do you have any ASC management arrangements wherein the management fee charges vary based on the revenue levels of the surgery center (i.e., do you use a sliding scale)?





22<sup>B</sup>

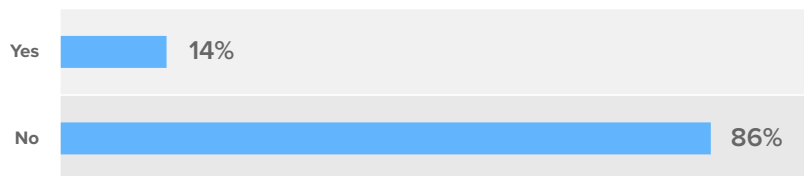
If you responded “yes” to 22A, at what threshold for annual ASC net revenues do management fees typically decrease?



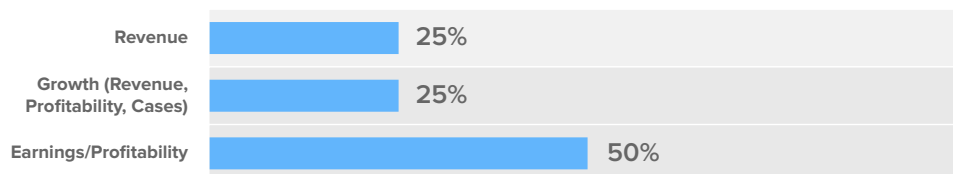
\* Does not total 100% due to rounding.

23<sup>A</sup>

Do you have any ASC management fee arrangements where in part of your fee is at risk?

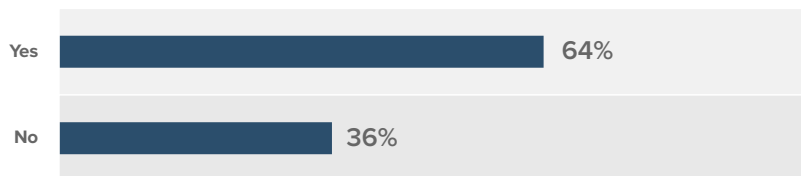
23<sup>B</sup>

If you answered “yes”, which factors may influence the magnitude of the management fee which you ultimately earn?



24

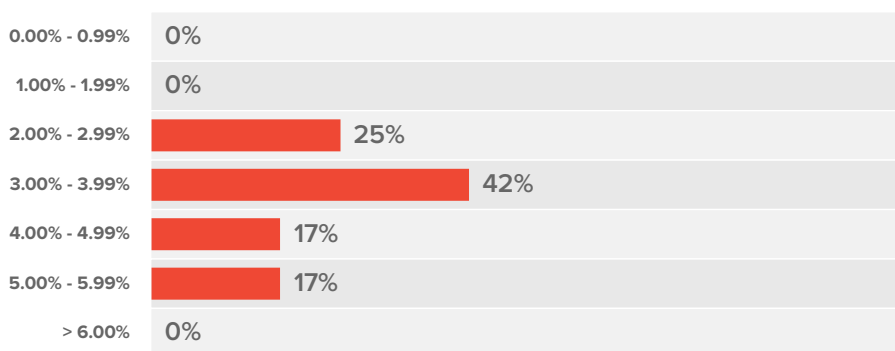
Does the management fee charged vary based on the level of services provided?



25

What is the typical management fee rate your company charges for surgical and specialty hospitals?

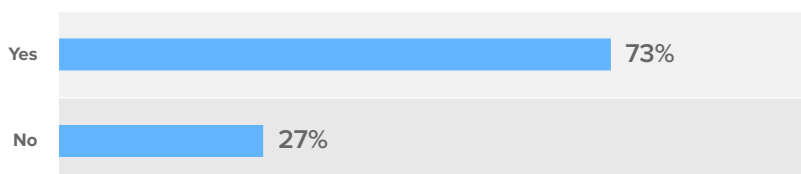
#### Management Fee as a % of Net Revenue



\* Does not total 100% due to rounding.

26

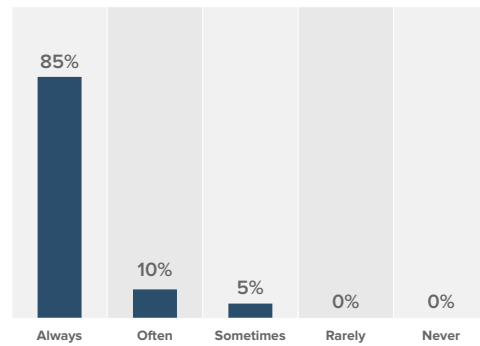
Do you maintain an equity ownership in all freestanding entities that you manage?



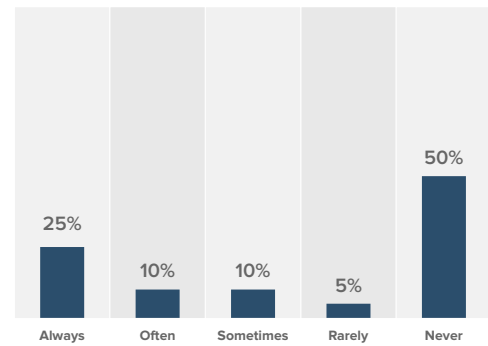
# 27

Which management services do you typically provide as part of your management agreement?

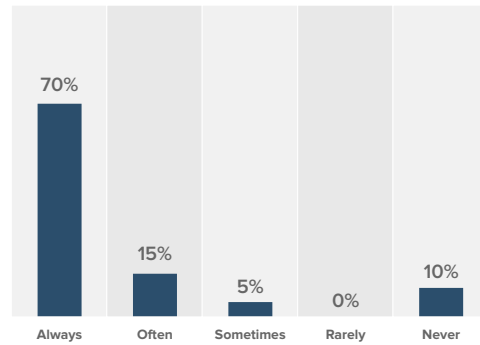
**Access to GPO**



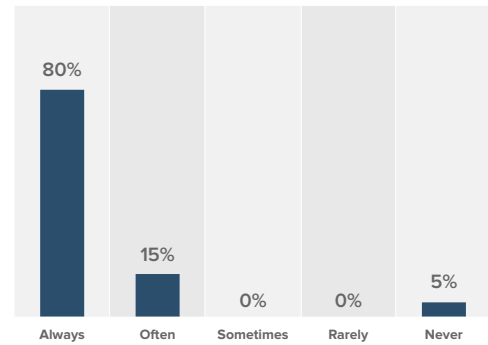
**Coding**



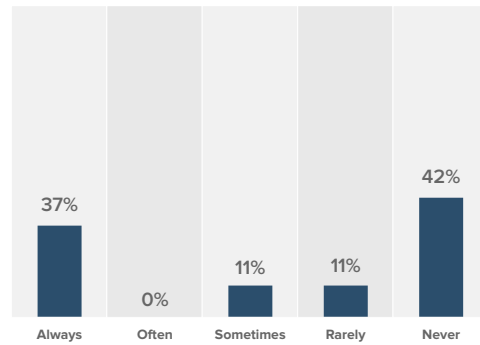
**Accounting**



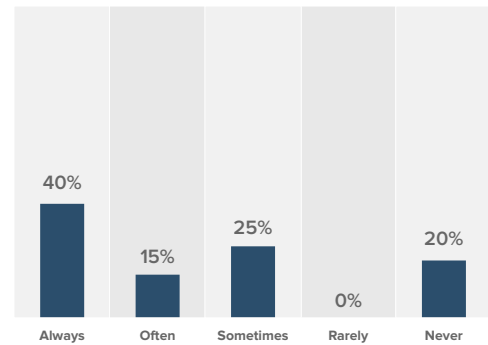
**Corporate Business Development Executive or Staff**



**Architecture & Design**

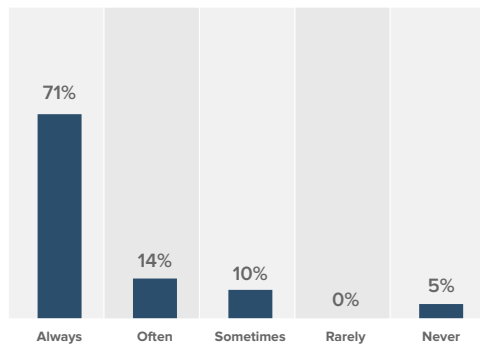


**Corporate Counsel or Legal Support**

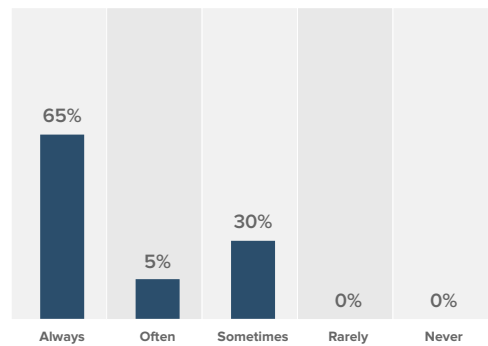


\* Does not total 100% due to rounding.

**Benchmarking Based on Other Equity Owned Centers**



**Corporate Human Resources Executive or Staff**

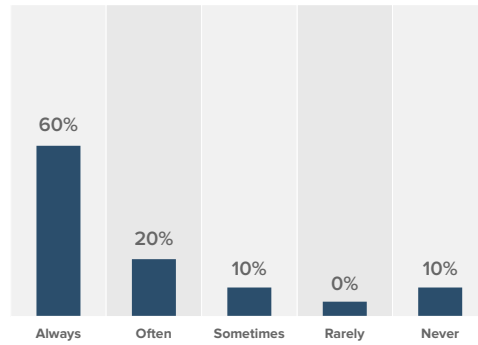


# 27

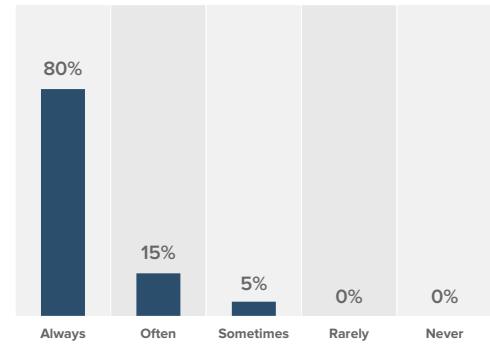
CONT'D

Which management services do you typically provide as part of your management agreement?

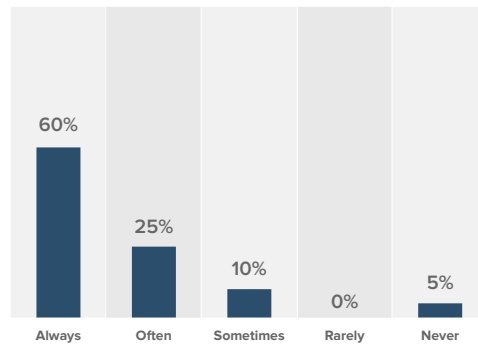
**Corporate Revenue Cycle Executive or Staff**



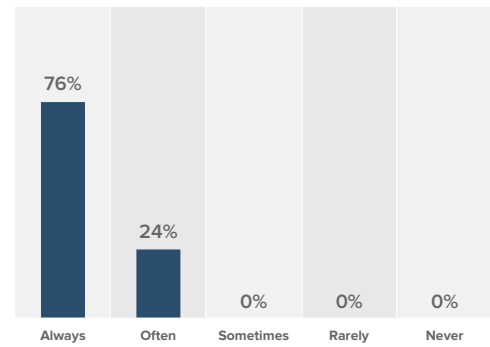
**Managed Care Contracting**



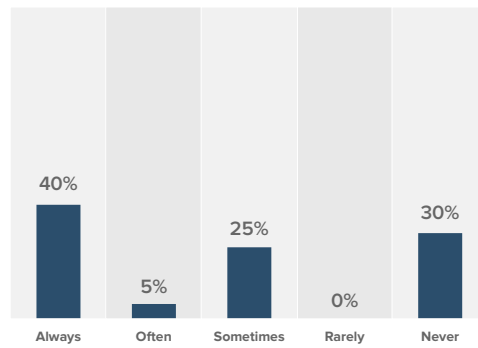
**Corporate Supply Chain Executive or Staff**



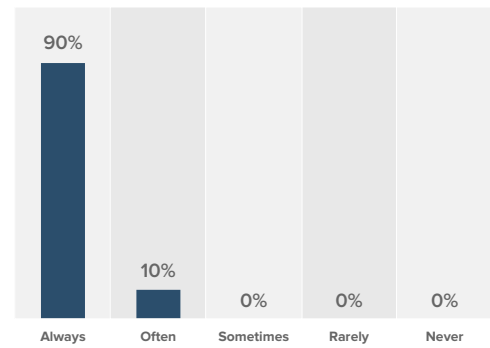
**Mock Accreditation Surveys**



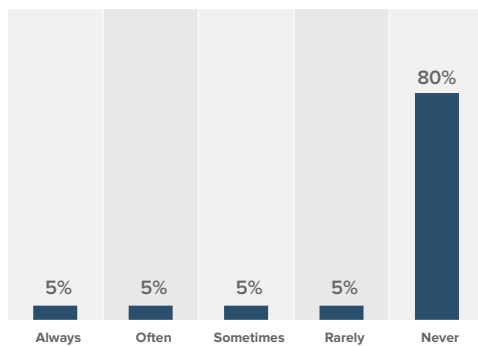
**Data Warehouse**



**Oversight by Regional VP of Operations**

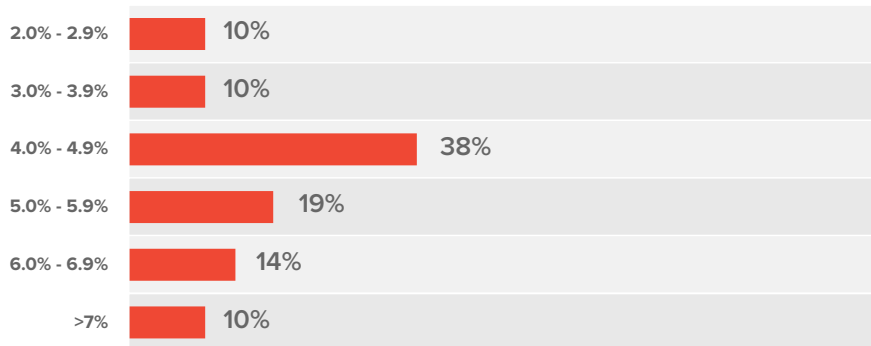


**Dictation**



## 28

What are the typical fees you have observed in the market for surgery center billing and collections provided by third parties (as a % of net revenues)?



\* Does not total 100% due to rounding.

## Participants:

- Ambulatory Alliances, LLC
- Ambulatory Surgical Centers of America (ASCOA)
- ASCs Inc.
- ASD Management
- Avanza Healthcare Strategies
- CHSPSC, LLC
- Cleveland Clinic
- Compass Surgical Partners
- Constitution Surgery Alliance
- Covenant Surgical Partners, Inc.
- Gastro Health, LLC
- HonorHealth
- IASIS Healthcare© LLC
- LifePoint Health, Inc.
- Meridian Surgical Partners
- Merritt Healthcare
- National Surgical Healthcare
- Partners Medical Consulting
- Physicians Endoscopy, LLC
- Surgery Partners, Inc.
- Surgical Care Affiliates (SCA)
- Sutter Health
- The Bloom Organization, LLC
- United Surgical Partners International (USPI)

## Disclaimer

The intent of this survey is to provide a summary of industry respondents' views regarding valuation, acquisition activity, ownership preferences and other trends regarding ASCs. Though our survey includes statistics regarding valuation multiples, this information should be used as general information only and should not be considered as providing any value guidance for any specific ASC interest. Business valuation is a complex process involving consideration and analysis of both financial and non-financial factors. The determination of fair market value should always be made by a qualified business appraiser with special knowledge of the subject healthcare industry.

Notes: \_\_\_\_\_

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With nearly two decades of experience and an exclusive dedication to serving the healthcare and life sciences industries, HealthCare Appraisers is nationally recognized as a full-service provider of healthcare valuation services and solutions.



## COMPENSATION VALUATION

We provide fair market value (FMV) opinions and automated valuation solutions for all types of financial arrangements entered into by physicians, hospitals, and other healthcare organizations.



## BUSINESS VALUATION

Our broad range of business valuation services include financial reporting, intangible assets and transactional consulting.



## FIXED ASSET VALUATION

Our real estate valuation experts specialize in performing thorough on-site valuations as well as desktop appraisals.



## REAL ESTATE VALUATION

Our real estate valuation experts specialize in performing thorough on-site valuations as well as desktop appraisals.



## LIFE SCIENCES & SPECIALTY SERVICES

Whether your valuation needs are simple or complex, our specialty valuation solutions are designed to keep you compliant and give you peace of mind.

### Need help with your Fixed Asset Transactions?

Fixed asset transactions are becoming increasingly complex and frequent. As the nation's leading FMV experts, HealthCare Appraisers offers automated, affordable — and defensible — valuations with our Fixed Asset Calculator.

**Schedule a live, custom demo today.**

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