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Considering Selling An Interest In Your Surgery or Endoscopy Center?

By Matt Searles, Managing Partner with Merritt Healthcare. Merritt is an owner & operator of ambulatory surgery Centers and also has an active advisory service, guiding sellers and buyers of ASCs through successful transactions.

The Current Market

There is currently a robust, active market for the acquisition of ASCs & endoscopy Centers. There are primarily several different types of buyers evaluating these opportunities, including national ASC companies, hospitals, large medical groups & private equity firms. For Centers with the right profile, multiples are still in the 7x earnings range. While consolidation has reduced the field of purchasers, there is still a strong interest from a number of buyers.

Why Consider Selling?

Selling an interest in your ASC has specific advantages:

- *Diversification, Reducing Risk.* Selling an interest can reduce your exposure to risks associated with ASC ownership and diversify your wealth.
- *Liquidity Event at Capital Gains Tax Rates.* Selling your Facility provides a liquidity event that is federally taxed at the capital gains tax rate of 15% versus 35% for ordinary income gains. Assuming you sell at 7 times earnings, it would take you 10+ years to earn an equivalent amount of income from your Center.
- *Economies of Scale.* Selling to a national ASC company or hospital can provide management, purchasing and contracting economies of scale that can enhance the value of your Facility.

What Makes a Facility Attractive to Purchasers?

Attractive facilities will have several key characteristics:

- *Consistent Earnings History.* Buyers will typically base a valuation on the prior 12 months of earnings before interest, taxes, depreciation and amortization ("EBITDA"). Consistency and growth in earnings will enhance a valuation.

- *Diversified Revenue Base.* Facilities where one physician accounts for more than 15-25% of the revenue will give purchasers pause. Revenue from multiple sources and multiple specialties can be attractive to buyers. Single specialty Centers can receive high multiples as well, but it is important to have a number of utilizing owners so that the loss of any one physician would not materially impact earnings.
- *Limited Out of Network Exposure.* In-network revenue streams will receive full credit in any valuation process. Out of network revenue streams are typically discounted heavily by potential purchasers.
- *Strong Growth Prospects.* Purchasers will only pay a premium multiple when they are certain that a Facility has strong growth prospects (new specialties, physicians, etc). Barriers to entry, such as exist in Certificate of Need states, are helpful as well.

Likely Purchasers

The most active acquirers of interests in ASC are certainly the national ASC companies. These companies will typically purchase up to 60% of an ASC, most typically they target a 51% interest. The national ASC companies have very strong management teams and can often provide economies of scale that improve a Facility's operations.

Local hospitals are often interested in acquiring local ASCs and are the only buyer who would be willing to buy 100% of the Center and enter into a management contract with the physicians. However, we have found that hospitals pay slightly lower multiples in the 100% sale scenario. This is because they are likely to require an independent appraisal of the ASC. These independent appraisers tend to be slightly more conservative in their approach and as a result, the values they provide could be slightly lower than you could expect from a strategic buyer.

Private equity buyers are typically more interested in purchases of multiple ASCs versus single Centers.

The Sale Process

The sale of an ASC, depending on the regulatory environment (i.e Certificate of Need), can take 6-12 months. The major challenges in the process are in making an effective presentation to purchasers given the complexities of the healthcare marketplace and of your ASC. It is critical that you understand your business and can present it optimally to the purchasing community. You must demonstrate the growth potential of earnings so that the buyers are comfortable assuming considerable growth into the future. Keep in mind that they will perform a discounted cash flow analysis using current earnings as the starting point. You will need to make a credible case for aggressive growth assumptions so that the analysis produces a high valuation (and translates into a high "multiple" of current earnings).

Before considering the sale of an interest in your Facility you will need to complete a comprehensive operational and financial review. As indicated, purchasers will generally use trailing 12-month earnings as a basis for their valuation, but if improvements are made prior to sale or are identified as one-time, non-recurring expenses, purchasers will add these items back to earnings, allowing for a higher valuation. Once your review is completed it is in your best interest to present the opportunity to all likely purchasers in order to create a competitive environment for your Center. Typically an Information Memorandum is the mechanism used to introduce your Facility to buyers. The

memorandum should be comprehensive and carefully written, usually 40-60 pages long. This report should cover financial and operational performance, the background/history of the Facility, description of its owners & utilizers, the competitive landscape, and highlight the growth potential of the Center.

Conclusion

The sale process can be long and complex, however, the rewards can be considerable. Not only can a liquidity event be realized, but you can also gain a value added partner who can enhance the performance of your Facility.

Contact Information

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