Healthcare Valuation

A Healthcare Reform Update

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Presenter Bio

Todd A. Zigrang, MBA, MHA, FACHE, ASA is the President of **HEALTH CAPITAL CONSULTANTS** (HCC), where he focuses on the areas of valuation and financial analysis for hospitals, physician practices, and other healthcare enterprises. Mr. Zigrang has over 23 years of experience providing valuation, financial, transaction and strategic advisory services nationwide in over 2,000 transactions and joint ventures involving acute care hospitals and health systems; physician practices; ambulatory surgery centers; diagnostic imaging centers; accountable care organizations, managed care organizations, and other third-party payors; dialysis centers; home health agencies; long-term care facilities; and, numerous other ancillary healthcare service businesses. Mr. Zigrang is also considered an expert in the field of healthcare compensation for physicians, executives and other professionals.

Mr. Zigrang is the co-author of the "*Adviser's Guide to Healthcare – 2nd Edition*" (AICPA, 2015), numerous chapters in legal treatises and anthologies, and peer-reviewed and industry articles such as: *The Guide to Valuing Physician Compensation and Healthcare Service Arrangements* (BVR/AHLA); *The Accountant's Business Manual* (AICPA); *Valuing Professional Practices and Licenses* (Aspen Publishers); *Valuation Strategies*; *Business Appraisal Practice*; and, *NACVA QuickRead*. Additionally, Mr. Zigrang has served as faculty before professional and trade associations such as the American Bar Association (ABA); the National Association of Certified Valuators and Analysts (NACVA); Physician Hospitals of America (PHA); the Institute of Business Appraisers (IBA); the Healthcare Financial Management Association (HFMA); and, the CPA Leadership Institute.

Presenter Bio

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Ms. Bailey-Wheaton conducts project management and consulting services related to the impact of both federal and state regulations on healthcare exempt organization transactions, and provides research services necessary to support certified opinions of value related to the Fair Market Value and Commercial Reasonableness of transactions related to healthcare enterprises, assets, and services. She serves on the Editorial Board of NACVA's *The Value Examiner*, and as a Vice Chair of the American Bar Association's (ABA) Young Lawyer's Division Health Law Committee. She has previously presented before the ABA and NACVA.

Ms. Bailey-Wheaton is a member of the Missouri and Illinois Bars and holds a J.D., with a concentration in Health Law, from Saint Louis University School of Law, where she served as Fall Managing Editor for the *Journal of Health Law & Policy*.

You can see her full CV at https://www.healthcapital.com/hcc/cvs/jbailey.pdf

Presentation Overview

- Tax Cuts & Jobs Act of 2017
- The Current State of Healthcare – The Four Pillars
  - Regulatory Updates
  - Reimbursement Updates
  - Competition Updates
  - Technology Updates

Tax Cuts & Jobs Act of 2017

Tax Cuts & Jobs Act of 2017

- Signed into law on December 22, 2017
- Brings non-profit entities more in line with their for-profit colleagues
- Corporate tax rate reduced from 35% to 21%
  - As a result, for-profit providers are anticipating tax reductions ranging between $10-500 million in 2018
  - Likely even more for pharmaceutical and health insurance companies
  - Only 21% of community hospitals owned by for-profit entities

"Seven key changes the new tax law will force hospitals to consider" By Harris Meyer, Modern Healthcare, http://www.modernhealthcare.com/article/20180102/NEWS/180109995 (Accessed 7/31/18). "Tax reform imposes costs on tax-exempt healthcare organizations as for-profit peers weigh benefits" PricewaterhouseCoopers LLP, February 2018, https://www.pwc.com/us/en/health-industries/health-research-institute/publications/impact-of-TCJA.html (Accessed 7/31/18). "New Excise Tax Cuts Into Tax-Exempt Executive Compensation" By Scott C. Withrow, Esq., ABA Health eSource, Vol. 14, No. 7.

Qualified Business Income (QBI)

- New Pass-Through Deduction for Qualified Business Income (QBI) – Section 199A
- Allows for an up to 20% deduction of QBI from:
  - Partnerships
  - Limited Liability Companies (LLCs)
  - S Corporations
  - Trusts
  - Estates
  - Sole Proprietorships
- Only applies to taxpayers with taxable incomes of less than $157,500 for single taxpayers and $315,000 for joint filers

"Mechanics of the new Sec. 199A deduction for qualified business income" By William A. Bailey, CPA, J.D., LL.M., Journal of Accountancy, May 1, 2018, https://www.journalofaccountancy.com/issues/2018/may/sec-199a-deduction-for-qualified-business-income.html (Accessed 9/6/18). "IRS issues proposed regulations on new 20 percent deduction for passthrough businesses" Internal Revenue Service, Press Release, August 8, 2018, https://www.irs.gov/newsroom/irs-issues-proposed-regulations-on-new-20-percent-deduction-for-passthrough-businesses (Accessed 9/17/18).

Qualified Business Income (QBI)

- "*Below the line*" deduction
- Based on an "*'artificial' calculation of business income instead of actual economic outlays required for most other business deductions*"
- Big tax benefit for non-corporate businesses
  - Included in the tax reform to equate non-corporation tax cuts with the cuts for C-Corps
  - Deduction taken at the following levels:
    - Partner
    - S-Corp Shareholder
    - Estate and Trust
    - Sole Proprietor
- Effective beginning after December 31, 2017 (sunsets in 2026)

Net Operating Loss (NOL) Changes

- Changes to the Net Operating Loss (NOL) carryover and carryback provisions
  - Statutory Definition: “the excess of the deductions allowed by [Chapter 1, Subchapter B, of the U.S. Code] over the gross income”, i.e., the amount that business deductions exceed a taxpayer’s gross income, “subject to certain modifications”
  - Historically, NOL carrybacks/forwards have been a means to treat taxpayers with different earning cycles, but similar annual income, in a more equitable manner

"Net operating loss deduction" 26 U.S.C. § 172(c) (2017). "Carry your losses (further) forward" By John Owsley, CPA, Ph.D., and John McKinley, CPA, CGMA, J.D., LL.M., Journal of Accountancy, May 1, 2018, https://www.journalofaccountancy.com/issues/2018/may/carry-forward-net-operating-losses.html (Accessed 9/6/18).

Net Operating Loss (NOL) Changes

- Prior to the passage of the TCJA:
  - NOL could be "*carried back*" up to 2 tax years, and forward up to 20 years, to offset taxable income
- Under the TCJA:
  - *"There shall be allowed as a deduction for the taxable year an amount equal to the lesser of—the aggregate of the net operating loss carryovers to such year, plus the net operating loss carrybacks to such year, or 80 percent of taxable income computed without regard to the deduction allowable under this section*"
- Meaning: "*NOLs can no longer be carried back but are allowed to be carried forward indefinitely*"
- Effective for NOLs occurring on/after January 1, 2018

"Carry your losses (further) forward" By John Owsley, CPA, Ph.D., and John McKinley, CPA, CGMA, J.D., LL.M., Journal of Accountancy, May 1, 2018, https://www.journalofaccountancy.com/issues/2018/may/carry-forward-net-operating-losses.html (Accessed 9/6/18). "Net operating loss deduction" 26 U.S.C. § 172(a) (2017).

Net Operating Loss (NOL) Changes

- Corporations cannot take into account the new deduction for foreign-derived intangible income and global intangible low-taxed income
- For business taxpayers other than C-Corps, the new deduction under Section 199A qualified business income is not allowed in determining an NOL

Section 172(d)(9). "Carry your losses (further) forward" By John Owsley, CPA, Ph.D., and John McKinley, CPA, CGMA, J.D., LL.M., Journal of Accountancy, May 1, 2018, https://www.journalofaccountancy.com/issues/2018/may/carry-forward-net-operating-losses.html (Accessed 9/6/18).

Net Operating Loss (NOL) Changes

Potential Consequences:

- The reform "*will generally have the effect of increasing the present value of total federal income taxes owed*"
  - *"Taking into account the time value of money, companies with intermittent loss years and startup companies with initial years of losses may fare less well than under previous law, all other factors being equal"*
  - *"[G]enerally, the changes to the NOL rules put greater emphasis on taxpayers' understanding of the timing of their income and deductions when assessing expected future tax liabilities. A taxpayer can no longer rely on the NOL carryforward provisions to result in no federal tax liability in years of low taxable income relative to prior loss years"*

"Carry your losses (further) forward" By John Owsley, CPA, Ph.D., and John McKinley, CPA, CGMA, J.D., LL.M., Journal of Accountancy, May 1, 2018, https://www.journalofaccountancy.com/issues/2018/may/carry-forward-net-operating-losses.html (Accessed 9/6/18).

Net Operating Loss (NOL) Changes

Potential Consequences:

- May raise costs for tax-exempt providers, especially in urban markets
- May spin off some entities as separate taxable corporations (but may raise the eyebrows of federal and state regulators)

"Tax reform imposes costs on tax-exempt healthcare organizations as for-profit peers weigh benefits" PricewaterhouseCoopers LLP, February 2018, https://www.pwc.com/us/en/health-industries/health-research-institute/publications/impact-of-TCJA.html (Accessed 7/31/18).
"Seven key changes the new tax law will force hospitals to consider" By Harris Meyer, Modern Healthcare, http://www.modernhealthcare.com/article/20180102/NEWS/180109995 (Accessed 7/31/18).

Employee Benefits and Compensation

- No longer allowed to offset income from unrelated business activities, i.e., fringe benefits (e.g., cafeteria earnings, employer-provided parking, transit passes, shuttle busses and vans) with losses from other unrelated business activities

"Tax reform imposes costs on tax-exempt healthcare organizations as for-profit peers weigh benefits" PricewaterhouseCoopers LLP, February 2018, https://www.pwc.com/us/en/health-industries/health-research-institute/publications/impact-of-TCJA.html (Accessed 7/31/18).
"Seven key changes the new tax law will force hospitals to consider" By Harris Meyer, Modern Healthcare, http://www.modernhealthcare.com/article/20180102/NEWS/180109995 (Accessed 7/31/18).

Employee Benefits and Compensation

- Any amount spent on the provision of qualified transportation fringe to employees of tax-exempt organizations now subject to the Unrelated Business Taxable Income (UBTI)
- Whether, in what circumstances, and in what amounts, should expenses related to employee parking, transit, and commuter shuttles be included in UBTI?

New Code Sections 82, 132. Code Section 217 (moving deduction). "Tax reform imposes costs on tax-exempt healthcare organizations as for-profit peers weigh benefits" PricewaterhouseCoopers LLP, February 2018, https://www.pwc.com/us/en/health-industries/health-research-institute/publications/impact-of-TCJA.html (Accessed 7/31/18).

Employee Benefits and Compensation

- Temporary elimination of the wage exclusion for reimbursements of qualified moving expenses and suspension of the moving expenses deduction (through 2025)
- Temporary elimination of the wage exclusion for reimbursements of the bicycling commuting deduction (through 2025)

New Code Sections 82, 132. Code Section 217 (moving deduction). "Tax reform imposes costs on tax-exempt healthcare organizations as for-profit peers weigh benefits" PricewaterhouseCoopers LLP, February 2018, https://www.pwc.com/us/en/health-industries/health-research-institute/publications/impact-of-TCJA.html (Accessed 7/31/18).

Unrelated Business Taxable Income (UBTI)

- UBTI must be calculated separately for each unrelated business activity
- Any NOL from one of those activities cannot offset income from another
- How should one define a "separate trade/business"?
  - How does this intersect with the new 80% NOL limitation?
  - Should debt-financed income be considered as not derived from a "tr*ade/business*" and thus not subject to this separation, a/k/a silo-ing?
- 1.4% excise tax on net investment income of private colleges and universities with large endowments

"Seven key changes the new tax law will force hospitals to consider" By Harris Meyer, Modern Healthcare, http://www.modernhealthcare.com/article/20180102/NEWS/180109995 (Accessed 7/31/18). "Tax reform imposes costs on tax-exempt healthcare organizations as for-profit peers weigh benefits" PricewaterhouseCoopers LLP, February 2018, https://www.pwc.com/us/en/health-industries/health-research-institute/publications/impact-of-TCJA.html (Accessed 7/31/18).

Unrelated Business Taxable Income (UBTI)

- Example: A 501(c)(3) has a $1 million gain from operating a commercial laboratory and a $1 million loss from a money-losing commercial joint venture
  - Old Rule: Gain/Loss would offset, and the 501(c)(3)'s net would be $0
  - New Rule: Gain and loss are calculated separately, and the 501(c)(3)'s net would be $1 million (on which it must pay taxes)

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"Tax reform imposes costs on tax-exempt healthcare organizations as for-profit peers weigh benefits" PricewaterhouseCoopers LLP, February 2018, https://www.pwc.com/us/en/health-industries/health-research-institute/publications/impact-of-TCJA.html (Accessed 7/31/18).

Unrelated Business Taxable Income (UBTI)

- Potential healthcare implication
  - Accountable care organizations (ACOs) wherein members receive reimbursement as part of shared savings
    - The shared savings is not a result of the provision of care (the business of the healthcare provider)
      - In fact, provider is being paid for ***not*** providing care
    - So does shared savings = UBTI?

Executive Compensation

- Section 4960 – Excise Tax on "*Excessive Compensation*"
  - New 21% excise tax on annual compensation > $1 million for an organization's 5 highest-paid employees (i.e., "*covered employees*")
  - Once a covered employee, always a covered employee
  - Includes remuneration from all "*related*" organizations, including "*supporting*"/ "*supported*" organizations
  - Could include severance payments that do not trigger the new "*parachute payment*" provision
  - ***Does not include*** pre-tax deferral contributions to employer-sponsored retirement plans (but does include distributions) or employer-made Roth or other after-tax contributions
  - Compensation for the direct provision of medical services ***do not apply***

"Seven key changes the new tax law will force hospitals to consider" By Harris Meyer, Modern Healthcare, http://www.modernhealthcare.com/article/20180102/NEWS/180109995 (Accessed 7/31/18); "Executive Compensation Under Tax Cuts and Jobs Act of 2017" Journal of Health & Life Sciences Law, Vol. 12, No. 1, p. 64-76.

Executive Compensation

- Section 4960 – Excise Tax on "*Excessive Compensation*"
  - Limits on deductibility of compensation expenses by certain taxpayers
    - For for-profit providers, the commission and performance-based compensation exceptions to the $1 million limit were repealed
    - Prior to the TCJA – The $1 million deduction limit was not applicable to certain performance-based compensation and commissions
    - Subsequent to the TCJA – Performance/commission compensation exceptions repealed

"Seven key changes the new tax law will force hospitals to consider" By Harris Meyer, Modern Healthcare, http://www.modernhealthcare.com/article/20180102/NEWS/180109995 (Accessed 7/31/18).

Executive Compensation

"*Covered Employee*" definition revised:

- "The principal financial officer is now included as a covered employee;
- All individuals who hold the position of either principal executive officer or principal financial officer at any time during the taxable year are now covered employees;
- Covered employees include officers whose total compensation is required to be disclosed to shareholders by reason of them being amongst the three highest paid officers (other than the principal executive officer or principal financial officer). This is not an operational change but conforms the statute to IRS Notice 2007-49; and,
- For a 'publicly held corporation' that is not required to file a proxy statement, covered employees are determined as if these rules applied"

"US tax reform: Impact of Section 162(m) changes and transition relief on excessive compensation" Deloitte, https://www2.deloitte.com/content/dam/Deloitte/us/Documents/Tax/us-tax-reform-162m-updates.pdf (Accessed 9/6/18).

Executive Compensation

- Section 4960 – Excise Tax on "*Parachute Payments*"
  - Different from the rule applicable to taxable entities – doesn't require change in control, but employment separation
  - "*Parachute Payment*" =
    - Upon separation from employment
    - ≥ 3 times the employee's "*base amount*" (the employee's average, taxable income over the last 5 years)
  - The tax is imposed on the amount over and above the base amount, ***not*** the amount over and above the 3x threshold
  - Note: The IRS will not double dip on the Excess Compensation and the Parachute Payment by taxing the same money twice

"Executive Compensation Under Tax Cuts and Jobs Act of 2017" Journal of Health & Life Sciences Law, Vol. 12, No. 1, p. 74.

Executive Compensation

Potential Consequences:

- Non-profit hospitals consisting of multiple tax-exempt entities may revise their entity structure so that they only have to pay for 5 high-compensation employees in total (instead of 5 per organization)
- Can pay specialized physicians over $1 million and parachute payments for medical services without incurring the 21% excise tax

"Seven key changes the new tax law will force hospitals to consider" By Harris Meyer, Modern Healthcare, http://www.modernhealthcare.com/article/20180102/NEWS/180109995 (Accessed 7/31/18). "New Excise Tax Cuts Into Tax-Exempt Executive Compensation" By Scott C. Withrow, Esq., ABA Health eSource, Vol. 14, No. 7.

Executive Compensation

Potential Consequences (continued):

- For those physicians performing both non-clinical and clinical duties, hospitals may reallocate the clinical and non-clinical compensation of physician executives to avoid the $1 million threshold
- Tax-exempt entities will see increased costs while for-profits will see an increase in revenues, from tax dollars and repatriated funds

"Seven key changes the new tax law will force hospitals to consider" By Harris Meyer, Modern Healthcare, http://www.modernhealthcare.com/article/20180102/NEWS/180109995 (Accessed 7/31/18).

Individual Mandate Tax Penalty Repeal

- Reduces penalty for not having health insurance for at least 9 months of the year to $0 as of January 1, 2019
- Potential Consequences
  - Projected to significantly increase the number of uninsured, and consequently, uncompensated care
  - CBO and JCT estimated that the number of uninsured may increase by 4 million in 2019 and 13 million by 2027, and premiums would consequently rise 10% per year from 2018 to 2027

"Seven key changes the new tax law will force hospitals to consider" By Harris Meyer, Modern Healthcare, http://www.modernhealthcare.com/article/20180102/NEWS/180109995 (Accessed 7/31/18).

Tax Cuts & Jobs Act of 2017

Overall Potential Consequences:

- Borrowing rates on tax-exempt municipal bonds may rise (corporate tax cut may make tax-exempt interest less attractive)
- Corporate tax rate reduced (may affect publicly traded hospitals' 2017 reporting)

"Seven key changes the new tax law will force hospitals to consider" By Harris Meyer, Modern Healthcare, http://www.modernhealthcare.com/article/20180102/NEWS/180109995 (Accessed 7/31/18).

Valuation Implications

Income Approach Implications:

- Overall, valuation methodology may swing more in favor of the Discounted Cash Flow (DCF) Method since history is under a different tax rule
- The discrete period to project cash flow needs to match the number of years that the new tax provisions are in effect (some are temporary)
- Projections of income tax expense and depreciation will be affected—also the benefits of NOLs
- Assumptions must be made as to how any cash savings will be used; not all of it will hit the bottom line immediately, depending on how it's used: for reinvestment, share buybacks, debt repayments, dividends, new hires, etc.
- Depending on how companies use extra after-tax cash flow, assumptions about growth will be affected
- Some industries get special tax breaks under the TCJA

Valuation Implications

Market Approach Implications:

- The use of the market approach may give way more to the income approach since the tax changes affect future income (Remember: Value is the expectation of future benefit)
- Healthcare market multiples increased throughout 2017 and likely already reflect the anticipated tax changes

Asset/Cost Approach Implications:

- When applying an adjusted book value methodology, you will need to adjust the estimated taxes on the difference between the appraised value and tax basis of the assets

Cost of Capital Implications:

- A material change is not foreseen in the risk-free rate or equity risk premiums
- Tax shield benefits of interest expense will decrease, affecting the cost of debt (may affect optimal capital structure) and companies that rely on debt capital financing will likely see an increase to their WACC

Valuation Implications

Pass-Through Entity (PTE) Implications:

- The revised difference between the effective rate for C-Corps versus pass-through entities needs to be carefully considered. PTEs appear to increase in value under the TCJA, but appraisers must consider the intent of the owner as to what he or she will do with this increase in value

- Tax rates for individuals and small businesses have a termination date, so determining a terminal value may be more complicated

- As part of the PTE tax relief, the owner's reasonable compensation figures into the calculation of the new QBI deduction (Section 199A); this means more scrutiny on reasonable compensation and the need for more studies

Valuation Implications – Healthcare Specific

- The TCJA may have implications on a physician's bottom line, as well as his or her overall practice distributions
- The TCJA may have implications on a physician's practice setting – e.g., independence vs. employment
- High-income physicians likely won't benefit from 20% deduction
- Lower-income physicians who may benefit from 20% deduction should ensure they are capitalizing on this new provision of the TCJA, as this deduction expires December 31, 2025

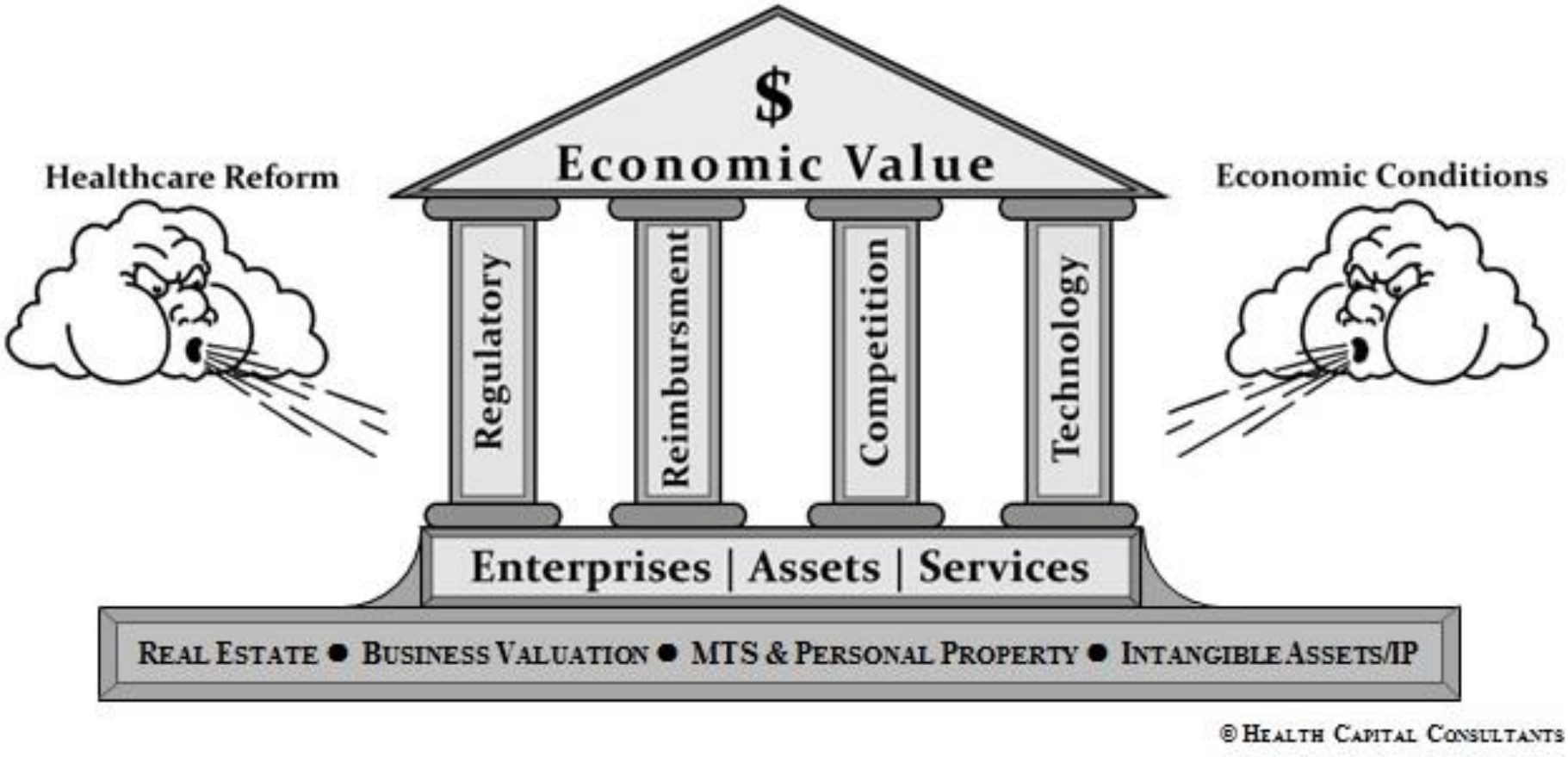
Valuation Implications – Healthcare Specific

- The decrease in the corporate tax rate, excluding other provisions of the tax law, will clearly benefit for-profit hospitals and health systems, as well as pharmaceutical companies
- Starting in 2019, the TCJA repeals the ACA Individual Mandate that requires all Americans under 65 to have health insurance or pay an annual penalty
- Increase in the Medical Expense Deduction will benefit low and middle-income individuals facing high medical costs, especially senior citizens and people with chronic illnesses – will this result in increased utilization of healthcare services?

The Current State of Healthcare

The Four Pillars

The Four Pillars of Healthcare Value



Regulatory Updates
Changes in Medicaid Expansion

- Reconsideration of Medicaid Expansion
  - Virginia
  - Maine
- Medicaid – The big winner in Midterm Elections:
  - Passed ballot measures to Expand:
    - Idaho
    - Nebraska
    - Utah
  - Kansas & Wisconsin elected Democratic governors in favor of expanding Medicaid

"Idaho, Nebraska and Utah Vote to Expand Medicaid" By Abby Goodnough, New York Times, November 7, 2018, https://www.nytimes.com/2018/11/07/health/medicaid-expansion-ballot.html (Accessed 11/8/18).

Regulatory Updates
Changes in Medicaid Expansion

- Imposition of work requirements (through §1115 Waivers)
  - Four states have had requirements approved:

    Arkansas | Indiana | New Hampshire | Wisconsin

  - 9 states have requirements pending
  - Varying requirements among states
    - Some exempt people starting at age 50, while others wait until 60 / 65
    - Required hours range from 80 to 100 per month

"Medicaid Waiver Tracker: Approved and Pending Section 1115 Waivers by State" Kaiser Family Foundation, November 2, 2018, https://www.kff.org/medicaid/issue-brief/medicaid-waiver-tracker-approved-and-pending-section-1115-waivers-by-state/ (Accessed 11/8/18)

Regulatory Updates
Association Health Plans

- June 2018 – Final regulations for ACA "*work around*" to current health insurance marketplace plans were released by U.S. Department of Labor to expand eligibility for Association Health Plans (AHPs)
  - AHPs can be created and sold within a region or state by small businesses or trade groups
  - Controversy – While AHP insurance may be more affordable, the plans are expected to be exempt from ACA requirements, including the "*10 Essential Health Benefits*" and "*guaranteed issue*" provisions, leaving individuals with less coverage

Regulatory Updates
Section 1332 Waivers

- Section 1332 of the ACA – Allows states to apply for "*State Innovation Waivers*," a/k/a "*State Relief and Empowerment Waivers*," to relax certain ACA requirements
- October 22, 2018 Guidance from Treasury and HHS
  - Will allow states more flexibility than previous guidelines to lower premiums and increase choices for their health insurance markets
  - Will allow states to provide options that are less than the "*minimum essential coverage*" under the ACA, including short-term plans

Regulatory Updates
Texas v. U.S.

- Plaintiffs – Texas + 20 Republican state attorneys general and governors and 2 individuals
- Argument – The ACA is now invalid because the *Individual Mandate*, the lynchpin of the law, was repealed
  - Individual Mandate is not severable from rest of the ACA
  - June 7, 2018 – U.S. Attorney General Letter
    - DOJ agrees with plaintiffs that Individual Mandate can no longer be held constitutional, but that the Mandate is severable from the ACA
    - DOJ does not believe that "*guaranteed issue*" provision, "*community rating*" provision, or requirement of providing the "*10 essential health benefits*" are severable, and **do not plan** to argue in support of their continuance

Regulatory Updates
Fraud & Abuse Law Reform

- Stark Law Request for Information (RFI)
  - Issued on June 25, 2018
  - Seeks input on undue regulatory impact that Stark Law has placed on VBR and coordinated care, and strategies to reduce burden
- Anti-Kickback Statute RFI
  - Issued on August 24, 2018
  - Solicited comments specific to 4 categories

Regulatory Updates
Fraud & Abuse Law Reform

- July 2016 Senate Finance Committee Hearing on Stark Law
  - Senate Finance Committee Majority Staff White Paper:

    "*The Stark law has become increasingly unnecessary for, and a significant impediment to, value-based payment models that Congress, CMS, and commercial health insurers have promoted. The risk of overutilization, which drove the passage of the Stark law, is largely or entirely eliminated in alternative payment models.*"

"Why Stark, Why Now?" Senate Finance Committee Majority Staff (2016), p. 2, 15-16.

Regulatory Updates
Fraud & Abuse Law Reform

- July 2016 Senate Finance Committee Hearing on Stark Law

  - American Hospital Association Letter to US Senate:

    "*As interpreted today, the two 'hallmarks' of acceptability under the Stark law – fair market value and commercial reasonableness – are not suited to the collaborative models that reward value and outcomes*."

American Hospital Association Letter to U.S. Senate, By Thomas P. Nickels, Letter to The Honorable Orrin Hatch and The Honorable Ron Wyden, re Stark Law, January 29, 2016.

Regulatory Updates
Fraud & Abuse Law Reform

- June 2018 CMS Request for Information regarding Stark Law
  - Approximately 2 years later, CMS published a Request for Information (RFI) seeking input on:
    - The undue regulatory impact that Stark Law has placed on VBR and coordinated care
    - Strategies to reduce this burden

"Medicare Program; Request for Information Regarding the Physician Self-Referral Law" Federal Register, Vol. 83, No. 122 (June 25, 2018), p. 29524.

Regulatory Updates
Fraud & Abuse Law Reform

- June 2018 CMS Request for Information regarding Stark Law
  - Information sought includes:
    - Requests on topics involving *alternative payment models* (APMs)
    - Additional exceptions to the Stark Law to facilitate innovation
    - Changes to the current provisions of Stark Law
    - Changes to existing compensation formulas
    - Exceptions necessary to protect *accountable care organizations* (ACOs) and bundled payment models

"Medicare Program; Request for Information Regarding the Physician Self-Referral Law" Federal Register, Vol. 83, No. 122 (June 25, 2018), p. 29525-6.

Regulatory Updates
Fraud & Abuse Law Reform

- June 2018 CMS Request for Information regarding Stark Law
  - July 17, 2018 – House Committee on Ways and Means hosted a hearing on modernizing the Stark Law to ensure a successful transition from volume to value-based Medicare reimbursement
    - HHS plans to make modifications to Stark Law administratively (i.e., not through Congress), which it will seek to accomplish by creating a proposal to address the comments that CMS receives and other efforts to streamline coordination of care
    - HHS Deputy Secretary, Eric Hagan, emphasized the agency's interest in regulatory reforms for both Stark Law and AKS
    - Hagan stated both laws could be stifling innovative arrangements, and thus, hindering better patient outcomes

"Hearing on Modernizing Stark Law to Ensure the Successful Transition from Volume to Value in the Medicare Program" Committee on Ways and Means, U.S. House of Representatives, July 17, 2018, https://waysandmeans.house.gov/event/hearing-on-modernizing-stark-law-to-ensure-the-successful-transition-from-volume-to-value-in-the-medicare-program/ (Accessed 7/16/18).

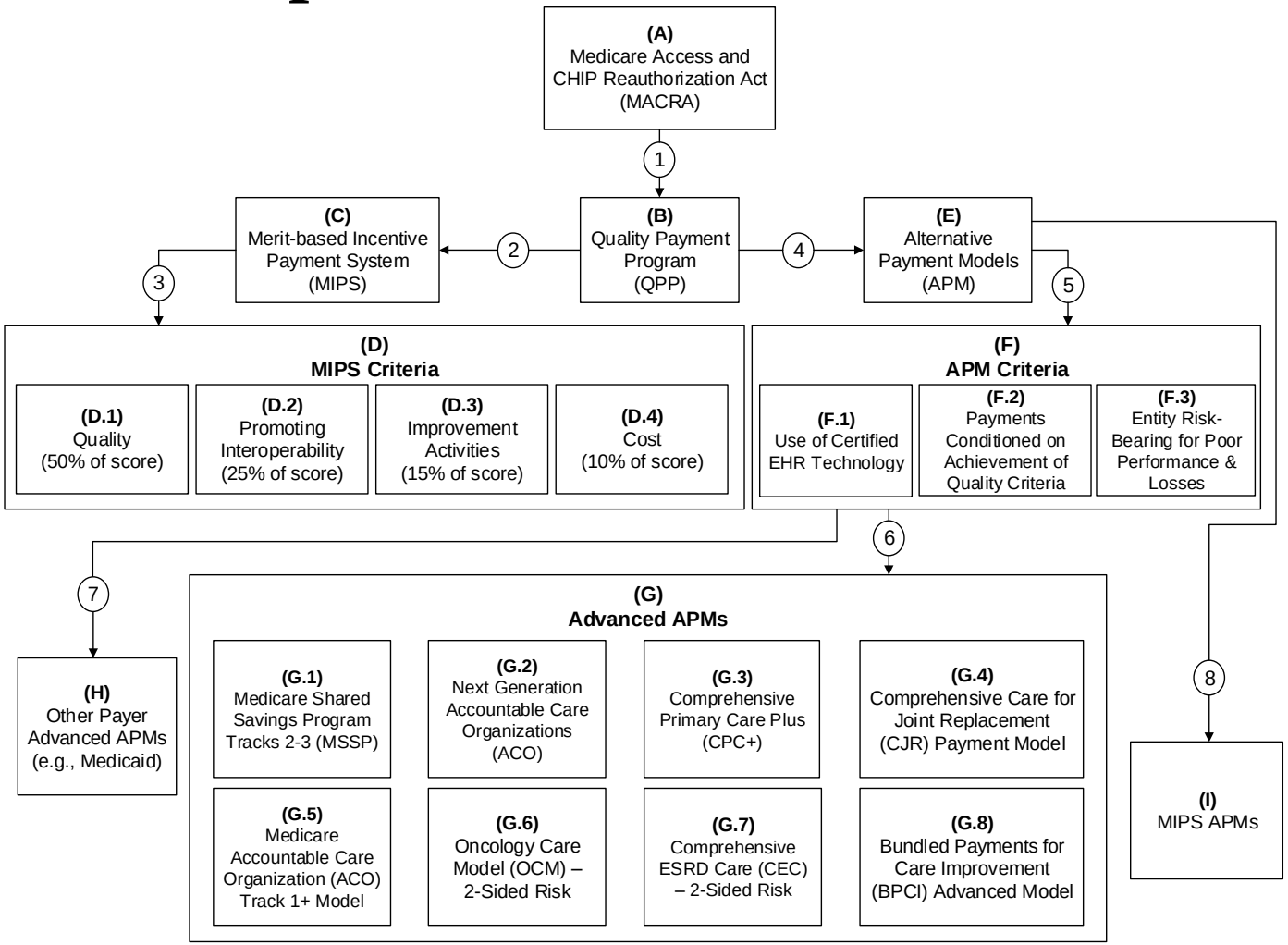
Regulatory Updates
Fraud & Abuse Law Reform

- June 2018 CMS Request for Information regarding AKS
  - August 24, 2018 – HHS Office of Inspector General (OIG) published another RFI seeking public input on changes to AKS
  - Seeking comments on ways that AKS safe harbors could be improved, specific to 4 categories:
    - Promotion of care coordination and value-based care
    - Beneficiary engagement, including beneficiary incentives and cost-sharing obligations
    - Other regulatory topics, including feedback on current fraud and abuse waivers, cybersecurity-related items and services, and new exceptions required by the Bipartisan Budget Act of 2018
    - The intersection of the Stark Law and AKS

"HHS Eying Stark and Anti-Kickback Reform" American Health Lawyers Association, July 20, 2018, https://www.healthlawyers.org/News/Health%20Lawyers%20Weekly/Pages/2018/July%202018/July%2020%202018/HHS-Eying-Stark-and-Anti-Kickback-Statute-Reforms.aspx (Accessed 7/23/18).

Regulatory Updates

Continued Implementation of MACRA



Regulatory Updates

MACRA Payment Structure & Timeline

	A	B	C	D	E
1	Performance Year	2017	2018	2019	2020
2	Payment Adjustment Year	2019	2020	2021	2022 (and on)
3	Annual Fee Schedule Update	+0.5%	+0.5%	+0.5%	TBD
	MIPS				
4	Maximum Positive Payment Adjustment	4%	5%	7%	9%
5	Maximum Negative Payment Adjustment	-4%	-5%	-7%	-9%
6	MIPS Performance Category Weights				
7	Quality	60%	50%	30%	30%
8	Cost	0%	10%	30%	30%
9	Improvement Activities	15%	15%	15%	15%
10	Promoting Interoperability	25%	25%	25%	25%
	Advanced APMs				
11	Bonus Quality Payment	5%	5%	5%	5%

"How the QPP Affects Medicare Part B Payments" The Physicians Advocacy Institute's Medicare Quality Payment Program (QPP) Physician Education Initiative, http://www.physiciansadvocacyinstitute.org/Portals/0/assets/docs/Background-Resources/How%20the%20QPP%20Affects%20Medicare%20Part%20B%20Payments.pdf (Accessed 8/14/18), p. 3.

Regulatory Updates – Valuation Implications
MACRA Ramifications

- Much debate still surrounding MACRA and the QPP – whether its stated goals will, in fact, be accomplished through its provisions
- MACRA sought to "*fix*" Medicare Part B SGR, under which payment policy hospitals were able to *"...mark up their employed physicians' services as 'provider based' and charge technical fees for their services*"
- MACRA ostensibly rectified this underlying "*payment anomaly*," i.e., "*physician services are worth more to Medicare in hospital employment than in private practice*"
- However, in reality, MACRA actually served to "*grandfather in most of the existing payment differentials while reducing some payments for hospital ambulatory services provided more than 200 yards from the main hospital campus*"

"The Tangled Hospital-Physician Relationship" By Jeff Goldsmith, Nathan Kaufman, and Lawton Burns, Health Affairs Blog (May 9, 2016), http://healthaffairs.org/blog/2016/05/09/the-tangled-hospital-physician-relationship/ (Accessed 5/16/17).

Regulatory Updates - Valuation Implications

Inherent Conflict between MACRA and Fraud & Abuse Laws

- The goals of VBR and federal fraud and abuse laws are fundamentally discordant
- MACRA (as well as the ACA) has furthered the transition to VBR, which payment models seek to reduce the overutilization of services, by incentivizing the provision of efficient, evidence-based care (in part through the utilization of big data), through a "*carrot and stick*" approach, i.e., through shared savings and losses
- In order to provide coordinated, efficient care to meet these VBR goals, many organizations are considering various alignment strategies that amass the needed specialties and resources to provide for the full continuum of a patient episode of care, to take advantage of the VBR reforms

"Remaining Stark-Compliant with Practice Losses" and Ancillary Services" By Daniel W. Kiehl, JD, LLM, Coker Group, November 2016, http://cokergroup.com/wp-content/uploads/2016/11/Remaining-Stark-Compliance-with-Practice-Losses-and-Ancillary-Services_November-2016.pdf (Accessed 5/3/17).

Regulatory Updates - Valuation Implications

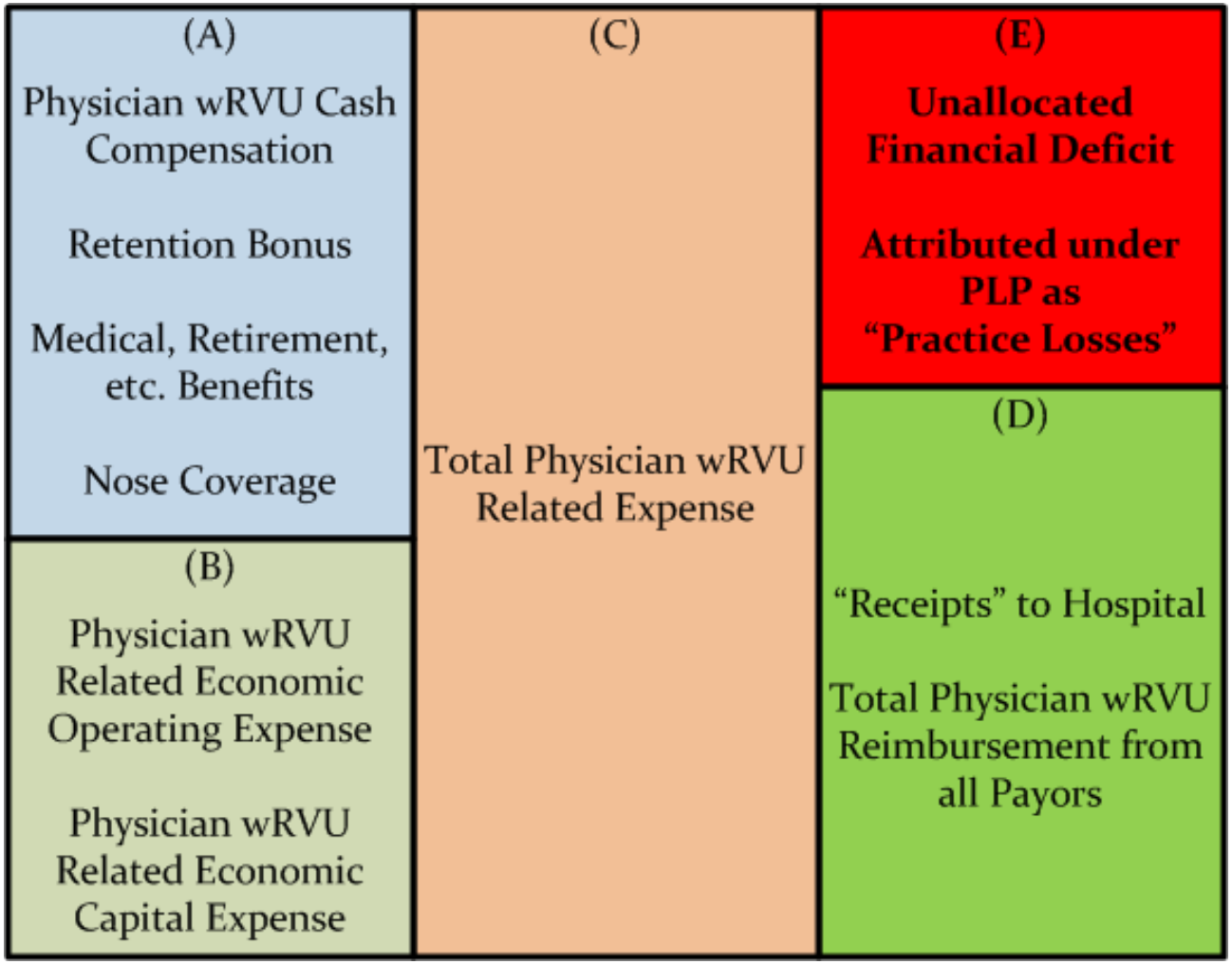
Inherent Conflict between MACRA and Fraud & Abuse Laws

- As a result of aligning, particularly when aligning through employment arrangements with hospitals and health systems, many hospitals or health systems sustain practice losses
- Due to a number of reasons, including:
  - Encountering a more adverse payor mix in a hospital setting
  - Needing to pay more competitive salaries to employed providers
  - The treatment of ancillary services by the hospital or health system

"Remaining Stark-Compliant with Practice Losses" and Ancillary Services" By Daniel W. Kiehl, JD, LLM, Coker Group, November 2016, http://cokergroup.com/wp-content/uploads/2016/11/Remaining-Stark-Compliance-with-Practice-Losses-and-Ancillary-Services_November-2016.pdf (Accessed 5/3/17).

Regulatory Updates - Valuation Implications

Summary of the Practice Loss Postulate



Regulatory Updates - Valuation Implications
Summary of the Practice Loss Postulate

(E)	(F)	(G)	(H)
Unallocated Financial Deficit **Attributed under PLP as "Practice Losses"**	Non-Monetary Benefits	Avoidance of Cost	Create Operational Efficiencies
		Economies of Scope	
		Economies of Scale	Diversify Supply Chain
		Organization as a Factor of Production	
		Social Benefits	Provide Continuum of Care
			Achieve Care Coordination
			Satisfy the *Triple Aim*
			Improve Population Health
			Complimentary and Requisite Care Mapping of Services

Reimbursement Updates
ACO Program Revamp

- August 9, 2018 – CMS issued proposed rule
- Will remove Track 1 and Track 2 models, which only had upside risk, from *Medicare Shared Savings Program* (MSSP)
- Will replace Track 1 and Track 2 with the new "*BASIC*" track
  - Will have same maximum level of risk as Track 1+ model
- Track 3 will be renamed the "*ENHANCED*" track
- Going forward, first-time MSSP ACOs will only have 2 years to transition to a two-sided risk model

"CMS Proposes 'Pathways to Success,' an Overhaul of Medicare's ACO Program" Centers for Medicare & Medicaid Services, August 9, 2018, https://www.cms.gov/newsroom/press-releases/cms-proposes-pathways-success-overhaul-medicares-aco-program (Accessed 11/14/18).

Reimbursement Updates
BPCI Advanced

- New voluntary episode payment model from CMS
- Qualifies as an Advanced APM under MACRA
- 32 clinical episodes (90 days in duration)
  - 29 inpatient
  - 9 outpatient
- October 9, 2018 – Approximately 1,300 participants announced (began performance period on October 1st)

"BPCI Advanced" Centers for Medicare & Medicaid Services, November 2, 2018, https://innovation.cms.gov/initiatives/bpci-advanced (Accessed 11/13/18).

Reimbursement Updates
Physician Fee Schedule

- 2019 Medicare Physician Fee Schedule (MPFS)
  - Positive adjustment of 0.11% to be applied to MPFS conversion factor (resulting in CF of $36.04)
  - *Merit-Based Incentive Payment System* (MIPS) & *Advanced Alternative Payment Model* (APM) changes
  - Office Visit Payments – From 5 Levels to 2 Levels (same payment no matter what the visit entails)
    - Estimated to save 51 hours per physician per year, due to decreased paperwork
    - Delayed until 2021

Reimbursement Updates
Outpatient Payment System

- 2019 Outpatient Prospective Payment System (OPPS) - hospital outpatient provider-based departments (HOPDs)
  - Would update outpatient payment rates by 1.35% in 2019
  - 4 changes expected to significantly impact HOPDs, specifically as regards:
    - Off-campus provider-based emergency departments
    - Site-neutral payments for clinic visits in all off-campus HOPDs
    - Payments for separately payable, covered outpatient drugs and biologicals acquired through the 340B Program
    - Expansion of services in excepted off-campus HOPDs

Reimbursement Updates
ASC Payment System

- 2019 Outpatient Prospective Payment System (OPPS) – ambulatory surgery centers (ASCs)
  - Would increase payment rates by 2.1% to ASCs that meet the quality reporting requirements
    - Now updating these rates using the hospital market basket, which it uses for HOPD payment updates
  - Expanded number of procedures payable at ASCs to ensure they remain competitive with HOPDs
  - CMS reconsidering whether to continue paying for spinal surgeries at ASCs (but for now is still allowing them to be done)

Reimbursement Updates
Valuation Implications

- The Shift from Volume (Fee-for-Service) to Value Based Reimbursement (VBR)
  - Challenges for determination of FMV
  - Challenges for compliance with AKS and Stark Law
- More integration models occurring
  - Pay-for-Performance (P4P) Arrangements
  - Shared Shaving Arrangements
  - Episodic Payments
  - Global Budgets
  - Leases (e.g., for PSAs and ASTCs)

Reimbursement Updates
Valuation Implications - P4P Arrangements

- Remuneration system in which part of the payment is dependent on performance
- Measured against a defined set of criteria
- Measures & performance standards for establishing target criteria
- Rewards (typically financial incentives) that are at risk, including the amount and method for allocating the payments among those who meet or exceed the reward threshold
- Example of a P4P Arrangement: Medicare's Hospital Readmissions Reduction Program

Reimbursement Updates
Valuation Implications – Shared Savings Arrangements

- Incentivizes providers to reduce healthcare spending for a defined patient population by offering a percentage of net savings realized as a result of their efforts

- Example of a Shared Savings Arrangement: Accountable Care Organizations (ACOs)

Reimbursement Updates
Valuation Implications – Episodic Payments

- A single price for all services needed by a patient for an entire episode of care (e.g., all inpatient and outpatient care they need after having a heart attack)
- An episode payment system reduces incentive to overuse unnecessary services during the episode, and gives providers the flexibility to decide what services should be delivered, rather than being constrained by fee codes and amounts
- Define what is included in an episode payment:
  - Length of time covered
  - Range of providers and services included
  - Not every type of condition or patient has to be paid on an episode basis
- Example of a Episodic Payment Arrangement: Bundled Payments for Care Improvement (BPCI) Initiative

Reimbursement Updates
Valuation Implications – Global Budgets

- A fixed prepayment made to a group of providers or a healthcare system (as opposed to a health care plan) that covers most or all of a patient's care during a specified time period
- Two key elements of coverage: Who and What
- They require tradeoffs between cost (price) of a service and the volumes of services delivered
- Example of a Global Budget Arrangement: Maryland's global budget program

Reimbursement Updates
Valuation Implications - Other VBR Models

- In response to the advent of VBR, most recently through MACRA, which concepts emerging reimbursement models rely upon to incentivize providers to achieve better outcomes at lower cost, hospitals are increasingly seeking closer relationships with physicians
  - Practice acquisitions
  - Direct employment
  - Provider services agreements (PSAs)
  - Co-management
  - Joint venture arrangements

"2014 Global Health Care Outlook: Shared Challenges, Shared Opportunities" By Deloitte Touche Tohmatsu Limited, New York City, NY, 2014, p. 13; "The 5 C's of 2013 Health Care" Deloitte Touche Tohmatsu Limited, 2012, http://www.deloitte.com/assets/Dcom-UnitedStates/Local%20Assets/Documents/us_chs_MondayMemo_2013Healthcare_%205Cs_021313.pdf (Accessed 6/4/14); "Co-Management Arrangements: Common Issues with Development, Implementation and Valuation" By Ann S. Brandy, et. al., American Health Lawyers Association, May 2011, http://www.healthlawyers.org/Events/Programs/Materials/Documents/AM11/hutzler.pdf (Accessed 6/5/14); "Top 10 Factors to Consider When Exploring Joint Ventures as an Affiliation Strategy" By Jonathan Spees, The Camden Group, June 2013, http://www.thecamdengroup.com/thought-leadership/top-ten/top-10-factors-to-consider-when-exploring-joint-ventures-as-an-affiliation-strategy/ (Accessed 6/5/14).

Reimbursement Updates
Valuation Implications - VBR Ramifications

- Corresponding with growing trend toward hospital-physician alignment, and specifically toward vertical integration, i.e., the "*integration of providers at different points along the continuum of care, such as a hospital partnering with a skilled nursing facility or a physician group*," there has been increased federal, state, and local regulatory oversight regarding the legal permissibility of these arrangements
- More intense regulatory scrutiny related to the AKS and the Stark Law, especially as these fraud and abuse laws relate to potential liability under the False Claims Act (FCA)
- Many of the exceptions and safe harbors in both the Stark Law and AKS require that any consideration paid to physicians not exceed the range of FMV and be deemed commercially reasonable

"The Value of Provider Integration" American Hospital Association, March 2014, http://www.aha.org/content/14/14mar-provintegration.pdf (Accessed 1/14/16) p. 2. See "Health Care Fraud and Abuse Control Program Report" U.S. Department of Health and Human Services and U.S. Department of Justice, https://oig.hhs.gov/reports-and-publications/hcfac/ (Accessed 5/18/17). "Health Care Fraud and Abuse Control Program: Annual Report for FY 1997" By The Department of Health and Human Services & The Department of Justice, Report for the United States Congress, Washington, DC, 1998; "Health Care Fraud and Abuse Control Program: Annual Report for FY 2007" By The Department of Health and Human Services & The Department of Justice, Report for the United States Congress, Washington, DC, 2008; "Health Care Fraud and Abuse Control Program: Annual Report for FY 2013" By The Department of Health and Human Services & The Department of Justice, Report for the United States Congress, Washington, DC, 2014. "Criminal Penalties for Acts Involving Federal Health Care Programs" 42 U.S.C. § 1320a-7b(b)(3)(B) (2012); "Limitations on Certain Physician Referrals" 42 U.S.C. § 1395nn(a)(1) (2012); "Personal Services and Management Contracts" 42 C.F.R. § 1001.952(d) (2007); "Bona Fide Employment Relationships" 42 U.S.C. § 1395nn(e)(2) (2010); "General Exceptions to the Referral Prohibition Related to Both Ownership/Investment and Compensation" 42 C.F.R. § 411.355(e)(ii)(B) (2014); "Exceptions to the Referral Prohibition Related to Compensation Arrangements" 42 C.F.R. § 411.357 (2010); "FMV: Analysis and Tools to Comply With Stark and Anti-kickback Rules," By: Robert A. Wade, Esq. and Marcie Rose Levine, Esq., Audio Conference, HCPro, Inc.: Marblehead, MA, March 19, 2008, http://content.hcpro.com/pdf/content/207583.pdf (Accessed 10/29/15), p. 6, 48.

Reimbursement Updates
Valuation Implications

- Continued push toward the outpatient site of service
- A "*leveling of the playing field*" between ASCs/HOPDs
  - Site-Neutral Payments for Clinic Visits
  - 2017 rule lowering payments for 340B-acquired drugs expanded to non-excepted off-campus HOPDs (originally just *excepted* off-campus HOPDs)
  - New types of furnished services provided at excepted off-campus HOPDs to be paid at 40% of the OPPS rate

"Medicare Program: Changes to Hospital Outpatient Prospective Payment and Ambulatory Surgical Center Payment Systems and Quality Reporting Programs: Final Rule with Comment Period" Federal Register, Vol. 83, No. 225, November 21, 2018, https://www.gpo.gov/fdsys/pkg/FR-2018-11-21/pdf/2018-24243.pdf (Accessed 11/29/18).

Competition Updates
Private Equity Buy-In

- A growing number of *private equity* (PE) groups are approaching large physician-held groups and other healthcare service enterprises, including hospitals and outpatient enterprises, seeking investment opportunities in the clinical services industry
- Why healthcare is attractive to PE firms
  - Industry considered stable
    - Aging Baby Boomer population
    - Influx of insured individuals under ACA and Medicaid Expansion
    - Rise in chronic disease incidence and prevalence
  - Healthcare industry has ranked in the top 3 industries in rates of return every year since 2011

"Private Equity and Venture Capital Funds Underperformed Public Markets During Q3 2016" Cambridge Associates, April 5, 2017, https://www.cambridgeassociates.com/press-release/private-equity-and-venture-capital-funds-underperformed-public-markets-during-q3-2016/ (Accessed 11/27/17); "How Private Equity Picks Healthcare Winners" By Kara Murphy and Nirad Jain, Bain and Company, June 20, 2017,

Competition Updates
Private Equity Buy-In

- Examples:
  - KKR (global investment firm) – Acquired Envision Healthcare Corporation, a publicly-traded company whose business includes physician services, post-acute care, and ASCs (owns/operates ASCs and hospital in 35 states), for $9.9B
  - Inova Health System (Washington, DC) – Created/Launched *Inova Strategic Investments*, which "*will invest in healthcare venture funds and will also invest directly into companies aligned with Inova's strategic priorities as part of Inova's vision to be a global leader in the delivery of personalized health*"
  - Spectrum Health (Grand Rapids, MI) – Created $100 million fund "…*to invest in personalized medicine, information technology, population health management and other emerging technologies*."

"How Private Equity Picks Healthcare Winners" By Kara Murphy and Nirad Jain, Bain and Company, June 20, 2017; "Midsize hospital systems taking the VC plunge" By Dave Barkholz, Modern Healthcare, March 4, 2017, http://www.modernhealthcare.com/article/20170304/TRANSFORMATION04/170309955 (Accessed 11/27/17); "KKR Completes Acquisition of Envision Healthcare Corporation" Press Release, Business Wire, October 11, 2018, https://www.businesswire.com/news/home/20181011005441/en/KKR-Completes-Acquisition-Envision-Healthcare-Corporation (Accessed 11/29/18).

Competition Updates
Healthcare Supply Shortages

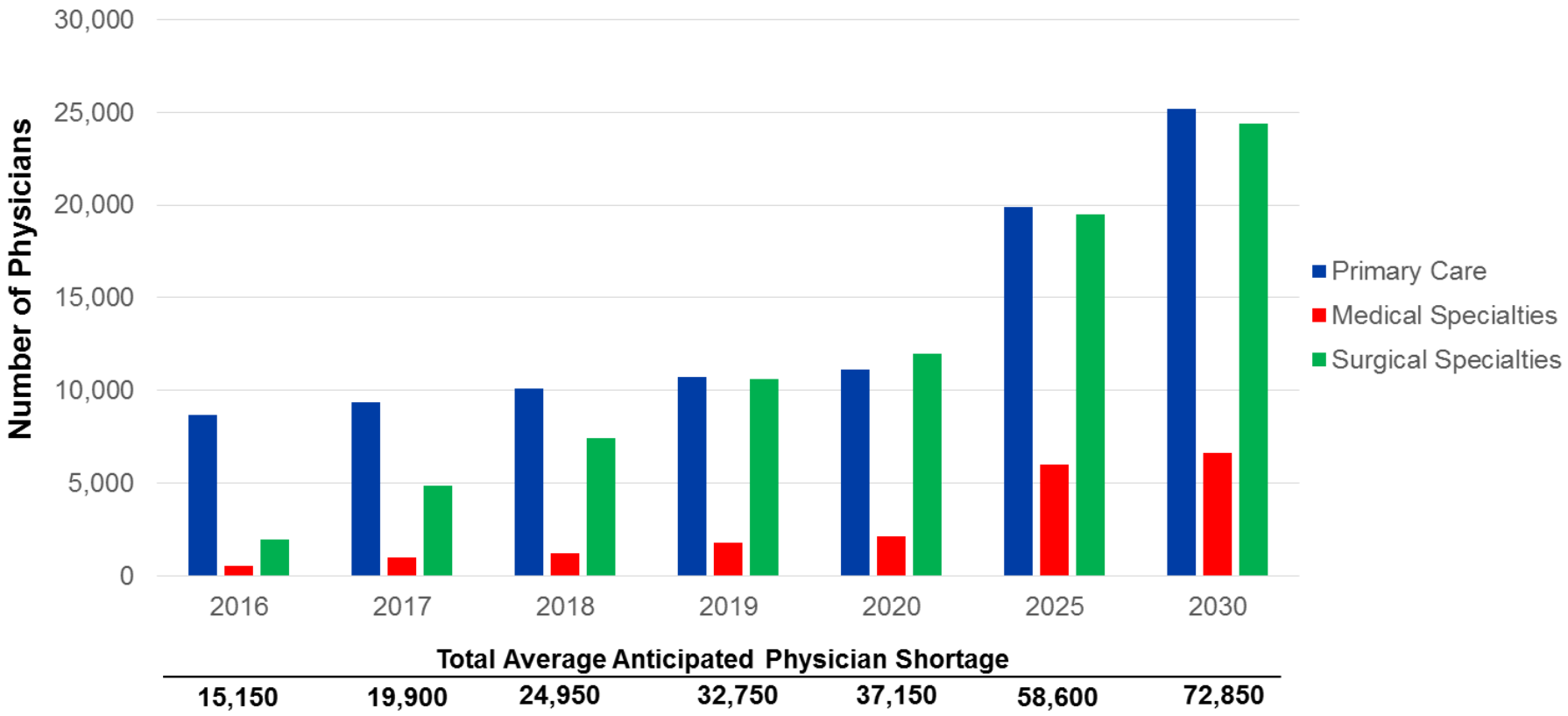
- Closing of Rural Hospitals
  - 64 closed between 2013 and 2017 (8 of those closed and reopened)
    - 77% of these were located in the South (22% in Texas alone)
    - > 50% were converted to another type of facility (urgent care, emergency care)
  - Over twice as many as the previous 5 years
  - Most were Medicare dependent
  - Rural hospitals in Medicaid Expansion states less likely to close

"RURAL HOSPITAL CLOSURES: Number and Characteristics of Affected Hospitals and Contributing Factors" U.S. Government Accountability Office, GAO-18-634, September 28, 2018, https://www.gao.gov/assets/700/694125.pdf (Accessed 11/29/18).

Competition Updates

Healthcare Supply Shortages

Anticipated Physician Manpower Shortages



"The Complexities of Physician Supply and Demand: Projections from 2015 to 2030" HIS Markit, Association of American Medical Colleges, February 28, 2017, https://aamc-black.global.ssl.fastly.net/production/media/filer_public/a5/c3/a5c3d565-14ec-48fb-974b-99fafaeecb00/aamc_projections_update_2017.pdf (Accessed 12/5/17), p. 50.

Competition Updates
The Year of the Mega-Mergers

- Payors
  - Cigna + Express Scripts
    - $52 billion deal
    - Combines 7th largest health insurance company and largest pharmacy benefit manager (PBM)
  - CVS + Aetna
    - $69 billion deal
    - Combines largest *retail pharmacy chain* and 3rd largest health insurance company
    - The horizontal consolidation portion of the merger (Medicare Part D Plans) had to be scrapped to pass DOJ review

"Merger of Cigna and Express Scripts Gets Approval From Justice Dept." By Reed Abelson, The New York Times, September 17, 2018, https://www.nytimes.com/2018/09/17/health/cigna-express-scripts-merger.html (Accessed 10/31/18); "Testimony Regarding CVS Health Corporation's Proposed Acquisition of Aetna Inc." By Richard Scheffler for the American Medical Association, June 19, 2018, http://www.insurance.ca.gov/01-consumers/110-health/60-resources/upload/Scheffler-CVS-Aetna-Testimony-06-19-18.pdf (Accessed 10/31/18).

Competition Updates
The Year of the Mega-Mergers

- Providers
  - Mercy + Bon Secours
    - 43 hospitals throughout the East Coast, OH, and KY
  - Advocate Health Care + Aurora Health Care
    - 27 hospitals throughout IL and WI
    - Became 10th largest U.S. non-profit hospital system
  - Memorial Hermann + Baylor Scott & White
    - 68 hospitals throughout over 30 Texas counties
  - CHI + Dignity Health
    - 139 hospitals – will be largest U.S. non-profit hospital system

"Advocate and Aurora to Merge, Creating Top 10 Health System Poised to Transform the Industry" Aurora Healthcare, December 4, 2017, https://www.aurorahealthcare.org/media-center/news-releases/advocate-and-aurora-to-merge-creating-top-10-health-system (Accessed 10/31/18); "Mercy Health and Bon Secours to merge" By Alex Kacik, Modern Healthcare, February 22, 2018, https://www.modernhealthcare.com/article/20180221/NEWS/180229982 (Accessed 10/31/18); "Struggling CHI stands to benefit from merger with Dignity" By Alex Kacik, Modern Healthcare, December 7, 2017, https://www.modernhealthcare.com/article/20171207/NEWS/171209893 (Accessed 10/31/18).

Competition Updates
Private Market Strategies

- Seeking to address healthcare supply shortages where government has failed to act
- Walmart
  - "*Healthcare Begins Here*" initiative
  - $4 Prescription Program
  - *Employers Centers of Excellence Network* (ECEN)
  - Potential partnership with Humana, to make Walmart one of the largest insurers in U.S.

"Making a Difference through Health: How PwC is Helping to Change Lives" Pricewaterhouse Coopers, December 2015, https://www.pwc.com/gx/en/healthcare/case-studies/making-a-difference-global-health-usa-case-study.pdf (Accessed 4/5/18), p. 15. "Walmart Announces Ambitious Goal: To Be the Number One Healthcare Provider in the Industry" By Dan Diamond, Forbes, October 6, 2014, https://www.forbes.com/sites/dandiamond/2014/10/06/walmart-announces-ambitious-goal-to-be-the-number-one-healthcare-provider/#1c3159f75be1 (Accessed 4/5/18). "Walmart in Early-Stage Acquisition Talks with Humana" By Dana Mattioli, Sarah Nassauer, and Anna Wilde Mathews, The Wall Street Journal, March 29, 2018, https://www.wsj.com/articles/walmart-in-early-stage-acquisition-talks-with-humana-1522365618 (Accessed 4/5/18).

Competition Updates
Private Market Strategies

- Amazon-J.P. Morgan-Berkshire Joint Venture
  - Announced January 2018
  - The non-profit will seek to utilize technology to cut employee healthcare costs
  - Have hired:
    - CEO, Atul Gawande, MD (surgeon, public health researcher and writer)
    - COO – Jack Stoddard (former Comcast digital health executive, has background with UnitedHealth Group)

"Amazon, Berkshire, JPMorgan's healthcare venture names COO" Reuters, September 4, 2018, https://www.reuters.com/article/us-berkshire-buffett-healthcare/amazon-berkshire-jpmorgans-healthcare-venture-names-coo-idUSKCN1LK2JX (Accessed 11/29/18).

Competition Updates
Micro-Hospitals

- Seek to bridge the gap between these urgent care centers and full service hospitals
- Have emerged as a popular option for:
  - Patients – Are typically conveniently located, and offer a shorter wait time than traditional hospitals
  - Providers – Relatively small overhead, can bill at hospital rates (in contrast to the lower rates billed by urgent care centers)
- Appear to be carving out a unique foothold in the marketplace by providing a balance between emergency and inpatient care and maintaining hospital services at the scale of an ASC

"Micro-Hospitals: Smaller Facilities with a Big Future" By Kim Slowey, Construction Dive, December 5, 2017, https://www.constructiondive.com/news/micro-hospitals-smaller-facilities-with-a-big-future/512235/ (Accessed 4/20/18); "Exploring the Growing Trend of Micro-Hospitals" By Conner Girdley and Tom Kim, Lancaster Pollard, https://www.lancasterpollard.com/the-capital-issue/exploring-growing-trend-micro-hospitals/ (Accessed 5/17/18).

Competition Updates
Valuation Implications

- The U.S. population is getting older and sicker, while there are fewer physicians available to care for them
- Private market trying out solutions to healthcare supply shortage problem that the government can't fix
- A shift away from the inpatient setting to micro-hospitals, urgent care and retail clinics
- Employers seeking to get rid of the "*middle man*"

Technology Updates
Telemedicine

- Another potential solution to physician manpower shortage and rising healthcare costs
- Biggest Hurdle to Innovation – Large discrepancies from state to state regarding telemedicine reimbursement
  - 49 states & DC reimburse for some form of live video for Medicaid FFS
  - 11 states offer some form of reimbursement for "*store and forward*" technology
  - 20 states reimburse for remote patient monitoring
  - 39 states & DC have laws governing private payor telehealth reimbursement policy

"State Telehealth Laws & Reimbursement Policies" Center for Connected Health Policy, Fall 2018, https://www.cchpca.org/sites/default/files/2018-10/CCHP_50_State_Report_Fall_2018.pdf (Accessed 11/29/18).

Technology Updates
Drug Pricing Changes

- Michigan & Oklahoma – Value Based Purchasing Contracts between Medicaid and drug manufacturers
- October 25, 2018 – Proposed plan to modify Part B payment model for pharmaceutical spending
  - *International Pricing Index* (IPI)
  - *Competitive Acquisition Program* (CAP)
  - *Average sales price* (ASP) add-ons

Letter to Kathleen Stiffler, State of Michigan Department of Health and Human Services from John M. Coster, PhD, RPh, November 14, 2018; Under the proposed program, Michigan Medicaid and each pharmaceutical company will agree to a payment for a medication in the event the drug works as claimed; if the prescribed medicine does not achieve the pre-determined clinical measures, the company will be required to send an increased supplemental rebate payment to Medicaid, effectively reducing the amount of money that the drug manufacturer would receive for the medication.

Technology Updates
Valuation Implications

- Technology may change the way care is delivered
  - Threats from substitute products or services (e.g., new drugs may reduce need for physician services)
- May change the type of assets valued
  - Shift to valuing more intangible assets

Questions?

If you have any questions regarding the content of this presentation, or on any other matter, please do not hesitate to contact us:

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