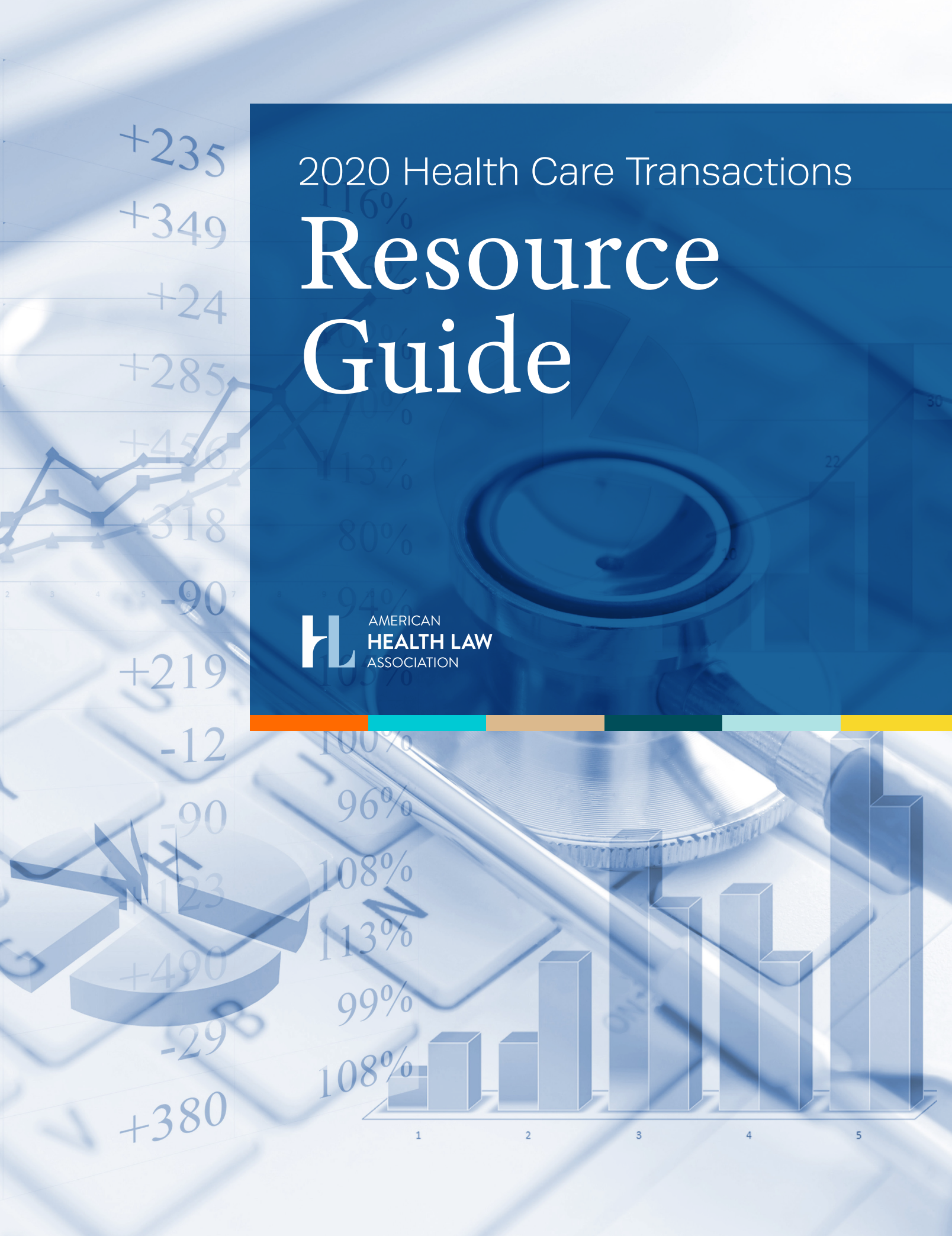


2020 Health Care Transactions

Resource Guide



Brand for Your Buck: Leveraging Brand as an Asset in Healthcare Alliances

Annapoorani Bhat, *Consulting Senior Manager* | PYA
abhat@pyapc.com

Jim Lloyd, *Principal* | PYA
jlloyd@pyapc.com

Michael Ramey, *Principal* | PYA
mramey@pyapc.com

The Cleveland Clinic, Mayo Clinic, and MD Anderson—each is a familiar brand name that signals high-quality patient care and outcomes. The far-reaching impact of these brands extends beyond the communities in which they first located. Hospitals seeking to strengthen their clinical know-how and differentiate themselves from other competitors within their respective markets have long sought alliances with these healthcare giants.

Similarly, regional and academic healthcare organizations with strong reputations, highly regarded service lines, and a commitment to high quality, are also exploring ways to leverage their organizations' valuable brands. Many smaller community hospitals lacking the resources to effectively compete on their own seek opportunities to affiliate with academic medical centers (AMCs) and larger health systems in their region. Such dynamics afford health systems with strong brands the opportunity to leverage their names for economic benefit through various forms of affiliations.

Typically, when an AMC or other health system with a strong brand enters into a joint venture, its ownership interest is determined based on its cash contribution or the value of contributed tangible assets. However, if the joint venture is to use the health system's brand post-transaction, this valuable intangible asset can also be considered a capital contribution. With greater awareness of the way in which a strong brand can help drive value in a new relationship, organizations across the United States are deploying various forms of branding arrangements as part of larger affiliation arrangements between healthcare providers.

Some branding arrangements are relatively simple, with standard rights and offerings provided by the licensor through a traditional royalty arrangement. These royalty arrangements usually involve annual payments for the association of the brand with local provider services and also may come with some clinical services or access to proprietary competencies of the licensor. Other more complex arrangements, such as clinical service lines, ambulatory services, or whole hospital joint ventures, may involve equity, control rights, monetary consideration, and/or preferred returns to the licensor in exchange for brand use in the venture.

An important first step in forming affiliations that leverage the brand's strength is to evaluate the brand's value, specifically the anticipated

incremental value that it will bring to the arrangement. Such valuations require a thorough analysis of multiple factors, such as each party's brand strength, competition for services, the margins achievable through the new venture, and ultimately, the anticipated impact of brand on cash flows. In the healthcare space, it is especially critical that the financial terms of these branding arrangements be at fair market value.

Brand as an Asset

A strong brand in healthcare can influence purchasers of care to select one provider over another in an otherwise intensely competitive market. Strong brands are usually tied to high quality, clinical innovation, and superior outcomes. Strong reputations and brands also help attract and retain top-quality physicians, academicians, and other clinical support staff. With the Association of American Medical Colleges predicting a national shortage of up to 121,900 physicians by 2035, attracting and retaining top-quality clinicians is a high priority for many hospital organizations.¹ While patients needing specialized services do seek out healthcare institutions that offer cutting edge treatment options, for many of the routine health services, patients can choose from a number of providers for the services they need. In such instances, a strong brand creates top-of-mind awareness, reduces perceived risks of seeing an unknown provider, and simplifies the decision-making process.

Patients needing specialized services sometimes must make the difficult decision to travel outside of their communities for medical care due to limited local resources. Fortunately, hospital alliances are making a positive impact on this issue. For example, an affiliation with cancer care networks, such as the Roswell Park Care Network² and the MD Anderson Cancer Network³ (to be elaborated upon later), allows community hospitals to benefit from these institutions' clinical expertise, signaling a higher level of care to their local communities, and thus reducing outmigration.

Brand affiliations almost always result in some knowledge transfer. The website for the Memorial Sloan Kettering Cancer Alliance elaborates as to why a partnership with such an organization may make sense for community hospitals:

“Across the United States, more than 80 percent of people with cancer seek treatment for their disease at a local provider in their community. But the latest advances in care and research can take years to reach these hospitals. The Memorial Sloan Kettering Cancer Alliance aims to bridge this gap through dynamic collaboration that allows community providers to offer state-of-the-art cancer care. With more than 130 years of experience in treating cancer, MSK has a unique opportunity to share the knowledge and best practices we have pioneered.”⁴

Types of Branding Relationships

The following are two examples of healthcare affiliations that typically involve co-branding:

Network Affiliations

Network affiliations provide a formal way for smaller organizations to gain access to additional clinical resources, otherwise difficult to obtain. Such arrangements typically include provisions requiring affiliates to adhere to certain clinical protocols and other processes in order to help prevent brand erosion. The Mayo Clinic Care Network and the MD Anderson Cancer Network are examples of such affiliation networks.

Mayo Clinic Care Network

In 2011, Mayo Clinic launched the Mayo Clinic Care Network (MCCN), a network of provider organizations that benefit from having access to Mayo’s expertise and physicians. The MCCN presently includes approximately 45 hospitals and health systems throughout the United States and internationally, each of which proudly proclaims its Mayo Clinic affiliation via marketing materials, on its website, and through other avenues. As part of the Mayo Clinic Care Network, affiliates can access Mayo Clinic’s clinical protocols, patient education materials, and physician resources, elevating the services they can provide.⁵

MD Anderson Cancer Network™

MD Anderson Cancer Network™ is a program of The University of Texas MD Anderson Cancer Center. The network offers three levels of membership: “certified,” “associate,” and “partner.” Certified and associate affiliates gain access to MD Anderson quality assurance programs and best practice guidelines. Partnering members receive full clinical integration. Associate and partner organizations are allowed to promote their affiliation on websites and in advertising. Cancer centers interested in becoming an affiliate undergo a rigorous review process, which typically takes six months and includes site visits and quality assessments by MD Anderson representatives. The review process also includes full assessments of potential candidates’ surgical, radiation, diagnostic imaging, and oncology departments.⁶ The implication is clear: only those organizations with the capability of maintaining, or advancing, the MD Anderson brand are admitted to the program.

Joint Ventures

Co-branding arrangements are common in healthcare joint ventures. Typically, the joint-venture parties contribute a variety of tangible and intangible assets, such as cash, equipment, clinical and administrative staffing, access to clinical protocols, and their respective brands. As indicated earlier, brands and other similar assets contributed to the joint venture can lower the amount of the cash investment otherwise required to obtain the desired ownership interest. Healthcare joint ventures are common in today’s competitive operating environment. Take Duke LifePoint Healthcare, for example, which involves a co-branding arrangement.

Duke LifePoint Healthcare

Formed in 2011, Duke LifePoint Healthcare collaborates with hospitals, physicians, and patients to bring quality and innovative healthcare services to communities.⁷ Better known as Duke LifePoint, this collaboration started many years prior when LifePoint Hospitals Inc. (LifePoint) approached Duke University Health System (Duke) for assistance in evaluating and improving a LifePoint area hospital’s cardiovascular service line. LifePoint saw clear benefits from leveraging Duke’s clinical and operational expertise and invested in a partnership that now helps bring about tangible improvements to an increasing number of facilities.⁸ Duke LifePoint pursues acquisitions, shared ownership, and governance of community hospitals seeking to participate in a stable, quality-outcomes-focused, well-funded system. Within that system, the functional roles of Duke and LifePoint clearly are delineated. Duke offers community hospitals clinical and quality guidance, as well as access to highly specialized medical services. LifePoint provides financial and operational resources, including access to capital for ongoing investments in new technology and facility renovations.

Evaluating Brand Strength

Determining the economic value that a brand may bring to a new affiliation transaction or arrangement is an involved process that requires analyzing a significant number of quantitative and qualitative factors. One such key factor is an entity’s brand strength. A brand strength assessment evaluates how interested parties (e.g., customers, patients, clinicians, etc.) view the entity’s services relative to those of competitors. Information and insights gained from evaluating an entity’s brand strength will assist in determining its value both on a stand-alone basis and relative to a transaction or arrangement.

A number of factors can influence a hospital’s brand strength, including:

Reputation

Among the elements that can shape the public’s perception of a health system, is its historical role in the community. For example, AMCs often serve as community safety net hospitals, ensuring care is available for the uninsured. While every community understands the critical need for access to care, such a designation can prove chal-

lenging to an AMC’s brand value. As a result, many AMCs devote significant resources to ensure the markets they serve are also aware of the research, medical advancements, and high level of specialized care they provide.

A hospital’s clinical accomplishments also influence reputation. Reports of bad outcomes, medical malpractice lawsuits, or the public release of data showing above-average infection rates can tarnish a provider’s hard-earned reputation.

Competition

To understand brand strength, it is important to evaluate the competitive landscape. Larger cities often afford multiple options for meeting patients’ medical needs. Brand recognition can be a key differentiator for healthcare organizations operating in highly competitive urban markets. The stronger the brand name, the greater the likelihood of retaining a loyal patient base and rising above the competition to be the provider of choice.

Provider Networks

Patients rely on their primary care providers to direct them to the right facility for surgery, imaging, and other services. Although health systems have frequently acquired provider practices over the last several years, many hospitals are now also employing non-acquisition strategies to affiliate with provider practices, such as co-management arrangements, joint ventures, and clinically integrated networks. These alignment strategies can be essential to the development of adequate provider networks, as well as improving hospital financial and clinical performance. They also create additional touchpoints and expand the visibility of the hospital or health system brand. A strong and extensive provider network is likely to have a positive impact on brand strength.

Patient Awareness and Loyalty

Evaluating brand recognition is a significant component of assessing brand strength. In the brand awareness continuum, potential patients first may become knowledgeable of a healthcare provider’s existence through advertisement, feedback from family and friends, or simply the provider’s physical presence. Through reinforcement, they move from “recognition” to a level of “familiarity,” resulting in top-of-mind awareness. Moving patients from brand familiarity to “loyalty” is the end goal of a healthcare marketing plan. However, the ultimate measure of the marketing plan’s success is the use of and patient promotion of the provider’s services.

Customer loyalty commonly is evaluated and measured by an organization’s Net Promoter Score⁹ (NPS), which is a metric developed from customer responses to just one or a few questions (e.g., “How likely would the individual recommend the [subject organization] to a friend or relative?”). Survey responses subsequently are compared to actual behavior over time, such as repeat business and referral activity, and then scored on a scale of 0 to 10. A comparison of NPS metrics among competitors also can be an effective way of evaluating brand strength. A comparable metric for hospitals is published on the Centers for Medicare & Medicaid Services (CMS) Hospital Compare website (Hospital Compare), where the percentage of “patients who reported YES, they would definitely recommend the hospital” is captured and updated each year.¹⁰

National Rankings

Multiple organizations, such as *U.S. News & World Report*, The Leapfrog Group, and Healthgrades, rank hospitals on a regular basis. The *U.S. News & World Report*’s annual “Best Hospital” rankings are highly coveted by many hospital executives seeking to distinguish their hospital’s services from competitors. Individuals can evaluate their options for healthcare services using Hospital Compare—its expanded hospital rankings include readmission rates, quality scores, efficiency measures, hospital-acquired conditions, and “never events” (e.g., surgery on the wrong limb).¹¹ Many hospitals pay—often at significant costs—to brand their websites or collateral marketing materials with rankings, awards, and scores.¹² Evaluating these rankings and ratings is an important part of brand strength assessments.

Brand Valuation Methodologies

Methodologies commonly used to value brands typically focus on the incremental value brands bring to the business enterprise. A brief overview of the most commonly used valuation methods in valuing brands follows. (The appropriateness of using one or more valuation methodologies will depend upon specific facts and circumstances.)

Relief-From-Royalty Method

The relief-from-royalty (RFR) method provides an indication of value based on the estimated royalty fees that could be avoided through ownership of the underlying asset, rather than licensing it from an outside party. As it relates to brands, the RFR method tends to be the primary approach when trying to determine what an upfront or ongoing payment should be to compensate for the use of the brand under an affiliation or a joint venture.

Brand Strength Continuum



The primary inputs for the use of this method are: (a) the selected royalty rate (or range of royalty rates) and (b) the attributable revenue stream. A royalty rate can be identified based on market data for similar assets, and certain other quantitative and qualitative factors relevant to the subject brand. This royalty rate is a proxy for the rate that a licensor and a licensee would negotiate for use of that brand if both had reasonably and voluntarily attempted to reach such an agreement. Because royalty rates from actual licensing agreements using hospital names are limited, the data search should consider related industries. Also, additional corroborative approaches may help create “bookends” to the analysis. The attributable revenue stream may include an existing revenue base or only consider incremental revenue. This will need to be assessed based on the facts and circumstances of each arrangement.

Incremental Benefits Calculation – “With and Without Scenario”

A provider deciding whether to affiliate with another organization must determine whether it will realize a positive return on its investment. To understand the incremental benefits of an affiliation, an organization can apply another approach commonly known as the “with-and-without scenario” calculation. The partnering provider will first assess the present value of future cash flows of its operations on an “as-is” basis and compare this business enterprise value to what would result from its affiliation with a national brand.

Such analyses are not pure financial calculations and can be complicated, as the affiliation also may involve management and professional services. To comply with Stark and Anti-Kickback regulations, it is imperative to first establish these agreements at fair market value before the eventual incremental benefit calculation is performed.

Protecting Brand Value

When developing arrangements that facilitate the contribution of the brand asset, it is important to document how the brand is to be applied in the context of the arrangement. Lack of clarity on form and function of brand use can create issues as the joint venture matures. For example, if an additional facility is constructed in a new location, or if a new service line is introduced, there must be clear guidelines for brand application to avoid ambiguity.

It is also important to make certain that the governance and operating structures provide the licensor with the necessary protection to ensure services delivered by the licensee are reflective of the desired level of quality and competency. In the healthcare industry, this can be achieved by establishing separate professional services agreements (PSAs) that provide for physician services and clinical expertise, or management services agreements (MSAs) that deliver administrative expertise that can elevate the customer experience at the affiliate or joint venture level.

Case Studies

It is helpful to consider every arrangement’s unique set of circumstances when determining if value can be attributed to the brand, and if so, what brand value would be. The following case studies illustrate varying arrangements and how brand value was determined in each circumstance.

Case Study 1: Cancer Center Joint Venture Between AMC and Community Hospital

In order to help elevate its clinical capabilities and to signal to its patient base that quality care was available within the community, a community hospital, inclusive of its existing cancer treatment facility, sought to establish a joint venture with an AMC whose brand was widely recognized, and also demonstrated high quality oncology care to its markets. The local hospital believed that its affiliation with the AMC would create opportunities for collaboration, provide access to clinical know-how, and help curb outmigration of patients who would drive past the community hospital’s facility to seek care elsewhere.

The initial allocation of joint venture ownership interest was based on the fair market value of the operations contributed by each joint venture participant. Additional ownership interest was then allocated to the AMC based on the fair market value of its brand name in the context of this proposed joint venture.

Here, the RFR method was used to determine the value of the AMC brand name in the context of the joint venture. A reasonable royalty rate range consistent with market observations for similar arrangements and assets was selected based on the strength of the AMC brand. This royalty rate range was applied to estimated and projected incremental net patient revenue based on market data for patient migration and the understanding that more patients would seek oncology services at the joint venture facility under an affiliation with the AMC.

Ultimately, this analysis determined a current value of the future benefits anticipated from the use of the brand within the context of the arrangement. The ownership percentage attributable to the AMC was more than merely the relative weight of contributed operations and cash, due to the value of the brand.

Case Study 2: Micro-Hospital Joint Venture Between AMC and Community Hospital

An AMC with strong brand recognition partnered with a community hospital to build a micro-hospital to serve a nearby rural community. The AMC was a significant provider of tertiary and quaternary services in the region and had invested heavily in marketing and community outreach. The community hospital was a much smaller market participant, known mainly within its immediate geography. The micro-hospital would be built to provide access to much needed care in the outlying community.

Under the proposed arrangement, the micro-hospital would be co-branded with both the AMC and community hospital. As part of the creation of the joint venture, each health system would contribute capital for the development of the micro-hospital. Additionally, the AMC evaluated its relative value contribution in the context of the joint venture.

A study of the AMC's brand was undertaken to determine its strength and competitive advantage in the primary and secondary service areas, where significant competition from other hospitals existed. The study involved the review of hospital ratings and rankings, accreditations, safety scores, breadth and depth of provided services, and the results of consumer surveys that measured patient awareness, and further, whether that awareness was translating into patient use of services (patient preference).

Once the brand strength in the primary and secondary service areas was evaluated, and it was established the AMC brand name was a contributory asset to the cash flows to be generated at the micro-hospital, a reasonable royalty rate was selected based on benchmark data, contribution margins, and other factors. This royalty rate was then documented within the arrangement as the formula for ongoing royalty payments during the term of the arrangement.

Case Study 3: Radiation Therapy Joint Venture Between AMC and Community Hospital

A community hospital operating a radiation therapy center sought an affiliation with an AMC to help improve the utilization of its center in a highly competitive environment. The cancer center also needed access to additional, highly specialized professional clinical services, and assistance with the center's administrative functions. As such, the parties entered into a joint venture, a PSA, and an MSA to support the enterprise.

The initial allocation of joint venture ownership interest was based on the fair market value of the operations contributed by each existing facility. Additional ownership interest was then allocated to the AMC based on the fair market value of its brand name in the context of this proposed joint venture.

The Incremental Benefits Calculation approach was used to determine the fair market value of the AMC's brand contribution. Once the incremental benefits were quantified, the result was translated into a percentage ownership interest. Part of the evaluation included an analysis to determine whether any AMC patients would seek care at this community facility due to proximity or other factors, thus cannibalizing the AMC's own patient base. Had that been the case, the revenue from these patients would have been excluded from the calculations.

Summary

Building and maintaining a strong brand in the healthcare industry involves substantial investments of time and capital. Strong healthcare brands are valuable because of their ability to support growth and profitability. Co-branding arrangements can have a material impact on joint ventures and other types of affiliation transactions, and the owner of such brands should be fairly compensated for allowing others the benefit of use.

PYA's valuation team has substantial experience assisting clients with a wide range of affiliation transactions including co-branding arrangements. For more information about PYA's transaction advisory and valuation services, contact Michael Ramey, Jim Lloyd, or Annapoorani Bhat at (800) 270-9629.

Endnotes

1. American Hospital Association, *AAMC updates physician shortage projections* (Apr. 25, 2019), <https://www.aha.org/news/headline/2019-04-25-aamc-updates-physician-shortage-projections> (last visited Mar. 12, 2020).
2. Roswell Park Care Network, <https://www.roswellpark.org/carenetwork>.
3. MD Anderson Cancer Network, <https://www.mdanderson.org/about-md-anderson/our-locations/md-anderson-cancer-network.html>.
4. Memorial Sloan Kettering, *MSK Cancer Alliance*, <https://www.mskcc.org/about/innovative-collaborations/msk-alliance>.
5. Mayo Clinic Care Network, <https://www.mayoclinic.org/about-mayo-clinic/care-network/members>.
6. MD Anderson Cancer Network, <https://www.mdanderson.org/about-md-anderson/our-locations/md-anderson-cancer-network.html>.
7. Duke LifePoint, *About Us*, http://www.dukelifepointhealthcare.com/about_us.aspx.
8. Advisory Board, *LifePoint CEO's partnership philosophy: Get 'in the trenches'* (May 17, 2016), <https://www.advisory.com/daily-briefing/2016/05/17/lessons-from-the-c-suite>.
9. Medallia, *Net Promoter Score*, <http://www.medallia.com/net-promoter-score/>. See also Frederick F. Reichheld, *The One Number You Need to Grow*, Harvard Business Review (Dec. 2003), <https://hbr.org/2003/12/the-one-number-you-need-to-grow>.
10. Medicare.gov, *Hospital Compare*, <https://www.medicare.gov/hospitalcompare/search.html>.
11. CMS, *Hospital Compare* (Oct. 19, 2016), <https://www.cms.gov/medicare/quality-initiatives-patient-assessment-instruments/hospitalqualityinits/hospitalcompare>.
12. Katie Bo Williams, *How much does using the U.S. News 'Best Hospitals' branding cost providers?*, Healthcare Dive (July 30, 2014), <https://www.healthcaredive.com/news/how-much-does-using-the-us-news-best-hospitals-branding-cost-providers/292206/>.

Ever step on one of these?

Sometimes it's the little things



If you've ever stepped on a LEGO® brick, you know this small misstep can produce big reactions. That's why PYA analyzes every detail of your transaction, no matter how small. For more than 35 years, our experts have guided the nation's leading healthcare organizations through the transaction process, delivering value while avoiding painful mistakes. We help you spot problems before you feel them, every step of the way.

Sample of Relevant Relationships

**BON SECOURS
MERCY HEALTH**


Dartmouth-
Hitchcock

 **EYECARE
PARTNERS LLC**


Queterra
capital

Baystate  Health

 **SHORE**
Capital Partners


SOUND
PHYSICIANS™


Waud Capital

Transactions Services

Operational Compliance Assessments | Due Diligence/Quality of Earnings | Strategic Assessments for Partner Selection
Revenue Integrity/Clinical Coding Compliance | Valuation Opinions | Regulatory Approval Assistance
Tax Planning/Compliance | Compliance Program Assessments | Post-Merger Integration Planning/Execution

WE ARE AN INDEPENDENT MEMBER
OF HLB—THE GLOBAL ADVISORY
AND ACCOUNTING NETWORK

800.270.9629 | pyapc.com

ATLANTA | KANSAS CITY | KNOXVILLE | NASHVILLE | TAMPA

LEGO is a trademark of the LEGO Group.

