

## Saving Our Center: How We Turned Around an Underperforming ASC

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### Risks vs. Opportunity

Roughly 30% of ambulatory surgery center (ASC) businesses fail, and many more never meet their financial goals and projections. That is a scary number for physicians to consider as they seek to develop their own ASCs, whether independently or as a joint-venture (JV) with a hospital. My experience in developing a multi-specialty ASC along with a group of colleagues and in partnership with a local non-profit hospital gave me real insight into the reasons behind those infamous statistics.

Our center did not fail per se, but a “cash call” (i.e., a re-investment by the surgeons and hospital) was necessary a year and a half after opening. A careful review of the numbers led us to the painful realization that we were losing money despite having a beautiful center patients loved, a steady stream of cases through our ORs, and generally efficient operations. But we were not meeting our projections. Bad contracts were the other fundamental problem we faced, though it took some time before we realized it.

However, after restructuring the business around properly aligned incentives and bringing in the right partner to manage operations at the center, performance turned around quickly. In fact, profits have recently been distributed among partners.

This article will highlight the mistakes we made in setting up the business, the resulting operational problems, and the steps we took to get the business back on track. It is a companion piece to an [article by my colleague, George Trajtenberg, M.D.](#), that discusses the requirements for structuring an ASC business as a JV with a hospital partner.

### Planning the Business

Six years ago, my physician-partners and I saw the writing on the wall – it was inevitable that an outpatient surgery center would be opening in our community and we wanted to play a role. The primary motivations of our group were to create an environment and culture where we could focus on doing the best work for our patients and gain more control over our schedules and lifestyle.

Naturally, our group liked the idea of ancillary income, but money was a secondary concern. We actually felt that an income stream from an ASC would be an effective way to boost the income of younger surgeons and, therefore, keep them in our community. And certainly we had no interest in hurting the hospital, which stood to lose cases.

There were several reasons we sought a JV with the hospital:

- The capital it could provide, which freed surgeons from writing big checks up-front;
- Our belief that hospital administration could provide financial, operational and management expertise the surgeons did not have;
- The PR value of the hospital's excellent name in the community, and
- A sense of guilt, as we would be taking a large number of cases out of the hospital.

All of these seemed like sound assumptions, but, looking back, it's easy to see that running a successful ASC requires different business skills and knowledge than running a hospital.

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### A Seemingly Great Start

To get the business off the ground, we hired a fee-only consultant to conduct a feasibility study, assist in design and construction of the new facility, help with staffing, and secure contracts with payers. We could have hired a development partner with a stake in the business, but neither the doctors nor the hospital wanted to dilute their ownership positions.

We worked in good faith to move the project forward, negotiating through several differences of opinion, including the question of whether anesthesiologists should be investors in the center. After more than two years of planning and development, we opened our doors. It was a beautiful facility, and from day one, things seemed to go very well. We had a steady stream of cases, good utilization and short OR turnover times. Most importantly, the outcomes and patient satisfaction were very high.

But soon enough the red ink on the balance sheet was too much to ignore. To diagnose the problems with the business, Dr. Trajtenberg and I went over every single assumption, and discovered that many of our problems were practically built into the business plan.

### The Diagnosis

We soon discovered that the initial feasibility study was built on inaccurate projections, in terms of both the volume and mix of cases. Some surgeons were too optimistic in how many procedures they could bring to the center. Because case volume represents the life blood of the business, projections must be rigorously and objectively reviewed, tested and verified by experts who really understand their meaning and value. For our center, the numbers were never sufficiently validated.

Another problem was sub-optimal reimbursement in most areas. It's impossible to overestimate the importance of strong contracts, and our center didn't have them in the beginning. In fact, the contracts we signed lead directly to our struggles. Further, we didn't realize that better contracts were possible. We also lacked contracts for carve-outs, implants and supplies. It's easy to overlook the many details involved in contracting and payer management (which are fundamentally different for ASCs and hospitals), but they can represent the difference between making and losing money.

In retrospect, other mistakes are obvious. For instance, hiring a fee-only consultant turned out to be a mistake. A partner with "skin in the game" is first and foremost concerned with the overall success of the center, rather than checking tasks off a to-do list. In fee-for-service relationships, consultants are not fully invested in long-term profitability. Their top priority may be to get contracts signed, not necessarily the best contract – that is, those that are most financially advantageous for the business.

Our consultant also underwent a restructuring of ownership and personnel changes during our project, developments which contributed to lengthy project cycles. Two full years passed from the time we chose the consultant to the opening of the center. I think a consulting firm motivated by the best interests of the business and with its own money on the line could have helped us avoid some of our mistakes and correct fateful decisions, and probably would have had a greater sense of urgency.

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I certainly don't mean to lay all the blame on the consultant. The physicians and hospital made mistakes, too, including one critical staffing error. The administrator we hired had run a profitable ASC, but, unlike our facility, it had no debt. We assumed he had the contracting and accounting expertise to do the job. Because of his presumed expertise, we limited the consultant's role after we opened and eliminated it one year after opening. Again, I don't mean to unduly fault the administrator, but billing, claims and coding problems mounted, and eventually we faced cash flow issues.

Perhaps the worst part was that the surgeon-partners didn't realize the extent or severity of the mistakes the business was making. Because none of the physicians really understood accrual accounting, we didn't know that appropriate adjustments had not been made. As a result, we couldn't clearly evaluate our situation. We assumed that our growing accounts payable was just the way ASC business worked. For six months we ignored that fact that we were failing. Due to accounting errors, we thought we would be okay if case volume increased, which turned out to be a false premise.

### A Recovery Plan

With an unprofitable center on our hands, we knew we had to take action. First, we renegotiated our debt structure with the bank and had our capital call. We tried to re-negotiate contracts, but we couldn't get very far with the payers. They probably knew we didn't have the leverage or necessary knowledge. And unbeknownst to us, they had incorporated us in the hospital's book of business. Then, we assessed our remaining options – either selling a portion of the center outright for a cash infusion (which seemed like a cure worse than the disease) or finding a new management partner with ownership interest.

Several of the prospective partners we talked to inspired confidence. One of the biggest national players obviously had the skills and experience to help us, but they demanded a large ownership stake, and adopted a “take it or leave it” approach. The management fee they proposed was more than they charged other ACSs in our area. That didn't seem in the spirit of true partnership. They talked a very good game, but were unwilling to “put their money where their mouth is” and link compensation to performance criteria. Still, because of their successful track record and our urgent need to stop the bleeding, we were very close to striking a deal.

Then, through the recommendation of a colleague at another center in the Philadelphia area, we met Blue Chip. Blue Chip's people were candid about where we'd gone wrong, openly shared their insights about how to fix the center, and had an inventive plan tailored to our specific situation and needs. Specifically, they understood the payer landscape and, based on their existing relationships, knew how to approach these companies with a mutually beneficial plan. They answered our questions honestly, which engendered trust in the relationship. This was the most critical point in our decision to move forward with Blue Chip as our new management partner.

***Hiring a fee-only consultant turned out to be a mistake. Equity-holding partners are motivated by the overall success of the business.***

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### Establishing Accountability

Blue Chip sought to be integrated into our business, aligning our business plan with theirs. Their willingness to balance risk and reward across all partners (including themselves) was another reason we chose them. In fact, they made their buying into in the partnership and management fee contingent on meeting specific performance targets and financial criteria.

Blue Chip bought most of the hospital's stake through a very creative arrangement whose value was demonstrated to initially skeptical hospital management. The hospital got to keep its seat at the table, maintaining some control and involvement, while the surgeons weren't diluted. The doctors also preserved their relationships with the hospital and continued to provide an asset in recruiting and retaining younger surgeons. Blue Chip took on all management responsibilities for a reasonable fee. But, basically, Blue Chip only makes money when the business as a whole succeeds. This is a win-win-win.

So what about the performance? I'm delighted to say the positive effects on the business were almost instantaneous. We negotiated better contracts on procedures where we'd been losing money, and covered carve-outs, implants and supplies. Improved claims, billing and accounting processes paid immediate dividends. Our previously uncontrollable accounts payable has fallen to almost zero and our new administrator can answer the phone without fear. Our partners were perhaps a little surprised how quickly profitability was achieved. Within six months of Blue Chip being in charge, we declared our turnaround a success and are very optimistic about the future.

### The Bottom Line: Profitability & A Bright Future

Surgeons who think hiring a fee-only consultant makes more economic sense than engaging an equity-holding management partner should consider how easy it is to lose money on an ASC. It's well worth investing in people who have the skills, knowledge and motivation to develop a solid ASC business model and then manage all the functions required to succeed over the long term.

You have to choose the right partner, of course, one that's willing to "put their money where their mouth is" and is as interested in promoting clinical excellence as in making money. Such a partner allowed us to move from sub-par performance to profitability in just a few months. And it gave us a clear, economically-beneficial way forward to provide quality care and a great experience in a center we and our patients love. In other words, our center not only looks great, but now the business performs beautifully, too.

*For more business best practices, please visit [www.bluechipsurgical.com/insights](http://www.bluechipsurgical.com/insights)*



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