

Potential Impact of CHAMP Section 651 Provisions on Valuation

The July 2007 Federal reauthorization of the State Children's Health Insurance Program (SCHIP) under the Children's Health and Medicare Protection Act of 2007 (CHAMPS) passed by the US House of Representatives [Bill # H.R.3162] contained initiatives in Section 651 aimed at eliminating the *whole hospital exception*. Although these provisions were not included in the final legislation vetoed by President Bush, there are indications that Section 651 language will again be proposed and, if enacted as part of future legislation, these provisions would have significant effects on physician investment time horizons and the valuation of surgical and specialty hospital enterprises.

Specifically, the CHAMP Section 651 provisions may obviate the economic ownership interests of physicians in legally held property under the valuation standard of *Fair Market Value* and the valuation premise of *value-in-use as a going concern*, resulting instead in lower values under the premise of *value-in-exchange* through *forced liquidation* (in contrast to orderly disposition) because of the insufficient exposure to market due to the 18 month compliance period.

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Additionally, CHAMP Section 651 provisions would put subsequent remaining physician investors' holdings in a minority position, resulting in an inability of physicians to control invested capital. The resulting lack of physician -investor control could affect investors' perceptions as to *risk* of the subject enterprise as related to future quality of care; convenience of provider and patient scheduling; and, the enterprise's ability to incorporate future technological innovations into the

venture. There is also the possibility of the loss of significant intangible asset value related to highly qualified, trained and assembled workforce in place, which physicians have excelled in developing, if physician participation in the surgical hospital investor pool is limited or prohibited, and general hospital systems or corporate buyers (to whom such workforce may be considered redundant) remain as the most probable owners.

With enactment of the proposed CHAMP Section 651 provisions, there may also be significant disruption of loan covenants guaranteed by physicians and their group medical practices which have invested in existing physician invested enterprises. This may have the unintended cascade-like consequence in visiting a catastrophic financial impact on the viability of those physicians' medical practices and may also result in personal loss of physician credit standing. Consequently, this may, in some cases, have an impact on the ability of physician owned facilities to maintain liquidity and, ultimately, creditworthiness and solvency, due to the disruption of working capital necessary to meet financial obligations, including the deleterious impact on the capital structure of physician invested hospitals resulting from the forced liquidations of physician equity which would change the balance of working capital and related lines of credit.

It should be noted that, aside from the proposed CHAMP Section 651 provisions, several states are also now moving forward with their own initiatives to limit physician ownership in surgical hospitals and other specialty providers, through such means as Certificate of Need (CON) and State self-referral regulations.



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