Creating a Joint Venture with a For-Profit Inpatient Rehabilitation Provider

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As hospitals migrate from a revenue base built on patient volume to one based on value and quality outcomes, the pressure to control costs and maximize revenue has escalated. In recent years, many organizations have looked beyond cost cutting toward affiliations and partnerships that create economies of scale, conserve precious capital, and spread risk. One option includes creating a joint venture between a health system's inpatient rehabilitation unit and a national for-profit inpatient rehabilitation provider with a hospital ownership percentage near 50%.

Joint ventures with for-profit inpatient rehabilitation providers can bring additional cash flow and profitability to a health system via the for-profit entity's managerial proficiencies. They are often able to do this by bringing core competencies that acute care hospitals may not have. National rehab providers specialize in this industry, and bring attention to detail to the rehab unit that is often absent when it is operated as a service line or cost center within a hospital. One common capability brought by these operators is an increase in the retention of inpatient rehab eligible patients that currently leave the health system, but could be kept in house. Health systems often have rehabilitation patient leakage that they are unaware of which these operators can identify and contain. This frequently includes recognizing those patients that are currently being sent to non-rehab facilities, including, but not limited to, nursing facilities, and outside the health system. The expertise of the manager can also help the joint venture better navigate complex compliance-related issues.

Inpatient rehab joint ventures are typically able to lower expenses from historical levels. They are able to do this by utilizing economies of scale given the size of the for-profit organizations, most notably supply expense, but also by using big data and their deep rehab experience to analyze other areas where costs can be cut. Further, for-profit providers typically have staffing models that can contain costs while maintaining the quality of care for the patient. Reimbursement is less commonly an area for improvement, as the for-profit entity commonly leverages the hospital partner's experience with managed care in its local market, but sometimes efficiencies can be identified here as well.

A management fee in typically charged for these services, but the overall expenses of the unit are still usually lower than its operations before the joint venture. However, despite the additional management fee and no longer having a 100% ownership interest in the service line, the return to the hospital is regularly greater than it was as a stand-alone department.

Creating a joint venture can also deter other rehab providers from entering the market. In states where a certificate of need is not required to open an inpatient rehab facility, joint venturing with a for-profit provider gives other national providers pause when considering opening a free standing center of their own as there is less opportunity to gain market share.

While varying from entity to entity depending on preferences, nearly all rehab joint ventures form a distinct board of directors. Having a board that is rehab focused helps emphasize rehab-specific issues that may be lost when it is a department in a health system. The board's makeup generally reflects the ownership interest of each entity. As previously mentioned, typically the health system owns about 50% of the joint venture. This helps safeguard both parties' interests and allows governance matters to be settled fairly. However, it is not uncommon for the joint venture's organizational document to specify certain decisions requiring a supermajority.

These joint ventures often build a freestanding rehabilitation facility once created with the service line while remaining in its current space until the new building is complete. The new facility customarily has all private rooms which are seen as attractive to both patients and providers. Depending on its previous setting, this can potentially offer relief to hospitals coping with limited space. When the rehab service line moves to the joint venture's new facility, hospitals can expand higher margin services into the vacated in-house space.

Once a health system chooses to pursue joint venturing its inpatient rehabilitation unit, the following steps should be taken:

– Obtain a valuation analysis in order to estimate the hospital's contribution to a joint venture.

– Identify potential joint venture partners for the rehab service line.

– Issue a request for proposal to gauge interest and narrow down the list of potential partners.

– Perform due diligence on remaining partners and schedule management interviews.

– Select a final partner and move forward with a letter of intent.

A joint venture with a national for-profit rehabilitation often leads to higher profitability and cash flow to a hospital. These joint ventures often improve the level of service in a community by providing more robust rehab services, opening up space for more services at the parent hospital, and contribute to the financial strength of a health system.