ACCOUNTANTS,
CONSULTANTS &
BUSINESS VALUATORS

HOME HEALTH CARE
AN INDUSTRY STUDY

Things you will learn from this whitepaper:

1. What are the valued added services now being offered by the home health care industry?
2. What are the contributing factors to the usefulness of home health care?
3. What are the most common challenges facing the home health care industry?

This whitepaper will have special interest to:

1. Attorneys consulting with home health care owners considering mergers or acquisitions.
2. Judges presiding over business disputes & litigation cases.
3. Business mediators & arbitrators.
4. Those concerned with the valuation of the home health care industry.

Notice & Disclaimer

In a forensic accounting setting, the purpose of an industry analysis is to allow a comparison of the subject company to its industry. This comparison is vital to assess the strengths and weaknesses of the subject company, as well as its industry and company specific risks.

The following study contains a brief, selected analysis of the specified industry. It is based upon a review of current economic statistics, articles in the financial press, reviews found in current business periodicals and information posted on numerous internet sites. It does not purport to be all-inclusive or to contain all of the information which a prospective investor or lender may require. Projections and opinions are based upon information provided by third parties. We make no representations or assurances that this information is complete or accurate. Neither Mark S. Gottlieb, CPA, PC nor any of its officers, employees, or representatives make any representation as to the accuracy of completeness of this report or its contents, nor shall any of the foregoing have any liability resulting from the use of the information contained herein or otherwise supplied.

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Industry Overview

The U.S. home health care industry is comprised of over 20,000 service providers, a staggering increase from 1963, when only 1,100 home health care providers existed. Estimated annual revenue for these firms, taxable and tax-exempt combined, tops $36 billion annually. Home health care firms deliver services to more than 7.6 million individuals, or roughly 2.8 percent of the U.S. population. Of all recipients, 68.6 percent are over the age of 65, and 62.3 percent are women.

Clients typically require services due to permanent disability, long-term health conditions, acute illness, or permanent illness. Specific conditions requiring home health care most frequently include diabetes, heart failure, chronic ulcer of the skin, osteoarthritis, and hypertension. Advances in medical devices and technology have made home care a viable alternative to institutional care for the treatment of such conditions, and although hospitals remain the primary providers of medical services, home health care services have capitalized on the need to lower the overall cost of medical care.

In addition to offering lower health care costs, home health care providers are supported by the fact that a majority of patients prefer to receive treatment in the comfort of their own homes. Medicare-certified hospice agencies, for example, expanded from a mere 31 establishments in January of 1984 to 2,444 such firms in December of 2003. The industry overall grew most dramatically around the turn of the 21st century, with total spending for home health care services skyrocketing from just $4.7 billion in 1997 to $38.3 billion in 2003.

Operations

Home health care services may be owned by various entities, including: government, hospitals, private companies, nonprofit organizations and visiting nurse associations. Private companies own 46 percent of all home health care agencies, and hospitals are second with approximately 27 percent. Around 12 percent are owned by nonprofit organizations or visiting nurse associations, and another 12 percent are government owned. Among providers not owned by the government, roughly 75 percent are owned by local health care firms.

Regardless of ownership, most health care providers offer a broad range of temporary and ongoing services. Respiratory therapy programs are a prime example of ongoing services; these provide air support for patients suffering respiratory ailments such as asthma, bronchitis and cystic fibrosis. Other ongoing services include: delivery of nutrients intravenously or through feeding tubes; the intravenous infusion of antibiotics to treat infectious diseases; and infusion therapies for patients with fully or partially dysfunctional digestive tracts. Temporary services may include physical therapy for post-operative and recovering patients, or for terminal, hospice patients.

Because home health care services are more limited in scope than hospital services, and because home health care relies on workers with fewer qualifications and skills than hospital staff, home health care can be offered at a much lower cost to providers than institutional or hospital care. Common services include:

- Part-time or intermittent skilled care
- Physical therapy

- The administration of medicine, rehabilitation, durable medical equipment and supplies
- Home health aide services
- Family and patient education

These services are generally divided into the following:

- Prevention
- Diagnosis
- Infusion therapy
- Skilled care
- Unskilled care
- Durable medical equipment

Of these, the three largest categories are infusion therapy, skilled care, and durable medical equipment. Infusion therapy consists of the delivery of intravenous products and services such as fluid replacements, chemotherapy and antibiotics. Skilled care includes nurses, home health aides, and therapists, all under the direction of a remote physician. Durable medical equipment includes ventilators, respirators and wheelchairs, and has grown rapidly due to advances in technology. According to study by Citigroup Smith Barney, home medical equipment services alone were valued at $13 billion in 2003.

Of the home health care industry's 20,000 agencies, 7,265 were certified by Medicare through the mid-2000s. This demonstrates a significant increase from 6,861 certified agencies in 2001. Such certification is highly desirable for firms, as Medicare pays the largest portion of home health care expenses, covering 31.9 percent, or $12.2 billion of total expenses. Private insurance payers and out-of-pocket payments are tied for second, with an 18 percent contribution each, totaling $13.8 billion. Medicaid accounts for a much smaller contribution, and state and local governments also cover a small portion of payments.

In order for a patient to qualify for home health care coverage under Medicare, a physician must determine that such care is necessary, that the care will be intermittent in nature, and that the patient is generally homebound. Medicare then covers:

- Part-time or intermittent nursing care
- Physical, speech, and occupational therapy
- Medical social services
- Equipment and supplies

For terminally ill patients, Medicare covers care provided by certified hospice organizations. Such providers specialize in pain relief, symptom management and general supportive services. In both curative and terminal scenarios, care is designated either full-time or part-time, with full-time care constituting services rendered in excess of 28 weekly hours (regardless of the number of providers). Such provisions have existed since Medicare’s enactment in 1965, when federal funding for home service care of the terminally ill became standard.

Medicaid, another social service provided by the U.S. government, also covers claims by clients of home health care providers, though the scope of coverage is significantly smaller. Unlike Medicare, Medicaid disseminates payments for home health care in three main categories: the traditional home health benefit (a compulsory provision by all states) as well as two optional programs: personal care and home/community-based waivers.

Government Involvement

Payment provisions such as Medicare and Medicaid notwithstanding, government involvement has an enormous bearing on the home health care industry. As with the health care industry at large, virtually every segment of home health care is influenced by legislation, social policy, and funding allocation. In a sense, the home health care industry lies at the center of a long-running national debate.

The Balanced Budget Act of 1997 illustrates this fact nicely. With this piece of legislation, annual reimbursements for home health care firms were capped on a per-patient basis, and providers were compelled to purchase surety bonds. The purchasing of bonds is currently overseen by the Centers for Medicare and Medicaid Services (CMS). In addition to changing the manner in which home health care firms provide basic services, the surety bonds enactment has complicated administrative responsibilities for most providers. Between 1997 and 2002, more than 3,500 agencies had either closed or quit accepting Medicare patients, according to the National Association for Homecare.

Equally as jarring to the industry was the Medicare Modernization Act of 2003. This controversial Act made large-scale changes to the amount and type of reimbursement entitlement for home health services that provide medical equipment to patients. Since this branch of services is one of the quickest growing and most highly profitable for firms, many providers have had to scramble in order to maintain profits in this volatile category. The legislation also introduced competitive bidding for contracts regarding the provision of medical equipment and Medicare billing, putting pressure on firms to lower cost of services in order to remain viable.

Industry Standards

Firms within the home health care industry may seek accreditation from The Joint Commission on Accreditation of Healthcare Organizations. Accreditation increases legitimacy and firm visibility, and is necessary to receive payments from government payment programs such as Medicare and Medicaid.

State and local governments also regulate the industry, often setting policy encouraging the utilization of home health care providers. For example, some states have imposed stays on nursing home construction, intending to funnel more patients toward home-based care. Recently, much legislation has concerned itself with the need to reconcile an aging U.S. population with reduced government spending, and some health care services have benefited greatly from such policies concerning funding

Workforce

Home health aides hold roughly 624,000 jobs. According to the U.S. Department of Labor, Bureau of Labor Statistics, overall employment of home health aides is projected to grow much faster than the average for all occupations through the year 2014. This will proceed from growing demand for home services, alongside efforts to limit overall healthcare costs.

Median hourly earnings of home health aides were $8.81 in May 2004. The middle 50 percent earned between $7.52 and $10.38 an hour. The lowest 10 percent earned less than $6.52, and the highest 10 percent earned more than $12.32 an hour. Median hourly earnings in the industries employing the largest numbers of home health aides by program in May 2004 were as follows:

- Nursing care facilities- $9.11
- Residential mental retardation, mental health and substance abuse facilities- $8.97
- Home health care services- $8.57
- Community care facilities for the elderly- $8.57
- Individual and family services- $8.47

Pay is fairly low for home health aides because little education is required; few firms require high school diplomas for workers. About 75 percent of aides work full-time, and the workforce is finally beginning to unionize. Training is provided to inexperienced workers by firms, and most workers are expected to pass a competency evaluation at the end of the training period. Aides who pass this evaluation are then registered as certified nurse assistants (CNAs) in state registries of nursing aides. If a firm wishes to receive reimbursement from Medicare, Federal law requires its home health aides to pass a competency test administered by the National Association for Home Health Care, covering:

- Communication
- Documentation of patient status and provided care
- Reading and recording of vital signs
- Basic infection-control procedures and maintenance of a healthy environment
- Basic bodily functions
- Emergency procedures
- Physical, emotional, and developmental characteristics of patients
- Personal hygiene and grooming
- Safe transfer techniques
- Normal range of motion and positioning
- Basic nutrition

Home health aides typically receive orders from registered nurses, physical therapists, or social workers. It is the health aide's duty to keep records of services provided and to record the condition of his or her patient. Depending on an aide's level of training and experience, various duties may be performed. The most experienced aides deal with medical equipment such as ventilators and respirators, in addition to performing basic support services.

There exist two primary organizations seeking to pair home health aides with employers. The National Association for Health Care Recruitment provides information, education, and networking for health care center recruiters. In addition, Cooperative Home Care Associates assists home health aides

in finding above-minimum-wage jobs. These organizations play an important role within the industry, as job turnover among home health aides continues to be high.

Industry Opportunities

Aging Population — Currently, over 24 million of the 77 million baby boomers have reached the age of 50, and by 2030, individuals aged 66 to 84 will comprise approximately 20 percent of the U.S. population. This trend will promote a rise in the demand for home health care services. The fact that the average lifespan of Americans continues to increase will also be a boon to the industry.

Hospice Providers — The high returns associated with Medicare reimbursement rates for hospice providers has lead many investor-owned companies to acquire or establish firms specializing in these services. This has fueled stock prices for hospice operations, encouraging many firms to either establish hospice programs or expand existing hospice operations.

Improving Technology — Advancements in technology have provided the industry with an ever-expanding array of options. Laptop computers allowing caregivers to enter data directly into electronic medical records have streamlined operations, and the utilization of digital cameras to send images to doctors for evaluation have reduced physician visits, increasing the utility of aides. While implementation costs may be high, such technology has greatly expedited operations for many firms.

Patients have begun to avail themselves of home care technology, as well. Vital signs may now be checked by patients themselves, with results transmitted via computer or telephone. Devices alerting patients when to record blood pressure, temperature or pulse have become common. Data are automatically sent to a nurse or physician who reviews the information. According to analysts at Forrester Research, the market for self-administered home health care technology is projected to reach $34 billion by 2015.

Public Support — Because home health care allows patients to receive treatment in the comfort of their homes while taking an active role in the health care process, general public support for the industry has always been high. The cost-effective nature of services has provided firms with another lobbying tool: for the year 2000, home health charges averaged $100 per visit, whereas daily hospital charges averaged $2,753. Despite recent legal issues, public support and demand for services within the industry appear robust.

Industry Challenges

Ethical Concerns — Much like the health care industry at large, ethical issues are a constant concern in home health care. Most recently, companies providing infusion therapy services found themselves the subject of public outcry, when it surfaced that many physicians were receiving weekly stipends for referring patients to firms. Along the same lines, some home health care firms had hired physicians from whom they bought infusion therapy practices, giving the appearance that the physicians were retained merely to write prescriptions for the company. These issues were brought to the legislature, and many states approved laws barring physicians from having financial relationships with various types of home health providers.

Legal Worries — Industry leaders such as Aetna U.S. Healthcare, Apria Healthcare, Tenet Healthcare Corporation and Columbia/HCA have faced a spate of lawsuits in the past decade. Other large players such as Coram have been done under completely by litigation. Lawsuits have revolved around issues such as reimbursement for services, fraudulent billing and suspect contracting with pharmaceutical companies. Although the industry has rigorously attempted to improve its reputation of late, the financial and social impact of such accusations continues to reverberate among home health care providers.

Reimbursement Cuts — In keeping with the concepts behind the Balanced Budget Act and Medical Modernization Act, state and federal governments constantly seek to rein in overall medical costs, including reimbursements paid to home health care providers. At best, changes in reimbursement policy add administrative headaches to providers; at worst, they diminish profit capabilities, and in some cases, force some providers to close their doors for good.

Industry Outlook

Since 1993, the rate of growth in health spending has roughly matched growth rates in the economy as a whole, and overall health care spending is projected to grow at a rate of 7.2 percent through 2015. With the increasing popularity of home health care services, the industry appears poised to capitalize upon this market potential. Annual growth of 13 percent over the first five years of the 21st century affirm this trend, with public payers, particularly Medicare, providing a boost. By 2015, average growth is expected to settle around 10.9 percent.

If the industry can continue to find and train workers, and avoid radical shakeups due to legislation such as the Medicare Modernization Act, advancements in technology should continue to pad profits. Public sentiment seems to move further toward home health care services with each passing decade, and the industry's fragmented nature should allow it to absorb specific demand for services. Overall, revenue trends are promising and sentiment within the industry is high.

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