

## **Freestanding Day Surgery Centres**

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**Published 2006**

### **Abstract**

The 1990's saw the rise of a number of different types of property assets. Freestanding Day Surgery Centres are one of these new asset types. They are neither hospitals nor medical centres. This paper looks at their development as a sector and identifies issues with regard to their investment performance and valuation.

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## Introduction

Two of the significant advances in medical technology in recent decades have been the reduction in the invasive nature of surgical procedures and the rise of intravenous sedation. These two trends have changed many operative procedures from large incisions where the patient was still “groggy” the next day to very small incisions where the patient is “well awake” within hours. These trends have contributed to the development of day surgery centres and day surgery units as a completely new class of property.

These changes have not necessarily reduced the time in surgery however they have significantly reduced the recovery time; which is when the patient recovers from the anaesthesia and is fit for discharge.

The reduction in recovery time has resulted in a reduced requirement for hospital beds for operative procedures. It is this reduction in requirement for hospital beds (overnight stays) that has given rise to this new day surgery property class and the associated valuation and investment approaches, which it requires.

Hospital valuation (and potential profitability) is based on the number of licensed beds. Day surgery centres do not have these beds and function differently as an asset class. Hospitals, especially larger hospitals, have “drawing power” in that they attract surgeons (and their patients) to them. The “drawing power” of day surgery centres reflects their low capital and ongoing cost structure, together with high patient efficiency and cost effectiveness, such that a large number of operations/procedures can be carried out on a day only basis with the same (if not higher) standard of quality and safety of patient care as is produced by hospitals.

Modern day surgery in Australia started approximately 25 years ago, however in the last 10-15 years the “freestanding” day surgery centre as a business has expanded rapidly.

### The Difference between Day Surgery Centres and Medical Centres

Medical centres are properties that contain a number of consulting/procedure rooms plus reception and administrative facilities. Some of these properties are purpose built as medical centres while others have been converted from a previous use (commercial/residential). They can be part of a larger complex containing associated medical uses (pathology, chiropractor, chemist) or other medical centres.

Day surgery centres are premises that are specifically set up to undertake operations under anaesthetic (general, IV sedation, regional block) and contain operating theatres, pre-op and recovery rooms, consulting rooms plus reception and administrative facilities. These are specialist constructed or adapted properties as the surgery usage requires additional building items (higher ceilings, air conditioning capacity, plumbing and medical gas reticulation, generator backup and additional lift capacity). Many traditional hospitals (both public and private) are able to undertake operations on a day surgery basis.

Many medical centres are called “Day Surgeries” and are capable of performing minor surgical procedures (eg mole removal, incising boils). This is termed **Office Based Surgery**. Different state legislation governs what activities (incising skin, type of anaesthesia) can be undertaken in office based surgery. Day surgery centres are licensed for surgery; medical centres are not licensed for office based surgery at the present time.

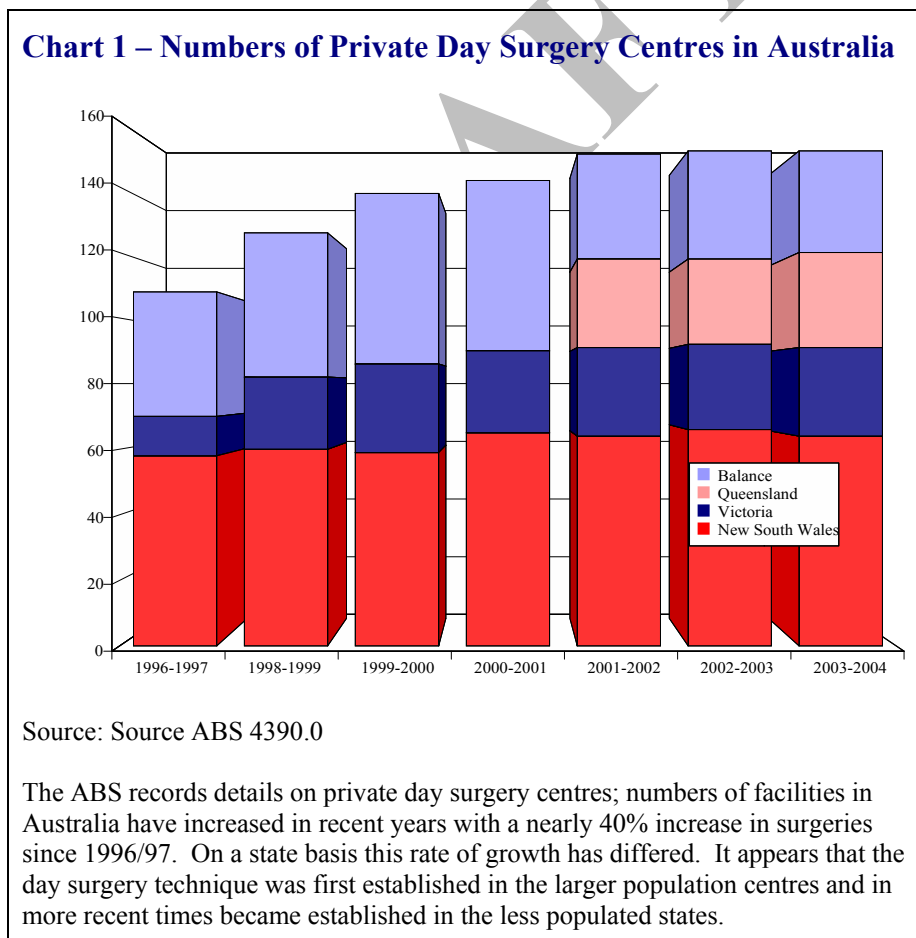
**Day Medical Centres** are premises for haematology/oncology, sleep disorders, sports medicine, fertility clinics and rehabilitation treatments.

## Day Surgery Centres

Day surgery centres are specialised facilities that enable patients to gain access to specialised surgical services and return home the same day. These facilities can be organised in the following ways:-

- A hospital (public or private) may provide day surgery services in parallel with inpatient services using existing admitting areas, wards, operating theatres and recover rooms;
- A hospital (public or private) may establish a day surgery facility within the hospital, sharing the theatre and recovery areas, but with separate admission and ward areas;
- A purpose built facility within an existing public or private hospital with its own admission, theatre, recovery and discharge areas; and
- A day surgery facility may be freestanding and purpose built. It may be managed by an existing hospital or operated independently.

Day surgery centres are licensed under the health regulations in their home state and consequently the precise definition varies from state to state.



## **Accreditation and Licensing**

Day surgery centres are required to be licensed under their relevant state health departments to perform day surgery procedures. Following this licensing the Commonwealth Department of Health and Ageing issues the day surgery with a provider number. This provider number then allows the day surgery business to negotiate with the health insurance funds.

Similar to a hospital, day surgery centres are constructed and fitted out to strict guidelines. In the initial development of the industry the Australian Day Surgery Council wrote the professional standards for establishments. These standards incorporate building construction and facilities, layout and services; medical, operational and administrative procedures; professional standards and principles of patient care. Accreditation of day surgery centres under these professional standards to ensure high standards is strongly advised, but not compulsory.

## **Components**

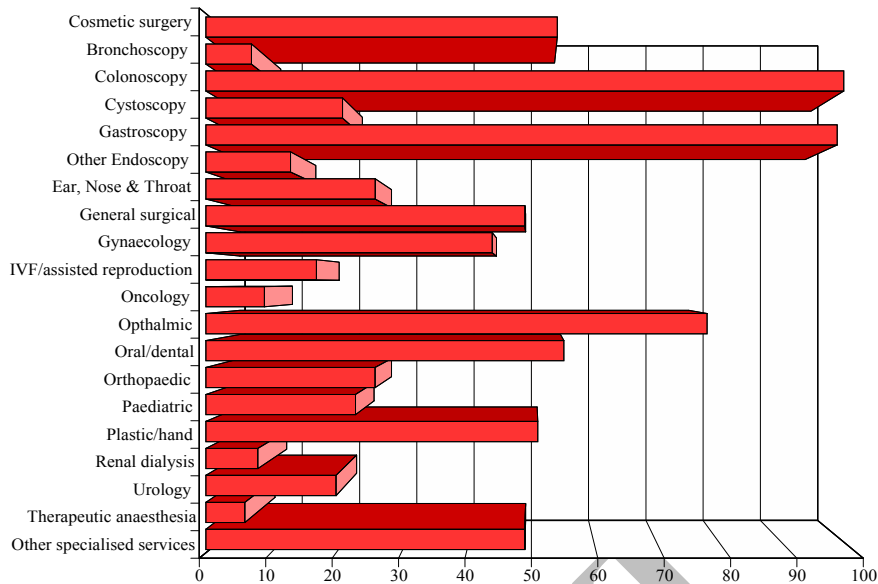
The major components of and activities within a day surgery centre comprise the following.

- Admission area, where the patient is admitted, administrative records are stored and comprises the initial waiting area.
- Consultation rooms where the patient has a pre-operative consultation; some tests may be carried out.
- Pre-operation area where the patient has changed into operating robes and waits for their procedure.
- The theatre where the procedure is carried out. A further refinement of the industry comprises theatres being set up for particular operations (eg knees, eyes). Surgeons are then able to streamline a series of similar procedures, facilitating “medical manufacturing” with the implied cost efficiencies.
- Recovery area, where the patient regains consciousness under constant nurse monitoring. Once they are able to walk and dress themselves they then move to the second recovery area which has easy chairs, a TV for entertainment plus some light refreshments (coffee, tea and Arnott’s Assorted Cremes).
- Discharge area where the final paperwork is completed and the patient goes home with a carer.

Further components include stores for medical equipment, service rooms for activities, changing and lounge room for surgeons and theatre staff plus conference and meeting rooms for staff and other functions.

The design of a day surgery centre incorporates a layout that facilitates the movement of clean items, equipment, linen, air conditioning to dirty areas and does not allow contamination back from dirty areas to clean ones.

**Chart 2 –Number Of Private Day Surgery Centres Offering Specialised Services - Australia 2003-04**



Source: Source ABS 4390.0

A range of specialised treatments is performed in private day surgery centres with the largest component comprising endoscopies of various types. It is estimated that 100% of endoscopies and the majority of ophthalmology procedures are performed in day surgery centres.

## Rationale for Growth

Apart from the advances in medical technology, causes for the growth in the numbers of private day surgery centres and the operations/procedures performed in them include the following.

- Advances in medical technology are resulting in increasing costs consequently medical practitioners and administrators are implementing ways of saving costs in other areas.
- Day surgery centres require less staff in comparison with surgery undertaken in a full hospital; also the facilities and staff are not needed at night, weekends or public holidays. Therefore, there is a reduction in costs in undertaking procedures in a day surgery centre.
- Government policy; as governments fund a significant component of medical facilities and services they are aware that costs can be mitigated by reducing hospital stays. This has resulted in a greater proportion of procedures being undertaken in private day surgery centres.
- Compared to hospitals, there are lower construction and ongoing costs. Coupled with premises size requirement of around 1,500m<sup>2</sup> - 2,000m<sup>2</sup> it is considerably cheaper to develop a day surgery centre.
- Consumer demand; patient awareness of the disruption that is attached to hospital stays (coupled with a popular perception that hospitals are not healthy places) has resulted in patients being more comfortable with and often preferring day surgery.

Further trends that have been noticed in the private day surgery industry echo those in the private hospital industry including the growth of national chains (Ramsay Health, Affinity, DCA) running “branded” hospitals and associated medical facilities. The benefits of a national chain include centralisation and specialisation of many administrative and management functions enabling the practitioners to concentrate on the medical component of their business.

Currently (2006) around 50% to 60% of all surgery in Australia is performed in day surgery centres; following the North American example, this proportion is expected to increase to around 80%. This will leave around 20% of all surgery that for reasons of recovery and complexity can never be (under current parameters) performed in a day surgery centre.

As the proportion of procedures undertaken in day surgery centres increases they will encompass procedures that have longer recovery and potential complication issues (in short all the “easy” procedures have already been moved to a day surgery environment). This then results in the requirement of some form of extended recovery facility or a medi-motel.

### **Extended Recovery Units and Limited Care Accommodation (Medi-Motels)**

One of the limitations to increased growth of day surgery centres is there are a number of procedures that are not currently undertaken in day surgery centres as patients are insufficiently recovered to be discharged on the same day. Elderly, those from regional/remote locations and those without adequate social backup are often unsuitable for discharge on the same day. The standard recovery areas of day surgery centres (freestanding or otherwise) do not facilitate this extended recovery period.

For these patients specifically designed and constructed extended recovery areas together with limited care accommodation (medi-motels) facilities are required. This accommodation is part way between a motel and an acute hospital. It would not require the capital cost of acute hospital accommodation with inbuilt resuscitation and related equipment; however it would need to be constructed to medical specifications and staffed by trained nurses. A further option is standard motel accommodation incorporating on call professional health care.

There is anecdotal evidence that motels/hotels in close vicinity to day surgery centres are being used as informal recovery accommodation for patients that are not suitable for same day discharge. A standard hotel room is not an ideal place for those who may have requirements for resuscitation or receiving special medication.

### **Investment in Day Surgery Centres**

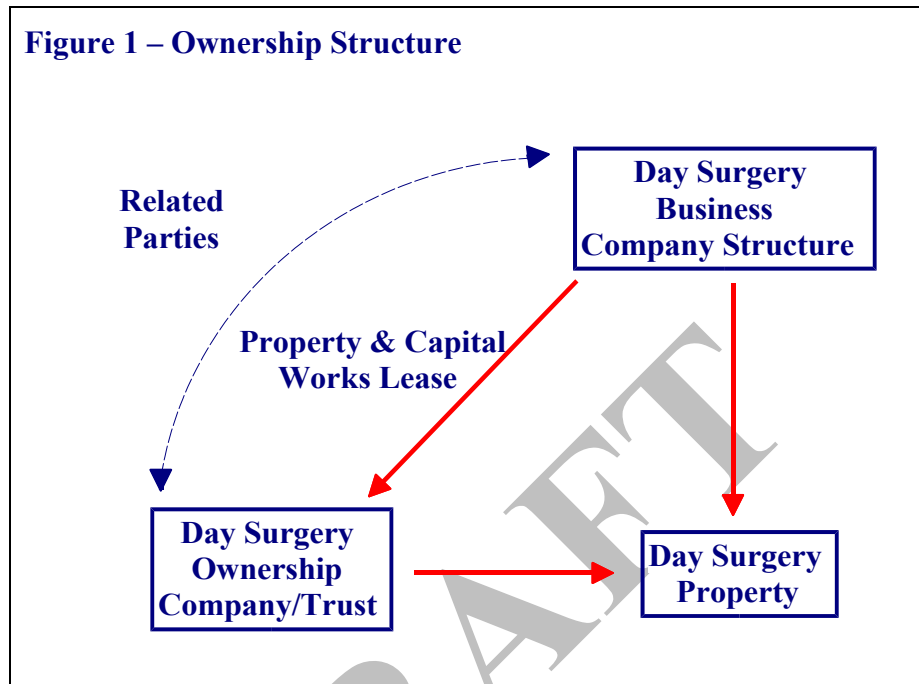
The essence of a day surgery centre is a group of medical specialists (surgeons, anaesthetists, etc.) in related or synergistic disciplines offering their services from the one business location. Alternatively medically orientated corporations may develop day surgery centres.

The specialists are not confined to day surgery centres and all of them have appointments at private/public hospitals.

Medical specialists are recognised as a financially strong group. The development and funding of a day surgery centre can therefore be driven by the equity and borrowing power of the occupying group. The result is that this is an asset class based on a specialised property with a linked business entity and is predominantly “owner occupied”.

Where day surgery centres have been developed as investments owned by an investor(s) and leased to a common tenant often the investor and tenant are a related party. Many of these investors and tenants are groups of specialists in either a company or a trust structure.

In conjunction with this owner occupied specialised asset class, transactions between the parties are at a company or a trust level, which do not necessarily reflect the value of the underlying real estate.



### Valuation Issues

In the development stage of a day surgery centre the main valuation requirement is for funding purposes. At this stage the land, buildings and capital works are a known quantum.

Once constructed, unless ongoing debt is utilised, the main requirement for valuers services is for balance sheet or share transfer purposes. Therefore the valuation basis is *in situ* with the associated business established. Value *in situ* is a function of the number of theatres in the surgery which impacts on the number of procedures that can be performed. This is also impacted by the following.

- The types of procedures that are performed. The most common are general surgery, plastic/aesthetic surgery, ophthalmology, endoscopy, orthopaedics and gynaecology.
- The level of capital works required for this individual day surgery. Understandably, day surgery centres established by groups of specialists with a particular discipline have specialised capital works. A day surgery centre set up for endoscopy cannot just suddenly be used for ear, nose and throat procedures. Furthermore, as new larger day surgery centres are now being constructed with state of the art technology, capital works can have a high level of obsolescence.
- The location of the facility; day surgery centres should be in locations within a reasonable distance (one hours drive) of a major public or private hospital.

Most leased day surgery centres have a close (incestuous) link between the nominal lessor and lessee and rents struck can be inclusive of the land and buildings component plus the specialised plant and equipment. In some instances the equipment supplier or finance company externally funds medical fit-outs. Valuers need to determine what components the lessor owns and what components the specialists use but are subject of other financing arrangements. This ownership ratio affects the nominal rent and the taxation (depreciation) benefits available to either the lessor or lessee.

Financiers may require a valuation of a completed and operating day surgery centre on the basis of vacant possession. There is limited sales evidence where a day surgery centre was vacated by one group of specialists and then reoccupied by a new group thus utilising any specialist capital works. In most instances where a vacant day surgery centre sale occurred, the property was redeveloped for an alternate use (residential, commercial).

### **Future Trends**

Many of the earlier day surgery centres have been in converted premises, either residential or commercial. There is now a greater trend for specifically constructed day surgery centres integrated with other uses. An example of this is the Medica Centre in Hurstville in Sydney's south, currently being developed. This will be an eight level building with approximately 12,000 square metres of medical and office space. The building will contain a six-theatre day surgery centre, six office levels containing nearly 60 medical consulting suites, radiology and pathology laboratories, nuclear medicine facility, ground floor medical related retail and parking for 500 cars.

### **Conclusion**

Day surgery centres are predicted to become the dominant centres for surgical procedures in major population centres.

They are a property asset driven by the occupants with varying arrangements between the lessors and lessees with regard to construction and fitting out costs. Consequently, it is difficult to obtain directly comparable sales and leasing evidence. Valuers need to exercise caution with regard to all documentation and financial/taxation arrangements.

### **Acknowledgements**

The assistance of Dr Lindsay Roberts FRACS is gratefully acknowledged. Dr Roberts was the Chairman of the Australian Day Surgery Council 1990-2000 and President of the International Association for Ambulatory Surgery 2001-2003.