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Demystifying Laboratory Capital Equipment Acquisition

Becky O'Neal, Otis Tracey & Hunter Bernstein

| Disclosures

- The presenters have no real or perceived conflicts of interest related to this presentation

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| Learning Objectives

At the end of this session, participants should be able to:

1. Recognize business terminology and basic FASB leasing rules relative to operating vs. capital leases
2. Describe the pros and cons of lab equipment acquisition options
3. Identify components of a long-term laboratory capital equipment plan

Pros and Cons of Lab Equipment Acquisition

Capital Purchase

Operational

Financial

Pros

- Flexible maintenance/service options (owner choice)
- Flexibility to change vendors
- Modifications/customizations allowed

- Equipment ownership (no payments, title passes)
- Depreciation schedule
- No volume commitment
- No lease/placement contracts to track

Neutral

- Carried on balance sheet (asset)

Cons

- No vendor responsibility or liability for maintenance/service.
- Increased risk of obsolescence

- Capital outlay required
- Equipment ownership (resale, trade-in, or disposal)
- Maintenance/service from vendor is contracted and purchased separately

Lease (\$1 Buyout)

Operational

Financial

Pros

- Equipment ownership (after all payments made and \$1 or other amount)
- Depreciation schedule (once owned)

Neutral

- Responsibility or liability for maintenance/service according to agreement

- Also referred to as a capital lease
- Carried on balance sheet
- Capital requirement based on lease classification

Cons

- No vendor responsibility or liability for maintenance/service.
- No flexibility to change vendors
- Increased risk of obsolescence
- Modifications/customizations not allowed

- Equipment ownership (resale, trade-in, or disposal after end of term buyout)
- Lease tracking required
- Written notice required at end of term

Lease (Fair Market Value Option)

Operational

Financial

Pros

- Shifts risk of obsolescence (walk-away option)

Neutral

- Responsibility or liability for maintenance/service according to agreement

- No equipment ownership (option to purchase at term for FMV)
- Carried on balance sheet
- Capital requirement based on lease classification
- Volume commitment according to agreement

Cons

- No flexibility to change vendors
- Modifications/customizations not allowed

- No depreciation schedule (while it is a lease)
- Lease tracking required
- Written notice required at end of term

Reagent Rental

Operational

Financial

Pros

- Shifts risk of obsolescence

Neutral

- Responsibility or liability for maintenance/service according to agreement
- End of contract options- return equipment, continue making payments into perpetuity, or construct new contract

- No equipment ownership (pay for use)
- Embedded lease that must be classified
- The rental payment is bundled into the reagent per unit price at the schedule level.
- Capital requirement based on lease classification

Cons

- Modifications or customizations not allowed

- No depreciation schedule
- Volume commitment
- Lease tracking required
- Residual amounts or overpayment if volumes vary
- May be more expensive long-term than purchase

Rental Equipment Only

Operational

Financial

Pros

- Shifts risk of obsolescence

- No volume commitments

Neutral

- Responsibility or liability for maintenance/service according to agreement
- End of contract options- return equipment, continue making payments into perpetuity, or construct new contract

- No equipment ownership (pay for use)
- Rent payment does not include reagents
- Capital requirement based on lease classification

Cons

- Modifications/customization not allowed

- No depreciation schedule
- Lease tracking required
- May be more expensive long-term than purchase

Cost Per Test (CPT)

Operational

Financial

Pros

- Shifts risk of obsolescence

- Usually lower cost than CPR due to increased volume (controls, validations, repeats, etc.) but can be misleading

Neutral

- End of contract options- return equipment, continue cost per test into perpetuity, or construct new contract

- No equipment ownership (pay for use)
- Embedded lease that must be classified
- Fixed bundled cost for each test performed on equipment (equipment, reagents, service)
- Capital requirement based on lease classification

Cons

- Modifications or customizations not allowed
- Logistics and tracking of reagents are cumbersome
- Supplies bypass SC ordering/inventory systems

- No depreciation schedule
- Volume commitment
- Lease tracking required
- Residual amounts or overpayment if volumes vary
- May be more expensive long-term than purchase

Cost Per Reportable (CPR)

Operational

Financial

Pros

- Shifts risk of obsolescence

Neutral

- End of contract options- return equipment, continue cost per test into perpetuity, or construct new contract

- No equipment ownership (pay for use)
- Embedded lease
- Fixed bundled cost for each test “reported” on equipment (equipment, reagents, service)
- May be more expensive than CPT

Cons

- Modifications or customizations not allowed
- Logistics and tracking of reagents are cumbersome
- Supplies bypass SC ordering/inventory systems

- No depreciation schedule
- Volume commitment
- Lease tracking required
- Residual amounts or overpayment if volumes vary
- May be more expensive long-term than purchase

Standardization/Market Share Agreements

Operational

Financial

Pros

- Standardized equipment across system or region
- Easy to incorporate instrument upgrades for aging instruments/equipment
- Easy to incorporate technology clauses

- Better pricing for both instrumentation and reagents/consumables
- Standardized contract terms across network

Neutral

- Customized approach to a partnership that commits a negotiated portion of the customer's market share
- Instrumentation can be included in the deal as "no charge" but a value has to be assigned for accounting

Cons

- Ties system to a specific equipment or vendor for the majority of volume or market share
- Vendor/supplier performance issues
- Changing vendors in the future requires system wide conversions

- Agreement/Lease tracking required



Business Terminology & Basic FASB Rules

*Otis Tracey, National Group Controller- HCA Laboratory
Services*

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Business Terminology & Basic FASB Rules

Basic Business Terminology

	Definition
Asset	Item of value owned by a company.
Balance Sheet	Statement of a business's assets, liabilities, and owner's equity as of any given date.
Income Statement	Also known as “profit and loss statement”. Shows income and expenses and resulting profit or loss over a specified period of time.
Operational Expense	An expenditure that a business incurs as a result of performing it’s normal business operations.
Capital Expense	Incurred to create a benefit in the future. They are long-term in nature and are generally used to acquire things like property, equipment, and technology.
Depreciation	A way to calculate the reduction in value of an asset due to use, wear and tear, and obsolescence.

Accounting Standards

FASB

Financial Accounting Standards Board is the independent, private-sector, not-for-profit organization, that establishes financial accounting and reporting standards for public and private companies and not-for-profit organizations that follow Generally Accepted Accounting Principles (GAAP).

FASB ASC 842

In 2019, The Financial Accounting Standards Board (FASB) published the lease accounting standard ASC 842, which replaces the lease accounting standard ASC 840. Determines the accounting for lab equipment leases.

FASB ASC 842 Rule Changes 2019 : Old versus New

Old Rule (ASC 840)	New Rule (ASC 842)	Impact to Accounting Practices?
Capital Lease Classification	Financing Lease Classification	None
Operating Lease Classification	Operating Lease Classification	Balance Sheet recognition for operating lease
Lease Classification is determined when lease is executed (Inception)	Lease Classification is determined at lease commencement (Go Live)	None
4 Criteria used to determine lease classification	4 Criteria used to determine lease classification	None

FASB ASC 842 Rule Changes 2019–

What Hasn't Changed

- FAS 13 Lease Classification Test
 - Ownership transfer
 - Bargain purchase option
 - Lease term greater than or equal to 75% of useful life of the asset
 - Present value of minimum lease payments greater than or equal to 90% of fair value of the lease

What Has Changed

- Balance sheet recognition for operating leases
 - Record a Right to Use asset
 - Lease liability

Lab Equipment Leases and Considerations

Lab Leases	Considerations
What is and isn't a lease?	Operating, Capital, and Finance leasing terms
Embedded leases and placements	"Right-of-use" requirements Separating the lease and non-lease components
Lease expiration tracking	Replacement Planning End of lease terms (notification requirements, current contract terms, buyout options)
Equipment Return Process	Avoid penalties Return to appropriate vendor (3 rd party owner)



Creating a Long Term Laboratory Equipment Plan

*Hunter Bernstein, Director,
Capital Equipment Services, HealthTrust*

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Creating a Long Term Laboratory Equipment Plan

Creating a Long-Term Laboratory Equipment Plan- Planning/Assessment

Determine Current Equipment Life

- Age of fleet
- Useful life
- Operational status

Evaluate Supplier Performance

- Test menus/quality scorecards
- Availability- supply chain, lead time, etc.
- HealthTrust vendor performance information

Choose Acquisition Model

- Organizational preference
- Capital dollar availability

Review Current Contracts

- Rental, lease, CPT/CPR agreements
- Commitments, expirations and terms
- Prioritize equipment categories

Consider Standardization

- Consistency – test results/redundancy
- Reduce SKUs
- Leverage volumes- vendor value adds

Assess Clinical/IT Workflow Impact

- Cost Effectiveness
- Turn-around time/Productivity
- Consolidation
- IT (vendor credits, LIS quotes, resources)

Creating a Long-Term Laboratory Equipment Plan- Planning/Assessment

Conduct RFP/RFI

- All category vendors (if supplier performance req. met)
- Utilize HT Resources (acct dir, sourcing team, etc.)

Compare Quotes

- Determine cost over term of agreement
- Include any value adds
- Compare to current cost- is there a savings?

Determine Rollout Plan

- Timeline to completion
- Considering conflicting activity (EPIC go live, mergers, etc)

Reference HealthTrust Member Portal

- SIP availability- Facility/Group
- eLOC requirements- tier optimization
- Participation agreements

Choose Preferred Vendor

- Lowest cost provider
- Must meet performance/quality requirements
- Include lab, clinicians (if applicable), supply chain, and IT

Complete Contracting

- Communicate roll-out plan to each site
- Add agreement to contracting system
- Schedule notification for contract review min. 18m prior to term

Long-Term Lab
Equipment Plan

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Thank you...

Becky Oneal; becky.oneal@healthtrustpg.com

Otis Tracey; otis.tracey@hcahealthcare.com

Hunter Bernstein; hunter.Bernstein@healthtrustpg.com