PHYSICIANS, HOSPITALS AND MANAGEMENT COMPANIES: A SUCCESSFUL PARTNERSHIP MODEL FOR A SURGERY CENTER

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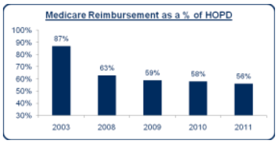
The New Outpatient Strategy: Hospital/Physician JVs

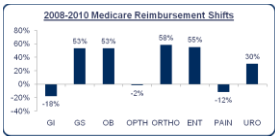
- There are approximately 5,300 ASCs in the U.S.
- 90% of ASCs have some degree of physician ownership
- Approximately 20% of ASCs have a hospital partner
- While some ASC specialties are better reimbursed by Medicare, many ASCs without hospital partnerships are paid less than 60% of what a hospital is compensated for the same outpatient surgeries
- Most U.S. locations are saturated with ASCs and, for the first time in recent history, net growth of ASCs has stalled
- Payers are all but eliminating most out-of-network reimbursements, thus reducing the profit margin of most ASCs

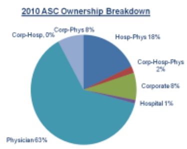
The Economics of a Physician/Hospital/Corporate Management Model

- Medicare pays the ASC the same per case regardless whether the ASC is part of a JV or not: payment is only higher if it is an HOPD
- Average reimbursement for independent ASCs is between $1,200-$1,700 per case, if the ASC is fully contracted
- Average reimbursement for hospital-affiliated ASCs is in the range of $2,200-$3,000 per case

Reimbursement and Ownership Dynamics



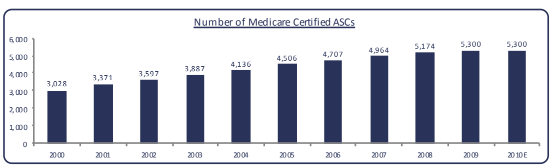


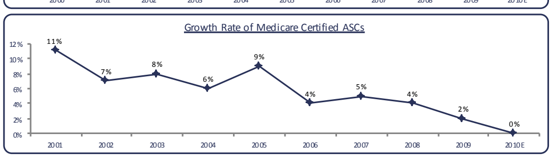


Commentary

- Over 90% of ASCs have physician ownership
- Approximately 20% of ASCs have a hospital partner
- Reimbursement shifts in recent years
- Evaporation of Out-of-Network reimbursement

ASC Growth Rates have Stagnated





Source: VMG/ Medpac

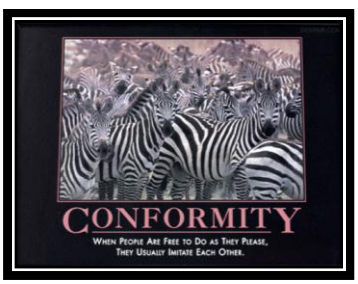
A Hospital Can Be A Good Partner if They Have Higher Contracted Rates and They Do Not Require Control of Clinical/Operations

- There is a historical reason why less than 20% of hospitals are partnered with physicians and it mainly has been because the hospital not only wanted majority ownership, but also control of operations
- Most hospitals historically only wanted to partner with surgeons if they could own most of the ASC, control it, and worse, manage it. This has changed dramatically the past few years
- Regent's ownership and governance model is a hybrid that allows the physicians to keep operational control, while providing the doctors a healthy financial result both in a sale and on future earnings. Most of our transactions provided the doctors who sold half of their interests with similar or higher financial returns annually than before the sale.

Why Partner With a Hospital?

- Significantly higher payments for cases with the hospital model versus the independent ASC model
- A strategic alliance with a hospital in concert with the aims of healthcare reform models
- Hospitals are now buying practices again and acquiring or developing ancillary services of which ASCs are a primary target
- Provides a wonderful hedge against shrinking surgeon reimbursements in their practices and at their ASCs
- Competitive advantage over ASCs that do not partner with hospitals; non-compete clauses

Why Partner?



Which Model Do We Usually Recommend?

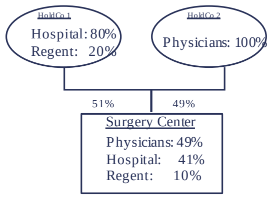
- Hospital Contracting Model
  - If it is structured correctly, the payments per case are at least 30% higher than an independent ASC and, at the same time, it provides protection for the doctors that the hospital cannot compete with them in other transactions and, allows the doctors to maintain daily clinical and operations control over the facility
  - The hospital forms a strategic alliance with select surgeons, while minimizing their financial investment and risk and, at the same time, prevents surgeons from competing with them in other transactions

Typical Ownership And Governance Model

Governance Structure

- Hospital has 2 board seats, Physicians have 4 seats, and Regent has 1 seat
- Physicians are Class A shareholders, while Hospital and Regent represent Class B shareholders
- Hospital controls Class B and majority vote
- Physicians retain voting control on clinical issues
- Maximizes physician financial upside while maintaining hospital's earnings consolidation ability

Typical Hospital Contracting Model



Regent Business/Partnership Model

Governance:

- Hospital votes Regent's ownership to demonstrate "control" on key legal and financial issues
  - Results in ability of the ASC to obtain "hybrid" payer contracted rates which are less than HOPD, but more than independent ASC rates
- Physicians maintain clinical control of operations even as minority owners, making it attractive to participate in these partnerships

Control Breakout

Physicians

- Medical Executive Committee recommendations
- Selection of anesthesia providers
- Daily operations decisions that require Board approval
- Approval of physician members that go to partnership vote
- Clinically-related operating policies and procedures
- Approval of equipment purchases as part of budget or are limited to a certain monetary value

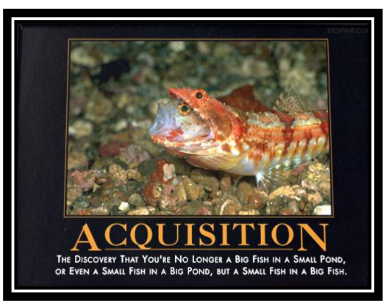
Hospital

- Budget
- Strategic decisions
- Disposition of assets
- Super majority rights related to types of procedures conducted

When Is It Best To Use Our Recommended Model?

- When the doctors trust the local hospital
- In an over-saturated competitive ASC market
- In a community where payors squeeze the independent ASCs on price and out of network facilities have to change to a contracted model
- In a market where the hospital of choice is accustomed to joint ventures with doctors
- Where hospitals are interested to partner with doctors
- In a market where the hospital has a strong track record of negotiating favorable contract rates and also has contracting power
- In an existing ASC, when the ASC has matured and/or does not see a significant increase in profits in the future
- If the local surgeons can utilize this model to form a strategic alliance with the local hospital of choice

The "Dreaded" Word ACQUISITION



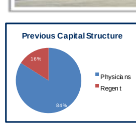
Case Study: Knightsbridge Surgery Center Columbus, Ohio

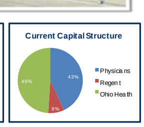
Background
- Founded in 2001, Knightsbridge Surgery Center (KSC) did not produce returns under initial management company
- Engaged RSH in 2004, which turned around facility to highly profitable through negotiating payors and canceling inadequate contracts

Problem
- Payor strategy loses momentum, diminishing returns
- OhioHealth seeks partnership yet physicians seek retention of clinical control

Solution
- Hospital acquires 49% stake but has 50% vote and tiebreaker rights on key management decisions
- Hospital investment predicated on attainment of performance benchmarks

Result
- Meaningful liquidity event for physicians' 49% interest
- Approximately 133% annual returns for OhioHealth
- Net Revenue Per Case 2x-3x that of ASC regional avg.





Summary Of Regent

- Founded in 2001; Headquartered in Chicago
- 24 facilities; 30 owned and managed historically
- Always a minority owner and manager
- 17 of 24 Partnerships are with hospitals
- Our investment in partnerships represents our own money, no outside investors , no bank financing; we carefully scrutinize all our acquisitions based on their ability to obtain a strong ROI for Regent ,our hospital and doctor partners
- Partnerships are not designed to be sold; Regent does not have investment bankers or venture capitalists requiring a sale a few years later; all facilities have to be profitable on an operational basis
- All of our facilities are clinically and financially successful;
- We are noted in the industry as having superb management skills with a strong focus on physician relations and successful clinical outcomes

Surgery Center Partnerships Nationally and Internationally

The Regent Approach

- Always a minority owner and manager
- Invests capital side-by-side with hospital and physician partners
- Partnerships are not designed to be sold; focus is long-term success
- All facilities demonstrate profitability on an operational basis
- All facilities are clinically and financially successful
- Recognized in the industry as providing superb management services with a strong focus on physician relations and successful clinical outcomes

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