How a Hospital/Physician ASC JV Affects Physician Alignment

Paul Eiseman, VP Business Development
Jeffrey Simmons, CDO
Regent Surgical Health
June 12, 2015

The ASC Market In The U.S.

- There are approximately 5,400 ASCs in the U.S.
- 90% of all ASCs have some degree of physician ownership
- About 30% of ASCs have a hospital partner
- Independent ASCs are typically paid less than 60% of what a hospital is paid for the same outpatient surgeries
- Most locations in the U.S. are saturated with ASCs and, for the first time in recent history, net growth of ASCs has stalled
- Payors have all but eliminated out-of-network reimbursements in most markets, thus reducing the profit margins of most ASCs

The Trends of ASC Ownership

- Follow the Money
  - Medicare payments for ASCs that are independent versus HOPD
- What alignments of ownership exist today?
- Are ASCs increasing or decreasing nationwide?
- Hospital/physician alliances: what we are seeing
- What to look for in a hospital partner
- A hospital contracting model to consider
As Fewer ASCs are Being Built, There is a Trend Toward Closer Alignments with Physicians & Surgeons

- As a result, more acquisitions are being completed, primarily by hospitals and ASC companies; oftentimes with a three-way partnership
- 80% of Regent’s new ASCs are partnered with hospitals and surgeons
- Most ASC transactions today are acquisitions due to the consolidation of the markets, the increase in IV activities by local hospitals; few ASC are being built
- More hospitals are seeking surgeons partnerships because many ASCs are available locally; hospitals do not have to acquire surgical practices to accomplish non competes and alignment patterns
- Some states are not allowing new ASC JVs without a hospital partner
- Hospitals are taking on more risk by developing ACO strategies and need a lower cost ASC to download cases from the hospital

The “Dreaded” Word ACQUISITION

Continued Price Transparency Requirements Will Benefit ASCs over Hospital Surgery Depts.
The Economics of a Physician/Hospital/Corporate Management Model

- Medicare pays the ASC the same per case regardless of 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.

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

- Less than 20% of hospitals are partnered with physicians, primarily because, in the past, 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

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.

Sample 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 have a good relationship/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 in partnering 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 HOPD Model
another model that works well in some situations...for now

**Structure**
- Hospital owns 49% of ASC, enabling HOPD rates
- Surgeons and management company engaged to provide operational and clinical oversight

**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 with 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 25% annual return for OhioHealth
- Net Revenue Per Case 2x-3x that of ASC regional avg.
Summary Of Regent

- Founded in 2001; Headquartered in Chicago
- 21 facilities; 23 owned and managed historically
- Always a minority owner and manager
- 15 facilities are with hospitals; 2 new hospital/surgeon partnerships will be implemented in the next three months
- 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

1. Center for Specialized Surgery
   Ft Myers, FL
2. Surgery Center of Mount Dora
   Mount Dora, FL
   Partnered With Leesburg Hospital
3. Robert Wood Johnson Endoscopy Center
   East Brunswick, NJ
   Partnered With Robert Wood Johnson University Hospital
4. Ambulatory Surgical Pavilion at Robert Wood Johnson
   New Brunswick, NJ
   Partnered With Robert Wood Johnson University Hospital
5. Marietta Surgery Center
   Marietta, OH
   Partnered With Marietta Memorial Hospital
6. Knightsbridge Surgery Center
   Columbus, OH
   Partnered With OhioHealth
7. Medical Center at Elizabeth Place
   Dayton, OH
   Partnered With Kettering Health System
8. Palos SurgiCenter
   Palos Heights, IL
   Partnered With Palos Community Hospital
9. Midland Surgical Center
   Sycamore, IL
   Partnered With Kishwaukee Community Hospital
10. IL Sports Medicine and Orthopedic Surgery Center
    Morton Grove, IL
11. Medical Center at Ravine Way
    Glenview, IL
    Partnered With Northshore University Health System
12. Loveland Surgery Center
    Loveland, CO
13. High Plains Surgery Center
    Cheyenne, WY
    Partnered With Cheyenne Regional Medical Center
14. Providence Health System
    Portland, OR
    Partnered With Providence Health System
15. Surgery Center of Reno
    Reno, NV
16. Endoscopy Center of Lodi
    Lodi, CA
    Partnered With Lodi Memorial Hospital
17. Lodi Outpatient Surgical Center
    Lodi, CA
    Partnered With Lodi Memorial Hospital
18. Surgery Center of Wasilla
    Wasilla, AK
19. Neurosurgery Ireland at Hermitage Medical Clinic
    Dublin, Ireland
    Partnered With Hermitage Medical Clinic
20. Cyber Knife Ireland
    Dublin, Ireland
    Partnered With Hermitage Medical Clinic
21. Stem Cell Clinic
    Roatan, Honduras
   *Under Development
   Partnered With Hospital Cemesa
22. Providence Health System/Portland
    Portland, OR
    Partnered With Providence Health System
23. Providence Health System/Palm Springs
    Palm Springs, CA
    Partnered With Providence Health System
24. Providence Health System/Spokane
    Spokane, WA
    Partnered With Providence Health System
25. St. Joseph Medical Center
    Stockton, CA
    Partnered With St. Joseph Medical Center
26. St. Joseph Medical Center
    Stockton, CA
    Partnered With St. Joseph Medical Center
27. St. John’s Medical Center
    Carlsbad, CA
    Partnered With St. John’s Medical Center
28. St. John’s Medical Center
    Carlsbad, CA
    Partnered With St. John’s Medical Center
29. St. John’s Medical Center
    Carlsbad, CA
    Partnered With St. John’s Medical Center
30. St. John’s Medical Center
    Carlsbad, CA
    Partnered With St. John’s Medical Center
31. St. John’s Medical Center
    Carlsbad, CA
    Partnered With St. John’s Medical Center
32. St. John’s Medical Center
    Carlsbad, CA
    Partnered With St. John’s Medical Center
33. St. John’s Medical Center
    Carlsbad, CA
    Partnered With St. John’s Medical Center
34. St. John’s Medical Center
    Carlsbad, CA
    Partnered With St. John’s Medical Center
35. St. John’s Medical Center
    Carlsbad, CA
    Partnered With St. John’s Medical Center
36. St. John’s Medical Center
    Carlsbad, CA
    Partnered With St. John’s Medical Center
37. St. John’s Medical Center
    Carlsbad, CA
    Partnered With St. John’s Medical Center
38. St. John’s Medical Center
    Carlsbad, CA
    Partnered With St. John’s Medical Center
39. St. John’s Medical Center
    Carlsbad, CA
    Partnered With St. John’s Medical Center
40. St. John’s Medical Center
    Carlsbad, CA
    Partnered With St. John’s Medical Center
41. St. John’s Medical Center
    Carlsbad, CA
    Partnered With St. John’s Medical Center
42. St. John’s Medical Center
    Carlsbad, CA
    Partnered With St. John’s Medical Center
43. St. John’s Medical Center
    Carlsbad, CA
    Partnered With St. John’s Medical Center
44. St. John’s Medical Center
    Carlsbad, CA
    Partnered With St. John’s Medical Center
45. St. John’s Medical Center
    Carlsbad, CA
    Partnered With St. John’s Medical Center
46. St. John’s Medical Center
    Carlsbad, CA
    Partnered With St. John’s Medical Center
47. St. John’s Medical Center
    Carlsbad, CA
    Partnered With St. John’s Medical Center
48. St. John’s Medical Center
    Carlsbad, CA
    Partnered With St. John’s Medical Center
49. St. John’s Medical Center
    Carlsbad, CA
    Partnered With St. John’s Medical Center
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

“I am a man of fixed and unbending principles, the first of which is to be flexible at all times.”
Everett Dirksen

Contacts

- Paul Eiseman, VP Business Development
  Phone: 502-541-1770
  Email: peisman@regentsurgicalhealth.com

- Jeffrey Simmons, Chief Development Officer
  Phone: 707.396.0138
  Email: jsimmons@regentsurgicalhealth.com