ASC Turnaround Strategies: Two Options
Partnering with Hospitals and Increasing Payer Contracts

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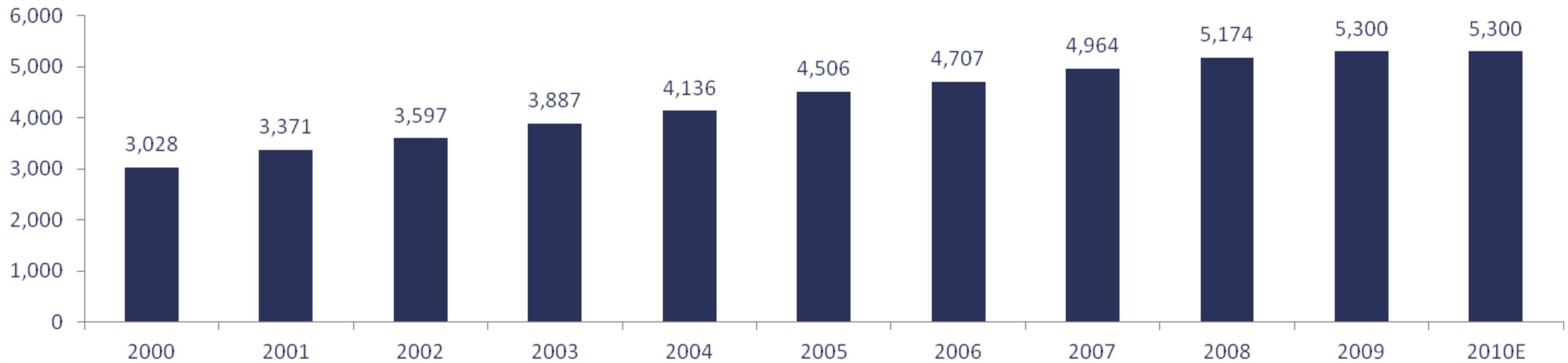
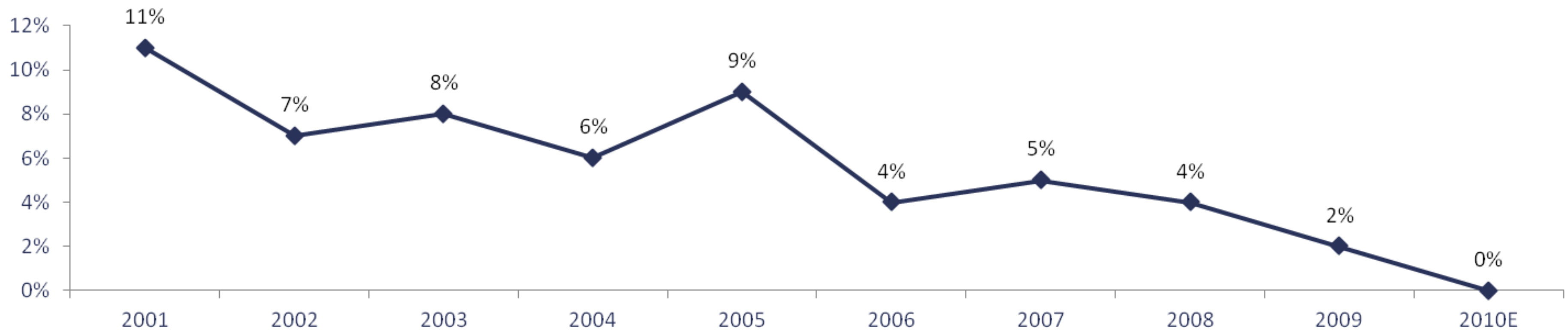
The ASC Market In The U.S.

- There are approximately 5200 ASCs in the U.S.
- 90% of all ASCs have some degree of physician ownership
- About 20% of ASCs have a hospital partner
- While some ASC specialties are being paid better by Medicare, many others are not and, most importantly, ASCs without hospital partnerships are 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 are all but eliminating most out-of-network reimbursements, thus reducing the profit margin of most ASCs

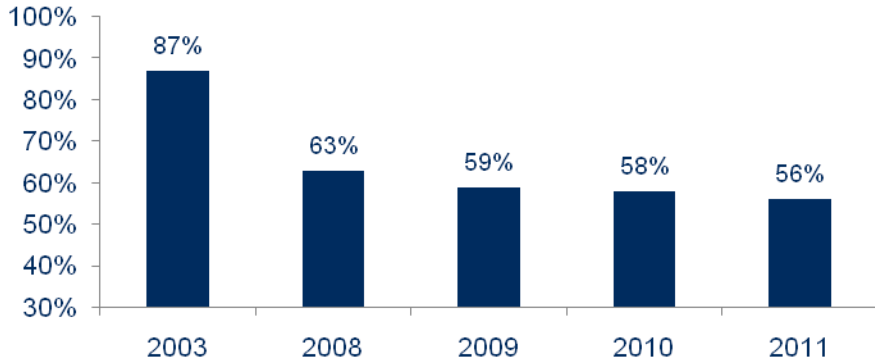
ASC Growth Rates have Stagnated

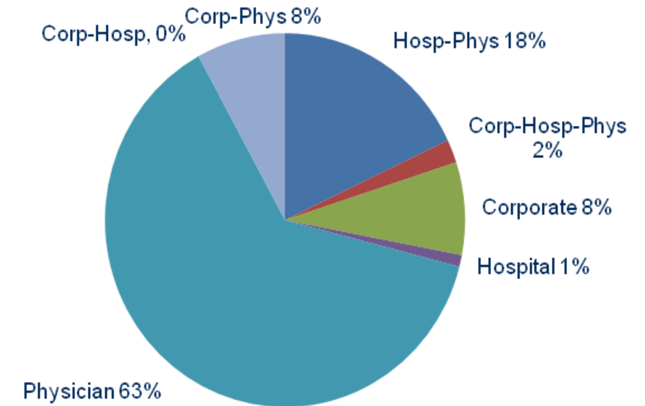


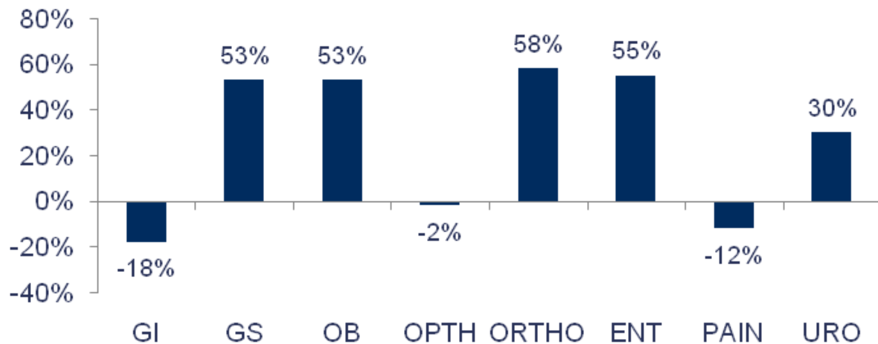


Source: VMG/ Medpac

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

The Economics of a Surgeon/Hospital/Corporate Management Model

- Medicare will pay the ASC the same per case regardless whether the ASC is independent or not
- The average reimbursement for independent ASCs is between $1200-$1700 per case
- The average reimbursement for hospital-affiliated ASCs is in the range of $2200-$3000 per case

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

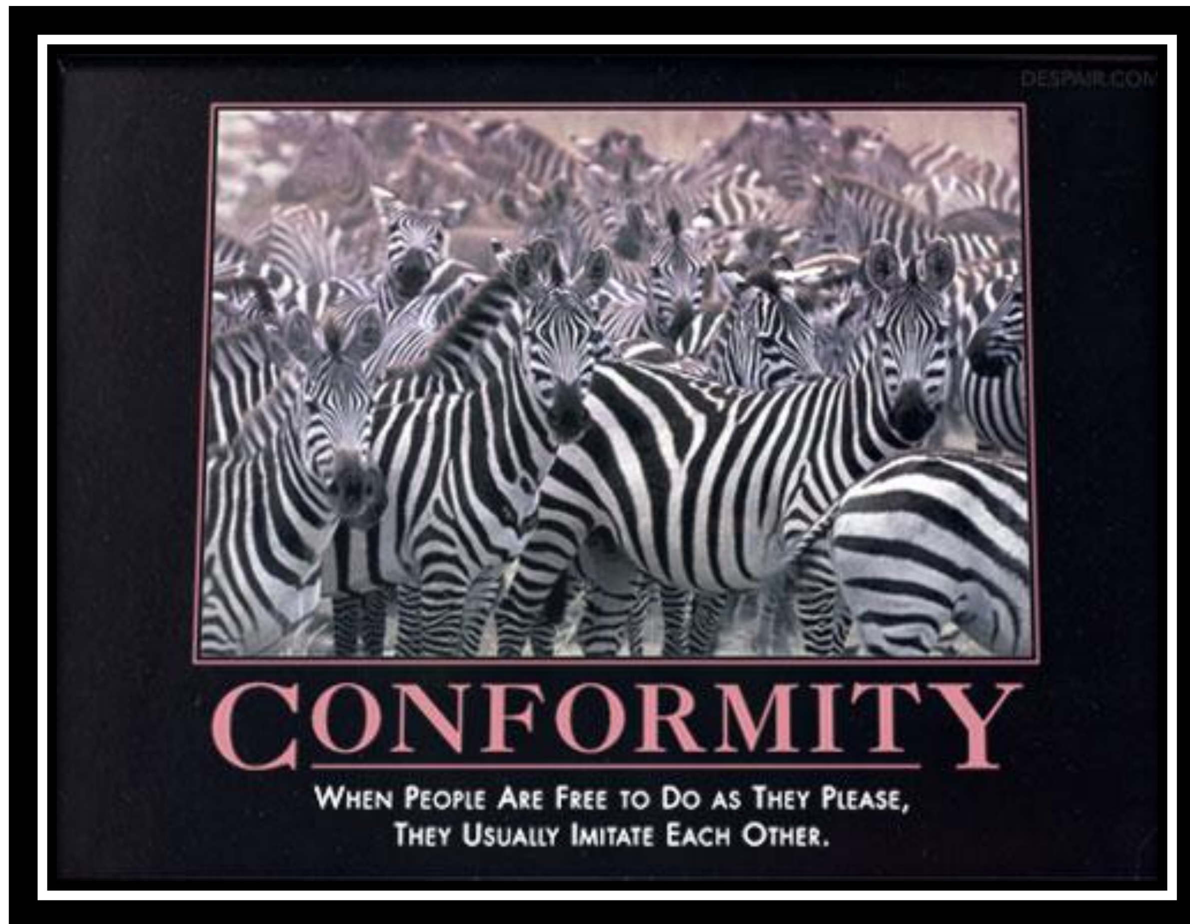
- Most hospitals historically only wanted to partner with surgeons if they could own most of the ASC, control it, and worse, manage it. This has changed dramatically the past few years

- 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?

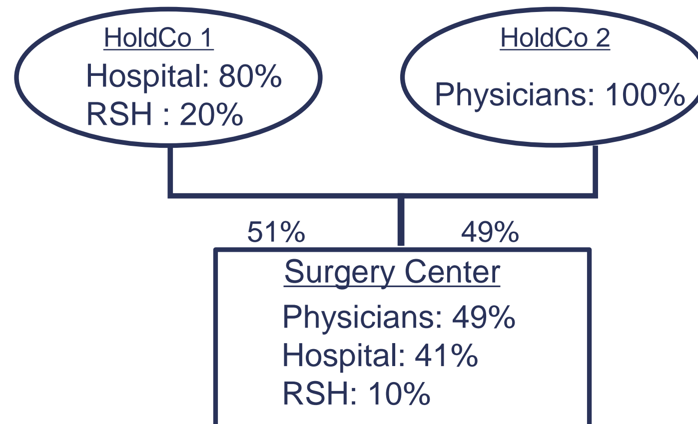


Which Model Do We Usually Recommend?

- 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

Different Ownership Models Exist Depending On Goals

Hospital Contracting Model



Structure

- Hospital has 2 board seats, Physicians have 4 seats and Regent has 1 seat
- Physicians are Class A shareholders and Hospital and RSH 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

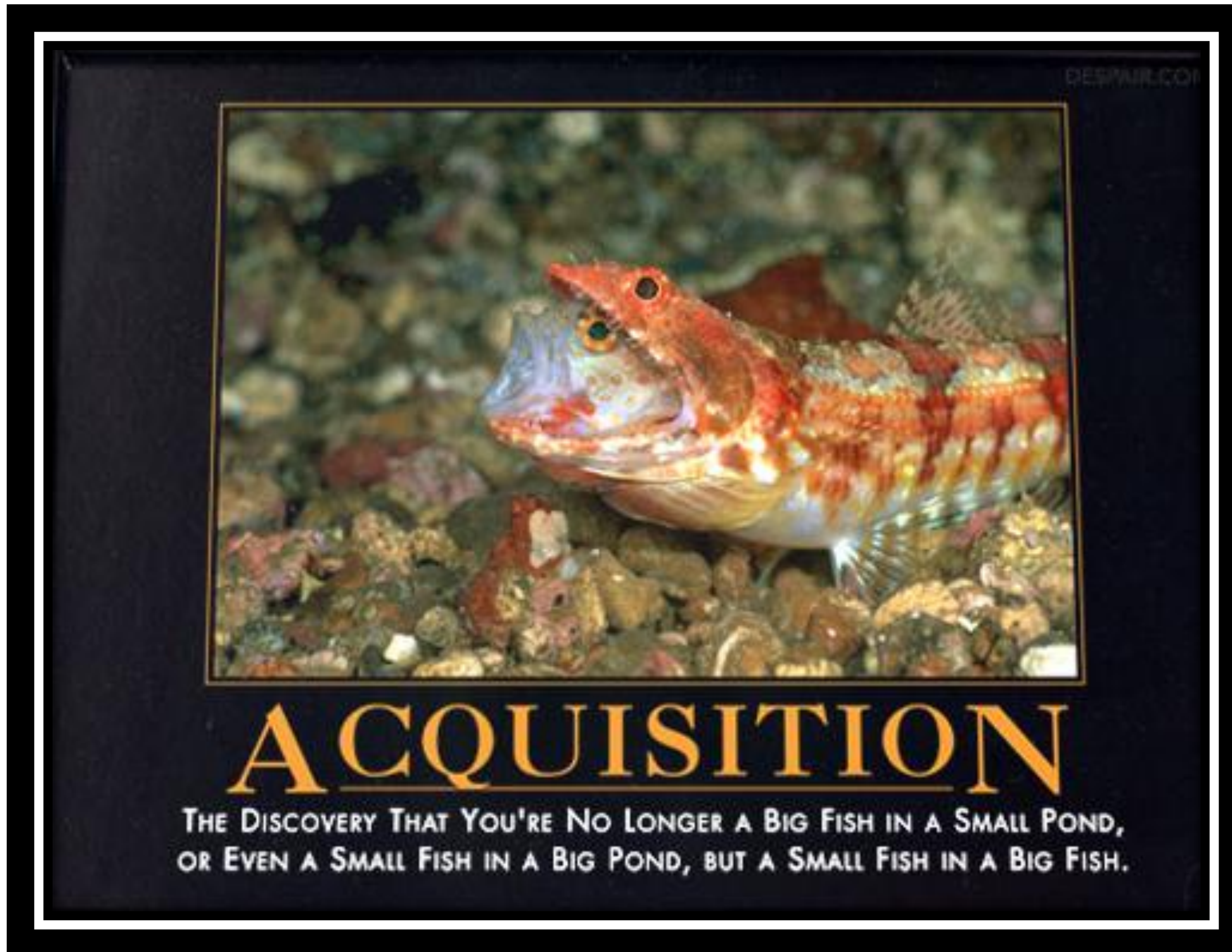
Example of Retained Physician Control After a Transaction is Completed

- Physicians Control (At Board Level)
  - 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 that are part of budget or are limited to a certain monetary value

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 payers and canceling inadequate contracts

Problem

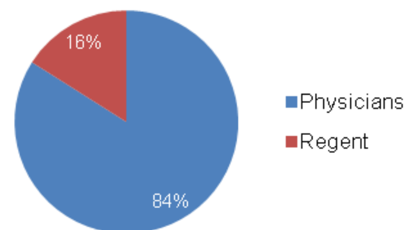
- Payer strategy loses momentum, diminishing returns
- OhioHealth seeks partnership yet physicians seek retention of clinical control

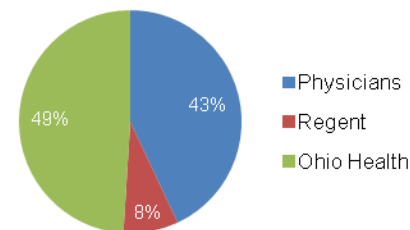
Solution

- 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.





Improving Payer Contracts If A Hospital Partnership Is Not Possible

- Key Tips to Consider
- A Few Comments About Medicare Cases
  - Dos and Don'ts

Medicare Cases

- Cataracts are profitable if high volume and doctor can perform two or more cases per hour. Think reimbursement per surgical hour
- Pain and GI are paid less than before, but remain profitable if Pain doctors use less expensive trays; avoid Permanent Pain Stims
- GI cases are profitable also dependent on volume and doctors avoid poly loops and more expensive disposables; be careful with new Medicare regulations that require OR nurses to replace techs as assistants
- Podiatry now Medicare profitable as long as you avoid cases with implants which are not covered and the doctor is reasonably fast. Think reimbursement per surgical hour
- General Surgery now profitable as long as expensive meshes on hernias are not used
- Orthopedics excellent but a big cause of alarm is to be aware of fracture repairs as costs for implants and screws are not covered by Medicare; most shoulders will lose money

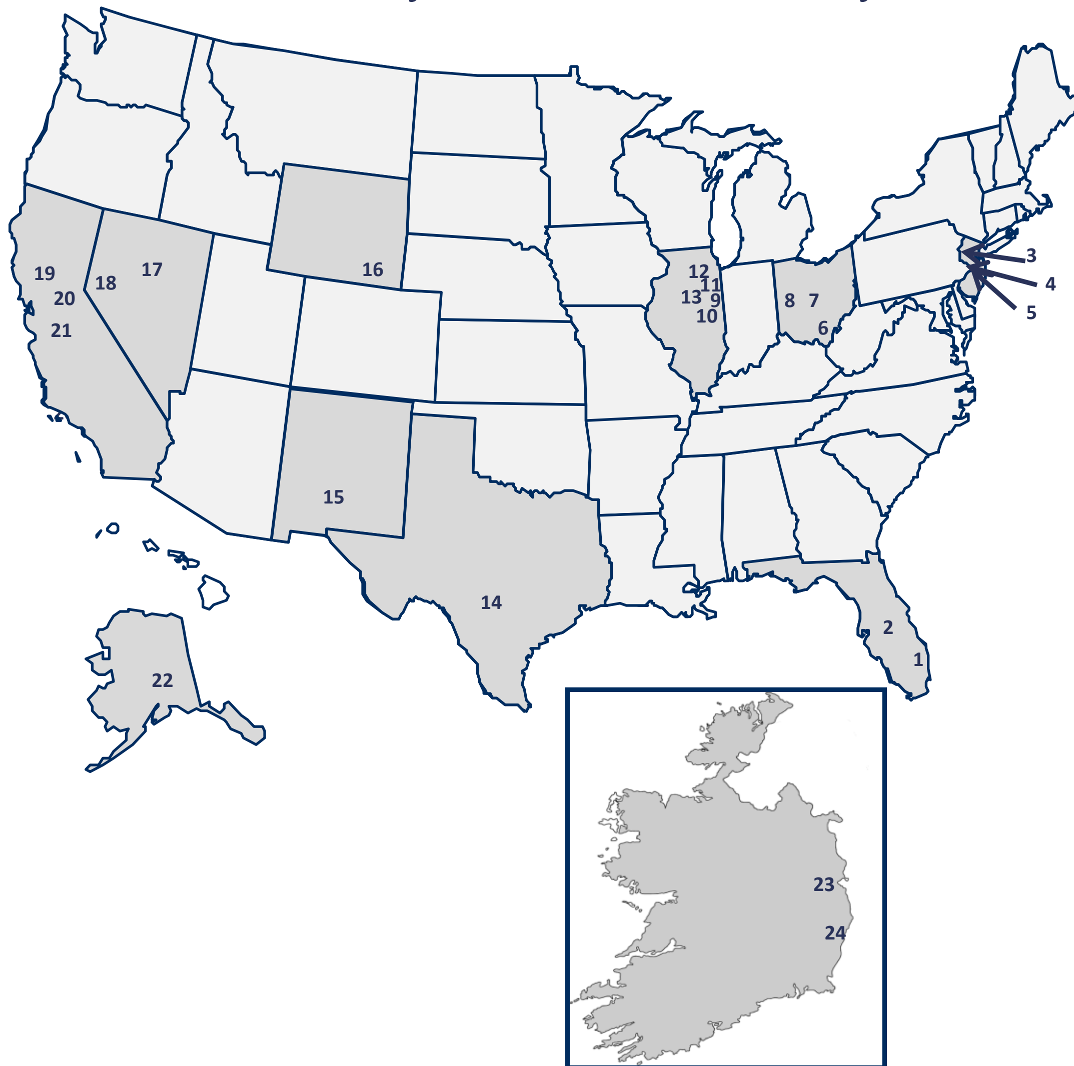
Tips on Contracting

- Build relationship with Payer
  - if they do not like you, they will be less inclined to help you
- Supply and demand of ASC market will drive reimbursement
  - Competition, hospital partnership, unique services and physician group important
- Renegotiate annually
  - Avoid multi year contracts
- All offers should be financially modeled
  - Actual reimbursement depends on volume of specialty cases
- Determine when to accept or not an offer
  - Time and revenue lost versus gains
- Understand the sales cycle
  - What are the credentialing, boiler plate and other legal issues that will add time to the start of implementing new rates
- Be concerned about the limitations of multiple procedure inclusions
- Include language limiting payers to unilaterally make material changes to a contract – e.g. hospital partnership
- Watch out for "lessee of language" clauses

Summary Of Regent

- Founded in 2001; Headquartered in Chicago
- 24 facilities; 30 owned and managed historically
- Always a minority owner and manager
- 16 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

Regent's Partnerships Nationally and Internationally



1. Paramount ASC
   Ft Myers, FL
   Under Development

2. Surgery Center of Mount Dora
   Mount Dora, FL
   Partner: Leesburg Hospital

3. Ambulatory Surgical Pavilion at Robert Wood Johnson
   New Brunswick, NJ
   Partner: Robert Wood Johnson University Hospital

4. Endosurgical Center of Central NJ
   East Brunswick, NJ
   Partner: Robert Wood Johnson University Hospital

5. Peninsula Ambulatory Surgical Center
   Bayonne, N J
   Partner: Bayonne Medical Center

6. Marietta Surgery Center
   Marietta, OH
   Partner: Marietta Memorial Hospital

7. Knightsbridge Surgery Center
   Columbus, OH
   Partner: Ohio Health

8. Medical Center at Elizabeth Place
   Dayton, OH
   Partner: Kettering Health System

9. Palos SurgiCenter
   Palos Heights, IL
   Partner: Palos Community Hospital

10. Midland Surgical Center
    Sycamore, IL
    Partner: Kishwaukee Community Hospital

11. IL Sports Medicine and Orthopedic Surgery Center
    Morton Grove, IL

12. Ravine Way Surgery Center
    Glenview, IL

13. Swedish Covenant ASC - Under Development
    Chicago, IL
    Partner: Swedish Covenant Hospital

14. The Center for Special Surgery at TCA
    San Antonio, TX

15. Southern New Mexico Surgery Center
    Alamogordo, NM

16. Cheyenne Surgical Center
    Cheyenne, WY

17. Summit Surgery Center at Saint Mary's Galena
    Galena, NV
    Partner: St. Mary's Regional Medical Center

18. Surgery Center of Reno
    Reno, NV
    Partner: St. Mary's Regional Medical Center

19. Advanced Surgery Institute
    Santa Rosa, CA

20. Lodi Outpatient Surgery Center
    Lodi, CA
    Partner: Lodi Memorial Hospital

21. Lodi Endoscopy Center
    Lodi, CA
    Partner: Lodi Memorial Hospital

22. Surgery Center of Anchorage
    Anchorage, AK

23. Neurosurgery Ireland @ Hermitage Medical Center
    Dublin, Ireland
    Under Development

24. Cyber Knife Ireland
    Dublin, Ireland
    Under Development

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