Why Less Is More: Embracing the Niche Network Model for Joint-Venture ASCs

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Today’s Presenters

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About Blue Chip Surgical

• Develops, manages and optimizes ASC businesses
• Nationwide network of 15+ ASCs
  ✓ Clinically distinguished, highly profitable
  ✓ 4 hospital/health system partners
  ✓ Experts in spine-focused ASCs
• Annual ROI of each project is typically 50-200%
• Focus on financial, payor, legal and operational matters
• Enables our surgeon partners to focus on patient care
• Build trust-based JVs built on aligned incentives, shared risk-reward and creative business models
About Sentara Healthcare

• 124-year not-for-profit mission
• 10 hospitals; 2,349 beds; 3,700 physicians on staff
• 10 long term care/assisted living centers
• Extended stay hospital
• 3 Medical Groups (600+ Providers)
• 432,600-member health plan
• Sentara College of Health Sciences
• $4.0B total operating revenues
• $5.0B total assets
• 24,000 members of the team
• Mission: We improve health every day

Sentara-Blue Chip Partnership

• Sentara Lake Ridge; Lake Ridge, VA
• CON required
• JV Structure
  ✓ Physician-led; 9 partners
  ✓ Orthopedic & spine surgeons; pain specialists
  ✓ All partners are board members – attend monthly, one-hour meetings
  ✓ Each partner adds unique value
  ✓ Sentara & Blue Chip hold minority stakes
  ✓ Real estate owned in part by Ortho MD partners
• Small, focused ASC: 1 OR + 1 PR with expansion options
• Capture market share: spine/ortho + other specialties in time

Sentara Objectives

• Stable medical community & engage with top talent
• Proactive succession planning
• Facility coverage
• Total clinical, strategic and economic integration
• Ensure long-term viability of critical programs
• Manage CON process briskly
  ✓ Decommission hospital OR & Transition to ASC
• Position for evolving reimbursement model
  ✓ Hospital ORs & beds may become a cost center, not a revenue generator
• Improve level of care via specialty service centers
  ✓ Musculoskeletal COE, MD office, imaging, ASC under one roof
ASC Investments: What Surgeons Want

- Control
  - Professional satisfaction
  - Personal – work/life balance
- Patient Focus
  - Excellent outcomes
  - Comfortable patient experience
  - A place to do their best work
- Productivity/Efficiency
- Financial Benefits
  - Economic stability
  - Ancillary income
  - Wealth-building

ASC Investments: What Hospitals Want

- Stronger Surgeon Relationships
  - Better communication
  - Sense of alignment
  - Loyalty – capture greater share from “splitters”
  - Capture surgeons aligned with hospital rivals
- Clinical Excellence
- Return on Investment
- Market Share
  - Brand awareness
  - Competitive advantage
- Control – typically 51% ownership
- Pricing Flexibility – ASCs allow for lower price points than hospital

Getting to Alignment with Surgeons

- Identify the best business model to achieve alignment
- Began with review of what both want to accomplish
  - Review of history
  - Competitive market dynamics
  - Why affiliation is being considered – MD & hospital perspectives
  - Affiliation options
- Present facts to address important questions
  - What is the motivation?
  - Why now?
  - What are the concerns of physician membership?
  - What can the health system offer versus not offering?
  - Benefits to both organizations compared to staying status quo?
The Problem with Traditional Multi-Specialty Model

- Too many specialties
  - Drives up capital costs
  - Risk of overbuilding
- Too many owners and/or wrong owners
- Generalist staffing – not truly “expert”
- Diluted financial results
  - Limited returns – can only make “restaurant money”
  - On small investments, 50% ROI may only = $6,500 annually
  - Same $ profit distributions to each surgeon for different specialties (e.g., neurosurgery vs. dentistry)

The Problem with Traditional Multi-Specialty Model (cont’d)

- Minimal cross-referral opportunities
- Non-committed owners
  - Misaligned incentives
  - Lack of shared vision
- Governance issues & complexity
  - Limited board participation by surgeon-owners
  - Lack of physician engagement due to minimal “skin in the game”

New Approach: “Niche Network”

- Network of single-specialty, “boutique” ASCs
  - Spine/Ortho
  - Women’s Surgery Center
  - Bariatric & Hernia
  - Pediatric
  - ENT
- Focus on clinical excellence & great patient experience
“Niche Network” Model

Musculoskeletal Surgery Center
Ortho | Spine | Pain | Podiatry

ENT Surgery Center

Women’s Health Surgery Center
GYN’s | GynoUrology | Plastics

Pediatric Surgery Center
ENT | GI | Ortho

General/GI Surgery Center
Bariatric | Hernias/Lap Choles
GI | Colorectal

“Niche Network” Business Model

• Creatively-structured joint venture models:
  ✓ Physician-led: surgeons are majority owners
  ✓ Hospital and managing partner equal minority stakes
  ✓ Nimble, responsive management structure
  ✓ Shared risk & reward
  ✓ Facilities configured to market niche
  ✓ All surgeon-owners assume leadership responsibility

“Niche Network” Business Model

• Hospital Equity Stakes – Why 51%?
  ✓ Not-for-profits expect 51% equity to preserve Not-for-Profit status
  ✓ For-profit hospitals & publicly-traded ASC management companies
    want to consolidate financials

• Surgeon Equity Stakes – Why 51%?
  ✓ Commitment & engagement – MDs “own” the center
  ✓ Well-informed, engaged surgeons make excellent business decisions

If hospitals must own 51%, future equity purchase options should be agreed at the outset.
Niche ASCs: Surgery Center for Women
Hospital creates opportunity for surgeons to own a portion of the real estate

Why “Boutique” ASCs

• Quality experience for both surgeon & patient
• The location factor:
  ✓ Surgeons will travel crosstown 2-3x/month for quality, productivity, compressed schedules, control, etc.
  ✓ Patients will travel crosstown for specialized experience, surgeon focus, easy parking, etc.
• Improved outcomes through “best practices”
• True expert staffing
• Full surgeon commitment – no “dead wood”
• Attractive financial benefits
• The “Board Meeting” advantage

Why “Boutique” ASCs (cont’d)

• Address hospital strategic agenda:
  ✓ Recruit "splitters" and surgeons from competitors
  ✓ Grow inpatient volumes through MD alignment
  ✓ Target hospital line development by specialty
• Improved “word of mouth” referrals
• New marketing opportunities:
  ✓ Direct-to-consumer
  ✓ Co-marketing with local teams, local celebs
  ✓ Smaller, nimble, agile – responsive to needs of marketplace
Boutique ASCs & ACOs

- Positioning for ACO and bundled payments:
  - Governance - engaged, informed surgeons
  - Ownership of the bundle
- Prepare for shift from revenue-based to cost-based models
  - New hospital metric: not how many beds filled, but how few

Niche vs. Multi-Specialty

<table>
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<th>Niche Centers</th>
<th>Invest</th>
<th>Annual ROI</th>
<th>Annual ROI %</th>
<th># Phys</th>
<th>Invest</th>
<th>Annual ROI</th>
<th>Annual ROI %</th>
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<tbody>
<tr>
<td>Spine/Ortho</td>
<td>$147,000</td>
<td>$211,000</td>
<td>54%</td>
<td>10</td>
<td>$31,000</td>
<td>$49,000</td>
<td>144%</td>
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<tr>
<td>Women's</td>
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<td>37%</td>
<td>15</td>
<td>$20,400</td>
<td>$7,500</td>
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<td>ENT</td>
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<td>General Surgery / Variants:</td>
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<td>TOTAL</td>
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<td>$528,000</td>
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<td>Multispecialty</td>
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<td>$273,000</td>
<td>54%</td>
<td>40</td>
<td>$12,250</td>
<td>$6,400</td>
<td>54%</td>
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For hospitals, niche investments offer bigger payoff – both financially and with stronger MD bonds.

Spine & Musculoskeletal ASCs

- Greenspring Surgery Center - Baltimore, MD
- Crane Creek Surgery Center - Melbourne, FL
- GNS Surgery Center - Athens, GA
- Mayfield Clinic - Cincinnati, OH
Questions and Discussion

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