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

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President, Sentara Northern Virginia Medical Center

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CEO, Blue Chip Surgical Center Partners
Today’s Presenters

Megan Perry, President
Sentara Northern Virginia Medical Center

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Blue Chip Surgical Center Partners
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

BLUE CHIP PARTNERS
Surgery Centers
“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
The Board Meeting Advantage

- Brief, regularly scheduled meetings – 9x year, 1 hr max
- Focused agenda for productivity & efficiency
- Distribution of profit check at meetings encourages attendance

Open communication and transparent information sharing build trust

- All owners are Board Members. Everyone participates & is kept informed of performance objectives
- Great chance for hospital execs to casually interact with MDs & build relationships

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Surgery Centers
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
If *niche hospitals* represent the future, why not *niche ASCs*?

**Niche Hospitals**
- Receiving Hospital
- Frail Elderly Hospital
- Community Hospital
- Scheduled Hospital
- Pediatric

**Niche ASCs**
- Ortho/Spine
- ENT & Eye
- Surgery Center for Women
- General Surgery/Bariatric
- Pediatric
# Niche vs. Multi-Specialty

For hospitals, niche investments offer bigger payoff – both financially and with stronger MD bonds.

<table>
<thead>
<tr>
<th>Niche Centers</th>
<th>Hospital</th>
<th>Average Physician</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Invest</td>
<td>Annual ROI $</td>
</tr>
<tr>
<td>- Spine/Ortho</td>
<td>$147,000</td>
<td>$211,000</td>
</tr>
<tr>
<td>- Women's</td>
<td>$147,000</td>
<td>$54,000</td>
</tr>
<tr>
<td>- ENT</td>
<td>$147,000</td>
<td>$125,000</td>
</tr>
<tr>
<td>- General Surgery / Bariatric</td>
<td>$147,000</td>
<td>$138,000</td>
</tr>
<tr>
<td><strong>TOTAL</strong></td>
<td>$588,000</td>
<td>$528,000</td>
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<table>
<thead>
<tr>
<th>Multispecialty</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>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>$510,000</td>
<td>$273,000</td>
<td>54%</td>
<td>40</td>
<td>$12,250</td>
<td>$6,600</td>
<td>54%</td>
</tr>
</tbody>
</table>
Parkway Surgery Center: Impact to Hospital

- Hospital viewed ASC as threat
- Per Hospital’s CFO: *five years later “no threat, data indicates the spine ASC was helpful to hospital”*
- Hospital inpatient neuro revenue increased as a result of the spine-focused ASC
  - Expanded Hospital OR capacity as a result of ASC – capacity for more complex cases
  - Surgeons attracted patients from larger regional area
  - Much less leakage from community
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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Appendix

Financials:
Multi-specialty: Capital and Expenses
Multi-Specialty ROI
Spine / Ortho ASC: Capital and Expenses
Spine Ortho ROI
Multi-Specialty: Capital & Expenses

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
<th>Details</th>
</tr>
</thead>
<tbody>
<tr>
<td>4 ORs, 2 PRs – 18,000 square feet</td>
<td></td>
<td></td>
</tr>
<tr>
<td>40 Surgeon-Owners – ENT, Eye, GI, General, GYN, Ortho, Ophthalmology, Pain, Plastic, Urology</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Capital Requirements</td>
<td>$7,450,000</td>
<td>Architecture, construction, legal, equipment, furnishings, working capital</td>
</tr>
<tr>
<td>Partner Contributions</td>
<td>$1,000,000</td>
<td></td>
</tr>
<tr>
<td>Bank Loan</td>
<td>$6,450,000</td>
<td>7 years</td>
</tr>
<tr>
<td>Revenue</td>
<td>$5,340,000</td>
<td>5,600 total cases at $954 average reimbursement</td>
</tr>
<tr>
<td>Expenses</td>
<td>$4,803,840</td>
<td>Staffing, suppliers, rent, services, interest &amp; principal repayment</td>
</tr>
<tr>
<td>Free cash flow</td>
<td>$536,160</td>
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# Multi-Specialty: ROI

<table>
<thead>
<tr>
<th>Partner</th>
<th>% Stake</th>
<th>Initial Investment</th>
<th>Year 2 Return</th>
<th>Year 7 Return</th>
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</thead>
<tbody>
<tr>
<td>Hospital</td>
<td>51%</td>
<td>$510,000</td>
<td>$262,718</td>
<td>$451,553</td>
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<tr>
<td>Surgeon Owners (40 @ 1.225%)</td>
<td>49%</td>
<td>$490,000</td>
<td>$273,442</td>
<td>$469,983</td>
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</table>

**Return on Cash Invested**

|                       |         |                  | 54%           | 92%           |

<table>
<thead>
<tr>
<th></th>
<th>Initial Investment</th>
<th>Annual Return</th>
<th>Annual Distribution</th>
</tr>
</thead>
<tbody>
<tr>
<td>Individual Surgeons</td>
<td>$12,250</td>
<td>54%</td>
<td>$6,600</td>
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</tbody>
</table>

**50+% ROI on small investments equals $6,600 annual distributions per surgeon – “restaurant money”**
Spine/Ortho ASC: Capital & Expenses

| 2 ORs, 1 PR – 6,500 square feet | 
| 10 Surgeon-Owners – Spine, Orthopedic, Pain |

| Capital Requirements | $3,340,000 | Architecture, construction, legal, equipment, furnishings, working capital |
| Partner Contributions | $600,000 |
| Bank Loan | $2,740,000 | 7 years |

| Revenue | $4,050,000 | 2,600 total cases (300 spine, 800 ortho, 1,500 pain) | $1,558 average reimbursement |

| Expenses | $3,185,240 | Staffing, suppliers, rent, services, interest & principal repayment |

| Free cash flow | $864,760 |
### Spine Ortho: ROI

<table>
<thead>
<tr>
<th>Partner</th>
<th>% Stake</th>
<th>Initial Investment</th>
<th>Year 2 Return</th>
<th>Year 7 Return</th>
</tr>
</thead>
<tbody>
<tr>
<td>Surgeon Owners</td>
<td>51%</td>
<td>$306,000</td>
<td>$441,030</td>
<td>$615,523</td>
</tr>
<tr>
<td>(10 @ 5.1%)</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Hospital</td>
<td>24.5%</td>
<td>$147,000</td>
<td>$211,866</td>
<td>$295,693</td>
</tr>
<tr>
<td>Management Partner</td>
<td>24.5%</td>
<td>$147,000</td>
<td>$211,866</td>
<td>$295,693</td>
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</table>

**Return on Cash Invested**

<p>| | | | | |</p>
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<tbody>
<tr>
<td></td>
<td></td>
<td>144%</td>
<td>201%</td>
<td></td>
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</table>

<table>
<thead>
<tr>
<th></th>
<th>Initial Investment</th>
<th>Annual Return</th>
<th>Annual Distribution</th>
</tr>
</thead>
<tbody>
<tr>
<td>Individual Surgeons</td>
<td>$30,600</td>
<td>144%</td>
<td>$44,103</td>
</tr>
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</table>

**140+% ROI on larger investments equals $44,000 annual distributions per surgeon – “Yale money”**