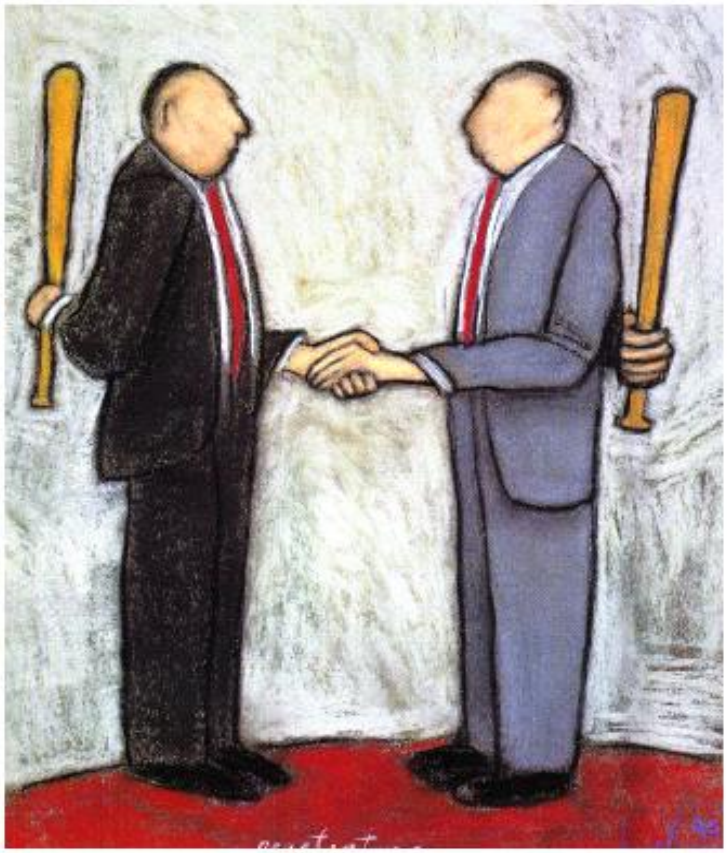
2009 Cancer Center Business Summit

October 8 – 9, 2009

The Adolphus Hotel • Dallas, Texas

Anatomy of a Cancer Center Transaction



A "Mock Negotiation"

Cancer Center
Business Summit
Dallas, Texas
October 8, 2009

Anatomy of a Cancer Center Transaction

- "Mock negotiation" of a transaction
- Five-physician medical oncology practice (Medical Oncology Associates - MOA)
- Three-physician radiation oncology practice (Radiation Oncology Associates - ROA)
- Community hospital (Highland Hospital)
- State with no CON; no corporate practice laws
- 60% Medicare; 30% commercial; 10% Medicaid

A people-friendly, Middle America, two hospital town

Anatomy of a Cancer Center Transaction

- A people-friendly, “Middle America,” two hospital town. Population 200,000
- Two medical oncology private practices (one of which is MOA). One radiation oncology private practice (ROA) with two employed rad oncologists at the competing hospital, St. Josephine’s
- St. Josephine: offers physician employment only. Highland Hospital: willing to explore private practice/hybrid arrangements

Scene 1
Physician meets physician

Anatomy of a Cancer Center Transaction

The Cast (in order of appearance)

- Scene 1: Physician Meets Physician
  - William Jordan, DO, the Medical Oncologist
  - Daniel Dosoretz, MD, the Radiation Oncologist
- Scene 2: Physician Meets Hospital
  - Michael Blau, JD, the Attorney
  - Michael Sack, the Hospital CEO

Scene 3
Consultants run the numbers

Anatomy of a Cancer Center Transaction

The Cast (in order of appearance)

- Scene 3: Consultants Run the Numbers

  Teri Guidi, MBA, Consultant #1

  Kelley Simpson, Consultant #2

- Scene 4: Wrap Up & Epilogue

  Richard Emery, Cancer Center Operator Perspective

Scene 1: Meeting of MOA and ROA Leaders: United We Stand

Why Come Together?

- Potential market growth opportunity to align with each other and Highland Hospital
- ROA does not want MOA to align with employed ROs at St. Josephine's
- Enhance bargaining power with HH
- Service diversification
- Integrated multi-disciplinary patient experience
- Quality and efficiency improvements from coordinated care
- Hedge bets on reimbursement erosion/trend toward global payments
- Shared ancillaries?
- Access to clinical trials?

Scene 1: Meeting of MOA and ROA Leaders: United We Stand

Should MOA/ROA Combine First?

- Business advantages
- Legal advantages
  - Cross-referrals
  - Shared ancillary revenue
  - Joint pricing

Scene 1: Meeting of MOA and ROA Leaders: United We Stand

Principal Obstacles to MOA/ROA Merger

- Shared governance
- Shared economics
- Change of brand identity
- Impact on referral sources (competing MO group)
- Different cultures
- Different IT platforms (and recent IT investments)
- Different billing arrangements
- Different debt profiles
- Different payment contracts/rates
- Different salary and benefit structures
- Different buy-sell arrangements
- Trust?

Scene 1: Meeting of MOA and ROA Leaders: United We Stand

Preliminary Decision on Practice Merger

- Merger would not be easy, and would take time and resources. Let's defer further consideration of merger until after we figure out if we can collaborate with Highland Hospital while retaining our independence.

Scene 1: Meeting of MOA and ROA Leaders: United We Stand

Do we need anyone else at this stage of the project?

- Other clinicians? Oncology surgeons? Urologists? Women's health specialists?
- Practice management company?
- Cancer center development company?
- Financial partner?
- Lawyer? Project counsel?
- Consultant?

Scene 1: Meeting of MOA and ROA Leaders: United We Stand

Conclusion

Let's go talk to Highland Hospital

Scene 2: ROA/MOA meets with Highland Hospital

Are there common goals and objectives?

Hospital Perspective

- Establish cancer care center of excellence for benefit of community
- Win-win-win: collaborate and grow market share while maintaining/enhancing hospital margins
- Position for future payment methodologies

Scene 2: ROA/MOA meets with Highland Hospital

Hospital Perspective (cont'd.)

- Alignment of Hospital and physician interests around quality and efficiency
- Shared responsibilities
- Shared risk and rewards
- Protect against destructive competition

Scene 2: ROA/MOA meets with Highland Hospital

- Consistent with Hospital tax-exempt mission, including serving all patients regardless of ability to pay
- Comply with legal requirements
- 340B pricing?
- Operationally and financially feasible?
- Durable/legacy
- Built on foundation of mutual trust and respect

Scene 2: ROA/MOA meets with Highland Hospital

MOA/ROA Perspective

- Generally subscribe to Hospital's principles, but:
- Skeptical about Hospital as partner
  - Trust v. mistrust
  - Practice autonomy v. Hospital control
  - Pace of decision-making
  - Hospital systems v. Practice systems
  - Hospital costs v. Practice costs

Scene 2: ROA/MOA meets with Highland Hospital

- Want to stabilize economics of practice in face of declining reimbursement and changing payment systems
- MOA can't afford to subsidize cost of chemo drugs for indigent patients
- Concern about losing referrals from PCPs and physicians employed by St. Josephine's
- If go it alone, could potentially develop own free-standing cancer center with ancillaries (lab, imaging, pharmacy, and lin acc) –with significant financial risk, and competition from both hospitals
- Other

Scene 2: ROA/MOA meets with Highland Hospital

Preliminary Decision

Parties agree that collaboration may be best strategic option if there is a legally compliant business model for the cancer center that is consistent with the common goals of the parties.

Scene 2: ROA/MOA meets with Highland Hospital

Potential Business Models

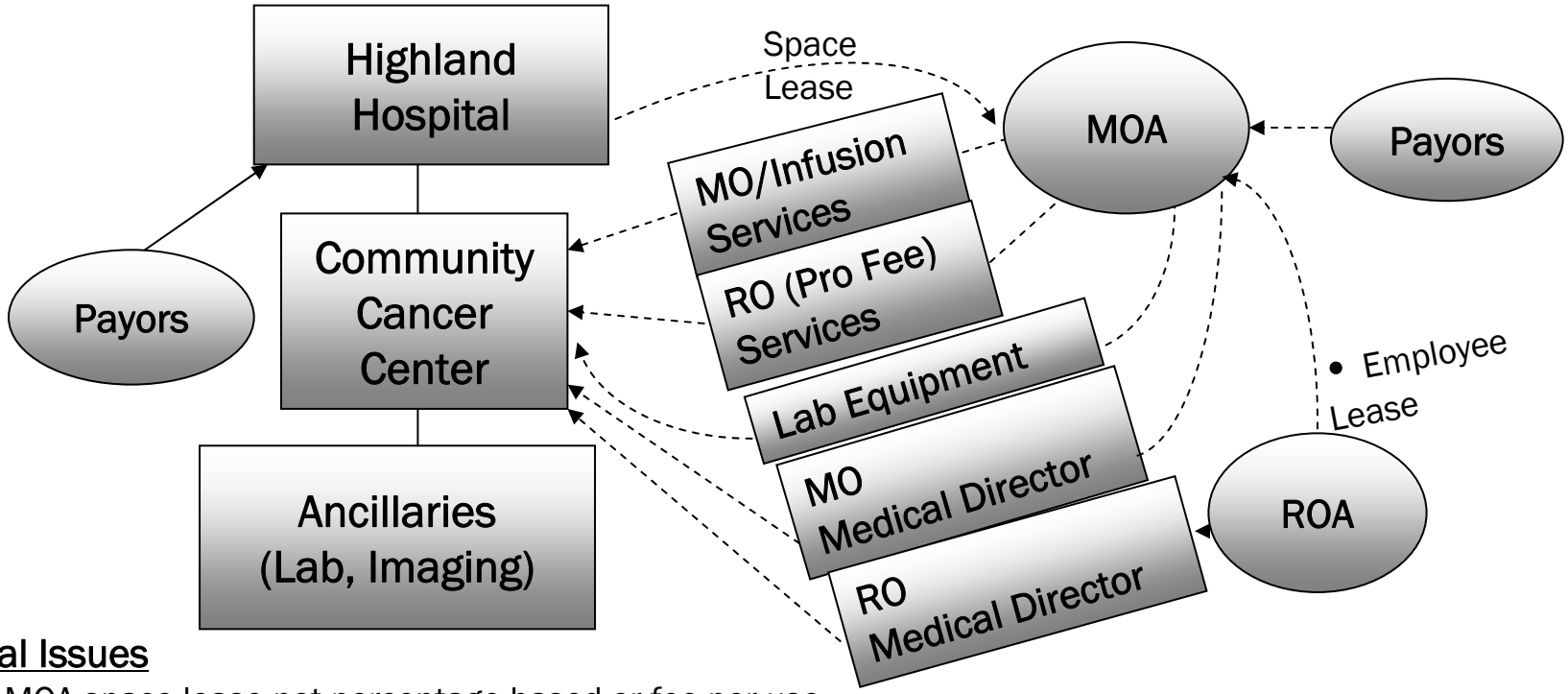
1. On-Campus Private Practice
2. Hospital Licensed Service with Modified Under Arrangements Joint Venture and Service Line Co-Management Agreement

Anatomy of a Cancer Center Transaction

Model 1: Private Practice On-Campus

- MOA leases space in Hospital Cancer Center
- MOA provides chemo as physician service (Physician Part B)
- MOA leases ROA physicians to provide RO pro services on Hospital radiation equipment; MOA bills for RO pro fees
- MOA sells certain assets to Hospital
- Hospital provides ancillaries (lab, imaging, radiation technical)
- Service line Medical Director agreements for MOA and ROA

Model 1: Private Practice on-Campus



<u>Legal Issues</u>

- MOA space lease not percentage-based or fee per use
- Lab equipment should be valued on a cost basis, not business enterprise basis
- All agreements must be fair market value
- No CON, but facility license
  - Outpatient facility
  - Linear accelerators
  - Imaging (MRI, PET/CT)

Model 1: Variants To Explore

- Eliminate RO employee lease – ROA keeps RO pro fee upside
- MOA keeps lab/lab revenue

Model 1: Private Practice On-Campus Benefit/Cost Scorecard

MOA	Hospital	ROA
• Infusion revenue New Revenue • FMV of Lab equipment • MO Medical Director fee • Mark-up on RO pro services? New Costs • Higher space lease cost? • Parking for employees? • Loss of lab margin vs. reduced lab staff costs • RO lease cost (including ramp-up)	New Revenue • Ancillaries – Lab, imaging • New admissions New Costs • Finances development of cancer center (space and equipment) • Pays for lab equipment • Incurs Medical Director fees	• Guarantee of existing pro fees? New Revenue • RO Medical Director fee No New Costs

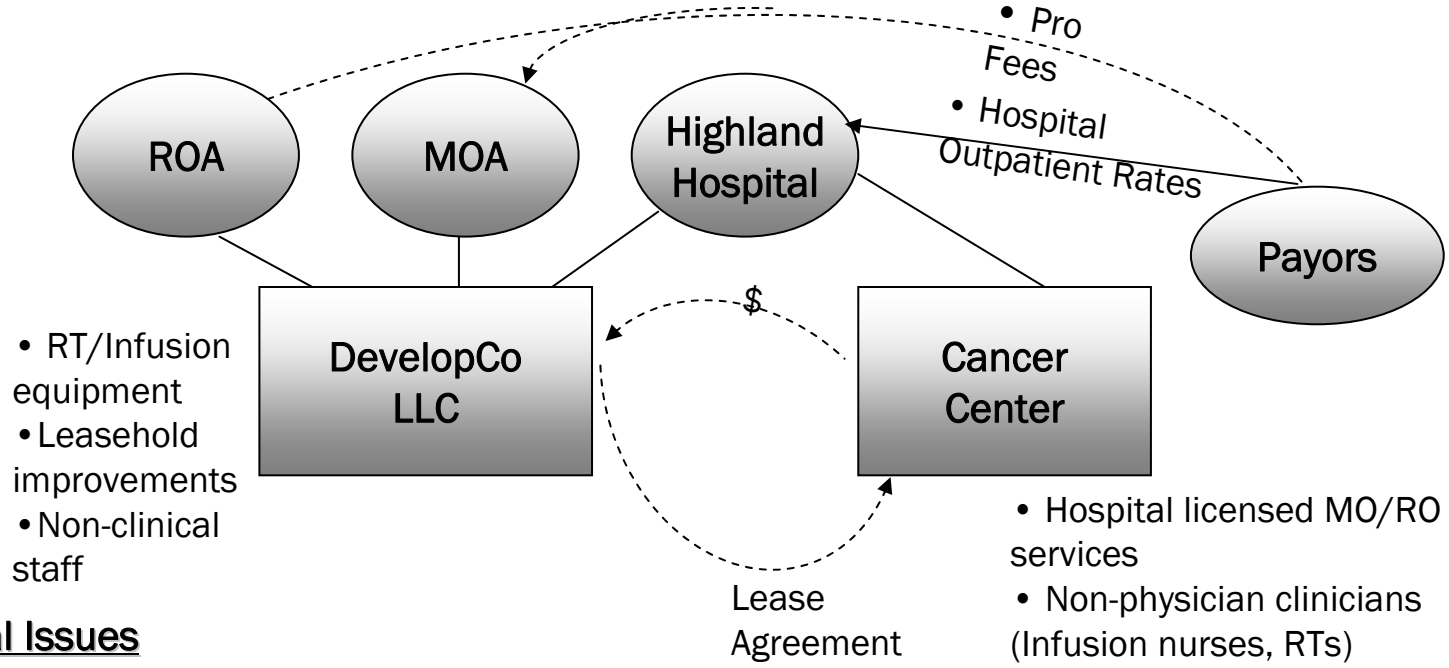
Anatomy of a Cancer Center Transaction

Model 2: Hospital Service and Co-Management

- JV entity to own equipment, tenant improvements and non-clinical staff
  - leased to Hospital at FMV
- Hospital is provider and bills for technical components of MO, RO, and ancillaries (Hospital Outpatient Rates)
- MOA and ROA bill for their own pro fees, or Hospital bills pro fees and pays contract rate to MOA/ROA
  - MOA and ROA can retain private practice space (or work out of hospital space)
- Service Line Co-Management Agreement – MOA and ROA provide comprehensive medical direction and co-management of service line – compensated with base and bonus fees

Model 2: Hospital Service and Co-Management

Equity Joint Venture Component

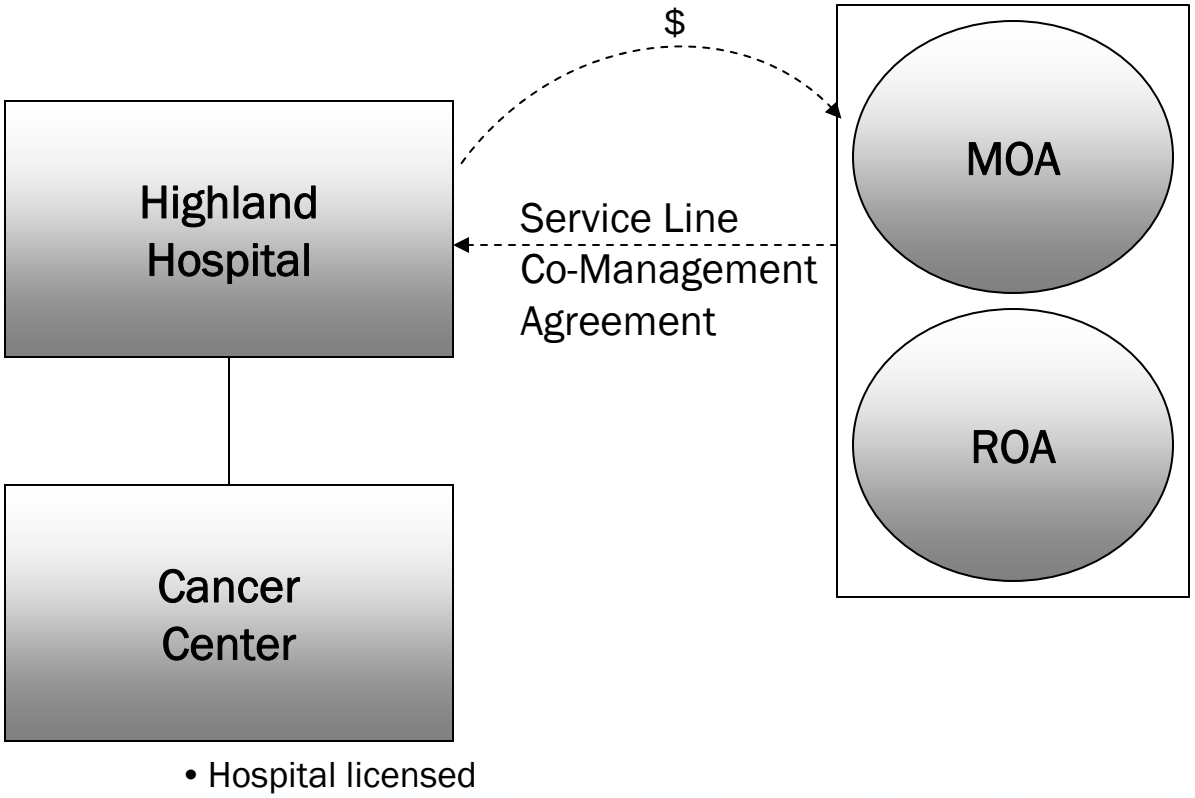


Legal Issues

- 340B pricing for drugs
- DevelopCo cannot "perform" the technical component of the RO/MO services
- Lease agreement cannot be percentage-based or per-click for equipment or leasehold improvements
- Lease agreement must be fair market value
- Site of service differential on pro fees if professional services provided in hospital space

Model 2: Hospital Service and Co-Management

Service Line Co-Management Component



Service Line Co-Management

There are typically two levels of payment to oncologists under the service line contract:

- Base fee – a fixed annual base fee that is consistent with the fair market value of the time and efforts participating oncologists dedicate to the service line development, management, and oversight process
- Bonus fee – a series of pre-determined payment amounts contingent on achievement of specified, mutually agreed, objectively measurable, program development, quality improvement and efficiency goals
- Pays participating oncologists 4-7% of service line revenues (on a fixed fee basis)

Sample Medical Oncology Performance Standards

- Increase in percentage of patients with written treatment plans at start of infusion
- Increase in percentage of written treatment plans with indication of:
  - Staging
  - Intention of therapy
  - Approved treatment regimen for tumor site/staging
- Increase in percentage of written treatment summaries at completion of course of treatment

Sample Medical Oncology Performance Standards

- Increase in patient satisfaction
- Increase in staff satisfaction
- Decrease in infusion site infections
- Substitution of lower cost drugs/items for drugs/items of equivalent efficacy and quality

Model 2: Hospital Service and Co-Management

- Legal constraints on Service Line Co-Management Agreements
  - No stinting
  - No steering
  - No cherry-picking
  - No gaming
  - No payment for changes in volume/referrals
  - No payment for quicker-sicker discharge
  - Must be FMV; independent appraisal required
- Proposed Stark Law Exception for Incentive Payment and Shared Savings Programs

Model 2: Scorecard

MOA	Hospital	ROA
• MO/Infusion professional fees New Revenues • DevelopCo distributions • Service line co-management payments New Costs • DevelopCo capital contribution • Eliminates drug and treatment nurse costs • Loss of lab revenue?	• MO/RO facility fees New Revenue • Ancillary services (lab, imaging and pharmacy) New Costs • DevelopCo capital contribution • Payments under DevelopCo lease • Co-Management payments	• RO pro fees New Revenue • DevelopCo distributions • Co-Management fees New Costs • DevelopCo capital contribution

Anatomy of a Cancer Center Transactions

Model 1 or Model 2?

- Confidentiality Agreement to share data and establish parameters of discussion
- Engage Consultants to run some numbers
- Scene 3 Consultants present the numbers

Assumptions for Model 1: Private Practice on Campus

- Baseline ROA salaries at current earnings, increase proportionately with growth
- MOA obtain 15% better performance for ROA professional fees from better contract terms and better collection rates
- MOA spends 3% in the billing of ROA (ROA previously spent 5%)
- HH anticipates 5% rise in imaging utilization and 3% better contract rates for lab than MOA prior to other volume increases
- MOA moves from $28/sq ft to $34/sq ft but gives up 2,000 sq ft for lab and common areas

Model 1: Before the Transaction: Participants' Current Situation

	MOA: 5-Person	ROA: 3-Person	Community Hospital	Notes
	1,250 New Pts	750 Courses of Tx	1,500 New Cancer Cases	Annual Volumes
Professional Collections	$20,500,000	$1,650,000	$ ----------	MO-E&M, Chemo Admin, Drugs & Procedures; RO Prof Svcs
Technical Collections	$300,000	----------	$9,750,000	Technical RO & Ancillary Svcs; Lab at MOA
Service Line Revenues	----------	----------	$3,450,000	HH revenue from other services to cancer pts
NET REVENUES	$20,800,000	$1,650,000	$13,200,000	
DIRECT EXPENSES	$18,075,000	$165,000	$4,850,000	Staff, Space, Equip, Supplies, Gen + Admin Expenses
CONTRIBUTION REVENUES/ ADJUSTED NET INCOME	$2,725,000	$1,485,000	$8,350,000	
CONTRIBUTION PER PHYSICIAN AND CANCER CASE	$545,000 $2,180	$495,000 $1,980	——— $5,567	

Model 1: The Transaction

	MOA	ROA	HH
Initial Contribution			$525,000
Annual Finance Payments			$414,507
Purchase of Lab and Misc. Assets	$200,000		$200,000
TOTAL	$200,000		$1,139,507

- Assumptions:
  - Initial contribution at 15% of loan amount for equipment and leasehold improvements
  - Finance payment amortized at 7% over 10 years

Model 1: After the Transaction… Participants' Future Position

	MOA 5-Person Private Practice	ROA 3-Person	Community Hospital	Notes
	1,313 New Pts	788 Courses of TX	1,575 New Cancer Cases	5% volume increase
Professional Collections	$21,784,875	$1,732,500	$----------	Prof Fees + Chemo
Technical Radiation and Ancillary Collections	----------	----------	$10,561,950	
Medical Directorships	$75,000	$75,000		
Lease			$5,712,000	
Oncology Service Line Revenue	----------	----------	$3,622,500	
NET REVENUES	**$21,859,875**	**$1,807,500**	**$19,896,450**	

Model 1: Position of Each Participant

	MOA 5-Person Private Practice	ROA 3-Person	Community Hospital
BEFORE THE TRANSACTION…			
Net Income	$2,725,000	$1,485,000	$7,932,500
Income Per Physician	$545,000	$495,000	----------
Income Per Cancer Case	----------	----------	$5,288
AFTER THE TRANSACTION…			
Net Income	$3,250,700	$1,720,875	$12,781,746
Income Per Physician	$650,140	$573,625	----------
Income Per Cancer Case	----------	----------	$8,225
ENHANCED POSITION	$525,700	$235,875	$4,849,246
Per Physician	$105,140	$78,625	----------
Per Cancer Case	$401	$300	$3,079

Model 1: After the Transaction… Participants' Future Position

	MOA 5-Person Private Practice	ROA 3-Person	Community Hospital
NET REVENUES	$21,859,875	$1,807,500	$$19,896,450
Direct Expenses	$18,809,175	$86,625	$5,242,500
Transaction			$1,139,507
Medical Directorships			$150,000
EXPENSES	$18,809,175	$86,625	$5,242,500
CONTRIBUTION REVENUES	$3,050,700	$1,720,875	$14,653,950
REVENUE PER PHSICIAN & CASE	$610,140 $2,324	$573,625 $2,185	---------- $9,304

Model 1: Future Growth Enhanced Positions

	Increase of 3% Annual Caseloads	Increase of 5% Annual Caseloads	Increase of 7% Annual Caseloads	Increase of 10% Annual Caseload
MOA	$360,220	$525,700	$691,180	$939,400
- per physician	$72,044	$105,140	$138,236	$187,880
- per case	$280	$401	$517	$683
ROA	$204,525	$235,875	$267,225	$314,250
- per physician	$68,175	$78,625	$89,075	$104,750
- per course	$265	$300	$333	$381
HH	$4,684,725	$4,849,246	$5,013,767	$5,260,548
- per case	$3,032	$3,079	$3,124	$3,188

Assumptions for Model 2

Provider-Based Service with Modified Under Arrangements Joint Venture and Service Line Co-Management Agreement

Model 2: Before the Transaction: Participants' Current Situation

	MOA: 5-Person	ROA: 3-Person	Community Hospital	Notes
	1,250 New Pts	750 Courses of Tx	1,500 New Cancer Cases	Annual Volumes
Professional Collections	$20,500,000	$1,650,000	$ ----------	MO-E&M, Chemo Admin, Drugs & Procedures; RO Prof Svcs
Technical Collections	----------	----------	9,750,000	Technical RO & Ancillary Svcs
NET REVENUES	$20,500,000	$1,650,000	$9,750,000	
DIRECT EXPENSES	$17,800,000	165,000	4,850,000	Staff, Space, Equip, Supplies, Gen + Admin Expenses
CONTRIBUTION REVENUES/ ADJUSTED NET INCOME	$2,700,000	$1,485,000	$4,900,000	
CONTRIBUTION PER PHYSICIAN AND CANCER CASE	$540,000 $2,160	$495,000 $1,980	——— $3,267	

Model 2: DevelopCo Transaction

	MOA	ROA	HH
Initial Contribution	($175,000)	($175,000)	($175,000)
Annual Finance Payments	(138,169)	(138,169)	(138,169)
Annual Lease Revenues			
Equipment	$174,163	$174,163	$174,163
Leasehold Improvements	26,705	26,705	26,705
Non-Clinical Staff	183,333	183,333	183,333
TOTAL Lease Revenues	$384,201	$384,201	$384,201
Annual Return on Investment			
Year 1: 23%	$71,032	$71,032	$71,032
Years 2-10: 178%	246,032	246,032	246,032

- Assumptions:
  - 1/3 ownership by each participant
  - Initial contribution at 15% of loan amount for equipment and leasehold improvements
  - Expense absorption of non-clinical staff at $500,000
  - Finance payment amortized at 7% over 10 years

Model 2: After the Transaction… Participants' Future Position

	MOA 5-Person Hospital-Based	MOA: 5-Person Private Practice	ROA: 3-Person	Community Hospital	Notes
	1,250 New Pts	1,250 New Pts	750 Courses of Tx	1,500 New Cancer Cases	
Professional Collections	$1,600,000	$2,000,000	$1,650,000	$ ----------	Prof Fees Only
Technical Collections	----------	----------	----------	24,750,000 9,750,000	Chemo RT & Ancillaries
DevelopCo Revenues	384,201	384,201	384,201	384,201	Lease Revenues
MOA Supervision Fee	600,000	600,000	----------	----------	Chemo Oversight
ROA Med Director Fee	----------	----------	----------	----------	
Co-Mgmt Model Base Mgmt Fee Bonus Mgmt Fee	 941,850 627,900	 941,850 627,900	 507,150 338,100	 ---------- ----------	
NET REVENUES	**$4,153,951**	**$4,553,951**	**$2,879,451**	**$34,884,201**	

Model 2: After the Transaction…
Participants' Future Position (*continued*)

	MOA: 5-Person Hospital-Based	MOA: 5-Person Private Practice	ROA: 3-Person	Community Hospital
NET REVENUES	$3,157,034	$3,557,034	$2,682,034	$29,768,284
Direct Expenses	$1,010,417	1,166,667	331,667	19,016,667
DevelopCo Contribution	175,000	175,000	175,000	175,000
DevelopCo Finance Payment	138,169	138,169	138,169	138,169
MOA Supervision Fee	----------	----------	----------	600,000
ROA Med Director Fee	----------	----------	----------	----------
Co-Mgmt Model	----------	----------	----------	2,415,000
Lease Expense	----------	----------	----------	1,152,603
EXPENSES	$1,323,586	$1,479,836	$644,836	$23,497,439
CONTRIBUTION REVENUES	$2,830,365	$3,074,115	$2,234,615	$11,386,762
REVENUE PER PHYSICIAN & CASE	$566,073 $453	$614,823 $492	$744,872 $993	---------- $7,591

Model 2: After the Transaction… Enhanced Position of Each Participant

	MOA: 5-Person Hospital-Based	MOA: 5-Person Private Practice	ROA: 3-Person	Community Hospital
BEFORE THE TRANSACTION…				
Net Income	$2,700,000	$2,700,000	$1,485,000	$2,450,000
Income Per Physician	$540,000	$540,000	$495,000	———
Income Per Cancer Case	$2,160	$2,160	$1,980	$1,633
AFTER THE TRANSACTION…				
Net Income	$2,830,365	$3,074,115	$2,234,615	$6,000,881
Income Per Physician	$566,073	$614,823	$744,872	———
Income Per Cancer Case	$2,264	$2,459	$2,979	$3,796
ENHANCED POSITION	$130,365	$374,115	$749,615	$3,243,381
Per Physician	$26,073	$74,823	$249,872	———
Per Cancer Case	$104	$299	$999	$2,162

Model 2: Future Growth of Incremental Contribution Revenues

	Contribution Per Case	3% Annual Caseloads	5% Annual Caseloads	7% Annual Caseloads	10% Annual Caseloads
MOA	$2,459	$3,165,963	$3,227,438	$3,288,913	$3,381,125
- Per Physician		$633,193	$645,488	$657,783	$676,225
- Incremental To Before Transaction		1,288 New Pts $465,963	1,313 New Pts $527,438	1,338 New Pts $588,913	1,375 New Pts $681,125
ROA	$3,079	$2,302,767	$2,347,452	$2,392,137	$2,457,675
- Per Physician		$767,589	$782,484	$797,379	$819,225
- Incremental To Before Transactions		773 Courses of Tx $817,767	788 Courses of Tx $862,452	803 Courses of Tx $907,137	825 Courses of Tx $972,675
HH	$3,796	$5,864,820	$5,978,700	$6,092,580	$6,263,400
- Incremental To Before Transaction		1,545 Cases $3,414,820	1,575 Cases $3,528,700	1,605 Cases $3,642,580	1,650 Cases $3,813,400

Anatomy of a Cancer Center Transaction

Preliminary Decision

Approach #2 is preferred

Subject to further due diligence

and definitive documentation

Anatomy of a Cancer Center Transaction

Potential Deal Breakers

- Governance/decision-making
- Deadlock/dispute resolution
- Capital contribution/costs
- Exclusivities and rights of first refusal
- Covenants not to compete/restrictive covenants
- Duration
- Termination/withdrawal rights
- Buy-out provisions
- Operational integration (staff, IT platform and interfaces)
- Timing and existing commitments (e.g., space leases)

Anatomy of a Cancer Center Transaction

Next Steps: Planning Phase

- Prepare legal documents
- Space planning
- Equipment selection
- Operational integration planning/team
  - Work plan (staff, work flow processes, IT systems)
  - Roles/responsibilities
  - Timetable
- Prepare for implementation and “go live”

Anatomy of a Cancer Center Transaction

Scene 4 Epilogue

Cancer Center Operator Perspective

Anatomy of a Cancer Center Transaction

Audience Question & Answer Period

Role	Name
Moderator	Ronald Barkley
Medical Oncologist	Dr. William Jordan
Radiation Oncologist	Dr. Daniel Dosoretz
Hospital CEO	Michael Sack
Attorney	Michael Blau
Consultant for Model 1	Teri Guidi
Consultant for Model 2	Kelley Simpson
Cancer Center Operator	Richard Emery