




MERIDIAN
SURGICAL PARTNERS

Performance, Efficiency, Achievement, Knowledge

DATA, DILIGENCE, AND DEDICATION MAKES NEW SURGERY CENTER A REALITY

*How Meridian Surgical Partners aligned with local physicians
to successfully develop the first surgery center in Cleburne, Texas.*

A De Novo Development Success Story



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BACKGROUND

Cleburne Surgical Center began with one surgeon's vision to build the first multi-specialty ambulatory surgery center in the small town of Cleburne, Texas. With a population of just over 29,000, Cleburne is located 30 miles south of Fort Worth. With only one hospital and no other ASCs within a 15-mile radius, Dr. Blaine Farless believed it was time to provide an alternative outpatient surgery setting to the patients and physicians in the area. As a successful surgeon, with a thriving orthopedic practice, he was frustrated with the limited options for his outpatient cases and the inefficiencies that existed within a hospital setting. His dream was to develop an outpatient surgery facility that provided an efficient, convenient, comfortable, and cost-effective environment that centered on patient care and outcomes.

He knew his and other physicians' input would be important; however, he also understood that developing a surgery center was a complex undertaking that would require the expertise and experience of an additional partner. Finding and selecting the right corporate partner became the crucial next step to ensure the success of the project

Syndicated partnership **May 2006**

Began construction **April 2007**

STRATEGY AND EXECUTION

Defining Project Scope

Led by healthcare veterans with years of management and development experience, Meridian Surgical Partners, entered the scene. Meridian took an analytical approach to determine the feasibility of the Cleburne Surgical Center project. First, working closely with Dr. Farless and his orthopedic practice partner Dr. Brad Harman, Meridian identified recruitment candidates for the partnership. It is crucial to carefully select the right number of partners and the appropriate mix of specialties to support a facility. A dominant sub-specialty thread such as orthopedics, pain management, otolaryngology (ENT), ophthalmology, gastroenterology, or general surgery gives the project its best opportunity for success. One of the first partners recruited was Dr. Michael Phillips, a local pain management physician. In addition to pain management, three more surgeons joined the group (orthopedics, ophthalmology, and gynecology). With recruitment underway, Meridian was ready to move onto the process of building financial projections.

Meridian used a variety of methods to determine the net transfer of cases that the physicians would bring to the center. Knowing that this information would reveal the scale of the facility and the ultimate cost to build the new facility, Meridian collected data from both physician practice billing systems and from in-depth interviews conducted with the physicians to gain intelligence. As part of this diligence, Meridian also took into account the current healthcare political landscape and the payor environment to apply the appropriate discounts. Once a realistic case volume was established, Meridian concluded that the facility could support two operating rooms (ORs) and one procedure room in an 8,300 square foot space, in addition to the medical office space that was part of the master plan of the project. Further historical experience and benchmarks were used to estimate operating costs, tenant improvements (construction), equipment, and the working capital needed to appropriately fund the project. After establishing a budget, a detailed multi-year business plan was developed and presented to the physicians.

COST TO BUILD

As a general industry rule of thumb, each OR can accommodate a maximum of 1,500 cases per year (depending on specialty). Plan to spend approximately \$1 million per OR. This consists of between \$450,000 and \$600,000 for equipment.

EQUITY

The need for equity is isolated to working capital – typically four to eight months' operating expenses translating into \$1 million to \$1.5 million. The investments range from \$10,000 to \$15,000 for a 1 percent interest in the partnership plus assumption of pro-rata debt dependent on debt structure.

3 MOST COMMON MISTAKES IN SURGERY CENTER DEVELOPMENT

- **Overbuilding** – this is a major part of the planning process in determining a realistic case volume and can be a significant driver in centers that fail.
- **Low case volume** – operating with less than the expected number of cases can result in negative cash flow that will wreck a business in the early stages and make it very difficult to recover.
- **Under capitalizing** – without accounting for and raising adequate working capital to operate during the ramp-up stage of the center, the business cannot operate to its full potential and can quickly lead to cash flow problems.

Partnership Formation

Supported by positive data, the decision was made to move forward with the development of the multi-specialty outpatient surgery center project and in May 2006 the partnership between Meridian Surgical Partners and six local physicians was officially syndicated.

Real Estate

As with all real estate, location plays a key role. The site for the future surgery center was centrally located at the intersection of the two major highways in the area, providing good visibility along with easy access to the facility. In addition, the center would be located only a few miles from the hospital and other physician offices for added convenience for patients and physicians.

Equity

After working capital needs were analyzed, the partnership decided to raise the \$1.5 M in cash needed to fund the pre-operation and post operation start-up phases of the project. These funds were used to pay for an administrator's salary several months prior to opening, and to fund the salaries of staff and the monthly short fall in operating cash until the partnership broke even. **In the case of Cleburne, the center generated positive EBITDA by the sixth month of operation and generated positive cash flow by the ninth month of operation.**

Debt

Meridian presented the Cleburne project to several financing institutions prior to syndication. Once the development phase was set to begin, a commitment was received to fund the tenant improvements and equipment with a seven-year capital lease. Because the project had many favorable factors, Meridian initially worked to obtain non-recourse financing; however, it did not have enough partners to get past a guarantee requirement.

Due to this, Meridian proposed (and the bank agreed) that the guarantee would be structured to burn off at any point after the first calendar year of operations in which the financial projections submitted were met on an annualized basis. To help with cash flows at the onset of operations, the debt was also structured whereby no payments were required for the first three months and interest only payments were required for the next three months.

Development

An architect with former ASC experience was selected to design the center and associated medical office building. Meridian took a hands-on approach to effectively lead the decision-making and streamline execution, while working closely with the architect and the physician partners to approve a design. The construction team was subsequently hired by the real estate partnership. Meridian incorporated a proprietary project management system that consisted of a timeline and communications strategy that

kept all parties well-informed and empowered throughout each phase of development. Through weekly meetings, all key members were briefed to ensure that milestones were being met. Throughout the process, physician partners were included and encouraged to be involved to their desired level.

Marketing

Promoting the future opening of the center to the community was important, so a construction site event was held a few months prior to opening. This proved to be successful in identifying additional physician and staff recruits. Press releases to the media and invitations to a select group helped spread the word about the event. An open house was hosted by the partnership one week prior to performing cases. Additionally, a corporate identity was developed that included of a logo, letterhead, literature, and website.



Opened/began performing cases **September 17, 2007**

Met budgeted case volume **December 2007**

OPERATIONS

A huge component of the project included the many tasks necessary to operate the center on a daily basis. A master checklist of items must be managed that include human resources/staffing, equipment planning, licensing, managed care contracting, inventory management, and information technology. In addition, the establishment of policies, procedures, and workflow plans are essential to efficiently operate the center.



Human Resources/Staffing

Identifying and hiring the center administrator was the first step in staffing the facility. With the leadership of an experienced administrator on board months before the center opened, a ramp-up plan was established and executed, designing initial staffing around a condensed schedule, opening only enough days to accommodate early volume, then expand to run a full schedule as volume dictates.

Equipment Planning

Meridian worked closely with an equipment planner with specific ASC experience to streamline the process of designing, purchasing, and placing the equipment in the center. The reputable equipment planner had established working relationships with regional and national manufacturers as well as the ability to work seamlessly alongside the architects and construction teams.

Licensing

Meridian moved early and quickly to begin the process of gathering information from all physician partners to submit for licensing. While the application for Medicare certification was completed well before the center opened, a decision was made in advance to apply for deemed status through the AAAHC (Accreditation Association for Ambulatory Health Care). **The survey was successfully completed within five months of opening.**

Managed Care

Reimbursement is the lifeline of an outpatient surgery center. Meridian used their relationships and expertise in the payor environment to negotiate and establish plans for ongoing contracting success. **The first major contract was successfully negotiated in the first six months of operation.**

Inventory Management

In order to effectively manage inventory and supply costs, preferences cards by procedure were created early and standardized among the physicians. Careful consideration was taken in choosing products to ensure the highest level of quality at the most cost-efficient price. Additionally, the physicians actively participated in the early decision making points around supplies and costs.

Information Technology

By determining the data points to capture in advance and prioritizing the tracking and reporting capabilities needed, Meridian made a well-informed decision on the type of information systems to implement. Additionally, Meridian monitored operations through a proprietary system that seamlessly extracts real-time data from the facility's existing information and billing systems and converts it into dashboard reports. With this data, Meridian can identify trends, benchmark and track key indicators against historical data from the center and other Meridian facilities. From the center level, administrators use the application to get a detailed real-time view of financial and clinical data allowing them insight to better manage day-to-day activities.



CHALLENGES

Managing Expectations

The strength of any partnership can be tested by its ability to address and resolve differences. One of the early obstacles Meridian faced was managing the expectations of the physicians. The physician partnership initially wanted to build a much larger 16,000 square foot facility comprised of four ORs. As an experienced ASC management and development partner, Meridian knew that overbuilding can quickly cause a project to fail. Supported by case volume data, Meridian presented the information to the physicians and convinced them to focus on an 8,300 square foot facility with two ORs and one procedure room, built with a shelled OR to meet anticipated future expansion. The surgery center was part of a master plan that included a physician clinic, offices, imaging, and other related medical businesses.

Changing Perceptions

As the first ASC in the area, the new facility would be a direct competitor of the hospital as related to outpatient procedures. Meridian was very sensitive to the fact that local physicians would have concerns about their loyalties to the hospital and fear of possible retribution for taking their cases elsewhere. They appropriately dealt with these concerns and leveraged the influence of the partners to help sway the thinking of potential recruitment targets.

As part of this, it was also important to ensure that local referring physicians, schedulers, and patients were educated about the benefits of a new outpatient surgery facility.

RESULTS

After an 18-month process, the Cleburne Surgical Center hosted an open house that was covered by media and attended by local physicians, city officials, and other community guests. Only 11 days after receiving their Certificate of Occupancy, Cleburne Surgical Center was delivered under budget, officially opening its doors and performing cases on September 17, 2007.

Initially offering outpatient procedures in orthopedics, pain management, ophthalmology, gastroenterology, gynecology and general surgery, Meridian continued to recruit physician utilizers to diversify its offerings to later include otolaryngology (ENT), plastic surgery, podiatry, and urology.

Due to the solid infrastructure that included a sophisticated business plan, industry relationships, operational expertise, and committed physician partners, the Cleburne Surgical Center exceeded expectations by...

- Meeting budgeted case volume in first three months of operation
- Generating positive EBITDA by the sixth month of operation and positive cash flow by the ninth month of operation
- Receiving Medicare certification within 6 months
- Obtaining first managed care contract within first six months of operation
- Realizing a 20% cash on cash return within first nine months of operation

Received Medicare certification **March 2008**

Generated positive cash flow **May 2008**



The future looks bright for Cleburne Surgical Center as its case volume increases and offerings expand, its reputation as an exceptional outpatient facility grows, and the mutually-beneficial relationship between the physician partners and Meridian continues to mature.

KEYS TO SUCCESS

- **Carefully select development partners** (legal, banking/lending, architect, construction, equipment, information technology, supplies, etc.) with relevant surgery center development experience so there is no learning curve to overcome.
- **Appropriately forecast case volume to determine project scope and budget** that ultimately drive all other aspects of the project including equipment, staffing, inventory and working capital.
- **A physician champion MUST emerge** in order to keep the project viable. This “lead” physician will serve as the voice of the physician partnership and will play a key role in recruiting new physicians, increasing awareness among referring physicians and patients, and sustaining hospital relations.
- **A detailed and data-driven business plan** will yield the best chance of successful execution which equates to positive cash flow and increased productivity.
- **Select a corporate partner with proven experience** in physician partnership development and ASC management.
- **Implement a marketing communications strategy** targeted to referral sources and utilizers that focuses on the benefits of the ASC. Using tools such as literature and a website can build awareness and reputation, leading to increased case volume.

Meridian Surgical Partners aligns with physicians in the acquisition, development and management of multi-specialty ambulatory surgery centers and surgical facilities. Meridian acquires interests in established physician-owned surgical facilities, as well as, partners with physicians seeking to grow their businesses locally through the development of new surgical facilities.

To learn more about our company and services visit our website at www.meridiansurg.com

