



ACCESS TO CAPITAL

2015 in Review and a Look into 2016

Thursday, December 10, 2015



Presenters



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The Deal & Regulatory Landscape

- Transactional Arena
 - M&A Continued to be Active
 - Two Primary Trends of Handling “Acquired Debt”
 - Bank Direct Purchases Continued to be Active
 - Issuance of Taxable Debt Still in Plan
- SEC Activity
 - Initial Settlements with Broker Dealers Relating to MCDC Initiative
 - Emerging Picture on What is “Material”
 - Anticipate 2016 to be Active with Issuer/Obligated Person Settlements
 - Focus on Policies and Procedures
- IRS Matters
 - 501(r)
 - Mixed-Use Projects and Implications for Health Care Organizations
 - Management Contracts

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Transactional Arena

- M&A Continued to be Active
- Two Primary Trends of Handling “Acquired Debt”
 - Incorporation: Refinance/Substitution
 - Separate Credit Systems
- Bank Direct Purchases Continued to be Active
 - What happens if banks reduce funding
 - Possible Tax Rate Changes
 - Rating Agencies prefer (or insist) that DP information be posted to EMMA
 - Posting may Create Issues
 - Tension between Keeping DP covenants on same terms as public debt; potential for Conflicting Rights
- Taxable Issuance—Still in Play
 - Rate environment
 - Benefits to consider

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SEC Activity

- Initial Settlements with Broker Dealers Relating to MDCI Initiative
 - SEC has charged 36 broker dealers for fraudulent offerings
 - SEC has sanctioned 22 broker dealers for fraudulent offerings
- Emerging Picture on What is “Material”
- Anticipate 2016 to be Active with Issuer/Obligated Person Settlements

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SEC Activity (continued)

- Focus on Policies and Procedures
 - Primary AND Secondary Market Disclosure
 - Importance of training
 - Importance of designating one or more persons to have responsibility
 - Year end review
 - Understanding of material events
- Increased Emphasis on Transparency, Liquidity and Fairness
 - Liquidity crisis?
- Quick Word on What is to Come
 - 2010 SEC Report?



IRS Matters

- 501(r)
 - Enacted in the Affordable Care Act
 - Community Health Needs Assessment requirements, financial assistance policy requirements, requirements relating to limitations on charges, and billing and collection requirements
 - Final regulations published December 31, 2014
 - Generally apply to taxable years beginning after December 29, 2015
 - Contain very detailed requirements that generally are not safe harbors
 - Requirements include not only conducting CHNA and adopting policies, BUT ALSO ACTUAL IMPLEMENTATION



IRS Matters (continued)

- Mixed-Use Projects and Implications for Health Care Organizations
 - Rules for equity contributions are generally more flexible, but not in all cases more favorable
 - “Floating use” is expressly permitted
 - A project that may be treated as funded in part with qualified equity is defined very broadly
 - Important limitations mostly concern timing
 - Favorable treatment of partnerships
 - No special elections or recordkeeping requirements
 - Effective dates
 - Implications for tax-exempt bond compliance procedures

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IRS Matters (continued)

- Management Contract Changes
 - NABL sent to the IRS and Treasury Department suggested revisions to expand the safe harbors against private business use in Rev. Proc. 97-13. NABL made three basic recommendations:
 - First, safe harbors for contracts having a term greater than five years relying on the “fixed fee” framework should be made more flexible in a manner comparable to the flexibility provided in Notice 2014-67 for five-year contracts, and certain principles developed in private letter rulings should be reflected in published guidance.
 - Second, there should be additional safe harbors that are not based on “fixed fee” limitations.
 - And third, the limitation set forth in the existing regulations prohibiting management and other service contracts “based, in whole or in part, on a share of net profits” should be reconsidered, and a more flexible rule focusing on control relationships should be adopted

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Strategies & Structures

Victor J. Radina
Executive Director
Morgan Stanley



EVOLUTION OF THE STRATEGIC PARADIGM

Webinar: Disruptive Medicine, 10/27/2015, 11:49:28 OCT 2015 12:34 PM ET

Evolution of Healthcare Delivery

- Not-for-profit healthcare delivery is evolving from volume-to-value-to-risk
- This is taking various forms as providers evolve from a fee for service paradigm to value focused, healthcare risk management
- There are four consistent themes across health system strategies

1

Alignment and integration of physicians across employment and affiliation, including incentives

2

Investment in healthcare information technology

3

Expansion of control over non-acute components of care continuum

4

Migration from fee for service to risk management



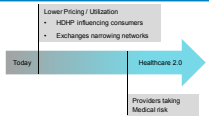
EVOLUTION OF THE STRATEGIC PARADIGM

Evolution of Healthcare Delivery

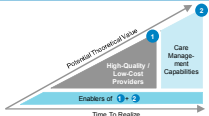
Size of lines and boxes indicate relative patient volume

- New models likely to emerge
 - Case management capabilities
 - Emergency room alternatives and primary care extenders
 - Urgent care / freestanding emergency departments

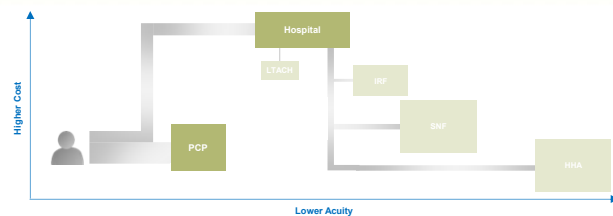
2015: Shift to Healthcare 2.0 will be "Tradable Theme"



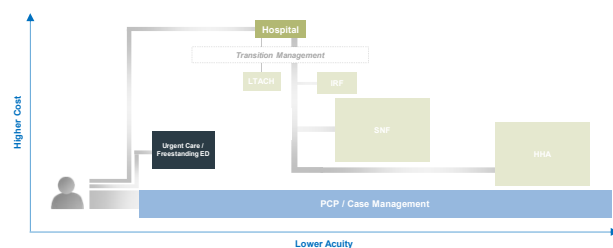
Characteristics for Success



Delivery System Today



Potential Delivery System



NONPROFIT HOSPITAL PAYOR STRATEGIES


Not-for-Profit Risk Strategies

- With significant investments in healthcare information technology and physician integration and alignment, not-for-profits are developing the capabilities to assume and manage risk through:



- As well as sponsored managed care organization ("MCO") growth through:



















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NONPROFIT HOSPITAL PAYOR STRATEGIES

Selected Payor/Provider Strategic Transactions

	----- Acquisition -----	
	----- Merger -----	
	----- Acquisition -----	
	----- Acquisition -----	
	----- Acquisition -----	
	----- Joint Venture -----	
	----- Established -----	

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NONPROFIT HOSPITAL PAYOR STRATEGIES

Ascension Health / U.S. Health and Life Insurance

Ascension Care Management

Transaction Highlights

- USHL's target market has typically been small employers (<100 employees), but the deal improves Ascension's ability to engage in risk-based contracting
- Expanded coverage provides infrastructure for population health management goals
- Acquisition improves Ascension's ability to offer exchange products through the CIN Together Health Network with Trinity

Transaction Overview


- In February 2015, Ascension announced plans to acquire U.S. Health and Life Insurance for \$50 million
- In 2013, USHL reported under \$67.4 million of net premium, with about half coming from Michigan – Licensed in 20 states, including Michigan, Ohio, Illinois and Indiana
- USHL was acquired through a new subsidiary, Ascension Care Management, which owns and operates businesses that are part of Ascension's population health management platform

Management and Board

Management, Ascension Care Management	
Anthony Tersigni	CEO
Anthony Speranzo	EVP, CFO
Joseph Impicicche	EVP, General Counsel

Geographic Foot Print

Expansion of Service Area Coverage



- USHL licensed states are shown in red
- Ascension benefits from USHL's significant overlap in geographic coverage with its hospital facilities, including Michigan, Illinois, Indiana, Ohio, Wisconsin and Texas

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Baylor / Scott & White Healthcare

Baylor Scott & White



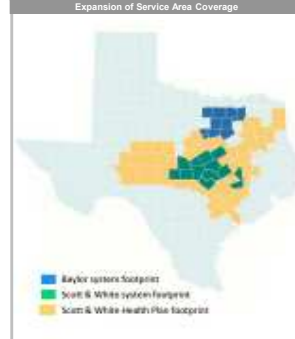
Transaction Highlights

- Created Texas's largest not-for-profit health system
 - \$9 billion total assets
 - \$5 billion combined FY14 revenues
 - 43 hospitals with a total of 5,400+ beds
 - 500+ patient care sites
 - 6,000+ affiliated physicians
 - 34,000+ employees
- Over 340,000 covered lives through combination of Scott & White Health Plan / Baylor Quality Alliance

Transaction Overview

- Baylor Health Care System and Scott & White Healthcare merged in October 2013 to form Baylor Scott & White
 - Merger prompted by healthcare reform and changes in delivery of care and physician alignment
 - Shift in emphasis from acute care to population health management
- Created Baylor Scott & White Quality Alliance as joint ACO
 - Part of integrated delivery network strategy moving forward

Geographic Foot Print



Management and Board

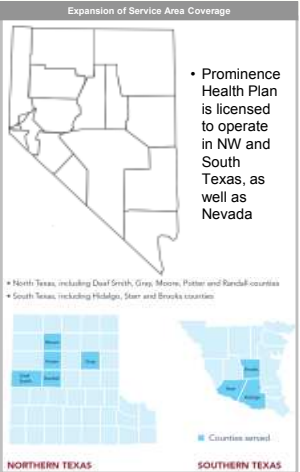
Management, Baylor Scott & White	
Joel Allison	CEO
Bob Pryor	President, COO, CMO
Steve Boyd	Chief Legal Officer



Universal Health Services / St. Mary's Health Plans

Prominence Health Plan

Geographic Foot Print



Transaction Highlights

- Prominence Health Plan's access includes 34 hospitals and over 3,500 providers in Nevada
 - Includes Medicare Advantage option in Nevada and Texas
- Products include:
 - Prominence HealthFirst (HMO and POS products in Nevada)
 - Prominence Health Insurance Company (PPO products in Nevada)
 - CDS Group Health (TPA services)
 - Nevada Preferred Healthcare Providers (PPO rental network to health plans, self-funded employers)

Transaction Overview

- Established in 1993 as St. Mary's Health Plans
- Acquired in 2014 by Universal Health Services and renamed Prominence Health Plans
- Acquisition enables UHS to deliver population-based care in northern Nevada
 - Part of strategic shift towards narrow networks
 - Close collaboration with local providers will enable UHS to deliver improved care management
- UHS plans to market Prominence closely with UHS physicians and facilities, expand PHP's products, services and geographic coverage

Management and Board

Management, Prominence Health Plan	
Markus Mueller	CEO
Dave Challis	VP, CFO
Doug Peters	Medical Director



Banner Health / University of Arizona Health Network

Banner University Medicine



Banner University Medicine

Transaction Overview

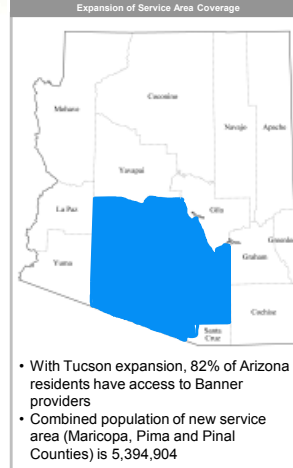
- Banner acquired UAHN for \$700 million in February 2015
- Expansion of Banner's statewide focus to include Tucson, Arizona's second-largest city
 - Establishment of a dedicated academic medical center in Phoenix (previously the nation's largest city without a university-affiliated hospital)
- Goals moving forward are:
 - Convert IT systems to Banner infrastructure
 - Expand relationships with commercial payers to Tucson market

Management and Board

Management, Banner Health	
Peter Fine	CEO
Dennis Dahlen	CFO
Kathy Bollinger	EVP, Academic Delivery

Notes
1. Population from 2013 U.S. Census Bureau data

Geographic Foot Print



Transaction Highlights

- Provided Banner with three health plans – a large Medicaid plan, a public exchange plan ending in 2015, and a small dual-eligibles plan
- Specific goals include:
 - Creating an academic brand in Phoenix
 - Building insurance infrastructure from UAHN health plans and statewide expansion
 - Using Banner's operating model to create significant synergies and efficiencies from scale and integration
 - Apply academic analytic rigor and research capabilities to Banner's clinical environment to accelerate improvement



Partners Healthcare / Neighborhood Health Plan



Transaction History

- NHP was founded in 1986
- Partners Healthcare acquired Neighborhood Health Plan (NHP) on October 1, 2012
- Terms of the acquisition included an agreement to jointly fund a 15-year, up to \$90 million grant program to invest in community health centers which serve NHP's population
- NHP has partnered with Partner's integrated Care Management Program (ICMP) clinical team for medical management of high-risk members

Neighborhood Health Plan

Membership Profile for the year ended September 30,

	2011	2012	2013	2014
Medicaid	149,468	157,367	161,517	233,216
Commonwealth Care	39,585	31,703	31,782	12,900
Commercial	54,054	62,391	71,163	84,196
Total	243,107	251,461	264,462	330,322

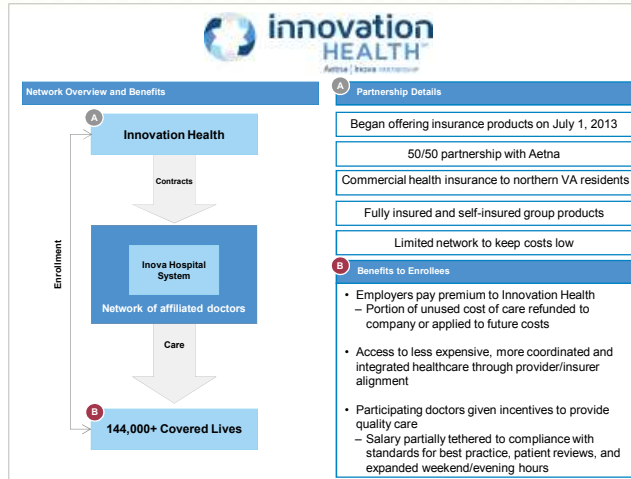
NHP Performance Impact

- In FY 2014, Partner's operating loss of \$22 million included a \$202 million loss at NHP, which had generated operating income of \$19 million in FY 2013
- Reasons cited by Partners for this result:
 - Over 70,000 new managed Medicaid members who generated a Medical Loss Ratio of 120%, far higher than anticipated
 - Need to post a \$92 million premium deficiency reserve for expected losses in FY 2015
- This loss was amongst the leading factors in a Moody's rating downgrade to Aa3 in January 2013
- In April 2015, Partners communicated its continued commitment to its ownership of NHP



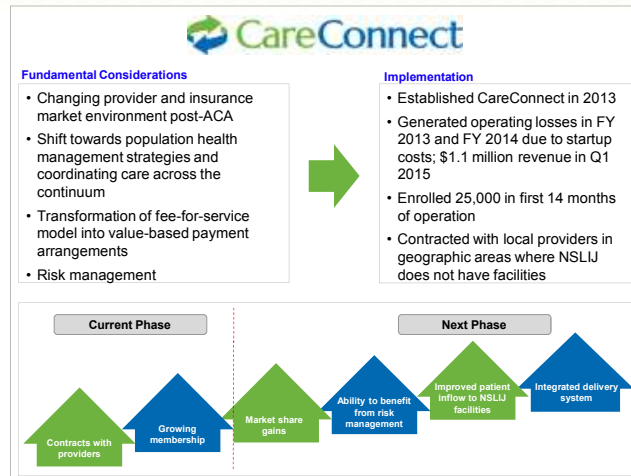
Narrow Network Venture

Aetna / Inova



Insurance Startup Venture

North Shore Long Island Jewish – CareConnect





NONPROFIT HOSPITAL PAYOR STRATEGIES

Trinity Health – Working with Payers to Create Insurance Product Offerings
 Capitation and Premium Revenue 5% of Total Revenue



NONPROFIT HOSPITAL PAYOR STRATEGIES

Health Plans Run by Not-for-Profit Providers

- Many organizations have health plans, a strategy that supports migration to risk management
- "Provider-sponsored health plans (PSHPs) are becoming increasingly prevalent in response to the changing dynamics and direction of the U.S. healthcare delivery system. The growth of PSHPs has, to date, helped providers diversify their business profiles while fostering development of the new skills needed under healthcare reform, including population health management."
 – S&P, June 2015

Organization	State/Head-quarters	Health Plan Name	Health Plan Members	FY 14 Premium / Capitation Revenue (\$MM)	FY 14 Total Revenues (\$MM)
Kaiser Permanente	CA	Kaiser Fdn Health Plan	10,100,000	\$38,587	\$56,433
UPMC	PA	UPMC Health Plan	2,320,000	\$4,813	\$11,416
HealthPartners	MN	Group Health Plan	1,500,000	\$2,711	\$5,505
Intermountain	UT	SelectHealth	720,000	\$1,829	\$5,573
Henry Ford Health	MI	Health Alliance Plan	700,000	\$2,272	\$4,712
Spectrum Health	MI	Priority Health	610,000	\$2,136	\$4,108
Group Health	WA	Group Health Coop	597,000	\$3,237	\$3,684
Providence Health	WA	Providence Health Plan	515,000	\$1,683	\$12,481
Gelsinger Health	PA	Gelsinger Health Plans	503,000	\$2,037	\$3,978
Presbyterian Healthcare	NM	Presbyterian Health Plans	450,000	\$1,672	\$2,653
Sentara	VA	Optima Health Plan	445,000	\$1,512	\$4,694
SSM Health	MO	Dean Health Plan	425,000	\$1,193	\$4,896
Boston Medical Center	MA	BMC Health Plan	335,000	\$1,706	\$2,829
Partners Healthcare	MA	Neighborhood Health Plan	330,000	\$1,622	\$10,906
Carle Foundation	IL	Health Alliance Plan	280,000	\$1,296	\$2,055
Marshfield Clinic	WI	Security Health Plan	230,000	\$1,013	\$1,987
Baylor Scott & White ⁽¹⁾	TX	Scott & White Health Plan	225,000	\$495	\$5,123
VCU Health System	VA	Virginia Premier	185,000	\$739	\$2,242
Baystate Health	MA	Health New England	182,000	\$590	\$1,827
St. Joseph Health	CA	Firstcare	175,000	\$1,131	\$5,632
Catholic Health Initiatives	CO	Prominence Health	104,000	\$171	\$13,889
UnityPoint	IA	Physicians Plus Insurance	85,000	\$232	\$3,705
Sharp Healthcare	CA	Sharp Health Plan	70,000	\$1,025	\$2,929
North Shore LJJ	NY	CareConnect	13,030	\$86	\$7,435

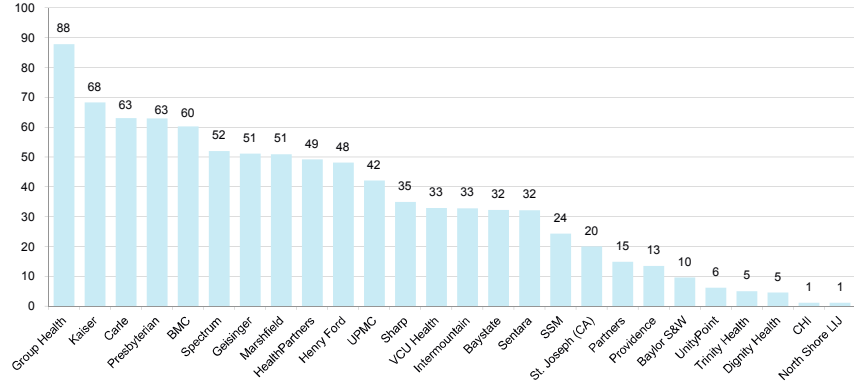
Notes
 1. Baylor Scott & White audited revenue data for the nine months ended June 30, 2014.
 2. All financial information for this analysis is derived from publicly available sources. Morgan Stanley does not certify to the accuracy or completeness of any information presented herein



Health System Premium/Capitation Revenue

Premium and Capitation Revenue as a % of Total Operating Revenue

(%)



Notes

1. All financial information for this analysis is derived from publicly available sources. Morgan Stanley does not certify to the accuracy or completeness of any information presented herein.
2. Data as of fiscal year 2014.
3. Ascension is not included in chart as acquisition of U.S. Health and Life Insurance Company did not take place until 2015.



Q&A Session



2016 Webinars

- **Planned Topics:**
 - Issuance of Taxable Bonds by Nonprofit Health Care Organizations: Special Considerations, Including Implications of New Rules for Mixed Use Facilities
 - Status of 501(r) Implementation and Possibility of Tax Reform
 - Overview of Healthcare Mergers and Acquisitions: Process and Diligence



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