

Atrius Health, Inc.

Analysis of the Reasonableness of
Assumptions and Prospective Financial
Schedules Used to Support Atrius Waltham

REPORT DATED AUGUST 13, 2024

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June 31, 2024

James Woolman
Vice President, Network Contracting and Financial Integration
Atrius Health
275 Grove Street
Newton, MA 02466

Dear Mr. Woolman:

Atrius Health (the "Applicant" or "Atrius") is filing an application for a Notice of Determination of Need ("Application") for the development of a freestanding ambulatory surgery center with six operating rooms (the "ASC", "Atrius Waltham" or the "Proposed Project") upon approval by the Massachusetts Department of Public Health. Veralon Partners Inc. ("Veralon") performed an analysis of the prospective financial schedules prepared by Atrius in connection with the Proposed Project in accordance with Massachusetts Department of Public Health Determination of Need ("MA DPH DoN") Application Instructions. At this time, Atrius intends to file a Determination of Need ("DoN") application with the Commonwealth of Massachusetts seeking approval for the Proposed Project.

This application includes a section regarding Financial Feasibility as referenced in the MA DPH DoN code section 100.210 specifically paragraph (A)(4) *Determination of Need Factors*. This Financial Feasibility component of the application provides "sufficient documentation of the availability of sufficient funds for capital and ongoing operating costs necessary to support the Proposed Project without negative impacts or consequences to the Applicant's Patient Panel." This report details our findings regarding the reasonableness of the assumptions used in preparation of the prospective financial schedules, and the feasibility of the Proposed Project based on the prospective financial schedules prepared by Atrius management ("Atrius Management") for the operation of the Proposed Project.

This report is to be used by Atrius in its DoN Application – Factor 4(a) and is not prepared for distribution for any other purpose.

I. EXECUTIVE SUMMARY

Atrius Management provided ten years (2026-2035), or the “Prospective Period”) of prospective financial schedules (the “Atrius Waltham Prospective Financial Schedules”) for Atrius Waltham under the assumption of a 100% ownership of the ASC by Atrius.

The scope of our analysis was limited to the following:

- An analysis of the Atrius Waltham Prospective Financial Schedules and the underlying assumptions used in their development; and
- Select financial ratio analysis of the Atrius Waltham Prospective Financial Schedules.

The Atrius Waltham Prospective Financial Schedules reflect positive earnings before interest, depreciation, and amortization (“EBIDA”) margins throughout the Prospective Period. Days cash on hand grows throughout the Prospective Period with a low cash point of 109 days after year 1 of operations. Based on our analysis of the Atrius Waltham Prospective Financial Schedules, we determined that the Proposed Project is reasonable, feasible and sustainable, and not likely to have a negative impact on the patient panel or result in a liquidation of assets of the Applicant.

The COVID-19 Pandemic has disrupted the operating environment for nearly all businesses, and in particular, those operating in the healthcare industry. The below considerations, among others, have acutely impacted healthcare providers:

- A likely permanent elevation of salary and wage expense for clinical and administrative staff, compounded by labor shortages;
- The availability of staff to meet the demands of budgeted/planned patient volumes; and
- Supply chain difficulties, contributing to difficulty in obtaining certain supplies, as well as elevated supply expenditures.

Atrius Management has represented that in the development of the Atrius Waltham Prospective Financial Schedules and associated underlying assumptions, they have taken into consideration the above factors and have considered the likely ongoing/future impact of the COVID-19 Pandemic.

II. RELEVANT BACKGROUND INFORMATION

Atrius is a multi-specialty physician organization operating throughout eastern Massachusetts. Atrius provides primary and specialty care to adults and pediatric patients as well as radiology, laboratory, and pharmacy services.

The ASC is a proposed freestanding ambulatory surgery center with six operating rooms, exclusively for Atrius patients, to be located in Waltham, Massachusetts. It is noted that at this time, Atrius does not currently operate any ambulatory surgery centers. Atrius will lease and renovate 22,000 gross square feet to open the Proposed Project where it will specialize in providing outpatient surgical services, performed by Atrius Health surgeons, including ear, nose and throat ("ENT"), general surgery, obstetrics and gynecology ("OB/GYN"), orthopedics, and podiatry (collectively the "Surgical Services"). Atrius is planning on contracting with Surgical Care Affiliates ("SCA"), a national leader in operational and management of ambulatory surgery centers to assist Atrius with providing core operational services for the ASC. Atrius physicians and clinical staff will provide patient care delivery.

III. SCOPE OF ANALYSIS

The scope of this report is limited to an analysis of the Atrius Waltham Prospective Financial Schedules prepared by Atrius Management and the supporting documentation to render an opinion as to the reasonableness of the assumptions used in the preparation and the feasibility of the Atrius Waltham Prospective Financial Schedules. Reasonableness is defined within the context of this report as supportable and proper, given the underlying information. Feasibility is defined as based on the assumptions used, and that the plan is not likely to result in a liquidation of the underlying assets or the need for reorganization.

This report is based upon prospective financial information provided to us by Atrius. Accordingly, we do not express an opinion or any other assurances on the underlying data presented or relied upon in this report. We do not provide assurance on the achievability of the results forecasted by Atrius because events and circumstances frequently do not occur as expected, and the achievement of the forecasted results are dependent on the actions, plans, and assumptions of Atrius. We reserve the right to update our analysis in the event that we are provided with additional information.

IV. SOURCES OF INFORMATION UTILIZED

In formulating our report, we reviewed the Atrius Waltham Prospective Financial Schedules and discussed corresponding assumptions with Management. The documents and information upon which we relied are identified below or are otherwise referenced in this report:

1. Atrius Waltham ten-year Prospective Financial Schedules, prepared as of May 20, 2024 and associated revenue and expenditure assumptions;
2. An overview of the Proposed Project and associated business case rationale provided by Atrius;
3. CPA Report Guidelines from the Determination of Need Program, dated March 2021;

4. Documentation provided by Atrius related to the source of capital funding for the Proposed Project;
5. Historical audited Atrius financial statements; and
6. Correspondence with Atrius Management.

V. REVIEW OF THE ATRIUS WALTHAM PROSPECTIVE FINANCIAL SCHEDULES

This section of our report summarizes our review of the reasonableness of the assumptions utilized in preparing the Atrius Waltham Prospective Financial Schedules as well as the feasibility of the Applicant.

The Key Metrics used in this report fall into three categories: liquidity, profitability, and solvency metrics. Liquidity ratios measure the quality and adequacy of assets to meet current obligations as they come due. Profitability ratios are used to assist in the evaluation of management performance. Solvency ratios are used to evaluate a company's ability to meet its liabilities.

I. Revenues

To determine the reasonableness of the prospective revenues, we reviewed the underlying assumptions provided by Atrius Management. Prospective net patient service revenues were assumed to grow approximately four percent annually (based on 2 percent annual growth in both case volume and revenue per case) after steady state volume levels are reached. Year one case volume is estimated to be 55 percent of stabilized year two case volume. Year two volumes assume an 83 percent utilization rate of six operating rooms.

In forecasting prospective revenues, Atrius Management has taken into consideration case type when developing volume and revenue per case estimates.

It is our opinion that the revenue growth of Atrius Waltham estimated by Management reflects a reasonable estimate of future revenues of the Applicant.

II. Expenses

We analyzed the expense categories included in the Atrius Waltham Prospective Financial Schedules for reasonableness. Our approach included a review of the total expenses for each expense category and expense growth assumptions in the Prospective Period for the Applicant. Below are the expense categories provided in the Atrius Waltham Prospective Financial Schedules along with relevant findings. Atrius has noted that physicians are not included in the Atrius Waltham Financial Schedules.

The operating expenses in the analysis include salaries and benefits, medical supplies, facility rent, management fees, other operating expenses, and depreciation and amortization.

- Salaries and benefits account for approximately 17 percent of total operating expenses and are assumed to grow at 3 percent annually. We note that physician expenses are not included in the Atrius Waltham Prospective Financial Schedules as these salaries will be paid by Atrius, and not the ASC.
- Medical supplies account for approximately 48 to 53 percent of total operating expenses throughout the Prospective Period and are assumed to grow at 4.5 percent annually. Medical Supplies were forecasted to be approximately 42 to 44 percent of net patient service revenue.
- Other expenditures were reviewed as follow:
 - Facility rent assumed to increase approximately 3 percent annually;
 - Management fees assumed to be approximately 1.2 to 1.3 percent of net patient service revenue;
 - Insurance assumed to increase 2 percent annually;
 - Bad debt expense assumed to be 2 percent of net patient service revenue;
 - Annual OM fees (back-office systems and processes, including: patient accounting system cost, clinical reporting, risk management/insurance, information technology, and related functions) assumed to increase 3 percent annually;
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 - RBO fee (revenue cycle, billing, collections and coding) expense assumed to be approximately 1.3 percent of net patient service revenue;
 - The SCA development fee is a one-time expense and represents planning and development costs associated with identifying a location, financial modeling of the center, and project management; and
 - Depreciation and amortization ranges from approximately \$1.7M to \$4.6M annually.

Based upon the foregoing, it is our opinion that the operating expenses forecasted by Atrius Waltham Management are based on reasonable assumptions and are feasible for the Applicant.

III. Capital Expenditures and Cash Flows

We reviewed documentation highlighting the availability of capital funds to support the Proposed Project and the future cash flows to determine whether sufficient funds would be available to sustain the operation of the Applicant.

Atrius has chosen not to include ongoing capital expenditures in the Atrius Waltham Financial Schedules as the facility will be newly constructed and not expected to necessitate significant capital investment in the short term. If capital expenditures were to be included in the Atrius Waltham Financial Schedules, set equal to depreciation, days cash on hand would decrease from 155 to 105 in year two of operations, and increase in subsequent years.

Accordingly, we determined that the prospective capital requirements and resulting impact on the cash flows are reasonable.

VI. FEASIBILITY

We analyzed the Atrius Waltham Prospective Financial Schedules and the resulting Key Metrics and determined that the Atrius Waltham Prospective Financial Schedules are based on reasonable assumptions. The Atrius Waltham Prospective Financial Schedules do not account for any anticipated changes in accounting standards. These standards, which may have a material impact on individual future years, are not anticipated to have a material impact on the feasibility of the Proposed Project.

The Applicant exhibits cash surpluses from operations (defined as EBIDA) in the Atrius Waltham Prospective Financial Schedules in each of the ten prospective years.

Based upon our review of the relevant documents, as referenced in Section IV, we determined the Atrius Waltham Prospective Financial Schedules exhibit a cumulative EBIDA surplus of approximately 21 percent of cumulative forecasted operating revenue for the Prospective Period. Based upon our review, the Atrius Waltham Prospective Financial Schedules are based upon reasonable and feasible assumptions. Accordingly, we determined that the Atrius Waltham Prospective Financial Schedules (associated with the Proposed Project) are a reasonable expectation and based on feasible and sustainable financial projections which are not likely to have a negative impact on the Atrius patient panel or result in a liquidation of assets of the Applicant.

VII. ASSUMPTIONS AND LIMITING CONDITIONS

Veralon relied upon the Atrius Waltham Prospective Financial Schedules provided by Atrius Management as the basis for Atrius Waltham's future financial performance and position shown in the report. The Atrius Waltham Prospective Financial Schedules provided by Atrius Waltham Management are assumed by Veralon to be Atrius Management's most accurate and complete forecast of Atrius Waltham's future financial performance and position and Veralon assumes no responsibility and provides no assurance of the accuracy or completeness of the Atrius Waltham Prospective Financial Schedules or the underlying data and assumptions used in these analyses.

Mr. James Woolman

August 13, 2024

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Some of the associated assumptions inevitably will not materialize, and unanticipated events and circumstances may occur; therefore, actual results achieved during the forecasted time period will vary from those described in our report, and the variations may be material.

Respectively submitted,



Daniel M. Grauman, MBA, CPA/ABV

Managing Director & CEO
Veralon Partners Inc.