CEO CFO

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With Four Specialty Surgical Hospitals in South Dakota and Oklahoma and One Ambulatory Surgery Center in California, Medical Facilities Corporation is Well Positioned for Growth Incorporating the Concept of "Hospitality" into Healthcare

Healthcare
Specialty Surgical Hospitals
(DR-TSX)

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Michael Salter, C.A., C.P.A.
Chief Financial Officer

BIO:
Prior to his involvement in the conception and formation of Medical Facilities Corporation in 2003, Mr. Salter acted as an accounting and financial consultant for a number of U.S. and Canadian based corporations, and more recently for Advisory Services, Inc., Scottsdale, Arizona. Mr. Salter was Corporate Controller from 1998 to 2001 for Olympus Hospitality Group, LLC, a hotel management company that had a portfolio of six destination resorts and a franchised hotel chain. From 1980 to 1995, Mr. Salter was employed by Alberta Energy Company Ltd., Calgary, Alberta, where he held a number of positions in accounting, finance and risk management. Mr. Salter is a Chartered Accountant and received his CPA certification in 1995.

Company Profile:
Medical Facilities Corporation (MCF) owns a majority interest in each of four specialty surgical hospitals (SSHs) located in South Dakota and Oklahoma, as well as a majority interest in one ambulatory surgery center (ASC) in California. The hospitals, which perform scheduled surgical, imaging and diagnostic procedures, have a combined total of 34 operating rooms and 101 overnight stay rooms. The ambulatory surgery center located in California, performs scheduled outpatient or same day scheduled surgical, imaging and diagnostic procedures.

Interview conducted by:
Lynn Fosse, Senior Editor

CEOCFO: Mr. Salter, would you tell us about the basic vision and focus at Medical Facilities Corp.?
Mr. Salter: Medical Facilities Corporation was established in 2004 when we conducted an initial public offering in Canada and listed on the Toronto Stock Exchange. The initiative for forming the company came from a group of physicians and surgeons who had up until that time owned three specialty surgical hospitals located in the major metropolitan areas of South Dakota. The physicians were interested in having outside ownership in the hospitals while retaining the balance of the ownership interest in the hospitals, and continuing to provide the active management of those hospitals.

CEOCFO: What guidance does Medical Facilities Corporation provide, or is it strictly the ownership?
Mr. Salter: It is primarily the ownership interest, so our executive is comprised of physicians representing the hospitals. I would have to say that the hospitals are decentralized operations, with MFC holding interests in those particular hospitals.

CEOCFO: Is it the same group of physicians involved at each hospital; is that the common thread?
Mr. Salter: No, they are different physicians at each one of the hospitals. The physicians that have an ownership interest in one do not normally have an interest in another one. There are a couple of exceptions to that, but they are small exceptions.

CEOCFO: Will you be adding any additional hospitals?
Mr. Salter: We acquired one additional hospital in 2005, that being Oklahoma Spine Hospital, a very similar type of facility to each one of the three that we initially started with in South Dakota. I would have to say that the initial thoughts at the time of formation of the company were that we would look to acquire additional 51% interest in other surgical specialty hospitals. I do not know how familiar you are with specialty surgical hospitals, but there are between two hundred and fifty to three hundred of them in the United States, most of them having significant physician ownership. Specialty hospitals have for a long time been the subject of restrictive legislation regarding physician ownership. Partly due to pressure from the large hospital lobbying groups, the Patient Protection and Affordable Care Act that was passed two years ago contained an outright restriction on physicians owning interests in hospitals if those hospitals take Medicare or Medicaid patients. While the Patient Protection and Affordable Care Act grandfathered all of the existing ones, including those owned by MFC, the landscape for acquisitions has changed.

CEOCFO: Do you see that as a strong point for your hospitals?

Mr. Salter: It is a mixed blessing. If you ask us if we agree with the prohibition on physician ownership, obviously the answer is an unequivocal no as we believe the ban is totally misguided and has been promoted by the big hospitals primarily for protection of their turf. Having said that, it does mean that existing specialty hospitals, including ours, have an exclusive license in their local market. Also, any non physician owner(s) of the existing grandfathered specialty hospitals who wants to divest of their interest would be possible acquisition targets for us given that the physician owners can't increase their ownership in such hospitals above what it was on enactment of the health reform act.

CEOCFO: Your website indicates "Our unique management philosophy focuses on efficiency and productivity of our facilities", how do you make that happen?

Mr. Salter: We do it in a number of ways. It would be fair to say that we view ourselves as a hospitality provider; meaning we incorporate the concept of "hospitality" into healthcare. If you look at the pictures of our facilities on our website and in our printed material you will readily see how we enhance the patient experience. Our doctors started out to build facilities that addressed everything they did not like about hospitals in general. Rather than drab, institutional colors we have nicely decorated and furnished rooms with wood paneling. Food service is four/five star restaurant quality. Wall or Murphy beds are installed in patient rooms, allowing a relative to stay overnight, which we think is a big plus for the patient. Turning to the physician side, the biggest advantages of our facilities is making life easier for the physicians, eliminating bureaucracy and enabling them to be more efficient (i.e. performing more surgeries in a given time period). For example, our turnaround times of our operating rooms is significantly lower than other hospitals. That allows us to focus on making the surgeon efficient, and efficiency is time, and time is money for them.

CEOCFO: What are you doing that is different, and how can you achieve such quick turn around of your operating rooms?

Mr. Salter: It is all about management. We do not have some of the restrictive work rules you might see in some hospitals. It is called all-hands-on-desk. One of the best analogies I can give you is if you go to an airport and fly one of the legacy carriers, then go to the same airport and fly Southwest Airlines. I have done both on occasion, and one thing I have seen on Southwest Airlines but not the others, is the captain or first officer helping the crew in the back put things tidy before the next group of passengers come on. Our philosophy and attitude is similar.

CEOCFO: Is it difficult to attract quality doctors to South Dakota?

If I look at our current investor base, which it is mainly Canadian, we see a lot of individuals seeking yield (i.e. cash return on their investment) We pay a dollar and ten cents and currently trade between $13 and $14, so obviously the yield is significantly better than you will get on your money down at the local bank, in a business we believe is quite sustainable and steady. I think those are the key points that investors should consider when looking at MFC. - Michael Salter, C.A., C.P.A.

Mr. Salter: In our facilities, I would say no. Many things determine where a doctor will ultimately locate his or her practice. Many doctors prefer to locate back in the communities where they grew up and I think this is more evident in communities similar to those we serve in South Dakota. The quality of life in these cities is really quite high, and they are great places to raise families. Furthermore, our facilities provide our doctors with the ability to provide superior treatment for their patients, perform surgeries in facilities that are state-of-the-art, and have a meaningful stake in hospital operation and ownership. They can do very well in these communities, so I think it all goes together and, as a result, we do not have a major problem in attracting physicians.

CEOCFO: How do you reach patients to attract them to your facility or do you work directly with physicians?

Mr. Salter: We reach out to both patients and physicians. It has historically been the way that the doctor will make the referral to a particular facility. Obviously, they will prefer to treat their patients at a facility where they enjoy working and where they can provide the best care for their patients. That still sustains today and will sustain into the future. However, we have seen a trend to patients taking greater interest in where they receive treatment, partly because of changes in healthcare. Patients are going to become discerning consumers; therefore, it is very important when you look at our hospitals that we score highly on surveys of patient care. If you look at our recent HCAHPS scores for instance, where all of our competition might be in the seventies, we are in the nineties on a scale out of one hundred, and I think that says something. You will start to see more and more where the patients will say 'doc I really like this place, and if you do not mind I would like to have my surgery there'.

CEOCFO: It sounds like your hospitals and doctors respect your patients!

Mr. Salter: I would say that is definitely true from our hospitals. I would not want to speak for our doctors, but I believe that they also feel the same way.

CEOCFO: How is business today?

Mr. Salter: If you look at our financial performance over the last eight years that we have been a public company, I think you would have to agree that we have done very well in terms of increasing patient numbers, and therefore revenues over the course of the last eight years.

We did see some softening in revenue over the last couple of years as the percentage of Medicare volume increased. Simply put, the recession caused some private insured patients to stay home rather than incur deductibles and copays during recessionary times. We do believe that our operations were less affected than some of our peers primarily because we operate in states such as South Dakota and Oklahoma, which have had and still have unemployment rates that are basically half of the national average. Also, foreclosure rates in these two states remained very low compared to national averages.

CEOCFO: Do you have a monthly distribution?
Mr. Salter: We do. We were structured to be very similar to the Canadian Income Trusts that were quite prevalent in 2000-2004. Our initial capital structure consisted of a unit that was comprised of two parts, one being a common share, and the other part being a piece of a subordinated note payable. The monthly payment to unit holders consisted of a dividend on the common share plus interest on the subordinated note. This changed in 2011 mid-year when the holders of our subordinated notes agreed to convert their notes into common shares. After this conversion a person who held one unit now owned one new common share. Where we used to pay a distribution of C$1.10 per unit per year we now pay C$1.10 per common share.

CEOCFO: What is ahead for Medical Facilities Corp.?
Mr. Salter: I think more of the same is ahead. Stability of operations, same hospital growth and sustainability of cash flow. Prior to the restriction on physician owned hospitals contained in the health reform act, we undertook expansions at all four of our surgical hospitals. We have been successful in increasing volume and we certainly have the capacity to continue to do just that. The one other area that we are interested in is ambulatory surgery centers. You will see us look for acquisitions in both the specialty hospital and ambulatory surgery center market that would be accretive and fit with our operating philosophy. I think that is where the future for MFC Lies.

CEOCFO: Why should investors pay attention to Medical Facilities Corp. today?
Mr. Salter: If I look at our current investor base, which it is mainly Canadian, we see a lot of individuals seeking yield (i.e. cash return on their investment) We pay a dollar and ten cents and currently trade between $13 and $14, so obviously the yield is significantly better than you will get on your money down at the local bank, in a business we believe is quite sustainable and steady. I think those are the key points that investors should consider when looking at MFC.

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