RCB Equities #1 – DCHS

Initial Business Plan Considerations

Background on Investment Group: RCB Equities #1 ("RCB") is a boutique financial advisory firm with a strong capital lending arm. RCB's principals and its main investment partner are the Ryzman Family of Los Angeles. The Ryzman Family started a small import-export business and turned it into American International Industries, a global leader in the beauty and skin care products. RCB has also partnered on capital projects Union Bank, Bank Leumi, and Deutsche Bank.

Most notably, RCB and their management team led Downey Regional Medical Center out of bankruptcy through creative financing and bottom line driven healthcare management decisions.

RCB's Assessment of Transaction Opportunity: RCB's mission is aligned with the mission of the Daughters of Charity: to provide compassionate, comprehensive, and excellent health care to all members of the community with integrity, clarity, and honesty. By creating a sustainable financial platform, RCB will seek to preserve the historic mission the Daughters of Charity worked so hard to create.

RCB has both the financial expertise as well as the proven healthcare management skills needed to take the Daughters of Charity Health System ("DCHS") to financial sustainability, and will achieve a healthy EBIDA within a three year time period. In addition, RCB has the capacity to undertake capital lending and has associated with a non-profit hospital operator, so that RCB can ensure that the mission of the Daughters of Charity continues for many years to come.

RCB sees three challenges to returning DCHS to sustainable EBIDA:

1. To eliminate the existing $9 million per month cash burn;
2. To execute a substantial business development program to expand the current revenue base; and
3. To provide the funding necessary to keep the system functioning during the implementation of the projects needed to meet the first two challenges.

Balance Sheet Restructuring: For RCB to make an intelligent investment into the DCHS system an improvement is needed in liability exposure, security, and collateral quality of DCHS's balance sheet. Areas identified by RCB include the unfunded pension obligations and the seismic liabilities. RCB continues to look at other areas, including the captive insurance company, capitation sharing obligations and cash performance versus accruals, among others. Each area and potential area for improvement represents a contingent liability that can amount to hundreds of millions of dollars. RCB will seek to systematically address each of these areas to provide certainty to the greatest extent practicable.

- Pension Underfunding: RCB will engage in discussions with organized labor to explore alternative financing for the defined benefit programs.
- Seismic: RCB will carefully review current construction plans and planned financing for the construction. Alternative funding (new bonds, local county support, federal grants, etc.) will be revisited to ensure that the required debt service and capital costs fit within the projected EBIDA.

Upon fashioning as much certainty as can be gained in currently contingent areas, RCB will fine tune its debt structure design for DCHS, and lend needed funding, or restructure the existing indebtedness, or both if required. The goal will be to fix a sum certain for the appropriate total capital for DCHS, and make sure that the resulting debt service can be met by the improved EBIDA.

Meeting the Challenges:

Challenge #1: Eliminating the existing $9MM per month cash burn

RCB will do this in two distinct ways: 1. Cost Control 2. Revenue Expansion

Cost Control: At first glance the mission delivering entities appear well run; however, global OSHPD data do suggest areas for potential improvement. For instance, the length of stay for Medicare patients at O'Connor Hospital is about 1.5 days too long on both ends of the bi-modal curve (between traditional and managed care Medicare). The non-labor unit costs at St. Vincent Medical Center, especially for purchased services, is high (although unit costs overall should improve just through introducing significant ER volumes). These two issues alone could enhance EBIDA by $30 million annually. RCB realizes that this will take a "roll up the sleeves" approach, and once on the ground RCB will be able to identify other areas of cost control. From detailed operational modeling of each hospital, RCB has seen that small improvements in unit costs and in unit revenues increase overall EBIDA substantially

RCB will look carefully into the current governance structure to find cost control opportunities. Alternative management structures favoring greater decentralization of administrative functioning might be viable. RCB will evaluate all operations to find cost control opportunities, but without sacrificing any of the ideals of service to the poor that the Daughters of Charity brought with them to the West Coast in 1852.

Revenue Expansion: To achieve immediate revenue expansion, RCB's management team will bring to bear its experience in payor negotations (including off-schedule renegotiations), and will open negotiating with all payors as soon as the transaction is completed. RCB will also make sure that the rollout of the St. Vincent Medical Center's Emergency Room initiative is implemented effectively.

Challenge # 2 – Execute a substantial business development program to expand the current revenue base.

Like virtually all other hospitals in the country, DCHS hospitals suffer from BEHS – Big Empty Hospital Syndrome. The unfortunate reality is that no ready cure exists for BEHS; there is no silver bullet to increase hospital census. In fact, many of the cost savings projects will likely target a lower length of stay, and, all else being equal; will result in lower hospital census.

Operationally, the use of the emergency room and the protocols for Observation Service can have a dramatic impact on hospital inpatient census and financial performance. In conjunction with the physicians at each facility, standards for Observation and emergency room practices will need to be studied and adopted by the elected medical staff and medical executive committees. Improving these areas is an important precatory step for further business development.

The business development program proper will rely on:

1. Massive rebranding campaign
2. Physician recruitment
3. Expansion of out of hospital patient management and care coordination
4. Outpatient service line marketing
5. Expanded partnering with key payors.

Rebranding: RCB will undertake a system-wide rebranding. Once a naming convention is settled on, it will pursue a multi-outlet media campaign to raise awareness of the new names, and raise awareness that these are the same quality DCHS facilities under new management, committed to the same compassionate care for all patients in the community. This rebranding will also highlight special services, such as the new emergency room at St. Vincent Medical Center, the world-class hearing clinic at St. Vincent Medical Center, and similar recognized programs and services at each of the other hospitals.

Physician Recruitment: A concerted physician recruiting effort will be undertaken, as well as efforts to limit 'patient leakage' from medical practices that already utilize DCHS facilities. In the case of St. Vincent Medical center, the recruitment campaign will reach out to physicians disenfranchised from other significant regional centers which have focused on narrowing their physician networks. Expansion of the Foundation and its membership will be pursued at all facilities. Expansion of teaching programs will also be examined, especially as a feeder for new physicians into the communities served by DCHS hospitals.

Expanded patient care coordination: In conjunction with physician recruitment, out-of-hospital patient management and coordination of care services will be expanded, both within system assets and with third parties such as extended care facilities. The expansion of the patient management and population health services will be marketed to physicians as a way of attracting doctors who are compatible with the new care models under healthcare reform.

Outpatient Services: The outpatient facilities and service lines will be highlighted for consumers. Numerous marketing programs will be implemented to try and achieve as much consumer engagement with the facilities as possible.

Payor Projects: RCB will seek to work with interested payors whenever it is possible to approach the market in attractive programs for employers; narrow networks, expanded capitation, or alternative products that can offer affordable options for employers while ensuring DCHS hospitals capture the patients in those programs.

Challenge #3 – To provide the funding necessary to keep the system functioning during the implementation of the first two challenges.

The final challenge of providing a funding runway is dependent upon the capital structure that is decided upon at the outset of RCB's involvement with the DCHS hospitals and the assessment of the specific projects to improve EBIDA and the time to implement them. RCB stands prepared to lend the funds needed to accomplish the challenges and meet the goals. RCB's preliminary view is that $90 million will be needed to meet these needs.

In conclusion, the true value of RCB's offer to acquire the DCHS assets through a member substitution lies in (1) the preservation of the essential non-profit mission established by the Daughters of Charity, and (2) the unmatched financial abilities, the seasoned managerial expertise in healthcare, and the experience in the financial markets of RCB.