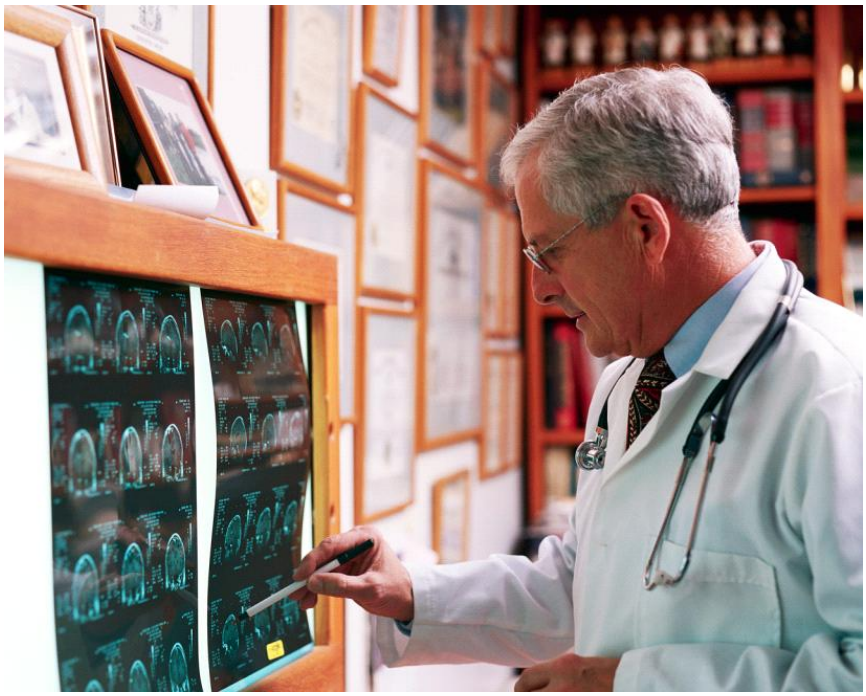
OUR RURAL HOSPITAL RADIOLOGY OUTSOURCING PROPOSAL



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Envisioning the Future

The outsourcing of the radiology department will improve the quality, service and financial performance of our institution by utilizing a focused management team driven by incentives and quality performance indicators.

TABLE OF CONTENTS

LIST OF FIGURES

LIST OF TABLES

Our Rural Hospital Radiology Outsourcing Proposal

ENVISIONING THE FUTURE

INTRODUCTION

Today, Our Rural Hospital (ORH) houses 250 beds but routinely operates about 150 beds. We serve a population of 50,000. This paper addresses the $1.5m deficit in fiscal year 2007 and forecast $2.5m deficit in 2008. This paper is a proposal to reduce the deficit in 2009 and eliminate it by 2010.

With all due respect, we would like the board to consider the outsourcing of the radiology department. The outsourcing of the radiology department will improve quality, service and financial performance of our institution by utilizing a focused management team driven by incentives and quality performance indicators. Our plan is to maximize the use of service level agreements with baseline targets to set goals in key quality and service indicators such as patient and physician satisfaction scores, report turnaround time, wait times and imaging station uptime.

The outsourcing will allow the department to grow. This will lead to better market penetration and efficiency in both materials and staff time. Through process improvement, our patients will get their results faster. More procedures will be executed which in turn, will generate more revenue. As the community appreciates the higher quality services and efficiencies, more patients will come to our institution than the one in the adjacent town.

The outsourcing agreement will have a positive impact on our mission:

> **"We strive to bring the highest quality services and act as a resource to our rural community."**

Better service and efficiencies will allow our community to receive higher quality care and a greater depth of services within the radiology department.

It will also positively impact our vision:

"We will redesign our care processes to provide healthcare that is safe, compassionate and high quality. In alignment with the needs of our community, we will grow our ambulatory services and community based services for the elderly."

Our new radiology department will accommodate service to growing numbers of the elderly which will translate to increased Medicare revenue streams.

Our plan will highlight the following areas:

- Demand
- Human resources
- Output and productivity
- Quality outcomes
- Process quality
- Change Management
- Costs

Our current plan is to outsource the radiology department to X-Rays 'r Us. Our current staff will be encouraged to work for the company. The company will be onsite and lease our space. They will provide all equipment and staff necessary to run an efficient and high quality department. The onsite radiology service line will be managed by a Director who reports directly to the Board.

DEMAND

Current State

1. Equipment
    a. Poor quality
    b. Poor reliability
    c. Poor throughput
    d. Use film based chemicals—expensive supplies and hazardous chemical
2. Evolving patients
    a. Obesity
    b. Aging
3. New technologies
    a. Digital radiology
    b. PACS system
    c. Voice recognition

ORH (Our Rural Hospital) is not currently serving our patients with the scope and quality of radiographic services which are needed to make us the preferred healthcare provider in the region. For this reason, our image in the community is diminished and some of our business is going elsewhere for care. The situation at

present is not irreversible, but major changes are necessary to stop the trend. We must deal with the issue despite the financial losses we have been experiencing.

Our current equipment although functional and capable of meeting the needs of the health system has not been maintained consistently with needed part replacements and routine maintenance services. As you have seen from the financials previously discussed at the board level, the equipment is fully depreciated. One major result of using this equipment is an unreliable and poor quality and consistency of service. Worn out equipment/tubes do not produce consistency of exposure between films and thus frequent retakes are necessary by our technologists in order to produce diagnostic quality images. This results in numerous retakes which are costly to the system (increased supply utilization and decreased throughput) and results in additional exposure to ionizing radiation for our patients which is a known health risk (albeit small for most patients). Frequent equipment failure leads to delayed imaging or cancelled imaging. For the inpatients, this may lead to additional length of stay. For outpatients, this is just one reason that we lose business to free standing image centers.

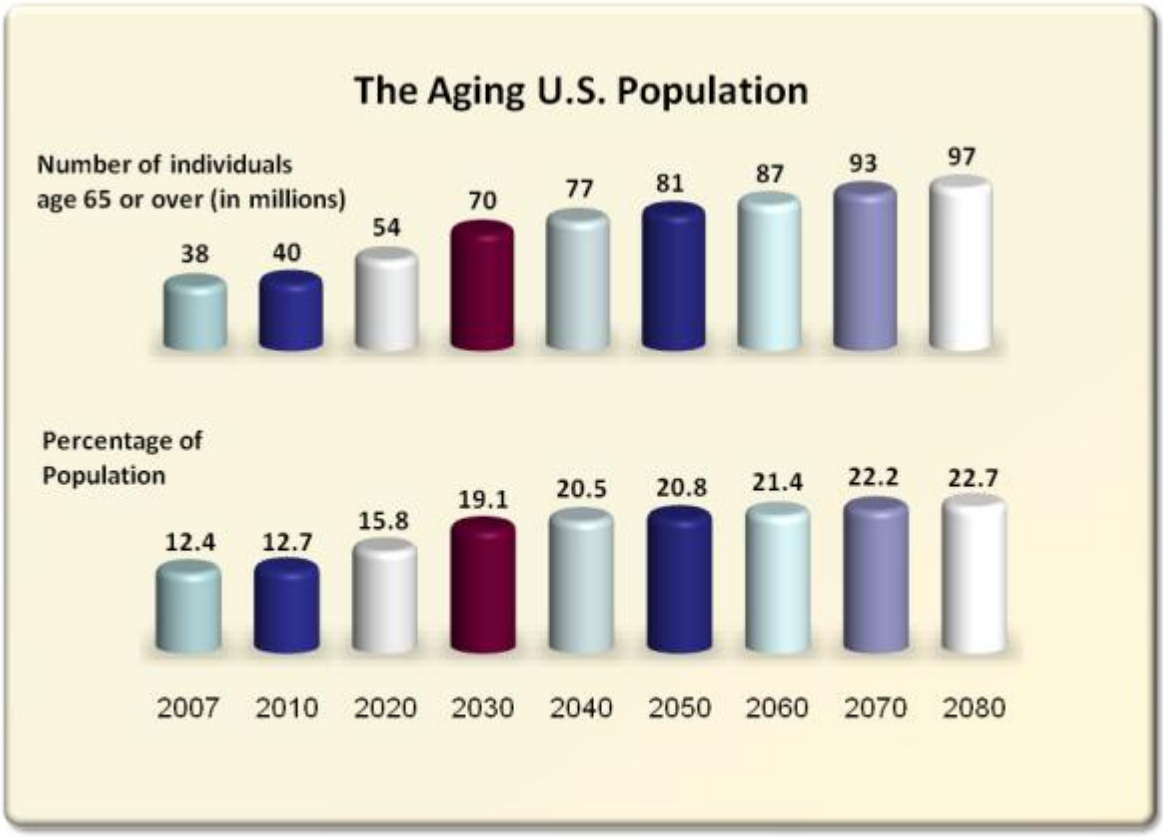
Our current department was designed in an era when radiology volumes were significantly less. By redesigning the department, we can have staging areas to prepare patients for their procedures and to dress afterward. By doing this, the utilization of the equipment and our radiology technologists will become far more efficient—doing more with less equipment and technologist time. Only by designing for efficiency can we achieve the improved service and costs which will make the outsourcing agreement economically feasible for ORH and our partner.

As we envision our new department we must plan for a variety of new pressures and opportunities:

a) Nationally, imaging services are growing at 20% annually. Without intervention or rationing, this trend is expected to continue.[1] At the same time, ORH has experienced a contraction of radiology services. This represents a tremendous unmet need and opportunity to expand our services to our patients and our medical staff.

[1] Health Care Financing Administration. *1999 HCFA statistics*. Washington, DC: US Government Printing Office; April 2000. HCFA publication 03421

b) Our patients are aging. As a rural community we are disproportionately affected by the flight of the young to metropolitan areas. This effect only accentuates the aging factor.



Source: U.S. Social Security Administration
2007 OASDI Trustees Report (April 2007), Table V.A.2

FIGURE 1 - AGING U.S. POPULATION

We must plan with this shifting demographic in mind. Aging patients use greater healthcare services (including radiology) and have greater difficulty with access issues. This is a factor which we must bear in mind as we design our radiology department for care for inpatients and outpatients.

c) Obesity is epidemic in the United States. Obesity rates have nearly doubled in the past ten years. Obese patients now account for over 15% of our patients. Obese patients require more medical care due to their co-morbidities. Thus, this is a population to be served. Overweight patients require equipment such as scanners of larger size along with imaging tables that accommodate their increased weight. As important as the radiology equipment, we must plan assist devices for hospital personnel to transport these patients. Without these, the on the job injury rate for hospital workers is high and costly.

d) Film based radiology utilizes hazardous chemical which contribute to indoor air contamination. Through digital radiology we will avoid the dangers of these chemicals. Digital radiology will eliminate the storage needs for the physical x-rays, improve access, decrease (or eliminate) lost studies.

e) Beyond digital radiology, we must implement a Picture Archiving and Communication System (PACS). This system is complementary to the digital radiology system, allowing the images to remain digital and stored in electronic form. PACS allow significant time savings for the technologist by eliminating the development / film processing in traditional film process, and the laser printing of images from digital image systems. Instead, the technologist does a brief quality control of the image and sends it to the radiologist for interpretation. The improved workflow is obvious. A small increase in volume will pay for the cost of the PACS within a few years. It is through these efficiencies that an outsourcing contract can be mutually beneficial to ORH and the outsource contractor.
Beyond the economic benefits of the PACS, the ability to provide remote access to the images creates a new opportunity to "bond" with referring MDs. Essential in the ability to view the images will also be the ability to view the interpretation/report from the same application.

f) New imaging modalities are arriving with a speed which we cannot keep up with. Two bear watching: Dual Source CT scanning and 3T MRI units.
    a. The Dual Source Computed Tomography (CT) scan allows acquisition of images in 83 msec. per slice as opposed to the 64-slice CT which requires 160 msec. This difference is crucial when trying to image the beating heart and perform a CT coronary angiogram. Rapid evaluation of the heart and lungs is vital for the Emergency Room MD who is charged with distinguishing pain from a heart attack from the myriad of other causes of chest pain. Again, such a scanner in our facility would improve the care delivered, efficiency of care and improve the public perception of our hospital to deliver state of the art care.
    b. 3T Magnetic Resonance Imaging (MRI)'s are actually installed in many hospitals across the nation. The difference between the 3T MRI and older generations of MRI scanners is the size of the magnet which translates to improved images with shorter acquisition times. In this era of declining reimbursement, it is likely that the usual life cycle of an MRI may be extended from the six to eight years to ten or more years. The relative small amount of money to be saved by purchasing the "mainstream" 1.5T MRI over the 3T MRI will look like a pittance when we decide a few years from now that the "community standard" dictates the 3T machine. By careful choice of our outsourcer/partner and careful structuring of this venture we should be able to optimize available technologies to serve our community.

g) With state of the art equipment, improved result delivery systems and a user friendly department, we will recapture much of the outpatient business which has been lost to other care providers. Doctors like to refer to centers which are easy for the patient to get in and out and which deliver the report/needed information with rapid turn-around. Our status as a hospital affords us better financial standing (better fee schedule over free standing image centers). This advantage should be used to help further our technologic advantage by keeping our equipment state of the art.

Some interesting facts related to Radiology are:

- The annual spending on diagnostic imaging in the United States is $100 billion, making imaging the second-largest and the fastest-growing item for healthcare payors.
- An estimated $30 billion of this spending is wasted due to inappropriate utilization of imaging or duplication of studies.
- Duplicate imaging studies account for 10 percent to 20 percent of every dollar spent on radiology services.
- CMS estimates that there will be 60.6 million individuals older than age 65 by the year 2025, a 74 percent increase from 1998.

- The number of musculoskeletal MRI studies performed on Medicare patients increased 134 percent from 1999 to 2005; at the same time, the number of conventional skeletal radiographs performed on these patients decreased by 4 percent[2]

CHANGE MANAGEMENT PLAN

To successfully manage the outsourcing initiative, we should collaborate with the commercial imaging diagnostics company to create an effective change management plan. The change management plan should include, at a minimum, the following components:

1. Vision
2. Communication strategy
3. Employee Transition strategy
4. Organization Design strategy
5. Transition and Change Acceptance

Vision

The hospital should establish a clear vision for the outsourcing initiative and its rationale. All stakeholders should know why the project was initiated, including the goals, scope, and the sponsors. We need to have an effective communication strategy to convey the vision to all stakeholder groups and to ensure their understanding of the initiative.

Communication Strategy

We should establish a broad-based communications strategy for the outsourcing initiative. We should define and communicate the ramifications of the initiative. This process will generate awareness and build strong relationships among the people needed to champion the project. The communication strategy should include the following
components:

- First, we should organize a series of seminars to educate employees and other stakeholders regarding the reasons for the outsourcing initiative. It is important that we explain why the initiative is critical for the hospital's survival.
- Second, we should use face-to-face communications to handle sensitive aspects of the initiative. We should also meet face-to-face with the commercial imaging company on a regular basis to get mindshare, clarity, and commitment on both sides.
- Third, it is important that we communicate objectively the impact on jobs: who may be losing their jobs, what other options are available to those affected by the initiative, and what the transition process will entail. This is very important for the sanity of the initiative.
- Finally, we should institute an open communication policy to stop the detrimental effect of speculations and rumors. It is the duty of the executive to be responsible and cordial to the employees who will be negatively impacted by the initiative.

Employee Transition Strategy

[2] Nunley, Ryan (2008 July). Newsletter Volume 2, No. 7. Retrieved August 4, 2008, from American Academy of Orthopedic Surgeons Newsletter Web site: http://www.aaos.org/news/bulletin/jul07/reimbursement1.asp

We should have an effective staff transition plan that includes appropriate redeployment, severance, and retention policies for those impacted negatively by the initiative. The plan should also address the most likely change compensation and incentive plans during the interim transition period. We should negotiate with the commercial imaging company to absorb some, if not all, of the employees in the imaging department.

Organization Design strategy

We should design a strategy to govern the new organization and the retained organization whose positions are affected by the change in roles and responsibilities due to outsourcing. Our change management process needs to be linked to contracts and should have a well-defined set of roles and responsibilities. The executives of the hospital should work with the imaging company to set measurable goals that can be translated into business value. This should be accompanied with service level agreements (SLAs) and key performance indicators (KPIs) to maintain flexibility and to avoid vendor complacency.

A level management position, "outsourcing relationship manager", should be established to manage the outsourcing relationship between the hospital and the commercial imaging company. This manager will be responsible for the outsourcing progress, productivity tracking, SLAs and so on. As part of the contract, the commercial imaging company will be required to have physician-driven management structure of radiologists who maintain close relationships in the medical community. The company should be American College of Radiology (ACR) accredited, and should play an active role in maintaining Joint Commission on the Accreditation of Healthcare Organizations[3] (JCAHO) standards. The commercial imaging company's staff should work in concert with the "outsourcing manager" to review and answer JCAHO questions regarding imaging diagnostics at the hospital.

Transition and Change Acceptance

The transition plan should include transition of both people and processes. It should also include a timeline and milestones. We should plan the timeline with enough time lags as outsourcing projects typically require time for establishing the relationship, adjusting to different business cultures, introducing details of the collaboration. We should also plan resource skills, training requirements, and cover all the elements needed to effectively minimize the inevitable resistance risks to outsourcing.

[3] http://www.jointcommission.org/

Project Timeline

Month	1	2	3	4	5	6	7	8	9	10	11	12
Strategic Planning												
Market Opportunity												
Physician Interviews												
Financial Opportunity												
Project Management												
Project Financing												
Equipment Selection												
Facility Design & Construction												
Used Equipment Sales												
Operations												
Scheduling Improvements												
Staffing plan												
Training												
Radiologist Process												
Report Delivery												
Management Services Contracts												
IT/PACS Planning												
Regulatory/Legal												
Ownership Structure												
JCAHO												
ACR Accreditation												

TABLE 1 – PROJECT TIMELINE

HUMAN RESOURCES

The transfer of Full Time Equivalents (FTEs) to an outsourcing company requires thoughtful consideration and advanced planning. In order for Our Rural Hospital to remain viable, the transfer of FTEs is a necessary step in the outsourcing of our Imaging Department. This undertaking requires collaboration between the Risk Management and Human Resources departments. Our goal is to ensure that we address the needs of the displaced or departing employees and the organization. Although the transfer of this workforce does not involve 100 employees, our organization is covered under the Worker Adjustment Retraining Notification Act

(WARN)[4], which requires us to notify the affected employees or their representatives (i.e., labor union) 60 days in advance of the planned event.

Based on the above information, the Image Review Group (IRG) proposes to outsource all positions that are a part of the Radiology Department, including the Director and Supervisory positions. Nursing care in the Radiology Department is delivered and governed by the nursing department and is not part of this outsourcing agreement.

The IRG is also mindful of the fact that it is in the organization's best interest to offer time-limited outplacement services as it helps deter legal actions by providing incentives to sign waivers of rights. To reduce the impact on those employees[5] who choose not to be outsourced, the IRG is recommending that outplacement services should be provided and should include:

- Resume writing
- Interview skills development
- Job search
- Group workshops
- One-on-one coaching

Health plan continuation for employees for up to 3 years at group rates will also be offered in compliance with the Consolidated Omnibus Budget Reconciliation Act of 1985[6].

Although our organization will recommend that the outsource group hire the displaced employees, the final decision is theirs to make. As previously mentioned, we will ensure that the deleterious effect of workforce reduction on the departing employees and the organization is minimized. Assisting the employees in re-establishing themselves in the job market is important. Employees who are reabsorbed in the organization will be afforded adequate training and education in order to lessen workflow disruption.

OUTPUT AND PRODUCTIVITY

Productivity of the Radiology Department will be increased as a result of new technology and workflow changes that the Radiology Outsource Company implements. This will lead to shorter turnaround time for interpretation of Diagnostic Images. This will lead to improvements in Patient Care.

The Radiology Outsourcing Company has expertise in managing Radiology Departments in a variety of settings. Because of their size, they have the ability to achieve economies of scale in the use of equipment that we could not. Because of their size, they are able to negotiate volume discount pricing for equipment, material and services that we could not.

Additionally, the Radiology Outsource Vendor will be able to offer services that we were unable to afford to deliver using the in-house model. This will reduce the number of patients that we need to refer elsewhere for procedures that we could not perform. This will result in improved patient satisfaction, improvements in patient care and additional revenue for the hospital.

[4] http://www.dol.gov/compliance/laws/comp-warn.htm
[5] Beigbeder, S. (2000, May). Risk Management:Easing workforce reduction. Retrieved July 28, 2008, from BNET.com: http://findarticles.com/p/articles/mi_qa5332/is_200005/ai_n21455295
[6] Labor, U. D. (2008, August 06). Health Plans and Benefits: Continuation of Health Coverage. Retrieved July 28, 2008, from U.S. Department of Labor: http://www.dol.gov/dol/topic/health-plans/cobra.htm

In the event that an on-site radiologist is unable to review a diagnostic image and create a report of their findings, the Radiology Outsourcing Company will use teleradiology techniques to have that work performed by a remote radiologist. State law requires that this interpretation is signed by a Radiologist that is licensed in the state. The Radiology Outsourcing Company will ensure that this is done legally and correctly.

Our Rural Hospital currently has a Patient Management System and a Billing System that are not interfaced. Data is "double entered" into each system. The plan is to develop two interfaces (see Figure 2 - New System Interfaces):

1. A Patient Demographic Interface (Admit, Discharge Transfer - ADT) from the Hospital's Patient Administration system to the Radiology Outsource Company's Patient Management System. This interface will include patient demographic information and insurance carrier information that are found in a typical Health Level Seven (HL7) ADT Message.
2. Procedure information from the Radiology Outsource System to the Hospital's Billing System. Information that is typically found in an HL7 Detailed Financial Transaction (DFT) message will cross.

These interfaces will cost $10,000 each to develop. They will improve the efficiency of the billing process and reduce the time between when a procedure is performed and when the hospital is reimbursed for that procedure.

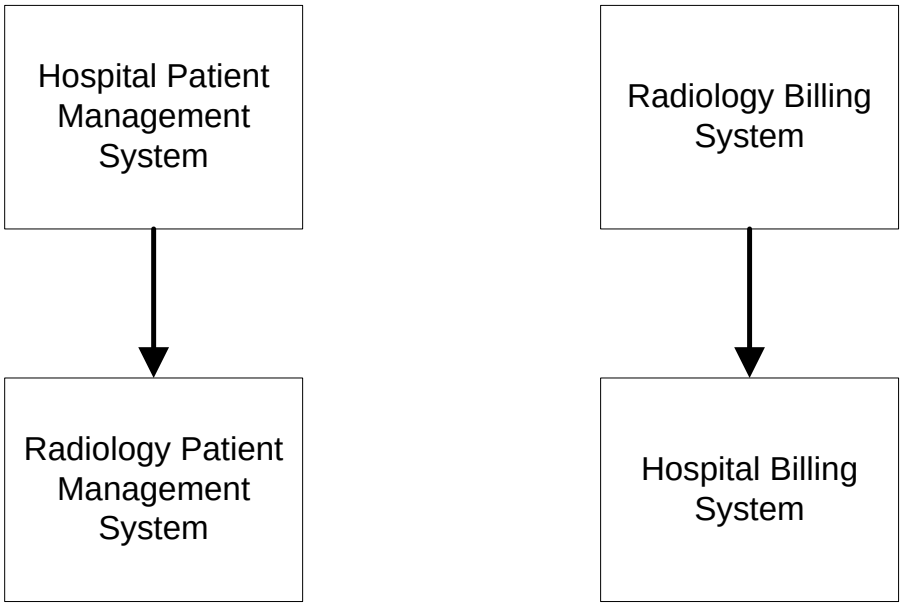


FIGURE 2 - NEW SYSTEM INTERFACES

QUALITY OUTCOMES AND PATIENT SATISFACTION

Providing quality outcomes for both the patients and the physicians involved, which includes the radiologist as well as referring physicians is critical to the success of the proposed venture. The main areas for consideration include efficiencies such as workflow processes, turnaround times, patient waiting times, quality and dependability of services and products, as well as work/life balance issues for the medical staff. Confidence in the integrity of the final product, ease of use, as well as peace of mind for patients and physicians are key to a meeting our goals of increased productivity and patient and physician satisfaction. The issues of data

integrity, Health Insurance Portability and Accountability Act (HIPAA)[7] compliance and accreditation are also areas of concern in providing a state of the art program that is efficient and cost effective.

Workflow Improvements

Through our outsourcing capabilities, we will provide a system to help our radiology department function more efficiently, allowing more time to determine ways to grow our business through streamlining work processes. This system offers the ability to view real time workflow and dictated reports online. The proposed system allows the flexibility to work from multiple locations, including the ability to work from home which allows physicians the ability to consider work/life balance issues.

Much of the administrative burden will be lifted from the radiology department, due to administrative assistance from the vendor, allowing them to concentrate on interpretation. This is possible through the ability to work with one work list backed by a quality control system at the outsourcer. The vendor is also available for overflow when case volume becomes unusually high. This allows the ability to provide consistent services of quality on an ongoing basis without disruption to the patient. The vendor can accept the data as fast as it can be sent due to the quality of the main servers, so quick turnaround times for reports are estimated at 21minutes for stat results to 30 minutes for regular procedures once the image is sent. The service is provided 24/7/365, eliminating down time and providing efficient service during emergency situations such as cardiac event evaluations, which is an area of growth for our facility. Customization and enhancements are available as needed to keep our system efficient and maintain optimal workflows. The system is user friendly and offers web based case management capabilities which also increase the efficiency of adding this type of system. Web access makes it possible to monitor the progress of orders. The vendor also provides various types of consulting such as PACS consultation, teleradiology and remote reading consultation, along with workflow, billing, and credentialing consultation which can provide valuable tools and information with which to grow our business and attract local patients who desire quality as well as efficient care.

Patients will see a streamlined workflow system that reduces their waiting time, provides consistent and quick responses, and allows them to receive services locally that previously required travel and increased costs to obtain.

Also, they will be able to discuss medical issues and concerns that involve imaging in their doctor's offices or over the phone during off hours while their doctor accesses the information online. This reduces the earlier system of traveling to the hospital to pick up films, lost films, and long wait times in order to access the information.

Physician/System Perspective on Quality

The vendor provides a state of the art system and equipment through a secure, encrypted authentication process which ensures security measures are in place. The data is fully secure, and the system had been developed to be HIPAA compliant, and is accredited by JCAHO. The services provided are flexible and can be customized to our facility's needs. Preliminary reporting and final reports are provided from Board Certified doctors, and all of the services offered through our facility have 24/7/365 coverage. The opportunity to take advantage of around the clock technical support will help us keep quality and turnaround times up to the standards expected by our patients and physicians. Sub-specialty interpretations are available as well as ongoing consultation services from the vendor as needed for cases requiring

[7] http://www.cms.gov/hipaa/

collaboration, one example being the proposed PACS. Quality assurance reports along with turnaround time reports are available on a quarterly basis. Malpractice insurance is also available through the vendor.

In addition to having real time access to data critical to making diagnostic decisions in the hospital, office, at home or on the road physicians can rest easy knowing that they are working with a system that is not apt to fail or get backlogged. There is greater assurance of "getting it right" with state of the art equipment that is supported around the clock by quality people and advanced technology. The availability of 24 hour coverage takes the burden off of scheduling staff around the clock in an already overburdened system.

Patient Perspective on Quality

Providing state of the art equipment and streamlining workflow efficiencies which allow real time access to patient reports will enhance the patient experience in our facility. Wait times will be reduced, equipment failures will be avoided, the need for duplicated efforts of the radiologist will be eliminated resulting in quicker turnaround times for reports. With new state of the art equipment, we will be able to provide additional services to the expanding elderly patient population and better serve the obese patient by having equipment that will accommodate their needs. These are areas that we have previously identified as growth areas. The ability to feel confident that one is receiving the best possible care is imperative to growing our radiology business. We will be able to market the enhancements to our department and tout the availability of these services provided locally. In the event of an emergency, patients can receive the same quality of care expected in metropolitan areas, locally, saving time and money. This is especially critical with our desire to increase our cardiac services. Community based physicians will be able to access their patients' images remotely, thus adding another dimension to the overarching ability to integrate services in a healthcare system that is known to suffer from fragmentation.

FINANCIAL AND COST ANALYSIS

The financial details and cost analysis are in the attached spreadsheet. This portion of the document is an overview of the details that are contained in the spreadsheet.

Financial Current State

We strived to get current financial baseline data from a real world hospital in existence. Our financial data comes from a real existing rural hospital in Northern California that has 210 beds and services a community of 40,000 people. When looking at the Radiology department General Ledger (GL), we were able to find opportunities immediately for outsourcing consideration. In terms of key cost factors, our radiology department has the following revenue, expense, and net results for our starting year.

Gross Patient Revenue- 98,301,225
Total Expense- 20,762,117
Net Revenue Result- 77,539,108

Expense Reduction

With an outsourced scenario under consideration we looked to the areas of wages, benefits, supplies, purchased services, professional fees, depreciation, and interest for savings opportunities. Within each area we were able to identify items for reduction or elimination in our future state. The result of these efforts reduced our GL expenses post outsourced by $8,410,750.70 in total. Percentage change by specific area is as follows:

Salaries- decrease of 100%
Benefits- decrease of 100%
Professional Fees- decrease of 99%
Supplies and Miscellaneous- decrease of 19%
Purchased Services- increase of 770%
Depreciation- decrease of 100%
Interest- decrease of 100%

Procedures/Visits/Patient Revenue

As a result of our outsourcing efforts, we are expecting a new and improved technology model for the future improvement in speed, quality, and efficiency of service, and increased volumes both in patient visits and procedures. The result of these efforts will yield an expected growth of 3% first year. With 3% growth expected in our radiology visits/procedures and the added new Positron Emission Tomography (PET) service, we are expecting increased revenues as well in the amount of just over $6.5 million.

Outsourced Services

By bringing in an outsourced entity to run our radiology department, we will be able to modernize our technology, processes, and output/service to our community at considerably less expense.

As we intend to fast track the outsource agreement, we chose to utilize a hybrid approach that includes a leased department with a cost plus reimbursement model for the salaries and benefits of the Radiology Outsource Vendor.

The agreement will be in place for two years. Following that, the parties will review the agreement on an annual basis.

Financial Future State

The bottom line of our efforts in reducing expenses, increasing revenue, and utilizing outsourcing services and technologies positively impacts our bottom line by 16%. Results of our net revenue before and after are seen below.

Net Revenue Baseline- 77,539,108
Net Revenue Post Outsourced- 91,845,086
Improvement=16%

SUMMARY

In conclusion, our proposed goal as mandated by our Executive Committee is an aggressive 2 year outsourcing effort that immediately provides benefits to our organizations operational efficiencies, finances, and patient care services. In brief summary of the information previously reviewed in this proposal, we ask the board to keep the following benefits in mind when deciding upon moving forward with this initiative:

- Our Radiology Department will move into the 21st century with the addition of PACS, Teleradiology capabilities, and P.E.T. services.
- Our current hardware portfolio will have longer life and consistent uptime eliminating service impacts
- Leased equipment needed in the future will eliminate the need for large capital purchases and leverage the outsourcer VHA discount status for reduced rates.
- Service Volume and Quality will improve.
- Continual cost overruns and deficits will decrease
- Patients will want to come to our organization versus our competitors.
- Revenue will increase.

These benefits are immediate and are all achieved with the 2 year plan. Once completed as our baseline of continued improvement, we will assess our achievements and move forward with the planning of a phase 2 over an additional 5 year period. At that point, we expect to be able to further leverage even more substantial growth and savings. Our model is a platform for future growth and continued agility.