



**NORTHSTAR HEALTHCARE**

**NORTHSTAR HEALTHCARE INC.**

**MANAGEMENT'S DISCUSSION AND ANALYSIS OF  
FINANCIAL CONDITION AND RESULTS OF OPERATIONS**

**For the Three Months Ended March 31, 2008**

**This MD&A replaces the previously-filed MD&A for the three months ended March 31, 2008**

*The following management discussion and analysis of the financial condition and results of operations of Northstar Healthcare Inc. (the "Company" or "NHC") for the three months ended March 31, 2008 is provided as of May 13, 2008. It is supplemental to, and should be read in conjunction with the financial statements of the Company for the three months ended March 31, 2008. The Company's financial statements are prepared in accordance with accounting principles generally accepted in Canada ("Canadian GAAP"). Substantially all of the Company's operating cash flows are in U.S. dollars; accordingly, all amounts presented herein are stated in thousands of U.S. dollars, except per share data, unless otherwise indicated.*

## **FORWARD LOOKING INFORMATION**

This management's discussion and analysis contains "forward-looking information" (as defined under applicable securities laws). Forward-looking information is typically identified by words such as "believe," "expect," "forecast," "anticipate," "intend," "estimate," "goal," "plan," and "project" and similar expressions of future or conditional verbs such as "will," "may," "should," "could," or "would". These statements reflect current beliefs and are based on information currently available to management.

By its very nature, forward-looking information involves significant known and unknown risks, uncertainties and assumptions. Important assumptions relating to the forward-looking information contained in this management's discussion and analysis include expansion, capital expenditures, competitive conditions and gross economic conditions.

Many factors could cause our actual results, performance or achievements to be materially different from any future results, performance or achievements that may be expressed or implied by such forward-looking information, including, without limitation, general business risks inherent in the ASC industry, including changing surgeon and patient preferences, numerous federal, state and local laws, competition from other healthcare providers and our dependence on payment from third-party payors, including private insurers, managed care organizations and government healthcare programs. For a description of risks that could cause our actual results to materially differ from our current expectations, please see section titled "Risk Factors" in NHC's Annual Information Form. Although the forward-looking information contained in this MD&A is based upon what management believes are reasonable assumptions, there can be no assurance that actual results will be consistent with these forward-looking statements. Should one or more of these risks or uncertainties materialize or should assumptions underlying the forward-looking statements prove incorrect, actual results, performance or achievements could vary materially from those expressed or implied by the forward-looking information. Certain statements regarding forward-looking information included in this MD&A may be considered "financial outlook" for purposes of applicable securities laws, and such financial outlook may not be appropriate for purposes other than this MD&A.

All forward-looking information in this MD&A is qualified by these cautionary statements. The forward-looking statements in this management's discussion and analysis are made as of the date hereof and except as required by law we do not intend, and do not assume any obligation, to update or revise these forward-looking statements.

## **NON-GAAP FINANCIAL MEASURES**

This management's discussion and analysis contains references to EBITDA (earnings before interest, taxes, depreciation and amortization). Management believes that EBITDA is a useful supplemental measure of cash available for dividends prior to debt service, capital expenditures, income taxes and other reserves. However, EBITDA is not a recognized measure under Canadian GAAP and does not have a standardized meaning prescribed by Canadian GAAP. Therefore, EBITDA may not be comparable to similar measures presented by other issuers. Investors are cautioned that EBITDA should not be construed as an alternative to net income or loss (which are determined in accordance with Canadian GAAP) as an indicator of the performance of the Company or its subsidiaries or as a measure of liquidity and cash flows.

## **PRESENTATION OF FINANCIAL INFORMATION**

The Company was incorporated on March 16, 2007 and completed its initial public offering and acquisition of its subsidiaries on May 17, 2007.

This management discussion and analysis includes the pro forma combined operating results of the Company for the period of January 1, 2007 to March 31, 2007, prior to the public offering. Certain figures disclosed in these pro forma combined operating results differ from the pro forma combined operating results previously disclosed in the Company's Business Acquisition Report, dated July 27, 2007, for the quarter ended March 31, 2007, as a result of management's change in estimates used to determine net patient service revenues made following the introduction of new reporting and trending software in the third quarter of 2007.

In addition, the pro forma combined operating results for the period of January 1, 2007 to March 31, 2007 are not necessarily indicative of the results that would have actually occurred had the transaction been consummated at the dates indicated nor are they necessarily indicative of future operating results or the financial position of the Company, as the pro forma combined operating results excludes expenses related to being a public issuer, as well as expenses of Northstar Healthcare Acquisitions, LLC, the Company's operating subsidiary.

We have also included a number of comparative operating statistics, such as cases and procedures performed at the facilities operated by the Palladium Partnership and the Kirby Partnership for the three-month ended March 31, 2008 compared with the prior year periods. Cases and procedures are key drivers of our revenues. This information is not intended to provide a comprehensive comparison of financial results, as gross billings and net patient service revenues vary by patient, insurance carrier and procedure.

## CORPORATE OVERVIEW

NHC was incorporated under the *Business Corporations Act* (British Columbia) on March 16, 2007. NHC is a corporation formed to indirectly acquire and/or manage ambulatory surgery centres in the United States, focusing initially on Houston and other metropolitan areas in Texas. NHC used the net proceeds of an initial public offering, including the over-allotment, to indirectly acquire a 70% partnership interest in the Palladium Partnership and a 60% partnership interest in the Kirby Partnership, which operate two ambulatory surgery centres (the "Northstar ASCs") located in Houston. In addition, NHC manages an ambulatory surgery centre in Dallas and three pain management clinics in Houston.

The Northstar ASCs are licensed ambulatory surgery centres that provide scheduled surgical procedures in a limited number of clinical specialties, which enables them to develop routines, procedures and protocols to maximize operating efficiency and productivity while offering an enhanced healthcare experience for both surgeons and patients. The Northstar ASCs consist of The Palladium For Surgery - Houston and the Kirby Surgery Center.

Together, the Northstar ASCs have seven operating suites, three procedure or treatment rooms typically used by pain management specialists or for colonoscopies, 12 pre-operation beds, 17 post-operation or recovery beds and 128 surgeons with medical staff privileges.

The Northstar ASCs do not offer the full range of services typically found in traditional hospitals, but instead focus on certain clinical specialties, including orthopedic surgery, podiatry surgery, ear, nose and throat ("ENT"), pain management and general surgery.

## RESULTS OF OPERATIONS FOR THE THREE MONTHS ENDED MARCH 31, 2008 TO THE PRO FORMA COMBINED RESULTS OF OPERATIONS FOR THE THREE MONTHS ENDED MARCH 31, 2007

(in 000's of US \$, except per share data)

	<b>Three Months Ended March 31, 2008 (Unaudited)</b>	<b>Proforma Combined Three Months Ended March 31, 2007 (Unaudited)</b>
<b>Net patient service revenue</b> .....	<u>\$ 10,953</u>	<u>\$ 11,120</u>

	<b>Three Months Ended March 31, 2008 (Unaudited)</b>	<b>Proforma Combined Three Months Ended March 31, 2007 (Unaudited)</b>
<b>Operating expenses</b>		
Salaries and benefits .....	1,537	1,323
Drugs and supplies .....	873	819
General and administrative.....	1,805	1,159
Depreciation and amortization.....	439	404
	<u>4,654</u>	<u>3,705</u>
<b>Income from operations</b>	<b><u>6,299</u></b>	<b><u>7,415</u></b>
<b>Other expense (income)</b>		
Distributions, other liabilities, non-controlling interest.....	427	547
Withholding taxes.....	345	383
Change in fair value of other liabilities, non-controlling interest....	(1,300)	-
Loss/(Gain) on foreign currency.....	2,846	-
State franchise tax .....	74	-
Other expense (income).....	(30)	13
	<u>2,362</u>	<u>943</u>
<b>Income before income taxes and non-controlling interests .....</b>	<b><u>3,937</u></b>	<b><u>6,472</u></b>
<b>Income tax expense</b>		
Current.....	(158)	(170)
Future .....	(309)	830
	<u>(467)</u>	<u>660</u>
<b>Non-controlling interests.....</b>	<b><u>2,302</u></b>	<b><u>2,267</u></b>
<b>Net Income .....</b>	<b><u>\$ 2,102</u></b>	<b><u>\$ 3,545</u></b>
<b>Net Income per common share (basic and fully diluted).....</b>	<b><u>\$ 0.15</u></b>	<b><u>\$ 0.26</u></b>
<b>Weighted average shares outstanding (basic and fully diluted) .....</b>	<b><u>13,900,852</u></b>	<b><u>13,900,852</u></b>

Net patient service revenue is reported at the estimated net realizable amounts from patients, third-party payors, and others for services rendered. Revenue is recognized upon the performance of the patient service. The amounts actually collected by the Company from third-party payors, including private insurers, are variable, even for identical procedures. An additional factor in the determination of net patient service revenues is the Company's payor mix, as between private health insurance plans, workers' compensation, directly from patients and from government payor plans. Management reviews and evaluates historical payment data, payor mix and current economic conditions on a periodic basis and adjusts the estimated collections as a percentage of gross billings (which are used to determine net patient service revenue) as required in subsequent periods based on final settlements and collections.

Net patient service revenues for the three months ended March 31, 2008 totalled \$11.0 million, a decrease of \$0.1 million or 1.5% compared to the three months ended March 31, 2007, which totalled \$11.1 million. Though the total number of procedures performed at the Northstar ASCs increased by 55 procedures during the three months ended March 31, 2008 as compared to the prior year period, the slight decline in net patient service revenues was due to a negative shift in payor mix at the Kirby Partnership. This shift in payor mix at the Kirby Partnership was partially offset by an increase of 10.8% in net patient service revenues at the Palladium Partnership.

Salaries and benefits for the three months ended March 31, 2008 totalled \$1.5 million, which exceeded the salaries and benefits for the pro forma three months ended March 31, 2007 by \$0.2 million or 16.1%. The increase was due to the inclusion of salaries and benefits for employees of Northstar Healthcare Acquisitions, L.L.C. ("Northstar Acquisitions"), the Company's operating subsidiary (as such salaries and benefits were not included in the pro forma combined results for the three months ended March 31, 2007), whose expense was \$0.3 million for the three months ended March 31, 2008.

Drugs and medical supplies for the three months ended March 31, 2008 increased to \$0.9 million or 8% of net patient service revenues compared to the three months ended March 31, 2007, for which drugs and medical supplies costs were \$0.8 million, or 7.4% of net patient service revenues. The increase of \$0.1 million or 0.6% of net patient service revenues was due to an overall increase of 55 procedures for the Northstar Partnerships and a decrease in net patient service revenues due to payor mix at the Kirby Partnership.

General and administrative expense for the three months ended March 31, 2008 totalled \$1.8 million, which exceeded the general and administrative expense for the pro forma three months ended March 31, 2007 by \$0.6 million, or 55.7%. As a percent of net patient service revenues, general and administrative expense increased to 16.5% for the three months ended March 31, 2008, an increase of 6.1% compared to the three months ended March 31, 2007, for which period the percentage was 10.4% of net revenues. The increase was primarily due to general and administrative expenses incurred by Northstar Acquisitions (as such general and administrative expense was not included in the pro forma combined results for the three months ended March 31, 2007). The majority of these general and administrative expenses, including legal, accounting, insurance and directors' and officers' compensation, relate to expenses associated with being a reporting issuer in Canada.

Distributions, other liabilities, and non-controlling interest totalled \$0.4 million, withholding tax totalled \$0.3 million, loss on foreign currency exchange contracts totalled \$2.8 million and change in fair value of other liabilities non-controlling interest totalled \$1.3 million. Non-controlling interests amounted to \$2.3 million based on percentage of minority interests owned by the physician limited partners and Healthcare Ventures Ltd. ("Ventures").

The loss on foreign currency exchange contracts of \$2.8 million relates to the change during the period in fair value of the five-year foreign currency exchange contracts entered into by the Company to hedge exposure to fluctuations between the U.S. dollar and the Canadian dollar for future Common Share dividends. This loss was as a result of the decline in value of the Canadian dollar during the period, net of realized gains recognized between the spot rate on the date of record and the exchange rate under the Company's currency instruments.

The \$1.3 million change in the fair value of other liabilities, non-controlling interest represents the change in fair value of the Class B Units of Northstar Healthcare Subco, LLC ("Northstar Subco") held by Ventures, which fair value was based on an external appraisal incorporating the discounted cash flow method as at March 31, 2008. This item is recorded as an income or expense of the Company under Canadian GAAP as a result of the negotiation right held by Ventures, which entitles it to request at any time after May 17, 2010 that Northstar Subco enter into good faith negotiations to purchase for cancellation of all or any portion of the Class B Units of Northstar Subco held by Ventures. The price paid for such Northstar Subco Class B Units will be equal to their fair market value plus the fair market value of a corresponding number of Class B Units of Northstar Acquisitions. Northstar Acquisitions will purchase for cancellation of all outstanding Class B Units of Northstar Acquisitions for a nominal amount on the date that all outstanding Class B Units of Northstar Subco have been purchased for cancellation from Ventures by Northstar Subco.

#### **NET PATIENT SERVICE REVENUES BY PAYOR MIX OF THE NORTHSTAR ASCS FOR THE THREE MONTHS ENDED MARCH 31, 2008 AND 2007**

Financial Class	Q1 2008 Net Patient Service Revenues by Payor Mix	Q1 2007 Net Patient Service Revenues by Payor Mix
Private insurance and other private pay ...	91.0%	90.5%
Workers compensation .....	5.1%	6.7%
Medicare/Medicaid .....	1.5%	0.9%
Other .....	2.4%	1.9%
<b>Total.....</b>	<b>100.0%</b>	<b>100.0%</b>

Net patient service revenues represent gross revenues received from patients less provisions for contractual adjustments with third-party payors, such as Medicare, Medicaid or private payors with managed care plans. This information is not intended to provide a comprehensive comparison of financial results, as reimbursement by insurance carrier varies based on deductibles, plan coverage and procedures performed.

Reimbursement is the highest from patients with private insurance and other private pay and lowest from patients with Medicare/Medicaid.

### CASE AND PROCEDURE MIX OF THE NORTHSTAR ASCS FOR THE THREE MONTHS ENDED MARCH 31, 2008 AND 2007

Speciality	Q1 2008 Cases	Q1 2008 Percentage of Cases	Q1 2008 Procedures	Q1 2008 Percentage of Procedures	Q1 2007 Cases	Q1 2007 Percentage of Cases	Q1 2007 Procedures	Q1 2007 Percentage of Procedures
Pain Management .....	1,284	56.2%	7,739	72.2%	1,210	52.8%	7,528	70.6%
Orthopaedics.....	516	22.5%	1,342	12.5%	527	22.9%	1,382	13.0%
Podiatry.....	120	5.2%	494	4.6%	151	6.6%	513	4.8%
Gastro-intestinal.....	130	5.7%	19	0.2%	151	6.6%	78	0.7%
General Surgery.....	79	3.4%	207	1.9%	92	4.0%	265	2.5%
ENT.....	161	7.0%	912	8.5%	166	7.2%	892	8.4%
<b>Total.....</b>	<b>2,290</b>	<b>100.0%</b>	<b>10,713</b>	<b>100.0%</b>	<b>2,297</b>	<b>100.0%</b>	<b>10,658</b>	<b>100.0%</b>

**Note:** A procedure is defined as the actual surgery or surgeries that are performed on the date of service for each patient (case). Each case typically includes numerous procedures. In prior management discussion and analysis reports, the Company provided the number of “unique” procedures per case as the total number of procedures during the period (i.e. a patient may have three different procedures performed, however, one of the three procedures might have been performed numerous times during the case). In this management discussion and analysis, the Company has calculated the total quantity of procedures performed on a case, regardless of the fact that the same procedure may have been performed numerous times. As a result, the total number of procedures has been adjusted in the 2007 period. This change in the number of procedures has no effect on the number of cases or net patient service revenues, and was adjusted to provide the total number of all procedures for analysis purposes only.

We have provided a number of comparative operating statistics, such as cases and procedures performed at the facilities operated by the Palladium Partnership and the Kirby Partnership for the three-month period ended March 31, 2008 compared with the prior three-month period. Cases and procedures are one of the key drivers of our revenues. This information is not intended to provide a comprehensive comparison of financial results, as gross billings and net patient service revenues vary by patient, insurance carrier and procedure.

A case is defined as a patient visit to the ambulatory surgery center on a specific date of service. A procedure is defined as the actual surgery or surgeries that are performed on the date of service. As a result, there may be more than a single procedure performed during a specific case.

Total cases for the three months ended March 31, 2008 were 2,290, a decrease of 7 cases over the 2,297 total cases in the same period in 2007. Total procedures for the three months ended March 31, 2008 were 10,713, an increase of 55 procedures over the same period in 2007, which totalled 10,658.

Cases and procedures for the three months ended March 31, 2008 fluctuated between specialties as a result of physician vacations, payor mix and seasonality of the first calendar quarter. Based on historical trends, net patient service revenues for the first and second calendar quarters typically trail the third and fourth calendar quarters by 4.0% to 5.0% in aggregate.

**RECONCILIATION OF NET INCOME TO EBITDA FOR THE THREE MONTHS ENDED  
MARCH 31, 2008 TO THE PRO FORMA COMBINED RESULTS OF OPERATIONS FOR THE  
THREE MONTHS ENDED MARCH 31, 2007**  
(in 000's of US \$, except per share data)

	<b>Three Months Ended March 31, 2008 (Unaudited)</b>	<b>Proforma Combined Three Months Ended March 31, 2007 (Unaudited)</b>
<b>Net patient service revenue</b> .....	\$ 10,953	\$ 11,120
Net income.....	\$ 2,102	\$ 3,546
Add:		
Depreciation and amortization.....	439	404
Loss on foreign currency exchange contracts.....	2,846	-
Change in fair value of other liabilities, non-controlling interest .....	(1,300)	-
Income taxes .....	(467)	660
<b>EBITDA net of non-controlling interests and before unrealized gain on foreign currency exchange contracts and change in fair value of other liabilities, non-controlling interest</b> .....	3,620	4,610
Less:		
Capital expenditures .....	(81)	(89)
<b>EBITDA net of non-controlling interests and capital expenditures, and before unrealized gain on foreign currency exchange contracts and change in fair value of other liabilities, non-controlling interest</b> .....	\$ 3,539 <sup>(1)</sup>	\$ 4,521 <sup>(2)</sup>
<b>EBITDA margin net of non-controlling interests and capital expenditures, and before unrealized gain on foreign currency exchange contracts and change in fair value of other liabilities, non- controlling interest</b> .....	32.3%	40.7%

(1) Cash available to the Company to pay dividends for the three months ended March 31, 2008 is \$158 less than EBITDA net of non-controlling interest and capital expenditures, and before unrealized gain on foreign currency exchange contracts and change in fair value of other liabilities, non-controlling interest, on account of current taxes.

(2) Cash available to the Company to pay dividends for the three months ended March 31, 2007 is \$170 less than EBITDA net of non-controlling interest and capital expenditures, and before unrealized gain on foreign currency exchange contracts and change in fair value of other liabilities, non-controlling interest, on account of current taxes.

EBITDA before non-controlling interests of the Physician Limited Partners and distributions to Ventures for the three months ended March 31, 2008 was \$3.6 million. The Company currently has a policy of distributing its available cash from consolidated operations, subject to applicable laws, by way of a monthly dividend on Common Shares, after the retention of amounts considered reasonable and prudent by the Board of Directors for working capital and other purposes, including capital investment and capital reserves. Cash dividends declared for the three months ended March 31, 2008 totalled \$4.2 million or \$0.299 (Cdn \$0.30) per Common Share.

The Company's current monthly dividend rate of Cdn \$0.10 per Common Share was established at the time of the initial public offering and was, in large part, based upon the historical results of the Northstar Partnerships (adjusted for certain factors) in connection with the change in capital structures additional expense as a result of becoming a reporting issuer.

## LIQUIDITY, CAPITAL RESOURCES AND FINANCIAL CONDITION

Liquidity refers to an entity's ability to meet its financial obligations and commitments as they become due. Management anticipates that cash flows from operations and funds provided from time to time under available credit facilities will provide the Company with sufficient liquidity to manage accounts receivable, medical supplies and other short-term cash requirements for the next 12 months. Management expects to have sufficient working capital to meet the Company's obligations in 2008.

The Company is dependent upon cash generated from operating activities of the Northstar Partnerships, which are the source of financing for its operations and for meeting its contractual obligations. A majority of the Northstar Partnerships' cash flows is distributed, on a monthly basis, to the Company and holders of minority partnership interests.

The Company currently has a policy of distributing its available cash from consolidated operations, subject to applicable law and the terms of any then existing indebtedness, by way of monthly dividends on the Common Shares, after the retention of amounts considered reasonable and prudent by the Board of Directors for working capital and other purposes, including capital investment and capital reserves. Included in the calculation of the Company's cash available to pay dividends is a cash reserve equal to 10% of the Company's aggregate monthly dividend, which is retained by the Company, through its subsidiary, Northstar Subco. In addition, any cash in excess of the cash reserve and the amount necessary to pay the monthly dividend is also retained by the Company. The calculation of the monthly 10% cash reserve was \$1.3 million for the period of May 17, 2007 to March 31, 2008. As of March 31, 2008, the Company had cash reserves of \$1.9 million. Had the Company not deferred a portion of the Subco monthly distributions to Ventures of \$0.9 million for the period of May 17, 2007 to March 31, 2008, such cash reserves balances would have been \$1.0 million.

The Company determines the amount of its monthly dividend based on periodic reviews of its estimated annual earning and related estimated annual cash flows.

The Company's cash flow will vary from quarter to quarter based on seasonality of the operations. Based on historical trends, net patient service revenues for the third and fourth calendar quarters typically exceed the first and second calendar quarters by 4.0% to 5.0% in aggregate.

The Company's cash flow from operations was \$6.5 million for the three months ended March 31, 2008. Dividends paid and distributions to non-controlling interests were \$6.8 million for the three months ended March 31, 2008. Capital expenditures were \$0.1 million for the three months ended March 31, 2008.

Cash dividends declared in the three months ended March 31, 2008 totalled \$4.2 million or \$0.299 (Cdn \$0.30) per common share.

	<b>1<sup>st</sup> Q 2008</b>	<b>4<sup>th</sup> Q 2007</b>	<b>3<sup>rd</sup> Q 2007</b>	<b>Period from May 17, 2007 to June 30, 2007</b>
Net patient service revenues.....	\$ 10,953	\$ 13,593	\$ 12,508	\$ 6,818
Net income.....	2,102	1,470	322	1,369
Net income per share.....	\$ 0.15	\$ 0.11	\$ 0.02	\$ 0.10

## CONTRACTUAL OBLIGATIONS

The Company leases property and certain equipment under non-cancellable operating lease arrangements which expire at various dates through 2014. Certain leases of real property provide options to extend the lease terms.

The following table outlines the future minimum payments under operating leases:

<u>Year</u>	<u>Amount</u>
2008 (remaining nine months) .....	623
2009.....	854
2010.....	867
2011.....	882
2012.....	880
Thereafter .....	751
Total .....	<u>\$ 4,857</u>

## FINANCIAL INSTRUMENTS

### Foreign Exchange Contracts

The Company entered into foreign currency exchange contracts to manage the Company's exposure to fluctuations in the exchange rate between U.S. and Canadian currencies, which arise from the payment of dividends on its Common Shares.

As of March 31, 2008, the Company is committed to deliver approximately \$1.3 million monthly in exchange for approximately C\$1.4 million for the contract period of April 2008 to June 2012 and \$1.4 million monthly in exchange for approximately C\$1.4 million for the contract period of June 2012 to December 2012, at stipulated exchange rates as follows:

<u>Contract Dates</u>	<u>US\$ to be delivered</u>	<u>Cdn\$ to be received</u>	<u>Cdn\$ per US\$</u>
April 2008 – June 2012	63,836	69,504	1.0888
June 2012 – December 2012	8,477	8,341	0.9840

The fair value of the Company's foreign currency contracts was \$2.2 million at March 31, 2008. Changes in the fair value during each reporting period are recorded as loss or gain on foreign currency in the consolidated statement of operations.

Ventures has provided collateral in the amount of \$5.0 million to secure performance under these contracts.

At the date of record, the Company records a liability based on the amount of U.S. funds required to pay the declared distribution using the Canadian to U.S. dollar foreign exchange spot rate then in effect. When the dividend is paid, the difference between the Canadian to U.S. dollar foreign exchange spot rate and the exchange rate under the Company's currency instruments is recognized as loss or gain on foreign currency. The gain recognized was \$0.4 million for the three months ended March 31, 2008.

## RELATED PARTY TRANSACTIONS

Physicians who represent the non-controlling interests in the Northstar Partnerships routinely provide independent professional services directly to patients utilizing the Northstar ASCs.

Ventures holds all of the Acquisitions Class B Units. Each Acquisitions Class B Unit entitles Ventures to receive monthly distributions of cash from Northstar Acquisitions equal to a specified percentage of Northstar Acquisitions' gross management fee revenues (including management fees earned for services earned under the Management and Cost Sharing Agreement between Northstar Acquisitions and the Northstar Partnerships and for services provided to other clients of Northstar Acquisitions), payable after all distributions have been made to the holders of Acquisitions Preferred Units and Acquisitions Class A Units. The specified percentage is currently equal to 12.5% and will decrease if Ventures disposes of Acquisitions Class B Units pursuant to its negotiation rate.

Ventures also holds all of the Subco Class B Units. Each Subco Class B Unit entitles Ventures to receive monthly distributions of cash from Northstar Subco on a *pari passu* basis with the holders of the Subco Class A Units, except if the Company's cash available to pay dividends for any month is less than 110% of the initial full monthly dividend, Ventures' distribution from Northstar Subco shall be deferred by the amount of any shortfall.

Ventures, as promoter, received \$15.8 million in net proceeds from the initial public offering (including the over-allotment option) and has provided a \$5.0 million revolving credit facility to the Company. The credit facility bears interest at the 30 day LIBOR plus 300 basis points, payable monthly. In addition, the Company has accrued a one-time commitment fee equal to 0.5% of the full amount of the credit facility, and will pay a fee equal to 0.25% per annum on all amounts not drawn on the credit facility. To date, no amounts have been drawn on the credit facility.

Ventures has also provided cash collateral of \$5.0 million as required to support the foreign currency arrangement. Ventures received a fee equal to 1.0% of the amount of cash collateral provided at closing of the initial public offering on May 17, 2007. The cash collateral remains the property of Ventures and all income earned thereon is for the benefit of Ventures.

Included in accrued liabilities and other current liabilities is \$1.0 million related to deferred Northstar Subco monthly distributions to Ventures and revolving credit facility fees. The operating agreement of Northstar Subco provides that until the earlier of December 31, 2010 or an announced increase in monthly dividends by the Company, if the Company's cash available to pay dividends for any month is less than 110% of the initial full monthly dividend, Ventures' distributions from Northstar Subco shall be deferred by the shortfall. The Company's cash available to pay dividends for June, August, November, December 2007 and January, February and March 2008 was less than 110% of the initial full monthly dividends; accordingly, the payment of \$0.9 million of the distributions due to Ventures on account of its Northstar Subco Class B Units for those months has been deferred until twelve months following the month of deferral, provided at such time the Company's 12-month trailing cash available for dividends exceeds 110% of the initial full monthly dividends.

The Company provides management services to the Palladium for Surgery - Dallas and River Oaks Pain Management (the "Managed Centers"). The Palladium for Surgery - Dallas is located in Dallas Texas and began operations in 2005. River Oaks Pain Management consists of three pain management clinics located in Houston, Humble and Baytown, Texas. The Company's CEO owns a 50% interest in River Oaks Pain Management and together with certain members of management owns 95% of The Palladium for Surgery - Dallas. The Managed Centers are managed by the Company pursuant to a management agreement. The management agreement provides for a management fee of 10% of collected revenues.

In October, 2007, the Company acquired an option to acquire a 60% interest in The Palladium for Surgery - Dallas. In consideration for the option, the Company has agreed to reduce the management fees it receives from The Palladium for Surgery - Dallas from 10% to 5.5% over the term of the option, upon the achievement of certain prescribed conditions. As of March 31, 2008, The Palladium for Surgery - Dallas had not met the prescribed conditions.

Revenue from management fees represents fees charged to the managed centers, based on a percent of collections, for managing the center's business operations. The revenue from these fees was \$0.1 million for the three months ended March 31, 2008, and was included in net patient service revenue.

These transactions are measured at exchange amounts which represent the amount agreed upon by the parties.

## **CRITICAL ACCOUNTING ESTIMATES**

The preparation of the financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenue and expenses during the period. Actual results could differ from those estimates.

Management estimates are required with respect to the valuation of financial instruments, acquired assets and liabilities, intangible assets, goodwill, accounts receivable, inventories and provisions for potential liabilities, determination of net patient service revenues and income tax provisions.

Net patient service revenues of the Company includes amounts for services billed to private insurance carriers, federal and state agencies and patients. Billed revenues are recorded net of the estimated contractual adjustments provided for under the various agreements with the majority of these third party payors. Management establishes the contractual allowance adjustments and allowances for doubtful accounts based on historical payment data, current economic conditions and other pertinent facts for each Northstar ASC. Management reviews and evaluates historical payment data and current economic conditions on a quarterly basis and adjusts its estimates as appropriate.

## **ADOPTING OF NEW ACCOUNTING STANDARDS AND DEVELOPMENTS**

### **Recent Accounting Pronouncements**

On January 31, 2008, the CICA issued a new accounting standard: Handbook Section 3064 Goodwill and Intangible Assets. Section 3064 replaces Handbook Section 3062 Goodwill and Other Intangible Assets and Handbook Section 3450 Research and Development Costs. Section 3064 establishes standards for recognition, measurement and disclosure of goodwill and intangible assets. This new standard will be effective for the Company in the first Quarter of 2009. The Company is currently evaluating the implications of this new standard.

In 2008, Canada's Accounting Standards Board ratified a strategic plan that will result in Canadian GAAP, as used by public companies, being converged with International Financial Reporting Standards over a transitional period currently expected to be about five years. The Company will be required to report using the converged standards effective for interim and annual financial statements relating to fiscal years beginning on or after January 1, 2011. The impact of this transition on the Company's consolidated financial statements has not yet been determined.

### **Adopting of New Accounting Standards and Developments**

Effective January 1, 2008, the Company adopted two new CICA standards related to the disclosure and presentation of financial instruments. Section 3862, Financial Instruments Disclosure and Section 3863, Financial Instruments Presentation, replaced Section 3861 Financial Instruments Disclosure and Presentation. The new disclosure standard increases the emphasis on the risks associated with both recognized and unrecognized financial instruments and how those risks are managed. The new presentation standard carries forward the former presentations requirements.

Effective January 1, 2008, the Company adopted Section 1535, "Capital Disclosures,". This standard establishes standards for disclosing information about a Company's capital and how it is managed in order that a user of the financial statements may evaluate the company's objectives, policies, and processes for managed capital.

Effective January 1, 2008, the Company adopted Section 3031, "Inventories", which is based on International Accounting Standard 2. Under the new standard, inventories are required to be measured at the "lower of cost and net realizable value", which is different from the existing guidance of the "lower of cost and market". The new standard also allows the reversal of any write-downs previously recognized.

## **MANAGEMENT'S RESPONSIBILITY FOR FINANCIAL REPORTING AND DISCLOSURE CONTROLS**

### **Internal Controls over Financial Reporting**

Disclosure controls and procedures within the Company are designed to provide reasonable assurance that all relevant information required to be disclosed in its annual and interim filings and other reports is recorded, processed, summarized and reported on a timely basis and is accumulated and communicated to the Northstar management.

The Company's Chief Executive Officer ("CEO") and Chief Financial Officer and Corporate Secretary ("CFO") are responsible for establishing and maintaining the Company's disclosure controls and procedures to provide reasonable assurance that all relevant information required to be disclosed is gathered and reported on a timely basis so that appropriate decisions can be made regarding public disclosure. It should be noted that while the CEO and CFO believe that disclosure controls and procedures can provide a reasonable level of assurance and they are effective, they do not expect that disclosure controls and procedures can prevent all errors and fraud. A control system, no matter how well designed or operated can provide only reasonable, not absolute, assurance that the objectives of the control system are met.

Internal controls over financial reporting are designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements in accordance with Canadian GAAP focusing in particular on controls over information. Management is responsible for establishing and maintaining adequate internal controls over financial reporting. A control system, no matter how well conceived and operated, can provide only reasonable, and not absolute assurance that the objectives of the control system are met. Because of their inherent limitations, internal controls over financial reporting may not prevent or detect misstatements. These weaknesses in internal controls over financial reporting result in a more than remote likelihood that a material misstatement would not be prevented or detected on a timely basis.

The CEO and CFO have designed such disclosure controls and procedures, or caused them to be designed under their supervision, to provide reasonable assurance that material information relating to the Company, including its consolidated subsidiaries, is made known to them by others within those entities, particularly during the period in which the annual filings are being prepared. The CEO and CFO have evaluated the effectiveness of the Company's disclosure controls and procedures and have concluded that they are adequate and effective as of March 31, 2008, based on such evaluation.

Common with many small businesses, such as the Northstar ASCs, lack of segregation of duties, weakness in control environment and IT general control processes have, to date, been identified as areas where weakness exist. The existence of these weaknesses is compensated by senior management monitoring. The Company is taking steps to augment and improve the design of procedures and controls impacting these areas of weakness over internal controls over financial reporting.

There has been no change in the design of the Company's internal control over financial reporting during the three months ended March 31, 2008, that would materially affect or are reasonably likely to materially affect the Company's internal control over financial reporting.

### **QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK**

In the normal course of business, we are exposed to market risks arising from adverse changes in interest rates and the C\$/US\$ foreign currency exchange rate. Market risk is defined for these purposes as the potential change in the fair market value of financial assets and liabilities resulting from an adverse movement in these rates.

We are exposed to fluctuations in the exchange rate between the Canadian dollar and the U.S. dollar because the Company's operations and earnings are in U.S. dollars and the dividends will be paid in Canadian dollars. In order to minimize the impact of fluctuations in the exchange rate between the Canadian dollar and the U.S. dollar, we have entered into Canadian dollar/U.S. dollar exchange contracts at a rate of US\$1 = C\$1.0888 until June 2012 and US\$1 = C\$0.9840 for the period from June 2012 until December 2012 for the total amount anticipated for dividends

to common shareholders. The agreements consist of monthly forward foreign exchange contracts, of which 56 are still open as of March 31, 2008.

At March 31, 2008, we had unrealized foreign exchange gains on the open forward currency exchange contracts, which had a value of \$2.2 million based on the open spot rate as of March 31, 2008. If the Company had liquidated the contracts and realized a gain, it would be exposed to fluctuations in the exchange rate between the Canadian dollar and the U.S. dollar with respect to the dividends to the common shareholders.

## **RISK FACTORS**

Please refer to the risk factors articulated in the Company's Annual Information Form for a list of the significant risk factors to which the Company is exposed.

## **OUTSTANDING SHARE DATA**

At March 31, 2008, the Company had 13,900,852 Common Shares outstanding.

## **OUTLOOK**

Healthcare delivery in the United States continues to be an issue receiving enormous attention in this presidential election year. The Democratic focus has been increasing access to care. The Republican focus is upon containment of costs. Experts predict that the demand for service will continue to increase as the population ages and technology continues to bring more procedures to the fore. Northstar's management believes that the Company is well positioned to benefit from that growth. Nonetheless, there will continue to be industry-wide pressures on reimbursement programs to limit the escalation in healthcare costs.

The Northstar ASCs added eleven new surgeons to its medical staff during the three months ended March 31, 2008, an increase of 8.6% over the period ended December 31, 2007. In addition, the Palladium Partnership expects to further increase its complement of surgeon partners during 2008, which management believes contribute to increased revenues and profitability.

The Company is implementing a number of new programs and continues to recruit new surgeons to add to its medical staff. Spine surgery is rapidly evolving in the outpatient surgery centers. Palladium has recruited a leading neurosurgeon to develop its spine surgery program. We expect to begin performing these surgical procedures in Q2 of 2008. The outpatient spine program has great synergy with our pain management doctors who perform the diagnostic procedures in advance of the surgery. Palladium is enhancing its recruitment and training of primary care physicians who are interested in learning to perform pain management procedures at Palladium. Physicians who received their training at Palladium performed more than 50% of all pain management cases performed at Palladium in 2007. Sinus surgery continues to be an area of high profitability and consistent growth. Palladium will continue its focus of recruiting additional sinus surgeons.

Performance at the Kirby center has lagged that which we have seen at Palladium. We do expect to see the development of a spine program and a hand surgery program over the next few quarters. The Kirby surgeons have adopted improved coding of their surgical cases and updates of fee schedules that will positively impact cash collections. Scheduling efficiencies have been implemented that will allow the Kirby Partnership to improve throughput and to bring additional surgeons to the medical staff. As of March 31, 2008 there were 24 actively practicing surgeons at Kirby as compared with 10 surgeons at the time of IPO. These additional 14 surgeons represent 10.6% of net patient service revenues at Kirby for the three months ended March 31, 2008.

Offsetting these positive results were shifts among some of the surgeons to lower reimbursed cases. Management continues to monitor the leading indicators closely.

As disclosed in the Company's MD&A for the third quarter of 2007, actual collections at the Kirby Partnership for the year ended December 31, 2006, the three-month period ended March 31, 2007 and the 46-day period ended May 16, 2007 (the day immediately prior to the completion of the Company's initial public offering) were lower than the reported net patient service revenues for those periods. The Company is currently in discussions with the physician limited partners at the Kirby Partnership regarding the recoupment from the physicians' escrow accounts of the difference between the reported net patient service revenues and the actual collections for these pre-IPO periods. In accordance with the escrow agreement, the escrow agent has been notified.

The Company intends to continue its strategies of enhancing the operating efficiency of the Northstar ASCs, pursuing acquisitions and continuing the cash distribution practices referred to in Liquidity, Capital Resources and Financial Condition section of this management's discussion and analysis.

### **ADDITIONAL INFORMATION**

Additional information relating to the Company, including the consolidated interim financial statements for the three months ended March 31, 2008, is available on SEDAR at [www.sedar.com](http://www.sedar.com).

May 13, 2008