

Background

Working with district hospitals offers unique challenges and opportunities. Here are principles, assumptions and preferences on which to base affiliations and merger with hospital/health districts. These have been gleaned from multiple documents related to hospital district proposals over the past 15 years.

Principles

1. In the current environment, frank governance conversations are essential. Therefore, having a non-public operating board that can deliberate with confidentiality often achieves better results.
2. There should be no overlaps between district commissioners and operating governing board membership.
3. Finances of small hospital/healthcare districts are often tenuous. A model in which the district owns and maintains the facility and another non-public entity owns the hospital operation and equipment can be advantageous. The risk of operating is removed from the district and the operating entity receives the benefit of a facility. It rarely is viable or politically possible to have an outside entity acquire a district facility.
4. There must be synergy between the district and the operating entity. This could be a referral source, investing in a high-growth area, consolidating support service thereby reducing operating expenses, among others. Ideally the district would be part of a general geographic service area in which the operator is a market-leading provider (usually #1 or #2 in the market).
5. The district should have a long-term levy to support the construction and maintenance of facilities. Typically, the levy should coincide with the useful life of the facility and must include adequate funds for general building shell maintenance and upgrades (25+ years).
6. A long-term lease (at least 25 years) with the district for the hospital facilities is essential to encourage partnership and operating investment. Aligning the lease with the facilities levy can be advantageous. However, it also creates a moment in time when the community and operator must come together to convince voters to support and new levy.

7. If a district is fortunate to have an operating levy in addition to a building levy, one use that often solidifies public support is the operation of a “free” clinic and/or support of citizens who have no insurance.
8. Small districts often employ physicians and other providers. In most cases establishing these as hospital-based practices provides a sustainable business model. The disadvantage is that patients receive split bills and may seek providers who are not hospital-based. Some subsidies of these practices may be necessary due to small and fluctuating volumes. However, they should be organized under a sophisticated practice management system of a larger provider with a physician practice infrastructure.

RFP Assumptions/Preferences

Proactive communications between the district and operator are essential. The CEO technically must report to the operator, yet have good communication skills to engender the support of the district/facility owner as well.

1. The parties should agree upon and support the mission and values of the operating organization. (make this explicit in every document from LOI to Definitive Agreement)
2. Create a detailed Term Sheet following acceptance of the Letter of Intent so that the Definitive Agreement is relatively easy to draft.
3. From Letter of Intent to Definitive Agreement between a district and operator typically generally require at least 6-12 months to negotiate. So far, the courts have permitted elected district commissioners to bind the district to long-term operating contracts. This is a list of critical items to include in an agreement:
 - i. Clearly defined accountability for general building maintenance (usually an operating duty) vs. facility upgrade/maintenance of building elements such as roof replacement, exterior replacement/maintenance, etc., (usually the district duty).
 - ii. Term and termination provisions. Termination should include significant demonstrable breach of duty by either party, bankruptcy, etc., with right to cure over a reasonable period of time.
 - iii. Clear delineation/separation of building owner duties and operator duties.
 - iv. A provision that delineates the patient quality and safety obligations of the operator.

- v. The provision for employee transitioning to the new operator, often including a reasonable level of employment preference in the new organization for all employees in good standing.
 - vi. Timeline for integration of the two organizations, including what systems and services will be integrated and which will remain quasi-independent, if any.
 - vii. Elected district representatives will come and go over the life of the agreement. The agreement must be written to withstand/minimize challenges from commissioners who are not supportive of the agreement.
 - viii. A minimum level of investment in equipment and small remodels by the operator should be required.
4. If there is a non-profit foundation associated with the district hospital, the district foundation bylaws should support and be aligned with the operating entity.
5. A stand-still period and negotiating exclusivity should be required once a Letter of Intent is agreed by the parties.

Ten Steps to Successful Affiliation

1. Understand that a hospital merger or affiliation means changes for everyone.
2. Loyalty to mission and community must supersede loyalty to the institution.
3. Clearly define principles and goals of affiliation, then clearly define power and control in the initial documents.
4. Boards need to take the lead.
5. Change means casualties, but service to the community via appropriate institutions is more important than individuals.
6. Identify deal breakers early on and be explicit in stating them.
7. Involve key decision-makers and stakeholders early on and often.
8. Involve the medical staff, especially when an individual hospital is at the center of the affiliation.
9. Develop a critical pathway to the final decision, structuring key decision points along the way.
10. Always keep in mind congruence of culture and values with the affiliating organizations.