

Notes for Hospital Lease, LATA and Administrative Assistance
September 24, 2012

INTRODUCTION

- The past and current Board of County Commissioners (BOCC) has been consistent with their guidance to Teton Valley Healthcare (TVHC) Board of Trustees (BOT) that we want a Conversion to a Non Profit Entity for some of the following reasons:
 - Idaho election laws have changed so that supplemental tax levies can only be placed on the May or November ballots. [For example, what the County did in 2008 (August Election) would not be possible and TVHC would have had to survive for 18 months without County assistance.]
 - A Hospital Tax District with a permanent tax base would have a difficult time to pass because it requires a super majority. [Last levy 1164 Yes - 1,040 No 52.8%]
 - Selling/privatizing the Hospital would mean a total loss of local control.
 - Idaho Statute 31-3515A provides a methodology to make a nonprofit Hospital but requires Local member board.
 - TVHC [the current hospital] is a larger operation than the County and provides essential services to the public but the County does not have the tax base or reserves to finance TVHC.
 - Health Care is very complex and is undergoing many complex changes which the County does not have the resources to dedicate to manage on day to day basis.
 - Hospitals across the country are undergoing many changes in governance and management structures. We are not the only people looking at new management structures.
 - We would like to formally expand our service area so Alta residents can participate in the new organization. The 2008/2009 \$4 million debt could have bankrupted Teton County if voters had not passed emergency levy.
 - The County needs to minimize their financial liability because we provide many other essential services that are required by law.
 - We believe with the hard work of the TVHC staff and BOT over the past 4 years plus the \$4.8 million tax payer infusion TVHC is in a financial position to operate as an independent entity.
- The Conversion to a Nonprofit has many timing issues and has required great effort.
- The Lease Agreement and Liquid Asset Transfer Agreement (LATA) detail the legal agreement between TVHC, Inc. and Teton County.

99 YEAR LEASE:

- The county shall retain ownership of all assets (real, personal and original working capital), including future leaseholder improvements and acquired assets (Article 2.3 defines);
- Teton Valley Healthcare (TVHC, Inc.) (nonprofit entity formed in January 2012) will manage and operate these assets in such a manner to protect the interests of the

county and carryout the original mission of the hospital (Lease Article 2.4, & most of Article 3);

- TVHC, Inc. must comply with numerous protective covenants of its 99 year lease with Teton County or face default of the agreement (Lease Article 7.1);
- The lease agreement provides adequate protections for Inc. to reasonably carry out its business without fear of future political changes to the Teton County governing (Article 4).
- TVHC, Inc is required to reinvest into the Hospital capital assets equal to its depreciation rate.
- TVHC, Inc is required to provide Quarterly Financial reports and Audited Annual Financial report. (Article 4.1)
- The base rent of the lease is \$1 per year (Article 2.6).
- Should Inc. default on provisions of the lease, the lease will be terminated, Inc. will dissolve and Teton County will take back possession of the assets (Article 7).
- Provisions limiting indebtedness have been added (Article 4.18).

LIQUID ASSET TRANSFER AGREEMENT:

- The hospital currently has, and thereby Teton County owns, a net positive working capital position in the operation – replacing this position would inflict an undue hardship on Inc. so essentially Teton County is allowing Inc. to ‘use’ this working capital from day one of its new operation. In non-legal simplistic terms, consider this ‘use’ by Inc. to be a loan from Teton County.
- Although the hospital serves the ‘greater good’ principle, both parties recognize and accept that its operation is a business. As such and in lieu of a stated rate of return, the lessee will compensate the lessor for the use of its liquid assets to operate this business. The annual base payment is minimal (i.e. \$70K for each year of operation under the lease). But the county can/will participate in the financial success of Inc. by receiving annual ‘bonus’ payments if/as Inc. produces net operating profits. The bonus payment is capped at 5% of net operating profit. In essence, these payment provisions transitions the hospital from a ‘public agency’ like status that has asked for and received public tax payer support to one of a private status that will pay something back to its owners (essentially the public) for its investment in the operation. Donations from TVH Foundation and grant money are not included in this provision.
- The BOCC has decided to establish a special reserve fund to hold payments received under this agreement. The concept is essentially one known as a ‘rainy day fund’ to ensure the best Health Care for the County. Future BOCCs can/may change this mandate but it is important that present Commissioners think that this money should be used to improve medical services to our constituents.

ADMINISTRATIVE ASSISTANCE

The BOT confirmed four directions with priorities for our new CEO Keith Gnagey on August 11, 2012:

1. Provide and maintain quality health care.
2. Complete the conversion to a nonprofit entity.
3. Adopt an Electronic Medical record Implementation plan with BOT approval.
4. Strengthen our administrative capability to support our quality health care.

Background:

Necessary changes and improvements in administrative changes have been an issue since October 2007. Both BOCC and BOT have made many difficult decisions without adequate information. The following provides a sequence of events that continue to this day.

- July 2008, TVHC CEO approached BOCC about a taxpayer levy or a possible bankruptcy.
- August 2008, taxpayer levy passes for 2 years at \$1.4M per year and BOCC loans \$400K to TVHC with support from 62.2% of voters (836 Yes – 509 No).
- November – December 2008 TVHC strategic plan drafted with Community input and includes recommendation to review different governance models.
- January 2009 TVHC asks TVHF for transfer of unrestricted monies.
- January 2009 TVHC uses 1st installment of levy to stay afloat.
- January – February 2009 new BOCC asks what liabilities and cash flow needs are at TVHC and administration can't answer. BOCC asked how TVHC will collect \$4 million in uncollected revenue and administration can't answer.
- Key Bank continues to call in Line of Credit and no other Bank willing to loan money.
- February 2009 TVHC CEO leaves and BOT member assumes interim CEO position.
- March – April 2009 BOCC hires outside consultants a northern Idaho Hospital CFO and Health Capital Group to get financial information.
- February – June 2009 BOT solicits help from local hospitals and outside groups without written scope.
- April 2009 BMH volunteers to help TVHC by supplying expertise in operational aspects.
- After numerous meetings considering employee input and public input, BOT selects BMH for consulting agreement.
- June 2009 Interim CEO and BOT committee start research into nonprofit entity.
- Summer 2009 BOT starts search for new CEO.
- December 2009 BOT selects new CEO. Some employees and public lobby to retain interim CEO.
- January 2009 - June 2009 transition with two CEOs in place with intent to fix billing.
- Summer 2009 BOT and BOCC try to get Tax Anticipation Note because TVHC had no ability to produce a cash flow model.
- Dec. 2009 special BOT committee recommended the most appropriate long term legal form for the hospital was nonprofit entity. This matter was tabled in favor of resolving more immediate cash flow issues at TVHC.
- June to December 2010 a Forensic Audit was performed on TVHC billing due to identified billing problems.

- Dec. 2010 TVHC nearly ran out of money again.
- BOT prepares a Plan B and stresses with CEO that TVHC cash position needs to change or new management will be needed.
- February 2011 new controller was hired for TVHC.
 - In mid 2011, the BOT determined that TVHC lacked the staff expertise to lead the EMR conversion process and comply with federal records requirements.
 - In July 2011, the BOT, staff and providers were lectured by a renowned expert in the field of hospital efficiency that most hospital problems are caused by flawed systems.
 - In late 2011, management informed the BOT that TVHC's billing system (already outdated and causing A/R and collection issues) could not be upgraded for any reasonable cost. BOT stressed that EMR needs to provide a robust and integrated billing and financial system.
 - In late 2011 a trend of medical and business affiliation became apparent in the health care industry, particularly as the largest ID hospital increased its takeover efforts and a regional hospital acquired a clinic in the TVHC market area.

Health Service Health Management Agreement

Based upon these conditions, the BOT concluded that TVHC remaining independent would likely not produce the operating results desired and more importantly, if the nonprofit conversion were not completed, would continue to expose the county to serious financial risk (even with the conversion, the privately operated hospital would have financial risk). Thus, the BOT sought to complete the restructuring of TVHC in a manner to permanently fix past problems and position the entity to remain viable into perpetuity. The BOT concluded that the fastest most efficient way to resolve its administrative/systems issues was to seek a business affiliation. The specific goals desired from such an affiliation were/are to achieve:

- Proven executive experience and execution in the health care industry;
- A deeper bench strength of administrative staff and support for the operations;
- Successful systems that increased the operating efficiency of the hospital.

Numerous hospital operators exist in the business that could provide these goals but in mid 2011 only BMH exhibited any interest in a business affiliation with TVHC. Discussions with BMH ensued during late summer 2011, as a part of the BOT's overall plan to complete the restructuring of TVHC and the results were well publicized and documented in a document called the Conversion Agreement (CA) that was approved by BOCC. Within the CA the concept of a business affiliation was developed via a Hospital Management Health Services Agreement (HMHSA). Key concepts of the draft HMHSA were/are:

- BMH would be responsible for the operation of TVHC, Inc. (the new hospital entity after legal conversion) and ensuring its mission statement was accomplished;

- The TVHC, Inc. board would approve the selection of the on-site senior administrator, annual budgets, capital spending plans and macro strategic direction of the operation as developed and proposed by BMH;
- TVHC, Inc. would pay BMH a base management fee and incentive fee annually for carrying out its responsibilities in the HMHSA;
- Upkeep, capital additions and leasehold improvements will be the responsibility of BMH to implement and execute on behalf of TVHC, Inc.
- TVHC, Inc. shall utilize a BMH sublicense on the McKesson software to accomplish its EMR requirements.
- Default and termination provisions exist for both TVHC, Inc. and BMH performance.
- Should TVHC, Inc. default in its lease obligations to Teton County, BMH would have the first right opportunity to purchase the hospital assets should Teton County desire to sell these assets.

Current Status with BMH

Technically, the CA terms have been breached because conversion of the hospital entity, executing a long term lease/LATA with Teton County and executing a HMHSA with BMH will not happen by the original term date of Oct. 1, 2012. There are numerous contributing factors to this breach but the prime factor is that management representing the interests of TVHC did not complete the planning required for an October 1 nonprofit conversion and the required due diligence of EMR software. In June 2012, BOT moved to table HMHSA for at least six months. In late July 2012, BMH agreed to modify the term dates for executing the HMHSA within the CA to late February 2013. Implicit to this modification is the need for TVHC, Inc. (still operating as TVHC) to complete its EMR due diligence. The BOT reorganized management of TVHC in Aug. 2012, in part, to ensure these tasks are indeed accomplished on a timely basis. BMH has agreed to help as appropriate with this effort.

Additional administrative strength is still essential for the long term success of Hospital and the ability to be prepared for the future changes in health care. In July 2012, TVHC wrote off \$115,000 for insurance billing errors and \$183,000 for bad debt. The total amount of bad debt write-off year to date 2012 is approximately \$1.8 million. If we don't choose to go with BMH with its proven track record working with us, we could develop detailed requirements and solicit management companies such as Quorum, Geisinger Health, Health Company of America and/or local hospitals. The lack of staffing depth is inherent in the operation of a hospital our size. Its impact has recently been demonstrated with the resignation of our recently promoted CFO, requiring a temporary CFO to fill the gap created. TVHC, Inc. Governance Board is committed to completing the restructuring of our local Hospital and will develop detailed plans with contingencies as we progress.