Health System Consolidation:
Implications for Baystate Health

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President & CEO

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What Is Driving Partnerships?

In search of...

- Economies of scale (e.g., admin, purchasing, IT, etc.)
- Partnership in/ownership of a health plan or licensed insurance product
- Critical mass of Primary Care Physicians across broad geography
- Clinical integration to become part of ACO/contracting entity
- Clinical excellence across the Network (e.g., superior outcomes at lower cost)
- Infrastructure to manage population health
Bombarded With Messages

Consolidation pace quickens...
Providers ink 93 transactions in third quarter [2013]


Some Recent Mega-Deals

CHP to assume minority ownership (30%) of Summa

Q3 2013

Significant Changes In Largest Markets

Reconfiguration in the Top 75 Metropolitan Statistical Areas in 2003-2011 was more dramatic and driven by three forces:

<table>
<thead>
<tr>
<th>Growth/Formation of Local and Regional Systems</th>
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<tbody>
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<td>• 130 independent hospitals joined systems between 2003 and 2011</td>
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<th>Independent Hospitals Joining Systems, 2003-2011</th>
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<tr>
<td>Local Competitor 35%</td>
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<td>Top 20 System 15%</td>
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<td>Regional System 50%</td>
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<th>Continued Catholic Consolidation</th>
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<td>U.S. Catholic Healthcare Systems</td>
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<td>1987 78</td>
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<th>“Active Portfolio Management” by Top 20 Systems</th>
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<td>• Exiting non-core markets</td>
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<tr>
<td>• Examples: CHP leaving Knoxville, TN; Tenet leaving LA, New Orleans, Miami, Philadelphia</td>
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<td>• Achieving scale and/or market influence in core markets</td>
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<td>• Examples: Ascension in Birmingham, AL; HCA in Denver</td>
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<td>• Expansion into specific markets, e.g., Trinity in Chicago</td>
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Springfield is the nation’s 86th largest MSA

Relatively Slow Movement of Independents to Systems

More community hospitals joining systems

- Between 2009 and 2012, 208 formerly independent hospitals joined systems.

- Between 2008 and 2012, growing portion of community hospitals in systems.


“For in many of these acquisitions, managerial intellect wilted in competition to managerial adrenaline.

The thrill of the chase blinded pursuers to the consequences of the catch.”

Warren Buffet, 
1983 Annual Chairman’s Letter
Berkshire Hathaway
Selected Failed Mergers

**1994-1997**
- "Too far away, philosophically & geographically"
  
**EGISINGER**
- Economies of scale not realized
- Cultural differences (academics vs clinicians)
  led to persistence of two clinical organizations
- Lack of PA community provider support

**1997-1999**
- "Too far away, philosophically & geographically"
  
**Atius Health**
- "Too far away, philosophically & geographically"
  
**Lahey Clinic**
- "Too far away, philosophically & geographically"
  
**Economies of scale not realized**
- Cultural differences (academics vs clinicians)
  led to persistence of two clinical organizations
- Lack of PA community provider support
Source: Managed Care, Nov 2003.

**2014**
- Discussions failed over "who would lead the new organization and serve on its board"

Repercussions of a Failed Merger

- Damaged reputations & lost community good will
- Ability to recruit and retain physicians, employees & Board Members
- Financial costs of diligence, as well as potential "break-up" costs
- Not all CEOs/leaders survive a failed merger

## Potential Approaches: Prototypes

<table>
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<tr>
<th>Description</th>
<th>Autonomy Retained</th>
<th>Autonomy Compromised</th>
<th>Autonomy Relinquished</th>
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<tr>
<td><strong>Alliances/Networks</strong></td>
<td>Collaboration around areas of mutual benefit</td>
<td>Merger or JOA* with Smaller Organization</td>
<td>Merger into Larger Organization</td>
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<td>Many currently focusing on contracting as “select network,” developing population health tools, or launching health plan; sharing best practices; economies of scale</td>
<td>Preferred partnership for affiliations but no loss of autonomy. Traditionally clinical. Increasingly around development of Clinically Integrated Networks/contracting partnerships, IT/EHR, Quality, service development. Can include one or more Joint Ventures.</td>
<td>Merger, JOA or acquisition in which independence (for smaller entity) is traded for security. For larger entity, dominant, if not exclusive, governance role within overall governance structure.</td>
<td>Merger, JOA or acquisition in which independence is traded for increased critical mass. Negotiated governance role within larger overall governance structure. Best practices would create a new unified governance structure with few layers and new Board members.</td>
</tr>
<tr>
<td><strong>Enhanced Access to Capital</strong></td>
<td>None</td>
<td>Limited unless smaller party has stronger financial position than parent (rare).</td>
<td>Potentially, if right partner selected.</td>
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*JOA – Joint Operating Agreement, also known as a “virtual merger”*
Alliances or networks other regional providers often focus on creating a “value network” and/or developing population health management capabilities. These networks often partner with insurers or leverage health plans owned by one or more members to create select or narrow networks of providers.

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<td>✓ Lowers individual organization’s financial risk of creating population health infrastructure.</td>
<td>✗ Similar to “Super-PHOs” of 1990s, most of which have disbanded.</td>
</tr>
<tr>
<td>✓ Appeals to stronger organizations uninterested in merging/forming integrated health system – may provide a springboard for tighter alignment down the road.</td>
<td>✗ Cumbersome structure of independent organizations, each of whom will act in own self-interest.</td>
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<tr>
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<td>✗ Organizations are competitors and, without assuming significant risk, may face anti-trust challenges.</td>
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Hospitals/Health Systems
- Atlantic Health System (NJ)
- Hackensack University Health Network (NJ)
- Lancaster General Health (PA)
- Lehigh Valley Health Network (Allentown, PA)
- Meridian Health (NJ)
- Reading Health System (PA)
- WellSpan Health (York, PA)

Creating foundational changes in health care quality and healthier communities in the Northeast

AllSpire Health Partners is an alliance of seven health care systems that have come together to serve patients, families and communities in New Jersey, New York, Maryland and Pennsylvania. At its core, AllSpire seeks to improve the quality, affordability and access to health care by sharing clinical, intellectual and economic capabilities. This new consortium will undertake joint activities in key areas of population health management, patient care services, research and education to enhance the value of health care for more than 9 million people in the communities we serve.

Source: AllSpire Health Partners Web site.
Description of Option

Multiple affiliations and/or JVs with a single organization while each maintains its independence under a master affiliation agreement (MAA). Typically each organization looks to the other first for services/ventures needed.

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<td>✓ Move toward aligning when one or both organizations not ready to merge since it maintains “status quo” in terms of governance and management.</td>
<td>✗ Questions about long term sustainability.</td>
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<tr>
<td>✓ May build “trust” and relationships to support more tightly integrated model.</td>
<td>✗ Independent organizations cannot collude or even appear to collude (e.g., need arms’ length transactions).</td>
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<tr>
<td>✓ Potential to share capital costs associated with investments via selected JVs.</td>
<td>✓ Each organization will act in own self-interest.</td>
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<tr>
<td>✓ Potential to access corporate expertise more easily.</td>
<td>✓ Complex to manage multi-relationships, especially when parties’ objectives may conflict.</td>
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<tr>
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<td>✗ Limited economic alignment.</td>
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<td>✗ Capital access limited to individual joint ventures.</td>
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The affiliation agreement includes service line arrangements and describes the intent of the hospitals to offer varied clinical services in several areas, with cardiology services and pediatric surgery already underway. The parties have agreed to explore additional joint clinical practices, shared satellite healthcare centers, and collaboration on clinical research... John Hopkins University physicians manage GBMC’s Cardiac Care Unit, oversee cardiology services in GBMC’s Emergency Department and supervise all heart-related inpatient and outpatient testing.

Anne Arundel Medical Center (AAMC) and Johns Hopkins Medicine renewed their strategic alliance agreement in January 2012. AAMC and Hopkins formed the alliance in 2007.

The wide-ranging strategic agreement includes a shared focus on health care reform, the potential of joint clinical programs, satellite health care centers, collaboration on clinical research, and exploration of the development of joint physician graduate medical education programs.

Based upon GBMC press release, July 2007
## Description of Option

A smaller hospital, provider organization, or health system merges into or enters into a Joint Operating Agreement (JOA).

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<td>✓ Alignment of mission and vision in corporate model.</td>
<td>✗ Many smaller organizations seek merger option only when they need access to capital/are financially challenged. Depending on partner, may weaken balance sheet and/or reduce access to capital.</td>
</tr>
<tr>
<td>✓ Ability to execute through unified governance and management structure.</td>
<td>✗ Local community opposition to larger health system governance/control.</td>
</tr>
<tr>
<td>✓ Creation of “critical mass” and ability to rationalize/consolidate services if geographically proximate.</td>
<td>✗ “We only wanted your money” can leave smaller entity resistant to changes once that initial need is met.</td>
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<tr>
<td>✓ Retention of governance, management, and identity of larger entity</td>
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Merger or JOA with Similarly-Sized Organization

Description of Option

Merger or JOA with a similarly-sized organization creates a new organization. Neither organization is dominant; a new image and identity may be created to brand entire health system.

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<td>✓ Create critical mass and, if geographically proximate, could consolidate selected services to improve cost effectiveness.</td>
<td>✗ Potentially difficult to determine governance, leadership structures with two relatively equal partners – no clear “parent” or leader</td>
</tr>
<tr>
<td>✓ Could enhance access to capital (or not depending on partner).</td>
<td>✗ Politically difficult to distribute (rather than duplicate) high-end services between locations.</td>
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<tr>
<td>✓ Possible retention of identity/brand, depending on terms of agreement.</td>
<td>✗ Cultural challenges can be real: similar mission, vision and values may be interpreted in vastly different ways.</td>
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<tr>
<td>✓ Spread corporate and administrative services over a large base.</td>
<td>✗ Hard to find strong, similar sized, interested party!</td>
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The boards of directors of both Rochester systems signed a merger agreement in September 2013 (completed in Summer 2014) that combined the two into one organization under a single parent company with equal representation from both systems. The new system:

- Comprises 5 hospitals spanning 4 counties.
- Is the second-largest employer in the region, with 13K employees.

Includes 528-based flagship Rochester General Hospital, a 120-bed community hospital, Rochester General Medical Group (40 practices), as well as ambulatory and long-term care components.

Includes three hospitals with 703 total beds, as well as ambulatory and long-term care components.

“Mergers of Equals”
Rarely Work Out As Intended

Schumpeter, “Love on the Rocks”
The Economist  5/17/14
Baystate: The Bird’s Eye View

- 4 hospitals with 900 beds, including sole AMC in western MA
- Baycare PHO with 1200 MDs
  - 500 employed MDs
  - 9 practices (34 sites) at level 1 NCQA PCMH certification
  - 60% of patients in alternative payment contracts
- Owned Health Plan (Health New England) with 150,000 lives in commercial, Medicare and Medicaid product lines
- VNA, hospice, infusion services
- Health Information Exchange
Prom Queen or Trojan Horse?

- Strong fundamentals in quality & finance with unusual system discipline
- LEAN PI infrastructure
- Far along in adaptation to health reform
- Market dominant
- Likely to experience $100M in cuts due to Rural Wage Index, DSH cuts and GME cuts
- High Medicaid mix but shut out of Mass waiver
- New competitors
- New management team and new strategic plan
Each Bar Represents 385 discharges from FY 2013 (1%)
Height corresponds to total operating margin per case
Partnerships are a means to an end.

That end is the value they bring toward the fulfillment of the mission

1. What do we want from a strategic partnership?

2. What do we need from a strategic partnership (i.e., we would not pursue this relationship unless it offered us the following…)?

3. What value do we bring to the partnership – and what would we like our future partner to recognize as the value that we bring?