How Affiliations Can Strengthen Organizations for the New Healthcare Era

Findings from HFMA’s Phase 3 Value Project Research

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Value Project Phase 3: Acquisition & Affiliation Strategies

• The first of five Phase 3 topics
• Based on:
  – Interviews with subject matter experts in strategic consulting, capital formation, and legal and regulatory issues
  – Survey of HFMA senior finance executive members (split evenly between stand-alones and systems/system-affiliated facilities)
  – Site visits and interviews at AllSpire Health Partners, Dignity Health, Froedtert Health, HealthPartners, New York – Presbyterian Hospital, North Shore – LIJ Health System, and SSM Health Care
Value Advisory Group and Sponsors

Research Highlights

- An emphasis on value-focused acquisition and affiliation strategies
- An understanding that different needs require different approaches
- The emergence of new organizational combinations
- A blurring of lines between competitors and collaborators
- The need to change governance and organizational structures as systems change
High Degree of Acquisition and Affiliation Activity

- Entered into an arrangement in the past five years: 42%
- Considering an arrangement in the next 12 months: 34%
- Open to an arrangement longer term (e.g., beyond 12 months): 30%
- None of the above: 19%

Note: Respondents could choose more than one answer.

Drivers of Acquisition and Affiliation Activity Today
HFMA Survey: Cost Efficiencies and Competitive Position Are Lead Drivers

What are the most important reasons for an organization to consider a new organizational arrangement?

- Cost efficiencies/economies of scale (58%)
- Improved or sustained competitive position (51%)
- Physician network/clinical integration (35%)
- Ability to manage the health of a defined population (28%)
- Access to capital (23%)
- Risk contracting experience (5%)

Interviews and Site Visit Research Identified Similar Internal Drivers

- Improving operational efficiencies
- Creating clinically integrated care delivery networks
- Accessing sufficient networks for population health management
- Developing or acquiring new capabilities (e.g., physician practice management, health plan experience, etc.)
- Rationalizing service lines or assets
For Stand-alone Facilities, the Need for Greater Efficiencies/Economies of Scale Stands Out

- Access to even broader populations to sustain full range of tertiary/quaternary services
- “Right place” pressures to perform lower acuity procedures in lower cost settings
- Maintenance of strong brand in their marketplaces (which may be local, regional, and national)

Academic Medical Centers Also Have Unique Acquisition and Affiliation Concerns

- Access to even broader populations to sustain full range of tertiary/quaternary services
- “Right place” pressures to perform lower acuity procedures in lower cost settings
- Maintenance of strong brand in their marketplaces (which may be local, regional, and national)
A Significant Trend

Mergers and acquisitions are occurring more frequently between organizations that are both financially strong

- Driven by strategy more than financial need
- Financially weaker organizations are more attractive if they possess other strategic assets: market position, affiliated physician networks, outpatient clinics, good payer mix

Organizations Look to Improve a Wide Range of Capabilities Through Acquisition or Affiliation Activity

<table>
<thead>
<tr>
<th>Capability</th>
<th>Improvement Expected</th>
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<tbody>
<tr>
<td>Management and restructuring of costs</td>
<td>65%</td>
</tr>
<tr>
<td>Patient population data analytics across organization</td>
<td>57%</td>
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<tr>
<td>Management of care continuum by physicians</td>
<td>57%</td>
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<tr>
<td>Optimization of service distribution across facilities</td>
<td>55%</td>
</tr>
<tr>
<td>Common clinical protocols across locations</td>
<td>51%</td>
</tr>
<tr>
<td>Management of risk-based payment</td>
<td>50%</td>
</tr>
<tr>
<td>Supply chain management</td>
<td>42%</td>
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<tr>
<td>Revenue cycle management</td>
<td>41%</td>
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</tbody>
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Drivers Are Influenced by Multiple Factors . . .

- Local market conditions
- Existing and desired organizational capabilities
- Organizational type (stand-alone vs. system, academic medical center vs. community hospital)
- Senior leadership and board sentiments

. . . And Can Be Countered by Obstacles to Acquisition or Affiliation

- Governance issues/desire for local ownership*: 65%
- Cultural fit between organizations: 68%
- Physician opposition: 22%
- Inability to integrate information technology: 19%
- Management concerns about retaining their positions: 14%
- Concerns about FTC response: 7%
- None: 2%

*Ranked 1&2
Acquisition and Affiliation Options

Traditional M&A Activity Leads, But Multiple Models Are Being Pursued

Which of the following options best describes the most significant type or arrangement your organization has pursued or is pursuing?

- Acquired by/merging into another hospital/health system
- Acquiring/merging with another hospital/health system
- Joint operating agreement with another hospital/health system
- Part of an ACO with another hospital/health system
- Joint venture with another hospital/health system
- Management services agreement with another hospital/health system
- Other

0% 10% 20% 30%

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Two Possible Paths to Greater Economies of Scale

- Seeking scale through geographic breadth
  - Good potential to gain operational efficiencies
  - Fewer antitrust concerns
  - Potential difficulty building sufficient presence in local markets

- Gaining economies within more local or regional markets
  - Opportunities for greater clinical integration
  - More potential to optimize and rationalize services and staffing across locations in the market
  - Greater risk of antitrust scrutiny
Other Trends

- Diminishing significance of not-for-profit/for-profit status of potential partners
- Vertical integration activity (a health system acquiring a health plan or multi-specialty physician practice)
- Investment in disruptive innovators/new technologies
- Diminishing appetite for hospital-heavy acquisitions
- Collaborative partnerships

A Closer Look at Collaborative Partnerships

- Offer possibility of adding scale without ceding control; question is whether there is enough “glue”
- Initial focuses include:
  - Group purchasing activity
  - Back-office functions
  - Sharing of best practices (both operational and clinical)
  - Forming accountable care structures for risk-sharing managed care activities
- Not yet on the agenda:
  - Decisions on which services should be provided by which organization
  - Control over clinical decision making
  - An integrated financial bottom line for the partnership
How Does an Organization Identify the Best Options and Partners?

- Three Key Questions:
  - Can my organization remain successful in its current configuration?
  - If not, based on critical success factors and organizational goals, what type of partnership makes the most sense?
  - What partner can best help my organization accomplish its goals?

How Does an Organization Determine Its Future Course?

- What business or businesses am I in?
- What is the growth trajectory for this business, and how can I best invest in areas with the highest growth potential?
- Do I have the right executive team and governance structure in place to position for the future?
- What forms of affiliation should we consider or engage in?
- What can we stop owning, and instead obtain through partnership or outsourcing?
Does Organizational Type Affect Acquisition and Affiliation Options?

• Academic medical centers and children’s hospitals
• Aligned integrated systems
• Multihospital systems (local, regional, national)
• Rural hospitals
• Stand-alone hospitals
• Others?

Concluding Thoughts and Questions

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