



**House
Legislative
Analysis
Section**

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THE APPARENT PROBLEM:

In response to problems faced by communities in financing hospitals, Public Act 47 of 1945 was enacted to provide for the establishment of joint hospital authorities, which are the entities formed when two or more cities, villages, or townships band together for the purpose of owning and operating a hospital. The organizations functioned well for almost four decades, fulfilling community demand for access to health services, and operating profitably under the cost-based reimbursement system. Regulatory and economic protections also insulated the hospitals from competitive market pressures.

Changes in the health care industry, however, have caught up with the hospitals, especially in the past five years. Since an authority is comprised of municipalities, an authority-owned hospital is designated as a "public agency" and cannot own corporate stock. In addition, authority-owned hospitals are barred from a wide range of diversification options: operation of off-site facilities such as medical laboratories, nursing homes, and clinics, as well as joint economic ventures such as the development of homes for the elderly. Some contend that such restrictions leave community/authority-owned hospitals at an economic disadvantage, since private and nonprofit hospitals are not restricted in these ways, and thus enjoy a competitive edge over their publicly-owned counterparts within the increasingly competitive health care industry. In addition, developments in the health care industry in recent years have increased the competitive nature of the industry. Changes in the way hospitals are reimbursed for their services, i.e., the predominance of the use of diagnostically related groups (DRGs), rather than "cost based" payment, and the types of services supplied (e.g., outpatient surgery, ambulatory care, and outpatient services) have greatly affected the way hospitals must operate.

Such developments have given rise to a need for diversification and innovation in the health care field. Recognizing this, Public Act 117 of 1987 amended the act to allow nine hospital authorities in the state that had member populations of less than 300,000 to sell, lease, or transfer a hospital within the authority to a nonprofit corporation. By limiting this provision to hospital authorities with service area populations of less than 300,000, the legislation excluded only the People's Community Hospital Authority (PCHA), which consists of five community hospitals and a freestanding ambulatory care center in eastern Washtenaw County, and western and downriver Wayne County. (At the time, PCHA had not yet decided whether it should sell its assets or reorganize into a private, nonprofit, tax-exempt corporation). PCHA recently decided that its best course would be to affiliate with a tertiary facility, and has now entered into an affiliation agreement with Oakwood Health Services Corporation, contingent upon legislation being passed that would grant it the same status as the other community hospital authorities in the state.

PEOPLES COMMUNITY HOSPITAL TRANSFERS

House Bill 5755 with committee amendments
First Analysis (6-20-88)

RECEIVED

Sponsor: Rep. Richard A. Young
Committee: Appropriations

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THE CONTENT OF THE BILL:

The bill would amend Public Act 47 of 1945 to allow a public community hospital established by a hospital authority under the act, whose jurisdiction had a population of more than 300,000, to provide by resolution for its sale, lease, or transfer to a nonprofit corporation. The bill would require that the resolution be adopted by a majority vote of the hospital board. The bill also would set requirements for the nonprofit corporation, set conditions for the sale or lease, and provide for the withdrawal from the hospital authority. The transfer could be for no or for a nominal monetary consideration, subject to all of the following terms and conditions:

a) The sale, lease, or transfer would be to a nonprofit corporation established under the Nonprofit Corporation Act, exempt from federal income tax provisions, and organized specifically for the ownership and operation of the hospital at the time of the sale, lease, or transfer, or within six months after that date.

b) The articles of incorporation of the nonprofit corporation and the contractual arrangements between the hospital authority and the corporation would at all times require that the corporation operate the hospital as a nonprofit community health facility open to the general public that served the general population in the service area of the authority.

c) The articles of incorporation of the nonprofit corporation and the contractual arrangements between the hospital authority and the corporation would at all times require that the nonprofit corporation could not sell all of the transferred assets without the express consent of the authority and the approval by a majority of the voters in an election conducted in the same manner as provided under the act for the approval of an additional tax for capital improvements. If all of the transferred assets were sold under this provision, the sale would be for market value, and the proceeds of the transaction would be turned over to the authority and used for health care needs within the authority service area.

d) The articles of incorporation of the nonprofit corporation and the contractual arrangements between the hospital authority and the corporation would at all times require that the corporation adopt and carry out policies designed to ensure that the hospital complied with Public Health Code requirements that patients not be denied appropriate care on the basis of source of payment.

As used above, "hospital" would include all property, real and personal, tangible and intangible, including without limitation cash, accounts receivable, and pension reserves used in the operation and management of one or more hospitals.

A sale or transfer of a hospital under the bill would not be construed as a violation of the act or of any bond resolution or ordinance adopted under the act, if the authority had

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outstanding self-liquidating bonds, provided that: 1) the outstanding bonds were "defeased" (made null and void), and 2) defeasance of existing bonded indebtedness was accomplished by depositing sufficient cash or United States Treasury obligations, or both, in escrow in an amount sufficient, including interest, to be earned on the funds and obligations placed in escrow, to provide for payment of all interest, principal, and premium, if any, when and as due on the outstanding bonds, including final payment. As used above, "final payment" would mean the final payment due at the maturity of the bonds or upon the redemption of the bonds prior to maturity on a date on which the bonds were callable for redemption if irrevocable arrangements had been made to call the bonds for redemption on that date.

The bill would require that, if a hospital authority passed a resolution providing for the sale, lease, or other transfer of a hospital, then the legislative body of a city, village, or township participating in the hospital authority could, within 60 days after the resolution was passed by the authority, pass a resolution to withdraw from membership in the authority. If the legislative body passed such a resolution, the authority resolution would not be effective until a majority of the hospital authority board concurred in the withdrawal. However, if the sale, lease, or other transfer of the hospital was not carried out, then the resolution to withdraw and the hospital authority's resolution of concurrence in the withdrawal would be void.

MCL 331.9

BACKGROUND INFORMATION:

In April 1987, the Speaker of the House — on behalf of the legislature — requested that a study of PCHA be conducted to analyze its current functions and to assess whether changes in the authority were necessary to ensure the continued fulfillment of the health needs of the people served. The study, conducted by the University of Michigan, was concluded in September, 1987. The study observed:

1. PCHA facilities were in a very vulnerable operating position, with limited market need for services, and faced a difficult set of circumstances, including potential financial insolvency.
2. PCHA was no longer viable as a health care organization on its current path and with its current structure.
3. The opportunities for PCHA to better serve its communities were limited, and would be facilitated by the tight linkage with and overlay of one or more senior partners.
4. The sale of PCHA assets was recommended. Given that sale might not be entirely consistent with other community needs or interests, two secondary alternatives were offered which could achieve a reasonable outcome for the communities.

The secondary alternatives recommended were: a) a tertiary referral center to aid in medical staff development and strengthening, development of clinical programs, enhancing public image, and to provide a teaching affiliation; b) reorganization of PCHA into a private, nonprofit, tax-exempt corporation, which would remove the constraints of the authority's "public" status, and enable a new governance structure and parity in terms of organizational flexibility with competitor hospitals. The study further recommended the a successful outcome under conversion to a private, nonprofit, tax-exempt corporation would be more likely if coupled with the formation of a trustee relationship with a tertiary care center.

5. Given the grave financial projections for PCHA and the necessary time for any change to occur, it was recommended the the legislature take decisive action in the next 90 to 120 days.

FISCAL IMPLICATIONS:

According to the House Fiscal Agency, the bill would result in no fiscal impact to the state. (6-15-88)

ARGUMENTS:

For:

Changing market conditions have motivated Peoples Community Hospital Authority (PCHA) and Oakwood Hospital to strive to maintain an adequate supply of primary, acute, and tertiary services for persons in their respective service areas. To develop a tertiary facility, Oakwood Hospital needs additional primary and acute care facilities, and PCHA needs to affiliate with a tertiary care facility and to upgrade its medical staff. Through their proposed affiliation agreement, each institution believes it will achieve its goals: Oakwood and the new corporation will use all facilities now owned and operated by the parties, as part of a total health delivery system; the infusion of \$25 million in capital will allow PCHA to improve its facilities and provide training to upgrade its medical staff.

For:

By allowing the sale, lease or transfer of an authority-owned hospital to a nonprofit corporation, the bill would give hospital authorities many opportunities to develop and to compete. Many feel that this is the only way that publicly-owned hospitals can survive and continue to provide health care to their communities.

For:

The bill would provides safeguards against side-stepping the wishes of the residents of the community-participants of the hospital authority. Before a hospital could be sold, leased, transferred, or transformed, the authority would be required to secure the approval of the voters of the affected municipalities. In addition, the nonprofit corporation would have to deposit into escrow sufficient funds to cover bond obligations.

Against:

As written, the bill contains no provision that would require PCHA to provide services to indigent patients. Since the other hospital authorities covered by Public Act 45 are required to provide this care (Public Act 117 of 1987 contained a provision that hospital care was to be provided "to a reasonable degree to indigent persons") why should PCHA be excluded?

Against:

The bill fails to address the state of contractual agreements between the hospital and employees, such as those involving pensions, pay rates, and benefit packages. Public Act 117 contained a provision which protected the interests of a hospital's employees by requiring the nonprofit corporation or subsequent entity to abide by an existing labor agreement for the term of that agreement. As written, House Bill 5755 contains no such provision.

Response: An amendment proposed by the sponsor would address this issue.

MORE

Against:

Why convert public assets into private assets? The construction and operation of these facilities were funded through the use of tax revenue and should be governed by the community. The provisions of the bill would turn over public assets to private, self-interested parties. It would be a case of robbing from the public coffers.

Response: The sale, lease, transfer, or transformation of a hospital to a nonprofit corporation would have to be approved by the voters of the participating communities. The major benefit to the public would come in the form of a better, more efficient, more up-to-date hospital.

POSITIONS:

The Department of Management and Budget supports the bill. (6-16-88)

The Service Employees International Union, Michigan Council, supports the bill, provided that it is amended to include the same contract protections of Public Act 117. (6-16-88)

The Michigan Hospital Association supports the bill. (6-16-88)

The Michigan Association of Community Hospitals and Physicians supports the bill. (6-15-88)

The Peoples' Community Hospital Authority supports the bill. (6-16-88)

The Department of Social Services has no position on the bill. (6-16-88)

The Department of Public Health has no position on the bill. (6-14-88)

The Department of the Treasury has no position on the bill. (6-13-88)

The Comprehensive Health Planning Council has no position on the bill. (6-15-88)

Citizens for Better Care has no position on the bill. (6-16-88)

The Michigan Health Council has no position on the bill. (6-20-88)

The Michigan Nurses Association has no position on the bill (6-20-88)