

The Regents of the University of California

COMMITTEE ON HEALTH SERVICES

September 17, 1999

The Committee on Health Services met on the above date at UCSF - Laurel Heights, San Francisco.

Members present: Regents Atkinson, O. Johnson, Khachigian, Kozberg, Leach, Montoya, Preuss, Sayles, and Vining; Advisory member Kohn

In attendance: Regents Bagley, S. Johnson, Lee, Nakashima, Pannor, Parsky, and Taylor, Regents-designate Coleman and Cowan, Secretary Trivette, General Counsel Holst, Assistant Treasurer Young, Provost King, Senior Vice President Kennedy, Vice Presidents Darling, Gomes, Gurtner, Hershman, and Hopper, Chancellors Bishop, Greenwood, Orbach, Tomlinson-Keasey, Vanderhoef, and Yang, and Recording Secretary Bryan

The meeting convened at 10:00 a.m. with Committee Chair Khachigian presiding.

1. UPDATE ON UCSF STANFORD HEALTH CARE AND CHILDREN'S SERVICES

Vice President Gurtner presented a brief progress report on UCSF Stanford Health Care. He noted that a report would be presented in October that examines the elements of the organizational structure of UCSF Stanford Health Care. The objective of the report is to develop a recommendation as to the appropriate structure to protect UCSF's academic research and clinical missions and maintain and enhance the financial achievements of UCSF Stanford Health Care, and to reaffirm the vision and mission of the merger. Options to maintain, dissolve, or modify the merger will be considered.

Mr. Gurtner recalled that a State Auditor's report concerning the merger indicated that, although the original business plan was sound, there were some problems, the first of which was that there was a failure fully to integrate faculty during the first 18 months. Also, there were unanticipated merger costs, deteriorating reimbursement rates, and a lack of timely financial information. The report demonstrated the complex challenges academic medical centers face nationwide. The implementation of the Balanced Budget Act over a five-year period will have a dramatic financial effect on the University's five medical centers, which serve a large managed-care population. California has the third lowest Medi-Cal rates in the nation and is the only state requiring SB 1953 seismic retrofits, the cost of which will be substantial. As the national debate about the funding of medical education expands, attention is being drawn to the inequities among various parts of the country in the way in which Medicare funds medical education. The conclusion of the Auditor's report was that UCSF and Stanford must implement survival strategies, whether alone or separately. The additional savings that are projected to be

achieved at UCSF Stanford by 2001 are based on the recovery plan assembled by The Hunter Group, but they will be possible only if revenue enhancement and cost savings are achieved. Decisions will need to be made as to how to protect each party in the event that substantial disproportionate losses occur in the future, and it may be necessary to modify the accounting and management structures. He noted that the current affiliation agreement may not be modified without the approval of The Regents.

Chancellor Bishop stated that it is imperative for both UCSF and Stanford that their hospitals thrive. He expressed his disappointment at the failure to achieve integration on a large scale, but he pointed out some extenuating circumstances, including the fact that a potential dollar value has never been placed on the consolidation. Neither the original business plan, the outside appraisals, nor the latest State audit have done so, although it was claimed originally that the merger would save money. He believed that it is possible that such consolidation might disappoint in a fiscal sense whatever the other benefits of consolidation might be. Also, the merger had only one year to accomplish consolidations. That effort was interrupted when all attention turned to immediate emergency interventions. He reported that in the first year, pediatric programs, which represent one-third of all the business of UCSF Stanford Health Care and which were provided with powerful incentives, took major strides towards consolidation. Several other clinical programs were lined up for possible consolidation before the merger became unstable, and those prospects might be developed if stability returns.

Chancellor Bishop noted that the Auditor's report included some suggestions for helping the situation, acknowledging that the current medical marketplace is punitive for academic health centers. The balanced budget of the federal government has been carved out of health care, and academic health centers are bearing a disproportionate share of that burden. They have routinely provided diverse and crucial social services without adequate compensation. In the past, they have dealt with the shortfall by generating budget surpluses in the profitable parts of the institutions. That is no longer possible, and new support must be found. Otherwise, all academic health centers face extensive restructuring and almost certain diminution. As the Auditor pointed out, the hospitals of UCSF and Stanford will have to continue rigorous controls of cost as well as efforts to increase revenue, irrespective of whether the merger survives or the two medical centers separate.

Dr. Larry Shapiro, Chair of the Department of Pediatrics, reported that some positive developments have occurred as a result of the merger. There has been progress in creating an integrated children's program, the Children's Health Initiative (CHI), within UCSF Stanford Health Care, with the help of the David and Lucile Packard Foundation. A single hospital administrative leadership has been created. There are one chief operating officer for the children's programs, a single director of nursing and patient care services, and an executive operating committee with considerable discretion. There is a single integrated financial statement, and permission has been received from the State Legislature to operate the children's facilities at UCSF and Stanford under a single hospital license. Practice integration has been achieved through the establishment

of cardiac and neuroscience service lines that coordinate the activities of physicians in a variety of departments and across the two campuses in delivering coordinated care to children with cardiac and neurologic disease. One example is the recruitment of the outstanding pediatric electrophysiologist in the country to treat children at both sites. In pediatric general surgery, faculty at both schools have established a joint practice with cross coverage arrangements and the adoption of best practices in the form of standardized clinical pathways to treat a variety of conditions. From the standpoint of training programs, advanced fellowship training has been integrated in six areas: pediatric neurosurgery, allergy immunology, medical genetics, gastroenterology, rheumatology, and academic general pediatrics. Four of these have already secured outside funding to support their educational efforts. All are able to provide more complete training with expanded clinical experiences and widened exposure to excellent inventors. The ambitious goals for the Children's Health Initiative are measurably to improve the health of children in northern California and to assure the academic and clinical preeminence for the children's health programs at UCSF and Stanford.

Dr. Shapiro reported that the vision for the CHI is to address major health needs of children through the collaboration of scientists and clinicians in the community. It is hoped to accelerate the cycle time for discovery, delivery, and dissemination of new information. There is to be a focus on advocacy for children. The development of the CHI began when senior pediatric faculty and campus leaders met repeatedly to identify and assess the major unmet health needs of children. A dialogue was begun with the trustees of the David and Lucile Packard Foundation, which has had a longstanding commitment to children's health issues. An organizational structure was created, a talented administrative staff was recruited, and the assistance of prestigious outside advisors was secured. Late last year, approval was received from the two universities and a commitment from the Packard Foundation to commit generous financial support for the next ten years. Since January faculty have been engaged in the planning and design of the CHI, which will have fundamental and applied research, service delivery, educational, and community service and outreach components. Faculty in all four UCSF schools have been involved.

Dr. Shapiro noted that the pediatric faculty at UCSF strongly support the continuation of the merged clinical program. There are several reasons the children's programs have enjoyed greater cooperation than the rest of the enterprise. There are special marketplace characteristics related to children's medical services. Children's services are present in fewer competing medical centers, and there are highly constrained resources for pediatric specialty care that make cooperation between the two sites effective at providing services that would be difficult for either to provide alone. There is a historic relationship between the two departments of pediatrics. The shared vision for children that has developed between the two faculties has been encouraged by campus leadership.

Regent Lee applauded the initiative and noted that problems of culture and location will need to be overcome throughout the merged entity. He believed that a management team must be built that can move the whole enterprise toward full integration quickly.

Regent Sayles asked whether there is a basis in the UCSF Stanford Health Care agreement for breaking apart the merger unilaterally as opposed to by mutual agreement. Deputy General Counsel Lunderg explained that there is a series of agreements covering the relationship with Stanford University and establishing the nonprofit public benefit corporation. The major consolidation agreement has a provision for dissolution that makes it possible for either party to call for dissolution if the purpose of the merger – that is, the support of the two medical schools – is not being fulfilled or if, based on the financial parameters that exist, there is a significant deterioration in various ratios that measure the financial health of the transaction. If either condition exists, there is the provision for representatives of Stanford and UC to come together and discuss ways in which the issues that relate to the financial problem can be resolved, and if resolution is not possible, either party may choose to dissolve the corporation based on some of the statutory grounds that exist in the nonprofit code of the State of California. Regent Sayles stressed the importance of knowing what the combined entity is expected to do going forward and comparing that with what a breakup would involve. Regent Pannor requested information about how UCSF Medical Center would fare as a stand-alone enterprise. Mr. Gurtner agreed that the first challenge is to assess the future status of the merger and attempt to come to a conclusion with Stanford as to what is in the best interest of both organizations. A recommendation will then be brought to the Regents.

Regent Kozberg asked what steps are being taken to integrate the faculty and workforce at all levels. Chancellor Bishop reported that all efforts at further integration are in suspension until a resolution to the current crisis is found. If the enterprise continues, incentives to integrate will need to be created. Once the organization is sound financially, time and effort can be devoted to creating these incentives. Dr. Lee Goldman, Acting Vice Chancellor for Medical Affairs, noted that, compared to where the merged enterprise was a year ago, the degree of integration currently in place is in line with expectations, based on the experiences of similar mergers.

Regent-designate Kohn noted that the experience gained through the integration of pediatrics programs should provide information helpful to other clinical programs. Dr. Goldman agreed but noted that for a variety of reasons integration may take longer in other programs. Dr. Kohn asked how the geographical separation of the campuses affects integration. Vice President Gurtner commented that the distance was irrelevant for much of the administrative infrastructure. As to the two hospitals, the debate continues as to whether it may be best to view UCSF Stanford Health Care as a merged entity serving two separate markets.

Regent Leach was optimistic that a successful path to the future will be found. He noted that the State Auditor's report was generally positive. He believed that the two hospitals have more to lose by separating than by remaining together. Nearly every academic center nationwide has had to reduce its support of the academic medical

education mission. UCSF Stanford Health Care must find efficiencies or face that threat, and it will need faculty cooperation. He reported that Acting Chief Executive Officer Hunter has been told by the board that his primary objectives are to maintain the quality of medical care and the degree of access to it and to make sure that the enterprise is on a sound economic basis going forward.

[For speakers' comments, refer to the minutes of the morning session of the Committee of the Whole.]

2. **ACTIVITY AND FINANCIAL STATUS REPORT ON HOSPITALS AND CLINICS**

Vice President Gurtner commented on the healthcare marketplace as it relates to the University's hospitals other than UCSF Stanford Health Care. He reported that although the general financial trend from July 1998 to June 1999 seems positive, the margins are declining fast. The current margin of 6 percent is projected to decline to about 4.5 percent next year. Revenues are expected to remain flat or decline. The University's hospitals are struggling to respond to their individual situations in an aggressive market. President Atkinson observed that the issue is national in scope and is not one that can be corrected simply by good hospital management. It is uncertain whether the kinds of support that have been available to medical centers in the past will continue. He believed that there is a national movement to destroy a great medical enterprise that has been very important to the welfare of nation. Regent Preuss acknowledged the effects of the changing face of medicine, but he emphasized that in response to this threat the University must operate its medical centers with a view toward survival. Mr. Gurtner believed that, as funding declines in the coming years, it will be necessary to reassess how medical education is to be delivered.

Assistant Vice President for Federal Governmental Relations Sudduth commented that it is likely Congress will provide some short-term relief this year from the effects of the Balanced Budget Act. This may include a one-year freeze in the reduction of some payments to teaching hospitals. Long term, however, there needs to be a fundamental change in how teaching hospitals are financed at the federal level. He was not optimistic that the efforts of Congress to effect any major overhaul of the system were going to be successful in the near future or were going to result in significant benefits for California.

The meeting adjourned at 11:10 a.m.

Attest:

Secretary