51st ASHE Annual Conference & Technical Exhibition 2014

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Mergers & Acquisitions:

Identifying, Avoiding and Rectifying Pitfalls at the Facility Level

SURVIVAL of the FITTEST

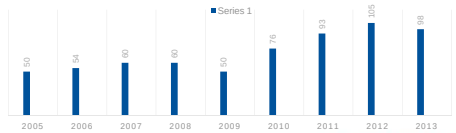
Learning Objectives

- Understand the issues, challenges and pitfalls of mergers and acquisitions at the real estate and facility management (and related operational) levels
- Assess the financial and operational implications that the various pitfalls can have on a hospital/health system
- Understand the key areas where real estate and facility managers can influence the merger & acquisition and/or merger integration process
- Learn the most constructive ways to present the need for proactive assessments, during due diligence or before a "transition" begins

The Healthcare M&A Landscape

	2005	2006	2007	2008	2009	2010	2011	2012	2013
# of Hospitals	50	54	60	60	50	76	93	105	98
Average #	2005-13	72		2010-13	93		2011-13	99	

HISTORICAL M&A ACTIVITY



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M&A Objective based on point of view

Decision making criteria in assessing mergers and acquisitions

How "Consolidators" Evaluate a Potential Acquisition:

- How much and how quickly will acquisition result in increased cash flow? Which expense items will be impacted?
- How difficult are the steps to achieve the desired cash flow? Will implementation be impeded by conditions pre-deal?
- Ability to expand clinical services to the communities they serve, and related contribution to earnings
- Better use of scarce community resources (capital and clinicians)
- Improved care for the vulnerable and other community benefits
- Defensive motivations

Stand-Alone Organizations Looking to Join A System Are Often Seeking:

- Mission compatibility (e.g., not-for-profit vs. for-profit, private vs. faith-based vs. governmental)
- Ensured long term viability
- Access to capital markets / capital infusion
- Generating economies of scale (cost savings)
- Support for physician recruitment and retention
- Clinical, managerial, and technological resources to reduce cost and improve quality
- Defense against competitive threats
- Creative ways to maintain local control (or to maximize sale proceeds)
- Management expertise to navigate health reform

In this round of health system consolidation, assets are not merely being "collected" acquirers have a clear plan to achieve strategic and financial benefits.

C-Suite's rationale for a merger

- **Achievement of scale**
  - Leverage resources and core competencies, reduce duplication of services
- **Financial Performance**
  - Higher margins, stronger contracting position, broader allocation of fixed costs, capital avoidance
- **Geographic and expert expansion**
  - Broader coverage of a geographic market and specialty areas—local, regional and/or national
- **Survival of the fittest**
  - Stave off merger or acquisition by a larger system; "maintain independence"

M&A Implications at the facility level

Potential pitfall areas when implementing C-Suite vision

- Condition of Physical Premises
  - Facility Signage and Branding
- Resources—Human Capital
  - Transition Communications
- Contractual Obligations
- Regulatory & Licensing

Condition of Physical Premises

Identifying the potential pitfalls and implications

Potential Pitfall	Implications
Condition of building shell, walls roof doors & windows	Impact on capital and operations budgets
Condition of existing MEP systems	Impact on capital and operations budgets
Condition of Security and fire systems	Capital expense and integration issues
Ability to support new technology/equipment.	Impact on ability to integrate with system
Signage and Branding	Impact on capital and operations budgets to re brand sites: interior and exterior signage, colors, FFE

Resources—Human Capital

Identifying the potential pitfalls and implications

Potential Pitfall	Implications
Existing staff skills	Are there staff on either organization with the skills needed to maintain the properties?
Existing staff levels	Will combining staff require layoffs? Are there the right staff in the right locations?
Compensation complications	Operating budget implications; shift differential, overtime requirements
Merger of union and non union staff	Appearance of union busting or challenge of unionizing
Transition Communications	Clinical staff usually impacted much less than non-clinical staff, organizations typically focus communications on clinical concerns

Contractual Obligations

Identifying the potential pitfalls and implications

Potential Pitfall	Implications
Maintenance contracts; out clauses, assignment clauses,	Ability to self perform work/convert to system provider
Provider challenges	Length of time to set up vendor for payment, vendor acceptance of T&Cs
AHJ contractual requirements	Local AHJ requiring licensed service personnel for work
CBA concerns	Impact the CBA may have on blending of staffs.

Regulatory & Licensing

Identifying the potential pitfalls and implications

Potential Pitfall	Implications
Independent physician practices now falling under hospital license	Capital and ops budget costs to bring practice up to hospital standards
Are both organizations accredited by the same agency?	Ops budget costs to educate staff or to convert to different deeming agency
Are there different AHJs	Different requirements for M&R
Potential risks from other agency inspections: OSHA, DOT, NRC, EPA, etc…	Potential impact to ops and capital budgets to address remedies required

M&A Perspectives from the trenches

Tony Dickamore, VP Facilities Management, HD, Kindred Healthcare

Summary of past 5 years at Kindred/affiliates (through M&A activity):

- Mergers and Acquisitions 56
- Divestitures 14
- Opened 5

- **Will add two or three photos of hospitals involved in these actions**

M&A Perspectives in the Trenches

A Timeline—A Gannt Chart

- Jun 2009 Joined Triumph Healthcare
- Sep 2009 Triumph acquires St. Agnes Mercy hospital
- Oct 2009 Open Mishawaka HIH hospital
- Nov 2009 RehabCare (15 hospitals) merges w/ Triumph Healthcare (20 hospitals)
- Apr 2010 Open 42 bed Houston Heights hospital
- Jan 2011 Open Joint Venture hospital in Rome Georgia
- Feb 1, 2011 Planned awesome vacation to Tahiti
- Feb 8, 2011 Kindred announced purchase of Rehabcare for $900M
- Feb 9, 2011 Cancelled awesome vacation to Tahiti
- Jun 1, 2011 Kindred (83 hospitals) acquisition of Rehabcare (38 hospitals)
- Nov 2011 Open NE Houston Rehab hospital
- May 2012 Open Central Texas Rehab Hospital
- Oct 2012 Acquisition and relocation of 67 bed Dayton hospital
- April 2013 Kindred announces plans to divests 16 hospitals
- July 2013 Acquisition and relocation of 54 bed Mercy and Christus JV hospital
- Sept 2013 Kindred sells 14 hospitals to Vibra Healthcare

M&A Perspectives in the Trenches

Critical Mindsets; Proven Practices

- **Flexibility: "Can't we just pick a date?"**
- **Knowledge is Key: What skeletons are in the closet?**
- **Due Diligence work—It's critical**
  - Kick the tires, walk through every building
  - Read the history books- Past surveys, Plan of Corrections
  - Talk to the neighbors—find the wrench turners and major service vendors
- **Environmental surveys—EPA violations (UST, radioactive labs, Asbestos)**
- **Assess your people**
- **Contracts, contracts, contracts**
  - How many contracts do you manage?
- **Whose Truck is it and who gets to Paint it?**
  - Standardization and consistency- it can wait

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