

CHE Conference Call
June 20, 1996
Proposed MUSC Columbia/HCA Lease

By conference call Commission members discussed concerns and recommendations pertaining to the proposed MUSC Columbia/HCA Lease. Pursuant to legislation enacted by the General Assembly, the Commission will submit various recommendations to the State Budget and Control Board.

The Commission has concluded that there are four areas of interest:

1. Impact on the Funding Formula

a. Annual Payments of \$30 million to MUSC - In the event future State appropriations to MUSC Academic Unit are increased significantly toward full formula, it may be appropriate to revisit the consideration of the \$30 million which generally speaking is a combination of the lease payment and the academic affiliation. This will basically replace existing revenues that are currently supporting MUSC academic programs.

It was moved (Goad), seconded (Ramage) and voted that the \$30 million payment to MUSC Academic Unit and the formula funded percentage be reviewed annually during the formula/appropriation process to determine whether offsets to the appropriations should be considered.

b. Research Funding - The Academic Affiliation Agreement states that "MUSC has a right of first refusal to staff and to conduct any educational and/or research program to be developed hereafter by Columbia/HCA at any of the Charleston system hospitals." Also, the Agreement states that "Columbia shall provide funding for Programs of Excellence in an amount of not less than \$7.5 million per year for ten years, which funds may be used for both capital expenditures and operating funds."

The CHE funding formula provides for a 25% match to be awarded to the institution of all externally generated, non-state, research expenditures. In neither case would the research grants qualify for the formula match because the grant would be made to Columbia/HCA and thereby be disqualified. Since the \$7.5 million is directly tied to the lease of a State asset, any portion of those funds used for research would be treated in the same manner as State funds and thereby be disqualified for the research match.

It was moved (Goad), seconded (Tolbert) and voted that federal or other grants made directly to Columbia/HCA and proceeds to perform research grants from the Programs of Excellence funds be disqualified for the formula 25% match.

c. Funds for Teaching Costs - Currently the Medical Center receives \$18 million in direct state appropriation and \$10 million from the MUSC Academic Unit for teaching costs associated with the medical and dentistry students as well as residents and interns. Since

clinical training will continue to be a major component of MUSC Academic Unit, the funds necessary to support those costs should be under the direct control of MUSC.

It was moved (Goad), seconded (Tolbert) and voted that the \$18 million currently appropriated to the MUSC Medical Center be appropriated instead to the Medical University Academic Unit. Additionally, the Commission recommended that the \$10 million be retained for the purposes for which it is now designated.

2. Academic Affiliation/Access

A primary concern of the Commission with regard to the academic programs at MUSC is the availability of the clinical facilities for educational purposes. The lease agreement provides for sound, ongoing access during the term of the lease.

Another issue relating to Academic Affiliation/Access has been specifically addressed by the General Assembly with the following legislative language: "Access for any person or group to use the services of the Medical University hospital and clinical services shall not be limited, restricted, denied, or allowed in a discriminatory manner that is prohibited by law; nor shall such access be denied based on lack of participation or membership in a particular health plan or network."

There was no further recommendation relating to these issues.

3. CHE Permanent Improvements (Lease) Guidelines

The Lease Agreement provides for an annual Base Rental of \$8 million per Lease Year throughout the Lease Term and any Renewal Terms. The property to be leased to the Columbia/HCA consists of the MUSC Teaching Hospital, the MUSC Children's Hospital, and the Psychiatric Institute. The initial term of the Lease shall be for 20 years and shall renew and extend for two periods of five years each without any act by Tenant or any notice by Tenant to Landlord. At the end of the lease period, Columbia/HCA will have no further claims on the leased property.

State law and Commission regulations require that in the event of the sale of any facility constructed with the proceeds of General Obligation Bonds, which are defrayed by the state treasury (as distinguished from institutional revenue), the proceeds must be returned to the State. It was moved (Goad), seconded (Kinon) and voted that while the law and the regulation do not speak to reimbursement for such facilities which are leased, the Budget and Control Board should explore the question of reimbursement for such facilities which are leased, rather than sold, including the Medical University facilities, which might have been financed through General Obligation Bonds.

4. Consideration of Reserves for Repurchase of Current Assets and Capital Improvements

The lease permits the Medical University to repurchase certain assets at the end of the

lease term at book value. The capital outlay for such a repurchase could place a sizable burden on the higher education budget if that became the source of revenue.

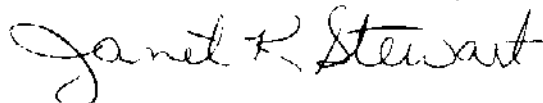
Mr. Gilbert stated that if a reserve fund is established, the funds should remain in South Carolina.

It was moved (Tolbert), seconded (Goad) and voted that consideration should be given by the Budget and Control Board and the Medical University of South Carolina for the establishment of a reserve fund during the period of the lease to permit orderly repurchase without undue hardship on the State budget or the appropriations for higher education. With respect to reserve funds and other funds controlled by the Medical University and Columbia/HCA as a result of this transaction, the State should require or encourage both entities to deposit or invest such fund in South Carolina financial institutions.

Dr. Maxwell expressed reservations and trepidations concerning the entrance of for-profit firms such as Columbia/HCA into the health care field. "Ostensibly the bulk of their funding comes from economies in funding similar to those achieved by 'less-than-car-lot-freight consolidators.' The claim that this is the case is not so strong as to dismiss fears that a second major reduction in costs may be due to a large reduction in indigent care. Maxwell expressed the hope that this structural change in the medical industry will not increase the stock of human suffering."

There being no further business, the conference call ended.

Respectfully submitted,

A handwritten signature in cursive script that reads "Janet K. Stewart". The signature is written in dark ink and is positioned above the printed name.

Janet K. Stewart

PROPOSED MUSC COLUMBIA/HCA LEASE

Pursuant to legislation enacted by the General Assembly, the Commission is submitting various recommendations to the State Budget and Control Board on the proposed Medical University of South Columbia lease to Columbia/HCA, a private corporation.

As agreed at the June 6 meeting of the Commission, the comments and recommendations of the Commission are limited only to the areas that fall under its jurisdiction.

In preparing its recommendations, the Commission called on the following resources:

(1) Numerous briefings and public hearings held during calendar years 1995 and 1996.

(2) A review of all documents provided by the Medical University and materials submitted by a number witnesses from both sides during public hearings.

(3) An informal review of the recommendations with senior officials of the Medical University and the Budget and Control Board.

The Commission has concluded that there are four areas of interest:

1. Impact on the Funding Formula

- a. Annual Payments of \$30 Million to MUSC
- b. Research Funding
- c. Funds for Teaching Costs

2. Academic Affiliation/Access

3. CHE Permanent Improvements (Lease) Guidelines

4. Consideration of reserves for repurchase of current assets and capital improvements

Issues that came to the Commission's attention that we believe warrant notification to the Budget and Control Board, along with Commission recommendations are outlined below.

1. Impact on the Funding Formula

a. Annual Payments of \$30 Million to MUSC

The lease provides for an academic affiliation payment from Columbia/HCA to MUSC in the amount of \$22 million per year, adjusted annually based on the Consumer Price Index (CPI). Also, the lease provides for an annual Base Rental of \$8 million per Lease Year and is also subject to CPI increases. These two amounts total \$30 million.

The related issues are, how will the revenue be used and should it be an offset against state appropriations? Also, how will the formula for the MUSC academic unit be affected by the revenues?

Discussion

Currently, MUSC-Academic Unit receives approximately \$31 million annually from the MUSC-Medical Center. These funds are primarily from disproportionate share funds. These are funds provided to certain medical centers that serve a higher than normal share of indigent care patients. It is anticipated that the disproportionate share funds will be eliminated by the year 2000.

These funds are not specifically addressed in the agreement because they were considered in the valuation process and have been "included" in the various revenue streams from Columbia/HCA to MUSC over the lease term. Generally speaking, one could say that the lease payment and the academic affiliation agreement payments, with a combined total of \$30 million, will ensure a flow of funds during the term of the lease equivalent to the current value of disproportionate share funds.

It is important to note that while these revenue streams may appear to be "new" money, they will basically replace existing revenues that are currently supporting MUSC academic programs.

Conclusion

Commission concurs that the \$30 million does not represent "new funds" to the MUSC Academic Unit, and that these funds should be retained by the Academic Unit, especially in light of the fact that appropriations to MUSC are only 70% of formula. However, it is important to note that full formula provides for an appropriate level of educational funding. Thus, in the event future state appropriations to MUSC Academic Unit are increased significantly toward full formula, it may be appropriate to revisit the consideration of the \$30 million.

Recommendation

The Commission recommends that the \$30 million payment to MUSC Academic Unit and the formula funded percentage be reviewed annually during the formula/appropriation process to determine whether offsets to the appropriations should be considered.

1. Impact on the Funding Formula

b. Research Funding

The Academic Affiliation Agreement states that "MUSC has a right of first refusal to staff and to conduct any educational and/or research program to be developed hereafter by Columbia/HCA at any of the Charleston System hospitals." Also, the Agreement states that "Columbia shall provide funding for Programs of Excellence in an amount of not less than \$7.5 million per year for ten years, which funds may be used for both capital expenditures and operating funds."

Discussion

To encourage and promote research at the institutions, the CHE funding formula provides for a 25% match of all externally generated, non-state, research expenditures. The research step further requires that the grants be awarded to the institution.

There are two issues identified by the staff relating to these two quotes. The first quote implies that Columbia/HCA will be receiving research grants. In the second quote, it appears that part of the \$7.5 million of Programs of Excellence funds from Columbia/HCA could be used by MUSC Academic Unit to perform research. It is the opinion of the staff that in neither case would the research grants, were they to materialize, qualify for the formula match. The reasons are, in the first instance, the grant would be made to Columbia/HCA and thereby be disqualified. In the second instance, since the \$7.5 million is directly tied to the lease of a State asset, any portion of those funds used for research would be treated in the same manner as State funds and thereby be disqualified for the research match, since they are realized from the lease of state assets.

Recommendation

The Commission recommends that federal or other grants made directly to Columbia/HCA and proceeds to perform research grants from the Programs of Excellence funds be disqualified for the formula 25% match.

1. Impact on the Funding Formula

c. Funds for Teaching Costs

Clinical training for medical students takes place at the Medical Center and the various clinics comprising the MUSC-Medical Center. Funds are appropriated/transferred to the Medical Center to cover the teaching costs associated with the medical and dentistry students as well residents and interns. Currently the Medical Center receives \$18 million in direct state appropriation and \$10 million from the MUSC-Academic Unit for a combined total of \$28 million.

Discussion

Since clinical training will continue to be a major component of MUSC-Academic Unit, the funds necessary to support those cost should be under the direct control of MUSC. The clinical training will take place not only at the Medical Center, which will be leased to Columbia/ HCA, but also at the various clinics, which will be under the control of MUSC.

Recommendation

The Commission recommends that the \$18-million currently appropriated to the MUSC Medical Center be appropriated, instead, to the Medical University Academic unit. Additionally, the Commission recommends that the \$10 million be retained for the purposes for which it is now designated.

2. Academic Affiliation/Access

One primary concern of the Commission with regard to the academic programs at MUSC is the availability of the clinical facilities for educational purposes. We find that the lease agreement provides for sound, ongoing access during the term of the lease.

Another issue relating to Academic Affiliation/Access has been specifically addressed by the General Assembly with the following legislative language: "Access for any person or group to use the services of the Medical University Hospital and clinical services shall not be limited, restricted, denied, or allowed in a discriminatory manner that is prohibited by law; nor shall such access be denied based on lack of participation or membership in a particular health plan or network."

Recommendation

The Commission has no further recommendation relating to these issues.

3. CHE Permanent Improvements (Lease) Guidelines

The Lease Agreement provides for an annual Base Rental of \$8 million per Lease Year throughout the Lease Term and any Renewal Terms. Base Rental is subject to a CPI increase on the first day of each Lease Year. Please note that this \$8 million has been addressed in section (1a.) of this paper as part of the \$30 million payment that Columbia/HCA will pay to the MUSC-Academic Unit.

Discussion

The property to be leased to the Columbia/HCA consists of the MUSC Teaching Hospital, the MUSC Children's Hospital and the Psychiatric Institute. The initial term of the Lease shall be for 20 years and shall renew and extend for two periods of five years each without any act by Tenant or any notice by Tenant to Landlord. This Lease shall continue in full force and effect for the entire Lease Term and may only be terminated prior to the end of the Lease Term by either (a) a mutual agreement in writing by Landlord and Tenant, (b) in accordance with the termination provisions of such other documents executed by and between Landlord and Tenant to the extent and only to the extent such documents expressly provide for the termination of this Lease, or (c) in accordance with the termination provisions of the Lease Agreement.

At the end of the lease period, Columbia/HCA will have no further claims on the leased property.

Recommendation

State law and Commission regulations require that in the event of the "sale" of any facility constructed with the proceeds of General Obligation Bonds, which are defrayed by the state treasury (as distinguished from institutional revenue), the proceeds must be returned to the State. While the law and the regulation do not speak to reimbursement for such

facilities which are leased, we believe the Budget and Control Board should explore the question of reimbursement for such facilities which are leased, rather than sold, including the Medical University facilities, which might have been financed through General Obligation Bonds.

4. Consideration of Reserves for Repurchase of Current Assets and Capital Improvements

The lease permits the Medical University to repurchase certain assets at the end of the lease term at book value. The capital outlay for such a repurchase could place a sizable burden on the higher education budget if that became the source of revenue.

Recommendation

Consideration should be given by the Budget and Control Board and the Medical University of South Carolina for the establishment of a reserve fund during the period of the lease to permit orderly repurchase without undue hardship on the state budget or the appropriations for higher education.

With respect to reserve funds and other funds controlled by the Medical University and Columbia/HCA as a result of this transaction, the State should require or encourage both entities to deposit or invest such funds in South Carolina financial institutions.