Public Focus

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Preparing for Leaner Times Ahead: The Role of the Public Hospital Governing Board

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Public hospitals continue to be essential components of America's healthcare system, but many of them face an uncertain future. Despite the positive impact of the Affordable Care Act on coverage, particularly in states that have expanded their Medicaid programs, a range of financial, regulatory, political, and competitive forces are converging to present significant challenges. Safety-net hospitals will need a full range of resources and strategies if they are to meet those challenges and continue to fulfill their essential, multi-faceted missions. Effective governance will be one of the most essential resources—while ineffective or dysfunctional governance could impede (or even doom) the necessary reforms and initiatives that will be required.

This article provides an overview of the specific trends and challenges likely to face public hospital boards in the next several years and summarizes some of the key steps public hospital governing boards can take in addressing those challenges and trends.[1]

The Challenges Facing Public Hospitals

The primary environmental factors likely to have a negative impact on public hospitals and health systems in the next five to 10 years will include (but are not necessarily limited to):

- Increased spending by public safety-net hospitals in response to the implementation of the ACA, especially in Medicaid expansion states, started contributing to declining public hospital profitability in FY 2016–2017. Medicaid expansion, combined with a reduction in uncompensated care, led to an initial improvement in financial performance. Surprisingly, the improvement was short-lived for some public hospitals. Revenue growth below expectations, combined with an "excess" of spending in anticipation of the ACA, may have contributed to a decline that has continued for such hospitals in 2018.
- While the ACA is far from dead, there has been an erosion since the 2016 elections in benefits, funding, government support, and other key features, including declines in Medicaid enrollment due to new federal and state requirements. All of these trends have a disproportionate impact on public hospitals.
- The Tax Cuts and Jobs Act (TCJA), passed in December 2017, eliminated the penalties associated with not having health insurance, effective in 2019. The Congressional Budget Office estimates an increase in the number of uninsured by 12 million in 2021.
- The growing use of "narrow network" managed care

According to the Pew Trusts, "Ten years after the recession began, states face fiscal and economic uncertainties." In its July 2017 report, "Ranking the States by Fiscal Condition," the Mercatus Center at George Mason University used 13 metrics that assess the extent to which the states can pay short-term bills and meet longer-term obligations. Medicaid expansion states in the Northeast, Mid-Atlantic, and Midwest along with Louisiana, California, and West Virginia appear to have below average fiscal condition.

1 This article is intended to be a companion to a new report by Dr. David Gruber and the research staff of the Health Industry Practice Group at Alvarez & Marsal. The report, which will be released in early January 2019, identifies and discusses in greater detail a number of the specific trends and challenges discussed in this article. It also proposes a range of operational, financial, and health delivery system reforms to help safety-net hospitals prepare to address future challenges.

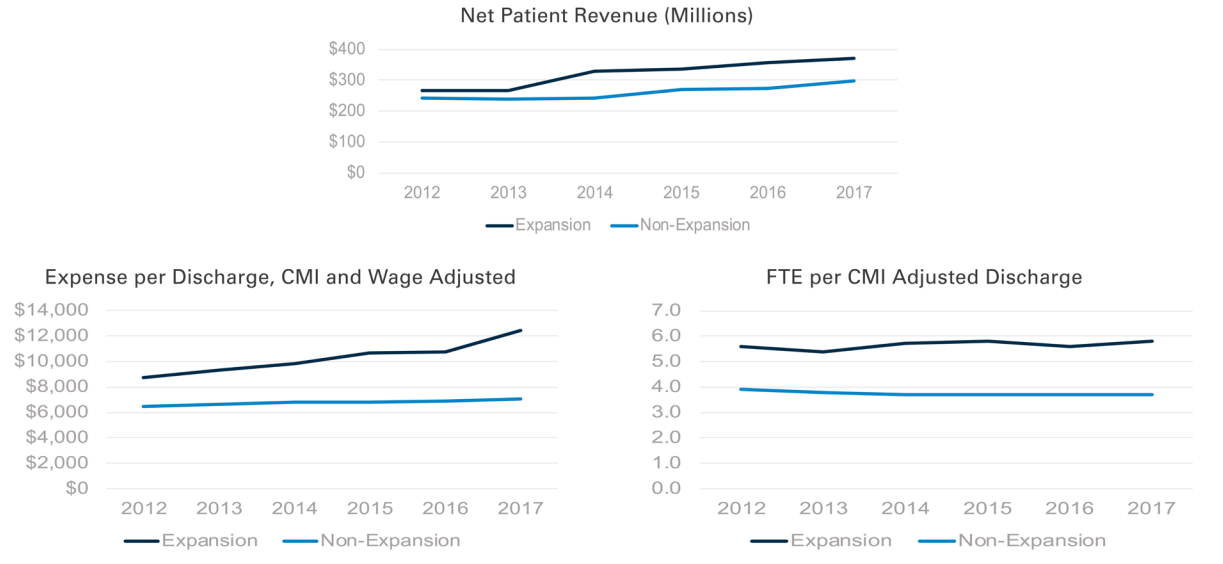
The U.S. population is rapidly aging, with the percentage of those over 65 forecast to increase from 49.2 million (15.2 percent of the population) in 2016 to 73.1 million (20.6 percent of the population) in 2030. More than 50 percent of the dual-eligible population is over 75 years old, the period of rising healthcare costs and the need for long-term care services, and this group is growing more rapidly than the overall Medicaid population. In 2018–2025, the prevalence of Alzheimer's disease and other dementias is projected to increase from 5.5 to 7.1 million, an increase of 29 percent.

plans in ACA exchanges that often exclude public teaching hospitals may also contribute to a future reduction in covered patients and increased fiscal uncertainty for such hospitals.

- Competition from larger, better resourced hospitals and health systems for insured Medicaid patients continues to increase, leaving public hospitals, which are often unable to participate in such systems, increasingly isolated.
- Federal budget deficits that are soon to exceed $1 trillion will combine with increasing fiscal pressure on states, particularly those in the Northeast, Mid-Atlantic, West Coast, and other regions with many safety-net hospitals and high Medicaid spending.
- While the Democratic takeover of the House in 2019 may offer some hope, possible future reductions in Medicaid and Medicare DSH payments, and increased pressure on 340B and other supplemental payment mechanisms that benefit public hospitals, remain real possibilities.
- Increased emphasis on value-based care leading to reimbursement pressures on hospitals serving large numbers of the remaining uninsured and underinsured.
- Increasing demand for behavioral health services, including substance abuse treatment, by patients who often lack adequate coverage is straining resources in many public hospitals.
- A perhaps unintended consequence of Medicaid expansion in certain states has been the state allocation of Medicaid DSH payments among a larger number of hospitals; i.e., leading to a reduction in payments to primary safety-net hospitals.

Exhibit 1: In 2016, despite net patient revenue growth in urban expansion state government hospitals of 3.8%, expense per discharge increased 15.7%

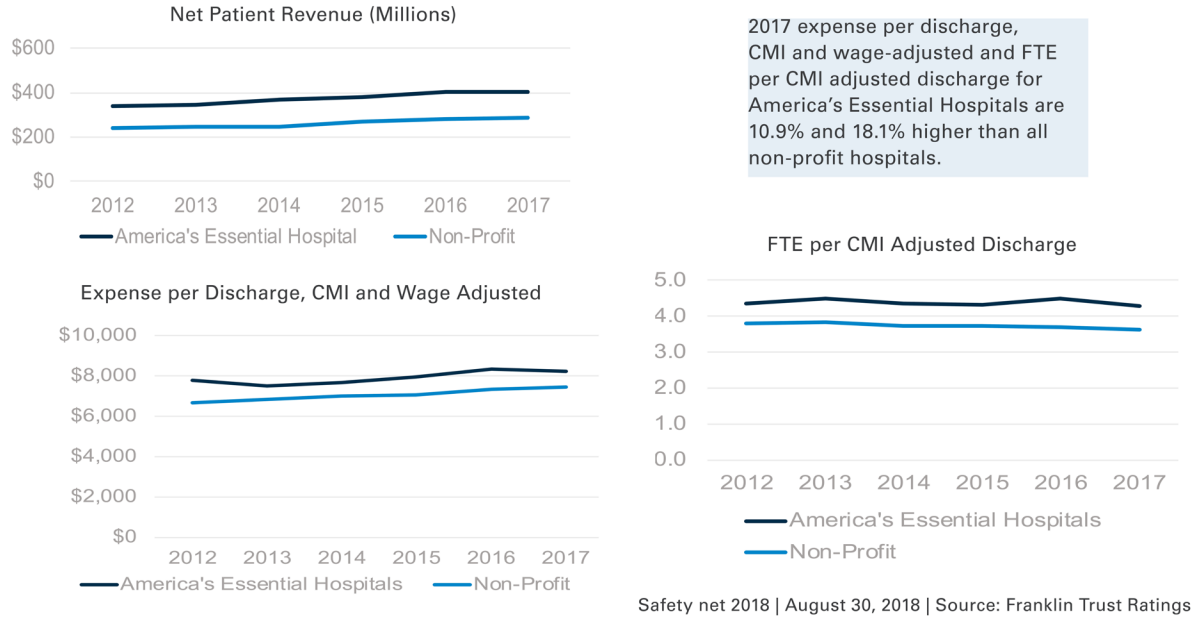
Sample of government, urban hospitals >99 beds; Medicaid expansion states (n=101 hospitals), non-expansion states (n=102)



Safety net 2018 | August 30, 2018 | Source: Franklin Trust Ratings

Exhibit 2: Safety-net hospital members of America's Essential Hospitals tend to be larger than other non-profit hospitals and have higher expense per discharge, CMI and wage adjusted

Hospital cohort: Non-profit, urban, >99 beds. Non-profit (n=1,194); America's Essential Hospitals (n=52).



Safety net 2018 | August 30, 2018 | Source: Franklin Trust Ratings

- The proportion of Medicaid spending devoted to elderly and disabled dual-eligible patients continues to increase; public hospitals are often at a disadvantage in attracting such patients.

The Role of Public Hospital Governing Boards in Meeting These Challenges

Effective governance will be an essential component of the ability of public hospitals and health systems to successfully respond to these challenges. To assist in developing and implementing effective strategies public hospital governing boards (and board members) can:

- **Get educated.** Public hospital board members should be proactive in learning about the challenges of the future. Management should provide board members with up-to-date information about each of the challenges the hospital is likely to face. Access to key publications (from The Governance Institute, Health Affairs, Kaiser Family Foundation, etc.), the opportunity to attend national or regional conferences, and regular presentations from key innovators (population health experts, financial turnaround specialists, healthcare marketing consultants, etc.) can bring public board members a much greater understanding of the job they need to do.
- **Improve strategic thinking.** Too often, members of public hospital governing boards are inordinately focused on specific matters affecting day-to-day operations, financial crises, patient care incidents, or meeting the needs of specific patient populations. Each of these issues may be important, but focusing too much attention on them in board meetings can rob the board as a whole of the time and resources to think strategically about long-term needs.
- **Set priorities and focus on the long-term mission and success of your hospital/health system.** Board members need to check constituency behavior at the boardroom door. Often, public hospital board members are nominated or appointed to represent certain constituencies. Some of those constituencies are no doubt important to the future success of the public hospital. However, it will be more important than ever in facing the challenges of the next several years for boards

Denver Health System: A Case Study in Effective Governance

Even those public hospital systems that have been considered successful and innovative, like the Denver Health System (DHS), are facing multiple threats today in the chaotic healthcare marketplace. At DHS, the governing board has played a key role in addressing those threats.

I had a recent conversation with Robin Wittenstein, Ed.D., Chief Executive Officer of DHS. Dr. Wittenstein is highly knowledgeable about safety-net health systems. She was appointed to her current position in 2017 following distinguished service as an executive leader at Penn State Health and as President and CEO of University Hospital and University of Medicine and Dentistry of New Jersey.

DHS has long been one of the nation's iconic public health systems—often a model and test bed for successful strategies that were later adopted by other systems. It was one of the first public health systems to restructure as a public health and hospital authority, directly employ its entire medical staff, own and operate its own network of federally qualified health centers, and explore delivery system redesign that expanded ambulatory care into a fully coequal part of a safety-net system, among other innovations.

Dr. Wittenstein described a number of recent challenges for DHS. These included state and local fiscal and political pressures, the consolidation of most of the rest of the hospital industry in Denver into just a few large systems, and the fact that DHS (like many safety-net systems) had invested considerable resources in anticipation of the implementation of health reform. Patients with coverage (and patient care revenues) did increase, but the investments had also contributed to financial stress for the system in 2016 and 2017.

Dr. Wittenstein said that effective governance was an important component of their ability to address multiple challenges: "The most valuable thing the Denver Health board did was to educate themselves about all of the potential problems and issues we were facing. We have engaged them in educational seminars, provided reading materials, encouraged them to look at our situation realistically and ask a lot of questions."

She also emphasized that the board was a full partner of the executive team, without crossing the line between governance and management. Because management was transparent about the risks they were facing, the board did not overreact: "We needed to get back to breakeven in 2017. We gave the board our plan. We were realistic and transparent about how long it would take, and that gave the board the freedom and comfort level to trust in our judgment. They gave us the time we asked for. But we worked closely with them to set milestones and we reported on our progress every month."

to maintain the discipline necessary to help management prioritize strategies and focus what may be limited resources on those actions most likely to ensure the hospital's future viability.

- **Improve community outreach.** Board members can be instrumental in forming bonds with other key players in their communities. An increased focus on value-based care and population health will require partnerships with other community organizations that pay attention to the social determinants of health status of vulnerable patients more likely to be served by public hospitals. These include organizations focused on housing, nutrition, education and training, environmental services, and a range of other activities that are essential to improving the health of vulnerable patient populations.
- **Care delivery transformation.** Understand the profound underlying changes that are taking place today in the diagnosis and treatment of many diseases and conditions, and support management in transforming the public health and hospital system from inpatient-centric to a more balanced mix of inpatient and outpatient/ambulatory care.
- **Set goals for operational and financial improvement, then give management the breathing room to achieve them.** Public hospital boards need to incent

management to work with the board to develop plans to achieve greater operational, competitive, and financial efficiencies, then provide management with the time and resources to implement those plans. It is more important today than ever before for both board members and executive leadership to maintain the dividing line between governance and management.

- **Focus on filling gaps in board member expertise.** Just as political, business, medical, scientific, and other healthcare industry demographics are empowering new generations of leaders, public hospitals need to have a succession plan for their governing boards that takes into account the changing demographics of their patient population and workforce, as well as the background and technical skills that will be most helpful in addressing the challenges of the future. While public hospitals can be more limited by political considerations than their non-profit counterparts in recruiting board members with a range of skills and experience, it can be helpful for public systems to adopt some of the approaches of the non-profit sector in identifying board members. Those include appointing independent nominating committees and developing a skills matrix for existing board members that can help identify gaps that need to be filled. And in those increasingly rare cases where elected bodies such as a City Council or County Board of Supervisors serve as the hospital's only governing board, elected officials should give serious consideration to following recent trends and appointing dedicated governing boards for their hospitals and health systems.

In conclusion, effective governance has never been more important for both public and private hospitals and health systems. Quite simply, public hospitals and health systems in most parts of the country still face more barriers to success than private systems, at a time when the challenges have never been greater. The current and future political, fiscal, and competitive environment requires all of the major components of a public system to be operating with peak effectiveness, including the system's governing board as well as its management, medical staff, workforce, and community advocates.

The Governance Institute thanks Larry S. Gage, Senior Advisor, Alvarez and Marsal, and Senior Counsel, Alston & Bird LLP, for contributing this article. *He can be reached at larry.gage@alston.com.*