Hospital Focus

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Is Healthcare a Charity, Social Service, or Business? Community Hospital Board Members Contemplate Their Role

By Rex Burgdorfer, Vice President, Juniper Advisory

Board members of independent hospital companies are in the cross-hairs. They govern during a time of intense industry and societal change. Situated at the center of a national struggle, they contend with front-page news, and tweets, daily. Directors are challenged not only by these major economic and political issues but also by the tremendous volume of day-to-day operational detail involved in running a complex enterprise.

Peter Drucker famously argued that hospitals were the most complicated form of economic organization.[1] Certainly, managing the large number of stakeholders—federal, state, and local governments, insurance companies, physicians, nurses, employees, unions, patients, local news outlets, and more—is a herculean task.

Juniper Advisory's bankers have been fortunate to work with over 225 hospital system boards across the United States over the last 25 years. We have tremendous respect for the volunteers that oversee non-profit hospitals. They work tirelessly to guide the strategic direction of what are almost always the largest employers in town and leading driver of economic activity. A hospital's importance to the vitality of a region cannot be overstated. That outsized impact seems indelibly tied to the decline of the middle class.

Fifty years ago, well-intended community members volunteered for hospital board responsibilities, agreed to meet quarterly, raised philanthropy, and served as a link to the community. The demands were relatively modest. Local awareness and prestige were high. It was more Rotary Club than high-stakes corporate boardroom drama. These were the golden years of the middle class—manufacturing output, civic involvement, patriotism, Elks Clubs, bowling leagues, corporate loyalty, pension plans, JFK Democrats, NASA. Bureaucracy that worked.

All of that changed in the past decade. Today, boards regularly meet multiple times per month, sometimes requiring early morning and late evenings on the same or contiguous days. Conferences, Webinars, and weekend teleconferences are common.

Increased work hours alone, though, would not be cause for concern. The trouble we observe is that this ***additional weight impairs boards as they attempt to nimbly navigate change.***

Fiduciaries are often so consumed by a changing business landscape and increased regulatory scrutiny that major strategic issues slip through the cracks. In a recent example, Juniper advised a hospital system that was considering strategic options that included business combinations. The potential partnership involved once-in-a-generation decisions, including tens of millions of dollars of value, hundreds of jobs, and a potential change-in-ownership of the community's most important and valuable asset.

The Juniper team participated in a three-hour board meeting. It was late in the evening, and the directors had worked full days in their professional lives. Information came at them like a firehose—a new IT installation, narrow network insurance contracts entering the market, a changing payer mix, increased pressure from commercial providers, operational challenges resulting from reduced

[1] The Drucker Institute, www.drucker.institute.

volumes and greater use of outpatient services, competitors vying for market share by building clinics in the market, physician recruiting shortfalls, foundation fundraising activities, ad infinitum. These topics occupied two-and-a-half hours, but could have taken 20 hours.

The process Juniper was managing (consideration of the sale of the company) was afforded less than 25 minutes. With little energy left in the room, it was impossible to establish a tangible direction. The conversation stalled, the process listed sideways, and the hospital languished for several extra months. This caused material unnecessary stress on the organization and exposed it to a host of unforeseen outside risks.

As the title of this article suggests, non-profit boards also suffer from an identity that is sometimes difficult to discern. Unlike in commercial corporations, directors are not elected by owners. They are self-perpetuating and not accountable to shareholders. Most we have met with are, understandably, unclear on whether they serve the community, patients, employees, physicians, or the corporation. And yet, most take in more than 50 percent of their revenue from Medicare and Medicaid.

Universally, hospital boards are populated by extraordinarily well-intended people. They are, however, commonly all local and not necessarily well-versed in the healthcare industry. In the view of many, this stunts innovation and is a leading cause of the industry's inefficiency. Contrast hospital governance norms with a major corporation. There, shareholders elect the board. Members are geographically diverse, bring ideas from a range of backgrounds, and, importantly, are paid experts. Ironically, corporate boards managing billion-dollar global enterprises are regularly smaller than a 50-bed community hospital.

Corporations also tend to use committees to a much larger degree than governments or charities. Director committees rely less on outside consulting assistance for routine decisions. In a public company capital markets transaction (for example, a debt or equity offering, or interest rate swap), there is no intermediary consultant between the issuer and underwriter or investment bank. Use of a consultant in this manner, however, is commonplace when non-profit hospital systems access capital. Why? Leadership of public companies are assumed to be sufficiently experienced and sophisticated to internally handle financing and capital structure issues. The result is that non-profit boards are much more involved, spending time and money on operational matters.

This is not intended to slight hospitals in the least. It does, however, provide one hypothesis for why so many hospitals appear fatigued, overwhelmed, and unable to chart a clear course for the future. As Peter Drucker believed, "Strategy is a commodity, execution is an art." Or as the Royal Bank of Scotland's television commercial championed, "Less talk, more action." A practical, "get things done" approach, however, often requires decision making in a compressed timeframe, something hospitals do not excel at. Perhaps the consulting culture, group-think mentality, and non-professional board populations are partly responsible.

One can easily understand the strategic challenge, though. Efficient markets in sectors like financial services and energy can tolerate failure. Allowing Lehman Brothers or Enron to fail, while economically painful, was not catastrophic. The hospital market is not so fortunate.[2] Effective board leadership and performance in the hospital sector can quite literally be a matter of life or death.

The Governance Institute thanks Rex Burgdorfer, Vice President, Juniper Advisory, for contributing this article. He can be reached at rburgdorfer@juniperadvisory.com.

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[2] "Consolidation in the Commercial Banking and Hospital Industries: Parallels and Contradictions," The Governance Institute, *BoardRoom Press*, June 2013.