‘Mission Driven’ — Restructuring Lower Bucks Hospital

BY ROBERT D. KATZ

Restructuring expert Robert Katz analyzes the turnaround of Lower Bucks Hospital, which found itself in a cash-flow crisis due to reductions in federal and state reimbursements and increases in healthcare and other costs. Katz notes the special challenges in restructuring a “mission driven” organization that impacts livelihoods as well as lives.

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In the restructuring world, the highs are the highest, the lows are the lowest — and sometimes it changes by the hour. The grenades keep coming in, and our job is to catch them and throw them out before they explode. Such is the world of Executive Sounding Board Associates (ESBA). Bankruptcy/restructuring attorneys, consultants, chief restructuring officers, lenders, appraisers, auctioneers, investment bankers, company owners or those dealing with a company in trouble or transition, can appreciate these thoughts.

An additional layer is added when dealing with a “mission driven” organization. Then it is not only, or even primarily, about profits or cash-flow, but usually and almost as important is the mission and the constituency that it serves.

That brings us to the anatomy of the turnaround for Lower Bucks Hospital (LBH), which was getting ready to celebrate its 60-year anniversary in a primarily lower middle-class area that serves a significant number of indigent people. With all the reductions in reimbursements from the federal and state governments and increases in healthcare and other costs, it found itself in a cash-flow crisis.

The Situation

Founded in 1954, LBH is a community hospital located in Bristol, PA. At the time, LBH offered a full range of acute, sub-acute, ambulatory and related services including cardiac catheterization, open heart surgery, diagnostic imaging, industrial health, mental health, home health and orthopedics. It is licensed to operate 186 beds and maintains a 36-acre medical campus along with an ambulatory surgery center and a health & wellness center. Starting in 2007, the hospital experienced, among other issues, a decline in net patient service revenue (NPR) due to a variety of factors including: 1) a deteriorating patient/payor mix that was exacerbated by the economic recession and higher unemployment rates, 2) lower reimbursement rates, 3) an increasingly competitive landscape and the impact of large capital enhancement initiatives by local competitors, 4) the hospital’s labor costs as a percentage of revenue were substantially above the market average, and 5) both regulatory requirements and existing labor agreements limited management’s ability to reduce costs in line with revenue.

As a result, LBH sustained operating losses and was forced to use substantial working capital, including cash and investments, for pension obligations and annual debt service. The lack of spending led to a decline in the hospital’s appearance, which then reduced physician referrals to LBH and further reduced NPR. These are some very core issues to most turnarounds, but when dealing in this space with the hospital, peoples lives and patient care, they truly fit the definition of life and death. Also a concern was preserving the hospital’s reputation of providing exceptional care and concern.

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The Solution

A new chief executive, Al Mezzaroba, was brought in to run the hospital. He is someone who understood not only the importance of managing the profitability and cash-flows, but also the impact of managing through the political and personnel issues. This is critically important when dealing with an entity that generates a significant portion of its revenue from government agencies and regulatory sources as well as dealing with multi-union, complex negotiations in a contract renewal year, all while going through a formal Chapter 11 restructuring.

Some of the steps taken by the turnaround team, but certainly not an all-inclusive list, included:

- Froze the pension plan in 2009 to create additional liquidity for hospital operations.
- Developed pension termination alternatives and negotiated with the Pension Benefit Guaranty Corporation (PBGC) a termination of the hospital’s underfunded defined benefit pension plan, the complexities of which would lend itself to an entire article, and covering it in one bullet point doesn’t do it justice.
- Negotiated with the indenture trustee for LBH bonds effectuating a forbearance agreement & restructuring alternatives.
- Preserved the hospital’s value and ability to serve the community.
- Increased cash-flow by obtaining grants and funding that laid the foundation for the turnaround.
- Reduced operating costs by enhancing inventory management and reducing headcount of non-essential staff.

- Worked with trade creditors to gain their support through the Chapter 11 that enabled the hospital to obtain the goods and services needed to treat its patients.
- Renegotiated contracts.
- Created a new structure that enabled LBH to recruit local doctor groups.
- Eliminated service lines with limited to no profitability.
- Renegotiated the collective bargaining agreement which reduced overall labor costs and created more flexible work rules.
- Preserved more than 1,000 jobs and now serves approximately 70,000 patients annually.

In a day and age when stand-alone Chapter 11 reorganizations are becoming rarer and rarer, the hospital overcame substantial challenges in exiting bankruptcy through a stand-alone plan of reorganization. The challenges included creating an operating model for LBH that would allow it to compete in the marketplace post-Chapter 11 emergence, developing a structure and operating plan and procuring new capital to fund the plan.

The Details

Due to strong competition in the marketplace from well-funded competitors, LBH's business plan needed to differentiate its service offering and drive higher margin services. Attracting physician groups to LBH requires significant capital outlays over the foreseeable future, including substantial improvements to the physical plant. Due to a significant decline in net patient revenue and operating margins over the preceding years, much of LBH's cash reserves were used to service debt and satisfy pension obligations. Therefore, LBH had significant deferred capital expenditures, which if left unaddressed, would hamper its efforts to attract patients to the facility, recruit new physician groups and ultimately threaten the hospital's existence.

LBH negotiated rates changes, substantially reducing overall labor costs through renegotiating collective bargaining agreements. ESBA, LBH's other professionals and the executive team developed a plan, strategy and vision, creating and implementing financial and operational improvements and held lengthy negotiations with all of the creditor groups (PBGC, Bond Trustee and Unsecured Creditors Committee) to negotiate a structure that focused on up-front payouts and limited continuing obligations on the part of the hospital. Focusing on the business plan initiatives enabled LBH to be successful going forward and provided the required funding of the initiatives. Ultimately the constituencies agreed that a flexible capital structure was essential for the continued viability of the hospital, and agreed to limit the request for continued post-emergence obligations.

LBH was granted the ability to use approved table gaming assessment received by the county from nearby Parx Casino. The hospital's management team, ESBA and LBH's other professionals negotiated a plan of reorganization including negotiating the "exit" funding to enable the hospital to emerge from bankruptcy that would assure of job retention and future job creation — one of the largest challenges.

Overcoming these trials enabled the hospital to continue saving lives in an underserved community, as it has for the last 60-plus years and hopes to do for the next 60-plus years. The primary benefits of this transaction were to allow LBH to remain as a full service acute care hospital for the benefit of the residents of Bristol, PA and to retain more than 1,000 jobs within Bucks County, PA. LBH's realigned capital structure and improved margins positioned the hospital to effectively compete against its larger competitors in the region going forward.

The hospital's emergence/operating plan forecasted for over $20 million in capital expenditure projects over the next five years, which will enable the hospital to upgrade its existing physical plant and sustain a competitive service offering while laying the foundation to attract new physician groups and potentially grow its revenue and capabilities.

The Team

In most walks of life, "who you do it with," or the players on the team (pardon the cliché), are usually as big a part of the success or failure as any other element. This case was a shining example of a multitude of constituents that worked together and gave on points. In addition to ESBA, which served as financial advisor to the hospital, the team included Saul Ewing's Jeffrey Hampton and Adam Isenberg as debtor's/hospital's counsel. Blank Rome's Regina Kelbon and Josef Mintz represented the unsecured creditors committee (UCC). Deloitte's Dan Polsky and Rich Infantino were financial advisors to the UCC. SSG Capital Advisors' Scott Victor, Matt Karlson and Terry Kohler were investment bankers to the hospital as well as the union. And the PBGC and the bond trustee all had representatives involved and were an important part of LBH's emergence.

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The Result

Within a short time after emergence, the hospital had attracted interest from a private hospital group that liked the opportunity and purchased LBH. The group agreed to infuse a significant sum sooner and beyond what was outlined, futhering the hospital's longevity, its ability to succeed and the opportunity to potentially celebrate its 100-year anniversary down the road.

It was and is special to be a part of a turnaround that had such a major impact in a community where not only people's livelihoods but also their lives are preserved. This includes treatment of more than 30,000 patients a year in LBH's emergency room, performing more than 5,000 surgical procedures (both inpatient and outpatient) annually and providing greater than 40,000 home visits annually through its home care division.

As I mentioned at the outset, in the world of restructuring, the highs are the highest, the lows are the lowest, and sometimes it changes by the hour — and there is nothing sweeter than when a company or organization emerges and supplemental events occur that give it an opportunity to continue to succeed. LBH has exceptional people serving this community, and it was our honor to be a part of helping them. abfj

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