

## Financial Pains Pushing Hospitals To Bankruptcy

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*Thursday, Apr 17, 2008* --- Hospitals have been suffering financial woes for a number of years now, and with a faltering economy and a tendency among governments to let the market decide which health care facilities survive, attorneys are expecting to see more hospital reorganizations, and collapses, in the coming years.

Inadequate Medicare reimbursement rates, the rise of new outpatient medical centers and the oversupply of beds are among the factors that are drowning more and more hospitals around the country, driving many into bankruptcy and forcing others to simply shut their doors.

“I think it has hit more of a crisis stage over the last two or three years, and now we're sort of in the depths of the crisis,” said Andrew Sherman, vice chair of the creditors' rights and bankruptcy reorganization practice at Sills Cummis & Gross PC. “At this stage, government is trying to allow market forces to take down hospitals, but the problem is that market forces may take hospitals away from individuals who need it. That's what makes a hospital unique, is that the community really needs it.”

Among those that have taken cover under Chapter 11 protection in recent years are Brotman Medical Center Inc. in Los Angeles, South Beach Community Hospital in Miami and New Jersey's Pascack Valley Hospital and Bayonne Medical Center.

New York City's St. Vincent Catholic Medical Centers emerged from bankruptcy last August, after two years in Chapter 11.

Other hospitals have instead been forced to close down. Holy Cross Hospital in Fort Lauderdale, Fla., for instance, recently announced that it had purchased the nearby, money-losing North Ridge Medical Center and planned to shut its doors.

St. Francis Hospital & Health Center in Blue Island, Ill., also said earlier this month that it would shutter its operations, although it plans to build a new \$140 million hospital in Janesville, Wis.

Many of these hospitals have closed because a drop in demand has left too many empty beds, and state governments have often been reluctant to step up and provide funding, attorneys said.

New York grew significantly “over-bedded” as occupancy declined by 17.5%

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over 23 years, according to a study released in November 2006 by a nonpartisan panel appointed to assess the state's short- and long-term health care systems.

Across the state, the occupancy rate fell to 65.3% in 2004 from 82.8% in 1983, leaving about one-quarter of hospital beds open, the study found. Over that time, 70 hospitals, as well as 63 nursing homes, closed down, it said.

To revive New York's health care system, the commission recommended cutting inpatient capacity by about 7%, or 4,200 beds. It also suggested reconfiguring certain facilities by, for instance, joining certain hospitals and medical centers, downsizing some and converting others to outpatient or urgent care centers.

The financial crisis for hospitals was particularly heightened after National Century Financial Enterprises, one of the U.S.' biggest health care lenders, went bust in 2002, according to an article by attorneys at Buchalter Nemer.

Since then, hospitals have also struggled to deal with repeated freezes on Medicare reimbursement rates and drops in Medicaid payment rates, which have made it difficult to care for growing numbers of uninsured patients, the attorneys said.

"Hospitals have traditionally run on very tight margins, so changes in circumstances have been very hard to deal with," said Mary Rose, an author of the Buchalter Nemer article and a partner in the firm's business practices and health care groups. "You have the tightening of government funding through Medicare and Medicaid over the past few years, and there may be further tightening in the future."

And when Medicare overpays a hospital and then seeks to recoup the difference, it cuts into the hospital's cash flow, added Rose's co-author, Benjamin Seigel, a partner in the firm's financial solutions practice.

"You're waiting a long time to get reimbursed, and it's the same thing with private insurance, so you have got to have a whole lot of money in the bank to wait and get the payments," Seigel said.

The fact that Medicare reimburses hospitals according to the procedure a patient receives, instead of the amount of time he spends under its care, works against a hospital's mission to treat patients according to their individual needs, Sherman noted.

"The shorter the length of the stay, the more profitable the hospital," he said. "It's counterintuitive; it's an economic incentive to kick you out as quickly as possible."

Hospitals located in areas where large parts of the population are uninsured also tend to suffer as a result, said Robert Richards, a partner in the corporate reorganization and bankruptcy practice at Sonnenschein Nath &

Rosenthal LLP.

“It's possible that might change depending on who becomes president in 2009, but in a lot of hospitals where people come into the emergency room without insurance, there's a lot of pressure on them to survive,” Richards said.

In addition, the rise in specialized medical centers that provide outpatient surgeries, MRI scans, physical therapy and other procedures has cut into lucrative business for general hospitals, attorneys added.

However, not all hospitals are hitting financial turmoil. Those moving into up-and-coming suburbs or areas where employment remains strong are continuing to do well, Richards said.

So a hospital like St. Francis, which announced plans on April 2 to close its century-old Blue Island, Ill., facility after losing more than \$40 million, may prosper in the expanding commuter community of Janesville, Wis., he said.

Nonprofit hospitals also tend to fare better because they have more options for finding the funding they need, Rose and Seigel said. As banks have become increasingly disinclined to lend costly money to hospitals, private hospitals are instead having trouble finding the funding they need to stay alive.

“The hospitals that survive best are the nonprofit hospitals,” Seigel said. “They are able to raise money through a whole host of charitable activities, they raise fortunes of money. For-profit hospitals can't do that.”

Still, when hospitals do file for Chapter 11 protection, their significant public value works strongly in their favor, as most parties to their bankruptcy proceedings, including the judge, would prefer to keep the facility open.

To find the financing needed to reorganize, hospitals can sell or lease back their real estate, downsize their operations by, for instance, closing down costly emergency rooms, forming joint ventures with clinics or urgent care facilities or converting to a nonprofit corporation that can solicit donations, Rose and Seigel said.

“Emergency rooms are often very expensive for hospitals, and under federal law, they have to treat whoever shows up, and many of those people can't pay and are using hospital emergency rooms for primary care,” Rose said. “What would relieve that would be clinics or other primary care facilities nearby.”

A hospital's success in bankruptcy court, however, depends largely on the symptoms it suffered before reaching for Chapter 11 protection, said Richards.

“If a hospital is over-leveraged, there are things you can do about that,” he

said. “If it's got Medicare problems, especially past overpayment issues, it's much harder to fix, unless the government determines that it wants to work with you.”

So far, however, New York is one of just a few states that have taken steps to examine, diagnose and attempt to cure their health care systems, even if that means letting some hospitals die. As long as the credit crisis persists and Medicare reimbursement rates remain low, many hospitals are unlikely to see improvements in their financial health, attorneys said.

“Across the country, with Medicare rates being out of touch and the increase of surgical centers, you will see more hospitals having to seek bankruptcy protection, at least over the next few years,” Sherman said. “There needs to be a form of planning on a statewide basis saying 'Where should health care be?' You can't allow market forces to come in and decide where health care should be delivered, because market forces may take hospitals away from individuals who need them.”