



KENAI PENINSULA BOROUGH

Legal Department

144 North Binkley Street • Soldotna, Alaska 99669-7520

Toll-free within the Borough: 1-800-478-4441, Ext. 2120

PHONE: (907) 714-2120 • FAX: (907) 714-2379

www.borough.kenai.ak.us

MIKE NAVARRE
BOROUGH MAYOR

MEMORANDUM

TO: Kelly Cooper, Assembly President
Members, Kenai Peninsula Borough Assembly

THROUGH: Mike Navarre, Borough Mayor *MD*

FROM: Colette Thompson, Borough Attorney *CT*
Angela Ramponi, Special Assistant to the Mayor *AR*

DATE: June 7, 2017

SUBJECT: Ordinance 2017-14, Approving an Operating Agreement with Central Peninsula General Hospital, Inc. for Central Peninsula Hospital and Other Medical Facilities

The borough administration and hospital administration have been negotiating a new operating agreement for the hospital and other medical facilities for the past 6 months. Following is a summary of the most significant changes to the existing contract with Central Peninsula General Hospital, Inc. ("CPGH, Inc.") to operate Central Peninsula Hospital and other facilities on behalf of the borough and the Central Kenai Peninsula Hospital Service Area. The attached tables outline new reporting and approval requirements.

1. The title of the document was changed from "Lease and Operating Agreement" to "Operating Agreement". Modifications were made to language throughout the document to reflect this change. In the past, the term "Lease" in the title has resulted in some issues with bond financing. The term was taken out of the title to mitigate these concerns. The borough continues to lease the property to CPGH, Inc.
2. Paragraph 4, Term. The new agreement includes a ten-year term, which is the same as the existing agreement. However, it provides for a five-year renewal instead of a ten-year renewal if no notice of termination is given one year before the ten-year term expires.
3. Paragraph 6, Communications with the Borough. New notification and communication requirements were added, including monthly meetings with the borough administration, several annual lists (discussed in Item 5 below) and other notifications in accordance with the Agreement. Language was also added addressing the IRS Form 990. The Form 990 is an Internal Revenue Service form that provides financial information about nonprofit organizations. Currently, CPGH, Inc. is required to complete this publicly available form. Language was inserted stating that, in the event CPGH, Inc. is no longer mandated to complete the form, the borough can require additional reporting of measured previously available on the Form 990.
4. Paragraph 8, Taxes; Cooperation on Bond Financing; Tax Exempt Status; Safe Harbor Compliance. Additional subparagraphs were added to this section to address both parties' concerns about bond financing, tax-exempt status, and safe harbor compliance.

5. Paragraph 9.c, Purchasing Procedures was modified to remove the requirement that the borough contract administrator approve all changes to CPGH, Inc. purchasing policies. The new language requires that CPGH, Inc. establish and follow competitive procedures, that copies of all updated policies related to purchasing are provided to the borough annually, and that the purchasing policies are publicly available.
6. Paragraph 10, Annual List Reporting Requirements. This new section was added to improve communication between CPGH, Inc. and the borough. On or before April 1 of each year, CPGH, Inc. must provide an updated annual list consisting of the following elements: Hospital Assets Schedule, Annual Projects List, Property Lease List, and Purchasing Policies List. The list will include information about capital infrastructure assets; major movable equipment assets (MRIs, CTs, etc.); all real property leases the hospital has entered into; any updated purchasing policies; and maintenance projects, capital projects, and equipment purchases planned for the next year.
7. Paragraph 11, Maintenance and Repair. The previous agreement considered repairs either “Routine Repairs” or “Major Repairs”. However, the agreement did not provide definitions. The new agreement defines both “Minor” and “Major” Maintenance based on the American Hospital Association estimated useful life of the asset¹. All Major Maintenance must be approved by the borough contract administrator, and CPGH, Inc. is required to notify the borough of Minor Maintenance Projects exceeding \$100,000. For example, replacing a large stretch of lights would be considered Minor Maintenance and not require borough approval. However, if this project was large enough to cost \$100,000 or more, advance notification would still be required.
8. Paragraph 12, Major Movable Equipment Purchases. A new section was added addressing Major Moveable Equipment Purchases, such as purchasing a new MRI machine. Consistent with the goal of improving both communication with the borough and flexibility for the hospital, the group determined that medical equipment purchases are an area where additional flexibility for the hospital is warranted. The details of such purchases, including assessing the type of equipment needed, the specifications of the equipment, the manufacturer, etc., are details best suited for analysis by the hospital administration. The new section requires assembly approval for equipment purchases costing \$2 million or more or requiring a state Certificate of Need. State Certificates of Need are required for certain projects costing over \$1.5 million.
9. Paragraph 13, Capital Improvement Projects. The capital improvement project section was revised to spell out communication and reporting requirements throughout the capital project process. Additionally, the thresholds for projects requiring assembly approval were raised. Under the new agreement, all capital improvement projects costing \$1 million or more, or that require an appropriation, require assembly approval. Contract administrator approval is needed for certain projects below that threshold, such as leasehold improvements costing \$100,000 or more. The attached tables outline approval requirements in more detail.
10. Paragraph 14, Real Property Acquisitions and Leases. A new section was added to clarify the requirements for real property acquisitions. All real property acquisitions, defined as acquiring any interest in real property that may obligate the borough in any way, require approval by the assembly. This includes all purchases of land or buildings, and any leases that obligate the borough in any way. Further, the process of acquiring these properties will be led by the borough.

¹ Copies of the American Hospital Association Estimated Useful Lives of Depreciable Hospital Assets, Revised 2013 Edition, will be available for assembly member review during committee meetings and assembly meetings or upon request at the mayor’s office.

Leases in the name of CPGH, Inc. as Lessee that do not obligate the borough in any way are not subject to these requirements. However, any such leases costing \$100,000 or more annually do require borough approval. For example, a storage space rented in the name of CPGH, Inc. for \$10,000 annually would need to be reported to the borough, but does not require approval. Additionally, the cumulative annual cost of all such leases is capped at \$400,000. Increases to the cap require assembly approval.

11. Paragraph 15, Subleases of Medical Facilities. A new section was added to address subleases to third parties. Previously, the contract required borough approval of all such subleases. In cases such as the Specialty Clinics building, which rents out office spaces to physicians, this would require significant borough involvement in operational decisions. To address this concern, the new section authorizes CPGH, Inc. to negotiate subleases under specific conditions, including giving advance notice to the borough contract administrator before executing the lease, the lease being in furtherance of the purposing of the Agreement, and the lease being at fair market value. Leases over \$250,000 or more per year require approval by the contract administrator.
12. Paragraph 16, Finances. This paragraph was revised to clarify that all transfers from the Plant Replacement and Expansion Fund (PREF) require appropriation by the assembly. The \$250,000 minimum limit on funds transferred from the PREF was removed, clarifying that any transfer of any value from this fund requires assembly approval. While PREF funds cannot be spent without appropriation, the CPGH, Inc. Operating Reserve can be spent in accordance with this agreement. The Operating Reserve may hold up to “90 days cash-on-hand”. The days-cash-on-hand ratio used in the health care industry represents the number of days an organization can continue to pay its operating expenses without new income. This 90-day limit is unchanged from the last agreement. The Memorandum of Agreement referenced contains details regarding management of PREF funds and is still being finalized. A copy will be provided to the assembly prior to final hearing on this ordinance.
13. Paragraph 18, Accounting/Audit/Reporting. Subparagraph (c), Audit was revised to require the auditors to give presentations to the assembly as well as the CPGH, Inc. board.

Subparagraph (e) Hospital Executive Incentive Plan was added to ensure access to data that may be needed for bond financing purposes. Incentive plan structures for “key employees”, such as executives, cannot take into account or be contingent upon a share of net profits from the medical facilities. The borough requires access to this information to ensure compliance. The new language requires that CPGH, Inc. provide any and all incentive plans for key employees, as defined by the IRS, to the borough upon request.
14. Paragraph 21, Defense and Indemnification. A defense and indemnification clause to protect the borough was added to the contract. Previous contracts did not have such a clause; however, due to the growth of the hospital over the term of the last agreement, the borough team felt it was appropriate to add one at this time.
15. Paragraph 24, Level of Services and Other Business Activities. The approval requirements in subparagraph (b) Expansion of Services/New Services were revised. The previous contract required prior notice of new or expanded services with a capital cost “in excess of \$250,000 on an annual basis”. The revised contract removes the reference to annual capital costs, requires assembly approval for all new or expanded services with an expected total capital cost in excess of \$250,000 and for all joint ventures.

Throughout the rewrite process, the teams worked to pair increased flexibility with improved communication between CPGH, Inc. and the borough. As the health care landscape continues to undergo

significant changes, the parties recognize that the hospital will need flexibility to adapt to a quickly evolving system, and that the borough will need avenues to remedy any concerns and to ensure that the best interests of the residents are being met. Robust communication between the two entities, structured vehicles for feedback and updates, and increased authority for the hospital to make certain operational decisions achieve this balance.

Your consideration and approval would be appreciated.

Reporting and Communication Requirements

Item	Description	What is included on list	Change from 2008
Annual Hospital Assets Schedule Par. 10.b	Annually updated breakdown of important capital infrastructure assets and major moveable equipment.	Assets, location, remaining useful life	*New*
Annual Projects List Par. 10.c	Annual list of reportable maintenance projects, equipment purchases, and capital improvements for the upcoming year	Project description, schedule, estimated cost, location	*New*
Annual Property Lease List Par. 10.d	All real property leases regardless of term length or cost All other operating and capital leases with terms greater than 1 year	Leased property, lessor/lessee, term, and cost. Copies of leases upon request	*New*
Annual Purchasing Policy List Par.10.e	Annual list of policies related to purchasing	List and copies of all policies that have been updated in the past year	*New*
Monthly Financial Report Par. 6.a	Written financial report	Balance sheet, cash flow statement, income statement, operating statistics	New template sample report attached to agreement
Quarterly Activity Report Par.6.b	Activity report, written and presented to assembly	Financial report plus statement of activities, issues and events	Unchanged
Updated CEO Contract Par.18.d	CEO contract	Full copy of contract	Unchanged
Executive Incentive plan Par 18.e	Incentive plan for all "key employees" (IRS definition)	Full copies of plans upon request	*New*
Form 990 Par.6	IRS Form 990 Information – reporting not needed when the form is publicly available, but may be needed in the event CPGH, Inc. is no longer required to complete the form	Info previously available on the 990 as required by KPB	*New*

Thresholds for Borough Approval

Item	Reporting	Contract Admin	Assembly	Other KPB Involvement
Maintenance and Repair Par. 11	Notify before all major maintenance and minor maintenance exceeding \$100,000 Annual list & notify when starting work	Major maintenance & minor maintenance exceeding \$100,000 that was not included on the annual list	N/A	KPB reserves right to manage any major maintenance projects. KPB can require submittals for approval of components, equipment and material for major maintenance projects. KPB can require major maintenance
Major Moveable Equipment Par. 12	Exceeding \$250,000 Annual list & notify when equipment is purchased	N/A	Exceeding \$2M or requiring Certificate of Need	
Capital Improvement Projects Par. 13	Exceeding \$250,000 or requiring permit* Annual list, notify at start, periodic updates, notify at completion.	Leasehold improvements over \$100,000 Projects requiring a permit*	Exceeding \$1M	KPB reserves right to manage any capital improvement project, and shall manage any project in excess of \$1M unless contract admin gives authorization to CPH to manage Can require submittals for approval on components, equipment, and material for any capital improvement project
Capital Improvement Planning Par. 13.a	Projects expected to cost in excess of \$1M	Involved in planning for all projects in excess of \$1M	N/A	Borough purchasing and contracting involved in all aspects of planning CPH may spend less than \$25K on preliminary conceptual designs, diagram, etc. before notice
Real Property Acquisitions Par 14.a	All real property acquisitions	N/A	All	All real property acquisitions are conducted by KPB unless CPH is given written authorization to do so
Leases (in which CPH is the lessee) Par. 14.b	Included in annual list	\$100K or more annual cost (each lease)	Exceeding \$400K annual cumulative cap	Cannot obligate KPB in any way; leases must contain clause stating this
Subleases Par. 15	Notify 7 business days prior for under \$250K, and 21 days prior for over \$250K	\$250K or more annually (each lease)	N/A	Requirements for leases to be at fair market value, in furtherance of purposes of Agreement, within authorized powers of the Service Area
New or expanded services Par. 24.b	Prior notice of all new or expanded services	N/A	Exceeding \$250,000 capital cost, and all joint ventures	All other approval requirements apply to new & expanded services

*requiring a permit through any Authority Having Jurisdiction as defined in the International Building Code, such as the 2006 IBC Section 105.2., impacting Life Safety Requirements, and/or decommissioning any asset or part of assets identified on the *Hospital Assets Schedule*

Definitions

1. **Reportable capital infrastructure assets and major maintenance:** Assets included in Part 1 of the AHA Estimated Useful Lives of Depreciable Hospital Assets, Revised 2013 Edition shall be used with a projected useful life in excess of eight (8) years. Major maintenance is renovation or replacement of any of these assets.
2. **Major Moveable equipment:** Equipment identified in the AHA Estimated Useful Lives of Depreciable Hospital Assets, Revised 2013 Edition, under Table 8, Diagnostic and Treatment Departments
3. **Capital improvements:** All projects not identified as Minor or Major Maintenance, Major Moveable Equipment, or Property Acquisitions.