

Kenai Peninsula Borough

Office of the Mayor

MEMORANDUM

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

THRU: Charlie Pierce, Borough Mayor *JCB*
James Baisden, Chief of Staff *JCB*

FROM: Colette Thompson, Borough Attorney *CT*
Brandi Harbaugh, Finance Director *BH*
Kim Saner, Human Resources Director *KS*
John Hedges, Purchasing and Contracting Director *JH*

DATE: October 24, 2019

SUBJECT: Ordinance 2019-32, Approving an Operating Agreement with South Peninsula Hospital, Inc. for South Peninsula Hospital and Other Medical Facilities (Mayor)

The borough administration and South Peninsula Hospital, Inc. ("SPHI") representatives have negotiated a new operating agreement for South Peninsula Hospital and other medical facilities. Following is a summary of the most significant changes to the existing contract with SPHI. Many of the changes align this agreement with the Central Peninsula Hospital, Inc. Operating Agreement which is expected to ease the borough's efforts to administer both agreements and provide SPHI with more flexibility. It also provides SPHI with clearer reporting requirements by listing them in a separate paragraph. Further, it provides for regular communications with the borough administration and departments.

1. The title of the document was changed from "Lease and Operating Agreement" to "Operating Agreement". Modifications were made throughout the document to reflect this change. In the past, the term "Lease" in the title has resulted in legal concerns with obtaining bond financing due to the strict limitations on private use of tax exempt bond financing. The title was also changed as it is in fact an agreement to operate the medical facilities. While the borough continues to lease or sublease property to SPHI for the nominal sum of \$1 per year, all revenues and expenditures of SPHI under this agreement are an enterprise fund of the borough.
2. Paragraph 4, Term. The new agreement includes a ten-year term, which is four years longer than the expiring six-year agreement. It was increased to address concerns about difficulties recruiting and retaining qualified administrative staff and service providers under a shorter term

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agreement. 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. This is the same length as the current Operating Agreement with Central Peninsula Hospital, Inc.

3. Paragraph 6, Communications with the Borough. New notification and communication requirements were added, including making reasonable efforts to meet at least quarterly with the borough administrator, providing new annual information and other notifications.
4. Paragraph 8, Taxes; Cooperation on Bond Financing, Tax Exempt Status; Safe Harbor Compliance. Additional subparagraphs were added to address 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 SPHI purchasing policies. The new language requires that SPHI 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 SPHI and the borough. On or before March 1st of each year, SPHI must provide an updated annual list including capital infrastructure assets; major movable equipment assets (e.g. MRIs, CTs, etc.); all current SPHI real property leases; all updated purchasing policies; all maintenance projects, capital projects, and equipment purchases planned for the next year, and a report describing SPHI's risk management program.
7. Paragraph 11, Maintenance and Repair. The previous agreement did not clearly define maintenance and repair projects. The new agreement defines both "Minor" and "Major" Maintenance based on the American Hospital Association estimated useful life of the asset. All Major Maintenance must be approved by the borough contract administrator, and SPHI 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 if it cost more than \$100,000 because of the type of work performed. However, if this project 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

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diagnostic equipment. The new section requires reporting all such purchases costing more than \$250,000, and assembly approval for purchases costing more than \$500,000 or requiring a Certificate of Need.

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 \$500,000 or more that were not previously appropriated, require assembly approval and appropriation. Contract administrator approval is needed for certain projects below that threshold, such as leasehold improvements costing \$100,000 or more.
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. Further, the process of acquiring these properties will be led by the borough.

Leases in the name of SPHI 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 SPHI 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. The new section authorizes SPHI 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 of \$250,000 or more per year require approval by the contract administrator. Any sublease of the hospital property owned by the City of Homer and leased by the borough will require approval by the City of Homer.
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. While PREF funds cannot be spent

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without appropriation, the SPHI Operating Reserve can be spent in accordance with this agreement. The Operating Reserve may hold up to "90 days' cash-on-hand".

13. Paragraph 17, Performance Measures. This section requires objective standards to be identified in the SPHI Strategic Plan against which SPHI performance will be measured. It also requires SPHI to prepare a Strategic Plan within the first 12 months of the agreement, maintain certification and staffing requirements, funding requirements for the now grandfathered pension plan, and processes to be followed to address problems if performance consistently does not meet the standards.
14. Paragraph 18, Accounting/Audit/Reporting. Subparagraph (c), Audit was revised to require the auditors to give presentations to the assembly as well as the SPHI board and Service Area Board. Subparagraph (e) Hospital Executive Incentive Plan was added to ensure access to incentive plan information that may be needed for bond financing compliance purposes.
15. Paragraph 21, Defense and Indemnification. A defense and indemnification clause to protect the borough from liability for certain claims was added to the contract.
16. Paragraph 22, Risk Management. This provision was expanded clarify the objectives and reporting requirements for SPHI's risk management program.
17. 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 \$100,000 on an annual basis". The revised contract 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.

As the health care landscape continues to change, 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 the best interests of the borough and its residents are being met. Regular communication between the two entities, structured vehicles for feedback and updates, and increased authority for the hospital to make certain operational decisions are expected to accommodate these requirements.

Your consideration and approval would be appreciated.