

Shake-Up At Sutter Doesn't Stop Construction of Hospital

Sutter Health Moves Ahead On Construction Of Local Mini-Hospital While Sutter's New President Considers Cutbacks At Home, Including Closure Of One Of Sutter's Flagship Facilities To Stay Declining Profits

by Mary Bryant

While an onslaught of winter storms has pushed back the scheduled opening of Sutter Health's new \$20 million hospital

in Mid-County until November, 1995, Sutter Health's new president and chief executive officer Van R. Johnson may be more concerned about the financial drought blighting the health care giant's main cash crop of big-city hospitals in Sacramento.

Johnson, 50, was appointed to head Sutter Health on January 18, and was quick to say that he would keep in place Sutter's ambitious expansion plans even if he wasn't sure pending the outcome of a formal evaluation whether he could keep open both of Sutter's Sacramento hospitals. Johnson replaced former Sutter CEO Patrick Hays, who suddenly resigned last October.

While Sutter's Boardmember Neil Perrington originally announced that a nation-wide search had been ordered to recruit a new CEO in November, Johnson was found closer to home.

Johnson has logged nearly a decade of service to Sutter, and once before replaced his predecessor in an executive shakeup.

That shakeup took place in March, 1993, and was a result of what was termed organizational restructuring that left Johnson working as Sutter's senior vice president and CEO for Sutter Health Central Area and President and CEO of Sutter's Community Hospitals in Sacramento.

Johnson is reportedly expected to stabilize Sutter's 15-hospital network in a fashion similar to the way he took charge of Sutter's Sacramento hospitals. When Johnson was appointed to oversee operations at Sutter's General and Memorial hospitals, the two facilities faced stiff competition from a reorganized, leaner and more efficient Mercy Health system, part of the same system that sponsors Dominican Santa Cruz Hospital, and from a market that was experiencing a jump in managed care plan enrollment.

During the early 1990s, while many hospitals weathered financial storms as a result of consolidating markets and increased rivalries, some did better than others. In Sacramento the contest wasn't that

close.

Between 1992 and 1993, Mercy officials saw an increase in net income of 45 percent from Mercy General Hospital, while Sutter leaders were contending with a weakening margin. Between 1992 and 1993, Sutter officials saw combined net revenues from Sutter General and Sutter Memorial decline by about 15 percent, a trend that has caused Sutter to plan an overhaul of their Sacramento hospitals. Sutter officials have announced that they are evaluating ways to stabilize their Sacramento operations, including the possibility of closing one of the system's flagship hospitals.

Ironically, besides the competition that Mercy has shown Sutter, the managed care market that permitted Sutter to build and grow toward an integrated system may also be guilty of thwarting the successful consummation of former Sutter CEO Patrick Hays' 10-year strategy to have Sutter rival such organizations as Kaiser Permanente and Catholic Healthcare West. With declining revenues from established profit-centers like the Sacramento

Hospitals and increasing demands for capital to cover the costs of new affiliations like the \$20 million to build a small acute-care hospital in Santa Cruz County, Sutter non-operating revenues dropped by 92 percent in 1993, leaving Johnson with what is expected to be a substantial job bracing-up one of the state's premier health networks.

Lots of Pieces

"Sutter Health has a national reputation for being on the leading edge of creating integrated health-care delivery systems. We've come a long way and we have most of the necessary pieces, but we're not fully there yet," said Johnson in a release announcing his appointment. "My challenge will be to take us the rest of the way."

Johnson's other challenge may be to smooth out the road Sutter is to travel. Among the particularly sharp curves will be making sense of a far-flung amalgamation of expensive health care divisions.

Prior to announcing his depart-

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ture last fall, Hays is the individual who is generally credited as being behind Sutter's acquisition of hospitals, physician groups, medical centers and long-term care facilities. A former Kaiser executive, Hays had envisioned Sutter someday rivaling the likes of Kaiser Permanente. However, even with an active bond market to cultivate and solid credit established, Hays saw his work building a billion-dollar self-contained health care delivery network experiencing setbacks. Not only did the health care market compress quicker than most could have imagined and competition prove more daunting, but Sutter executives also experienced their own mishaps.

For instance, while no one could have projected that a state recession might mean state employees would be less willing to take chances switching health care plans when Sutter planners first considered purchasing and promoting their own health insurance plan to be known as Omni Health, the no holds barred battle by Kaiser to take on all new comers and maintain their membership rosters could have been expected. Also predictable was the bitter fight that pursued the break-off of Sutter's once productive relationship with Foundation Health, an early player in the managed care game and one of Sutter's strongest allies until Sutter went their own way.

Still, Sutter's Omni plan is on the move to communities like Santa Cruz, picking up new enrollment and in the past few months posting modest profits.

Omni directors have applied to the state's Department of Corporations for permission take their managed care plan (Omni Health Plan, Inc.) into a number of Bay Area communities, including Santa Cruz County. And, new enrollment by state workers during the plans last open enrollment period has meant more growth for

Omni, one of the state's smaller HMOs.

The second and third quarters of 1994 showed a small profit of about \$800,000, making a noticeable dent in the losses Omni experienced during the 1992 and 1993 calendar years. Between 1992 and 1993, Omni Health reported losses of more than \$3 million.

What's Next?

The question of what is next for the not-for-profit Sutter is a matter of debate. Johnson has a reputation as a strong and capable hospital administrator. Along with members of his board, Johnson has reiterated his support for the integrated health care system concept. However, Sutter Health has apparently now moved from the list of predators to the list of prey, as rumors have been repeated throughout health industry publications that all or part of Sutter Health's 15-hospital, 3,000 physician member system may be coming up for sale. Sutter officials have even acknowledged considering a partnership venture with Columbia/HCA a for-profit, national health care behemoth, Columbia/HCA. Not that all the heat generated some 150 miles away in the state's capitol has helped local Sutter administrators contend with their own rainy days.

"If the weather holds, we will actually be seeing patients the first part of November," estimated Catherine Nichols, who has been appointed as the director of Sutter's Santa Cruz Maternity and Surgical Hospital. "But, please understand that's not cast in concrete because construction projects just don't go that smoothly."

This is a description also fitting of the on-going talks among doctors of Santa Cruz Medical Clinic and Sutter officials.

When Sutter Health executives first announced they would apply for permits to build a local hospital, it was assumed that would mean the doctors who invited Sutter to consider building a hospital would

someday affiliate with one of Sutter's established physician groups.

However, even after Sutter officials announced Sutter had purchased one-third of the company that manages the Santa Cruz Medical Clinic, more was expected. A simple share in ownership of assets is not the kind of commitment Sutter executives are used to settling for when promising to build big new projects for doctors. Physicians who were part one of the west coast's most prestigious medical groups, the Palo Alto Medical Clinic, reportedly got a commitment by Sutter to build \$100 million medical center when they affiliated their foundation with Sutter (a foundation being a kind of non-profit holding company for doctors).

Although, unlike Palo Alto Medical Group members, Santa Cruz Medical Clinic doctors appear to be holding out on Sutter.

While about 20 local independent family practitioners recently finished the process of formally affiliating with the physician foundation sponsored by Catholic Healthcare West after beginning talks well after the time Sutter and Clinic administrators first sat down to strike a deal, the doctors of the Santa Cruz Medical Clinic have seemingly hesitated to expand their share of ownership of the area's most profitable multi-specialty group practice with Sutter.

"The medical clinic is still freestanding. It's not affiliated with anybody at this point," said Nichols, acknowledging that Sutter currently holds a one-third ownership of the Clinic's management and asset corporation, and has established a Bay Area Medical Foundation of its own to form partnerships with physicians.

"Nothing additional has happened yet," said Nichols of the reported on-going discussions between Sutter and the Clinic to form a foundation affiliation. □

Sutter's Sacramento Hospitals Register Impact of Managed Care & More Competition on Profits

