Hospitals - Watsonville ~~the~~ Hospital

COVER STORY

MAKING TOUGH DECISIONS—

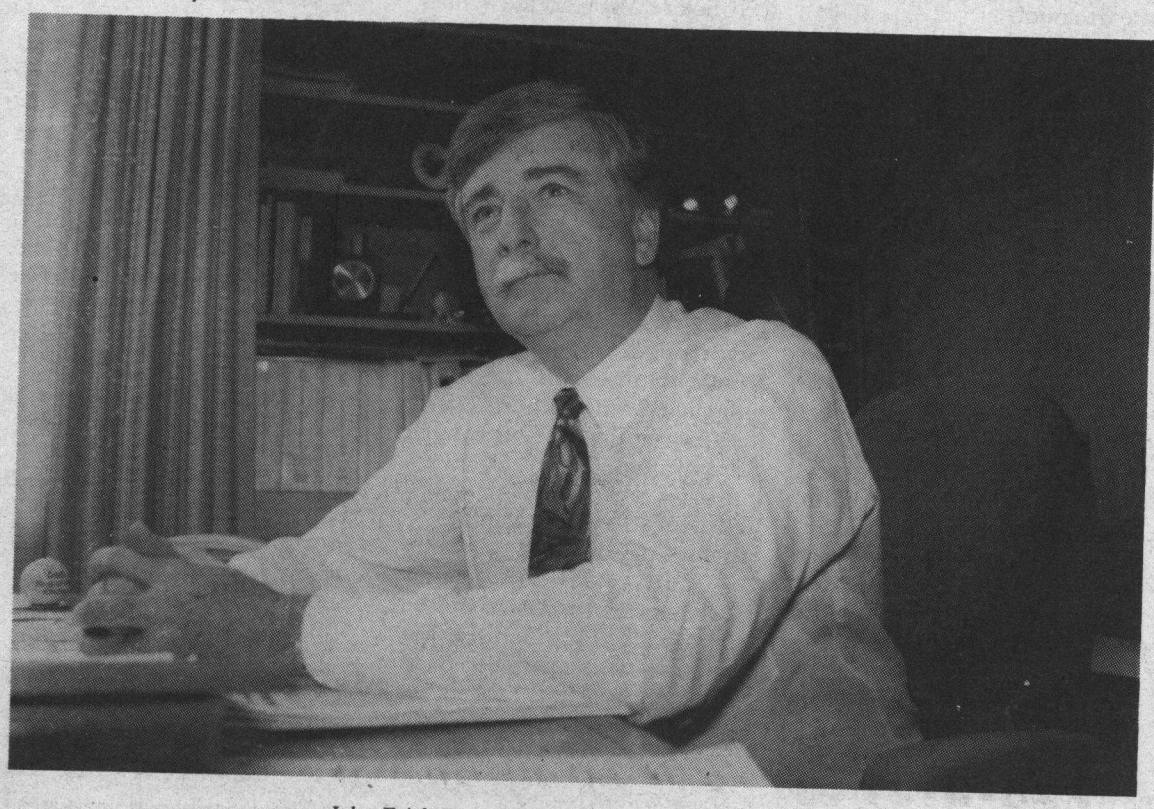
A Year of Choices Lies Ahead for Watsonville Community Hospital

by Mary Bryant

[Editor's Note: The following is the third and final part of a series on the progress of recovery efforts by Watsonville Community Hospital following extensive damage from the Loma Prieta Earthquake].

Imagine you were one of the lucky ones. In an age of turmoil and despair, fate steps in to make you an exception to all the rules. In an industry beset by controversy and conflict, a capricious act of nature offers safe ground for you to address all the difficult questions that lay ahead. In a country where health care dollars have become scarce, the future promises hope and prosperity. Imagine if it were only all true.

Watsonville Community Hospital.



John Friel, President and Chief Executive Officer of Watsonville Community Hospital

Understanding all the problems facing Watsonville Community Hospital is no easy task. But to appreciate the unique nature of all the issues at play, one must also acknowledge the great hopes that hospital leaders have put in the construction of a new medical campus, a project they believe they can have—start to finish—complete within four years from today. These are the hopes that have insulated this revered private non-profit organization from very difficult times and even more difficult decisions. These are the hopes that have kept alive dreams.

To begin, consider the bleak economic trouble that awaits many small hospitals. Then, contemplate the needs of an ever-growing population of people who want more medical attention, but are less and less able to pay the price for modern miracles. Remember that during the past two years combined, you have posted operational losses of $2.2 million.

Now if you aren't already distressed, weigh the prospects of delivering health care for a population of over 100,000 men, women and children in a facility designed almost 30 years ago. Can you ever keep up with all the changes?

But then, you are one of the chosen. A powerful earthquake has shaken the walls of your hospital, yet the main supports of the building's foundations seem to have stood the strain. The repairs are so extensive that you believe the state and federal governments will have to build you a new facility using disaster relief funds.

Now, instead of worrying about tomorrow while struggling through today, your

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doctors and nurses can be busy designing a state-of-the-art medical campus. Instead of trying to decide what programs you can afford to offer the community, you hold meetings with architects and engineers to plan and consider all the new facilities that might be in store for the future. Instead of making difficult choices about what new medical technology you can buy, you can pick from the best on someone else's tab. Instead of fretting about how to build additions to handle the extraordinary increases in out-patient services while in-patient beds go empty, you can design floor plans that make sense for an emerging health care market.

In some ways, it is a dream come true. Or at least it is until you have to wake-up.

Hospital administrators at South County's only acute care facility are now having to cope with a surprising variety of very unpleasant realities, all details they thought were concerns of the past.

Disaster relief funds are presently some $38 million short of the latest construction cost estimates for a new facility. And even if the new federal monies are found to make-up for all the anticipated expenses, a doubtful proposition at best, a state representative responsible for the job believes the state's share of these dollars will, at the least, fall some $13.5 million shy. Plus, to "do the deal," Watsonville Hospital will have to give its biggest and best asset—its current facility, to the federal government as part of the agreement.

This is not to mention that the hospital will also have to, once again, under the upscaled construction cost forecasts, prove to state and national agencies that the repair costs are greater than 50 percent of the replacement price of a new facility, a job that was much more easily accomplished when the construction projections were only $48 million, instead of the $74 million in 1996 dollars that are now anticipated.

Even worse, there are no quick fixes or answers in sight, since the hospital has recently learned it has yet to even complete all the necessary preliminary application forms for government agencies to begin considering increasing funding limits.

But we are probably going a bit fast over some very important points, questions that have yet to be answered.

Learning the Ropes

Trial and error are maybe the most apt words to describe Watsonville Community Hospital's progress on the road to recovery. Then again, there are no maps to follow through the complicated maze of state and federal disaster relief rules and regulations.

In some cases, it is likely the law even has yet to be written. In many cases, the hospital may have to test the limits of many levels of government in its search for much needed cooperation. In short, the future is far from certain. But with this said, let's move on to what we know.

The Challenges

Over two years ago an earthquake roared through most of Northern California, leaving behind an unsurpassed economic and emotional toll in its path.

Lives were lost, homes destroyed, roads shattered, businesses collapsed and great hardships endured. But this really isn't a story about the 1989 Loma Prieta Earthquake, it is an account of Watsonville Community Hospital's attempt to heal from the worst disaster in its almost-100-year history.

The first setbacks to curing the ills of this modern facility were the months it took to begin to diagnose the symptoms (see article: Fixing What Broke, *Mid-County Post,* 1/21/92 edition).

Repairs that were initially estimated at a few million dollars grew to $20 million by March 1990; to $30 million by June 1990; to $48 million for a replacement structure in October 1990; to almost $74 million in January 1992, again for a replacement structure based on a 1996 completion schedule. The more damage found, the more it cost to repair. The closer they looked at what they need in a new facility, the more it cost to build.

Hospital administrators at the South County's only acute care facility are now having to cope with a surprising variety of very unpleasant realities, all details they thought were concerns of the past.

And these are all only projections, and do not take into account the $2.7 million already spent on interim work to bring the existing building back to temporary operational standards.

But determining what went wrong, what needed fixing and how much it cost may yet prove to be the easy part.

This is not to say that designing and constructing an acute health care campus is a simple chore under California's rigorous codes and the constant scrutiny of engineers from the Office of Statewide Planning and Health (OSPHD).

It's just that finding the money to hire scores of designers, pay construction workers, buy new equipment and the like, may prove the greatest challenge of all, especially for a non-profit agency that didn't carry earthquake insurance and which has limited resources to independently launch any substantial construction project.

In other words, Watsonville Community Hospital is an organization that is good at giving thousands of people medical care but now has to rely on others to help define its future.

Disaster Relief Funding

"The problem here is this is a large project. In this particular case, you can safely say that the hospital was somewhat traumatized by this whole situation," Paul Jacks,

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Manager of the Public Assistance Branch of the California Office of Emergency Services (OES) said in a recent interview with *The Post*.

"I mean it is not easy to wake up one day and find out your building is no good anymore... What you have here is a classic case of how the recovery process works in the large scale of things," Jacks added.

Or in this case, it may also mean it takes a long time to work. But maybe when it comes to the blending of both heath care concerns and state bureaucracies, time is relative.

The only other case of a major completed hospital replacement project under the recent disaster relief funding laws is the Olive View Hospital in Southern California, work that took almost 16 years from beginning to end (see article: Southern Californians Know the Feeling). But now, let's look at the playing field and the rules of the game.

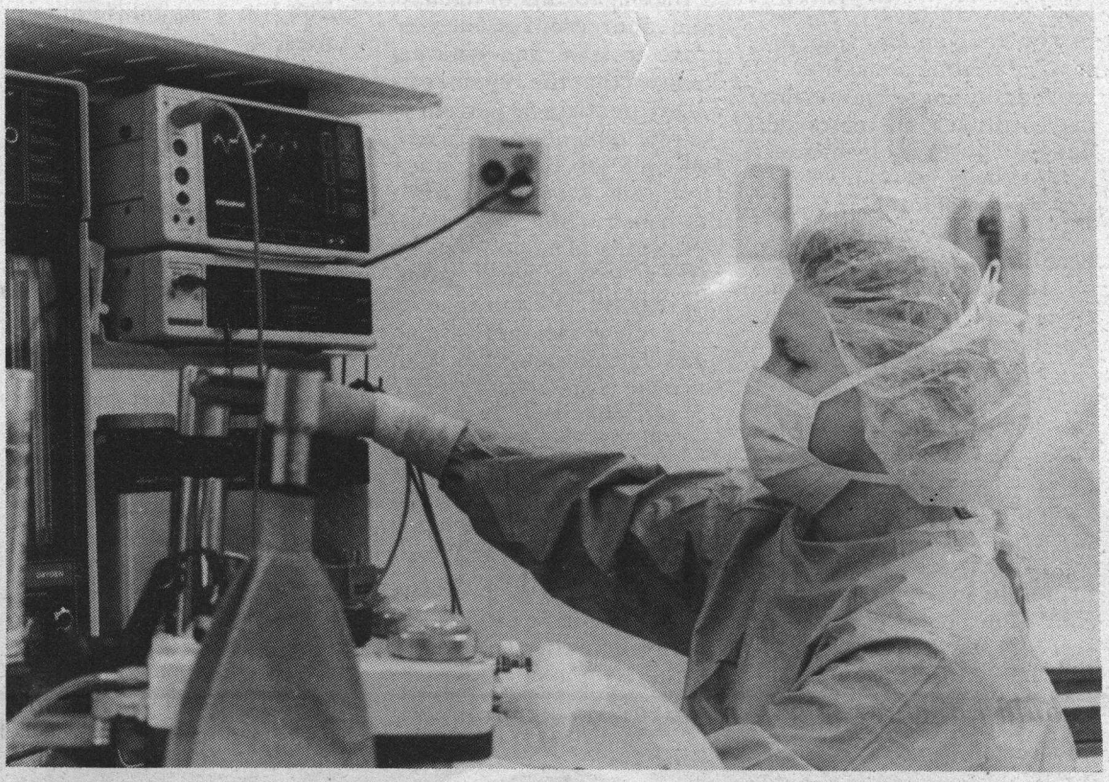
The Federal Emergency Management Administration (FEMA) is the agency charged with disbursing relief dollars to states for eligible victims of nationally declared disasters. FEMA has its own rules, laws enacted by Congress, about who and what is eligible for its programs.

The California Office of Emergency Services (OES) is the state agency responsible for managing the FEMA dollars, giving out grants and funding the portion of monies the federal agency doesn't offer to victims of disasters—in the Watsonville case 25 percent of the cost of repairs. OES also has its own rules, and when it comes to making certain decisions, must bow to the regional FEMA director.

In the case of the South County hospital project, the OES division that oversees the work is the Public Assistance Branch (OES-PAB). The OES-PAB is also the group that handles the repair costs and work needed by public agencies, like counties, cities and school districts.

There are currently only two projects in the range of $50 million under way: Watsonville Hospital and the Oakland City Hall. Jacks, of OES, expects up to 10 big assignments to come through his office in the next year as a result of the earthquake.

With the exception of the hospital and a building on the campus of Stanford University, all the major earthquake funds are designated for public entities. But what they do may not be as important as how they do it.



What's Eligible

Paperwork is the stuff that makes the state disaster relief agency's wheels go around, or at least there's lots of it. Up to the present, Watsonville Hospital's repairs to their current facilities have required at least 40 different project applications to be completed and tracked thought the process. And even with all this effort, the hospital is still shy about $1 million in reimbursements.

Bring this point up to the state and they get a bit testy. Why hasn't the hospital been paid for the eligible work?

"Probably because they haven't requested it. There are these little mechanical things that have to be done," Jacks said. "We have 700 applicants and we don't know when they run out of money."

But it's not the money that has been approved, about $30 million, it's the money that isn't in the hospital's state account that has hospital directors worried, a number close to $38 million. Presently the federal and state agencies have only signed-off on the October 1991 estimate for repairs, a figure far shy of current estimates.

And to understand this point, and much of the story, you will have to remember the first golden rule about disaster relief financing: Spend as little money as possible to get the job done.

In this case, before the hospital can argue for more dollars to build a new building, they must first prove repair costs are going to be more than 50 percent of replacement estimates, and that all claimed expenses on either side of the repair/replacement equation are eligible. And this is the job they thought was once complete.

"What happens here is they [the hospital] send up estimate and say it's going to cost $70 million. Well, the early estimates seemed to please them," Jacks reported. "There was absolutely no dispute over the early estimates. Then all of a sudden you get an estimate in here for $25 to $30 million more. This is bound to raise some concerns that we have to take a look at because there is such a variance between the previous estimate. I'm not saying it is wrong, but what it means is it has to be looked at."

Replacement Versus Repair.

"If that is what they say, that is what they say. But you know, $30 some odd million is not exactly a small chunk of

change. I think there are things that could be done, but some steps are going to have to be taken," Jacks said. "I am concerned about the fact that these steps have not been taken up until now."

It likely should be said in reasonable defense of the hospital's current president, John Friel, that he has only been on the job less than a year, a year that has seen a threatened strike by nurses, operational losses to overcome and a group of doctors proposing to open a competing mini-hospital in Capitola.

Friel says he's on the job now. He also suggests that it wasn't until recently that FEMA representatives suggested the hospital reconsider the originally agreed on construction estimates. This is when he reported that the hospital administrators discovered the problem, an issue that has caused great concern for all.

"Our sense would be that $42 million, plus inflation [$48 million], is not enough to replace what we have. If we had to build a $42 million hospital, it would be smaller," Friel said.

And a smaller hospital doesn't seem to be what anyone wants. In fact, if the preliminary sketches of architects and the reports of consulting planners and futurists are any measure, the hospital community is hoping for, if not bigger, much better.

The new and modern campus proposed so far includes great attention to the design details of what some believe is the future of modern health care.

Instead of semi-private rooms where patients now have to be separated by gender, the new hospital would have private rooms with accommodations so family members could stay and help with some care. Instead of rooms designed to care for patients with illnesses now commonly treated by more sophisticated medications at home, the emphasis would be on tending to the more seriously sick or injured. Instead of out-dated and inefficient work stations, care would flow from centralized units. Instead of labs being separated from too small out-patient surgery services, an out-patient wing would be devoted to the one-day procedures which are taking the place of what used to be lengthy stay operations. Instead of maternity care being given in rooms once built for the sick, a birthing center would provide the latest in choices for women. Instead of waiting in emergency rooms, a "fast track" component would aid workers in the delivery of "urgent" care.

In short, hospital leaders have hoped to bring the best of modern technology to a comfortable setting with all the amenities any patient could want. But back to the catch: they have to find the money.

The Problem May Be The Solution.

Hospital directors are counting on what caused the problem in the first place to now be the solution to their present dilemma.

"The land below is what we seem to have the problem with, in that it fell away from the slab," Friel said. "The fact is that hospitals have to [now] meet an 8.1 earthquake resistance [standard], and this one was built to a 7.1 [code]."

And it is this point that gets a little tricky.

"Land is not eligible yet. It could be. They would have to file a request for relocation which they have never done."

—Paul Jacks, Office of Emergency Services

Soils engineering is a science of its own. If repairing the facility means bringing it up to current code, then engineers won't know exactly what they will have to do to the existing foundation to repair it; that is, they won't know until they tear-up the first floor of the hospital, a job that would only be undertaken if they were to begin repairs.

Experts can estimate, however, that the river bottom land the hospital now sits on is not the best for constructing multi-story facilities. Hospital leaders can also argue that better land exists at a price, and that the price should be paid for through disaster relief.

But this is a claim they will have to sell to almost everyone, since land isn't supposed to be part of the deal, a point that's a bit tougher since the hospital first agreed to pay for the property on its own. That was, until they realized they needed the argument to win monies for the escalated construction estimates.

"Land is not eligible yet. It could be," Jacks said. "They would have to file a request for relocation which they have never done... If it's granted then that becomes a definite factor. Then we are obviously operating on a replacement type of situation... That may be a fact that allows us to get past the 50 percent [repair cost] rule," Jacks added.

But in the case of land, the hospital will have to make its case to the regional FEMA director, since this is one of the regulations that lies at the federal level.

Still Short of Dollars

Every way you look at the deal, the hospital is going to wind-up short of dollars unless leaders were to choose to make repairs in lieu of building a new building. The only question is: How much? And while this discussion could become controversial and lengthy, let's just take a brief look.

To understand this point, we must first consider the "Stanford Bill" passed last year by the state.

State legislators decided, in the case of the only other non-profit agency applying for substantial disaster relief, that $5 million was going to be the limit. In other words, no matter what the state's share of the replacement or repair expenses calculated out to be at 25 percent, there was going to be a cap on spending.

Lawmakers even went as far as to strip private non-profits from coverage under the relief funds for future disasters.

Friel said, in response to these concerns, "We are not going to roll over." But politicians facing California's worst budget disaster in history may not be an easy audience to convince.

"The way you have to look at this is that whatever the ultimate approval is, all the state is going to pay is $5 million... They are just short the amount in terms of the 25 percent [share]," Jacks said.

Responding to the same question, State Assembly Member Sam Farr was only slightly less firm. "I don't know what the status of the funds are right now... But I can tell you that $18.5 million for a hospital from state funding is incomprehensible at this point."

And with this understood we can now examine the most obvious possibilities:

— No more additional monies are approved, leaving the hospital short $38.3 million for a new facility, when you deduct already made repair costs to the current facility.

— FEMA comes up with their part, but there is no more money from the state, leaving the hospital $16.2 million shy of needed dollars.

— Both FEMA and the state come up with the full funding for eligible expenses,

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Repair or replace? The future of Watsonville Community Hospital remains unclear.

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leaving the hospital less in the hole.

But what does the hospital do if it doesn't get the money?

Borrow, according to Friel, a point that may prove to be as controversial as any other.

"Our optimism is still high that the federal government is going to be supportive. I think what we would end up having to do, if the bottom line came down [the fact] there would be no more money, then we would work with the government grant and look at borrowing additional money... Clearly the community needs a hospital," Friel said.

And while how much is borrowed is certainly critical to any discussion, let's look at the short-fall scenario if the state doesn't come up with full funding.

In this case, the hospital would have to pay for about $16.2 million in costs. On a 30-year note at seven percent interest, a fair industry standard, the payment would be $1.3 million a year.

But remember, Watsonville Hospital hasn't shown an operating profit since 1989, and then it was only $939,000.

In fact, if you calculate the revenues using the 1989 profit margin of two percent, the hospital would have had to pick-up about $21 million more for that year in new revenues past inflation, just to break even. This would not allow the institution a margin for reserves or new projects. It certainly wouldn't keep pace with the cost of buying the latest in modern technology.

But there is another way to look at the same dilemma. If the hospital was to earn enough profit to carry the added debt load based on last years revenues, then it would have to increase its bottom line by over three percent, a profit margin they haven't seen in many years.

This is also to beg the question of how much money could be saved in expenses if a new facility proved to be more efficient, but then again this is a time when hospitals across the nation are already having to get by on much less. And, as a point of reference, Dominican Hospital made $230,000 in operational profits on almost triple Watsonville Hospital's revenues last year, a year when Watsonville Hospital lost over $600,000.

But there's more. Taking on new debt while the hospital is already highly leveraged, relies on the premise that "bricks and mortar" will bring patients to your facility.

Some would argue it's doctors that admit patients to hospitals, and that more doctors like to work in population areas with more people—patients who more typically carry insurance and are able to pay bills.

And, doctors tend to not want to travel far from their offices to see those people that they are caring for in a hospital.

Some would also suggest that unless Watsonville Hospital attempts to duplicate some of Dominican's expensive services, like heart surgery, it will have a hard time drawing additional revenue. In other words, the reason some travel away from home is simply because the care isn't available nearby. But to offer these kinds of specialty programs, the hospital would have to consider spending an extraordinary number of their own dollars, or borrow more to build more.

And all of this begs the question: When you are worrying about making it through an operation, do you really care if there's new paint on the walls or an entertainment enter in your room?

Friel has a different way of looking at the same issue.

"Amenities are as important to patients in the hospital as they are in department stores. Comfort in the hospital is very important, privacy is very important... We are thinking that a new location, as well as our new design, is going to make the Watsonville Community Hospital of the future very attractive to people... they will be willing to travel to be here," Friel said.

Solutions

In what has been more a dismal picture than not, there are some hopes that remain.

Again, the hospital may be more apt at raising dollars or finding governmental support than could be expected at this point.

For instance, the hospital has yet to seek the advice of independent FEMA consultants, experts that cities and counties commonly rely on when the going gets tough.

There is also the 90 percent "cash out" solution, which would allow the hospital to withdraw all but 10 percent of what is remaining in their currently approved relief fund account. Under the same alternative, the hospital could also argue for more repair costs that they believe necessary, and then claim 90 percent of what might be a greater amount. These dollars could then be used for any similar community project or could go towards building a smaller and more affordable hospital.

And, finally, there is again the possibility of repairing the present facility.

This is an option Friel, for one, hasn't wanted to look closely at in the past. He points to the fact it would be very difficult, would require closing or relocating many current hospital services for about a year, would necessitate bringing in portable buildings, would create a considerable disruption to providing quality patient care, and would not advantage the institution with a brand new facility in the end. He is even more worried that the hospital would lose market share to competitors and that it might have trouble regaining it once the building was reopened.

These are all good points that are well worth noting. These are all good points, if the hospital can afford the decisions. And these are all points that will play into making the tough choices in the year of decisions that lies ahead for health care leaders. ❑

Editor's Note: The following article originally appeared in the September 11, 1990 edition of the Mid- County Post.