

THE UNIVERSITY OF MICHIGAN
REGENTS COMMUNICATION

Approved by the Regents
June 21, 2012

REQUEST FOR ACTION

SUBJECT: Michigan Health Corporation (MHC) Annual Business Plan

ACTION REQUESTED: Approve the MHC FY2013 Annual Business Plan and Budget

BUSINESS PLAN:

The Bylaws of MHC provide that MHC will annually submit a business plan to the Board of Regents for approval. MHC submitted its last business plan to the Board of Regents in June 2011. Since that time, MHC has focused on the operations of its existing subsidiaries and has exited from the Central Michigan Community Hospital Radiation Oncology venture. In addition, MHC approved several new ventures, Michigan Advanced Development and Manufacturing Center, Michigan Health Ventures Limited Partnership (the parent of Michigan Advanced Development and Manufacturing Center), Physician Organization of Michigan ACO and Paradigm.

MHC will begin its seventeenth year of operations in FY2013. The ventures in which MHC participates are expected to generate approximately \$129 million in net patient revenue in FY2013. MHC's share of these revenues, based on MHC's ownership interest in the ventures, is approximately \$29 million in net patient revenue.

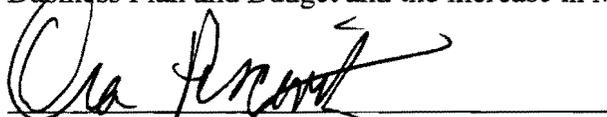
MHC has received prior Regent approval to invest up to \$30 million in venture activity. With the growth of MHC and in order for MHC to continue to invest in new ventures that are consistent with the UMHS strategic plan, MHC needs to increase the investment level.

Paradigm is a venture that has received the support of the Health Affairs Committee and has been approved by the MHC Board of Directors. The total UMHS commitment for Paradigm is \$15 million and as such, MHC requests an increase in its maximum commitment level to \$45 million.

The MHC Board of Directors and the MHC Sole Member Representative have unanimously approved the FY2013 Business Plan and the request to increase the capital investment level of MHC to \$45 million for submission to the Board of Regents.

APPROVAL REQUESTED:

The Board of MHC recommends that the Board of Regents approve the MHC FY2013 Annual Business Plan and Budget and the increase in MHC capitalization to \$45 million.



Ora H. Pescovitz, M.D.

Executive Vice President for Medical Affairs

Chair, Chief Executive Officer & Sole Member Representative, MHC

June 2012

**Michigan Health Corporation
FY2013 Annual Report and Business Plan**

I. MHC OVERVIEW

Introduction

The Fiscal Year 2013 (FY2013) Business Plan for Michigan Health Corporation (MHC) provides an overview of the direction for MHC and its subsidiary organizations, as MHC begins its seventeenth year of operation.

Structure and Governance

MHC is a non-profit, non-stock membership corporation solely owned and operated by the University. MHC is part of the University of Michigan Health System (UMHS).

The MHC Board meets on a regular basis and as necessary to conduct business. The Board of Directors are: Ora Pescovitz, M.D., Executive Vice President for Medical Affairs (Chair and Chief Executive Officer); Douglas Strong, Executive Director of the Hospitals and Health Centers (Vice Chair and Chief Operating Officer); Timothy Slottow, Chief Financial Officer of the University (Treasurer); James Woolliscroft, M.D., Dean of the Medical School (Secretary); and Glenna Schweitzer, Associate Vice Provost and Executive Director of the Office of Budget and Planning for the University.

MHC Subsidiary Organizations

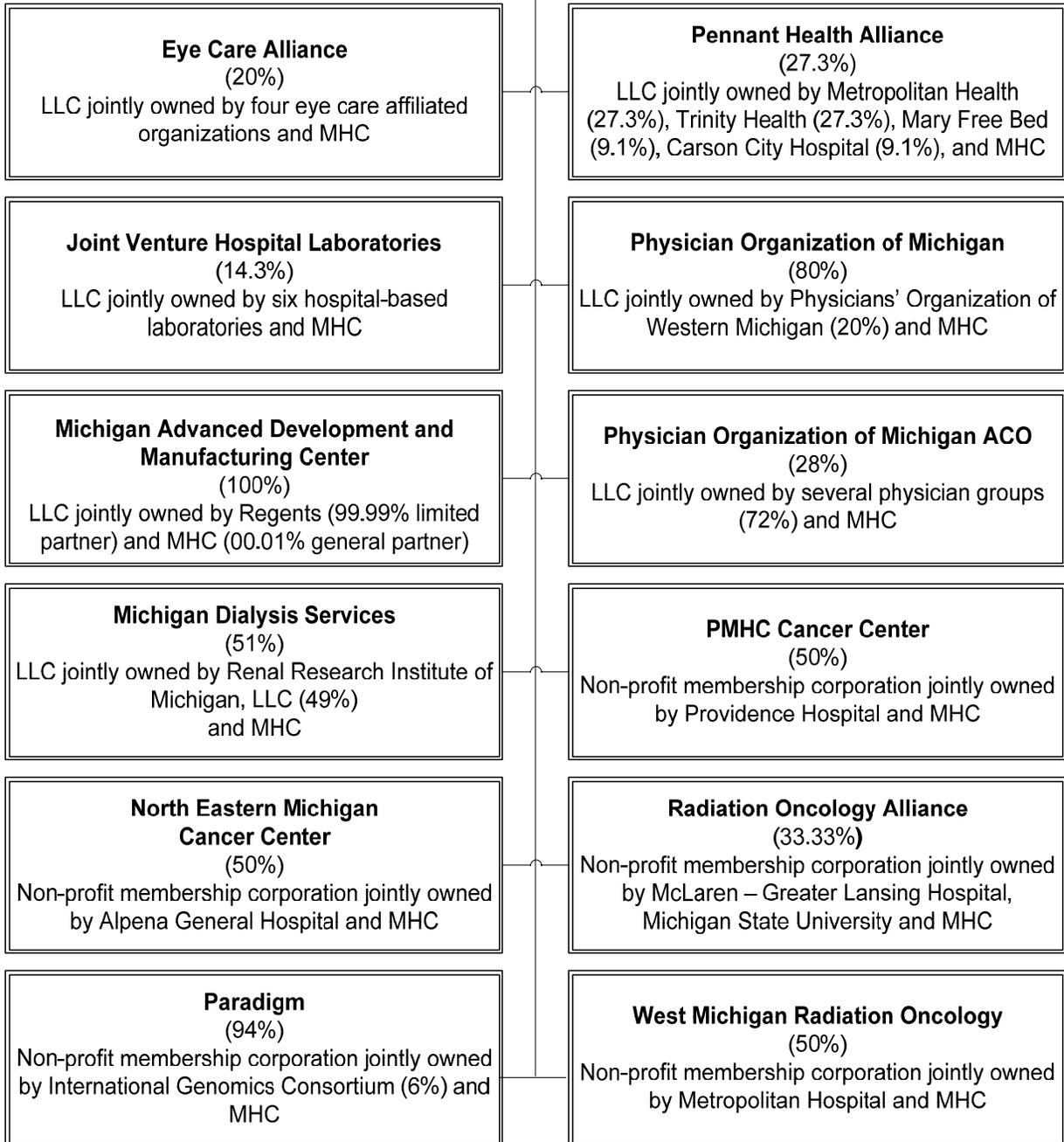
As MHC completes its sixteenth year of operation, the MHC Board has approved a total of twenty-three subsidiary organizations since its activation in 1996. Eleven subsidiaries, or proposed subsidiaries, have been terminated and twelve subsidiaries are operational. During this past year, MHC completed its exit from the Central Michigan Community Hospital Radiation Oncology venture. Ventures that became fully operational include Pennant Health Alliance (PHA) and Physician Organization of Michigan (POM).

Physician Organization of Michigan ACO (POM ACO) was formed to allow UMHS and physician groups to participate in the Medicare Shared Savings Program as an accountable care organization. Michigan Health Ventures Limited Partnership (MHV) was set up with MHC as the general partner to manage its wholly owned subsidiary, Michigan Advanced Development and Manufacturing Center (MADMC). MADMC was established to apply for a potential contract with the Department of Defense (DoD). Finally, Paradigm, a new company to assist physicians treating cancer patients was approved.

In response to other healthcare changes and patient care needs and as part of the UMHS strategic plan, MHC is also investigating relationships with other hospitals, physician groups and healthcare providers in Michigan. The chart on the next page shows each of the current subsidiary organizations under MHC.

Regents of the University of Michigan

Michigan Health Corporation (MHC)
(Non-profit membership corporation wholly owned by the Regents)



NOTE: MHC also owns Class B membership interest in Great Lakes Lithotripsy, LLC.

II. FY2012 FINANCIAL PERFORMANCE OF SUBSIDIARIES

Most MHC subsidiaries are past their development and start-up stages and are now ongoing operations. The exceptions to this are MHV including its subsidiary MADMC, POM ACO and Paradigm which are still being developed. MHC will continue to focus on operational and financial performance reviews and address what management and funding actions to take if subsidiaries do not meet their activity and financial goals. Other than adding new ventures, the most significant change that occurred in FY2012 was the exit from Central Michigan Community Hospital Radiation Oncology.

The Consolidated Statement of Operations on page five summarizes the projected net gain or loss for MHC as a whole and by venture. In FY2012, MHC is projected to have a gain of \$2.3 million which is favorable to budget by \$400,000 for established ventures and MHC Administration. Incorporating the new start-ups that expensed (\$3.4) million, MHC is projecting an overall loss of (\$1.1) million.

III. MHC FISCAL YEAR 2013 BUDGET

The MHC Fiscal Year 2013 Budget was developed from each subsidiary's financial plan, MHC's financial statements, projected results of the subsidiary's operations, and known/planned changes for the coming fiscal year. MHC's consolidated financial statement is displayed on page five. Highlights of the financial statement are identified below.

Consolidated Statement of Operations Summary

The Statement on page five summarizes the FY2012 projected net margin and the FY2013 budget for MHC as a whole and by venture. This summary identifies the direct results of operations of the subsidiaries, but does not reflect ancillary benefits to the Health System such as increased research funding paid to UMHS and professional net income or expanded patient care service opportunities for the Hospitals and Health Centers and the Medical School Faculty Group Practice. MHC is budgeting an overall unfavorable net margin of (\$4,975,845) for FY2013 compared to a projected loss of (\$1,116,769) for FY2012.

In FY2013, all established ventures are expected to have a positive net margin. An exception to this is Eye Care Alliance, which has lost some business due to contract changes. Recently opened ventures are not expected to have a favorable margin in FY2013. The focuses of Physician Organization of Michigan, Pennant Health Alliance, and Physician Organization of Michigan ACO are administrative and network relationships with other hospitals and physician groups in response to the changing health care environment, rather than revenue generation. While they may not have a favorable MHC margin, other units in the Health System receive benefits from these MHC ventures. In addition, Paradigm will be in its start-up phase and have minimal revenue in its first year of operation. Preliminary indications are that the DoD contract will not be awarded to MADMC. The FY2013 margin information included in this Business Plan for MADMC reflects a conservative approach and assumes that MADMC does not receive the contract and only expenses to wind down MADMC will be incurred. Should MADMC be awarded the contract, MADMC could have an average margin of \$250,000 per month.

MHC recognizes its general partner responsibilities in monitoring and approving the activities of MADMC and its notice and consultation requirements with the Regents relating to certain actions as outlined in the corporate agreements establishing this venture. A separate business plan for MADMC will be presented to the Regents when more definitive information regarding the DoD contract is available.

Investments Summary

In 1996, the Regents approved a capitalization level of \$30 million for MHC. MHC has made investments in ventures over the years and many ventures have not only repaid MHC the full investment amount, but have provided cash distributions in excess of the MHC original investment. It is projected that as of June 30, 2013, MHC will have an outstanding investment amount of \$18.6 million, leaving \$11.4 million of the original capitalization available for investment in other ventures.

Through careful planning and monitoring of venture activity, MHC has been able to invest in ventures within the \$30 million limit set by the Regents in 1996. Changes in the health care industry currently necessitate ventures and collaborations on a larger scale. There are now a few specific opportunities that are being pursued by the Health System as part of its strategic plan that require large investments over the next twelve months, and these strategic investments cause us to need a significant increase in the \$30 million limit. Therefore, as part of this Business Plan, MHC is requesting that the capital investment limit be raised from \$30 million to \$45 million. This will allow MHC to proceed with establishing Paradigm, information for which has previously been provided to the Health Affairs Committee.

Michigan Health Corporation
Consolidated Statement of Operations
ProForma Summary of Net Gain / (Loss) by Joint Venture
FY2012 Budget, FY2012 Projection and FY2013 Proposed Budget

	<u>FY2012</u> <u>Budget</u>	<u>FY2012</u> <u>Projection</u>	<u>FY2013</u> <u>Budget</u>
<u>Established Ventures and MHC Administration</u>			
Eye Care Alliance (20.00%)	\$ 16,015	\$ 3,725	\$ (2,040)
Joint Venture Hospital Laboratories (14.3%)	0	0	0
Michigan Dialysis Services (51.00%)	252,365	719,571	214,315
North Eastern Michigan Cancer Center (50.00%)	410,831	420,098	422,419
PMHC Cancer Center (50.00%)	1,583,779	1,455,503	1,269,329
Radiation Oncology Alliance (33.33%)	85,092	48,870	41,053
West Michigan Radiation Oncology (50.00%)	32,891	109,534	91,392
Subtotal Net Gain/Loss	<u>\$ 2,380,974</u>	<u>\$ 2,757,301</u>	<u>\$ 2,036,468</u>
Michigan Health Corporation - Administrative Activity	<u>(423,127)</u>	<u>(422,268)</u>	<u>(546,549)</u>
Net Gain/Loss	<u>\$ 1,957,847</u>	<u>\$ 2,335,033</u>	<u>\$ 1,489,919</u>
<u>Recently Opened Ventures</u>			
Michigan Advanced Development and Manufacturing Center, LLC (100%)	\$ 0	\$ (3,028,000)	\$ (120,000)
Paradigm (94.00%)	0	0	(5,298,347)
Pennant Health Alliance (27.3%)	(267,451)	(237,322)	(225,983)
Physician Organization of Michigan (80.00%)	(851,026)	(186,480)	(462,365)
Physician Organization of Michigan-ACO (28.00%)	0	0	(359,070)
Net Gain/Loss	<u>\$ (1,118,477)</u>	<u>\$ (3,451,802)</u>	<u>\$ (6,465,764)</u>
Total Net Gain / Loss	<u>\$ 839,370</u>	<u>\$ (1,116,769)</u>	<u>\$ (4,975,845)</u>

The FY13 MADMC Budget reflects the cost of closing MADMC because no DoD contract has been awarded at this time. If the contract is awarded to MADMC, MADMC could generate a favorable margin of \$250,000 per month.