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# MEMORANDUM

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Date: July 1, 2014

To: The Honorable Chair and Members  
Pima County Board of Supervisors

From: C. H. Huckelberry  
County Administrator

A handwritten signature in black ink, appearing to be "CHH", is written over the printed name "C. H. Huckelberry".

Re: **Banner Health Potential Assumption of Lease Agreement of The University of Arizona Medical Center–South Campus and the South Campus Operating and Funding Agreement with Pima County**

## Background

As you are aware, The University of Arizona Health Network (UAHN) and the Arizona Board of Regents (ABOR) voted to authorize UAHN and The University of Arizona (UA) to enter into exclusive negotiations with Banner Health. Attached is the agenda item as it went before the ABOR on June 26, 2014, which delineates the Principles of Agreement – the essential elements for negotiations. The executed documents state that Banner will assume the Lease Agreement of The University of Arizona Medical Center – South Campus (UAMC-SC) and the South Campus Operating and Funding Agreement with Pima County.

## UAMC-SC Historical Overview

In June 2004, the Pima County Board of Supervisors voted that the County cease operation of Kino Community Hospital and transfer the state license to University Physicians, Inc. (UPI), the physician faculty practice for The University of Arizona College of Medicine. Under this agreement, the County would lease Kino Community Hospital to UPI and monitor service utilization and growth initiatives. UPI operated the hospital under its property lease with the County using various names for the hospital from June 16, 2004 until June 2010.

In June 2010, the clinical practices, hospitals and healthcare plan affiliated with The University of Arizona reorganized into UAHN. UAHN operates two hospitals now known as UAMC-SC and The University of Arizona Medical Center – University Campus (UAMC-UC), as well as the provider based clinics and related services.

Now renamed UAMC-SC, the Kino Community Hospital has become a modern, full-service teaching facility, training the next generation of healthcare professionals while providing state of the art trauma, surgical, general medicine and behavioral health services to the residents of Pima County. Working in partnership with Pima County, UAHN has been the

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recipient of new federal funds, expanded the array of clinics providing services to local residents, and has greatly increased Graduate Medical Education (GME) fellowships.

Table 1 below shows the improvement in patient and service volume from Fiscal Year (FY) 2003 through FY 2013 (revised and updated from memorandum Amendment to Intergovernmental Agreement with Arizona Board of Regents and The University of Arizona Health Network, Inc. dated May 13, 2014).

**Table 1: UAMC-SC Patient Volume Comparison - FY 2005 to FY 2013**

<b>Category</b>	<b>FY 2005</b>	<b>FY 2013</b>	<b>Change</b>	<b>% Change</b>
Adjusted Patient Days	39,440	86,508	47,068	119%
Total Average Daily Census (ADC)	65	106	41	63%
ICU ADC	2	8	6	300%
Medical/Surgical ADC	13	43	30	231%
Behavioral Health ADC	50	55	5	10%
Total Clinic Visits	48,830	162,821	113,991	233%
Total Emergency Dept. Visits	30,356	42,017	11,661	38%
Total Surgical Procedures	662	3,350	2,688	406%

As Table 1 illustrates, there has been significant growth across several sectors of the hospital; especially in surgical volume, clinic visits and medical/surgical patient admissions. The hospital now includes a renovated and expanded emergency department, a Level IV Trauma Center operating in conjunction with the Level I Trauma Center at UAMC-UC, and a newly opened medical/surgical inpatient ward that has significantly expanded patient capacity at the facility.

Who is Banner?

*Corporate Profile*

Banner Health is a nonprofit corporation based in Phoenix, Arizona that operates, owns or leases hospitals, clinics, nursing homes, clinical laboratories, home health agencies, health insurance and other health-related businesses in seven states. In 1999, Lutheran Health Systems, based in North Dakota, and Samaritan Health Systems, based in Phoenix, merged

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to form Banner Health. The resultant corporation has over 36,000 employees and operates 24 hospitals. Banner Health also operates Banner Medical Group, a 1,000-plus physician group, and Banner Health Network, a 300,000-member insurance and managed care organization.

Banner operates 15 hospitals in Arizona, as well as three research locations and six outpatient or specialty care centers. Of the eight Arizona Banner hospitals rated by Hospital Safety Score, four have received "A" rankings, while two others received "B" scores.

*Financial Report*

The 2013 financial report for Banner Health shows \$8.2 billion in total assets, an increase of over \$600 million from the previous year. This includes \$133 million in cash or equivalent, and receivables in excess of \$500 million for the year ending December 31, 2013. Total liabilities are listed at \$3.9 billion, the majority of which is long-term debt; down from \$4.1 billion in 2012.

For 2013, expenses (\$4.8 billion) account for 95 percent of operating revenue (\$5.1 billion); but with nearly \$600 million in investment income, there was a net gain of \$843 million (\$433 million in net cash from operations). This gain is an increase of 25 percent over 2012 figures. Patient service revenue exceeded \$4.4 billion, a slight gain over the previous year. The "net community benefit" (charity care, unpaid public programs, community and professional activities, contributions, etc.) for Banner Health in 2013 was \$444 million.

*Recent Activity*

On June 9, 2013, Banner officially acquired Casa Grande Regional Medical Center (CGRMC), a 177-bed facility that had recently entered bankruptcy proceedings (December 2013). There is no publically available information on the retention of CGRMC staff, though the newly re-launched website does suggest maintenance of employment and a news article dated February 6, 2014, quotes Banner as promising to hire all existing employees provided they pass background screening. The facility has been renamed Banner Casa Grande Medical Center following the acquisition. The cost of the acquisition is a reported \$87 million.

What rights and/or responsibilities does the County have regarding the Lease and/or IGA to review or provide input on the change in ownership and possibly operations?

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Under the terms of the lease, the lessee (UPH) is prohibited from assigning the lease to any other entity. Thus, any merger or acquisition with the intent of operating the UAMC-SC facility would require the agreement of the County as the sole authority to assign the lease to a new organization.

The intergovernmental agreement (IGA) between Pima County and the ABOR for shared funding of GME is contingent upon GME continuing at the facility following any merger or acquisition. Should the IGA be terminated for any reason, clauses therein will trigger the immediate dissolution of the Lease Agreement.

Who or what organizations need to approve the transaction?

An array of local, state and federal organizations will be required to approve various phases of any merger or acquisition including, but not limited to, the Centers for Medicare and Medicaid Services, the Arizona Department of Health Services (AzDHS), AzDHS Division of Behavioral Health Services, the UAHN Board, the ABOR and others.

Conclusion

The UAMC–SC has come a long, long way since Pima County first transitioned operations in June 2004. I am optimistic the collaboration with Banner Health will provide for the long-term stability of the hospital operations.

As Banner Health, the UA and UAHN negotiate the details of the merger and long-term academic affiliation, the County will continue to work closely with representatives of UAHN to ensure the critical services, operations and financial standards mandated by Pima County are provided and maintained by any future operator.

I will continue to update the Board as additional information becomes available.

CHH/mjk

Attachments

c: Jan Leshner, Deputy County Administrator for Medical and Health Services



**ARIZONA BOARD OF REGENTS  
UNIVERSITY OF ARIZONA  
CANCER CENTER  
1515 N. Campbell Avenue  
Tucson, AZ  
Thursday, June 26, 2014**

**10:00 a.m. JOINT ABOR AND UAHN BOARD MEETING**

UAHN Call to Order  
ABOR Call to Order

**PRESENTATIONS AND DISCUSSIONS**

**UAHN REQUEST FOR AUTHORIZATION**

**Request for Authorization for the University of Arizona Health Network to Enter into Exclusive Negotiations with Banner Health, in Coordination with the University of Arizona and ABOR**

The UAHN Board is asked to authorize the University of Arizona Health Network to enter into exclusive negotiations with Banner Health, in coordination with the University of Arizona and ABOR (collectively UA)

**ABOR REQUEST FOR AUTHORIZATION**

- 1. Request for Authorization for the University of Arizona to enter into Exclusive Negotiations with Banner Health, in Coordination with the University of Arizona Health Network (UA)**

The Arizona Board of Regents is asked to authorize the University of Arizona to enter into negotiations with Banner Health in coordination with the University of Arizona Health Network.

**11:30 a.m. ADJOURNMENT**

**PLEASE NOTE: This agenda may be amended at any time prior to 24 hours before the Board meeting. Estimated starting times for the agenda items are indicated; however, discussions may commence, or action may be taken, before or after the suggested times. Any item on the agenda may be considered at any time out of order at the discretion of the Board Chair. The Board may discuss, consider, or take action regarding any item on the agenda. During the meeting, the Board may convene in Executive Session regarding any item on the agenda.**

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## EXECUTIVE SESSION AGENDA

June 26, 2014

**NOTE:** This agenda may be amended at any time prior to 24 hours before the Board meeting. The executive session is scheduled for 8:30 a.m. on Thursday, June 26, 2014. The executive session may be recessed and continued as necessary.

Statutory Authorization

A.R.S. § 38-431.03

Items to be Discussed

- (A.3)           A.   Legal advice and discussion concerning proposed authorization for the University of Arizona to enter into negotiations with Banner Health, in coordination with the University of Arizona Health Network (UA)

Instruction re: Confidentiality

Pursuant to A.R.S. §38-431.03(B) & (C) all are reminded that minutes of and discussions that occur in executive sessions are confidential by law and that violations of that confidentiality may subject the individuals involved to such penalties as are prescribed by law, including fines, costs, attorneys' fees, and removal from office.

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**Item Name:**        **Request for Authorization for the University of Arizona to Enter into Negotiations with Banner Health, in Coordination with the University of Arizona Health Network (UA)**

Action Item       Discussion Item       Information Item

<b>Issue:</b> The Board is asked to authorize the University of Arizona to enter into negotiations with Banner Health in coordination with the University of Arizona Health Network.
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**Background**

- The University of Arizona Health Network (UAHN) is a private and independent entity which comprises the University of Arizona Medical Center-University Campus, the University of Arizona Medical Center-South Campus, University of Arizona Medical Center-Diamond Children's, University of Arizona Physicians, The University of Arizona Health Plans, and affiliated physician offices.
- After strategic planning and analysis, UAHN identified Banner Health (Banner) as a strategic partner with which it desires to affiliate as outlined in the Principles of Agreement (a copy of which is attached) to enhance and strengthen UAHN operations.
- The University of Arizona (UA), operating the College of Medicine-Tucson (CoM-T) and the College of Medicine-Phoenix (CoM-P) as part of the Arizona Health Sciences Center, works closely in coordination and cooperation with UAHN in areas such as physician training and research.
- As UAHN moves forward with exclusive negotiations with Banner, UA wishes to coordinate with UAHN and Banner in those negotiations, particularly as they relate to Banner's long-term commitments to UA, CoM-T and CoM-P.
- In 1984, the Board leased and conveyed the assets of the hospital to the University Medical Center Corporation (UMCC) (now part of UAHN) to operate the hospital. Once the negotiations with Banner are completed, final Board approval will be required.

**Contact Information:**

Ann Weaver Hart, President, The University of Arizona

520-621-5511 [Hartaw@email.arizona.edu](mailto:Hartaw@email.arizona.edu)

**Statutory/Policy Requirements**

Arizona Revised Statutes, §15-1637 (Lease of Property for Health Care Institution)

ABOR Policy 7-202 (Real Property Ownership and Procedures)

**Discussion and Strategic Implications**

The contemplated transaction is expected to include:

- Banner's 30-year commitment to provide substantial financial support for the CoM-T and CoM-P.
- A 30-year academic affiliation and close collaborative opportunity with a leading Arizona-based non-profit healthcare provider that will allow and encourage the parties to build upon each other's strengths while continuing provision of healthcare services to the people of Arizona, medical education and graduate medical education to UA students, and research opportunities to UA's faculty physicians.
- Significant capital improvements and enhancements to the faculty-based academic medical center in Tucson in support of the CoM-T as well as a new faculty-based academic medical center in the form of Banner Good Samaritan Medical Center to support the CoM-P.
- Banner's assumption of the financial obligations and responsibilities of UAHN's business and clinical operations, including the faculty practice plan; and
- Banner's purchase of the land associated with the University Medical Center.

The action of the Board in this item is to authorize negotiations. Final agreements, such as those for the transfer of assets and sale of land, will be required to be presented to the Board for approval.

**Recommendation to the Board**

It is recommended that the Board authorize the University of Arizona to engage in negotiations with Banner, in coordination with UAHN, that are substantially and materially consistent with the Principles of Agreement as described in this executive summary and to authorize the President of UA and her designees to take all appropriate actions related to those negotiations



THE UNIVERSITY OF ARIZONA  
HEALTH NETWORK



June \_\_, 2014

### **PRINCIPLES OF AGREEMENT**

These Principles of Agreement (these "Principles") for the combination of the University of Arizona Health Network ("**UAHN**") into Banner Health ("**Banner**") and a long-term academic affiliation between the University of Arizona ("**UA**") and Banner will guide the creation of:

- an Arizona-based organization that improves care for all of the State's citizens;
- a state-wide system that reliably and compassionately provides high quality health care throughout all of its providers and facilities;
- a thirty year commitment to UA's College of Medicine – Tucson ("**COM-T**") and College of Medicine – Phoenix ("**COM-P**") that will support the State of Arizona's position as a first tier research and training destination with world class physicians through significant annual funding to establish a secure and sustainable operational foundation and the creation of an Academic Enhancement Fund to support the COM-T and COM-P;
- a nationally leading organization that transforms health care by delivering better care, enhanced service, and lower costs through new approaches focused on wellness; and
- a substantial capital investment in UAHN's facilities and commitment to the Tucson community.

The purpose of these Principles is to set forth certain essential elements and understandings pursuant to which Banner, UAHN, and UA intend to enter into a strategic affiliation through Banner's acquisition of UAHN and its subsidiary organizations and Banner and UA entering into a long-term academic affiliation agreement.

#### **1. Banner's Acquisition of UAHN and Its Subsidiary Organizations.**

1.1 Facilities and Organizations to Be Acquired. Banner will acquire The University of Arizona Medical Center ("**Medical Center**"), the faculty practice plan known as University Physicians Healthcare ("**UPH**"), the three health plans owned by UAHN and UPH, and all other subsidiary organizations of UAHN. Banner also will assume the Lease Agreement of the South Campus of The University of Arizona Medical Center (the "**South Campus**") and the South Campus Operation and Funding Agreement with Pima County.

1.2 Banner's Financial Commitments at Closing. At the closing of the transaction described herein (the "**Closing**"), Banner will:

- 1.2.1 Pay the amount (currently projected to be approximately \$146 million) needed to defease all of the long-term indebtedness of UAHN and its subsidiaries;
- 1.2.2 Assume, whether directly or indirectly, all of the liabilities of UAHN and its subsidiary organizations;
- 1.2.3 Pay \$300 million to UAHN for the sole purpose of establishing the Academic Enhancement Fund (as described below in Section 4.6);
- 1.2.4 Agree to substantial capital commitments for projects to support the clinical enterprise in Tucson (as described below in Section 1.3); and
- 1.2.5 Commit to annual Funds Flow Support Payments (as described below in Section 4.4).

1.3 Banner's Capital Commitment. Banner will spend or otherwise have committed to spend \$500 million within five years of Closing on capital projects in Tucson to support the clinical enterprise. These capital projects will include the expansion and renovation of the Medical Center and construction of a new multi-specialty outpatient clinic and ambulatory surgery center.

1.4 Banner Board Representation. Upon Closing, Banner will appoint one person who is a member of the UAHN Board of Directors to be a voting member of the Banner Board of Directors (the "**Banner Board**") to serve at least one three-year term. If this appointee does not complete three consecutive three-year terms on the Banner Board, Banner will appoint a director who is either a resident of the Tucson community or an individual with university-level academic experience to serve at least through the ninth anniversary of the Closing. Post-Closing, Banner will continue to consider individuals from the Tucson community and individuals with university-level academic experience for membership on the Banner Board.

1.5 Banner's Additional Post-Closing Commitments. Banner will make a number of additional critical post-Closing commitments, including the following:

- 1.5.1 Continuation of key services and programs provided in Tucson for five years after Closing;
- 1.5.2 Co-branding the operations and activities of UPH, Medical Center, South Campus, and Banner Good Samaritan Medical Center ("**BGSMC**") with the Banner and UA names and logos;
- 1.5.3 Prohibition on the sale, closure, or conversion to for-profit status of the Medical Center or BGSMC for ten years after Closing, subject to certain exceptions;
- 1.5.4 Employment of the employees of UAHN and its subsidiaries for at least six months after Closing at their current base salaries and retention of their

seniority for employee benefits purposes, subject to certain requirements and exceptions; and

- 1.5.5 Continued participation of the Medical Center, South Campus, BGSMC, and all UPH physicians in the Medicare and Medicaid programs.

## **2. Faculty Practice Plan and the Banner Academic Division.**

2.1 **Exclusive Practice Plan and Dual Employment.** UPH will be reorganized to become the exclusive faculty clinical practice plan for the COM-T and COM-P. The COM-T and COM-P faculty will provide clinical services exclusively through UPH, with certain exceptions. The COM-T and COM-P faculty will also be employed by UA for educational and research purposes.

2.2 **Banner Academic Division.** Banner will establish the Banner Academic Division that will include the clinical, clinical research, and teaching operations of the UPH physicians; the residency and fellowship programs at the Medical Center, South Campus, and BGSMC; and the medical student rotations from the COM-P and COM-T.

2.3 **Academic Management Council.** Banner will establish the Academic Management Council ("**AMC**") to serve as the Board of Directors of UPH and to oversee the operations and activities of the Banner Academic Division. The AMC will be composed of six persons, three appointed by Banner and three appointed by UA, except in the instance of a prolonged budget deadlock or poor operating performance. One of UA's three appointees will be UA's Senior Vice President for Health Sciences who will also serve as the Chairman of the AMC. The AMC will act by consensus governance or block voting, except in the instance of a prolonged budget deadlock or poor operating performance. The AMC's specific power and authority will be subject to certain reserved powers of Banner. The President of the Banner Academic Division will be employed by Banner and will report to the AMC.

2.4 **Financial Responsibility.** Banner will be financially responsible for UPH and the Banner Academic Division.

## **3. Banner's Purchase of the Land.**

Banner will purchase the land associated with the Medical Center from the Arizona Board of Regents ("**ABOR**") for the purchase price of \$21 million. The proceeds from this sale will be used solely for capital expenditures and operating expenses associated with COM-T.

## **4. Academic Affiliation Agreement.**

4.1 **Long-Term Academic Affiliation.** At Closing, Banner and UA will enter into an Academic Affiliation Agreement ("**AAA**") that will cover both the COM-T and COM-P and require Banner to maintain the Medical Center as a faculty-based academic medical center to support COM-T and transition BGSMC to a faculty-based academic medical center to support COM-P, subject in each case to Banner's ability to provide a substitute or replacement facility. The AAA will have a term of 30 years. Throughout the AAA's term, Banner will be required to provide acute care hospital facilities within the Tucson and Phoenix metropolitan areas with adequate facilities and clinical capabilities to serve as academic medical centers for COM-T and COM-P, respectively.

4.2 Exclusive Partners. UA will be Banner's exclusive academic medical partner in the State of Arizona, except for Banner's relationship with the University of Texas in connection with the Banner MD Anderson Cancer Center and other mutually agreed exceptions, and Banner will be the exclusive hospital academic partner of UA, COM-T, and COM-P. UA's current agreement with Dignity Health for the new cancer center in Phoenix will remain in place.

4.3 Teaching Programs. All current teaching programs will continue. After Closing, any addition, modification, or termination of a teaching program will require approval of the AMC. The number and allocation of COM-T and COM-P residents and fellows will continue. After Closing, the AMC will have the authority to determine the number and allocation of residents and fellows.

4.4 Funds Flow Support Payments. For the first 15 years of the AAA, Banner will budget and fund the following annual funds flow support payments:

- 4.4.1 the amounts funded during fiscal year 2013 by UAHN and Banner to support the teaching programs and related clinical practices at the Medical Center, the South Campus, BGSMC, and UPH (the "**Base Funds Flow Support Funding**"), plus
- 4.4.2 \$20 million (the "**Incremental Funds Flow Support Funding**"), plus
- 4.4.3 a variable amount equal to one-half of the combined operating income of the Medical Center, BGSMC, and UPH in excess of a 5% operating margin ("**Variable Academic Support Payment**").

The Base Funds Flow Support Funding and Incremental Funds Flow Support Funding will be subject to adjustment based upon certain changed circumstances. In addition, Banner and UA will renegotiate (within certain limits) the amounts of the Base Funds Flow Support Funding, Incremental Funds Flow Support Funding, and Variable Academic Support Payment to be applicable during the last 15 years of the AAA.

4.5 Use of Funds Flow Support Payments. The AMC will determine the specific expenditures to be funded from the Base Funds Flow Support Funding and Variable Academic Support Payment pursuant to an established methodology and other requirements. As determined by the AMC, the Incremental Funds Flow Support Funding will be used solely to support the clinical enterprise of the Medical Center, BGSMC, and UPH, including for those programs and services provided by UA, COM-T, or COM-P that support and are accretive to such clinical enterprise, as approved by the AMC.

4.6 Academic Enhancement Fund. UA will establish a foundation, trust, or other restricted fund (the "**Academic Enhancement Fund**") for the sole purpose of providing \$20 million of annual support for academic enhancements, faculty recruitment and program development at the COM-P and COM-T. At Closing, UAHN will contribute to the Academic Enhancement Fund the \$300 million payment it receives from Banner. Banner will guarantee that the Academic Enhancement Fund has sufficient funds to make each annual \$20 million support payment during the 30-year term of the AAA. Any amount remaining in the Academic Enhancement Fund at the end of the AAA's term will be disbursed to UA (or its designee).

4.7 Unwinding and Remedies. If Banner terminates the AAA, if UA terminates the AAA as a result of the material breach of Banner, or if the AAA is not renewed at the expiration of its term,

UA/ABOR will have an option to acquire the Medical Center (including the land), South Campus lease, and Tucson-based component of UPH ("***Southern Arizona Business***") at fair market value. If, however, Banner terminates the AAA as a result of the material breach of UA, this purchase option would not be applicable and Banner would have, in addition to any other available remedies, the right to put the Southern Arizona Business to UA/ABOR. Under no circumstances may the Medical Center or the Tucson-based portion of UPH be transferred by Banner unless the transferee's acquisition of the Medical Center and Tucson-based portion of UPH is subject to assumption of Banner's obligations under the AAA.

\* \* \* \*

The foregoing Principles do not create or constitute any legally binding obligations or agreement by or among Banner, UAHN, and UA, but are intended solely as a proposed guide to the negotiation and preparation of mutually satisfactory definitive agreements ("***Definitive Agreements***"). No legally binding obligations by or among Banner, UAHN, or UA regarding this contemplated strategic affiliation transaction will arise or exist unless and until all of the parties execute and deliver the Definitive Agreements, except that the parties shall be bound by the Confidentiality and Non-Disclosure Agreement dated December 13, 2013, as amended.

**THE UNIVERSITY OF ARIZONA HEALTH NETWORK,  
INC.**

By: \_\_\_\_\_  
Name: \_\_\_\_\_  
Title: \_\_\_\_\_  
Date: \_\_\_\_\_

**THE ARIZONA BOARD OF REGENTS, for and on  
behalf of THE UNIVERSITY OF ARIZONA**

By: \_\_\_\_\_  
Name: \_\_\_\_\_  
Title: \_\_\_\_\_  
Date: \_\_\_\_\_

**BANNER HEALTH**

By: \_\_\_\_\_  
Peter S. Fine, FACHE  
President and Chief Executive Officer  
Date: \_\_\_\_\_