Chapter 14:
Facilitating the Closure of Non-Essential Hospitals

Key Points

- **In an effort to strengthen the acute care hospital system, the Commission believes that non-essential hospitals should be allowed to close if they experience financial distress.**
- **A Certificate of Need (CN) application is necessary for a hospital closure, but, the current application process commences relatively late in the course of a hospital's period of distress. The CN process should be refocused on an orderly closure rather than the decision to close.**
- **The costs associated with closure are substantial – the State should develop a fund to partially support the closure process. Public funds should not be used to bailout bondholders who assumed a certain level of risk as investors. A top priority should be providing some economic protection for hospital employees.**
- **The State should help with the process of identifying alternative uses for closed hospitals.**

The goal of the Commission's work is to strengthen the acute care hospital system in New Jersey, and allowing some non-essential hospitals to close should help strengthen the rest of the hospitals in the State by consolidating patient volume in fewer hospitals and reducing excess capacity. In this chapter, we discuss New Jersey's and other states' policies for facilitating the closure of hospitals, offer recommendations for New Jersey to consider in helping non-essential financially distressed hospitals in closing and evaluate potential alternative uses for closed hospitals' facilities.

I. Policies for Assisting Hospitals in Closing

This section of the chapter reviews the existing policies in New Jersey related to hospital closures and examines approaches used by other states to support hospital closings.

A. Current New Jersey Policies

New Jersey's principal policy governing hospital closure is the Certificate of Need (CON, or CN as it is known in New Jersey) program. Although New Jersey's CN program focuses primarily on the approval of new and expanded hospital services, hospitals seeking to close must submit a CN application for termination/discontinuation of service and these applications are subject to full CN review.[141] The CN process requires an applicant to justify the need for the proposed action, demonstrate that the action will not have an adverse impact on access to healthcare services in the region or statewide, and show that the action will contribute to the orderly development of adequate and effective health care services. In making determinations of need, the Department of Health and Senior Services takes into consideration criteria such as the availability of facilities or services which may serve as alternatives or substitutes, the need for special equipment and services in the area, and the adequacy of financial resources and revenues.

B. Other States' Policies

While states and local governments have assisted in hospital closures in a variety of mostly ad-hoc ways — including transitioning patients to other facilities,

[141] N.J.A.C. 8: 33-3.2

assisting employees in finding new employment, and facilitating property sales and debt repayment, as in New Jersey — the principal procedure other states use is the CN program. In addition to New Jersey, 34 other states and the District of Columbia have certificate of need statutes, and of these, nine others (Alabama, Connecticut, Hawaii, Illinois, Iowa, Kentucky, Maryland, Tennessee, and Vermont) also require hospitals to submit applications to close. In addition to these nine states, two states (Alaska and Arkansas) require a notification of closure, but not a formal CN application.

All CN states that require applications to close, except Hawaii, Illinois and Tennessee, require a hospital to complete the standard CN application, modifying responses in the application to reflect the reduction or closure of services, as opposed to the expansion of services. Illinois and Hawaii have specific requirements and review criteria for CN applications related to the discontinuation of services, as described in Table 14.1 below.

Table 14.1:
Additional CN Requirements/Review Criteria for Illinois and Hawaii

State	Additional Requirement/Review Criteria
Illinois	**Applicants must provide the following:** • **Reason for discontinuation;** • **Other services or facilities in planning area that are available and willing to assume applicant's workload;** • **Closure plan indicating the process used to provide alternative services or facilities for patients prior to or upon discontinuation.** **Applications are reviewed to determine that:** • **Stated reasons for discontinuation are valid;** • **Discontinuation will not adversely affect the services needed by the planning area and will not have an adverse effect on the delivery system by creating demand for services that cannot be met by existing area facilities;** • **Discontinuation is in the public interest and will not cause planning area residents unnecessary hardship by limiting access to needed services for low-income persons, racial and ethnic minorities, women, handicapped persons, the elderly and other underserved groups.**
Hawaii	**In the case of elimination or relocation of a facility or service, applications are judged by:** • **The need that the population currently served has for the service;** • **The extent to which that need will be met adequately by the proposed relocation or by alternate arrangements;** • **The effect that the elimination or relocation of the service has on the ability of the elderly, low-income persons, racial and ethnic minorities, women, persons with disabilities and other underserved groups to obtain needed health care.**

Beyond the CN process, two states – New York and Maryland – have other programs to support hospital closures. The Maryland Hospital Bond Indemnification Program, enacted in 1985 by the State's General Assembly as part of overall legislation to reduce excess hospital capacity, helps pay costs associated with a hospital's closure. A hospital that intends to close can apply to the program for payment of the principal and interest on non-insured public-body issued bonds and some costs for closing. In its application, a hospital must demonstrate how its closure will reduce the State's excess hospital capacity. If the hospital's application is accepted, the Maryland Health Services Cost Review Commission assesses a temporary fee on all other Maryland hospitals to pay off the obligations and closing costs. New Jersey's version of a bond indemnification program is the Hospital Asset Transformation Program. However, the New Jersey Hospital Asset Transformation Program has never been funded.

New York has received an 1115 Research and Demonstration waiver from the United States Department of Health and Human Services to implement reform initiatives that will improve quality of care and result in long-term savings for both New York and the Federal government. Under this 1115 waiver, New York must invest $3 billion over five-year period to receive up to $1.5 billion in federal financial participation (FFP) over five years for designated state-funded health care programs that currently serve low-income and uninsured New Yorkers, and that are not otherwise eligible for federal matching funds. These federal funds are intended to "free up" state funds for New York to invest in its health care reform initiatives. As part of its agreement with the federal government, New York is required to generate $3 billion in gross Medicaid savings ($1.5 billion in federal savings) over the five-year demonstration period. Should the State not achieve these savings by the end of the demonstration, it will be required to refund to the federal government the difference between the federal investment in the Federal-State Health Reform Partnership (F-SHRP) reforms and the federal savings generated.[142]

New York has allocated $550 million of the 1115 waiver funding for assisting hospitals and nursing homes in implementing the recommendations of its Commission on Health Care Facilities in the 21st Century in reshaping the health care market in the state. Hospitals and nursing homes have submitted grant request for financial assistance totaling $2.5 billion and New York made the first grant award of $17 million in late August for closure of St. Vincent's Midtown Hospital in Manhattan.

It is important to reiterate that the federal government's support to New York is contingent upon the State achieving specific savings targets, and to note that New York's 1115 waiver includes major Medicaid and health system changes, such as an expansion of the State's Medicaid managed care program. Thus, the breadth of New York's demonstration project is well beyond the New Jersey's Commission scope and a similar 1115 demonstration project waiver for New Jersey is likely not feasible.

II. Issues Associated with Hospital Closures

Closing any business presents a myriad of challenges and issues to the owners, employees, vendors, and consumers. Because hospitals are complex organizations with many constituencies, the issues associated with closing a hospital are particularly challenging. Table 14.2 identifies some of the major issues and considerations that must be addressed in closing a hospital.

[142] Centers for Medicare and Medicaid Services, "New York Federal-State Health Reform Partnership Section 1115 Demonstration Fact Sheet," (October 1, 2006). Available online: http://www.cms.hhs.gov/MedicaidStWaivProgDemoPGI/downloads/New%20York%20FSHRP%20Fact%20Sheet.pdf

Table 14.2:
Checklists of Issues and Considerations to Address in Closing a Hospital

- ☐ Governance and Authority
- ☐ Accreditation and Regulatory Requirements
- ☐ Communications with Key Constituencies
- ☐ Employees
- ☐ Medical Staff
- ☐ Financial
- ☐ Legal
- ☐ Patients
- ☐ Operations
- ☐ Asset Disposition

We briefly discuss some of the major employee- and financial-related issues below. A more detailed discussion of these and the other issues listed in Table 14.2 are included in Appendix 7.

A. Employees

Because closure of a hospital directly and perhaps most significantly, affects its employees, issues related to a hospital's employees represent one of the more challenging considerations in closing a hospital. This can be especially true in markets in which unions have a substantial presence, such as in New Jersey. Among the many employee-related issues that must be addressed in a hospital closure are severance payments, termination of benefits, settlement of contracts, and notification requirements as specified in union contracts, the federal government's Worker Adjustment and Retraining Notification (WARN) Act which specifies timeframes for notifying employees of layoffs.

B. Financial

The financial issues associated with the closing of a hospital are numerous, highly complex and often unique to the specific hospital. In addition, the costs of closing a hospital are substantial. By way of example, in response to the recently released recommendations on realigning hospital resources by the New York Commission on Health Care Facilities, hospital executives released estimates of the costs to close their facilities, including an estimate of $67.7 million to close St. Joseph Hospital (127 beds) and $250 million to close Erie County Medical Center (406 beds).[143] On a per bed basis, the cost to close these facilities was estimated to be $533,071 and $615,764, respectively.

The key financial issues that must be addressed when closing a hospital are listed in Table 14.3.

[143] Franczyk, Annemarie, "Closing hospitals will cost millions," *Buffalo Business Journal* (November 17, 2006). Available online: buffalo.bizjournals.com/buffalo/stories/2006/11/20/story1.html.

Table 14.3:
Checklist of Key Financial Issues to Address When Closing a Hospital

- ☐ Operational cutoff date and coordination of final closing, cost report, audit, and tax returns
- ☐ Notification of finance constituencies, including banks, service bureaus, system support (payroll, regulatory reporting), collection agencies, trustees of restricted funds, vendors, payers, IRS, insurers, etc.
- ☐ Daily cash management
- ☐ Property inventory and disposition
- ☐ Supply consolidation, control and security
- ☐ Implement revised invoice aging policy
- ☐ Implement authorization of all disbursements by CFO/CEO
- ☐ Determine flow of funds for prepaid expenses, advances, escrowed funds
- ☐ Billing and collection of accounts outstanding
- ☐ Preparation of necessary financial reporting required to support debt actions
- ☐ Terms of all unapplied restricted gifts, donations or grants
- ☐ Previous cost report controversies, appeals or reversals
- ☐ Pending rate appeals or amounts in controversy
- ☐ "Related organization" reimbursement issues
- ☐ Existing or remaining obligations under state regulations and effect of closure on such obligations.
- ☐ Preparation of termination notice to Medicare
- ☐ Determination of Medicare payment rules following termination
- ☐ Preparation of cost report covering period up to date of cessation (due no later than 45 days past, no exceptions)
- ☐ Evaluation of the sale of property for recapture rules under Medicare
- ☐ Insurance contracts, self-insurance trusts, etc. for general liability, auto, fire and casualty, professional liability, Workers' Compensation
- ☐ Determination of insurance needs for future operations or potential liability
- ☐ Notification of all insurance carriers of closing date to terminate or modify policies as appropriate
- ☐ Tail insurance for Directors and Officers (D&O)
- ☐ Tail insurance options for malpractice insurance

Recommendations:

The State should develop and fund a program to help pay some of the costs of closing a hospital.

- The program should not pay for what is often the largest cost associated with closing a hospital, namely the hospital's debt obligations financed through bond issues. Bondholders assume risk when they purchase bonds, and default is clearly one of those risks and it is not the State's responsibility to provide a bailout for investors.

- Hospital employees should be provided appropriate economic protection and should receive severance pay for a similar duration as the hospital's executives.

Other hospitals will likely benefit from reduction in excess capacity resulting from hospital closures, so a potential source of funding for this program is a special temporary assessment on the rest of the hospitals in the closed hospital's market area proportional to their expected financial gain or a more long-run statewide fund supported by hospitals for such purposes.

The State should review the CN hospital closure process. It should be streamlined and refocused to permit a more rational closure and realignment process than results from markets forces and the bankruptcy process.

Currently, New Jersey's CN process handles an application to close a hospital in much the same way that it does for initiation of a new hospital service. New Jersey should retain a review process for closing hospitals, but should streamline it to make it timelier and change its focus to providing assistance in planning and executing orderly closure instead of reviewing the need for closure. Currently staff of the Department of Health and Senior Services (DHSS) expend significant time and effort in trying to ensure orderly closure of a hospital, however, their role is often reactive. DHSS staff should refocus their efforts by proactively assisting hospitals that intend to close with the planning and execution of their closure. This could include, for example, designating an office that would serve as a single point of contact for hospitals planning to close and that would provide a resource clearinghouse and website of case studies, best practices and checklists related to the closure process. The CN closure process should also emphasize community notification and input and ensuring the provision of alternative sources of health services affected by closure. This includes access to reproductive health services that might be limited if surrounding institutions do not provide such services.

III. Alternative Uses for Non-Essential Acute Care Facilities

The process of converting a facility to another use, particularly one that is non-health care related, can be a difficult, time-consuming and expensive. While there are examples of hospitals that have been converted to other health care uses, and fewer examples of conversion to non-health care use, it is also common for closed hospital facilities to sit vacant for years, while buyers and sellers agree on terms, or while the sale is mired in legal issues or community disagreements over the facility's disposition. This section provides information about how closed hospital facilities can be re-used for other purposes and provides recommendations for the State's role in the re-use of closed hospital facilities.

A. Re-use of Closed Hospital Facilities – Health Care Re-use

Among the factors that influence the potential re-use of closed hospital facilities are location and demographics of the community, the age and size of the facility and campus acreage. Regulatory considerations such as zoning laws and legal restrictions and community/public opinion and preferences also influence the potential re-use of closed hospital facilities. Typically, a combination of several or all of these factors determines how a closed hospital's facility is re-used, and experience and research shows that virtually no situation is the same, as demonstrated by the examples outlined below. Nonetheless, some overarching findings emerged from a review of the re-use of closed hospitals around the country over the last several years. These findings include:

- Closed hospital facilities are most commonly used for health care services, but rarely for general acute care hospitals.

- Non-health care uses of closed hospitals are driven largely by the value of the land they occupy.

With respect to the first finding, a study conducted by the University of California at Berkeley provides a good summary of the predominant re-use of hospitals for health care related purposes. The study identified 23 facilities that were closed in California between 1995 and 2000.[144] However, the researchers were able to locate information about the current use of only eight of those facilities and Table 14.4 outlines the re-use for those eight facilities. Five of the six closed hospital facilities that were being re-used for medical purposes were for outpatient services or non-acute care services. The Berkeley research also identified two closed hospitals' facilities that were for sale and, interestingly, one of the conditions of their sale was that they could not be used for medical purposes.

The information in the University of California at Berkeley study parallels the professional experience of consultants engaged by the Commission, research and anecdotal information, examples of which are shown in Table 14.5.

Table 14.4:
Re-uses of Some Closed Hospitals in California

Health Care Purposes
Rural health center operated by a city
Dialysis center operated by a private entity
Outpatient facility for a large managed care plan
Medical offices with a fitness center
Assisted living facility
Acute care hospital under new ownership
Non-Health Care Purpose
Multi-use senior center operated by local government
Administrative office for healthcare system while hospital was offered for sale

[144] "California's Closed Hospitals, 1995 – 2000." April 2001.

Table 14.5:
Re-uses of Closed Hospitals in Other States

State	Closed Hospital	Re-use
Illinois	Mary Thompson Hospital	Residential and outpatient substance abuse treatment center for women and children
Kansas	Memorial Hospital	Prison hospital
Maryland	North Charles Hospital (Maryland)	HMO primary care center
New York	Butterfield Memorial Hospital	Outpatient center
	Brooklyn Hospital Center Caledonian Campus	Full service diagnostic and treatment center
	Columbus Community Healthcare	Diagnostic and treatment center
	Genesee Hospital	Outpatient services for a while, now only physician offices
	Interfaith Medical Center	Methadone maintenance treatment center
	Mohawk Valley General Hospital	Primary care extension clinics
	St. Mary's Hospital	Mental health and substance abuse services
	Samaritan Medical Center Stone St. Division	Diagnostic and treatment and dialysis center
	Staten Island University Hospital Concord Division	Urgent care center
	Union Hospital of the Bronx	Full service diagnostic and treatment center
Ohio	Columbus Community Hospital	Diagnostic and treatment center

The facilities of most of the hospitals in New Jersey that have closed since 2000 are being used for ambulatory care purposes as shown in Table 14.6.

Table 14.6:
Re-uses of Closed Hospitals in New Jersey

Closed Hospital	Re-use
Irvington General Hospital	FQHC
South Jersey Hospital Millville	Ambulatory services
South Jersey Hospital Bridgeton	Emergency and outpatient services
West Hudson Hospital	Ambulatory services
Virtua West Jersey Hospital Camden	Emergency and outpatient services
Saint Francis Hospital (Jersey City)	St. Francis Rehabilitation Center

B. Re-use of Closed Hospital Facilities – Non-Health Care Re-use

The second theme related to re-use of existing hospitals is that in many cases, the land on which a closed hospital sits is more valuable than any health care re-use that can be made of its physical plant. For example, three former hospitals in Chicago were demolished and the land redeveloped for residential condominiums and town homes in the past twenty years, and all of them were in desirable, dense, mixed use areas in the City's near north and Lincoln Park neighborhoods. Additional examples in New Jersey include the University Medical Center at Princeton, which has sold its acute care hospital to a developer who plans to convert it to a mixed-use facility, and the recently announced development of a condominium complex on the site of the closed Hospital Center at Orange.

In addition to the examples cited above, there are several examples in which hospitals built replacement facilities and re-purposed the old facility for non-health care uses. The following case studies outline this alternative.

- **Platte Valley Medical Center (Brighton, Colorado)**

  In July 2007, Platte Valley Medical Center in Brighton, Colorado, a city of more than 20,000 people located 20 miles from Denver, closed its 26-year old facility when its newly constructed hospital with more beds and space opened. The City of Brighton is purchasing the old facility. The City plans to convert the old building to an educational facility and is currently in discussions with local community colleges about their interest in using the facility for classes and programs.[145]

- **University Medical Center at Princeton**

  University Medical Center at Princeton is constructing a new hospital, which will consolidate its current two campuses – one with the acute care hospital and one with a long-term care facility – on a new site. To help finance the new hospital project, the Medical Center has sold the property where its 206-bed acute care hospital is located to a developer who will convert it for a mixed-use facility primarily for residential

[145] Navigant Consulting, Inc. client project.

purposes. The property was attractive to developers not only because of its location in a desirable area, but also because of the size of the hospital. Renovating the hospital's 296,000 existing square feet of space, rather than constructing a new building, allows for a higher density project than would be allowed under zoning regulations for new construction. The hospital's existing parking structure was another attractive feature for developers. Princeton University has purchased the Medical Center's long-term care property.[146]

- **Salt Lake City Veterans Administration Hospital**

  The facility that opened as the Salt Lake City Veterans Administration Hospital in the 1930s was converted to Primary Children's Hospital in the 1960s. The Children's Hospital closed in 1990 when it was relocated to a new facility in a different location. The old building sat mostly vacant for more than 15 years until 2005 when construction of a luxury condominium complex began. The exterior of the old hospital was preserved, but the building's five floors and 80,000 square feet were gutted and 28 condominiums, ranging in price from $500,000 to $2.5 million, were constructed.[147]

Recommendation:

The State should help facilitate re-use of closed hospital facilities for other purposes.

One of the many concerns associated with closure of a hospital is what will happen to its building and site. Historically, the State has encouraged and facilitated the reuse of closed hospital facilities for other health care services. Several former New Jersey hospital facilities, for example, are being used for non-acute health care services, such as primary care clinics. The State should continue to encourage and facilitate re-use of closed hospital facilities for other health care purposes, as appropriate, by working with local officials to identify health care and community services organizations that could use the vacated facilities, expedite resolution of zoning issues, and perhaps provide low cost loans for renovations. When re-use for health care services is not appropriate or feasible, the State could collaborate with local economic development officials to create a package of incentives to attract proposals from private developers. These incentives could include expedited planning review process, zoning exceptions or assistance and property tax breaks.

IV. Conclusion

The Commission recognizes that one of the outcomes of its efforts to ensure that the State has a rational distribution of financially viable acute care hospitals and services sufficient to meet the needs of its residents is that some non-essential, financially-distressed hospitals may close. As such, it is important that the State not only support essential, financially distressed hospitals, but also has in place policies and procedures to ensure that the closure of financially distressed hospitals that are not essential is as orderly as possible.

Most often closed hospital facilities are used as non-inpatient health care centers. Non-health care commercial re-uses are also possible if a closed hospital's land is more valuable than any potential health care reuse of its physical plant. However, the opportunities for non-health care commercial re-use or redevelopment are highly dependent on the demographics of the area and its economic conditions. As a result, given the challenging demographic and economic conditions of several of the areas in New Jersey with the most financially distressed hospitals, it is likely that many of the non-essential hospitals that close will be used to provide non-inpatient health care services because they cannot be re-used or redeveloped in the foreseeable future.

[146] Navigant Consulting, Inc. client project.

[147] Hilton, D., "Old hospital evolving into luxury condos." Deseret Morning News. October, 5, 2005.