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Improved Joint Venture Performance Through Enhanced Governance

In today's health care environment, the need for collaboration has perhaps never been stronger, with hospitals and health systems pursuing partnerships in a number of ways, including alliances, networks, affiliations and, at times, full mergers and acquisitions. In both the for-profit and nonprofit sectors, one form of collaboration — joint ventures — has long been viewed as a sound strategy for achieving multiple objectives.

Joint ventures can take many forms. In health care, these can include whole hospital joint ventures, where a for-profit partner holds a 50 percent or greater interest in the venture and operates the hospital. Here, however, we will focus more narrowly on joint ventures that are devoted to a specific type of business or service and that are a separate legal corporation with multiple owners that each contribute resources and share governance through a board or other structure with fiduciary responsibility. These more traditional health care joint ventures, many of which are now maturing, offer insights into success factors for collaboration and suggest opportunities for improving joint venture performance through improved governance.

A LITTLE CONTEXT

For-profit corporations use joint ventures to achieve several aims, including:

- Enhancing their market position.
- Entering new markets.
- Developing new products and services.
- Gaining access to resources, capabilities and competencies that individual partners may not have internally.
- Increasing efficiencies/achieving economies of scale.
- Sharing risks and rewards.
- Driving new revenue and growth.

Health care organizations striving to achieve their missions while transforming care delivery are also using joint ventures to achieve the above aims and respond to a number of additional challenges. These include consumer requirements for affordable, high-quality care and service close to home; the rise of value-based payment systems; the need to deliver improved health outcomes for individuals, populations and communities; and a host of other imperatives.

In response to these challenges, joint ventures have become more diverse and complex in a number of ways.

Historically, hospitals or health systems typically partnered with physicians or physician groups or a company with expertise in the business of the joint venture, according to Michael Peregrine, a partner in the Chicago-based law firm McDermott Will & Emery. Today, providers are forming joint ventures with a wider range of partners, including pharmaceutical and medical device companies, information systems firms, and innovation and research organizations.

"Fifteen years ago, health care organizations established joint ventures to achieve specific goals often tangential to their core inpatient business, for example, to develop a diagnostic imaging center or provide home health care," says Victoria Poindexter, a principal with the independent, health care-focused investment banking and strategic advisory firm Hammond Hanlon Camp.

Carey Gehl, executive director of growth at UnityPoint Health, a multistate health system based in Iowa, agrees that joint ventures and their flexible governance structure can be complex but says they are necessary when looking to form strategic partnerships.

"UnityPoint Health considers using joint ventures to form partnerships as much as it considers full affiliations," she says. "We identify and pursue collaborations with many organizations, including nontraditional partners, such as historical competitors, to enhance Triple Aim objectives for our patients."

Market and product development are still reasons for health systems to develop joint ventures. They are, however, being used to achieve new purposes as well.

"As the focus on population health management grows, health systems need to understand their own capabilities and where gaps may exist so they can identify partners with new competencies to fill any such gaps and maximize care delivery," Gehl says. "Joint ventures are one avenue to enhance a health system's capabilities."

By Mary K. Totten and Pamela R. Knecht

According to Poindexter, the use of joint ventures is increasing around hospital service lines and ancillaries such as laboratory services, for developing facilities such as behavioral health hospitals or ambulatory surgery centers with external, for-profit experts, and for creating insurance plans. These newer joint ventures are intended to have a substantial strategic and financial impact on the health system.

"Today's health care joint ventures are viewed as central to the organization's future success and are being more carefully structured around issues such as ownership, control and the purpose of the venture because of the need for increased risk-sharing to create greater value and offer services across the continuum," Poindexter says.

A CASE IN POINT

Partnerships have always had both strategic and financial importance for Silver Cross Hospital in New Lenox, Ill.

Silver Cross is an independent, 302-bed community hospital in a market where large health systems — both for-profit and nonprofit — are aligning with smaller systems and hospitals to form expanded networks.

The idea for partnering came out of a board strategic planning session in 2006. At that time, the focus was on expanding service lines. According to Silver Cross CEO Ruth Colby, the strategic question was, "If we can't be the best on our own, how do we bring the best to Will County — our primary service area?"

Silver Cross uses a variety of partnership approaches. The historical core of Silver Cross' partnership strategy, however, includes a number of clinical service line joint ventures with area academic and specialty hospitals and health systems to provide best-in-class care for services that Silver Cross could not deliver in the same way alone. This joint venture core continues to evolve and has expanded to include partnerships among the hospital, physicians and for-profit companies.

"The Silver Cross partnership strategy is embedded in our culture and is critical to successfully pursuing our course as an independent hospital in a consolidating market," Colby says.

Through selecting best-in-class partners, Silver Cross enhances its image and increases its ability to provide excellent care and expanded services locally.

Joint ventures also contribute substantially to Silver Cross' bottom line and help create new income streams to offset declining reimbursement and contraction of inpatient care. Both Fitch Ratings and Moody's Investors Services cited Silver Cross' partnership strategy, including its experience with joint ventures, as key to growing its patient base, developing new areas of expertise and sustaining its credit rating.

As joint ventures mature, they experience growing pains. According to Colby, some of these can be alleviated if partners focus on key success factors, preferably early on or during joint venture formation. Her success factors are in the sidebar on Page 42.

THE NEED FOR MORE EFFECTIVE GOVERNANCE

According to Peregrine, another success factor for maturing joint ventures is effective governance. Attending to governance effectiveness in both newly forming and more mature joint ventures, he says, can pave the way for improved performance and strengthen the foundation for sustaining the partnership.

"Earlier joint ventures were established with a focus on meeting legal and regulatory requirements and structuring and operating the business, with less attention paid to governance," he says. "They also tended to avoid addressing tough issues, such as defining an exit strategy, that evolving organizations are likely to face down the road." While "bare bones" governance structures and practices may have initially served these fledgling enterprises, Peregrine says, they are no longer sufficient to support maturing ventures of growing strategic and financial importance and may create significant challenges for their owners and board members.

A key challenge, he says, is when initial joint venture governance is not detailed or specific enough to handle difficult issues that face more-sophisticated organizations. These might include disputes or questions related to growth — such as taking on new venture partners — how additional capital will be contributed to the venture or how the business will be valued in the event of a sale.

Another major challenge is that many joint ventures have become big, complex organizations that still rely on outmoded governance structures and practices — for example, the expectation that board members will represent the interests of the partner organizations that appointed them instead of the best interests of the venture. These challenges give rise to others, including deadlock and issues related to breaching the fiduciary duty of loyalty.

Other governance challenges for maturing joint ventures, Colby notes, include the failure to assess the compatibility of partner organization cultures, insufficient board member understanding of the joint venture business or agreements, building trust among board members who are not all on the same "home team," and turnover among board members resulting in loss of "corporate memory" about joint venture operations and development.

ADOPTING GOVERNANCE BEST PRACTICES

To address these challenges, joint venture boards and leaders are beginning to put into place the following best governance practices, which many hospital, health system and other corporate boards have adopted over more than a decade:

Competency-based board composition: Although joint venture partners usually appoint the members of the venture board, they have an opportunity to select individuals with specific skills that can enhance joint venture effectiveness, such as strategic planning, risk management, venture capital experience or previous board experience in complex organizations.

Board orientation: Conducting a thorough orientation for new board members and periodic refreshers for the full board can help build a consistent level of knowledge and awareness of the joint venture's purpose and scope, operation and development so that all board members share a similar context for governing.

Evolution of Health Care Joint Ventures: Simple to Complex

FROM	TO
Two partners	Multiple partners
Few types of partners: other hospitals, physicians, some for-profits with venture-related expertise	Diverse partners from diverse industries outside of health care
Single joint venture	Multiple interrelated joint ventures operating at multiple levels
Purpose tangential to care delivery	Purpose directly related to clinical care and services across the care continuum
Getting the deal done	Carefully structuring deal terms, venture operations and venture governance
Less attention to venture time horizon	Anticipated time horizon with defined exit strategies
Avoiding tough decisions on tough issues	Addressing tough issues during joint venture formation

Board orientation also provides an opportunity to remind all directors of their governance roles, responsibilities and fiduciary duties. Orientation is particularly important for new board members, such as physicians, who may not have previous board experience.

Understanding fiduciary duties: It is critical for joint venture board members to understand that their primary duty of loyalty is owed to the joint venture itself.

Clarifying relative authority and decision-making: Venture boards function more effectively when they understand the decisions the board itself can make and those reserved to one or more members, owners or partners. Directors also should be aware of decisions that require a simple majority versus, for example, a supermajority vote. Developing a written authority matrix often provides needed clarity.

Ongoing board education: Joint venture boards should take the opportunity — at meetings and through periodic board retreats — to keep abreast of the changing environment in which the venture operates, to plan for the venture's development and growth, and to further strengthen relationships and build a common culture among joint venture board members and executives.

Terms and term limits: As in most governance contexts, use of terms and term limits for board members is a double-edged sword. On the positive side, they provide for regular and orderly turnover and the chance to bring new perspectives and skills to governance. The downside is loss of "corporate memory," skills and commitment that resided in outgoing directors, and the time and work needed to bring incoming directors up to speed and develop relationships with other board members. Joint venture boards should periodically take time to evaluate the pros and cons of terms and term limits for board members, taking into account the changing governance needs of their maturing organizations.

Board succession planning: Even when board members are appointed to serve in perpetuity, turnover inevitably happens. Boards that take a competency-based approach to governance have the opportunity to identify and prepare incoming appointees so they can hit the ground running when their board service begins. Getting incoming appointees up to speed on the joint venture business, its issues and challenges and having them spend time with partner organization executives serving on the joint venture board are just some ways to build competence, reduce the learning curve and help new appointees more quickly contribute value to governing the venture.

Adding independent directors to the joint venture board: Having directors who do not have a financial or other interest that might bias their decision-making helps to counteract the traditional approach to joint venture board formation in which each venture partner appoints an equal number of board members who are expected to represent the interests of the partner that appointed them. Independent directors can help joint venture boards move beyond representational governance, minimize conflicts and voting deadlock, and bring outside expertise to board deliberations and decisions. Peregrine suggests that appointing a lead independent director, as is often the case on for-profit boards where the CEO is also the board chair, can help guide the board agenda and, if appointed alternately among partners, contribute to a sense of shared purpose and goals.

Adopting standardized processes for joint venture governance: An example would be having each partner use the same process for appointing board members to avoid imbalances, such as those that occur when some board members serve in perpetuity while other seats turn over due to ex officio appointments.

Codifying and documenting board practices: These procedures can be specified in written bylaws, charters, meeting agenda templates and calendars, authority matrices, and other documents that specify how the board conducts its work. Documented practices also can include policies that address governance challenges such as conflicts of interest, confidentiality and dispute resolution.

Developing a deeper focus on compliance issues and mechanisms at the joint venture level: This may include development of a compliance plan for the venture, appointment of a venture compliance officer and creation of a venture board compliance committee. All would replace relying on the compliance apparatus of one of the venture partners.

Expanding use of board committees: Many joint venture boards have few or no committees. As ventures mature, however, their boards may begin to realize the increased focus and efficiency that committees can bring to board work. Audit, executive compensation, quality of care, risk management and strategic planning are examples of governance responsibilities joint venture boards are developing committees to help address.

Formalizing relationships between the venture board and parent/owner organizations: Increased communication and interaction between venture boards and the boards of their partners or owners can increase transparency and awareness of joint venture performance and governance effectiveness. The Silver Cross board, for example, receives a complete overview of partnerships and joint ventures annually, with specific issues discussed as needed at board meetings throughout the year.

Full board and individual member performance evaluation: Conducting regular performance assessments based on predetermined criteria not only holds the board and its members accountable to good governance standards and practices but also identifies opportunities to improve governance that can translate into better partner relationships and venture performance.

LOOKING AHEAD

Hospitals and health systems are increasingly using joint ventures to meet multiple objectives such as delivering high-quality care, expanding services, sharing risk, creating new revenue streams and gaining expertise that is not available internally. As ventures mature, they are likely to encounter obstacles that can be minimized if partners attend to a variety of success factors early on, especially governance effectiveness.

As joint ventures grow in strategic and financial importance to health care organizations, hospital and health system boards should ensure they are well-versed on joint venture performance, challenges and governance. Joint venture boards also can benefit from adopting governance best practices that other corporate boards, including those of hospitals and systems, have long employed to help drive improved performance for the boards and the organizations they govern. **T**

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Key Success Factors for Joint Ventures

Joint venture owners/partners can benefit from addressing the following issues up front:

- Ensure partners share a common culture, vision and values and an ongoing commitment to strengthening the culture.
- Perform thorough due diligence on each partner.
- Adopt a win-win attitude. Define "gives and gets" in advance and identify issues that will be nonnegotiable for each partner.
- Commit to putting in the time. Working with partners often requires double or triple the normal amount of time to ensure success.
- Schedule regular (weekly) communication. Expect face-to-face interaction and involvement of partner organization CEOs and C-suite executives.
- Establish an operating committee that meets at least quarterly to allow partner executives to work together regularly.
- Commit to joint problem solving and shared decision-making.
- Ensure there are good relationships at the top. Partner organization CEOs should be able to pick up the phone and talk with each other when necessary.
- Clearly define roles and reporting relationships for joint venture staff and administrators.
- Develop and agree upon joint venture performance metrics and measurement systems. Metrics should be objective and reported on regularly, and they should allow for early interventions.
- Ask and answer the tough questions. Addressing them early on is likely to minimize conflict and make the joint venture simpler to operate and easier to unwind when the time comes.
- Clearly define exit strategies and obligations associated with breaching the joint venture agreements and be fully informed of consequences before the partnership begins.