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Citizens of Lakewood
Lakewood, Ohio 44107

Re: Frequently asked questions related to Lakewood Hospital

Dear Fellow Citizens of Lakewood:

Since receiving the January 2015 letter of intent among the Lakewood Hospital Association (LHA), the Lakewood Hospital Foundation (LHF) and Cleveland Clinic with respect to a proposed plan for Lakewood Hospital and future healthcare delivery in Lakewood, the City Council and administration of the City of Lakewood have been working diligently, in good faith and with all deliberate speed to understand and assess the proposed plan.

These efforts have included over 30 meetings by City Council with representatives of LHA, LHF, the Cleveland Clinic, LHA's consultant Subsidiary Healthcare, the city's consultant Huron Business Advisory, human service organizations and other community organizations and members of the public, as well as analysis of the existing lease and definitive agreement relating to Lakewood Hospital entered into in 1996.

A number of questions and issues of interpretation regarding the lease and definitive agreement have been raised. In the interest of ensuring the citizens of Lakewood have the relevant information needed to assess the future of Lakewood Hospital, the following are answers to some frequently asked questions.

Why can't the city just enforce the 1996 lease and require the Cleveland Clinic to continue to operate Lakewood Hospital for the remaining term of the lease?

This question goes to the heart of persistent misconceptions about Lakewood Hospital. The city is not a party to any agreement with the Cleveland Clinic. The parties to the

1996 lease are the city and LHA. Under the lease, LHA makes a commitment to run a hospital, not the Cleveland Clinic. The Cleveland Clinic is not a party to the lease and does not have any rights or obligations under the lease.

The agreement to which the Cleveland Clinic is a party is the 1996 definitive agreement. LHA and the Cleveland Clinic are the parties to the 1996 definitive agreement. The city is not a party to the definitive agreement.

There is a widespread perception that LHA's operational, maintenance and other obligations associated with Lakewood Hospital under the lease are passed through to the Cleveland Clinic in the definitive agreement. This is not the case. While the Cleveland Clinic does have some obligations under the definitive agreement, affirmative requirements to operate Lakewood Hospital for the lease term (or any term) or provide specific services at Lakewood Hospital are not among them. The party with those affirmative obligations is LHA, not the Cleveland Clinic, pursuant to the terms of the lease.

Why can't the city just enforce the 1996 lease and require LHA to continue to operate Lakewood Hospital for the remaining term of the lease?

The city does have the option of enforcing its rights under the lease and requiring LHA to continue to operate the hospital in accordance with the requirements of the lease—but this may not be in the best interests of the city or its residents. If the city did elect to enforce LHA's obligation to continue to operate the hospital for the remainder of the lease term, there are several possible outcomes that need to be weighed:

- LHA continues to perform its obligations under the lease, but cash and other asset reserves are depleted and the hospital condition continues to deteriorate. Analysis by Huron, an independent consultant hired by the city, concluded that LHA will “exhaust its investment portfolio before the end of the lease term” and concludes that “the ability of the hospital to continue operating as a going concern is highly speculative”. If LHA is able to fulfill its obligations for the remainder of the lease, at the end of the term, the hospital property (with capital needs in excess of \$91.5 million) and other assets will return to the city without any guarantee of a partner to continue to operate the hospital.
- LHA defaults on its obligations to operate the hospital and the city has to enforce its remedies under the lease. The lease provides that the city has all rights and remedies available at law or in equity to enforce the lease, but a Court may be unwilling to require operation of a hospital by LHA and only those monetary damages awarded by a Court that LHA can afford to pay would be available. This would again mean the hospital property (with capital needs in excess of \$91.5 million) and other assets will return to the city without any guarantee of a partner to continue to operate the hospital.

- LHA is unable to continue to operate the hospital and elects to file for bankruptcy. A bankruptcy court could release LHA from its obligations under the lease and the definitive agreement and the city would once again be left without a partner to operate the hospital and the hospital property (with capital needs in excess of \$91.5 million).

Under each of these scenarios, the city is left with the hospital and its assets, but without a viable partner to operate the hospital (or any other healthcare facility) going forward. As the Huron report concludes, if LHA is forced to continue to operate under the existing lease and is unable to improve performance, address facility issues, retain physicians and find a new healthcare provider partner, “the cost to the community in terms of financial losses and lost services could be significant.” The likelihood of the city finding a new operating partner in time to preserve hospital assets appears to be small. As discussed in both the Subsidium and Huron reports, the hospital was marketed to most local healthcare systems and a select group of national organizations. While a few local systems initially expressed interest, no systems have presented the city or LHA with an offer to run Lakewood Hospital as it is currently operated. The city has only received an offer from the Cleveland Clinic to operate a family health center.

Can’t LHA just continue to operate Lakewood Hospital—even if it is experiencing losses—because the Cleveland Clinic is required to cover LHA operating deficits?

No. Pursuant to the 1996 definitive agreement, the Cleveland Clinic is required to ensure that LHA has a cash-to-debt ratio of 1:1 on a fiscal year basis. This “cash-to-debt ratio” requirement is not the same as a requirement that the Cleveland Clinic cover operating deficits.

The hospital can be operating at a loss, but the Cleveland Clinic is not required to provide any funds until LHA expends a significant amount of its cash or incurs significant debt, such that the amount of debt outstanding is equal to or greater than the cash held by LHA. The report prepared by Huron Business Advisory confirms that the Cleveland Clinic would have no obligation to provide funds to LHA unless LHA’s debt increases significantly.

Because the definitive agreement requires the Cleveland Clinic’s approval before LHA can incur debt in excess of \$500,000 or engage in unbudgeted capital projects in excess of \$500,000, it is unlikely that LHA would be in a position to trigger the cash-to-debt ratio requirement without the Cleveland Clinic’s approval.

Who is responsible for the operation of Lakewood Hospital and maintaining its assets, including capital expenditures?

Under the 1996 lease, LHA (not the city and not the Cleveland Clinic) is required to maintain the hospital in “good repair and operating condition” and to “replace equipment and other personal property necessary to [hospital activities].” As confirmed by the city’s outside legal counsel, Thompson Hine LLP, this requirement likely would not be interpreted by a court as requiring LHA to make material capital investments in the hospital necessary to maximize hospital revenues or to operate the hospital as a state-of-the-art facility.

As noted above, the 1996 definitive agreement does not include a commitment by the Cleveland Clinic to operate a hospital, nor does it place any responsibility on the Cleveland Clinic to maintain the hospital or to make capital repairs or improvements beyond investments during the first five years of the definitive agreement. The definitive agreement does include some commitments by LHA to make capital investments in the hospital; however, these commitments could only be enforced by the Cleveland Clinic, not the city (as noted above, the city is not a party to the definitive agreement). Additionally, LHA reports that it has met the capital investment obligations contained in the definitive agreement.

To summarize: (1) The Cleveland Clinic does not have a lease with the city and is not obligated to run Lakewood Hospital through the end of the city’s lease with LHA. (2) LHA, the city’s tenant and the entity responsible for running the hospital, could cease operating the hospital notwithstanding the lease, leaving the city with no partners to run the hospital. (3) The Cleveland Clinic is not required to cover LHA’s operating losses. And (4) neither LHA nor the Cleveland Clinic is obligated to invest significant capital money into the hospital facility—making major improvements at the hospital the city’s responsibility.

It’s my hope these questions and answers will help inform your views on the city government’s and the citizens’ roles in supporting a robust healthcare delivery model in Lakewood for years and decades to come.

Very truly yours,



Kevin M. Butler
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