

HealthLeaders

10 Steps for Evaluating and Selecting a Strategic Partner

By Mark Dubow, for HealthLeaders News, 8-31-2006

Management teams of healthcare organizations are often approached by members of their medical staff, real estate investment trusts, equipment vendors and others seeking to form partnerships. While the pressure to rapidly close a deal is significant, there are two considerable risks:

1. Partnerships that are inherently inappropriate are formed, fail, and must be unwound.
2. Fearing failure or a loss of control, leaders delay potentially dynamic partnerships and thus do not capitalize on an important opportunity.

These and other shortfalls can be minimized by applying the following 10-step approach to evaluating and selecting a strategic partner.

Step 1: Identify imperatives for partnering.

Before considering a partnership, clarify your organization's long- and short-term objectives. A partnership should not only be a "win-win" for the involved parties, it should help your organization achieve significant strategic advantages, such as:

- Gaining access to a potential pool of patients, clinical or management resources or capital that would not otherwise have been readily attainable
- Strengthening competitive position or even co-opting a potential competitor
- Providing a mechanism to more rapidly achieve a necessary end point than would otherwise be possible

If a potential partnership does not provide a strategic and compelling benefit, do not consume resources in its pursuit.

Step 2: Set criteria for evaluating potential partners.

Prior to identifying or beginning a dialogue with potential partners, take time to set out the criteria for evaluating the opportunity. While the criteria should be tailored to the specific opportunity, it is generally helpful to consider the following issues:

- The opportunity to enhance expertise in areas like patient care operations, service line leadership, utilization management/quality assurance and customer service
- The opportunity to enhance expertise in diagnostic and therapeutic skills, evidence-based medicine protocols and hospitalist services
- The capability to fill medical staff gaps, add clinical equipment, offer desirable acute or ambulatory care facilities or other resources
- The potential impact on the recruitment and retention of physicians, nurses and staff
- The ability to enhance competitive differentiation, market share and financial performance
- The extent of gain in leverage with payors, employers and purchasing companies
- The transaction's effect on access to capital
- The degree of cultural fit between the organizations
- The ability to "close the deal" in a timely manner

The last point is often a hot button issue for healthcare executives. It is valuable to recog-

nize that no typical time frame exists for completing a partnership. Factors that influence the time to close include:

- The extent to which the parties agree on the partnership's objectives and agree on the issues of structure, governance and funds flow
- The complexity of the partnership model and the related "deal points"
- The degree to which the interested parties' legal counsels share a common interpretation of regulatory guidelines specific to partnerships
- The time needed to complete due diligence reviews, including valuation studies

Step 3: Identify potential partners.

Utilize the experience of your board members, management team and outside advisers to identify potential strategic partners. This is an opportunity to think creatively. On occasion, the strongest strategic partnership involves bringing multiple entities to the table.

A multi-hospital system in the Midwest, for example, provided orthopedic, neuroscience and rehabilitation services on a disaggregated basis to residents in a broad geographic area. A strategy was set to integrate and co-locate those services, then position the resulting entity as a regional institute—which required a new legal entity, a series of joint ventures, and new operational procedures to ensure efficient patient flow and clinical information. To accomplish this, members of the medical staff (including specialists), the management teams of each of the hospitals, and a local community-based athletic club worked together to help design the partnership. The institute is now operational, and its management team attributes a portion of its success to the broad base of constituents who assisted with planning and implementation.

Step 4: Conduct a preliminary screen and qualify the potential partners.

A preliminary screen should be conducted to filter out potential partners that do not offer a sufficient benefit to your organiza-

tion. At this level, scrutiny should be given to four issues:

1. To what extent does the potential partnership contribute to meeting your organization's strategic imperatives?
2. What does the potential partner bring to the table, and what are its weaknesses? In addressing this question look for indicators of potential benefits related to:
 - Management and/or clinical care expertise, resources (i.e., facility, equipment, information technology and personnel)
 - Access to capital, and
 - Relevant supporting relationships (i.e., contracts, partnerships and affiliations/alliances).

At the same time, look for signals concerning significant weaknesses associated with:

- Management (competencies/capabilities and stability)
 - Revenue (track record on achieving growth, extent to which revenue streams have an uncertain future--i.e., potential decline in insurance coverage)
 - Reliance on one or a limited number of revenue sources (i.e. a single physician or medical group)
 - Expense (pending capital investment requirements, degree of control over labor and supply cost escalation), and
 - Reputation and image.
3. What is the probability of successfully implementing a partnership with this entity? An organization with a track record of successful partnerships and evolving to address changing internal and market characteristics has a greater likelihood of success. Similarly, when the two entities share common vision, values, cultures and performance metrics, the working relationship is more likely to succeed.
 4. What are the opportunity costs of not pursuing a partnership with this entity?

These questions should be addressed based on publicly-available information and not depend on a request for proposal or entry into a confidentiality agreement. Effective detective work should include investigating the prospective partner's internal and external publications (newsletters, press releases, advertisements, annual reports and articles posted on its Web site) and reviewing local media coverage specific to the organization. Internet searches may

also be used to gather information about the organization's characteristics, major initiatives and profiles on members of the management team. Historical performance (patient care activity, financial and clinical outcomes) may be reported or benchmarked by state and/or federal agencies, insurance companies and public "report card" agencies. Finally, site "drive-bys," "walk-ins" and discussions with other entities who have interacted with the prospective partner in the past may provide insight, as well.

The process should be completed within a few days and result in identification of no more than three or four organizations to be studied in greater depth.

Step 5: Complete a detailed assessment and prioritize the potential partners.

To support a detailed analysis, issue a formal request for proposal and enter into a confidentiality agreement. After review of the submitted proposals, it is generally helpful to interview representatives of the potential partner and to conduct a site visit to observe their resources and operations. Typically, a well planned one- to two-day site visit will help your organization develop a thorough understanding of the prospective partner. Throughout this process, your organization should be assessing the following:

- To what extent does the candidate meet the criteria (Step 2) previously established?
- What factors would influence revenue and cost trends relevant to the partnership? Are they favorable? Controllable?
- What are the key competencies required for the success of the partnership? Do the parties have those competencies?
- What are the major investment requirements and timing necessary to make the partnership successful? Can we afford them?
- Which key constituents must support this partnership for it to be successful? What is their degree of support?

This step should result in a prioritized list of potential partners.

Step 6: Evaluate the deal's structural options.

At this stage, the dialogue will generally be between your organization and the highest priority partner. The interchange will focus on options for structuring the partnership. While the tendency is to consider cash deals

(acquisitions and joint ventures), there are multiple other potential formats such as leases and contractual agreements. Additionally, combinations of these approaches could be used. The advice of legal, financial and other business advisors is generally helpful at this stage.

Step 7: Identify operational implications of the deal.

In this step, attention would be devoted to jointly defining roles and responsibilities. Control, "rights of first refusal" and funds flow processes would each be set forth.

Step 8: Prepare financial analyses.

Once the preliminary structure and funds flow have been clarified, it is appropriate to define the resource requirements (personnel, equipment, facilities, IT). If the partnership includes an acquisition, merger or joint venture, a formal asset valuation analysis by a certified party is usually necessary.

Step 9: Conduct negotiations.

Ultimately, the formation of a strategic partnership hinges on the final negotiations between the parties and the ability to reach compromises. Here, too, an objective third party (business strategy consultant, attorney) can help facilitate the process and find common ground that satisfies the objectives of all parties.

Step 10: Close the deal and implement the communication plan.

In the euphoria of completing a strategic partnership, the parties often charge ahead to their next opportunity or challenge and neglect to give attention to communicating the deal. The communication stage provides the initial opportunity to gain the attention and enhanced loyalty of targeted patients, physicians, payors and other constituents.

Mark Dubow is a vice president of The Camden Group, a national healthcare business advisory firm with offices in Los Angeles and Chicago. He may be contacted at mdubow@thecamdengroup.com.

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