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# Four O.C. hospitals on track

## IHHI is trimming losses at four central O.C. hospitals, but some doctors and employees aren't satisfied.

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SANTA ANA – Larry Anderson felt raked over the coals.

Two years ago, as it was attempting to buy four central Orange County hospitals, Anderson's startup company, **Integrated Healthcare Holdings Inc.**, ran into a wall of angry doctors. When the outcry from local physicians spurred alarm among elected officials and regulators, IHHI's primary investor was forced to withdraw.

But Anderson and his boss, Bruce Mogel, rolled with the punches. They lined up new investors and completed the \$70 million purchase. Their prize? Ownership of four hospitals that, Anderson says now, collectively were losing about \$4 million a month.

Today, Anderson says he's "looking at the other side of the horizon." The company's executives and managers have spent the past two years trying to turn around the financial performance of the hospitals, which include two Western Medical Centers (in Santa Ana and Anaheim), Chapman Medical Center in Orange and Coastal Communities Hospital in Santa Ana.

That goal seems on track. The company has cut its operating loss roughly in half, to about \$7 million, for the nine months ended Dec. 31, compared to the same period a year earlier.

And the four hospitals, which serve some of the poorest areas of Orange County, appear to be performing adequately in providing care under more than a dozen contracts with the county.

"So far, so good," said Orange County Supervisor Bill Campbell, who chaired hearings in 2005 that scrutinized IHHI's purchase plans.

Anderson, Mogel and Dan Brothman, their top operations executive, are looking to expand by acquiring more hospitals. They recently lost in a bid to buy Anaheim Memorial Hospital.

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MODERN MEDICINE: From left, CEO, Bruce Mogel, President, Larry Anderson, and Dan Brothman Senior Vice President, all with Integrated Healthcare Holdings Inc., are responsible for acquiring this GE nuclear camera for Western Medical Center. The half-million dollar machine can do many medical tests including cardiac monitoring, bone scans and detecting certain types of cancers.

CHAS METIVIER, THE ORANGE COUNTY REGISTER

### IHHI's hospitals

The four hospitals owned by Integrated Healthcare Holdings Corp. operate about 12 percent of the hospital beds in Orange County. They include:

- Western Medical Center-Santa Ana: with 282 beds, it operates one of three trauma centers in Orange County;
- Western Medical Center-Anaheim: 188 beds;
- Coastal Communities Hospital, Santa Ana: 178 beds;
- Chapman Medical Center, Orange: 114 beds;

IHHI is based in Santa Ana. Bruce Mogel is the company's chief executive. Its Web site is [www.ihhioc.com](http://www.ihhioc.com).

But challenges remain. Relationships with some of the doctors who practice in IHHI's hospitals are still strained. Suppliers have at times cut off deliveries to some hospitals because IHHI didn't pay its bills quickly enough. And the company is involved in difficult negotiations with some of its labor unions.

Meanwhile, the investor whose reputation caused a public outcry two years ago is about to return by exercising warrants to buy a big chunk of the company's stock.

## **RANCOROUS START**

The story begins in early 2004, when **Tenet Healthcare Corp.**, then facing federal investigations over its Medicare billing practices and other issues, decided to sell 27 of its 86 hospitals, including four in Orange County.

Mogel and Anderson, who had previously run **Alta Healthcare Systems**, a chain of hospitals in Los Angeles County that serves primarily indigent patients, had formed a company and were looking to own and/or manage hospitals. They offered to buy Tenet's Orange County hospitals.

One of their lawyers introduced them to Dr. Kali Chaudhuri, a Riverside surgeon who was interested in being part of the deal. Boosted by \$10.5 million from Chaudhuri, they signed an agreement to purchase the four hospitals from Tenet.

But when Anderson and Mogel sought state licenses to operate the hospitals, Chaudhuri's past became an issue. Many local doctors had been left unpaid when a chain of Southern California clinics that Chaudhuri owned, **KPC Medical Management**, went bankrupt in 2000, owing \$400 million. The clinics' 300,000 patients had been stranded for a time without access to their doctors or medical records. The events had left many doctors deeply distrustful of Chaudhuri.

"I guess we underestimated the emotional aspect of the physicians in the area and how they viewed it," Anderson said.

After doctors protested and regulators objected to Chaudhuri's involvement, he agreed to exit the transaction, his money replaced by a group of Orange County physicians led by Dr. Anil Shah, a Santa Ana cardiologist. To go away, Chaudhuri and his attorney, William Thomas, got warrants to buy as much as 25 percent of IHHI stock, and Chaudhuri got 49 percent of IHHI's land and buildings. Thomas has said he and Chaudhuri plan to exercise the warrants soon and be "minority, passive shareholders."

Chaudhuri's retreat didn't end the rancor. Dr. Michael Fitzgibbons, a former chief of staff at Western Medical Center-Santa Ana, had been part of a group of doctors that had hoped to buy that hospital before Tenet sold it to IHHI. After the sale, he sent emails to other doctors expressing doubts about IHHI's financial viability. The company sued him for defamation and lost.

Fitzgibbons and other doctors complain that IHHI is under-capitalized and that its debt siphons away revenue that otherwise could be used to improve equipment at the hospitals.

To fund its hospital purchases, IHHI borrowed \$50 million at 14 percent interest from **Medical Capital Corp.**, an Anaheim lender. Medical Capital recently offered to cut the rate on IHHI's main loan to 9 percent, reflecting IHHI's improved creditworthiness after two years of payments.

Shah, IHHI's top shareholder and a member of the company's board of directors, said the interest rate is still too high.

"Management should be focusing on getting working capital money at market rates," he said.

## LOSING MILLIONS

Why would anyone want to buy hospitals that were losing \$4 million a month?

Anderson says hospitals are "great businesses," even when they depend, as do IHHI's, largely on government programs to cover care for the poor.

Western Medical Center-Santa Ana is one of the county's three trauma centers, where victims of life-threatening injuries are taken. That has enabled the hospital to develop expertise in areas of care, such as treating burn victims, that help it to be profitable, said Steven Blake, IHHI's chief financial officer.

A few years before Tenet sold it, Western Medical Center-Santa Ana was comfortably profitable. But as Tenet struggled with legal and regulatory uncertainties, the hospital's finances worsened, Anderson said.

"That smells like a great opportunity because we're small, nimble and very experienced at doing exactly what Tenet was not able to do in that environment," Anderson said. "So we knew that even though these things were throwing off huge losses, there was an opportunity to turn them around."

Western Medical Center-Anaheim was another story. That hospital was losing about \$1.8 million a month around the time IHHI bought it. Its problems stem in part from its 91-bed psychiatric ward, which often takes in homeless patients who have gone off their medications, then must find a place for them to go before it can discharge them, said Casey Fatch, the hospital's CEO.

Fatch has been working with the county government to get homeless patients placed more quickly once they are stabilized, reducing the hospital's costs. It's good for the patients, he said, because they are better off in a group home or other out-patient environment.

"What works financially for the hospital and what's better for the patient line up," Fatch said. "That doesn't happen a lot in my business."

Brothman has saved \$30,000 a month at Western Medical Center-Santa Ana by bringing its foodservice operation in house after it was outsourced under Tenet, he said. The company has invested \$4 million in new equipment for that hospital, including a nuclear camera for cardiac monitoring and other tests.

To reduce interest expense, IHHI has pushed suppliers to their limit – and sometimes beyond – by delaying bill payments, said Blake. Suppliers have at times put IHHI's hospitals on "credit hold," refusing to make deliveries until they are paid, he said.

Joe Ruocco, a lab worker at Western Medical Center-Anaheim, said a credit hold in February caused the hospital to run out of a type of kit used to test for pneumonia. In one instance, he had to send a specimen to Santa Ana for testing, forcing an 11-month-old baby to wait an extra two hours in the emergency room, he said.

Ruocco's union, SEIU United Healthcare Workers West, is unhappy with the progress of negotiations with IHHI to renew an expired labor contract, he and other members said.

Dr. John Luster, the chief of staff at Chapman Medical Center, said the hospitals' "dedicated employees and physicians deserve far more credit than IHHI" for keeping things running smoothly.

On that count, IHHI's Mogel doesn't disagree. "The single greatest value we purchased was the employees," he said.