September 19, 1979

TO: MEMBERS, METROPOLITAN HEALTH BOARD

The Citizens League expressed to you, first in 1977 and again this past June, our concern about the need for the Twin Cities community to find some effective way to restrain the growth in health-care costs. This concern focused -- as we said in the title of our major report -- on the need for "More Care About the Cost in Hospitals." We recognized then that capital facilities are but one part of the overall problem of costs. But it is an important part of the problem -- both in itself, and to the extent that an issue about construction represents a test of the willingness of the system to face the issue of expenditure control generally. In 1977 we pointed to one part of the facilities question that we saw as particularly important: The question of the re-distribution of bed capacity around the region, in relation to the effort to reduce the size of the total hospital plant, in which we estimate the community is currently carrying a surplus of from 1500 to 3500 beds. We concluded that any bed-redistribution program must wait until the bed-reduction program has been completed. Last June, we again urged that, in order to advance the public interest in cost restraint, you continue to maintain a tight control on the flow of new investment into the system.

In recent weeks we have been considering, as you have, how this concern for restraining investment applies, in the situation created by the package of applications for certificates-of-need submitted by Fairview Community Hospitals. There seems little question but that, with the three-year, staged program for the reduction of hospital capacity only just designed, and with implementation only barely begun, the bed-reduction program is not in any sense achieved. A proposal for bed-redistribution at this point, from no matter what hospital, should therefore be denied.

We urge this action also because of our concern about the risk that approval of such an application now would result in a surge of investment into the system. This is partly a matter of the cost of the projects now proposed. But partly also (if not very largely) it is a matter of the other proposals that would be stimulated by an approval of what is now before you. This larger, and longer-term, dimension of the present issue should be a major part of your concern. As we pointed out in the 1977 report, there are a number of hospital relocations being contemplated. Fairly rapidly, proposals would likely appear for completing, on the south and east sides of the region, the 'ring' of suburban hospitals that began to emerge during the 1960s on the west and north. This, in turn, would almost certainly stimulate -- in a kind of defensive and competitive response -- proposals from the hospitals near the center of the

region to strengthen their position through the upgrading or modernization of their facilities. The result could be, in total, a substantial increase in hospital investment. This would seriously impair the prospects that remain for removing capacity from the system, since facilities just re-built are unlikely to be closed.

In arriving at this conclusion and recommendation, we have thought carefully about the argument made to you by Fairview, that competitive market forces rather than planning controls should be used to govern the development of the hospital system. In our 1977 report, we looked toward the same objective. We were unable to conclude, however, that at this point in time, even in this community, market forces are effective enough to be relied on. There is, to be sure, a kind of competition among the hospital institutions. There is, a competition among hospitals for doctors, and for patients. But the competitive forces that are critical are those that would work effectively to restrain the expansion of the physical plant and services.....by raising a real prospect that over-expansion could mean financial failure for a hospital. These we find substantially missing. We are aware of the pre-paid health-care delivery plans, and of their potential for -- in time -- restraining the rise in costs and capability. We have encouraged their development, and will continue to do so. But we are realistic about how small a proportion these represent, of the bed-days of care purchased in total, in the community; and therefore about their ability to be a significantly restraining force on capital expansion in the next few years. The dominant factors in hospital capital expansion today are: the growing practice by hospital of borrowing the money for expansion; the effect of tax-exempt industrial development bonds in enlarging the pool of capital available for lending; and the willingness of the third-party insurers to reimburse the hospitals for their payments for principal and interest. Near-term, then, there is no realistic substitute for the certificate-of-need.

Longer-term, we are not so sure the certificate-of-need will be the most desirable -- or even a very effective -- control on expansion. The kind of quasi-administrative, quasi-political proceeding you are now going through has been a most difficult one . . . for you, on the Health Board; for the applicant; and for the other hospitals in the community. No one involved with the issues in the health care system can happily contemplate so painful a process from here on, with application after application, indefinitely into the future. You will need to consider, too, whether the process of planning and voting will be able to handle the issues that will arise as you work through the remaining policy questions . . . of a suburban hospital 'ring,' about the future of the 'rural ring' and about the number and organization of hospital 'centers' in the core of the region. Under the pressures to be fair, and consistent, your process could conceivably work well to approve everything. It could conceivably deny everything. The question is whether it will be able to make the discriminations that are needed -- approving some applications, and saying 'no' to others.

A system of control built around market forces might be both more desirable and more effective, if it could be developed. An effort should now be made to do precisely this. We believe there is a considerable potential for success. In part, it would involve the expansion of the programs now existing, which buy hospital care on a price-conscious basis. In part, too, it would involve introducing some new forces directly into the market for hospital capital. The Citizens League is not prepared to bring you recommendations, now. We do, however, intend to pursue this line of discussion vigorously over the next few months.