

September 25, 2018



## Review of Process



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## TODAY

- *Review* activities to date
  - Collaborative effort
  - Controlled competitive process
  - Business combination transaction
  
- *Continue* good decision-making
  - Gradual, rigorous
  - Open, public
  - Best healthcare for residents of Indian River County
  
- *Discuss* next steps
  - Board meetings to approve documents - - October 3
    - IRCHD
    - IRMC
  - Governmental approvals

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# **1. COLLABORATIVE EFFORT**

## COLLABORATION

- Formation of Collaborative Committee - - Winter 2017
- James Orlikoff visit
  - National perspective on issues facing hospitals with local government
- Review with Stroudwater
  - Determination of shared objectives
  - Review of business circumstance and strategic options
- Conclusions
  - Maintain and improve access to clinical excellence
  - Need for resources
  - Sub-optimal position relative to emerging healthcare landscape

## **2. CONTROLLED COMPETITIVE PROCESS**

## PROCESS

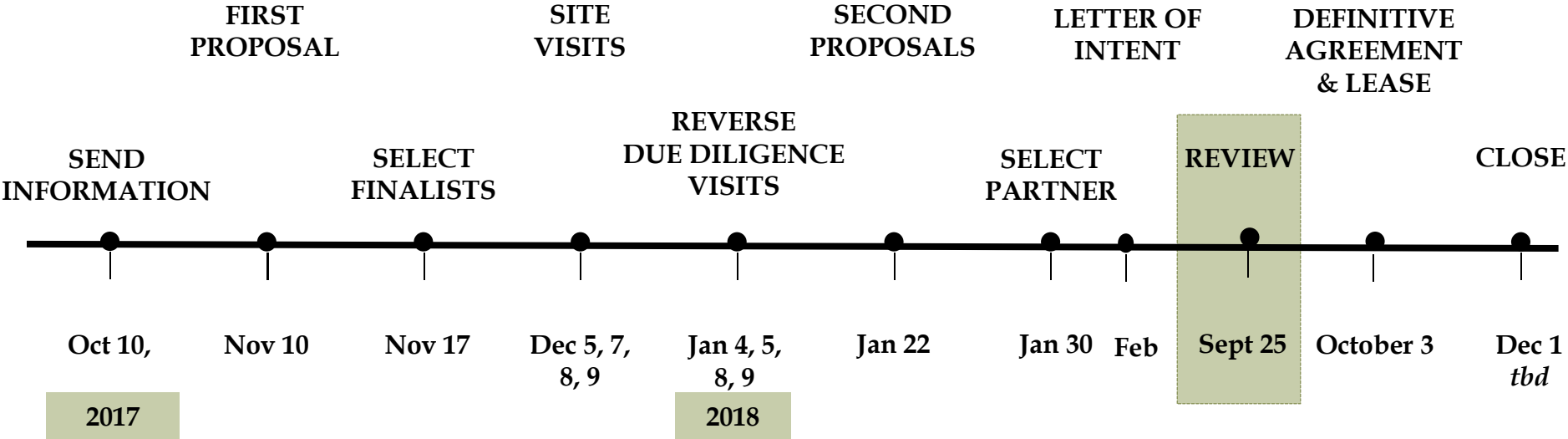
- Objectives of the process
  - Gradual decision-making
  - Input from market
  - Openness
  - Fairness to all potential partners
  
- Comity between IRMC and IRCHD
  
- Selection of partner by IRMC and IRCHD

## COLLABORATIVE OBJECTIVES

- **QUALITY**
  - Clinical
  - Patient-first culture
  - Care for all
- **FINANCIAL WHEREWITHAL**
- **THRIVE UNDER FUTURE HEALTHCARE ENVIRONMENT**
  - Physicians - - integration, staff development
  - Post-merger integration
  - Population health, risk-based contracts
  - Investments in technology, facilities, programs, people
  - Governance, community
  - Technology



# TIMELINE & EVENTS OF CONTROLLED, COMPETITIVE PROCESS



## TRANSACTION PHASE

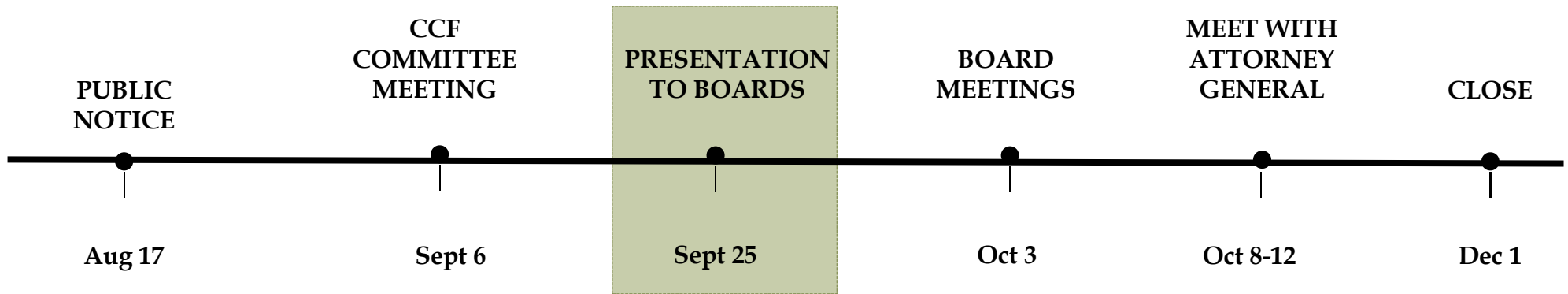
- Due diligence – each party of the other
- Legal details of Membership Substitution Agreement
- Legal details of Amendment to Lease and other District agreements

### **3. COMMENTS**

- Rigorous
  - Strong team effort by boards, managements, advisors
  - Stout report for District
  
- Thoughtful
  
- Public, open
  
- Superior outcome
  - Quality of partner
  - Community benefit
  - Transaction terms
  
- Distinguishing features
  - Cooperation between IRMC & IRCHD
  - Community support

## **4. NEXT STEPS**

**TIMELINE** *through close*



NEXT STEPS

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# **IRMC, DISTRICT & CCF TRANSACTION: SUMMARY OF MEMBER SUBSTITUTION AGREEMENT**

**SEPTEMBER 25, 2018**

D. Louis Glaser  
Partner  
Katten Muchin Rosenman

# Agenda

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- Process to date
- Member Substitution Agreement
  - Transaction structure
  - Governance
  - Financial and other commitments
  - Commitment Integrity Committee
  - Operational covenants
  - Representations and warranties
  - Other agreements
- Approvals and next steps



# Process to Date

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- Collaboration Committee:
  - Stroudwater: Strategic Options Assessment, March 2017
  - Juniper Advisory: joint presentation, March 2017
- IRMC engaged Juniper Advisory, August 2017
- Development of evaluation criteria for potential suitors, September 2017
- Instruction Letter to potential suitors, October 2017
- Indications of Interest (“IOIs”), November 2017

# Process to Date

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- IOIs evaluated & suitors selected, November 2017
- Suitor visits to Vero Beach, December 2017
- Visits to suitor locations, January 2018
- Second submissions/proposals from suitors, January 2018
- Selection of Cleveland Clinic Foundation, January 2018
- Non-Binding Letter of Intent, February 2018
- Due diligence and reverse due diligence, Spring & Summer 2018
- Negotiation of “Definitive Agreements”, May to present 2018

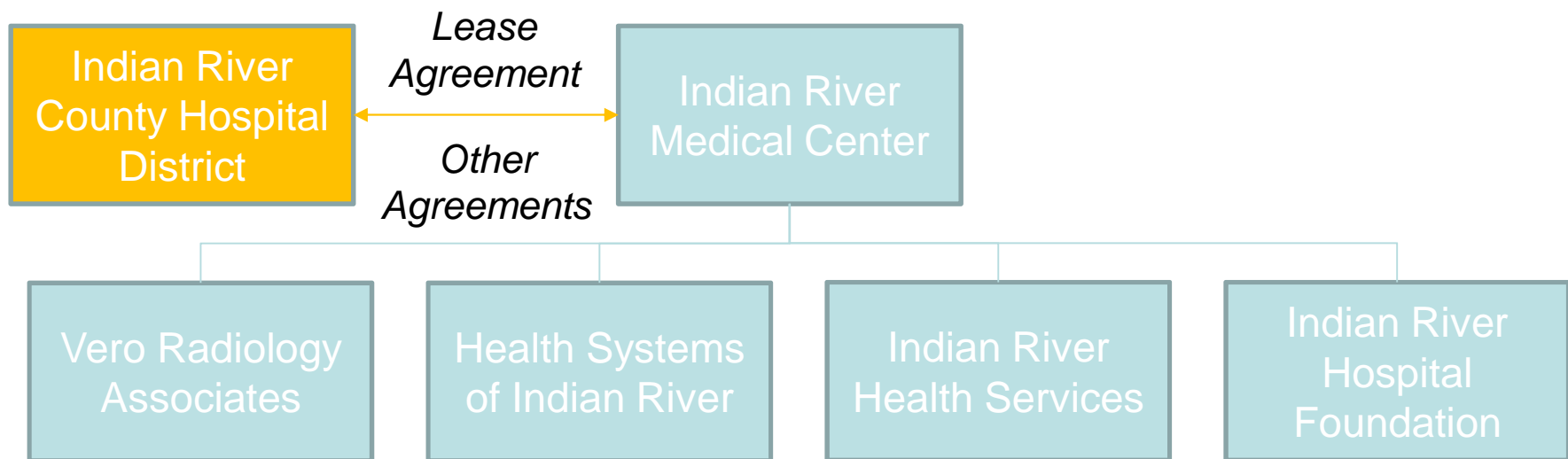
# Member Substitution Agreement

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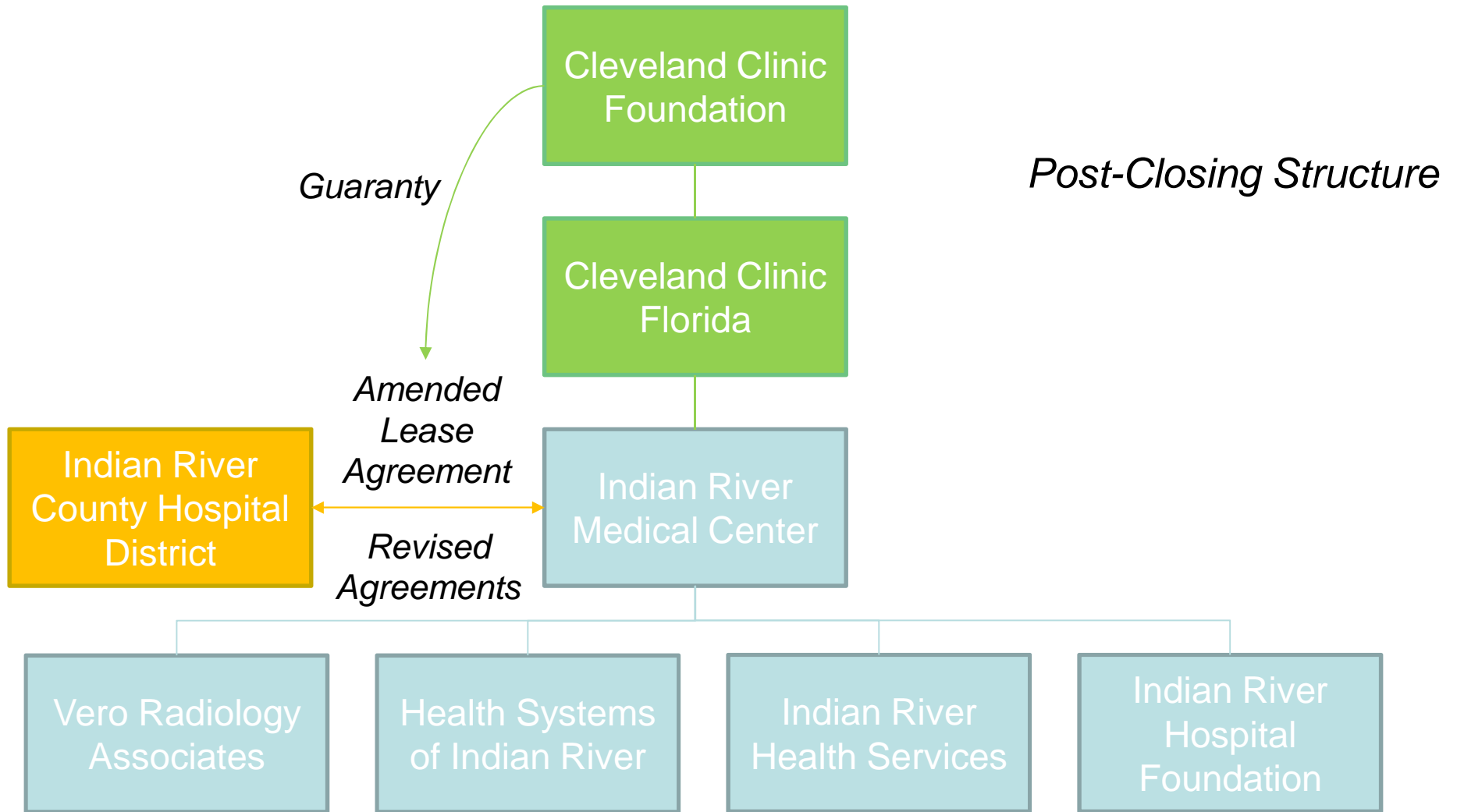
- “Road Map” for transaction:
  - Transaction structure
  - Terms and obligations
  - Other agreements to be delivered
- Parties:
  - Indian River Medical Center (“IRMC”) and its Affiliates
  - Indian River County Hospital District (“District”)
  - Cleveland Clinic Foundation (“CCF”)
  - Cleveland Clinic Florida

# Transaction Structure

*Current Structure*



# Transaction Structure



# Governance

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- Current IRMC Board of Directors (17 members):
  - 12 Independent Directors, with 3 selected by District
  - 1 elected IRMC Medical Staff representative
  - 4 *ex officio*:
    - President (Non-Voting)
    - IRMC Foundation Chair
    - Chief of Medical Staff
    - Vice Chief of Medical Staff

# Governance

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- Vacancies in elected Directors filled by Board from list presented by Nominating Committee
- Elected Directors may be removed as follows:
  - Any Director – by  $\frac{3}{4}$  vote of Independent Directors
  - Independent Director – by majority vote of District Trustees if Director acts inconsistent with public purpose

# Governance

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- Post-Closing IRMC Board of Directors (17 members):
  - 3 residents of Indian River County who are current IRMC Board members
  - IRMC Foundation Chair *ex officio*
  - District Chair *ex officio* (while Amended Lease in effect)
  - Resident of Indian River County (non-Trustee) selected by CCF from slate approved by District (“Community Rep”)
  - 2 physicians on IRMC Medical Staff
  - 9 individuals selected by CCF



# Governance

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- Vacancies in elected Directors:
  - For 10-year period following closing, Community Rep selected by CCF from slate approved by District
  - All others filled by CCF
- Elected Directors may be removed by CCF

# Governance

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- Reserved powers of Cleveland Clinic over IRMC:
  - Amend Governing Documents (except Fundamental Commitments, District Chair *ex officio*, and manner of election of Community Rep during 10-year period)
  - Approve/ratify budgets and strategic plans
  - Approve mergers, consolidations and dissolution
  - Approve sales or encumbrances of assets in excess of dollar amount
  - Appoint and remove corporate officers
  - Approve creation of subsidiaries and affiliates

# Governance

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- IRMC Affiliates:
  - Boards continue to be elected in same manner
  - Vacancies continue to be filled in same manner
  - IRMC holds reserved powers over affiliates consistent with CCF's over IRMC (IRMC Foundation exceptions below)
- IRMC Board Chair to serve as *ex officio* member of Cleveland Clinic Florida Board

# Financial and Other Commitments

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- Certain commitments and obligations of Cleveland Clinic (“Fundamental Commitments”)
- Set forth in the Member Substitution Agreement
- Made over the 10-year period following the closing (“Commitment Period”)

# Financial and Other Commitments

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- CCF capital commitment to IRMC during Commitment Period of at least \$250 million:
  - Routine maintenance
  - Non-routine development, improvement and expansion of facilities
  - Information technology
  - Outpatient surgery center development
  - Strategic capital investments (e.g., acquisitions)
- Pursuant to capital plan approved by IRMC Board

# Financial and Other Commitments

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- Provide or arrange for the provision of funds to cure IRMC default on existing indebtedness during Commitment Period
- Prohibition on sale or change in control of IRMC during Commitment Period

# Financial and Other Commitments

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- Will cause IRMC to maintain and operate following services during Commitment Period:
  - Maternity care (labor, delivery and OB), inpatient well baby care/pediatrics and gynecology
  - Behavioral/mental health
  - Inpatient and outpatient cardiovascular services of Welsh Heart Center
  - Inpatient and outpatient cancer services of Scully-Welsh Cancer Center
  - Gastroenterology services of Scully Endoscopy Center

# Financial and Other Commitments

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- IRMC could cease to provide any of the foregoing if:
  - Another health system provides at a comparable level within greater of Indian River County or 25 miles of IRMC
  - Meet with the District
  - After meeting, provide 90 days notice to Commitment Integrity Committee, District and the public



# Financial and Other Commitments

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- IRMC Foundation:
  - Retain current primary mission and purpose of raising funds for and supporting IRMC
  - Governing Documents cannot be amended (including changing mission and purpose and board membership) without both IRMC and IRMC Foundation Board approval
- Provisions are intended to ensure that IRMC Foundation funds are retained and used locally

# Commitment Integrity Committee

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- Purpose is to monitor and enforce CCF's Fundamental Commitments during the Commitment Period
- Comprised of 4 members:
  - 2 selected by current IRMC Board
  - 2 selected by District
  - No more than 1 of the 4 members may be a District Trustee
- Members serve independently and objectively, and not as agents
- Decision to bring an enforcement action requires 3 of 4 votes

# Commitment Integrity Committee

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- Any ongoing expenses funded by IRMC
- Expenses of an action to enforce CCF commitments funded by CCF
- If Committee brings an action and:
  - Prevails, expenses are paid by CCF do not reduce its capital obligation to IRMC
  - Does not prevail, expenses paid by CCF reduce its capital obligation to IRMC included in the Fundamental Commitments

# Operational Covenants

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- IRMC Medical Staff will continue as an independent medical staff organization with its own bylaws, rules and regulations
- IRMC will move to CCF “master brand” and naming
- CCF anticipates retaining IRMC employees at closing at current wages and benefits – eventually will move to CCF benefits
- Existing IRMC severance agreements and policies will be honored
- IRMC collective bargaining agreement will be honored

# Representations and Warranties

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- IRMC:
  - Fundamental reps (*i.e.*, ability to consummate transaction)
  - Standard reps regarding business, financials, assets, operations, agreements, permits and compliance
- District:
  - Fundamental reps
- Cleveland Clinic:
  - Fundamental reps
  - Certain other common reps

# Representations and Warranties

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- IRMC disclosures updated between signing and closing
- Termination rights only if:
  - Breach of a fundamental rep
  - Breach of other rep and results in “Material Adverse Event”
- No post-closing indemnity obligation for IRMC

# Other Agreements

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- Amended and Restated Lease
- Guaranty Agreement
- Declarations of Easements
- Amended and Restated Indigent Care Agreement
- Amended and Restated Partners Agreement

# Approvals and Next Steps

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- Finalize agreement
- Obtain parties' approvals
- Execute agreement
- Obtain required third party and governmental consents and approvals



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**A Briefing for the Indian River  
County Hospital District Trustees  
*and the*  
Indian River Medical Center  
Board of Directors**

**The Proposed Transaction  
with Cleveland Clinic**

**September 25, 2018**

**William A. Boyles**

# THE PROCESS

## *a Brief Overview*

- Reverse due diligence –58 documents [3,936 pages].
- Informational briefings with the Trustees.
- Frequent phone calls.

## THE PRIMARY DOCUMENTS

- Amended and Restated Lease Agreement between the District and IRMC
- Guaranty Agreement
- Declaration of Easements, Covenants, Conditions and Restrictions
- Third Amended and Restated Agreement for Indigent Care Services
- Amended and Restated Agreement for Operation and Funding of the Partners in Women's Health

# The Amended and Restated Lease Agreement

# AMENDED AND RESTATED LEASE

## *Main Points*

- Term
- Rent
- Service Line Commitment
- Indigent Care
- Reporting Requirements
- Insurance
- Assignment and Subleases
- Default
- The End of the Lease

# AMENDED AND RESTATED LEASE

## *Term*

- Initial Term = 30 years
- Renewal Term
  - 3 terms of 15 years each
  - at IRMC/CCF's discretion

# AMENDED AND RESTATED LEASE

## *Rent*

Initial Term = Prepaid Rent

- Indigent Care – after 36 months IRMC/CCF assume 100% of Indigent Care Responsibility – approximately \$7 Million per year.
- Continued payment of maintenance, repairs and commitment to improvements.



# AMENDED AND RESTATED LEASE

## *Rent*

Renewal Term(s) Rent Per Year = Land Value  
x Market Capitalization Rate.

*Land value and market capitalization rate  
determined by an appraiser.*

# AMENDED AND RESTATED LEASE

## *Service Line Commitment*

First 10 years:

- Maternity care, well-baby care, pediatrics and gynecology
- Behavioral and mental health services
- Inpatient and outpatient cardiovascular services by the Welsh Heart Center
- Inpatient and outpatient cancer care services by the Scully Welsh Cancer Center

# AMENDED AND RESTATED LEASE

## *Service Line Commitment*

- Gastroenterology services by the Scully Endoscopy Center

### Exceptions:

- Another hospital provides the service at a comparable level in the county or within a 25-mile radius of the Hospital.
- IRMC/CCF provides notice and meets with the District.

# AMENDED AND RESTATED LEASE

## *Service Line Commitment*

### Enforcement:

- Through the Commitment Integrity Committee under the Member Substitution Agreement.

# AMENDED AND RESTATED LEASE

## *Indigent Care*

Provided by IRMC/CCF:

- Throughout the Lease Term.
- In accordance with CCF's Indigent Care policy.
- In general as currently drafted:
  - Annual family income up to 250% of the Federal Poverty Guidelines = free care
  - Annual family income 251% to 400% of the Federal Poverty Guidelines = discounted care
  - Emergency care and "medically necessary care" are covered under the policy

# AMENDED AND RESTATED LEASE

## *Reporting Requirements*

Report provided twice a year to the District (once in writing, once verbal)

- Healthcare services offered or contemplated
- Capital spending
- Annual goals, benchmarks and achievement rates for quality
- Indigent care provided
- Annual AHCA report

# AMENDED AND RESTATED LEASE

## *Insurance*

- Property, Liability, Automobile
- Worker's Compensation
- Business Interruption
- Malpractice
- Self-Insurance permitted [if Guarantor has a financial net worth over One Hundred Million Dollars]

# AMENDED AND RESTATED LEASE

## *Assignment and Subleases*

- During first ten years of the Initial Term – District must consent to any assignment (unless a transfer to an affiliate of CCF).
- Thereafter, except as otherwise provided by law and the other provisions in the lease, no consent required for an assignment.
- No consent required to a sublease of a portion of the premises so long as its term will expire or can be terminated prior to the expiration of the lease term.



# AMENDED AND RESTATED LEASE

## *Default*

### **Major Event of Default = lease termination an option:**

- Failure to pay renewal term rent.
- Failure to operate an acute care hospital on the premises for one month (subject to force majeure delays, casualty interruptions, etc.) during first 10 years.
- Failure to provide acute care services to the residents of the County through facilities located in the County for one month (subject to force majeure delays, casualty interruptions, etc.) during years 11 through 30.
- Lessee or Guarantor files petition in bankruptcy or insolvency.

# AMENDED AND RESTATED LEASE

## *Default*

**Other Events of Default = money damages,  
specific performance:**

- Failure to comply with lease terms and conditions.

# AMENDED AND RESTATED LEASE

## *Upon Expiration of the Lease Term*

- Working facility is returned to the District.
- Ability to purchase:
  - Specialized, cutting-edge equipment for the depreciated book value, and
  - Undepreciated personal property added during the preceding five years for the depreciated book value.

# Guaranty Agreement

# GUARANTY

## *Who and What*

- Guarantor = The Cleveland Clinic Foundation, Ohio, not-for-profit.
- Guarantees Lessee's performance of its covenants and payment of rent under the lease.

# GUARANTY

## *Substitute Guarantor*

In the event of an assignment or change of control a substitute Guarantor may be tendered by Cleveland Clinic Foundation:

- Must have 1.5 billion dollars Total Operating Revenue (excluding investment income, extraordinary items and other non-operating gains) for the immediately trailing twelve month period.
- Must be headquartered in the United States.
- Must have EBITDA = 4% average annual return on Total Operating Revenue (excluding investment income, extraordinary items and other non-operating gains) for the preceding three years.
- Must execute a guaranty in substantially the same form as the original guaranty.

# Declaration of Easements, Covenants, Conditions and Restrictions

## DECLARATION

- Gives CCF a degree of control over the future development of the entire hospital campus and adjacent parcels owned by the District.
- Restrictions do not apply to current tenants.
- Memorializes current easements and relationships among the three parcels.



# Third Amended and Restated Agreement for Indigent Care Services

## INDIGENT CARE SERVICES

### *funding from the District*

- Funding is expected to be appropriated annually at \$500,000 a month, payments beginning after closing, not to exceed \$15 Million over the life of the agreement.
- Remainder of funding from Lessee for entire lease term.
- Assuming funding at \$7 Million a year, the indigent care portion of the transaction results in reduced costs to the District of **\$195 Million** over 30 years.

# Agreement for Operation and Funding of the Partners in Women's Health

# PARTNERS IN WOMEN'S HEALTH

## *The Partner's Program*

### *Services provided by IRMC/CCF:*

- Preconception care and counseling
  - Prenatal care
  - Obstetrical care
  - Post-partum care and counseling
  - Qualification of uninsured mothers for appropriate financial assistance programs.
  - Professional services of a pediatric hospitalist
  - Gynecology services for eligible patients
  - Professional services of perinatologist
- *Proposed funding by the District for 2018-2019 fiscal year = \$1.7 Million.*
- *Current agreement provides for \$100,000 additional funding for meeting quality metrics. This has now been removed.*

# Questions?