

# Doctors' Hospital hunts capital

McLaren CEO: \$40M in improvements needed

By [Jay Greene](#) - February 13, 2011

The 42 physician owners of **Doctors' Hospital of Michigan** face tough challenges as they seek to raise millions of dollars in capital to take the next step in turning around their financially troubled for-profit hospital in Pontiac.

At the top of their list is finding \$30 million to \$40 million to invest in new equipment, building maintenance, renovations and other improvements at the 45-year-old hospital, said Phil Incarnati, CEO of **McLaren Healthcare Corp.**

Last week, McLaren sold its \$5 million investment in Doctor's Hospital for \$3 million, primarily because of the capital and equipment needs the hospital requires immediately, Incarnati said.

"We have no ties to them now, but the amount of working capital is still an issue. The facility is old and hasn't been maintained enough," he said. "There are a lot of needs. It is a substantial investment."

Incarnati said Doctors' Hospital requires \$10 million to \$20 million in basic building improvements and \$20 million in a modern information technology system.

And if the Doctors' Hospital owners can't raise the money to purchase an electronic health records system and demonstrate "meaningful use" by 2015, Medicare reimbursements will be cut 1 percent in 2015, 2 percent in 2016 and 3 percent in 2017.

"Patients deserve the best quality available, but they won't easily come to a hospital that is bootstrapped, financially troubled, with old systems and no ability to buy modern equipment," said Jim McTevia, managing partner of Bingham Farms-based consulting firm **McTevia & Associates**.

Officials for Doctors' Hospital did not respond to interview requests last Tuesday and Wednesday.

While a bank loan for a cash-strapped hospital might be difficult, Greg Moore, health care chair at **Clark Hill** in Birmingham, said venture capital investors could be interested in Doctors' because of health care reform.

"There is more interest among health care venture capital funds these days for investing in ventures like Doctors' Hospital if they have the right business model," Moore said.

"Venture capital firms see the legislation as adding paying customers," Moore said.

But for Doctors' Hospital to attract investors or to sell long-term bonds, the hospital has to show some profitability, McTevia said.

"They have the deck stacked against them because the secret for any health care organization is revenue, and they serve a census population who are not wealthy," McTevia said.

McTevia said venture capitalists look for a strong return on investment.

"It would be a long time for this hospital to throw off any kind of return for investors," he said.

In 2010, Doctors' Hospital lost about \$1 million, but that was lower than the \$3.3 million loss posted in 2009, according to the Louisville-based **American Hospital Directory**.

In 2008, the doctors and McLaren purchased the shuttered hospital formerly known as **North Oakland Medical Center and Pontiac General Hospital**, which lost \$31.2 million the year it closed. The hospital had lost \$24 million from 2005 to 2007.

"There were no negative feelings, despite that we lost the money," Incarnati said. "The disagreement was the long-term viability without any cash infusion. We were not willing to put in any more money than the \$5.5 million."

From the beginning, the doctors only raised "half of what they committed to do," Incarnati said.

Flint-based McLaren initially invested \$2 million, or a 35 percent stake, in the hospital when the physicians purchased it in 2008.

The system later loaned \$3 million to the hospital in a secured note tied to the assets of the hospital, Incarnati said. Later, McLaren extended a \$500,000 line of credit for a \$5.5 million total investment.

"We put Clarence Sevillian, one of our rising stars, in there (as CEO)," Incarnati said. "He did a good job, reduced the losses."

But Incarnati said physician owners did not admit as many patients to the hospital as expected.

Incarnati said another reason McLaren backed out of its equity ownership is that Doctors' owes an undetermined amount to Medicare.

"Doctors' made payments to them over the past two years, but there is an outstanding balance still owed," he said.

Moore said Doctors' Hospital could survive even in a market as competitive and distressed as Pontiac, where unemployment is 23.9 percent compared with 10.6 percent statewide, according to the **Michigan Department of Energy, Labor and Economic Growth**.

"It ought not to be the same strategy as **St. Joseph Mercy Oakland and POH Medical Center**," Moore said. "They need to fill a niche that the other two hospitals are not filling."

Jack Weiner, St. Joseph's CEO, has said there is no need for three hospitals in Pontiac because patient volumes have been flat the past several years.

"We are doing a little better this year, but it is a tough market," he said.

St. Joseph Mercy, which has begun or completed \$186 million in capital projects the past three years, is backed by Novi-based **Trinity Health**, which owns 46 hospitals, including 12 in Michigan.

"The doctors deserve a lot of credit. We created efficiencies for them and the losses were reduced. We just didn't see it going anyway," Incarnati said.