

Affiliations & Mergers

Acquisitions

Dispositions

Closures

SPONSORSHIP TRANSITIONS:
CONSIDERATIONS FOR NOT-FOR-PROFIT SENIOR LIVING PROVIDERS

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Ziegler

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ABOUT | THE AUTHOR

Lisa McCracken joined the senior living team at Ziegler in July 2013. As a senior vice president of senior living research and development, her primary focus is concentrated on conducting market research and trend analyses for educative purposes in the form of presentation modules, newsletters, and research publications. In addition to providing support to several senior living bankers, she also facilitates the *Ziegler CFO HotlineSM*, an electronic interchange of information among CFOs of senior living providers, and coordinates regional educational workshops for senior living professionals, part of the *Ziegler CFO Workshop SeriesSM*.

Prior to joining Ziegler, Lisa served as president of a national senior living research and consulting firm. For more than 13 years, she also served as managing partner and vice president of research. Lisa's expertise is in conducting research in the not-for-profit senior living sector, writing white papers and articles on various industry topics, and presenting research findings to providers and experts in the field. She is a seasoned lecturer, facilitator and researcher.

Lisa has served on various state, regional and national workgroups such as the LeadingAge Engaging Consumers Cabinet, the Quality First Task Force and the LeadingAge (then AAHSA) Education & Planning Committee. Outside of senior living she has extensive experience in the healthcare and public health sectors with community health improvement, community benefit and planning activities.

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WHY ALL THE BUZZ ABOUT | SPONSORSHIP TRANSITIONS?

Over the past 10-20 years, the entire healthcare sector has undergone significant consolidation. The number of smaller, community hospitals has dropped considerably as our changing healthcare system has dramatically shifted the structure of the marketplace. In turn, a number of other subsectors within the healthcare universe have transformed as organizations joined together to become stronger in their ability to thrive during turbulent times. This is true for home health, physician practices, healthcare technology and yes, senior living.

Before moving forward into a deeper conversation around “Sponsorship Transitions,” it is important to talk about definitions. Sponsorship Transition is an umbrella term that has been coined to describe several types of not-for-profit transactions:

- Affiliations & Mergers: Two organizations who come together under common control
- Acquisitions: An asset purchase by a new owner or sponsor
- Dispositions: Single-site campus or non-core asset released into the marketplace
- Closures: An entity ceases operations

The transfer of sponsorship reflects the support of not-for-profit senior living organizations and the mechanisms by which these transactions take place. It is generally embraced within the not-for-profit sector as opposed to the use of “M&A” activity within the for-profit, private sector.

A Response to Changing Times

The increased activity in recent years is a function of a number of increasing pressures on senior living providers.

In many instances, organizations who can build greater scale and sophistication through partnering are in a better position to be successful long-term amid these changing times. The sidebar graphic to the right outlines the common drivers for sponsorship transitions among today’s not-for-profit senior living providers.

It is important to specifically comment on the role that succession planning and C-Suite retirements have had on the industry consolidation. Everyone who is even remotely connected to the senior living field is aware that the Baby Boomer cohort is dramatically impacting the national and global aging population. Roughly 10,000 Baby Boomers turn 65 every day. Many of these Baby Boomers are today’s C-Suite executives. Ziegler conducted research of all the sponsorship transitions between 2010 and early 2018 and identified that nearly 50% of the situations involved leadership turnover as one of the drivers. The retirement of a long-time CEO with no clear internal successor will often stimulate conversations at the board level to explore affiliation.

SPONSORSHIP TRANSITION DRIVERS

- *Complexities of Healthcare*
- *Leadership Turnover*
- *Competition*
- *Ability to Attract & Retain Talent*
- *Board Strength*
- *Technology Demands*
- *Financial Pressure*
- *Reinvestment Requirements*
- *Access to Capital*
- *Hospital Consolidation in the Marketplace*
- *Growth Capital*
- *Diversification of Service Lines*

A Discussion About Size and Scale

Ziegler often gets asked the question, “How big is big enough?” The answer to this question is not a simple one and often comes down to sophistication, overall revenue, and the ability to be competitive in your local market(s).

No, bigger is not always better, particularly with increasing size, decisions may take longer, communication can be slower, and there have been examples of mega-organizations with a large national footprint who have struggled. However, given the growing complexity of the sector and the sponsorship transition drivers that were previously outlined, the larger you are and the greater your sophistication, the more likely you will be able to sustain yourself in the long-term. Size can indeed be your friend. So, what specifically does greater size and sophistication bring to the table?

- Greater ability to attract top-talent
- Higher level of board engagement
- Improved purchasing power
- Ability to spread overhead
- Ability to create specialized positions (e.g., IT, Healthcare, Workforce)
- Enhanced brand awareness
- Stronger partner to healthcare partners
- Growth in mission and an expanded vision
- Increased ability to borrow capital
- Greater diversification of services

Many senior living providers are acknowledging the ability to escalate their own pace of growth through affiliations, mergers and acquisitions as opposed to new campus development, which is generally a resource-heavy endeavor that can take 2-3 times longer to come to fruition. Additionally, providers who have chosen to dispose of a community often utilize sale proceeds to fund future growth initiatives.



KEY DISCUSSION POINTS FOR | SENIOR LIVING PROVIDERS

It is always encouraged for organizations to have discussions about growth specifically the board and leadership's interest in growth, through sponsorship transition. Whether a decision is made to move in that direction or not is a personal one, but the journey of the conversation is important. There is a clear difference in sophistication and ability to quickly take advantage of opportunities among organizations who have undertaken affiliation readiness discussions and those who have not. Being prepared and very clear on the position of the board, as well as key stakeholder groups, is a clear sign of sophistication. It is recommended that time be devoted to generative discussion during regularly-held board meetings, strategic planning retreats, or within strategic planning committee meetings. There are several key themes that can drive strategic conversations at the board and leadership team level. The following generative questions can provide guidance to organizations who are having the discussion.

Why do we want to grow?

What is the organization's readiness for growth?

Is the organization looking to be the affiliator or is there willingness to be the affiliatee?

What is the organization's criteria for a potential partner?

Why Do We Want to Grow?

If the board's answer to this question is "We are not interested in growth," then the conversation stops there. Indeed, for some that is the answer. The reality is, there are some organizations that are not growth-oriented and are comfortable with maintaining the status-quo. While there is danger in that line of thinking, that debate is for another time. There are some organizations who are divided on this topic. In those instances, time needs to be spent working through the varying opinions and landing on a unified position within the organization. For those who have general agreement around the need to grow and evolve, having clarity around the reasons for growth is important. Starting with that simple question, "Why do we want to grow?" can stimulate meaningful dialogue and serve as a foundational element to any growth or strategic plan.

What is the Organization's Readiness for Growth?

There are many elements that go into whether an organization is sufficiently prepared for growth. Three in particular stand out as important to assess when growth through sponsorship transition is a strategy.

The first element relates to the organization's **risk tolerance**. This includes not only the obvious elements of financial risk associated with various growth strategies, but also the pace at which the organization is comfortable moving forward. Some organizations prefer to move more quickly while others may feel that a more measured pace of growth best fits with the internal culture. Knowing where the board and leadership is along the risk spectrum is important. If various stakeholder groups are on different pages, that will inevitably result in internal friction.

The second element relates to **resources**. What resources, both financially and from a human capital standpoint, does the organization have to devote to an affiliation or acquisition? Even before any sponsorship transition gets to the finish line, there is a significant amount of work that goes into evaluating potential partners, getting to know the other organization and the due diligence process to name a mere few. There may be occasions where an organization desires growth, but the timing might not be ideal for a variety of reasons. It can be hard to say no or walk away from opportunities, but if the resources are simply not available to pursue a sponsorship transition, the organization needs to have the discipline to say no. Having said that, there are also times where priority needs to be reassessed. How high of a priority are the growth initiatives? If the board positions growth through affiliations, acquisitions or mergers as a top priority, other items might need to shift to ensure this work gets the appropriate amount of attention.

The final readiness element to comment on relates to the **corporate structure**. Without a doubt, certain organizational structures can facilitate growth while others can hinder it. It is important to talk with legal counsel about current and future goals and assess whether the current structure is supportive. The right corporate structure not only aligns with growth objectives, but is an effective tool in mitigating risk.

Affiliator or Affiliatee?

This discussion is generally one related to control. Are you willing to become a part of another organization through a transfer of sponsorship or are you only interested in growth whereby you are the primary sponsor and other organizations fold into yours?

It is noteworthy to acknowledge that when you are in a position of financial and operational weakness you may not have a choice in this regard. For those who are approaching this topic strategically and from a position of strength, this question is a healthy one to discuss as a group. There are a number of successful examples on both sides of this equation. The board and leadership team need to determine what degree of control they desire within the new entity, which is generally reflected at the governance level through board representation.

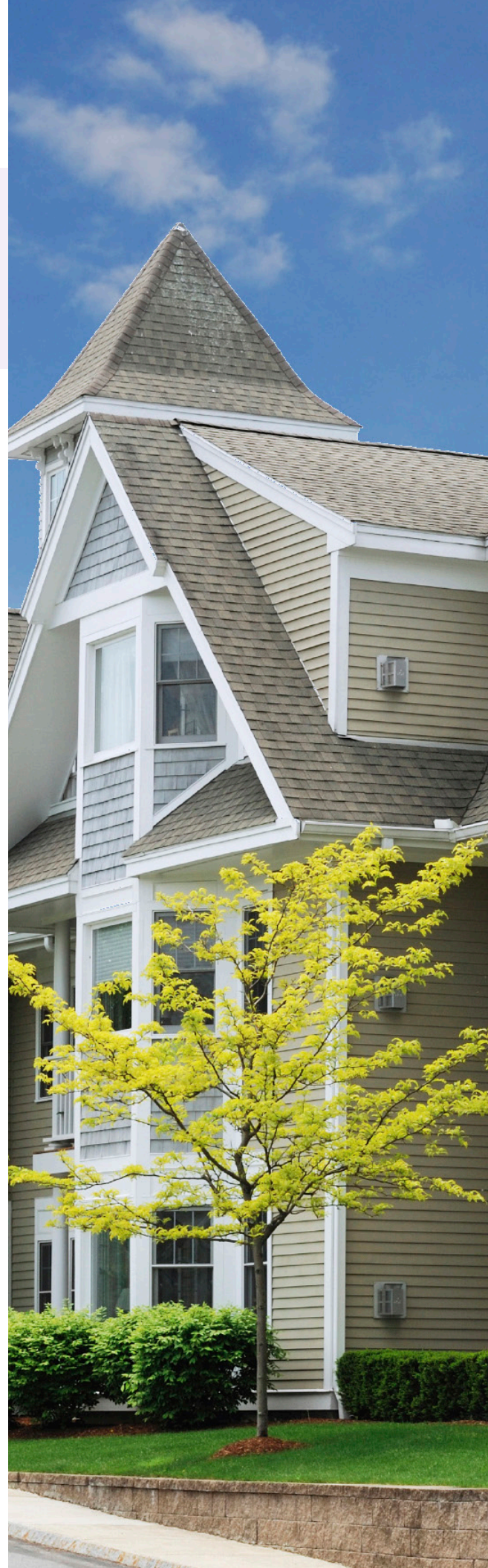
What is the Organization's Criteria for a Potential Partner?

Spend time as a group discussing your organization's criteria for partnership. It is recommended that you start by identifying the short list of non-negotiables and then back it up with "nice to have" criteria.

The reality is, until you have the partnership opportunity in front of you, one cannot fully predict all of the characteristics and nuances that may come into play. What is important is for the leadership team to understand the board's perspective. This understanding can free up time and allow the leadership to conduct preliminary exploration of sponsorship transition opportunities without having to regularly check in with the board to get their perspective. This is another example of sophistication. When the leadership team is clear on the goals and expectations of the board, they can be much more nimble and are better prepared to respond to opportunities. Organizations who have not yet defined their criteria, if approached for an affiliation or acquisition opportunity, will likely be surpassed by others who can move more quickly. The opportunity will be lost. Common elements on the criteria grid include:

- **Mission alignment**
- **Geographic proximity**
- **Financial and operational health**
- **Community/facility type**
- **Service line diversification**
- **Strength of existing leadership team**
- **Reputation**
- **Compatibility with existing service lines**
- **Quality**
- **Unit mix compatibility**
- **Ability to expand/continue growth**
- **Need for capital**
- **Reinvestment requirements**

It is recommended to have a list with an abbreviated number of criteria with limited specificity behind each. Having too many parameters and criteria can significantly limit potential opportunities.



STRATEGY VS | NEED-DRIVEN DECISIONS

Yes, we have saved this for last. The previous discussions have been under the working assumption that the organization has the ability to determine its future direction and is generally looking at sponsorship transition from a strategic standpoint. Unfortunately, there are indeed examples where organizations are limited in their choices because of operational and/or financial pressures. A community might be feeling early signs of distress with declining occupancy, perhaps a few covenant violations, and a pending CEO retirement. A multi-site organization may have been subsidizing an under-performing community for multiple years to the tune of several million dollars in a competitive, difficult market and decided that the bleeding needs to stop. Between 2010 and 2018, roughly 260 not-for-profit communities have been sold to for-profit owners and operators and more than 40 not-for-profit communities have closed.¹

Waiting Too Long

It is imperative that the board and leadership not ignore warning signs and be proactive with pursuing sponsorship transition or disposition strategies before it is too late.

This is the job of the board and executive leadership and being asleep at the wheel or looking the other way for too long can have tragic consequences. These discussions are difficult and can truly test the mission, vision and values of the organization, but it is important to not wait too long to make decisions. There are indeed potential partners who are willing to purchase distressed properties, but in those scenarios the existing sponsor will have little control, will obtain a much lower sale price than what it would have a few years earlier, and will have a limited number of interested candidates. The reality as well is that there will likely be few, if any, not-for-profit purchases at the table if the property is in too great of financial distress. By waiting too long, organizations often lose control of the very mission they are trying to preserve.

THE HARD TRUTH CHECKLIST

- ***Are we facing leadership turnover with no clear successor and limited ability to attract top talent?***
- ***Are we struggling to be among the top one or two leaders in our market?***
- ***Are we having occupancy challenges that continue to deepen?***
- ***Are we having financial challenges and are struggling to meet debt obligations?***
- ***Are we limited in our ability to borrow additional capital for reinvestment needs?***
- ***Are we able to recruit and retain subject-matter experts to oversee specialty areas within the organization (e.g., technology, payment and healthcare reform)?***
- ***Are reputation and quality issues negatively impacting our organization?***


¹Ziegler Investment Banking

LEARNING FROM | OUR PEERS

Much knowledge is gained by learning from others who have gone through some form of sponsorship transition. One of the notable attributes of the not-for-profit senior living sector is the willingness for others to share their stories. This section is intended to highlight several examples of not-for-profit sponsorship transitions and put forth real-life examples that connect the dots with the variety of themes covered in this paper.

“Our boards agreed, that at the completion of the merger, if all we accomplished was one plus one equals two, we will have failed. We need to accomplish something greater by coming together.”

- Bob Dahl, CEO, Cassia

<p>Merger of Equals (Multi-sites)</p> 	<ul style="list-style-type: none"> • Two, Minnesota-based multi-site providers merged to create a new parent organization, named “Cassia” • Retiring C-Suite team, competitive healthcare environment and long history of knowing one another in similar regions led to the merger • New organization has more than 45 market-rate communities and an annual revenue of nearly \$250 million
<p>Single-Site Provider Joining a System</p> 	<ul style="list-style-type: none"> • New-Jersey based single-site Life Plan Community joins Philadelphia-based multi-site organization • Retiring, long-time CEO; starting to feel occupancy pressures and ability to thrive as single-site organization • Formal search took place and Acts Retirement-Life Communities was chosen as the new sponsor
<p>Merger of Equals (Single-sites)</p> 	<ul style="list-style-type: none"> • In 2012, two, Kansas-based single-site organizations, Kidron Bethel Village and Schowalter Villa, came together to form “Bluestem Communities” • Have successfully grown the Bluestem services to include a multi-county PACE platform
<p>Not-for-Profit Acquisition</p> 	<ul style="list-style-type: none"> • Sponsor of St. Joseph’s John Knox Tampa Bay, a Life Plan Community in Tampa, Florida, was looking to sell the community and Concordia Lutheran Ministries, headquartered in Pennsylvania, was the successful bidder • Concordia has repeatedly grown through acquisition, particularly of distressed or low-cost communities and facilities, and will reinvest and stabilize the community to achieve improved financial performance
<p>Not-for-Profit Disposition of SNF</p> 	<ul style="list-style-type: none"> • After much analysis and deliberation, decided to sell Kansas City Presbyterian Manor due to ongoing skilled nursing and reimbursement pressures in Kansas and needed to rebalance overall portfolio, lessening healthcare exposure • Partnered with Ziegler to conduct a search for a new owner and closed the sale to a reputable, for-profit entity in July of 2016

ZIEGLER'S COMMITMENT TO SPONSORSHIP TRANSITIONS

Ziegler's ongoing commitment to the senior living sector is evident by the creation of the sponsorship transitions team. This specialty team represents Ziegler's ability to play a strategic, advisory role in support of not-for-profit organizational growth and mission enhancement.

WHO WE ARE

Ziegler is a privately held, national boutique investment bank, capital markets and proprietary investments firm. It has a unique focus on healthcare, senior living and education sectors, as well as general municipal and structured finance. Headquartered in Chicago with regional and branch offices throughout the U.S., Ziegler provides its clients with capital raising, strategic advisory services, fixed income sales, underwriting and trading as well as Ziegler credit analytics.

PRODUCTS & SERVICES

We customize solutions to meet our clients' strategic and financial objectives, and take a true advisory approach into our engagements and long-term relationships.

- Assessing organizational readiness and strategic opportunities for sponsorship transition
- Identifying potential candidates for a sponsorship or affiliation transition (for either party involved)
- Supporting co-venture initiatives in support of healthcare realignment
- Advising organizations on due diligence work and risk identification
- Supporting all parties through the transition and integration of the two organizations

CONTACT US

For further information on Ziegler's services related to not-for-profit Sponsorship Transitions, please contact the Ziegler banker in your region or reach out to Stephen Johnson, practice leader, at sjohnson@ziegler.com.

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