



Carol -

I see you have SS 398  
on the agenda next week. But -  
here is our most recent audit of the  
MCH Hospital & Clinics Authority -  
the the book -  
Jan

Jan

Is this an item  
for Jennifer?

AN EVALUATION

*University of Wisconsin  
Hospital and Clinics Authority*

01-12

WISCONSIN  
LEGISLATIVE AUDIT BUREAU



AN EVALUATION

*University of Wisconsin  
Hospital and Clinics Authority*

*01-12*

*June 2001*

**2001-2002 Joint Legislative Audit Committee Members**

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Gary R. George, Co-chairperson  
Judith Robson  
Brian Burke  
Peggy Rosenzweig  
Mary Lazich

**Assembly Members:**

Joseph K. Leibham, Co-chairperson  
Samantha Starzyk  
John Gard  
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State Auditor - Janice Mueller

Editor of Publications - Jeanne Thieme

Audit Prepared by

Don Bezruki, Director and Contact Person  
Julie Gordon, Director  
Dean Swenson  
Tim Coulthart  
Jolie Frederickson  
Conor Smyth  
James Zylstra

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**Appendix 5—Response from the University of Wisconsin Hospital and Clinics Authority**

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State of Wisconsin \ LEGISLATIVE AUDIT BUREAU

JANICE MUELLEF  
STATE AUDITOR

22 E. MIFFLIN ST., STE. 500  
MADISON, WISCONSIN 53703  
(608) 266-2811  
FAX (608) 267-0411  
Leg\_Audit.Info@legis.state.wi.us

June 21, 2001

Senator Gary R. George and  
Representative Joseph Leibham, Co-chairpersons  
Joint Legislative Audit Committee  
State Capitol  
Madison, Wisconsin 53702

Dear Senator George and Representative Leibham:

As required by s. 13.94(1)(o), Wis. Stats., we have completed an evaluation of the implementation and operating agreements between the University of Wisconsin (UW) and the UW Hospital and Clinics Authority. The Authority is an independent, nonprofit entity established by the Legislature in 1996 to operate the 536-bed hospital and a number of clinics on the UW-Madison campus, as well as other outpatient clinics and facilities in the Madison area. In fiscal year (FY) 1999-2000, the Authority had revenue of \$400.0 million and operating expenses of \$395.0 million; in September 2000, it employed 4,263 full-time equivalent staff.

The Authority was created to allow increased management flexibility in hospital operations and greater competitiveness in a changing health care environment. Although it has not engaged in networking activities to the extent that had been envisioned at the time it was established, it has established relationships with a number of health care entities. It has also used the \$106.5 million in bonding authority authorized by the Legislature to engage in an aggressive building program, including construction of two outpatient clinics in Madison.

The Authority's financial performance, like that of other academic medical centers, has been mixed. Revenue in excess of expenses declined from \$13.8 million in FY 1996-97, the Authority's first year of operation, to \$5.0 million in FY 1999-2000; however, it increased during the first ten months of FY 2000-01.

The Authority is generally fulfilling its statutory mission of delivering comprehensive, high-quality health care, including charity care; providing medical instruction; sponsoring and supporting health care research; and providing medical outreach services statewide. In FY 1999-2000, the Authority transferred \$16.3 million to UW medical, nursing, and pharmacy schools and spent directly another \$14.7 million in support of medical education.

We appreciate the courtesy and cooperation extended to us by the Authority. The Authority's response is Appendix 5.

Respectfully submitted,

Janice Mueller  
State Auditor

JM/DB/ao

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## Summary

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The University of Wisconsin Hospital and Clinics Authority is an independent, nonprofit public entity that was established in 1996 to allow the University of Wisconsin Hospital and Clinics (UWHC) to operate with increased flexibility. The Authority operates a 536-bed teaching hospital and a number of clinics that had been operated as part of the University of Wisconsin (UW)-Madison, as well as other outpatient clinics and facilities in the Madison area. Its four-part statutory mission includes patient care, medical education, research, and public service. In fiscal year (FY) 1999-2000, the Authority's revenue was \$400.0 million and its expenses were \$395.0 million. In September 2000, it employed 4,263 full-time equivalent staff.

1995 Wisconsin Act 27, which created the Authority, also required it to enter into a series of agreements with the Board of Regents, including an affiliation agreement that defines the relationship between the Authority and UW-Madison, and a lease that allows the Authority to use state-owned property. In addition, the two parties entered into a conveyance agreement that transferred various assets and liabilities from UW-Madison to the Authority, and an operating and services agreement. Statutes require the Legislature's Joint Committee on Finance to review the affiliation agreement and the lease before June 29, 2001, to determine whether these agreements should be continued or modified. They also direct the Legislative Audit Bureau to conduct an evaluation of the agreements. Therefore, we determined whether the Authority and the Board of Regents have adhered to the agreements they signed; reviewed the Authority's networking activities and its capital acquisition, personnel, and purchasing practices; and examined the Authority's financial and operational performance.

The agreements have resulted in significant ongoing cash transfers between the Authority and UW-Madison. For example, in FY 1999-2000, the Authority paid \$32.9 million to UW-Madison, including funds to support medical education. Similarly, UW-Madison paid the Authority \$12.5 million for various supplies and services, as well as salaries for staff of the Authority who provide services to UW-Madison. Officials of the Authority and UW-Madison are generally satisfied with the agreements and the working relationship the agreements define, and except in a few minor instances they have complied with the agreements' requirements.

To compete in the health care market more effectively, the Authority has established relationships with a number of entities that operate under the name UW Health, including approximately 50 outpatient clinics.



Among these are clinics that had been operated by Physicians Plus Medical Group, S.C., a 225-member physician practice plan that was acquired by the UW Medical Foundation in 1998 and currently operates as a separate division within it. The Joint Committee on Finance recently voted to make tax-exempt, beginning in January 2002, property owned or leased by the UW Medical Foundation.

Although it has developed relationships with other entities, the Authority has not engaged in networking activities to the extent that had been envisioned at the time of its creation. On the other hand, the Authority has taken advantage of its increased operational flexibility to engage in an aggressive building program. Statutes allow the Authority to issue up to \$106.5 million in bonds for any purpose. As of March 2000, the Authority had issued bonds to the full extent allowed by statutes. The Governor's 2001-03 Biennial Budget Proposal recommends increasing the Authority's bonding limit to \$175.0 million.

Despite its nonprofit status, the Authority must maintain a strong financial position to operate effectively in a changing health care environment and support a mission that includes medical education, research, public service, and charity care. To date, its financial performance, like that of other academic medical centers, has been mixed. Total revenue has exceeded expenses in each year since the Authority's creation, but operating revenue has increased less rapidly than operating expenses. As a result, revenue in excess of expenses, or "profits," declined from 4.3 percent of revenue in the Authority's first year of operation to 1.3 percent in FY 1999-2000. However, these "profits" increased to 4.9 percent of revenue in the first ten months of FY 2000-01.

The Authority's cash reserves exceeded the level that had been maintained at the time of its creation but have fallen since June 1997. Statutes require the Authority to retain a minimum level of cash reserves recommended by an independent auditor. However, the Authority's auditor has declined to recommend a specific level of cash reserves; instead, it has suggested a range based on other hospitals' reserves. Authority officials indicate they try to maintain the Standard & Poor's median for hospitals rated "A." While the Authority's cash reserves are within the range suggested by its auditor, they have declined in three of the last four years. If the cash reserves were to fall below the recommended range, the Authority's creditworthiness would be affected, which would in turn affect its ability to finance facility and equipment improvements.

In contrast to declines in profitability and cash reserves, the number of inpatient admissions to UW Hospital increased 5.0 percent from FY 1995-96, the year before the Authority was established, through FY 1999-2000. During the same period, UW Hospital's average daily census remained relatively constant, ranging from 337 patients in

FY 1997-98 to 352 in FY 1998-99. Its occupancy rate during this period ranged from 71.7 percent to 76.4 percent. Outpatient clinic visits increased from 342,405 in FY 1995-96 to 442,339 in FY 1999-2000, or by 29.2 percent; net revenue from outpatient services represented 35.8 percent of net patient service revenue in FY 1999-2000, compared to 28.7 percent in FY 1996-97.

Although there have been mixed trends in the Authority's financial and operational performance during the first four years, officials believe that overall performance will improve and that the Authority is well-positioned to compete in the health care market. Nevertheless, these mixed trends in financial and operational performance suggest that continued scrutiny by the Legislature may be warranted to ensure the Authority continues to meet its statutory mission.

A variety of measures indicate that the Authority is maintaining the high level of service that UWHC had provided when it was operated by UW-Madison. As part of its mission to provide patient care, the Authority reduces or forgives the cost of medical services to certain qualified individuals. In FY 1999-2000, this charity care totaled \$7.3 million and had increased 15.9 percent from the level provided before the Authority was established. The proportion of gross patient revenue the Authority has devoted to charity care in recent years is comparable to charity care levels at 12 other large Wisconsin hospitals.

The Authority also appears to have maintained and in some cases increased its support of medical education at UW-Madison. Deans of the medical, nursing, and pharmacy schools are satisfied with the level of financial support, which includes direct transfers that increased from \$13.1 million in FY 1996-97 to \$16.3 million in FY 1999-2000, and direct expenditures for medical education that increased from \$12.7 million to \$14.7 million in the same period. The Authority also transferred \$6.3 million to support capital expenditures of the UW Medical School. It pays \$79,864 annually to lease property from the UW Medical School and provides additional indirect support, but officials do not maintain the records needed to determine the value of this support.

Officials of the Authority and of UW-Madison indicate that support for medical research has been maintained at the same level provided when UWHC was operated by UW-Madison. The Authority does not provide a significant amount of direct funding for health care research, but it does provide research space and services. For example, it operates a general clinical research center where studies funded by the National Science Foundation are conducted, as well as a clinic that houses the Women's Health Initiative, which conducts research on breast cancer and osteoporosis. Medical professionals at UWHC also conduct clinical trials of new drugs, technology, and procedures. We were unable to quantify the overall value of outreach activities sponsored by the

Authority, but officials believe they are at least maintaining the level of effort that had been provided in the past.

In advocating for the Authority's creation, UWHC officials had contended that the hospital's operations were constrained by excessive oversight, especially related to capital acquisition, personnel, and purchasing. Capital acquisition procedures have changed considerably since the Authority's creation. Now, the Authority can complete projects on state-owned land if they cost less than a specified threshold—which was \$277,800 in FY 2000-01—without obtaining outside approval and review. In its first four years of operation, 103 of the Authority's 109 projects fell below the threshold. Projects on state-owned land that cost more than the threshold continue to require review by UW-Madison, the Board of Regents, and the Department of Administration.

The Authority also gained considerable flexibility in personnel management, which officials indicate has addressed many concerns that were raised before the Authority's creation. For example, the Authority now has responsibility for recruiting and supervising all UWHC staff. It also assigns employees to specific job classifications, and it bargains separately with represented employees' unions. Staff increased from 3,803 in September 1997 to 4,263 in September 2000, or by 12.1 percent. Under a contractual services agreement, 1,917 blue-collar, technical, and administrative staff remain employees of a state agency that receives its entire budget—\$67.5 million in FY 2000-01—from the Authority.

The Authority was able to promptly negotiate three of its four union contracts for 2001-2003, but negotiations for the nurses' contract have been protracted, and the nurses' union filed an unfair labor practices complaint with the Wisconsin Employment Relations Commission on May 15, 2001. While issues between the Authority and the nurses' union are complex, many appear to be influenced by the difficulty the Authority has had in employing and retaining a sufficient number of nurses, especially inpatient nurses.

Authority and union officials have separately indicated that currently, salaries overall are generally competitive and that recruitment and retention difficulties are caused, in part, by a general shortage of nurses nationwide. However, union officials also cited the greater use of forced overtime at the Authority as a factor contributing to retention difficulties. Nurses' union data, which we adjusted to reflect differences in staff sizes, indicate the Authority required extra shifts four times more often than extra shifts at UW Hospital were required by Meriter Hospital in 2000. The Authority indicates that its nurses worked 2,598 mandated extra shifts in 2000, which is an average of 3.35 mandated extra shifts per nurse. It should be noted that because some hospital and clinic units may require mandated overtime more

frequently than others, the experience of an individual nurse may vary considerably from the average. For example, information from the Authority indicates that 12 percent of nurses had six or more mandated shifts in the prior 12 months, while 88 percent had five or fewer such shifts.

Authority officials indicate they are continuing to take steps to lower their nurse vacancy rate, which should reduce the need for mandatory extra shifts. The vacancy rate has declined from 21.0 percent in July 2000 to 11.6 percent in May 2001. Nevertheless, the officials indicate that because of the large number of specialty beds they have, they need to recruit relatively larger numbers of nurses with specialized training than surrounding hospitals. Consequently, recruitment and retention will continue to be challenging.

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**WISCONSIN LEGISLATIVE AUDIT BUREAU  
AUDIT SUMMARY**

Report 01-12

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June 2001

**UNIVERSITY OF WISCONSIN HOSPITAL AND CLINICS AUTHORITY**

1995 Wisconsin Act 27 created the University of Wisconsin (UW) Hospital and Clinics Authority as an independent, nonprofit public entity on June 29, 1996. The Authority operates a 536-bed teaching hospital, a number of clinics on the UW-Madison campus, and other outpatient clinics and facilities in the Madison area. In fiscal year (FY) 1999-2000, the Authority's revenue was \$400.0 million and its expenses were \$395.0 million. It employed 4,263 full-time equivalent staff in September 2000.

**The Authority and UW-Madison Have Complied with Their Agreements**

Act 27 required the Authority to enter into several agreements that define the relationship between the Authority and UW-Madison. These agreements help ensure the Authority continues to support medical education at UW-Madison, and allows the Authority to lease a portion of the Clinical Sciences Center, which contains the UW Hospital, and other on-campus facilities the State owns. Significant ongoing cash transfers between the Authority and UW-Madison occur as a result of these agreements. In FY 1999-2000, the Authority paid UW-Madison \$32.9 million to support medical education and pay for supplies and other services, and UW-Madison paid \$12.5 million to the Authority for the salaries of Authority staff who support UW-Madison's research activities. The Authority and UW-Madison have complied with the main provisions of their agreements, and both parties are generally satisfied with their working relationship.

**The Authority Has Undertaken an Aggressive Building Program**

Since 1996, the Authority has used its statutory ability to issue bonds for any purpose to undertake an aggressive building program. It has issued \$106.5 million in bonds, the full limit allowed by statutes, to finance a number of projects, such as construction of the UW Health-East Clinic and UW Health-West Clinic in Madison. These two projects total 235,000 square feet.

The Authority and several other health-related entities collectively use the name UW Health for marketing and public relations purposes. UW Health is a registered trademark of the Board of Regents, which has granted the Authority and other participating parties, including UW-Madison and the UW Medical Foundation, a royalty-free license for its use. These parties collaborate in the delivery of patient care, health care education, and research. UW Health also includes several nonprofit, tax-exempt corporations, including University Health Care, Inc. and University Community Clinics, Inc., that assist in networking activities, including purchasing and developing local and regional physician practices. In FY 1999-2000, the Authority provided \$4.2 million to these two nonprofit corporations.

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## **The Authority's Financial Performance Has Been Mixed**

To continue its mission of providing high-quality health care and supporting medical education, the Authority must maintain a strong financial position. Like academic medical centers nationwide, the Authority's financial performance has been mixed. Revenue in excess of expenses, or "profit," declined from \$13.8 million in FY 1996-97, the Authority's first year of operation, to \$5.0 million in FY 1999-2000, but it increased during the first ten months of FY 2000-01.

During the Authority's first four years, various measures of operating performance, such as the number of inpatient admissions to UW Hospital, were positive. For example, annual inpatient admissions increased from 19,247 in FY 1995-96 to 20,202 in FY 1999-2000, or by 5.0 percent. Visits to the Authority's outpatient clinics increased 29.2 percent during this same period, and totaled 442,339 in FY 1999-2000. However, during the first ten months of FY 2000-01, the Authority did not meet its operating performance goals.

The Authority's mission is to deliver comprehensive, high-quality health care, including charity care to the indigent; provide a suitable environment for medical instruction; sponsor and support health care research; and conduct outreach activities. The Authority is generally fulfilling its statutory mission. For example, in FY 1999-2000, charity care totaled \$7.3 million, and had increased 15.9 percent from the level provided before the Authority was established. The Authority also has maintained, and in some cases increased, its support of medical education at UW-Madison.

## **The Authority Has Had Difficulty Employing a Sufficient Number of Nurses**

The Authority has considerable flexibility in personnel management, which addressed many concerns that were raised before its creation. However, while the Authority was able to promptly negotiate three of its four union contracts for 2001-2003, negotiations for the nurses' contract have been protracted, and the nurses' union filed an unfair labor practices complaint with the Wisconsin Employment Relations Commission in May 2001. While issues between the Authority and the nurses' union are complex, many appear to be influenced by the difficulty the Authority has had in employing and retaining a sufficient number of nurses, especially inpatient nurses. Union officials also cite the greater use of forced overtime at the Authority as a factor contributing to retention problems.

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## Introduction

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**The Authority is an independent public entity that began operation on June 29, 1996.**

The University of Wisconsin Hospital and Clinics Authority is an independent, nonprofit public entity that was created on June 29, 1996, to allow the University of Wisconsin Hospital and Clinics (UWHC) to operate with increased flexibility. The Authority operates a 536-bed teaching hospital and a number of clinics that had been operated as part of the University of Wisconsin (UW)-Madison, as well as other outpatient clinics and facilities in the Madison area. Its four-part mission, which is mandated in statutes, includes patient care, medical education, research, and public service. In fiscal year (FY) 1999-2000, the Authority's revenue was \$400.0 million, and its expenses were \$395.0 million. In September 2000, it employed 4,263 full-time equivalent (FTE) staff. The Authority is governed by a 15-member board of directors, which appoints the chief executive officer. Appendix 1 describes the board's membership, which includes members of the Legislature, the Board of Regents, and gubernatorial appointees.

The Authority was created in 1995 Wisconsin Act 27, the 1995-97 Biennial Budget Act, in response to concerns that if UWHC could not respond rapidly to changes in the health care market and compete successfully with other local and regional medical facilities, its ability to continue to deliver high-quality patient care and to provide continued financial support for medical education at UW-Madison would be jeopardized. UWHC officials also asserted that their purchasing, personnel, and capital acquisition activities were excessively constrained by state and university oversight requirements.

The legislation that created the Authority also required it to enter into an affiliation agreement with the Board of Regents that defines the relationship between the Authority and UW-Madison and specifies the amount of annual financial support the Authority will provide for medical education at UW-Madison, as well as a lease that allows the Authority to use state-owned property and specifies the amount the Authority will pay the State to lease the Clinical Sciences Center, which houses the hospital, clinics, and other facilities on the UW-Madison campus. Statutes also provide the Authority with the ability to issue bonds for any purpose up to a limit established by the Legislature, which is currently \$106.5 million.

In addition, statutes require the Joint Committee on Finance to review the affiliation agreement and the lease before June 29, 2001, and every five years thereafter, to determine whether these agreements should be continued or modified. Section 13.94(1)(o), Wis. Stats., directs the Legislative Audit Bureau to conduct an evaluation of the agreements.

Therefore, we:

- determined whether the Authority and the Board of Regents have adhered to the primary provisions of the affiliation agreement and lease, as well as other agreements they signed;
- reviewed the Authority's networking affiliations with other health-related organizations;
- examined the Authority's financial and operating performance and the extent to which it has fulfilled its statutory mission; and
- examined whether the restructuring has allowed the Authority to improve its capital acquisition, personnel, and purchasing processes.

In conducting this evaluation, we spoke with officials of the Authority and the University, including the deans of the UW Medical School, the UW School of Nursing, and the UW School of Pharmacy; reviewed the contracts and agreements between the Authority and the Board of Regents; reviewed available data and other information concerning the Authority's finances and operations, including the amount of support it provides for medical education; analyzed comparative data for other Wisconsin hospitals; and reviewed statistics on academic medical centers nationwide.

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## Agreements with the University of Wisconsin Board of Regents

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**Several agreements define the relationship between the Authority and UW-Madison.**

In addition to the affiliation agreement that defines the relationship between the Authority and UW-Madison and a lease that allows the Authority to use state-owned property, the Authority and the Board of Regents have entered into a conveyance agreement that transferred various assets and liabilities from UW-Madison to the Authority, and an operating and services agreement. The affiliation agreement and the lease include all statutorily required provisions, and officials of the Authority and UW-Madison are generally satisfied with all of the agreements and the working relationships the agreements define. However, the Authority has not complied with a small number of technical requirements.

### **Affiliation Agreement**

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**An affiliation agreement stipulates the Authority's support for medical education at UW-Madison.**

The affiliation agreement, which was signed in 1996, helps to ensure that the Authority fulfills its statutory mission, including maintaining the level of financial support for medical education at UW-Madison that had been provided by UWHC before June 1996. The agreement has a term of 30 years and is automatically extended for 1 year each July 1 unless termination procedures are exercised. Section 233.04(7m), Wis. Stats., requires the affiliation agreement to contain provisions that ensure:

- the Authority financially supports UW-Madison's medical educational, clinical, and research activities;
- the Authority maintains cash reserves at a level recommended by an independent auditor;
- the Authority develops standards for the selection and financing of any corporation or partnership that provides health-related services, and these standards are consistent with the Authority's and the Board of Regents' missions; and
- the Board of Regents establishes reasonable charges for any services that it provides the Authority.

In addition to these statutory provisions, the affiliation agreement sets forth the broad principles that govern the relationship between the Authority and the Board of Regents, including recognition of how each entity's planning efforts can affect the other. For example, the Authority

and the Board of Regents have each agreed to consider the effect of their plans on the other's mission and to cooperate in conducting research.

The affiliation agreement also specifies the responsibilities of the Authority and the Board of Regents in such areas as personnel, education, research, and external relations. For example, the Authority and UW-Madison fund a joint public affairs office in order to present a unified image to the public. Each must also notify the other regarding changes to personnel policies. Finally, because UWHC had previously used the UW Foundation—an independent, nonprofit, tax-exempt corporation that attempts to secure private financial support for UW-Madison—for its fund-raising efforts, it was agreed that the Authority would continue to do so.

### Lease

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**The Authority has signed a 30-year lease for all on-campus facilities it occupies.**

Construction of the 480,000 square foot Clinical Sciences Center, which contains the 536-bed UW Hospital, outpatient clinics, and other facilities, was completed in 1979 at a cost of \$101.5 million. It was one of the most ambitious capital construction projects ever undertaken by the State. A lease between the Authority and the Board of Regents was executed in 1996 to protect this investment and other on-campus facilities the State owns. Statutes allow a lease term of up to 30 years. Like the affiliation agreement, with which it runs concurrently, the lease is automatically extended each July 1 for an additional year unless termination procedures are exercised by either party. Statutes stipulate that the lease contain other provisions requiring:

- the Authority to pay annual rent of \$1.00 plus an amount equaling the debt service on all outstanding bonds issued by the State to finance the construction of the Clinical Sciences Center and other on-campus facilities that the Authority leases;
- the State to own any facility that the Authority constructs on state-owned land, as well as any modifications the Authority makes to on-campus facilities; and
- the Board of Regents to be protected from all liability associated with the Authority's management and use of the on-campus facilities.

In addition to the required provisions, the lease contains provisions to protect the State's interest in its property. Under these provisions, the Authority must:

- use the Clinical Sciences Center and other on-campus facilities to further its statutory mission;
- furnish the State Building Commission with the opinion of a nationally recognized bond counsel if it sublets any portion of the leased facilities, because subletting a significant portion of the building could affect bondholders' financial interests and the Authority's tax-exempt status; and
- pay maintenance expenses for interior common space within the Clinical Sciences Center, based on the proportion of space it occupies.

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**The Authority leases 58 percent of the Clinical Sciences Center on the UW-Madison campus.**

Since the Authority's creation, it has leased 58 percent of the Clinical Sciences Center. UW-Madison occupies the remaining 42 percent, using it for instruction, research, and laboratory work that supports medical education.

Authority and UW-Madison officials believe that the terms of the lease have worked well, and both parties have complied with it substantially. However, we noted a few minor instances in which the Authority and UW-Madison have not complied with some requirements. For example, the Authority did not obtain the opinion of bond counsel when it sublet 352 square feet in the Clinical Sciences Center to University Health Care, Inc., a nonprofit corporation that is partially controlled by the Authority, or 458 square feet to Ameritech for telephone wiring. Authority officials did not obtain the bond counsel's opinion because they considered the subleases a continuation of arrangements that predated the Authority's creation, and the amount of space that was sublet was insignificant.

In addition, the Authority did not charge UW-Madison for its share of maintenance expenses for the interior common space within the Clinical Sciences Center from June 1996 through October 2000. Under the terms of the lease, we estimate UW-Madison should have paid approximately \$189,350, or 42 percent of total maintenance costs incurred by the Authority from FY 1996-97 through FY 1999-2000, based on the proportion of space UW-Madison occupies in the building. Authority officials attributed this oversight to improper computer coding and indicated that UW-Madison was properly charged for maintenance expenses beginning in November 2000.

## Conveyance Agreement

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### A conveyance agreement transferred assets and liabilities to the Authority.

To facilitate the June 1996 restructuring, the two parties entered into a conveyance agreement that transferred from UW-Madison to the Authority UWHC's:

- assets and liabilities;
- tangible personal property, including UWHC patient and financial records;
- contracts, including leases for all equipment used by UWHC; and
- Personnel Commission cases, unemployment compensation claims, and other pending personnel matters.

As shown in Table 1, the \$103.0 million transferred from UW-Madison to the Authority included \$101.2 million that had previously been managed by the State of Wisconsin Investment Board. State funds shown in the table are the unencumbered balance of UW-Madison's 1995-96 appropriation for UWHC, which 1995 Wisconsin Act 27 required to be transferred to the Authority. Act 27 also required UWHC to transfer \$15.0 million to the General Fund.

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Table 1

### Assets Transferred to the Authority 1996

<u>Type of Asset</u>	<u>Amount</u>
Investments*	\$101,195,288
State Funds	1,362,906
Gifts and Grants	399,262
Student Loans	<u>45,932</u>
Total	\$103,003,388

\* These investments, which consist of various marketable securities used for capital replacement, bond indenture, and debt retirement purposes, had been managed by the State of Wisconsin Investment Board and are now managed by the UW Foundation.

## Operating and Services Agreement

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**An operating and services agreement addresses various aspects of the Authority's operations.**

The Authority is permitted by 1995 Wisconsin Act 27 to enter into agreements with the Board of Regents as is necessary or convenient for its mission. Accordingly, in June 1996 the parties entered into an operating and services agreement that addresses such areas as:

- security, landscaping, and snow removal;
- Authority employees' access to the University's facilities, such as sports complexes and libraries;
- the use of trade names, trademarks, service marks, and logos;
- payment of utility expenses, such as electricity, water, and sewer services;
- parking arrangements and the use of the University's fleet vehicles; and
- the use of the University's state and federal environmental permits for the Authority's operations.

## Transfers between the Parties

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**The Authority paid \$32.9 million to UW-Madison in FY 1999-2000.**

Execution of these agreements has resulted in significant ongoing cash transfers between the two parties. As shown in Table 2, the Authority paid UW-Madison \$32.9 million in FY 1999-2000 for its share of the services provided under the various agreements. All amounts the Authority pays UW-Madison are reflected in state appropriations.

Table 2

**The Authority's Payments to UW-Madison\***  
 FY 1996-97 through FY 1999-2000  
 (in millions)

	<u>FY 1996-97</u>	<u>FY 1997-98</u>	<u>FY 1998-99</u>	<u>FY 1999-2000</u>	<u>Percentage Change for Period</u>
Affiliation Agreement	\$13.1	\$14.5	\$18.4	\$18.5	41.2%
Operating and Services Agreement	10.5	10.6	10.4	10.9	3.8
Other**	<u>2.5</u>	<u>3.1</u>	<u>3.1</u>	<u>3.5</u>	40.0
<b>Total</b>	<b>\$26.1</b>	<b>\$28.2</b>	<b>\$31.9</b>	<b>\$32.9</b>	<b>26.1</b>

\* The Authority also pays the Department of Administration for the debt service on all outstanding bonds issued by the State to finance the construction of the Clinical Sciences Center. Debt service was approximately \$4.0 million annually from 1997 through 2000.

\*\* Includes funding for services not stipulated in any agreement, such as for services provided by the State Laboratory of Hygiene and other UW-Madison laboratories.

Similarly, the Authority receives payments from UW-Madison for various services that it provides. As shown in Table 3, UW-Madison transferred \$12.5 million to the Authority in FY 1999-2000, including payment for services the Authority provides in support of UW-Madison's research grants and for supplies.

Before the 1996 restructuring, general purpose revenue (GPR) funded 143.0 FTE staff positions at UW-Madison that also provided services to UWHC. When the Authority was created, an agreement was reached that divided compensation responsibility between the Authority and UW-Madison for these positions, which include specified clinical pharmacist, medical technician, and custodian positions. UW-Madison agreed to fund 91.27 FTE positions, and the Joint Committee on Finance reduced UW-Madison's GPR position count by 91.27 FTE positions. While the staff in these positions continue to provide services to UW-Madison, they are now employed by the Authority and the UW Hospitals and Clinics Board, a state agency that was created at the time of the restructuring and that has the same board of directors as the Authority. Included in the \$12.5 million that UW-Madison paid the Authority in FY 1999-2000 is approximately \$4.0 million in GPR to help fund these positions, and this amount is reflected in state appropriations.

Table 3

**UW-Madison Payments to the Authority**  
 FY 1996-97 through FY 1999-2000  
 (in millions)

	<u>FY 1996-97</u>	<u>FY 1997-98</u>	<u>FY 1998-99</u>	<u>FY 1999-2000</u>	Percentage Change In Period
Salaries and Fringe Benefits	\$6.4	\$ 7.3	\$ 8.7	\$ 9.0	40.6%
Research Grants and Services	0.8	1.2	1.2	1.7	112.5
Supplies	0.7	0.6	0.7	0.6	(14.3)
Other	<u>1.3</u>	<u>1.2</u>	<u>1.0</u>	<u>1.2</u>	(7.7)
Total	\$9.2	\$10.3	\$11.6	\$12.5	35.9

It should be noted that nonstatutory provisions in 1995 Wisconsin Act 27 required the Board of Regents to submit a report on savings resulting from the transfer of UWHC's operations to the Authority. The report indicated UW-Madison would save approximately \$175,600 each year in GPR that had previously been used to provide unreimbursed administrative, legal, human resources, and facilities planning and management services to UWHC. In 1996, the Joint Committee on Finance, using an estimate of higher savings, reduced the University's annual budget by \$237,700 and deleted 2.12 positions to reflect these savings.

Although we found general compliance with the terms of all agreements between the Authority and the Board of Regents, documentation for the amounts transferred from the Authority to UW-Madison could not be completely reconciled to the University's accounting records, and portions of the annual amounts to be transferred under the agreements are frequently provided after the year has been completed. However, officials of both the Authority and UW-Madison are generally satisfied with the terms of the agreements and the process for negotiating the annual adjustments, and they believe no significant changes are needed.

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## Relationships with Health Care-Related Entities

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In the early 1990s, officials of UW-Madison and UWHC believed that in order to compete in the health care market, UWHC needed to form networks with other health care-related entities, such as managed care organizations, in order to share information, financial support, and patients. At the time, officials believed these networks would provide educational opportunities to medical students and provide revenue to ensure UWHC's financial success.

While the Authority has relationships with a number of entities that operate under the name UW Health including approximately 50 outpatient clinics, it has not engaged in networking activities to the extent that was envisioned at the time of the restructuring because the Authority concluded that other strategies were more effective. Instead, it has used available bonding authority to engage in an aggressive building program to increase the size of its outpatient clinics. In addition, the UW Medical Foundation's acquisition of the 225-member Physicians Plus Medical Group, S.C., has made it unnecessary for the Authority to consider joint ventures with other physician providers.

### UW Health

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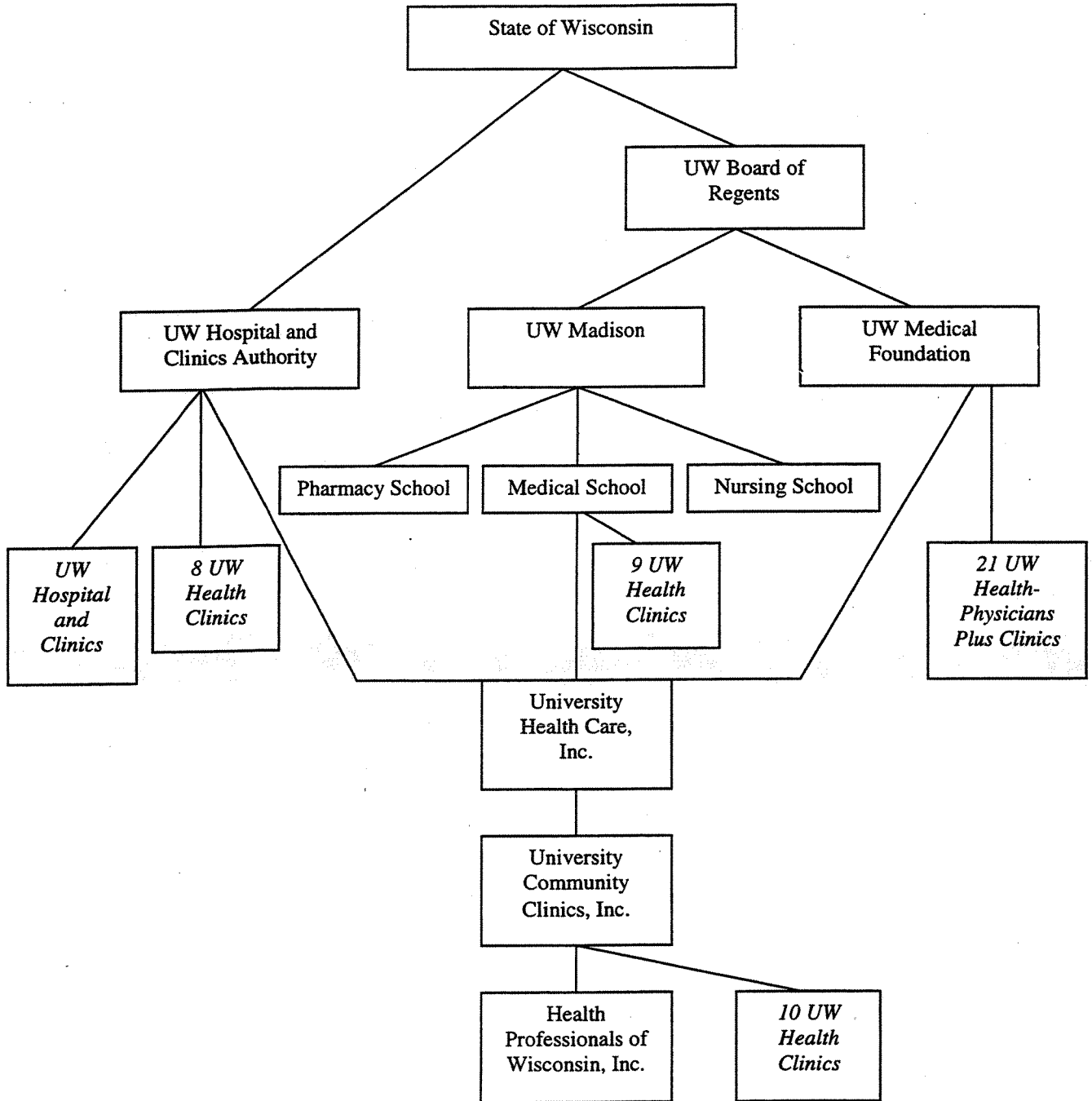
**The Authority and several other entities operate collaboratively as UW Health.**

The Authority and several other health-related entities collectively use the name UW Health for marketing and public relations purposes. UW Health is a registered trademark of the Board of Regents, which has granted the Authority and other participating parties a royalty-free license for its use. Figure 1 shows the current entities associated with UW Health and their organizational relationships with the State and the Board of Regents. These entities collaborate in the delivery of patient care and the pursuit of their educational and research missions. All of the outpatient clinics currently operating under the name UW Health are listed in Appendix 2.



Figure 1

Entities Associated with UW Health



UW Hospital, which is the 536-bed teaching hospital, and a number of clinics housed in the Clinical Sciences Center serve as the primary teaching facility for the UW Medical School, UW School of Nursing, and UW School of Pharmacy. In addition, the Authority is responsible for graduate medical education, which includes training approximately 440 residents each year. The 797 physicians who are members of the UW Medical School faculty serve as the medical staff at UW Hospital, outpatient clinics in the Clinical Sciences Center, and other clinics operated by the Authority. Medical faculty provide patient care and teaching services, and they conduct research.

### **UW Medical Foundation**

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**The UW Medical Foundation handles billing for all physician services.**

The UW Medical Foundation, whose creation in 1995 was authorized by the Board of Regents, is a nonprofit, tax-exempt foundation that operates as a medical education, research, and patient care organization. The UW Medical Foundation functions as the clinical practice plan for the member physicians, handling billing for all physician services provided to patients.

Before May 1995, each of 14 UW Medical School departments was responsible for providing financial support to the UW Medical School from its patient revenue, as well as for managing its own clinical practice. As a result, each department had a medical faculty practice plan to collect physician fees from patients and distribute them among member physicians. In May 1995, the Board of Regents and the UW Medical Foundation entered into an agreement to replace the 14 plans with 1 plan. Under this agreement, the UW Medical Foundation operates exclusively in support of the UW Medical School and contributes a portion of its annual patient revenue generated by medical faculty physicians to the UW Medical School.

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**The UW Medical Foundation paid the UW Medical School \$56.1 million in 1999.**

The agreement provides for three types of financial support to the UW Medical School:

- operating expenses, which are used primarily for faculty and support staff compensation that is not fully funded by UW-Madison;
- the medical school development fund, which is controlled by the dean of the UW Medical School and supplements state and federal appropriations; and

- the departmental research and development fund, which is controlled by departmental chairs and used by each department within the UW Medical School to support research and programmatic expenses.

As shown in Table 4, the UW Medical Foundation's support for the UW Medical School increased from \$36.5 million in 1997 to \$56.1 million in 1999, the most recent year for which data are available.

Table 4

**UW Medical Foundation Support for the UW Medical School**  
(in millions)

<u>Type of Support</u>	<u>1997</u>	<u>1998</u>	<u>1999</u>	<u>Percentage Change</u>
Operating Expenses	\$19.7	\$31.7	\$34.9	77.2%
Medical School Development Fund	11.5	12.8	14.1	22.6
Departmental Research and Development Fund	<u>5.3</u>	<u>6.4</u>	<u>7.1</u>	34.0
Total	\$36.5	\$50.9	\$56.1	53.7

In the mid-1990s, one of the trends in medical care was an increased emphasis on primary care. To increase revenue by expanding the number of physicians at the UW Medical Foundation, as well as to increase the number of primary care physicians available to teach at the UW Medical School, the UW Medical Foundation purchased the 225-member Physicians Plus Medical Group in February 1998. This purchase, which included all Physicians Plus clinics, made the UW Medical Foundation the largest medical group in the state and the eighth-largest in the nation.

**The UW Medical Foundation is attempting to have clinics it purchased exempted from local property taxes.**

Although the purchase of the Physicians Plus Medical Group was completed in 1998, the UW Medical Foundation has experienced operating and other difficulties with the merger, and Physicians Plus continues to operate as a separate division within the UW Medical Foundation. Currently, the UW Medical Foundation plans to integrate Physicians Plus fully by June 30, 2001, although whether it will be able to do so by that date is uncertain. The UW Medical Foundation has also filed a lawsuit in Dane County Circuit Court against nine communities in south-central Wisconsin over the tax status of the Physicians Plus Medical Group clinics it acquired in 1998. The UW Medical Foundation

is attempting to have the clinics removed from local property tax rolls, but the communities have refused. It should be noted that the Legislature's Joint Committee on Finance recently voted to make tax-exempt, beginning in January 2002, property owned by or leased to the UW Medical Foundation. Furthermore, like other UW Medical School physicians, the former Physicians Plus physicians are insured by the State against malpractice claims because they are considered faculty members of the UW Medical School.

### **University Health Care, Inc.**

University Health Care, Inc., and its related subsidiaries provide the main networking relationships of both the Authority and the UW Medical Foundation. University Health Care is a nonstock, nonprofit, tax-exempt corporation originally created in 1983 under the direction of the Board of Regents. Before the Authority was created, UWHC participated in networking activities with University Health Care and its subsidiary, Health Professionals, Inc. However, in 1994 (report 94-5), we found that UWHC and University Health Care were inappropriately using state funds to create a health care network. The Attorney General subsequently concluded in June 1994 that University Health Care's creation was improper because the Board of Regents did not follow statutory procedures; exercise final authority over University Health Care's operations; or impose minimum controls over University Health Care, such as compliance with open meetings and public records laws. Moreover, the Attorney General believed that the activities of Health Professionals, including its acquisition of medical practices, were not authorized or controlled by the Board of Regents. As a result, the Attorney General determined that it was improper for Health Professionals to receive public funds because the necessary accountability of those funds could not be assured. 1995 Wisconsin Act 27, which created the Authority, removed the legal impediments to UWHC's subsidizing, with hospital revenue, the activities of University Health Care and its subsidiaries, because this revenue was no longer considered state funds.

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**University Health Care negotiates health care contracts with insurers and others.**

University Health Care's board of directors currently consists of the Authority's chief executive officer, the UW Medical Foundation's president, the UW Medical School's dean and physician-in-chief, and University Health Care's president. University Health Care now fulfills two roles. First, because insurers, employers, and health maintenance organizations often prefer to negotiate health care contracts with one entity, University Health Care is under contract with the Authority and the UW Medical Foundation to act as their authorized agent in the negotiation of contracts for the provision of hospital and physician services. As of February 2001, University Health Care had entered into approximately 70 of these health-service contracts. Second, University Health Care assists in the development of a regional health care delivery

system. For example, it coordinates the schedules of UW Medical Foundation physicians who provide services at clinics located throughout the state.

### **University Community Clinics, Inc.**

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**University Community Clinics purchases and administers physician practices for UW Health.**

University Health Care's subsidiary, Health Professionals, was subsequently renamed University Community Clinics, Inc. This nonstock, nonprofit corporation purchases and develops local and regional physician practices for UW Health by acquiring, managing, and providing administrative services such as billing, recruitment, and management services. As of June 2001, University Community Clinics operated ten clinics in south-central Wisconsin. University Community Clinics is a partial owner, along with Blue Cross & Blue Shield United of Wisconsin, of Health Professionals of Wisconsin, Inc., a for-profit corporation. Health Professionals of Wisconsin owns the real estate of two University Community Clinics clinics. In 2000, University Community Clinics made \$78,120 in lease payments to Health Professionals of Wisconsin for these two clinics. University Community Clinics' board of directors includes University Health Care's board of directors, University Community Clinics' medical director, a member appointed by the UW Medical Foundation, and a physician employed by University Community Clinics.

The Authority and the UW Medical Foundation—but not the UW Medical School—provide financial support to University Health Care and University Community Clinics. Their contributions fund the administrative costs that University Health Care incurs during its negotiation of health care contracts, as well as those that University Community Clinics incurs during its acquisition of clinical practices. The debt that University Community Clinics incurred in acquiring clinics was a cumulative \$3.4 million in 2000.

The contributions are made through University Health Care, which annually requests funds from the Authority and the UW Medical Foundation on behalf of both itself and University Community Clinics. The Authority and the UW Medical Foundation provide the funds to University Health Care, which subsequently gives a portion to University Community Clinics. As a result, neither organization contributes directly to University Community Clinics. As shown in Table 5, support by the Authority and the UW Medical Foundation for University Health Care and University Community Clinics increased from \$5.3 million in FY 1996-97 to \$6.1 million in FY 1999-2000.

Table 5

**Support for University Health Care and University Community Clinics,  
by Source\***

	<u>FY 1996-97</u>	<u>FY 1997-98</u>	<u>FY 1998-99</u>	<u>FY 1999-2000</u>
<b>University Health Care:</b>				
Authority	\$ 785,417	\$1,087,300	\$1,087,300	\$1,087,300
UW Medical Foundation	<u>755,000</u>	<u>750,000</u>	<u>750,000</u>	<u>750,000</u>
Subtotal	1,540,417	1,837,300	1,837,300	1,837,300
<b>University Community Clinics:</b>				
Authority	2,063,759	3,100,000	3,100,000	3,100,000
UW Medical Foundation	<u>1,649,780</u>	<u>1,200,000</u>	<u>1,200,000</u>	<u>1,200,000</u>
Subtotal	<u>3,713,539</u>	<u>4,300,000</u>	<u>4,300,000</u>	<u>4,300,000</u>
Total	\$5,253,956	\$6,137,300	\$6,137,000	\$6,137,000

\* The UW Medical Foundation's fiscal year corresponds to the calendar year, while the Authority's fiscal year follows the State's.

As noted, the Authority's arrangements with University Health Care and University Community Clinics, including its financial contributions, are now permitted by statutes, and responsibility for managing and overseeing the two entities is shared by the Authority, UW Medical Foundation, and UW Medical School. In addition, UWHC entered into a joint venture in 1994 with Chartwell Midwest, an Illinois general partnership, to provide home infusion services, and the Authority has maintained this arrangement. However, the Authority has not exercised its networking authority to the extent permitted by, for example, entering into new arrangements with other health-related entities, such as joint ventures to provide home health care and long-term care for patients who no longer need hospital services but who cannot live independently.

**Issuance of Bonds**

Since its creation, the Authority has used its ability to issue bonds for any purpose, as provided by s. 233.20, Wis. Stats., to complete a number of projects, including construction of two outpatient clinics in Madison: UW Health-East, and UW Health-West. These projects allow

the Authority to serve additional patients, accommodate new physicians, and compete in the health care market with other providers.

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**The Authority has issued \$106.5 million in bonds to fund construction projects.**

1995 Wisconsin Act 27 limited the Authority to issuing \$50.0 million in bonds, but this limit was increased by \$56.5 million in 1999. As of March 2000, the Authority had issued bonds to its full limit of \$106.5 million. As noted, under its lease with the Board of Regents, the Authority is also responsible for debt service on all outstanding bonds issued by the State to finance construction of the Clinical Sciences Center. The debt service for all of these bonds is included in Appendix 3.

The Authority's bonds are not considered a debt of the State. Nevertheless, it should be noted that to help the Authority purchase bond insurance, the Board of Regents passed a resolution stating that it would not terminate the affiliation agreement or the lease unless the Authority substantially violated either agreement. Further, statutes indicate that in the event of the State terminating the agreements, adequate protection must be provided to the bondholders, which could mean assuming responsibility for any outstanding bond debt.

As shown in Table 6, the Authority used the proceeds from its April 1997 bond issue of \$50.0 million to complete seven projects worth \$54.6 million. Officials explained that they used interest from the bond proceeds and other income to fund the costs in excess of \$50.0 million.

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Table 6

**Projects Funded with April 1997 Bond Revenue**  
(in millions)

<u>Project</u>	<u>Cost</u>
UW Health-West Clinic (June 1999)	\$17.3
UW Health-East Clinic (November 1999)	15.4
Outpatient Treatment Center at Clinical Sciences Center	8.8
Purchase of University Station Clinic	6.9
Portion of Medical School Addition at Clinical Sciences Center	3.6
Linear Accelerator for Radiotherapy Department	0.8
Cardiac Intensive Care Unit at Clinical Sciences Center	0.7
Bond Issuance Costs	<u>1.1</u>
Total	\$54.6

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In March 2000, the Authority issued an additional \$56.5 million in bonds. As shown in Table 7, the Authority plans to fund several projects with the proceeds from this bond issue.

Table 7

**Estimated Cost of Projects to Be Funded  
with March 2000 Bond Revenue  
(in millions)**

<u>Project</u>	<u>Estimated Cost</u>
Expansion of Ambulatory Care Facilities at Clinical Sciences Center	\$24.4
Construction of Additional Operating Rooms at Clinical Sciences Center	17.6
Expansion of Pediatric Intensive Care Unit	5.9
Medical Flight Helicopter Relocation	3.7
Relocation and Equipment Costs of Projects	2.9
Bond Issuance Costs	<u>2.0</u>
<b>Total</b>	<b>\$56.5</b>

**Future Operations**

**The Healthstar initiative is a significant capital building project on the UW-Madison campus.**

All UW Health participants will benefit from a six-year Healthstar initiative, created in the State's 1997-99 capital budget, which was designed to improve health education at UW-Madison. The initiative includes three projects that will be located near the Clinical Sciences Center:

- the \$45.0 million Rennebohm School of Pharmacy building, funded by \$15.0 million in bonds that will be repaid with GPR and \$30.0 million in gifts and grants;
- the \$65.9 million Health Sciences Learning Center, including a library, distance education facilities, and other instructional space, funded by \$41.9 million in bonds that will be repaid with GPR, \$5.9 million in bonds that will be repaid by program revenue, and \$18.1 million in gifts and grants; and



- \$12.0 million for utilities associated with the initiative, funded by bonds that will be repaid with GPR.

University officials also indicate that the Healthstar initiative may eventually fund an interdisciplinary research complex that will conduct molecular, cancer, cardiovascular, and other research.

Authority and UW Medical Foundation officials indicate that restructuring and consolidation of operations of the various clinics owed by the partners in UW Health will be necessary in the future. They note that University Community Clinics' acquisitions, along with the UW Medical Foundation's purchase of the Physicians Plus Medical Group and its clinics, resulted in too many primary care clinics, including several with overlapping service areas. Therefore, University Community Clinics closed and consolidated four primary care clinics between 1999 and 2001, leaving it with eight primary care and two alcohol and drug treatment clinics. Authority officials have stated that University Community Clinics' \$3.4 million debt is being reduced by closing clinics, consolidating operations with Physicians Plus clinics, and implementing administrative changes such as reductions in clinic expenditures. They anticipate that the debt will be eliminated within two years.

Some UW-Madison officials believe greater integration and coordination is needed in managing UW Health clinics. Coordinating patient billing, admissions, and records, for example, would improve efficiency in the clinics' operations. In addition, these officials believe that patient service would be improved if appointment scheduling, admissions information, and other medical records were shared more efficiently when patients are referred among clinics or to UW Hospital, the 536-bed hospital operated by the Authority.

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**The Authority's strategic plan emphasizes coordination with the UW Medical School and the UW Medical Foundation.**

Improved coordination among the participants in UW Health is reflected in the Authority's updated strategic plan, which was adopted by its board of directors in April 2001. The plan emphasizes integration and coordination with the UW Medical School and the UW Medical Foundation and reflects all three organizations' goals. Strategies in the new plan include:

- aligning the strategic, operational, and organizational interests of the Authority, the UW Medical School, and the UW Medical Foundation to ensure a coordinated market approach, including integration of clinic facilities, patient registration and scheduling, and information services to limit duplication, as well as promotion of the UW Health name to minimize confusion regarding patient services;
- developing management and organizational structures to reinforce the Authority's commitment to high-quality customer service;
- adopting a position concerning the Authority's relationship with Meriter Hospital, the Madison hospital at which some Physicians Plus physicians practice, including initiating discussions regarding the need to improve communication and collaboration; and
- positioning the Authority as the preeminent regional referral source through the development of tertiary services in geriatrics, women's services, and children's services that focus on clinical programs in transplants, cardiology, oncology, neuroscience, and trauma-critical care.

These goals are similar to those articulated in the UW Medical School's 1998-2000 strategic plan, which identified efforts to integrate planning, management, and communication among the three primary members of UW Health: the Authority, the UW Medical School, and the UW Medical Foundation.

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