Shareholder Value and the Performance of a Large Nursing Home Chain

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Objective. To analyze corporate governance arrangements and quality and financial performance outcomes among large multi-facility nursing home corporations (chains) that pursue stakeholder value (profit maximization) strategies.

Study Design. To establish a foundation of knowledge about the focal phenomenon and processes, we conducted an historical (1993–2005) case study of one of the largest chains (Sun Helathcare Inc.) that triangulated qualitative and quantitative data sources.

Data Sources. Two main sets of information were compared: (1) corporate sources including Sun's Security Exchange Commission (SEC) Form 10-K annual reports, industry financial reports, and the business press; and (2) external sources including, legal documents, press reports, and publicly available California facility cost reports and quality data.

Principal Findings. Shareholder value was pursued at Sun through three inter-linked strategies: (1) rapid growth through debt-financed mergers; (2) labor cost constraint through low nurse staffing levels; and (3) a model of corporate governance that views sanctions for fraud and poor quality as a cost of business.

Conclusions. Study findings and evidence from other large nursing home chains underscore calls from the Institute of Medicine and other bodies for extended oversight of the corporate governance and performance of large nursing home chains.

Key Words. Nursing home chains, shareholder value, governance, performance, policy

During the 1990s, the U.S. nursing home industry was transformed by the growth of large, multifacility corporations (chains) through successive mergers (Kitchener and Harrington 2004). Management researchers heralded this process of nursing home “chaining” as an effective means of delivering efficiency and quality improvements in member facilities through techniques including standardization of services and knowledge transfer (Banaszak-Holl et al. 2002; Kamimura et al. 2007). In contrast, economic sociologists identify chaining as one of the managerial practices used by firms implementing the “shareholder value” concept of control which demands that corporate exec-

utives maximize profit for the benefit of stockholders, at the expense of all other goals (e.g., service quality) and constituencies such as consumers and employees (Fligstein 2001). While studies of shareholder value in many industries, including health care, report the limited success of practices such as merger and labor cost control, little is known about the ways that shareholder value has been pursued within individual health care corporations and the implications for financial and quality performance (Fligstein and Shin 2006).

This paper advances knowledge of the pursuit of shareholder value in health care by analyzing one managerial practice (the development of large chains) in an under-researched industry (nursing homes) considering both financial and quality performance measures. To build a foundation of knowledge about this process, we present an historical case analysis (1993–2005) of one of the largest nursing home chains: Sun Healthcare Group Inc. (henceforth Sun). The paper is structured in four main sections. We begin by locating the growth of nursing home chaining within the spread of shareholder value strategies and discuss some of the early indicators of governance and performance problems. We then explain our historical case design that involved triangulating national corporate data with information from external sources, and analyzing detailed quality and financial performance data for Sun facilities in California. In the third section, our findings show that at Sun, shareholder value was pursued using three interlinked managerial practices: (1) rapid growth through debt-financed mergers; (2) labor cost constraint though low nurse staffing levels; and (3) viewing sanctions for fraud and poor quality as a cost of business. These findings and evidence of similarities among other large nursing home chains are a matter of considerable public concern because the government pays for 71 percent of their revenues to serve many of the nation's most frail and vulnerable citizens (U.S. CMS 2003).

THE SHAREHOLDER VALUE CONCEPTION OF CORPORATE CONTROL

From the early 1980s, financial institutions (e.g., investment banks) grew frustrated with American industrial performance and encouraged publicly held

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corporations to adopt the “shareholder value” conception of corporate control (Davis and Stout 1992; Fligstein 2001; Zorn et al. 2005). Following economic agency theory (Jensen and Meckling 1976), the central tenet of shareholder value logic is that the relationship between financial markets, corporate boards, and managers requires that firms: (1) prioritize increasing returns on their assets in order to increase profits and stock prices for stockholders, and (2) subjugate all other goals (e.g., quality) and constituencies such as consumers and employees (Fligstein 2001). The imperative for managers and corporations to operate to this logic is reinforced through an incentive structure that includes both, penalties for nonconformance (e.g., boards firing managers and financial institutions facilitating hostile takeovers of firms with low stock prices) and rewards for compliance such as high managerial remuneration and continued corporate independence.

Through combinations of coercive and mimetic adoption of the shareholder value logic during the 1980s and 1990s, corporate executives increasingly viewed their firms in the same way as stock analysts would and implemented three managerial practices designed to appeal to financial institutions. First, because firms with lots of cash, little debt, and low stock prices became merger targets, corporations increasingly borrowed money to pay for acquisitions (Davis and Stout 1992). Second, attempts to constrain labor costs through lay-offs and low staffing levels were intensified (Hallock 1998). Third, creative financial ploys were used to bolster financial reports including stock buybacks and fictitious capital formation (Westphal and Zajac 2001; McLean and Elkind 2003).

SHAREHOLDER VALUE AND NURSING HOME CHAINING

Before 1965, the U.S. nursing home sector was, in large part, a cottage industry of local “mom and pop” providers (Kitchener and Harrington 2004). A key catalyst for corporate growth was the 1987 expansion of the Medicare nursing home benefit and the introduction of a cost-based reimbursement system that included payment for ancillary services such as therapies (Lehman Brothers 2004). While corporate chains emerged as a dominant organizational form in the nursing home field during the 1990s, less attention has been given to analyzing chain performance than has been given to comparing the performance of for-profit and nonprofit facilities, which has generally shown that for-profit nursing homes achieve lower costs and higher efficiency but that

nonprofit facilities produce higher quality care and more trustworthy governance (Schlesinger and Gray 2005).

Based on some early reports that nursing home chain facilities tended to have lower operating costs than independent facilities (e.g., Arling, Nordquisk, and Capitman 1987; McKay 1991), chains were promoted as a “rational” (value-free) means of pursuing goals including efficiency and access to capital through the stock market (e.g., Knox, Blankmeyer, and Stutzman 2001). One of the first U.S. studies to concentrate on the growth of nursing home chains in the 1990s provided four important insights (Banaszak-Holl et al. 2002). First, while the proportion of chain-owned facilities increased from 39 to 54 percent of the nation’s approximately 16,500 nursing homes, most chains were for-profit and relatively small, operating in one or a only a few states. Of the 4,770 chains identified in 1997, 89 percent had 2–10 homes, 8 percent had 11–50 homes, and only 2.6 percent had 51 or more homes (Banaszak-Holl et al. 2002). Second, nursing home chaining occurred primarily through 5,000 acquisitions and mergers of individual facilities or other chains (not new building). This occurred, in part, because many states restrict the growth of new nursing home beds. Third, some nursing home chains purchased low-quality facilities with the stated goal of “turning around” performance. Fourth, large national publicly held chains grew such that in 2001, the eight largest chains operated nearly 20 percent of all nursing home beds (see Table 1), and exerted considerable influence over the industry (Banaszak-Holl et al. 2002).

Table 1: Characteristics of the Eight Largest U.S. Nursing Home Chains, 2001

<i>Corporation</i>	<i>Nursing Home Beds</i>	<i>Total Facilities</i>	<i>% of Revenue from Government</i>	<i>Total Operating Revenue</i>	<i>CEO Compensation</i>
Beverly Enterprises	51,054	466	77	\$2.7 billion	\$3.6 million
Manor Care	41,613	299	61	\$2.7 billion	\$8.1 million
Kindred Health Care	39,293	305	79	\$3.1 billion*	\$12.8 million
Mariner	38,700	326	80	\$1.9 billion	\$1.3 million
Integrated Health Services	34,797	300	78	\$1.8 billion	NA
Life Centers of America	28,226	213	67	\$1.3 billion	NA
Sun	27,954	229	82	\$2.1 billion	NA
Genesis	25,821	240	61	\$2.6 billion	NA

*Schneider and O’Connor (2002) CEO compensation is total compensation e.g., including stock options.

Source: AHCA (2002):44 (U.S. operations only).

While the performance of large nursing home chains has rarely been addressed within academic research, it has attracted concern among policy makers and government officials (U.S. CMS 2003). In the late 1990s, as the nursing home industry received widespread criticism for intractable quality problems and low staffing (Institute of Medicine [IOM] 2001), one of the largest chains (Kindred) reached a \$1.3 billion settlement with the government for fraud and another (Beverly) had a corporate “monitor” imposed by the Department of Justice (Kitchener and Harrington 2004). Then, in 2000, five of the nation’s largest chains elected to operate under bankruptcy protection, involving 1,800 nursing homes (American Health Care Association [AHCA] 2002; U.S. CMS 2003).

Evidence that member units of bankrupt large chains operating in California did not report financial losses casts some doubt on the stated “necessity” for entire chains to enter bankruptcy, rather than selected operating divisions (Kitchener, O’Neill, and Harrington 2005). Although it is acknowledged that large chains suffered financially from the 1997 introduction of Medicare prospective payment system (PPS), the General Accounting Office (U.S. GAO) argued that Medicare PPS rates were “adequate,” and that the large chains’ bankruptcies stemmed from “poor” business strategies including rapid expansion and sizeable transactions with third parties (U.S. GAO 2000, 2002). It has also been reported that two common managerial practices among large nursing home chains in the 1990s were to acquire facilities with the goal of changing Medicaid beds into higher-revenue generating Medicare beds, and to adopt “creative” financing sources including the establishment of real estate investment trusts (REITS). These are separate corporate entities that own the land and/or buildings which are leased to nursing home corporations that are sometimes related companies (Lehman Brothers 2004).

METHODS

Study Design and Data Sources

This foundational study of shareholder value and the performance of a large nursing home chain used an historical (1993–2005) single case study to generate a basis of understanding (Pettigrew and Whipp 1991). Following best practices in case research, this study design systematically examined a set of specific research themes by triangulating the best available qualitative and quantitative data sources as part of a deliberate search for disconfirming

evidence (Sofaer 1999; Yin 1999). Two main sets of information were compared: (1) corporate sources including Sun's Security Exchange Commission (SEC) Form 10-K annual reports, industry financial reports, and business reports, and (2) external sources including, legal documents, press reports, and publicly available California facility cost reports and quality data. While the SEC 10-K reports are certified by corporate officials as being accurate, many amendments can be filed making it difficult to ensure that all data are captured and complete. The innovative nature of this study also required us to draw on material that is not published in peer-reviewed academic journals (e.g., business press reports). Where such material is reported here, all possible efforts were made to verify the information and contradictory data and interpretations are reported.

Case Selection

Sun was purposively selected for this study for a combination of empirical and pragmatic reasons. Of empirical concern, Sun presented an exemplar case of a large nursing home chain that pursued the shareholder value strategy of expanding through mergers, to become the second largest in chain 1998 (Vickery 2005). Pragmatically, the authors had access to public information on Sun at the national level as well as detailed financial and quality data on the chain's California facilities (called Sunbridge), which represented 8 percent of total free-standing facilities in California. The state data facilitated an in-depth examination of the chain performance, which could not be replicated in other states.

Research Themes and Data Sources

This historical case study of Sun concentrated on two organizational issues that have been under-researched in industry-level analyses of shareholder value: (1) approaches to corporate governance, and (2) financial and quality performance outcomes. Each issue (a research theme) is outlined in Table 2, which summarizes the indicators used (and rationale), and their sources. Although it would have been valuable to have interview data on corporate strategies, their collection was beyond the scope of this study.

Data Analysis

For the national-level quantitative data outlined in Table 2, descriptive statistics were computed for each of the indicators showing changes over time. For the California performance data, descriptive statistics were used to

Table 2: Research Themes, Indicators (Rationale), and Data Sources

<i>Research Themes</i>	<i>Indicators, Rationale</i>	<i>Analysis and Reporting</i>	<i>Data Sources</i>
Governance National and California	Organizational strategy, e.g., state goals, integrity agreement, and structure, e.g., numbers and mix of facilities/services, employees (Pettigrew and Whipp 1991)	Trends 1993–2005 (Table 2) and qualitative account	Securities and Exchange Commission Form 10-K reports (Sun 1996–2006); industry reports, news releases, newspaper reports; U.S. OIG (2001)
Financial performance National	(1) Revenue sources, (2) stock price, (3) P/E ratio, (4) total assets, (5) long-term debt, (6) net revenue, & (7) net earnings (Pettigrew and Whipp 1991)	Trends 1994–2005 (Table 3)	Securities and Exchange Commission Form 10-K reports (Healthcare Group Inc. 1996–2006)
California	Average care expenditures—direct, indirect, and total—per resident Sun versus CA average	Trends 2000–2003 (Figure 5)	California Cost reports (COSHPD 2000–2004)
Quality National	Federal Regulatory Oversight. The U.S. DOJ and the U.S. Office of the Inspector General instituted corporate oversight and corporate integrity agreements on Sun	Qualitative analysis	U.S. Office of Inspector General (OIG) (2001)
California	Complaints. Average substantiated complaints per facility per year Sun versus CA average (Harrington et al. 2004; Stevenson 2005)	Trends 2001–2003 (Table 4)	California automated certification and licensing administration information and management system (CDHS 2001–2004)

California (cont.)	Survey violations. Federal and state facility average: Sun versus CA (Harrington et al. 2004)	Trends 2000–2003 (Table 4)	California automated certification and licensing administration information and management system (CDHS 2001–2004)
	Staffing hours per resident day—RN, LVN and NA—Sun versus CA (IOM 2001; U.S. CMS 2001; Schnelle et al. 2004; Harrington 2005)	Trends 2000–2003 (Table 4)	California Office of Statewide Health Planning and Development (COSHDP 2000–2004)
	Nursing staff turnover (% of all nurses who left employment with the facility during the year. CA average versus Sun (Harrington and Swan 2003))	Trends 2000–2003 (Table 4)	(COSHDP 2001–2004)
	Enforcement actions against Sun	Qualitative analysis	Documents from California Bureau of Medi-Cal Fraud and Elder Abuse (BMFEA) actions against Sun (e.g., <i>California v. Sun Health Care Group Inc.</i> 2001, 2005)
	Consumer litigation against Sun (Johnson et al. 2004)	Qualitative analysis	Documents from California Advocates for Nursing Home Reform (2003) litigation action against Sun

compare Sun's facilities with all other free-standing nursing facilities for the period of 2000–2003 on five of the most commonly used outcome measures: complaints, quality violations, staffing levels, turnover rates, and financial performance. In addition, litigation and enforcement actions taken by the California State Attorney General were analyzed.

FINDINGS

The findings from this case analysis are presented in two main sections. The first provides an historical account of the national development of Sun that concentrates on its approach to corporate governance, and its financial and quality performance. The second section draws on recent financial and quality data from California to present a detailed analysis of performance at the state level.

THE NATIONAL DEVELOPMENT OF SUN

Sun Rise

In 1989, Sun was established by CEO Andrew Turner with seven facilities that housed 954 licensed beds in Washington and Connecticut. Initially, Sun pursued shareholder value using two main managerial practices: (1) debt-financed growth through mergers, and (2) the provision of fee-for-service therapies to postacute nursing home patients who were diverted away from hospitals after the introduction of the diagnostic-related group (DRG) payment system (Sun 1996a). As shown in Table 3, within 9 years, Sun's strategy of purchasing other firms produced a chain that employed 80,720 persons working in 397 nursing facilities that were owned, leased, or managed across 26 states facilities. Additionally, Sun had diversified to include 1,798 ancillary service firms (e.g., pharmacies, therapy providers, and staffing agencies) and 186 international facilities in countries including the United Kingdom and Australia (Table 3). Around Sun's peak in 1997–1998, its stock price of nearly \$17 indicated financial institutions' satisfaction that corporate assets of \$2.6 billion were financed by long-term debt of \$1.57 billion (Table 3).

Shareholder Value, National Governance, and Quality

From the early 1990s, Sun's model of corporate governance clearly reflected the shareholder value logic in two main ways. First, Sun challenged the

Table 3: Sun Healthcare Group Inc., Structure and Financial Summary, 1993–2005

	1994	1995	1997	1998	1999	2001	2003	2004	2005
Structure					<i>Bankruptcy</i>				
Nursing home facilities	55	131	321	397	346	229	215	98	134
Occupancy rate	NA	NA	NA	NA	91%	89.3%	90.1%	91%	87.3%
Other facilities*	0	0	8	39	31	18	18	16	21
Total beds	6,252	15,921	36,655	44,941	39,867	27,954	26,287	11,007	16,965
Ancillary services [†]	13	797	1,630	1,794	1,591	660	620	493	452
States	NA	16	26	26	27	25	25	14	19
Employees	NA	27,100	68,900	80,720	57,100	36,000	33,000	15,800	22,000
International facilities	0	53	163	186	178	0	0	0	0
National ranking on size [‡]	—	NA	NA	2nd	3rd	7th	9th	10th	6th
Finance									
Total assets (\$ millions)	NA	\$1,043	\$2,579	\$2,468	\$1,438	\$650	\$300	\$313	\$512
Net earnings/(loss) (\$millions)	NA	(\$24)	\$35	(\$754)	(\$1,089)	(\$69)	\$1,047	(\$19)	\$25
Long-term debt net of current portion (\$ millions)	NA	\$348	\$1,568	\$706	\$146	\$97	\$79	\$107	\$187
% Revenue from medicaid	NA	34%	NA	NA	46.7%	45.8%	49.4%	49.2%	47.1%
% Revenue from government [§]	NA	57%	NA	NA	66.7%	71.9%	77.6%	78.9%	78.2%
CEO salary, bonuses, and other compensation (\$ thousands) [¶]	\$794.6	\$600.7	\$6,040.6	\$659.6	\$700	\$4,904	\$1,468	\$1,953.5	\$2,260.4**
Average stock price ^{††}	\$19.97	\$16.63	\$16.75	\$16.81	\$1.13	\$0.05	\$1	\$9	\$6.60
Dividends ^{‡‡,§§}	NA	NA	NA	NA	—	—	—	0	0

*Other facilities include rehabilitation, mental health, and assistive living.

[†]Ancillary services include: rehabilitation therapy, pharmacy, and staffing.

[‡]Adler (1999). *Contemporary Long Term Care*. Vickery (2001–2006). Top 50 Nursing Home Chains, Provider.

[§]Net earnings or losses are the net revenues minus costs and expenses. Revenue sources include inpatient services in nursing homes and other long-term care facilities.

[¶]Government revenue includes Medicare and Medicaid.

^{||}Does not include stock and other compensation for the CEO from 1994 to 1998.

**In 2002.

^{††}In 2006.

^{‡‡}Stock Check. Provider. 1994–2005.

^{§§}*Reuters Investment News*.

Source: SEC Annual 10-K-A Reports Filed by Sun (Sun 1994–2006); NA, not available.

traditional “mom and pop” model of locally based nursing home care by growing through mergers. For this strategy, the business press portrayed Turner a hero who was impatient with the traditional approach to industry governance, which he derided as “lacking innovation” (Nakhnikian 2000, p. 4). Second, Turner’s desire to “cut redundancy and fat in the system” was reflected in low nurse staffing levels in the chain’s nursing homes (Odenwald 1996a, p. 15). Additionally, legal and regulatory actions over governance and poor quality were viewed as a normal component of Sun’s pursuit of shareholder value. In its 2005 annual report, for example, Sun explained multiple legal problems by stating:

We are a party to various legal actions and administrative proceedings and are subject to various claims arising in the ordinary course of our business, including claims that our services have resulted in injury or death to the residents of our facilities, claims relating to employment and commercial matters. . . . We operate in industries that are extensively regulated. As such, in the *ordinary course of business*, we are continuously subject to state and federal regulatory scrutiny, supervision and control . . . (Sun 2005, F-41 emphasis added)

As early as 1995, state survey agencies in Connecticut, Louisiana, Oregon, Texas, and Washington issued survey violations and decertification notices to a number of Sun facilities and investigations were undertaken by the Office of the Inspector General (OIG) for quality, fraud, and abuse (Sun 1996a). Following these problems, Sun entered into a corporate compliance program with the OIG in 1996 (Sun 2000). In 2001, after further quality problems, Sun entered into a new formal Corporate Integrity Agreement (CIA) with the OIG requiring the implementation of a comprehensive internal quality improvement program and a system of internal financial controls with external oversight (U.S. OIG 2001; Sun 2002: p. 14).¹ In addition to poor quality throughout the 1990s, Sun had multiple corporate governance lawsuits regarding false and misleading financial reporting and improper billing (Odenwald 1996b; Sun 1998a, 1999a). At the end of 1999, Sun’s insurance carriers declined to renew its general and professional liability insurance so that, in response, Sun established a self-funded insurance program (Sun 2000). In 2002, Sun reported that a “number” of litigation actions were still pending but it signed a settlement agreement with the Department of Justice in eight cases by paying \$1 million in cash and signing a promissory note for \$10 million, while three other cases were settled separately (Sun 2002).

Somewhat ironically, a number of shareholder lawsuits were also filed against Sun in the mid-1990s. In 1996, six civil class action complaints were

filed against Sun in New Mexico, alleging misrepresentation and failure to disclose material facts about the OIG investigation which artificially inflated the price of Sun's securities (Sun 1996a).² In 1997, Sun received court approval for a \$24 million settlement of certain class-action shareholder lawsuits, while other class action lawsuits were filed by shareholders alleging that Sun failed the impact that Medicare prospective payment would have on corporate operations (Sun 1998).

Shareholder Value and Bankruptcy

Over-burdened with debt, Sun's financial standing deteriorated to the extent that in October 1999, the chain filed for Chapter 11 bankruptcy protection in Delaware and suspended stock trading (Table 3). As with many of the larger national chains, Sun attributed its financial problems to a combination of external problems including: the low reimbursement rates of most state Medicaid programs, the imposition of the Medicare PPS for skilled nursing and therapy services that had previously been billed as fee-for-service, and a decline in the demand for the company's therapy services. (Sun 1999a, p. 6). Bankruptcy reorganization led to a changing of Sun's senior officers. In 2001, Richard Matros became Chair and CEO, all previous directors resigned, and four new directors were appointed to represent creditors (Sun 2002). Soon afterwards, Matros acknowledged previous internal (managerial) problems:

If you look at the companies in our business that didn't go into Chapter 11, they didn't grow in the same way, they didn't accumulate debt in the same way. They took the same hit on reimbursement that others did, but it didn't force them into Chapter 11 (Piotrowski 2002).

The new CEO's recovery strategy involved three main approaches that prioritized increasing shareholder value over quality improvements. The first involved stopping paying rent on 60 percent of the nursing homes that he intended to divest from (Killean 2004). The second stage involved trying to sell Sun's ancillary businesses to raise cash. While the institutional pharmacy business (Omnicare) was sold in 2003, an agreement to sell the rehabilitation business (20 percent of Sun's 2003 revenue) to the rival Beverly chain was reversed with the buyer's CEO citing "certain issues that arose during the due-diligence process" (Killean 2004). Matros articulated a third element of the corporation's strategy concerned the prioritization of cost control over quality:

Sun must, and will, continue to maintain its commitment of high quality patient care. But under these circumstances, Sun also must, and will, continue to make the

hard decisions required to maintain patient care while reducing costs wherever possible in light of the government's deep cuts in funding (Sun 2003, p. 1).

To operate these policies, Sun began a comprehensive restructuring program that included the elimination of more than 10,000 positions (Table 3). Sun emerged from bankruptcy in February 2002 after its reorganized business and consolidated financial statements were approved by the United States Bankruptcy Court (Sun 2002, 2003). However, in Sun's first quarter after bankruptcy the company defaulted on its bank financing after failing to report \$40 million of costs in 2001. In response, Sun divested another 134 facilities, secured \$56.2 million in private financing, got the "going concern" qualification lifted by the auditors, and was listed on NASDAQ in March 2003 (Killean 2004). Financially the corporation's position strengthened with net revenues of \$882 million, net earnings of \$25 million, and stock reaching \$14.30 in February 2004, before leveling at around \$8 (Stock Check 2005). However, no dividends were paid during the period of 2002–2006 (Reuters Stock Reports 2007).

Shareholder Value and Corporate Governance in California

Behind Sun's improving postbankruptcy financial performance, the performance of Sun in California (where Sun operated as Sunbridge) demonstrates continuing governance and performance concerns. As with the corporate chain, the number of California facilities declined dramatically, from 100 facilities at the end of 1997 to 18 facilities in 2003 (Sun 2005).

In common with the parent corporation, Sunbridge's governance and poor quality in California were reported from the early 1990s and the subject of consistent legal and regulatory action (CDHS 1994; U.S. GAO 1998). In 1998, a Sunbridge facility received a citation with a \$20,000 penalty for the hospitalization and death of a resident. Another citation with a \$10,000 penalty was issued against a Sunbridge facility for inadequate nursing care that led to the hospitalization of a resident with sepsis, pneumonia, and leg infection that resulted in amputation in 1999 (CDHS 2001). Sunbridge's quality problems in California intensified with an investigation at its facility in Burlingame. As a result of not having a functioning air conditioning system during a heat wave, three residents died and seven were hospitalized in 2000. After the California licensing and certification program (CDHS 2000a) issued 10 citations and 71 deficiencies for poor quality of care to the facility, Sunbridge pleaded no contest to a felony violation of elder abuse in an action brought by

the California Attorney General's Bureau of Medi-Cal Fraud and Elder Abuse (BMFEA) in 2001.

As a result of Sunbridge's problems at its Burlingame facility, the Attorney General began a more extensive investigation of the corporation's operations in California. In October 2001, the California Superior Court issued the state's first permanent injunction and final judgment (PIFJ) against a national chain for poor quality of care and elder abuse (*California v. Sun Healthcare Group Inc* 2001). Sun settled the state's civil complaint by agreeing to carry out all provisions of state and federal regulations governing quality of care and to comply with Sun's 2001 CIA with the U.S. OIG (*California v. Sun Healthcare Group* 2001).

Sunbridge's overall compliance with the 2001 permanent injunction was investigated by the California Attorney General's Office in 2004 and 2005, because the state licensing and certification program found extensive patient neglect and discovered serious, systemic problems in Sunbridge facilities including: false records, inadequate pressure ulcer care, dehydration, malnutrition, weight loss and patient safety, insufficient staffing, inadequate supervision, and a lack of staff training. In 2003, the Attorney General alleged the 2001 PIFJ had been violated. In January 2004, 12 Sunbridge employees at its Escondido-East facility were arraigned on criminal negligence charges for injury and harm to residents and on misdemeanor charges for falsifying paperwork with fraudulent intent (Sun 2004).

In September 2005, Sunbridge resolved the new allegations by the Attorney General by agreeing to a second Permanent Injunction and Final Judgment which involved requirements including: paying \$2.5 million for investigation costs and civil money penalties, agreeing to increase total nurse staffing to meet the state mandated 3.2 hours per resident day (hprd), and hiring a compliance officer and a wound care consultant (*California v. Sun Healthcare Group Inc.* 2005; Vanderwold 2006). In addition to the state actions concerning quality and governance, in 2003, a nonprofit consumer advocacy organization filed a lawsuit charging Sun with unlawful business practices, unfair and fraudulent business practices, and false advertising (*California Advocates for Nursing Home Reform v. Sun Healthcare Group Inc.* 2003). The lawsuit alleged that Sunbridge facilities in California were more than 1 million hours on aggregate below the state's 3.2 nursing hprd direct care requirement, which resulted in a savings of more than \$15 million by not meeting the staffing standard in 2000. The litigation was settled out of court in 2004 and the settlement results were not made public.

Shareholder Value: Quality and Financial Performance

Sun's nursing homes in California performed badly when judged by the standard measures of nursing home quality: complaints, survey violations, staffing levels, and staff turnover rates.

As shown in Table 4, even after the first permanent injunction was obtained by the state Attorney General in 2001, Sun facilities in California accumulated higher average numbers of substantiated complaints (i.e., investigated and confirmed) than other facilities in 2002 and 2003. Contrary to expectations of standard quality levels among chain facilities, the average number of complaints per Sun facility in California ranged from 22 to zero in 2003. Between 2000 and 2002, Sun facilities in California also attracted more federal and state survey violations than other facilities in the state and attracted more of the most serious violations awarded by both state and federal inspectors (Table 4). Sunbridge facilities had a total of 1,296 federal and state violations in 2000, 1,294 in 2001, and 1,362 in 2002 (CDHS 2004). As with complaints, there was a wide range in the number of violations in Sun nursing homes in California such that in 2002, one facility had 77 total deficiencies whereas another had only one.

Table 4 shows that Sunbridge nursing facility staffing levels were low compared with the average free-standing nursing facility for the years 2000–2002. In 2000, Sunbridge had a total of 2.71 hprd, 16 percent below the state's minimum requirement established for the year 2000 (3.2 hprd) and 34 percent below the (4.1 hprd) level recommended by experts (US CMS 2001; Schnelle et al. 2004). Even in 2003 when average total nurse staffing in Sun's California facilities met the state minimum, 23 percent of Sunbridge nursing homes still did not comply. Over the 4-year period, Sunbridge RN staffing was 20 percent lower than the California average and 63 percent lower than the 0.75 hprd recommended by experts (COSHPD 2004). Consistent with Sun's low staffing levels in 2000 and 2001, facilities in California reported a 95–98 percent average turnover rate that was nearly 20 percent higher than the state average (Table 4), although its turnover rates declined as Sun began to increase staffing and sell facilities in 2002–2003. Again, however, there was significant variation between facilities with one reporting a 284 percent turnover rate and another reporting 3 percent turnover.

In terms of financial performance, given evidence of Sunbridge's history of low staffing in its California nursing homes, it is not surprising that average daily facility expenditures were 18 percent lower than the state averages over the 4-year period from 2000 to 2003 (COSHPD 2004). Despite only just

Table 4: Facility Quality Performance, Sun and California Averages, 2000–2003

	2000			2001			2002			2003			2000–2003 Average		
	Sun	CA	NA	Sun	CA	NA	Sun	CA	NA	Sun	CA	NA	Sun	CA	NA
Substantiated complaints	NA	NA	NA	2.6	1.6	1.6	2.2	1.7	1.7	1.6	2	2.1	2.1	1.8	1.8
Survey violations															
State (serious)	4.29 (0.94)	3.36 (0.49)	5.69 (1.03)	5.69 (1.03)	3.93 (0.6)	6.58 (1.42)	4.17 (0.64)	2.91 (0.83)	2.97 (0.41)	4.87 (1.06)	3.61 (0.54)	3.61 (0.54)	4.87 (1.06)	3.61 (0.54)	3.61 (0.54)
Federal (serious)	15.7 (4.8)	11.5 (3.5)	14.2 (4.4)	14.2 (4.4)	12.1 (3.6)	14.4 (4.5)	11.2 (3.7)	6 (2.5)	9.1 (3.5)	12.58 (4.05)	10.98 (3.58)	10.98 (3.58)	12.58 (4.05)	10.98 (3.58)	10.98 (3.58)
Total (serious)	19.99 (5.74)	14.86 (3.99)	19.89 (5.43)	19.89 (5.43)	16.03 (4.2)	20.98 (5.92)	15.37 (4.34)	8.91 (3.33)	12.07 (3.91)	17.44 (5.11)	14.58 (4.11)	14.58 (4.11)	17.44 (5.11)	14.58 (4.11)	14.58 (4.11)
Staffing hours per resident day															
RN	0.29	0.36	0.3	0.3	0.35	0.28	0.35	0.27	0.33	0.28	0.35	0.35	0.28	0.35	0.35
LVN and NA	2.42	2.76	2.77	2.77	2.91	2.96	3.03	3.12	3.08	2.82	2.94	2.94	2.82	2.94	2.94
Total	2.71	3.12	3.07	3.07	3.26	3.24	3.38	3.39	3.41	3.1	3.29	3.29	3.1	3.29	3.29
Staff turnover (%)	95.1	78.6	98.4	98.4	79.2	49.3	70.9	51.5	64.4	73.58	73.28	73.28	73.58	73.28	73.28

Source: Authors' tabulations from California Department of Health Services (CDHS), Certification and Licensing Division, 2000–2004. Automated Certification and Licensing Administrative Information and Management System (ACLAIMS) Data. Sacramento, CA: CDHS.

having emerged from bankruptcy, Sunbridge facilities sent a total of \$30.8 million in 2001, and \$35.6 million in 2002 to Sun's corporate home office for administrative services and profits (COSHPD 2004). This represented 11–15.5 percent of total revenues in 2001 and 2002, respectively, ranging from 5 to 24 percent of individual facility revenues. Just as the national chain experienced a reduction in the proportion of revenue from (higher paying) private pay clients and became more reliant on government funds (Table 4), Medicaid revenues in California increased from 62 percent in 2000 to 73 percent in 2003, and income from private-pay and other sources declined from 30 percent in 2000 to only 17 percent in 2003 (no table shown) (COSHPD 2000–2004).

DISCUSSION AND CONCLUSION

This historical examination of the way that a large nursing homes chain has operated the shareholder value conception of control reports that Sun combined three main managerial practices: (1) rapid growth through debt-financed mergers; (2) labor cost constraint through low nurse staffing levels; and (3) viewing sanctions for poor quality and governance as a normal cost of business.

Rapid Growth through Mergers

As noted earlier, management researchers have heralded nursing home chaining as an effective means of delivering efficiency and quality improvements across member facilities (e.g., Banaszak-Holl et al. 2002). This study shows that although the stock price of Sun rose as it grew rapidly through mergers, this was financed by huge debt and did not achieve good (or standardized) quality performance. The chain's poor financial performance occurred even though member facilities were required to pay considerable annual sums to corporate headquarters.

Labor Cost Constraint

In line with shareholder value logic, Sun operated a policy of labor cost constraint that was realized through low nurse staffing, and staff reductions following bankruptcy. Our detailed examination of recent California data showed that even as the poor quality of care in Sun's facilities was sanctioned by corporate compliance agreements, Sun's nursing homes reported high

turnover rates (2000–2001) and low staffing levels, which were in many cases below the minimum level required by state law.

Sanctions as a Normal Cost of Business

The third managerial practice used in Sun's pursuit of shareholder value is to treat regulatory sanctions as normal costs of business (Sun 2005). Consistently from 1989, Sun had regulatory actions imposed by a number of states for poor quality of care as evidenced by regulatory violations (including many that jeopardized the health and safety of residents). Additionally, the corporate governance of Sun was sanctioned through governmental actions for fraud and improper billing, and shareholder legal actions for misrepresentation of its financial status and lack of disclosure. Although some of Sun's most problematic governance issues arose before bankruptcy, this study demonstrates that strong traces persist with, for example, the recent nonpayment of rent on leases, and failures to comply with mandated minimum staffing levels in California.

An alternative (managerial) explanation for our finding of Sun's persistent governance and quality problems would be that the parent corporation was unaware of the serious problems in some of its individual facilities and/or that it was not able to turn the facilities around and bring them into compliance. While the wide variations in quality among facilities reported here may indicate this, it contradicts managerial analysts' assertions concerning the capacity of managers to realize the stated goals of nursing home chaining such as efficiency and standardization (Banaszak-Holl et al. 2002). To some extent, this analysis of Sun may support economists' argument that the workings of the market ensured that Sun paid the price for its poor quality of care and governance issues. However, in contrast to the central prediction of the shareholder value logic (that poor performance results in hostile takeover), Sun maintained independence after restructuring under Chapter 11 bankruptcy protection.

Our analysis of the way that Sun responded to financial institutions' expectations that publicly traded nursing home chains adopt the shareholder value conception of control supplements larger-scale analyses of the ways that nursing home corporations have responded to other environmental changes (e.g., Medicare PPS) through managerial practices including: developing subacute and rehabilitation care services (Zinn et al. 2000; Zinn, Mor, and Gozalo 2007), exiting states with high litigation activity (e.g. Florida and Texas), concentrating on Medicare postacute care (Stevenson, Grabowski, and Coots

2006), and establishing facilities as limited liability corporations to protect themselves from litigation (Cody 2006). Those studies typically confer that the near future for larger publicly held nursing home chains seems relatively secure. There is, however, greater concern over the capacity of independent facilities to survive the pressures for corporate consolidation that are described in the paper.

It was noted earlier that other large chains have pursued similar stakeholder value management practices strategies to Sun and produced common outcomes such as bankruptcy, low staffing, poor quality, and sanctions for bad governance. Assessment of the extent to which the analysis presented in this paper is transferable beyond the case of Sun is, however, a question for future research (Yin 1999). If the analysis presented here does not hold across wider cases or if, at least, it falls short of being “transferable,” then researchers should try to identify intervening factors that explain the variation.

One major policy issue for government, which provides 71 percent of the revenues for large publicly traded nursing home chains, is how to safeguard residents and employees in a context that is dominated by the countervailing demands of the shareholder value concept of control. Although this study reported that Sun was subjected to considerable regulatory activity, our findings reiterate research evidence that limited agency resources and political will to enforce regulations continue to ensure ineffective government oversight of nursing homes (Harrington, Mullan, and Carrillo 2004). The relative success of the California Attorney General’s actions against Sunbridge suggests that focusing regulatory activity on chains at the state level may be an approach that other states might consider. Above all, this study underscores the imperative to collect, analyze, and publish enhanced governance and performance data on nursing homes, particularly large chains.

ACKNOWLEDGEMENT

We would like to thank Toby Edelman for her comments on an early draft of this paper.

NOTES

1. Interestingly, the problems that Sun had with the California Attorney General’s Office, which began in 2000, were not reported in annual SEC Form 10-K reports until 2003 (Sun 2003). In 2004, Sun reported that the State of California alleged

that the company violated its Permanent Injunction and Final Judgment with the California Attorney General and that employees of one facility were arraigned on criminal charges (Sun 2004).

2. Sun defined subacute care facilities as ones that provided a minimum of 4.5 nursing hours and 1 hour of therapy per patient day, for patients with medically complex conditions (Sun 1996, p. 9).

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