10 Key Issues in Health Care Facility Vendor Contracts

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Vendors often present hospital and health care facility general counsel offices with their "template" form agreement and tell facilities' general counsel offices that the form "is signed by all of our customers." Meanwhile, the facilities' executives are pressing to get the contract reviewed and signed quickly. Most vendor agreements, however, *are* negotiable and *should* be negotiated in order to better protect the interests of the facility.

This article sets forth strategies for negotiating some of the key provisions in a vendor contract which may be controversial between the vendor and facility. (Agreements for certain vendor contracts, such as software and IT services, and compliance auditing, have other key provisions which can be addressed in a separate article).

Limitations of Liability

Most vendor contracts contain a clause that limits the vendor's financial liability. Generally, these provisions disclaim any liability for consequential damages, lost profits, and other incidental damages. They also usually set a dollar amount (such as the fees paid to vendor over a set period of time) as the ceiling for any other liability under the contract.

The facility should request this clause be deleted in its entirety because the vendor has expertise in its services and should be responsible for any mistakes it makes (defects in its products, negligence, etc.). If the vendor is confident in its abilities, and is anxious to get a new client, the facility may be successful. If not, the facility should, at a minimum, seek to expand the "cap" on liability to be as high as possible, and limit the scope of this provision by including carve-outs for matters such as: (a) breaches of major ("mission critical") contract requirements; (b) breaches of confidentiality obligations; (c) intellectual property infringement; (d) matters covered by the vendor's required insurance; (e) negligence; and (f) willful misconduct. Also, if this limitation remains, it should be reciprocal and apply in favor of the facility too.

Indemnification

Ideally, the indemnification language should be broad, covering any damages/liabilities caused by the vendor and its agents and by their contract breaches. In addition, it should provide that, at the option of the facility: (a) the vendor must defend the facility in addition to indemnifying it; or (b) the vendor must reimburse the facility for the facility's costs of defense, as incurred, on an ongoing basis.

Further, any indemnification obligation is only as strong as the underlying credit-worthiness of the indemnifying vendor. Many times large vendors pitch a deal, but when the initial contract is presented to the facility, the vendor uses a small subsidiary or a local shell entity as the contracting entity. If so, the facility should insist that the entity pitching the services be the contracting party, or in the alternative, fully and unconditionally guaranty the indemnification (and all other obligations) under the contract.

If the vendor is asking the facility to indemnify it, the facility should assess whether, in light of the nature of the contract, such indemnification is overbroad or should be deleted. For example, if the vendor will manage an entire service line of the facility, the vendor may ask to be indemnified for damages arising from the management services, and may refuse to provide any indemnification to the facility. The vendor would argue that it is providing a "management team" and if the facility used its own managers/officers to run the service line, the facility would be responsible for damages arising from the conduct of its managers/officers.

The facility should respond that the vendor is in the business of providing management services, the facility should be entitled to rely on the experience and capabilities of the vendor, and the vendor should stand behind its reputation and experience. If the vendor insists on being indemnified by the facility and the facility desires to proceed, the scope of the indemnification in favor of the vendor should be narrow, and, *at a minimum*, contain carve outs for the vendor's acts that are in bad faith, fraudulent, grossly negligent, or constitute willful misconduct.

Term and Termination

The length of the contract term and whether there is a termination for convenience clause generally are negotiated business terms. Auto-renewal clauses provide some benefits, including avoiding potential regulatory compliance issues in certain instances, while fixed terms force the parties to renegotiate business terms upon expiration. With auto-renewals, however, either party usually can provide a without cause termination notice to end the arrangement or to trigger a re-negotiation. This is a double-edge sword; if the clause is reciprocal (and "goes both ways"), it can be good or bad depending on which party wants to continue on the same terms and which party wants to renegotiate. A facility should always have an alternative vendor lined up on acceptable terms before providing a termination notice.

Vendors may be averse to "termination for convenience" provisions, especially if they are making a significant investment in starting up the services to be provided under the agreement. In such case the facility may consider negotiating a long notice period (e.g., 120 or 180 days), or only

allowing the "out" after one year, 18 months, or the initial term. Another compromise approach is negotiating a defined penalty for early termination by the facility to help compensate the vendor for any initial investment. Keep in mind that usually (but not always) these provisions are reciprocal.

A provision should also specifically describe how the vendor must cooperate in transitioning to a replacement vendor upon termination, including any post-termination services and the cost thereof. Similarly, the facility should delete any restriction on its ability to contract with a competing vendor upon termination.

Expense Payments

Many times a vendor contract may require that certain of the vendor's expenses be paid by the facility. To protect the facility, any such provision should: (a) specify exactly which expenses will be reimbursed; (b) only cover actual out-of-pocket expenses, without any mark-up; (c) expressly not cover the vendor's "corporate overhead" (e.g., home office staff & expenses); (d) expressly not cover costs of subcontracting services the vendor is supposed to be providing (e.g. preparation of financial reports, etc.); (e) cover only non-luxury transportation and lodging; and (f) require that expenses over a certain threshold be consented to by the facility in advance in writing.

Assignment; Change of Control

More often than not, selecting a major vendor with which the facility wants to contract is a long process. Therefore, the facility should make sure that its efforts are not thwarted by an assignment, merger, business sale, or other event which allows a different vendor to take its place (including one the hospital deliberately did not select or would not select). An anti-assignment provision (which includes "change of control" events) will protect the facility in this regard. By the same token, the facility itself will want the flexibility to be able to assign its rights and obligations under the contract to an affiliate or a successor.

If this "double-standard" is not accepted by the vendor, then the facility may consider: (a) negotiating a list of parties to which the vendor may not assign the contract (i.e. vendors that work for competitors of the facility, or vendors with which the facility has had poor experience); or (b) having the ability to reject a vendor's successor that does not meet certain criteria, such as having (i) a similar reputation for quality service and (ii) the same or better financial wherewithal as the vendor.

Dispute Resolution

An entire article can be written on the pros and cons of mandatory arbitration provisions. But keep in mind that arbitration can also be costly and time consuming. If an arbitration clause is included, consider: (a) specifying that expedited arbitration rules will be followed or requiring specific time-frames for completion of the arbitration; (b) whether discovery will or will not be allowed; (c) carving out proceedings seeking injunctive relief; (d) the differences in the procedural rules of the arbitrating agency (e.g., AAA, JAMS, AHLA, etc.); (e) whether a prevailing party's costs be reimbursed by the non-prevailing party; and (f) requiring a ruling in favor of one party (to avoid the tendency of arbitrators to "split the baby").

Also consider requiring that disputes first be escalated to a designated senior decision-maker for each party, who are required to meet in person two or three times for a few hours in a 20-30 day period seeking to resolve the dispute in good faith.

Venue

Most vendor contracts set forth the venue most convenient for the vendor, which is sometimes inconvenient for the facility. The facility should demand that its local venue be specified in the contract because the facility is part of regulated industry and governed by local rules and regulations. If not accepted, then other options include: (a) a "cross venue" provision, which requires that the party initiating the claim file it in the other party's venue; (b) selecting a neutral venue that is equally inconvenient to both parties; or (c) being silent, in which case venue will be determined by the applicable state or federal rules.

Scope of Services and Performance Standards

Contracts must clearly set forth a detailed description of the services to be performed, the required timeframes for such services, required standards and milestones, response times for support or responding to complaints, and required written and in-person reports. This seems obvious, but all too often the business team of the facility chooses a vendor based upon "glossy" brochures, PowerPoint presentations, and verbal promises made to management at meetings. It is imperative that anything important in such representations and materials be incorporated into the text of the contract or be attached as exhibits thereto and expressly incorporated by reference. Otherwise, none of those representations are legally binding.

Also, carefully review the content in the attachments, schedules, and exhibits to the form of contract that the vendor provides. At times these "add-ons" can be comprehensive and contain new or inconsistent terms that supersede the contract terms, or "water down" protections to the facility that are contained in the body of the agreement.

Moreover, it is preferable to specify penalties for the failure to meet the important requirements and performance standards in the contract. Finally, vendor contracts should specify that large portions of the compensation due to the vendor are required to be paid only upon the vendor meeting one or more key performance metrics. Financial incentives are the best way to motivate achievement of the facility's objectives and the contract's requirements

On-Site Personnel

If the contract involves the placement of vendor personnel at the facility's premises, the contract should: (a) provide the facility an express right to require that certain employees/agents be removed and replaced by the vendor; (b) require that all such staff adhere to all of the policies, procedures, and codes of conduct of the facility (e.g., Health Insurance Portability and Accountability Act policies, compliance program, wearing identification, obtaining immunizations, etc.); and (c) prohibit the vendor from subcontracting its duties and responsibilities to others.

Privacy and Security Considerations

In an agreement where a vendor will have access to protected health information (PHI), a business associate agreement (BAA) must be signed. Vendors who regularly access or maintain PHI may insist on using their own form of BAA (and there could be a "battle of BAA forms," which could be the subject of yet another article). In short, facilities with some leverage should insist on their standard form BAA, and should ensure that such BAA's indemnification provision is consistent with the indemnification provision in the main vendor agreement. The facility should also restrict the vendor from storing any of the facility's data at, or allowing access thereto from, offshore locations. In this regard, the facility should also perform diligence on the vendor's overall cybersecurity processes and compliance.

Conclusion

While not an exhaustive list of provisions that should reviewed and negotiated before entering into a vendor contract, the foregoing topics are offered as a guide for negotiating major provisions that are either significant to the vendor relationship or tend to be overlooked in negotiating a vendor contract. In the end, a contract with a vendor should not only fulfill the facility's immediate needs, but do so in a manner that best protects the interests of the facility.

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