Complete Solutions for Healthcare Management

Fallbrook Healthcare District

FHD Board of Directors Approved

Contingency Plan

June 11, 2014

Project Background

- In 1998, Fallbrook Hospital Corporation (FHC) entered into a lease and operational agreement with Community Health Services (CHS), a for-profit hospital operating and management company based in Brentwood, Tennessee.
- At the termination of the Lease in 2028, FHC will transfer back to Fallbrook Healthcare District (FHD) all assets and liabilities associated with the Hospital facilities and related operations.
- In 2011, FHD Board members initiated the accumulation of a "lease termination contingency reserve." This reserve (The Contingency Reserve) balance stands at $9.7M as of June 30, 2013. The purpose of the reserve is to ensure that adequate funding is available to FHD should CHS terminate their obligations under the Lease.
- As part of its stewardship to the community the District's initial contingency planning effort was undertaken in-house in 2003-4. An updated Plan was created in 2007-2008 as part of a Strategic Planning process. In 2013, and mindful of recent trends in local market healthcare provider dynamics and the impending changes associated with the Affordable Care Act (ACA) and related California MediCal initiatives, the FHD Board has requested that the contingency plan (the Plan) be updated

HFS consultants

Goals & Objectives

The primary Plan's focus should be on putting in place the necessary measures to secure sufficient Hospital operational management and other required assets to maintain the availability of FHD healthcare resources to the community should the relationship with CHS be terminated.

The main objectives are:

1. Current financial position
2. An evaluation of the market for alternative facility operators and/or managers. Program specific cost reduction
3. The development of potential alternative operator relationship terms scenarios and the impact, or adequacy of Contingency Reserve funding given the needs under each scenario
4. An evaluation of alternative uses for what would become FHD Hospital facilities subsequent to Lease termination

Project Scope

Our scope of work includes the following four deliverables:

- Part I: Abbreviated market and financial analysis
- Part II: Evaluate the adequacy of the Contingency Reserve
- Part III: Analysis of the market for alternative facility operators/managers
- Part IV: Identification of alternative Hospital facilities' uses

HFS consultants

Part I – **Abbreviated Market and Financial Analysis**

- Market and demand analysis:
  - Service Area definition. **OSHPD data from the year ended June 2013 provides the basis for the definition of Fallbrook market area**.
  - Acute care use rate and market share analysis. **Based on OSHPD data related to all market area providers. Current market shares may differ due to the emergence of new market are providers such as LLU Murrieta and Temecula Valley Hospital.**
  - Demographic projections
  - Acute and other FHD services utilization projection

- Financial Analysis:
  - Historical Financial Performance. All historical financial data derived from OSHPD data.
  - Benchmark operational indicators (financial ratio and operational indicators analysis)
  - Projected five year income statement
  - Productivity Analysis

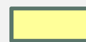
HFS consultants

Part I – Abbreviated Market and Financial Analysis: **Service Area**

patzip	Acute Disch	Percent	Cumul %
Primary Service Area			
92028	1,883	64.1%	64.1%
92592	215	7.3%	71.4%
92591	91	3.1%	74.5%
Total PSA	2,189	74.5%	
Secondary Service Area			
92088	79	2.7%	77.2%
92003	73	2.5%	79.7%
92563	67	2.3%	82.0%
92562	56	1.9%	83.9%
92590	14	0.5%	84.3%
Total SSA	289	9.8%	
Total TSA	2,478	84.3%	

Part I – Abbreviated Market and Financial Analysis: **Service Area**

Primary Service Area

 Secondary Service Area

HFS consultants

Part I – Abbreviated Market and Financial Analysis: **Acute Market Shares**

Total Service Area

Facility	Total Acute Discharges	Percent of Total
Southwest Healthcare System-Murrieta	8,960	40.7%
Fallbrook Hospital District	2,478	11.3%
Palomar Medical Center	1,112	5.0%
All Other Facilities	9,474	43.0%
Total	22,024	100.0%

Primary Service Area

Facility	Total Acute Discharges	Percent of Total
Southwest Healthcare System-Murrieta	3,886	32.4%
Fallbrook Hospital District	2,189	18.2%
Palomar Medical Center	817	6.8%
All Others	5,115	42.6%
Total	12,007	100.0%

Part I – Abbreviated Market and Financial Analysis: **SNF PSA Market Shares**

Total Service Area

Facility	Total SNF Discharges	Percent of Total
Fallbrook Hospital District	357	85.6%
Palomar Medical Center	35	8.4%
All Others	25	6.0%
Total	417	100.0%

Primary Service Area

Facility	SNF Disch	Percent of Total
Fallbrook Hospital District	322	92.3%
Palomar Medical Center	21	6.0%
All Others	6	1.7%
Total	349	100.0%

Part I – Abbreviated Market and Financial Analysis: **Population Growth**

Area	2000 Census	2013 Estimate	2018 Projection	Absolute Change	2013-18 Percent Change
Primary Service Area	110,618	165,856	178,482	12,626	7.6%
Secondary Service Area	61,352	135,696	149,222	13,526	10.0%
Total Service Area	171,970	301,552	327,704	26,152	8.7%
California	33,871,636	38,199,831	39,836,763	1,636,932	4.3%
United States	281,421,906	310,650,750	323,031,618	12,380,868	4.0%

Part I – Abbreviated Market and Financial Analysis
Population by Age

Area	2000	2013	2018	Absolute Change	2013-18 Percent Change
Primary Service Area					
Ages 0-17	34,691	45,666	46,986	1,320	2.9%
Ages 18-44	42,433	57,783	61,878	4,095	7.1%
Ages 45-64	22,020	43,788	47,819	4,031	9.2%
Ages 65+	11,474	18,619	21,799	3,180	17.1%
Total	110,618	165,856	178,482	12,626	7.6%
Females 15-44	23,841	27,231	29,049	1,818	6.7%
Secondary Service Area					
Ages 0-17	19,353	38,871	40,687	1,816	4.7%
Ages 18-44	22,876	49,058	53,278	4,220	8.6%
Ages 45-64	11,292	33,120	38,329	5,209	15.7%
Ages 65+	7,831	14,647	16,928	2,281	15.6%
Total	61,352	135,696	149,222	13,526	10.0%
Females 15-44	13,090	15,165	16,286	1,121	7.4%
Total Service Area					
Ages 0-17	54,044	84,537	87,673	3,136	3.7%
Ages 18-44	65,309	106,841	115,156	8,315	7.8%
Ages 45-64	33,312	76,908	86,148	9,240	12.0%
Ages 65+	19,305	33,266	38,727	5,461	16.4%
Total	171,970	301,552	327,704	26,152	8.7%
Females 15-44	36,931	42,395	45,335	2,940	6.9%

Part I – Abbreviated Market and Financial Analysis: **Historical Utilization**

	Historical Years Ended June 30,			
	2010	2011	2012	2013
Discharges:				
ICU	208	219	185	161
Med/Surg	1,885	1,819	1,709	1,569
OB	578	605	547	528
Total Acute	2,671	2,643	2,441	2,258
SNF	432	421	418	414
Total Discharges	3,103	3,064	2,859	2,672
Days:				
ICU	809	888	740	672
Med/Surg	5,472	5,267	4,621	4,402
OB	1,011	1,171	1,047	1,014
Total Acute	7,292	7,326	6,408	6,088
SNF	26,337	26,342	24,491	23,465
Total Days	33,629	33,668	30,899	29,553
ER Visits (OP)	9,411	9,411	9,009	10,363

Source: OSHPD "Hospital Annual Financial Disclosure Report" from appropriate timeframes.

HFS consultants

Part I – Abbreviated Market and Financial Analysis: **Historical Financial Performance**

	Historical Years Ended June 30,			
	2010	2011	2012	2013
Net patient services revenue:				
Inpatient	$ 26,988	$ 31,229	$ 27,513	$ 25,142
Outpatient	16,741	20,125	19,390	17,186
Provision for bad debts	(5,303)	(4,369)	(5,450)	(4,513)
Net patient service revenue	38,425	46,985	41,454	37,815
Other operating revenue	186	447	484	491
Total revenues	38,611	47,432	41,937	38,306
Expenses:				
Salaries	17,552	17,444	18,057	17,356
Benefits	5,944	6,190	5,968	6,044
Professional fees	1,676	1,809	1,566	2,474
Supplies	6,736	7,796	7,451	6,866
Purchased services	4,919	5,050	5,603	5,382
Other expense	1,774	2,987	3,644	3,958
Lease and rentals	1,549	1,026	1,050	1,062
Insurance	781	461	483	591
Depreciation and Amortization	1,192	1,902	1,975	2,219
Interest	1,278	5	6	10
Total expenses	43,401	44,670	45,804	45,961
Income from operations	(4,790)	2,762	(3,866)	(7,655)
Nonoperating revenue and expense:				
Investment income (loss)	(187)	(154)	(619)	(418)
Total non-operating revenue and expense	(187)	(154)	(619)	(418)
Excess/(Loss) of Revenues over Expenses	$ (4,977)	$ 2,608	$ (4,486)	$ (8,072)

Part I – Abbreviated Market and Financial Analysis: **Ratio Analysis (Based on 2013 historical results)**

	2013 Fallbrook	A	B	C	D	E	F	G
		Comparable Facilities						
Liquidity ratios:								
Current ratio	3.13	3.98	0.67	0.62	1.10	0.97	0.09	0.65
Days in receivable	56.45	123.67	66.55	48.87	105.93	60.80	58.72	61.65
Days in payables	23.42	24.85	48.89	12.74	119.68	43.63	5.65	35.23
Days unrestricted cash on hand	(0.05)	75.81	1.69	-	-	-	-	25.08
Profitability:								
Total margin	(0.21)	0.10	(0.02)	(0.06)	(0.02)	0.01	(0.21)	(0.04)
Operating margin	(0.20)	0.01	(0.02)	(0.06)	(0.05)	(0.03)	(0.21)	0.01
EBIDA margin	(0.14)	0.03	0.02	(0.05)	0.01	0.01	(0.16)	0.05
Return on assets	(0.18)	0.06	(0.03)	(0.31)	(0.03)	0.01	(0.26)	(0.04)
Return on equity	(2.40)	0.10	(0.47)	0.58	0.04	0.01	0.20	(0.14)

Source: Ratios computed by HFS based on information from the OSHPD "Hospital Annual Financial Disclosure Report" for each facility.

Part I – Abbreviated Market and Financial Analysis: **Ratio Analysis Definitions**

	Definition
Liquidity ratios:	
Current ratio	Current Assets/Current Liabilities
Days in receivable	AR, net/NPR (incl B. Debts)*365 days
Days in payables	AP/Oper exp less S&W, Ben, Depr, Amort*365 days
Days unrestricted cash on hand	Cash/Oper exp less Depr & Amort*365 days
Profitability:	
Total margin	Net Income/(Loss)/Total Oper revenue
Operating margin	Oper Income/(Loss)/Total Oper revenue
EBIDA margin	Oper Income/(Loss) less Int, Depr, Amort/Total Oper Rev
Return on assets	Net Income/(Loss)/Average Total Assets
Return on equity	Net Income/(Loss)/Unrestricted Net Assets

Part I – Abbreviated Market and Financial Analysis: **Fallbrook Staff Benchmarking**

- Comparison of Fallbrook operations with similar facilities in California indicate potential savings opportunities from adjustments to hospital staffing
  - All Fallbrook and benchmarked facility data derived from Office of Statewide Healthcare Planning Department (OSHPD)
  - Benchmarked facilities include:
    - Similar sized facilities
    - Similar service mix (i.e. acute vs. skilled nursing beds)

HFS consultants

Part I – Abbreviated Market and Financial Analysis: **Fallbrook Staff Benchmarking**

			FALLBROOK HOSPITAL DISTRICT 06/30/13 OSHPD Report					Fallbrook Hospital vs. Other SNF +/- 7,500 APD: Top Performance Thresholds			FTE Opportunity vs. Benchmarks			Annualized $ Opportunity vs. Benchmarks		
No.	**OSHPD Departments**	**Unit of Service Description**	**Unit of Service Count**	**Prod Hours**	**Avg. Hourly Rate**	**Prod FTE**	**Prod Hours per UOS**	**Best**	**2nd**	**3rd**	**Best**	**2nd**	**3rd**	**Top**	**2nd**	**3rd**
	DAILY HOSPITAL SERVICES															
1	MSurg Acute and Observation	Patient (Census) Days	4,402	49,048	$ 35.15	23.58	***11.14***	10.52	10.68	11.49	1.3	1.0	-	$ 95,654	$ 71,006	$ -
2	Medical/Surgical Intensive Care	Patient (Census) Days	672	23,379	$ 37.75	11.24	***34.79***	21.14	22.83	26.10	4.4	3.9	2.8	$ 346,207	$ 303,400	$ 220,559
3	Obstetrics, Labor & Delivery and Nursery	Patient (Census) Days	1,427	19,866	$ 40.79	9.55	***13.92***	16.02	20.73	-	-	-	9.6	$ -	$ -	$ 810,334
4	Skilled Nursing Care	Patient (Census) Days	23,465	88,112	$ 21.00	42.36	***3.76***	5.30	7.06	8.87	-	-	-	$ -	$ -	$ -
	AMBULATORY SERVICES															
5	Emergency Services	Visits	11,708	37,598	$ 36.36	18.08	***3.21***	2.07	2.87	3.73	6.4	1.9	-	$ 484,343	$ 145,105	$ -
	ANCILLARY SERVICES															
6	Clinical Lab & Blood Bank	Tests	94,198	27,760	$ 31.52	13.35	***0.29***	0.15	0.18	0.30	6.4	5.0	-	$ 421,382	$ 327,488	$ -
7	Surgery and Recovery Services	Operating Minutes	153,041	37,501	$ 38.76	18.03	***0.25***	0.16	0.21	0.22	6.3	2.2	2.2	$ 508,204	$ 180,495	$ 174,591
8	Cardiology Services	Procedures	9,991	4,470	$ 34.95	2.15	***0.45***	0.20	0.21	0.50	1.2	1.1	-	$ 85,417	$ 81,628	$ -
9	Rad Diag, MRI & CT Scan	Procedures	14,251	20,961	$ 34.73	10.08	***1.47***	0.97	1.21	1.59	3.4	1.8	-	$ 248,676	$ 129,955	$ -
10	Nuclear Medicine	Procedures	455	2,079	$ 43.96	1.00	***4.57***	0.88	2.28	-	0.8	0.5	1.0	$ 73,768	$ 45,783	$ 91,393
11	Ultrasonography	Procedures	3,172	5,166	$ 47.91	2.48	***1.63***	0.82	1.12	1.43	1.2	0.8	0.3	$ 123,210	$ 77,229	$ 30,836
12	Respiratory Therapy	Respiratory Therapy Adj. Inpatient Days	33,468	12,542	$ 32.17	6.03	***0.37***	0.12	0.56	0.66	4.0	-	-	$ 270,563	$ -	$ -
13	Physical and Occupational Therapy	Sessions	22,278	24,990	$ 43.17	12.01	***1.12***	0.58	0.78	0.79	5.8	3.7	3.5	$ 519,854	$ 330,094	$ 314,414
14	Speech-Language Pathology	Sessions	379	4,938	$ 41.14	2.37	***13.03***	0.26	0.32	-	2.3	2.3	2.4	$ 199,120	$ 198,157	$ 203,149
	GENERAL SERVICES															
15	Dietary and NonPtMeals	Patient Meals	116,825	36,684	$ 15.42	17.64	***0.31***	0.19	0.24	0.28	7.0	3.9	2.0	$ 222,954	$ 125,050	$ 64,322
16	Plant Ops & Maint	Gross Square Feet	78,513	10,566	$ 24.07	5.08	***0.13***	0.06	0.09	0.12	2.7	1.7	0.6	$ 135,822	$ 86,285	$ 28,162
17	Sterile Processing	Number of Surgeries	2,686	487	$ 14.62	0.23	***0.18***	1.50	3.39	7.50	-	-	-	$ -	$ -	$ -
18	Pharmacy	Pharmacy Adjusted Inpatient Days	43,154	13,514	$ 44.50	6.50	***0.31***	0.06	0.27	0.63	5.2	0.8	-	$ 484,074	$ 77,739	$ -
19	Purchasing and Stores	$1,000 of Gross Non-Capitalized Purchases that pass through the purchasing department	6,809	3,614	$ 26.22	1.74	***0.53***	1.14	1.24	1.32	-	-	-	$ -	$ -	$ -
20	Housekeeping	Square Feet Serviced	62,444	32,618	$ 11.72	15.68	***0.52***	0.16	0.22	0.32	10.7	9.0	6.1	$ 261,679	$ 218,933	$ 149,710
21	Data Processing	$1,000 of Gross Patient Revenue	206,784	4,448	$ 35.95	2.14	***0.02***	0.06	0.07	0.13	-	-	-	$ -	$ -	$ -
	FISCAL SERVICES															
22	Patient Acctg and Credit & Collections	$1,000 of Gross Patient Revenue	206,784	15,090	$ 23.74	7.25	***0.07***	0.00	0.16	0.18	6.9	-	-	$ 341,770	$ -	$ -
23	General Accounting	Hospital FTE Employees	307	5,313	$ 30.88	2.55	***17.31***	5.05	23.29	34.85	1.8	-	-	$ 116,206	$ -	$ -
24	Admitting	Admissions	2,602	25,554	$ 17.88	12.29	***9.82***	5.89	8.28	10.85	4.9	1.9	-	$ 182,670	$ 71,888	$ -
	ADMINISTRATIVE SERVICES															
25	Hospital Administration	Hospital FTE employees	307	11,719	$ 54.86	5.63	***38.17***	18.85	35.49	50.87	2.9	0.4	-	$ 325,385	$ 45,223	$ -
26	Public Relations	$1,000 of Total Operating Revenue	207,276	2,184	$ 37.32	1.05	***0.01***	0.01	0.01	0.01	0.1	-	-	$ 7,675	$ -	$ -
27	Personnel	Hospital FTE Employees	307	3,614	$ 36.21	1.74	***11.77***	14.75	21.60	25.17	-	-	-	$ -	$ -	$ -
28	Medical Records	Adjusted Patient Days	52,289	9,534	$ 25.06	4.58	***0.18***	0.16	0.28	0.54	0.5	-	-	$ 25,654	$ -	$ -
29	Medical Staff Administration	Physicians on Active Staff	75	1,766	$ 22.51	0.85	***23.55***	10.00	27.11	31.19	0.5	-	-	$ 22,870	$ -	$ -
30	Nursing Administration	Nursing Service FTE Personnel	85	14,927	$ 47.94	7.18	***175.61***	38.19	57.16	92.00	5.6	4.8	3.4	$ 559,971	$ 482,693	$ 340,710
31	Inservice Education - Nursing	Hours of Nursing Inservice Education	1,145	4,888	$ 33.28	2.35	***4.27***	0.84	1.23	1.34	1.9	1.7	1.6	$ 130,668	$ 115,963	$ 111,532
32	Utilization Management	Admissions	2,602	6,406	$ 30.09	3.08	***2.46***	2.83	3.75	4.39	-	-	-	$ -	$ -	$ -
						270					**94.4**	**48.5**	**35.4**	**$ 6,193,797**	**$ 3,114,114**	**$ 2,539,712**

Part II – **Evaluate Adequacy of Contingency Reserve**

Components of Contingency Reserve:

- Termination Assets
- Net Working Capital
- Cash Reserves
- Replacement of Operational Infrastructure

- Dollar range estimates of each component
- Potential exclusions from reserve estimates
- Additional funding requirements

HFS consultants

Part II - Evaluate Adequacy of Contingency Reserve: **Summary of Contingency Reserve Elements**

Contingency Reserve Elements:	Range	
	Low	High
Termination Assets*	$ -	$ 17,892
Net Working Capital	5,105	5,105
Cash Reserve	3,645	7,290
Replacement of operational Infrastructure	11,800	17,400
	$ 20,550	$ 47,687

* For the low range, repurchase liability dependent on the circumstances of early termination per the Lease.

HFS consultants

Part II - Evaluate Adequacy of Contingency Reserve: **Termination Assets**

	Ten Year Historical Trending of Fallbrook Property, Plant and Equipment (in thousands)									
	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013
Land*	$ 1,300	$ 1,300	$ 1,300	$ 1,300	$ 1,300	$ 1,300	$ 1,300	$ 1,300	$ 1,300	$ 1,300
Buildings and improvements*	5,378	5,344	5,471	6,578	6,675	20,101	20,106	20,040	19,967	20,153
Equipment	5,356	4,707	6,492	5,470	6,409	8,129	8,286	8,584	8,200	8,420
Accumulated depreciation	(4,945)	(4,133)	(5,706)	(6,066)	(6,784)	(8,150)	(9,161)	(10,487)	(10,067)	(11,995)
Construction in progress	397	341					-	150	431	14
Net PPE	$ 7,486	$ 7,559	$ 7,557	$ 7,282	$ 7,600	$21,380	$20,531	$19,587	$19,831	$17,892

* Lease does not require the District to "repurchase land/improvements" which it already owns and did not transfer title to FHC.

HFS consultants

Part II - Evaluate Adequacy of Contingency Reserve: **Net Working Capital**

Amounts as of June 30, 2013: (in thousands)

Assets:	
Patient accounts receivable, net	$ 5,848
Inventories	1,739
Prepaid expenses and other	(91)
	7,496
Liabilities:	
Accounts payable and accrued expenses	1,306
Employee compesation payable	1,085
	2,390
Net Working Capital Requirements	$ 5,105

Part II - Evaluate Adequacy of Contingency Reserve: **Cash Reserves**

	Actual FYE 2013
Total Operating Expenses	$ 45,961
Less: Depreciation and Amortization	(2,219)
Cash Related Expenses	$ 43,742
Reserve of Cash Related Expenses:	
1 month reserve	$ 3,645
2 month reserve	$ 7,290

Note: Amounts in thousands

HFS consultants

Part II - Evaluate Adequacy of Contingency Reserve: **Replacement of Operational Infrastructure**

	Range		Computation	
Replacement of operational Infrastructure:	Low	High	Low	High
Estimated Costs:				
Legal Fees	$ 200	$ 300	Estimate	Estimate
Other Consulting Fees	250	400	Estimate	Estimate
Funding of negative cash from operations	8,780	11,706	1.5 years	2 years
Ongoing capital expenditures	-	1,684	None	2 years of equip
Operational capital structure replacements:				
Patient Accounting - Outsourced	409	585	7% of AR, net	10% of AR, net
IT Start-Up Costs	500	1,000	Estimate	Estimate
Human Resources - Outsourced	1,446	1,446	One month payroll	One month payroll
Financial Reporting Start-Up Costs	200	300	Estimate	Estimate
Estimated Replacement Costs	$ 11,786	$ 17,422		

NOTE: Amounts in thousands and computated based on FYE 2013 financial results

Part II - Evaluate Adequacy of Contingency Reserve: **Ongoing Expenditures from Infrastructure Replacement**

- Ongoing outsourcing expenditures:
  - Patient Accounting
    - 7 to 10% of net patient revenue
  - Human Resources
    - 1.5 to 2.5% of payroll expenses
  - Financial Reporting
    - $300,000 to $500,000 annually

Part II - Evaluate Adequacy of Contingency Reserve:
Items Excluded from Reserve Analysis

- Potential adjustment for purchasing contracts
- Possible cash flow requirement to insurance contracts for change in operators
- No adjustments made for change in insurance contract rates
- Assumed purchase service contracts would continue with no significant expense change such as:
  - Housekeeping
  - Dietary
  - Laundry
  - Maintenance

HFS consultants

Parts I & II – Status Summary: **Where does this leave us?**

- Current hospital operations negative cash flow = $5.8M/yr.
- Operational enhancement opportunities exist. No ability to accurately quantify.
- Stand-alone status provides few market or strategic, or payor contracting advantages.
- Contingency reserve requirements exceed current District funding capacity.
- District ability to fund transitional cash requirements through proceeds of general obligation bonds (if proceeds could be used for such a purpose) is limited (see following debt capacity analysis)

District Debt Capacity Analysis – Estimate of Income Available for Debt Service

			2013
Property Tax Revenue		$	1,465,253
Expenses			964,233
Operating Income			501,020
Other Income			22,501
Add: Depreciation			1,657
Income Available for Debt Service		$	525,178
Debt Service Assuming Debt Service Coverage			
Requirements of:	1.25 x	$	420,142
	1.50 x	$	350,119

HFS consultants

District Debt Capacity Analysis – Estimate of Debt Capacity

Debt Capacity:

Coverage Requirement of		1.25
	Term	
Interest	20	30
4.50%	$ 5,465,186	$ 6,843,653
5.50%	$ 5,020,862	$ 6,106,243

Coverage Requirement of		1.50
	Term	
Interest	20	30
4.50%	$ 4,554,321	$ 5,703,044
5.50%	$ 4,184,052	$ 5,088,535

HFS consultants

Parts I & II – Status Summary:
What are our options?

- Negotiate with CHS to modify lease agreement and sustain /secure CHS presence
  - Shorten term;
  - Establish transition period terms and provisions;
  - Renew commitment regarding provision of core-serivces
- Seek new manager/lessee relationship
- Seek affiliation relationship with regional healthcare system/integrated provider
- Transition FHD into alternate provider

Part III - **Evaluation of market for alternate facility/service operators and managers**

- Identify key features of affiliation partners
- Compile information regarding most recent affiliations, operations, or management agreements
- Identify likely for-profit and non-profit affiliation candidates
- Outline of various affiliation, operating or management agreement structures

Part III – Market of Alternate Operators:
Key Features of Affiliation Partners

- Regional provider concentration.
  - Payor contracting leverage
- Long term commitment to region.
- Positioned to transition into integrated provider model (accountable care organization).
  - Provider network includes integrated (or ability to integrate) professional resources.
- Sufficient capital available to cover FHD cash requirements.

Part III – Market of Alternate Operators: **Affiliation Partners - What are they looking for?**

- Ability to re-direct patient volume to network tertiary providers and specialists (benefit from hub and spoke model)
- Opportunity to establish new market presence (i.e. expand brand name) and expand on underperforming provider market share
  - "Halo effect" impact on new affiliate acute provider operations
  - New market for establishment/expansion of physician provider network
- "Pick up" from overlay of Network contracts on new affiliate provider operations

Part III – Market of Alternate Operators: **Current Affiliation Examples – Exhibit A**

- Exhibit A – Desert Mtn. Pass District Hospital/San Bern Teaching Hospital Network
  - District Hospital leased assets to newly formed lessee entity comprised mostly of Teaching Hospital Network;
  - Primary upsides include:
    - Strategic benefit of professional network and ability to re-direct volume, enhance and secure District Hospital market share;
    - Enhanced payor contracting;

HFS consultants

Part III – Market of Alternate Operators: **Current Affiliation Examples – Exhibit B**

- Exhibit B – Central Valley Stand Alone District Hospital
  - Comparable in size and service mix (acute/SNF) to FHD
  - Licensed as Critical Access Hospital (CAH – therefore benefits from Medicare cost-based reimbursement)
  - Operating growing successful Rural Health Clinic (RHC)
  - Expanding Emergency Department volumes leading to ED renovation and overall facility face-lift
  - . . . Ability to sustain stand-alone operations = QUESTIONABLE

Part III – Market for Alternate Operators: **Potential Affiliation Partners (1)**

- Universal Health Systems
  - Currently operates:
    - Corona Regional Medical Center
    - Inland Valley Medical Center (Wildomar)
    - Rancho Springs Medical Center (Murrieta)
    - Temecula Valley Hospital (opened Fall 2013)
    - Surgery Center of the Temecula Valley (SCTV)
  - Facilities all owned (except joint ventured SCTV)
  - Strength of physician/professional component of integrated network = unknown

Part III – Market of Alternate Operators: **Potential Affiliation Partners (2)**

- Loma Linda University Medical Center
  - Currently Operates:
    - LLUMC
    - LLU Children's Hospital
    - LL Behavioral Medicine Center
    - LL Heart & Surgical Hospital
    - LLU Murrieta
    - Expanding private physician network + LLU Faculty Medical Group

Part III – Market of Alternate Operators:
Potential Affiliation Partners (3)

- Scripps Health
  - Currently Operates:
    - Scripps Green Hospital
    - Scripps Memorial Hospital Encinitas
    - Scripps Memorial Hospital La Jolla
    - Scripps Mercy Hospital
    - Scripps Clinic
    - Scripps Coastal Medical Center (Series of 9 integrated professional and ancillary service providers)
    - Specialty Centers (including 7 specialty imaging and other specialty service providers)

Part III – Market of Alternate Operators: **Potential Affiliation Partners (4)**

- Other potential affiliation partners:
  - Tri-City Medical Center
  - Palomar Medical Center
  - UC San Diego Health System
  - Sharp Health System

Part III – Market of Alternate Operators: **Potential Affiliation Structures**

- Asset Purchase – Buyer would purchase tangible assets (termination assets) from FHD (or directly from CHS) under terms of asset purchase agreement
- Lease Agreement – Lessee would operate hospital under terms of lease agreement similar to current CHS lease.
- Management Agreement – manager would provide executive management, financial reporting and other "ala carte" services to support hospital operations in return for a management fee.
- Hybrid – combination of two or more of above may be necessary to facilitate operational and asset transfer.
- Consolidated License – a hospital in close proximity of Fallbrook could consolidate licenses.

Part III – Market of Alternate Operators: **Advantages of Consolidated License Structure**

- Single Ownership
- Single License
- Single Medical Staff
- Essential Clinical Services can be dispersed between two facilities (greater operational efficiencies)
- Elimination of duplicate overhead (e.g. one H/R department instead of two)
- May be other synergies (reimbursement, strategic, contracting, physician strategies, etc.)

Part IV - **Evaluate Alternative FHD Facilities' Healthcare Uses**

- Identify community healthcare service needs;
- Evaluation of structural options for alternate facility uses

Part IV - Alternative FHD Facilities' Healthcare Uses: **Community Healthcare Needs**

- Fallbrook Healthcare District is located in Census Tract 018904, San Diego County and is not considered to be outside an urbanized area
  - Can not be considered for Critical Access Hospital
  - Can not be considered for Swing Beds
- Bed configuration (total 140 beds)
  - 47 licensed general acute care beds (4 perinatal, 4 ICU, 4CCU, 35 med/surg)
  - 93 licensed skilled nursing beds (6 beds de-licensed in 2002)
    - According to CDPH only 91 are certified

Part IV - Alternative FHD Facilities' Healthcare Uses: **Community Healthcare Needs**

- Fallbrook is an unincorporated community in northern San Diego County California
- Fallbrook is an unincorporated community in northern San Diego County, California. The Fallbrook census-designated place (CDP) population was **30,534** at the 2010 census, up from **29,100** at the 2000 census.
  - Fallbrook median age is 34.7 years & median income is $54,282
- Fallbrook is known for its avocado groves and claims the title "Avocado Capital of the World.“
- Fallbrook is 6 miles west of Interstate 15 or 5 miles north of State Route 76

HFS consultants

Part IV - Alternative FHD Facilities' Healthcare Uses: **Current Healthcare Services**

- Fallbrook Healthcare District only general acute care facility
  - Closest alternate hospital is Temecula Valley Hospital at 13.6 miles and Tri-City Healthcare District at 17.3 miles. These distances were derived from Google Maps using the respective facilities' street addresses. (Mileage measures differ depending on the source (Google Maps vs Mapquest, etc.). Pursuit of joint license or other affiliation strategies that will depend on distances between providers will need to be prefaced by a formal establishment of mileage and approval by appropriate governmental agency)
- Fallbrook Skilled Nursing Facility
  - Hospital Based and census of 58 during last survey
- Home Health Agencies
  - One home health and hospice
  - One home health and infusion service
- Retirement Communities
  - One with independent and assisted living with memory care
  - One with independent and assisted living
- Clinics
  - Three health centers, one with urgent care
  - One behavioral health clinic

Part IV - Alternative FHD Facilities' Healthcare Uses: **Current Healthcare Services**

Hospital Status with Seismic Safety as of 9/30/2013

County Code	Facility Name	City	Building Nbr	Building Name	Building Status	SPC Rating	2007 Hazus Score (%)	2010 Hazus Score (%)	OSHPD NPC Rating	SB499 Item 2 Ext. Status
37- San Diego	Fallbrook Hospital District	Fallbrook	BLD-02092	Main Hospital	Completed	2	0.42		1	In Review
37- San Diego	Fallbrook Hospital District	Fallbrook	BLD-02093	Med/Surg Addition	Completed	2	0.14		1	In Review
37- San Diego	Fallbrook Hospital District	Fallbrook	BLD-02094	ICU/CCU	Completed	2	0.03		1	In Review
37- San Diego	Fallbrook Hospital District	Fallbrook	BLD-02095	ER Addition	Completed	4			1	In Review
37- San Diego	Fallbrook Hospital District	Fallbrook	BLD-02096	Perinatal Addition	Completed	4s*			1	In Review

*Provided by self report- not verified by OSHPD

FHD used HAZARDS U.S. (HAZUS), a state-of-the-art methodology, to re-assess the seismic risk of SPC-1 buildings. Buildings that are determined to pose a low seismic risk may be reclassified to SPC-2. Two structures were reclassified from 1 to 2. The SPC-2 buildings would have until 2030 to comply with the structural seismic safety standards. Rating 4 is a replace also, with the transferal of some or all the acute services to SPC-4 buildings

Part IV - Alternative FHD Facilities' Healthcare Uses: **Inpatient Rehabilitation Facility (IRF)**

- Requirements for Inpatient Rehabilitation Facility
  - Licensed as a General Acute Care Hospital
  - All patient rooms and multipurpose rooms must be ADA
    - FHD rooms do not meet this requirement, would require extensive renovation
  - Need for a physiatrist to oversee the program
    - Do not know if there are available physicians

Part IV - Alternative FHD Facilities' Healthcare Uses: **Inpatient Rehabilitation Facility (IRF)**

- Pros
  - Considered a specialty hospital and do not need surgery or emergency services
- Cons
  - Renovation costs for ADA would be prohibitive
  - Ability of procuring a physiatrist to act as medical director is unknown
- Conclusion
  - Not a viable alternative

Part IV - Alternative FHD Facilities' Healthcare Uses: **Inpatient Psychiatric Facility (IPF)**

- Requirements for Inpatient Psychiatric Facility (IPF)
  - Licensed as a General Acute Care Hospital
  - All patient rooms and multipurpose rooms must be safe from potential harm
    - Need for renovation of windows, hardware, and need for seclusion
  - Need to recruit and sustain psychiatric medical staff and related support providers

Part IV - Alternative FHD Facilities' Healthcare Uses: **Inpatient Psychiatric Facility (IPF)**

- Pros
  - Considered a psychiatric hospital and basic services do not require surgery or emergency services
- Cons
  - Current IPF's located in Murietta (13 miles) and Oceanside (12.8 miles)
  - Renovation costs for safety requirements would be prohibitive
  - Ability to attract psychiatrists is unknown
- Conclusion
  - Not a viable alternative

Part IV - Alternative FHD Facilities' Healthcare Uses: **Long-Term Care Hospital (LTCH)**

- Requirements for Long Term Care Hospital
  - Licensed as a General Acute Care Hospital
  - Must show an average length of stay of greater than 25 days for a period of six months
    - Will need revenue sources to fund during this time (Prospective Payment System – PPS - as basis for Medicare payment only)
  - Will need to have in wall suction/gases and electrical amperes to handle as many as 25-30 ventilators
  - Will need to have a pulmonologist to oversee the program
    - Do not know if there are available physicians

Part IV - Alternative FHD Facilities' Healthcare Uses: **Long-Term Care Hospital (LTCH)**

- Pros
  - There are no LTCH services outside of San Diego primary area
- Cons
  - Renovation costs for service provisions would be prohibitive
  - Must operate for at least 6 months as a PPS/General Acute Care Hospital (GACH) with an Average Length of Stay (ALOS) of 25+ days
  - Ability to attract pulmonologists having the capacity to provide necessary coverage services is unknown
- Conclusion
  - Not a viable alternative

Part IV - Alternative FHD Facilities' Healthcare Uses: **Distinct Part Nursing Facility (DPNF)**

- Requirements for DPNF
  - County or District Hospital
    - Governmental entities can operate existing facilities as DPNF of their existing facility.   No requirement for the DPNF to be physically connected to hospital)
    - Would not have to meet seismic conditions
    - DPNF advantage is higher reimbursement limits than freestanding facility
  - Non-governmental Hospital
    - Not an alternative since acute and long term care services have to be attached within same physical structures

Part IV - Alternative FHD Facilities' Healthcare Uses: **Distinct Part Nursing Facility (DPNF)**

- Pros
  - Do not need to meet seismic requirements
  - Medi-Cal rates are at a higher reimbursement level than freestanding
  - Do not need to be physically attached to the acute district hospital
- Cons
  - Would need to keep some acute care beds within the district

Part IV - Alternative FHD Facilities' Healthcare Uses: **Freestanding Emergency Department (FED)**

- Requirements for Freestanding Emergency Department
  - California State law indirectly prohibits FEDs through its strict requirements for emergency facilities.
  - An exception to State law provides for the operation of a potential look-alike FED for urgent/emergency care in rural areas when the local EMS agency approves such operation.
  - Four facilities have been approved under this exception.
  - The facilities are essentially urgent care centers that are allowed to accept emergency patients.
  - None of the facilities advertise themselves as "emergency centers" and none are open 24/7.
  - All bill the emergency visits as outpatient clinic visits (much lower reimbursement).

Part IV - Alternative FHD Facilities' Healthcare Uses: **Freestanding Emergency Department (FED)**

- Pros
  - Would maintain a minimal level of emergency services locally
- Cons
  - Requires coordination with other facilities for inpatient admissions
  - Probable low reimbursement
- Fiscal Impact
  - Would probably operate at a loss
- Conclusion
  - Not recommended

Part IV - Alternative FHD Facilities' Healthcare Uses: **Rural Health Clinic (RHC)**

- Requirements for Rural Health Clinics:
- The following two requirements are necessary to establish a new rural health clinic:
  - Non-Urbanized as defined by the Census Bureau
  - The clinic has to be located in an area that is designated as either a health professional shortage area (HPSA) or a medically underserved area (MUA)
- Fallbrook is listed as urbanized as defined by the Census Bureau and therefore, not eligible for this program.

Part IV - Alternative FHD Facilities' Healthcare Uses: **Federally Qualified Health Center (FQHC)**

- Requirements for Federally Qualified Health Centers
  - 9 to 25 member board with 51% of them being patients
  - Located in a medically underserved area or medically underserved population
  - Licensed as a community clinic
  - Needs based formula to determine whether application warrants this federal designation
    - Number of FQHC's and number of low income patients being served in the area

HFS consultants

Part IV - Alternative FHD Facilities' Healthcare Uses: **Federally Qualified Health Center (FQHC)**

- Pros
  - Cost based reimbursement for primary care services
- Cons
  - Public board requirements of 51% of the board being patients
  - One year application process
- Fiscal Impact
  - Difficult to determine at this point
- Conclusion
  - There is one FQHC already in Fallbrook serving the low income population. This would be a barrier for another applicant to get approval for a FQHC.

HFS consultants

Part IV - Alternative FHD Facilities' Healthcare Uses: **Home Health Agency (HHA)**

- Home Health agency
  - There are currently two Home Health Agencies in the community of 30,000 residents.
    - The number of agencies continues to increase, with more than 420 new agencies and almost 11,900 total agencies in 2011. Most new agencies are concentrated in a few states (Texas, California, Florida, Illinois). Most of the growth has been in for-profit agencies.
    - The number of agencies per 10,000 fee-for-service (FFS) beneficiaries has risen 57 percent from 2.1 to 3.3

HFS consultants

Part IV - Alternative FHD Facilities' Healthcare Uses: **Home Health Agency (HHA)**

- Pros
  - No hospital-based HHA in district
- Cons
  - Area already saturated with HHA's
- Fiscal Impact
  - May represent small revenue generating opportunity
- Conclusion
  - Worthy of further evaluation although does not represent a solution to overall problems

Part IV - Alternative FHD Facilities' Healthcare Uses: **Swing Beds**

- Swing beds
  - Fallbrook is not eligible for Swing Beds as it is considered urbanized as defined by the Census Bureau. Swing bed eligibility requires that the Hospital is located in a non-urbanized area as defined by the Census Bureau. Both the rural health clinic and swing bed programs use this same exact Census Bureau definition to determine program eligibility.

HFS consultants

Part IV - Part IV - Alternative FHD Facilities' Healthcare Uses: **– Freestanding Skilled Nursing Facility**

- Requirements for Freestanding Skilled Nursing Facilities
  - Fallbrook currently has its own skilled nursing facility which is only at approximately 62% occupancy
    - In order to add additional beds in the community, the census should remain at least 90% occupancy

Part IV - Alternative FHD Facilities' Healthcare Uses: **Freestanding Skilled Nursing Facility**

- Pros
  - Would not need to staff at acute standards, only SNF ratios
- Cons
  - Not enough demand to support additional SNF beds
  - Reimbursement less in freestandng SNF than in DPNF
- Fiscal Impact
  - The cost of the services would exceed the revenues received
- Conclusion
  - Not a viable alternative

Part IV - Alternative FHD Facilities' Healthcare Uses: **Ambulatory Surgery Center**

- Requirements for Ambulatory Surgery Center
  - District would find it necessary to lease to separate ASC entity (ASC entity most likely physician/surgeon owned)
  - As such operating rooms would have to be separately licensed (separate entrance and patient exit)
- May represent physician investment opportunity, although many freestanding ASCs already exist

HFS consultants

Part IV - Alternative FHD Facilities' Healthcare Uses: **Ambulatory Surgery Center**

- Pros
  - May represent opportunity for District to generate rental income from leasing operating rooms to separate Joint Ventured ASC entity
- Cons
  - Stiff competition from several other already existing ASCs
  - JV entity formation, marketing and development generally time consuming
  - Risk of JV entity disintegrating (for variety of reasons)
- Fiscal Impact – marginal given competitive market for ASC facilities
- Conclusion – not likely to represent significant opportunity

Part IV - Alternative FHD Facilities' Healthcare Uses: **Freestanding Dialysis Center**

- Requirements for a Freestanding Dialysis Center
  - Freestanding clinic would require separate licensure
  - In excess of 90% of services reimbursed by Medicare (Medicare responsible for all End Stage Renal Disease – ESRD – patients)
  - Third party operated clinic (i.e. through DaVita, etc.) would be structured as lease with hospital as lessor/service provider
  - Most clinics operate roughly 25 dialysis stations and require approximately 15,000 vists/year for breakeven
  - Requires nephrologist to perform medical directorship and clinical oversight
  - Breakeven volume typically generated as a function of referral relationships with at least 3 established nephrologists

Part IV - Alternative FHD Facilities' Healthcare Uses: **Freestanding Dialysis Center**

- Pros
  - May represent opportunity for incremental rental revenue under facility lease agreement with independent dialysis operator (such as DaVita)
  - May represent opportunity for incremental operating income as expansion of hospital outpatient services (may require separate freestanding outpatient license)
- Cons
  - According to the National Kidney and Urologic Disease Information Clearinghouse, ESRD incidence rate = approx 350/Million population. Therefore, total hospital service are would include an estimated 350 ESRD patients. If each patient generated 1 visit per week, total service area dialysis market equates to approx. 6000 visits per year. Limited market size equates to minimal financial upside potential.

Conclusion

HFS consultants

Thank You

HFS Consultants

505 Fourteenth Street, Fifth Floor

Oakland, CA 94612-1912

510.768.0066

info@hfsconsultants.com

www.hfsconsultants.com

BRANCH OFFICES: Oakland | Fresno Area | Orange County | San Diego County
Milwaukee Area | Chicago, IL | Pheonix, AZ | Portland, OR