Bartlett Regional Hospital

To: Board of Directors of Bartlett Regional Hospital **April 21, 2023**
From: Sam Muse, CFO
Subject: Funding Strategic Initiatives

♦ ISSUE

As part of Bartlett's phased approach to financial sustainability, management continues to review all strategic initiatives to ensure our capital is aligned in a way that will maximize our financial flexibility to ensure we can meet the needs of the community not only for today but, more importantly, for the years to come.

♦ BACKGROUND

Construction Improvement Projects:

As part of this review, management has assessed all Capital Improvement Projects initiated by Bartlett that have cash appropriations through Assembly action. Currently, those projects include:

- Administration Building Siding ($43,000 in Fund Balance available)
- Crisis Stabilization ($500,000 in Fund Balance available, expected to be fully spent very soon)
- Study-Secondary campus Access ($88,000 in Fund Balance available)
- **Deferred Maintenance (~$3.5M in Fund Balance available)**
- **Emergency Department Addition ($12M in Bond Funds available, project not yet underway**)
- Bartlett Parking Study ($72,000 in Fund Balance available).
- Bartlett CT/MRI Replacement ($600,000 in Fund Balance available, project underway)

Of these projects, only the Emergency Department Addition has funds that could reasonably be altered/delayed in a way that would meaningfully improve Bartlett's flexibility going forward. The remainder of the projects are too far along in their progression and/or simply don't have significant amounts of monies left in them. The other project that Bartlett could potentially access is Deferred Maintenance. However, deferred maintenance, by nature, includes many items that aren't discretionary to the hospital and will need to be addressed.

That said, the Emergency Department Addition project is ramping up, with subcontractors to be awarded soon. And the Hospital is incurring costs weekly related to activity. These costs will increase in the coming weeks as the project continues to move forward. The longer we continue, the more difficult it becomes to alter or delay.

Bond Funding:

In March of 2022, Bartlett Hospital issued $21,497,218 in revenue bonds. Of this issuance, $8,000,000 was appropriated to the Crisis Stabilization project, $12,000,000 was appropriated to the Emergency Department Addition project, $1,358,000 was placed in a bond reserve account, with the remainder paying issuance costs. This has left the hospital with almost $39,000,000 in bond debt and annual payments (principal & interest) associated with that debt totaling $3,000,000.

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The following is a summary of changes to long-term debt for the year ended June 30, 2022:

	Beginning Balances	Additions	Reductions	Ending Balances	Amounts Due Within One Year
Bonds payable:					
2013 Hospital revenue refunding bond	$ 7,500,000	$ -	$ (910,000)	$ 6,590,000	$ 945,000
2021 Hospital revenue refunding bond	10,760,000	-	(90,000)	10,670,000	175,000
2022 Hospital revenue refunding bond	-	18,775,000	-	18,775,000	370,000
Bond premium	139,484	2,722,218	(94,095)	2,767,607	295,026
Total bonds payable	$ 18,399,484	$ 21,497,218	$ (1,094,095)	$ 38,802,607	$ 1,785,026

Annual debt service requirements to maturity are as follows:

Year Ending June 30	Principal	Interest	Total
2023	$ 1,490,000	$ 1,376,069	$ 2,866,069
2024	1,770,000	1,313,196	3,083,196
2025	1,845,000	1,236,919	3,081,919
2026	845,000	1,157,262	2,002,262
2027	1,930,000	1,114,939	3,044,939
2028 - 2032	10,815,000	4,683,738	15,498,738
2033 - 2037	10,750,000	2,623,784	13,373,784
2038 - 2042	6,590,000	855,750	7,445,750
	$ 36,035,000	$ 14,361,657	$ 50,396,657

Bartlett has rate covenants associated with all revenue bonds. These covenants require that Bartlett Hospital's revenues less the cost of operations and maintenance must be at least 115% of the annual debt service (principal + interest) of the hospital. In short, the Hospital would need to generate about $3,450,000 in income a year to satisfy these requirements. Certain items included in accrual accounting measures of income, such as depreciation, can be added back to achieve this goal. However, Bartlett hospital is currently on pace to lose $10,000,000 on an accrual basis. Even adding back depreciation, that will still leave the Hospital well short of breakeven and even shorter from the $3.45M needed to meet our covenants.

The operating losses as well as the already heavy debt load will make it more difficult to access the bond market in a meaningful way in the immediate future. Additionally, any bonds that we might be able to obtain soon would be risk adjusted, meaning likely higher interest rates to reflect additional risk that any lender would take on. Furthermore, any debt that the Hospital takes out in the private market, which would be quicker and easier to access, would generally have shorter durations of payback and, again, higher interest rates. This is not to say that Bartlett couldn't access the market, but management believes it could be costly to do so at this time. And certainly, with more debt, more of future free cash flows would also be used in paying interest on that debt.

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Cash Position:

As of December 2022, Bartlett had $40,000,000 in unrestricted cash with which it can fund operations, capital purchases and fund other strategic initiatives. This reflects a roughly $13,000,000 decrease in unrestricted cash from a year earlier. Additionally, over the last several months, Bartlett Hospital has seen decreases in cash from operating the hospital on a day-to-day basis.

As addressed earlier, Bartlett has ~$16,000,000 of cash restricted for use in capital projects initiated by Bartlett and appropriated through the Assembly. The cash in capital projects generally has two flavors, bond funds and Bartlett fund balance. And, of those two flavors, bond monies make up about $12,000,000 and sit entirely in the Emergency Department Addition project. Without any action by the board and/or Assembly, these funds will go to zero in the next year as the projects complete.

Strategic Initiatives Priorities:

Within the last several months, many new initiatives have presented themselves to Bartlett, including Wildflower Court, Home Health and Hospice, and the potential to bolster Bartlett's specialty clinics. With Bartlett's resources to pursue these initiatives thinning, it has become more imperative to ensure we apply our capital strategically. Each initiative that we undertake will have a different impact on our community, our culture, and our financial sustainability. And, certainly, many of these projects come with a cost to implement, with the hope they bolster the Hospital in differing ways for years to come. However, Bartlett is at a juncture where it will be difficult to pursue many large initiatives simultaneously. So, these initiatives must be weighed against each other.

Again, of the strategic initiatives currently underway, the Emergency Department project represents the most significant opportunity for reassessment. The project, as initially outlined, would cost $17,000,000 to construct. Currently, there are $12,000,000 in bond funds appropriated to the project. To complete, assuming some success in value engineering or reducing the scope of the project, it would still be necessary for Bartlett to appropriate another $3,000,000 - $5,000,000 in unrestricted cash to the project. This money would come from the current $40,000,000 balance, reducing it to $35,000,000 - $37,000,000. If Bartlett were to pursue other strategic initiatives in conjunction with the Emergency Department, utilizing cash to do so, we would potentially reduce our cash position to anywhere between $20,000,000 and $25,000,0000, depending on the final cost of those projects. At average daily operating expenditures of $350,000 for the Hospital, this represents around 2-months of operating expenditures.

Alternatively, if the Emergency Department project did not move forward, the bond funds currently appropriated to the project could be used elsewhere. The real opportunity in this scenario would be that there is currently $7,000,000 in unrestricted funds appropriated to the Crisis Stabilization project that management believes we would be able to substitute with some of the remaining bond funding. By pulling the unrestricted funding back, this would bolster Bartlett's unrestricted cash balance, increasing it to ~$47,000,000. Moreover, there would still be a remaining $5,000,000 in bond funds available without a purpose. In discussions with Bond Counsel regarding these bonds, management believes the remaining funding could be used in a wide variety of ways, including potential capital software implementations or virtually any phase of a future capital need that may arise, including ones associated with the Emergency Department.

♦ OPTIONS

As part of the phased approach to financial sustainability it is necessary to review all current and potential projects moving forward to ensure that they both align with the strategic vision of the hospital including promoting the long-term sustainability of the hospital.

Given the changing the changing landscape with strategic initiatives and the financial state of the hospital, it is imperative that the Board discuss the merits of each project and prioritize them, to ensure pressing projects receive the first infusion of capital and are nurtured first.

Senior Leadership Team recommendation:
Senior Leadership recommends that the Emergency Department Addition project be put on hold indefinitely, pending further deliberation regarding strategic initiatives and best allocation of immediate resources given the current environment.