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MEMORANDUM

To: Commissioners

From: Paul Parker PCP

Date: June 21, 2012

Re: Carroll Hospital Center
Docket No. 12-06-2330
HSCRC Memorandum and Errata

* *

As a supplement to the staff report and recommendation on the above-captioned project released last week, attached is a memorandum from Health Services Cost Review Commission staff that reviews revenue and expense assumptions employed by Carroll Hospital Center and key financial ratio performance implied by the hospital's financial projections if this project is implemented. HSCRC staff found that the project is financially feasible based on the reasonableness of the assumptions used by the hospital and its analysis of the financial ratios. We regret that this opinion was not available last week for inclusion as an appendix to the staff report and recommendation.

Additionally, we would like to point out an omission and an area of the report that contained some erroneous figures.

1. On page 2, third paragraph, reference is made to the current capital expenditure threshold applicable to hospitals, but the actual threshold was inadvertently left out of the paragraph. That threshold is $11.35 million.
2. Some incorrect figures were included in Table 8 on page 26. A corrected Table 8, showing the corrections is shown on the following page along with a corrected paragraph that followed Table 8, reviewing Carroll Hospital's operating margin performance.

Table 8: Carroll Hospital Center
Recent Financial Performance

	Fiscal Year Ending		
	Jun-30-2008	Jun-30-2009	Jun-30-2010
REGULATED OPERATIONS ONLY			
Net Operating Revenue	$ 165,163,581	$ 173,755,553	$ 177,318,406
Net Operating Income	$ 16,057,126	$ 12,053,197	$ 9,970,747
Net Operating Margin	9.72%	6.94%	5.62%
REGULATED AND UNREGULATED OPERATIONS			
Net Operating Revenue	$ 222,615,025	$ 235,044,615	$ 236,986,105
Net Operating Income	$ 10,545,271	$ 4,129,112	$ (1,295,873)
Net Operating Margin	4.74%	1.76%	-0.55%
Operating Margin – Peer Group 2 Regulated			
Average	5.11%	6.45%	6.04%
Median	~~5.20%~~ 4.84%	~~5.90%~~ 5.61%	6.42%
Operating Margin – Peer Group 2 Regulated and Unregulated			
Average	~~2.38%~~ 1.99%	1.89%	1.79%
Median	~~1.99%~~ 2.38%	1.93%	1.66%
Average Operating Margin – State-Wide Regulated and Unregulated			
Regulated and Unregulated	2.30%	2.60%	2.60%
Regulated	5.20%	5.90%	6.20%

Source: Health Services Cost Review Commission, Disclosure of Hospital Financial and Statistical Data dated September, 2011 which reports regulated and non-regulated activity as reported on the R/E Schedule of the Annual Report.

As reflected in the table above, CHC's operating margin for services regulated by HSCRC ranged from ~~minus .55%~~ 5.62% to ~~4.74%~~ 9.72% in the last three fiscal years. This was below the average performance of its peer group for the last ~~two~~ years, but above the average performance of the peer group ~~for FY 2009 and~~ in FY 2008 and FY 2009.

Finally, while not an error, in reviewing Table 10, we noted that inclusion of a line showing "non-operating income (loss)" would have been a useful addition to this table so that the bottom line of the table, "net income (loss)," could be better understood. The following version of Table 10 provides this line item.

Table 10: Carroll Hospital Center, Historic and Projected Financial Performance (in current year $000's)

	Historic		Current	Projected			
	2010	2011	2012	2013	2014	2015	2016
Gross Patient Service Revenue	216,631	226,344	253,825	254,149	255,420	256,747	258,135
Allowance For Bad Debt	4,064	8,388	8,579	8,590	8,633	8,676	8,720
Contractual Allowance	23,126	24,990	30,577	30,609	30,762	30,932	31,121
Charity Care	4,992	3,012	3,168	3,173	3,188	3,204	3,220
Net Patient Service Revenue	184,449	189,953	211,501	211,777	212,837	213,935	215,074
Other Operating Revenue	2,790	3,604	4,653	4,684	4,738	4,812	4,916
Net Operating Revenue	187,449	193,557	216,154	216,461	217,575	218,747	219,990
Salaries, Wages, Benefits.	111,310	109,245	118,088	118,198	118,771	119,836	121,426
Contracted Services	26,444	24,963	29,304	29,311	29,442	29,696	30,078
Interest on Current Debt	6,788	6,889	7,248	7,188	7,108	7,016	6,911
Current Depreciation	13,638	13,070	15,045	14,653	1,407	15,022	15,313
Project Depreciation	-	-	-	-	-	1,324	1,589
Current Amortization	164	164	164	164	164	164	164
Supplies	27,587	25,463	32,843	32,962	33,214	33,587	34,121
Operating Expenses	185,931	179,794	202,692	202,476	203,106	206,645	209,602
Income from Operation	1,308	13,763	13,462	13,985	14,469	12,102	10,388
Non-Operating Income (Loss)	(2,825	7,427	(10,000)	5,624	5,825	5,056	5,076
Net Income (Loss)	(1,517)	21,190	3,462	19,609	20,314	17,158	15,464

Source: CON application

STATE OF MARYLAND
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MEMO

To: Paul Parker, Maryland Health Care Commission
From: Gerard J. Schmith GJS
Subject: Carroll Hospital Center ("CHC," or "Hospital") - CON Request, #12-06-2330
Date: June 19, 2012

On April 27, 2012 you requested that we review and comment on the financial feasibility of CHC's proposed capital project. The Hospital is seeking approval to construct an Outpatient Cancer Center, which involves the expansion and renovation of the existing Richard N. Dixon Building on the Hospital campus. The total cost of this project is estimated at $27,975,000. The Hospital intends to finance the cost of the project through a combination of cash from operations ($17,975,000) and philanthropy ($10,000,000.)

Data

We have reviewed the project and the accompanying financial projections provided by the Hospital. The data reviewed include audited financial data for the fiscal years ending June 30, 2010 and 2011, budgeted data for the fiscal year ending June 30, 2012, and projected data for the fiscal years ending 2013 through 2016.

Revenues

We have reviewed the assumptions regarding the projections of operating revenue. The Hospital indicated that it would not need an increase to rates in order to complete the project, but has reserved the right to request an increase in the future. The Hospital has made a number of assumptions regarding volume changes and rate increases which may or may not occur during the projection period. Staff believes that the Hospital will need to manage cost regardless of the actual changes that occur. All other changes to net operating revenues are considered reasonable and achievable.

Expenses

We have reviewed the assumptions made on the projection of expenses. The Hospital has assumed various fixed/variable cost relationships for different categories of expenses. The HSCRC staff has estimated that these category of expenses resulted in an overall 80% variable and 20% fixed assumption for changes to cost related to changes in volumes (net of changes due to project depreciation and interest.) CHC currently operates under the HSCRC's Total Patient Revenue System (TPR.) Under the TPR, the Hospital is provided an incentive to control total volume growth and is rewarded by being provided a fixed amount of revenue regardless of its actual growth. Therefore, the Hospital will need to remain efficient, not only in its management of cost, but also in its management of volume in order to maintain the projected profit results.

Financial Ratios

Included as Attachment I are the financial ratios that the HSCRC staff believes to be the most important.

A review of the financial ratios shows that CHC is projected to generate relatively high Operating and Excess Margins throughout the construction period. These margins will decline to more reasonable levels as CHC assumes the depreciation associated with this project. However, since the Hospital is not taking on any additional debt, Debt Service Coverage Ratio (DSCR) will remain at reasonable levels each year even though Days of Cash on Hand decline. Finally, Debt to Capitalization continues to decline throughout the projection period.

Therefore, the HSCRC staff believes that the project is financially feasible.

Carroll Hospital Center

Attachment I

Financial Ratios - Based on "Multi-Year Financial Projections"

Includes Inflation	HSCRC Target Values	FYE 2011	2012	2013	2014	2015	2016
Key Statistics							
Operating Revenue (in thousands)		$193,558.0	$216,153.0	$217,319.0	$220,610.0	$227,315.0	$235,221.0
Operating Income		$13,764.0	$13,461.0	$8,832.0	$6,801.0	$5,497.0	$6,280.0
Excess Revenue over Expenses		$21,191.0	$3,461.0	$14,456.0	$12,646.0	$10,553.0	$11,356.0
Profitability							
Operating Margin	**2.75%**	7.11%	6.23%	4.06%	3.08%	2.42%	2.67%
Excess Margin	**4.00%**	10.54%	1.68%	6.48%	5.58%	4.54%	4.73%
Debt Related							
Debt to Capitalization	**40.00%**	53.00%	52.00%	50.00%	47.00%	45.00%	43.00%
Debt Service Coverage		4.90	2.70	3.90	3.70	3.70	3.80
Liquidity							
Days of Cash on Hand	**115**	232	202	203	160	157	157