

## IS THE HOSPITAL SICK?

### A DARK DAY IN FEBRUARY

Health assessments tend to be complicated and confusing.....whether it's physical health, mental health, or even financial health. In the medical world, most lay people know, for example, that a rising white blood cell count is not good. It's connected to infection. It could be an indication of something as simple as a seasonal allergy or it could be something much more serious....like say, sepsis. More tests and further analysis is a reasonable course of action. Likewise in the financial world, a battery of tests is used to assess financial health. Not one isolated test can tell the whole story and, in fact, it's often misleading.

In preparation of this special report I reached out to numerous sources of information. I started with a review of the audit reports and financial statements going back to 2006. I spoke with County Commission Chair Reid West. I had another long conversation with the hospital liaison, Commissioner John Kolb. I spoke with the chair of the current hospital Board of Trustees and also met with two other trustees, the hospital CEO and CFO. As past chair of the Hospital Foundation, I have obviously had conversations with hospital staff, the former hospital trustees and hospital administrator. I reached out to the American Hospital Association, the Wyoming Hospital Association, and a national hospital data gathering organization. I also spoke with a prominent bond attorney and visited a similar hospital in Wyoming. And lastly, I fell back on my own experience with a national CPA firm.

What's been presented is the hospital's days cash on hand has slipped to 88 days, that at 75 days there is a default on the bonds, that we are 13 days from that event, and the hospital is in a financial crisis. Is that the real story?

The 88 days cash on hand is correct and it has been trending downward. This financial test is called a liquidity ratio.....designed to examine if an organization has enough cash to meet its daily expenses. It is not a test of profitability....but simply says, like a high white blood cell count, more looking is required. For example, in the audit reports no less than 12 financial tests were performed.

So what else can we learn? An important number is annual revenue. I compared revenues from 2011 to 2016. I chose 2011 because that is the time the previous administration was put in place.....and 2016 since those are the most recent numbers. In 2011, gross revenues were about 90 million dollars. In 2016, gross revenues were 147 million dollars. That's an increase of over 60 percent in income....a remarkable and impressive number.

But revenues alone do not tell the whole story. Expenses need to be factored in to get a better financial health picture. Here we look at profitability margins.....notoriously thin in the health care industry. I looked at the net revenues for the past four years. The years seesawed from small gains to small losses year after year with the overall result being a small gain. In 2016, the hospital lost 1.5 million dollars. It sounds like a lot, but it must be compared to revenues to get the margin picture. It's about one percent of revenue. Not a concerning number. In 2015, the hospital had a gain of 2.7 million....a margin gain of about 2 percent. So, for the past two years the hospital has made money on its operations. The reduction in days cash on hand is not the result of operating expenses.

Further analysis shows the expenses have been paid, accounts payable have been reduced, payments on the bonds are current and occupancy rates are high.

Next I looked at cash balances. Here it gets a bit more complicated....sorry about that. I compared cash balances of 2010 to 2016. In 2010 the cash balance was less than 14 million....in 2016 it was over 20 million. So if cash is up why did days cash on hand go down?

Many factors affect that number. To explain, let's say cash balances were constant....that is to say, 20 million today and 20 million five years ago. As revenues have increased, expenses correspondingly increased and the daily expense figure goes up. So the same cash in the bank covers fewer days. So even when the days cash figure goes down, it does not reveal the fact that cash balances went up. Other factors negatively affect that number....particularly capital purchases like medical buildings, expanded services requiring additional medical equipment, and general hospital expansion and equipment replacement.

Next I looked at other hospitals to get a picture of this hospital relative to the industry. Of particular interest was this days cash on hand figure. In other words is 88 days a bad situation.

From the American Hospital Association I got the days cash on hand for all hospitals of similar size in the country. I found the median was 20 days. If you look at just government hospitals, like this one, the number goes up to 42, but still half of this hospital. From the national hospital data gathering organization I looked at Sheridan Memorial Hospital. I chose Sheridan because of the similarities to this hospital. It's about the same size, it too is a county hospital, it has a cancer treatment center, its revenues are comparable, and its daily expenses are similar. The Sheridan facility has only about 6 million dollars in cash and only 28.4 days cash on hand; above the national median, but well below this hospital. In my site visit to the hospital and my conversation with their CFO I heard of no financial crisis concerns despite cash and days cash on hand being less than a third of this hospital.

I also looked at days cash on hand historically. Of particular note is 2008. In 2008 the hospital's days cash was only 52, well below the bond requirement of 75 days that has been in place since 2006. I could find no record of management change, no hospital board changes, no management company takeover, or any bonds being called.

To explain that for me, I reached out to a bond attorney to confirm the difference between breaking the bond covenants and defaulting on the bond. I was told the covenants are promises made by the hospital to the bondholders. Breaking a covenant is like breaking a promise. It is not a dollar default on the debt. You break a promise, you need to fix it. In the case of this hospital, according to the bond attorney, that would mean hiring a health care consultant to sit down with the administration and together devise a plan to correct the deficiency.

And then there's the concern of the downgrading of the bond rating. I was curious why that didn't happen in 2008 when the days cash was 52. I discovered the hospital didn't have a bond rating in 2008. When I inquired further I was told the hospital's financial condition was such it couldn't even sell junk bonds in 2008. The bond rating wasn't even obtained until 2013. A rating was requested to take variable rate bonds to a fixed rate, a much more predictable cost, and to lower the interest rate.

So, is the hospital sick? It is evident from historical benchmarks, current financial tests, comparative analysis within the hospital industry, and an understanding of the working of bonds....it is not.....at least not through 2016. In fact, one of the new hospital trustees told me, "It's not as bad as we thought." The declining days cash on hand has been primarily influenced by capital expenditures and growth. Year to date figures show a downtrend in net profit, but not a financial crisis. To quote Richard Gundling, vice president of Healthcare Financial Management Association, in regards to days cash on hand, "There are no magic numbers and your cash levels depend largely on your strategies, your market, and your opportunities." It would seem the hospital has a rising white blood cell count, as in days cash on hand, but other indicators, even some I haven't talked about, suggest it's not a fatal disease, not a crisis, but more like a seasonal allergy.....or maybe it's just growing pains.

So why all the sudden hospital changes? Why the loss of five trustees at one time and, within hours, the dismissal of the CEO? I don't know. That would require a different kind of investigation and was not within the scope of this financial report. I'm sure there are a number of plausible explanations for what took place on February 7<sup>th</sup>. But I suggest you ask your own questions and form your own opinions as to what happened on that dark day in February.