

PRESIDENT’S MESSAGE
By Blaine Bandi

On January 19 and 20, NAHEFFA members met in Chicago to discuss Build America Bonds and Healthcare Reform. This “mini-conference” marked the first time that NAHEFFA simultaneously presented a conference to a live and internet audience. Over the course of the two days, 14 Authority representatives participated in person and 13 Authorities participated over the internet. I am extremely grateful to all of the members and speakers whose assistance contributed to the success of this topical conference. I am especially grateful to our hosts, the Illinois Finance Authority, and Pamela Lenane and Shannon Govia for their outstanding support as hosts, arranging for speakers and providing technological assistance.

The “webinar based mini-conference” format allows us to be more topical with our subjects. It also is less expensive to produce and permits participation by members operating under travel restrictions. I anticipate that we will increase our utilization of “webinar” technology as topics of interest develop within the industry and among the membership.

Speaking of technology and in recognition of the end of my term as President of NAHEFFA, I would like to share with you a parting edition of “What I Learned”. This one deals with home smoke detectors.

- Home smoke detectors operate on a battery backup.
- Even those that are wired into a home’s electrical power supply emit a beeping sound when the battery needs to be replaced.

- By design the smoke detector emits this sound only between 2:00 and 3:00 AM.
- By design the low battery alarm can only be heard by the family dog for two nights prior to being audible to the human ear.
- The alarm is very upsetting to the family dog. He will engage in barking, wailing, licking and other histrionics to awaken someone to secure his release into the backyard.
- I am the only one in my family who has not developed immunity to the dog’s pleas for assistance.
- When awakened from a deep sleep on night one, these actions are very reminiscent of Lassie seeking out someone with opposable thumbs to rescue Timmy from the well.
- When awakened from a deep sleep on night two, I mentally weigh the merits of allowing Timmy to remain in the well. “He has to learn sometime”, crosses my mind. By the time the dog has pulled the covers off the bed I realize I have neither a well or a Timmy.
- The family dog will not come back in the house after securing his freedom from the annoying alarm.
- The dog is genetically hard wired to warn all members of his species in the neighborhood of the offending alarm through a series of barks and howls.
- On the third night, when the alarm is finally audible to the human ear, sleep deprivation and echoes make it nearly impossible to discern from atop a ladder which of the many candidate alarms is the offending party.
- Surprisingly enough, once the alarm is audible to the human ear, it is less traumatic to the canine ear.

- As I stand atop the ladder awaiting the next pinging clue, I realize the dog is able to convey through facial expressions alone “If you had listened to me on either of the previous two nights and fixed this with your opposable thumbs, we’d both be asleep now”.
- Smoke detectors operate on 9 volt batteries.
- Nothing else in your house, with the exception of transistor radios, operates on 9 volt batteries.
- If you happen to have a transistor radio in your house, the battery has probably been dead for 20 years.
- Removing the dead battery from the offending smoke detector does not stop the alarm.

IN THIS ISSUE...

- Fall Conference Reminder
Page 2
- Washington Advocacy Report
Pages 2-3
- The 3 Year Diploma
Page 3
- Credit Ratings for Hospitals and Health Care Systems
Pages 3-4
- Converting from Tax-Exempt to For-Profit Status
Page 4
- Briefly Noted
Pages 5-6
- Monitoring Debt Covenants and Working with Lenders in Trying Times
Page 7

PRESIDENT'S MESSAGE

Continued from page 1

- Removing the smoke detector from the ceiling and disconnecting the power supply does not stop the alarm.
- At this point there is an overwhelming urge to refer to the offending device as "Jason".
- Wrapping the alarm in towels and placing inside a closed clothes dryer does not render it inaudible.
- Placing the towel wrapped alarm at the bottom of the recycling container with nearly a week's worth of sound baffling waste does not render it inaudible.
- Three progressively violent hammer strikes will render it inaudible. For those of you wondering, it does not sing "Daisy Bell" at the end.
- A lifetime supply of 9 volt batteries is available at Costco for \$14.95.

I realize after two years in office I risk becoming as annoying as a low battery alarm. I remain hopeful that my term has come to an end before any of you were inclined to allegorically disconnect me, wrap me in towels or administer hammer strikes. I am extremely grateful to the members of the Board, the Committee chairs and members, and the membership at large for their confidence and support during my term. It has been a pleasure and an honor to serve as NAHEFFA's first president. I plan to remain actively involved in helping NAHEFFA enhance its members' ability to finance all eligible not-for-profits in our communities.

I also would be remiss if I did not point out my gratitude to Tanya Wilson (Wisconsin). Her design skills are on display throughout our quarterly newsletter. Her editorial skills significantly improved the illusion of my literacy. Most importantly she always accepted my submissions

fashionably late and with a kind word on content.

I look forward to seeing all of you in Washington DC (March 22-24) as we elect new officers and meet with regulatory agencies and Congress.

FALL CONFERENCE REMINDER

NAHEFFA's fall conference is scheduled for September 22-24th in Jersey City, New Jersey. The location for the conference is the Hyatt Regency Jersey City on the Hudson (www.jerseycity.hyatt.com). The conference committee would appreciate your ideas and recommendations for potential topics and speakers. Please contact the committee chair or any of the committee members with your suggestions.

WASHINGTON ADVOCACY REPORT

*By Charles A. Samuels
Mintz Levin*

Dated: February 2010

The New Year provides great opportunities and perils in Washington for health and education financing. Three important tax provisions for tax-exempt financing are "in play." Passage or not may greatly affect the ability of NAHEFFA authorities to provide reasonable, low-cost financing to education and healthcare institutions.

The President has proposed the extension and expansion of the popular Build America Bonds program. BABs are a new borrowing tool for state and local governments, enacted as part of the American Recovery and Reinvestment Act of 2009. These bonds are taxable bonds issued by state and local governments. The Treasury Department makes direct payments to state and local government issuers to subsidize a portion of their borrowing costs, presently in an

amount equal to 35% of the coupon interest of the bonds.

At this time, issuance of BABs is limited to original financing for public capital projects for which issuers could otherwise use tax-exempt governmental bonds. The President proposes not only to make permanent this program, and allow it to be used for current refundings and working capital, but, most importantly for us, proposes to allow financing for 501(c)(3) non-profit entities, particularly non-profit hospitals and universities. The subsidy level would be reduced to 28% under the newly expanded program effective January 1, 2011.

NAHEFFA supports the expansion of the program to 501(c)(3) financing because in certain circumstances this is an efficient way to provide the subsidy (which in this case go to the non-profits). Often these financings are done in tandem with tax-exempt bonds, and it is critical that tax-exempt financing options remain in place.

NAHEFFA's success in obtaining liberalization of the bank deductibility rules has proven to be a great success. Many non-profits have benefited from the incentives for banks to purchase their debt and the new ability of statewide issuers to issue bank qualified bonds since the qualification is now measured at the borrower level. Efforts are underway to extend this provision beyond this year and possibly to make it permanent.

The change in law clarifying that Federal Home Loan Bank guarantees of their members letters of credit are not a prohibited "federal guarantee" has been well utilized, particularly in restructuring bonds and providing assistance to small borrowers of tax-exempt bonds traditionally ignored by credit enhancement providers. There have been over 129 tax-exempt bond transactions utilizing the FHLB guarantee and over 65 in the education and

WASHINGTON ADVOCACY REPORT

Continued from page 2

healthcare sectors. NAHEFFA is engaged with a coalition which includes the AHA and the 12 federal home loan banks to extend or make permanent this useful provision which has not caused any loss of federal government revenue.

An activist federal government also creates some concerns for tax-exempt financings. As of this writing, health reform legislation is in jeopardy, and it is unclear whether provisions adding new financial burdens and community benefit responsibilities for hospitals (as well as new insured patients) will be enacted. Pending financial services legislation attempts to reform the credit rating system, but otherwise presently does not seem to have a huge impact on municipal finance. We are awaiting, however, regulatory and legislative proposals from the SEC which would increase disclosure requirements and might seek direct regulatory authority over issuers for the first time. MSRB continues to enhance its EMMA reporting system and, for example, is looking at adding information on credit ratings.

It should be an interesting year as we head toward the mid-term elections.

THE 3 YEAR DIPLOMA – REINVENTING HIGHER EDUCATION

Some forward-looking colleges are rethinking the old way of doing things and questioning decades-old assumptions about what a college degree means. For instance, why does it have to take four years to earn a diploma? By eliminating that extra year, three year degree students can save as much as 25% in costs.

Instead of taking 30 credits a year, these students take 40. Some students do this by adding summer classes and/or adding

extra courses each semester. The three-year degree is starting to catch on, but it isn't a new idea. Geniuses have always breezed through and some institutions have offered students a three-year option for 40 years or more by having "short terms" in May and June to earn the credits required for graduation.

Changes at the high-school level are also helping to make it easier for many students to earn their undergrad degrees in less time. One in five students arrive at college today with Advanced Placement credits amounting to a semester or more of college-level work. Many universities, including large schools like the University of Texas, make it easy for these AP students to graduate faster. According to the U.S. Department of Education's most recent statistics, about 5% of U.S. undergraduates finished with bachelor's degrees in three years.

There are drawbacks to moving through school at such a brisk pace. For one, it deprives students of the luxury of time to roam intellectually. Compressing everything into three years also leaves less time for growing up, engaging in extracurricular activities, and studying abroad. On crowded campuses it could mean fewer opportunities to get into a prized professor's class. Another risk: the new campus schedules might eventually produce less revenue for the institution and longer working hours for faculty members.

Whether they experiment with three-year degrees, offer year-round classes, or challenge the tenure system, universities are slowly realizing that to stay competitive and relevant they must adapt to a rapidly changing world. A three-year degree is not for every student. Campuses willing to adopt convenient schedules along with more-focused, less-expensive degrees may find that they have a competitive advantage to attracting bright, motivated students. (Source: *Newsweek*; 10/26/09)

CREDIT RATINGS FOR HOSPITALS AND HEALTH CARE SYSTEMS – A NEW ALTERNATIVE

A.M. Best, known for providing ratings services for insurance companies, also provides issuer credit ratings (ICR) on hospitals and health care systems. Unlike a bond rating, an ICR is an overall rating of the entire system's ability to meet its ongoing senior financial obligations, based on a comprehensive quantitative and qualitative evaluation of the system's balance sheet strength, operating performance and business profile.

Many interested parties have a stake in the financial stability of a hospital or health care system and would value the transparency a rating can provide. From grantors, loan underwriters and lessors of high tech equipment in the private sector, to politicians, officials, regulators, and even Medicaid and Medicare on the State and Federal levels, many could benefit from a clearly presented financial picture and outlook.

Likewise, there are many types of transactions that touch one or more aspects of a hospital or health care system's operations, including financing, funding, contract negotiation, regulatory compliance and ultimately, solvency.

There are additional reasons for obtaining a rating when a hospital is part of an integrated delivery system. For example, many health care systems utilize captive insurance companies as a risk-management tool and to contain medical malpractice premiums. In addition, many systems own or affiliate with a health insurance company. The benefits of such integrated delivery systems include negotiating leverage with other managed care payors, creating a stable revenue stream and achieving economies of scale. The benefits to health insurers and

CREDIT RATINGS FOR HOSPITALS AND HEALTH CARE SYSTEMS – A NEW ALTERNATIVE

Continued from page 3

captives being rated include increased access to brokers and reinsurers, fulfillment of regulatory requirements and better appeal to E&O carriers, to name a few.

When rating such systems, the insurance company is not evaluated by A.M. Best as a “stand-alone” insurance carrier; it is typically part of a larger organization with access to substantial financial, technology and management talent resources at the system level.

A.M. Best’s ratings incorporate both publicly available documents and confidential information provided by senior management. During company meetings, senior management presents to A.M. Best its strategic and financial business plan and forecast and an explanation of the various items outlined in those plans. While experience is important, the rating is as much forward-looking as it is based on historical experience.

After the ICR has been determined, the system has year-round access to the rating analysts, which provide senior management with an opportunity to discuss various business plan modifications as they develop and the effect that certain operational or financial changes may have on the rating.

For integrated delivery systems, the analytical team spends a substantial amount of time looking at both the system and the insurer. The analysts try to ascertain a better understanding of the issues impacting each operating entity in the system, in addition to the economics between the system and the insurer and

the system’s level of commitment to its subsidiaries.

The financial strength rating (FSR) of the health plan and/or captive insurers demonstrates their ability to pay policyholder claims, while the ICR of the health care system and hospitals shows whether the ultimate parent/owner can act as a “financial backstop” for these entities if needed. This two-tiered approach provides a complete financial profile of the entire integrated health care delivery system.

To learn more about A.M. Best’s Credit Ratings for hospital and health care systems, please visit the website <http://www3.ambest.com/health/healthcare/> or contact Michael Hoppes, business development manager, at (908) 439-2200, ext. 5154.

CONVERTING FROM TAX-EXEMPT TO FOR-PROFIT STATUS – AN INCREASING PROBABILITY

Approximately 85% of all hospitals operating today are not-for-profit. However, national health care reform, combined with extraordinarily difficult markets for tax-exempt issuers are leading a number of not-for-profit hospital executives and boards to consider giving up their tax-exempt status and converting to for-profit status. A profound impact on the hospital sector will occur if a few of the leading health care systems currently contemplating conversions actually make the leap.

No matter what comes out of Washington as “health care reform”, it is a safe bet that new regulations will be imposed on not-for-profit hospitals. One proposed bill includes requirements for a community needs assessment every three years that would force all not-for-profits to justify and report on their ability to meet community

health care obligations. Other parts of the bill have provisions prescribing financial assistance policies, specifications for how charges must be limited, and policies for how collections are conducted. In other versions of health care reform, more stringent provisions would require not-for-profits to provide charity care and community benefits demonstrably equal to or greater than the value of their tax benefits.

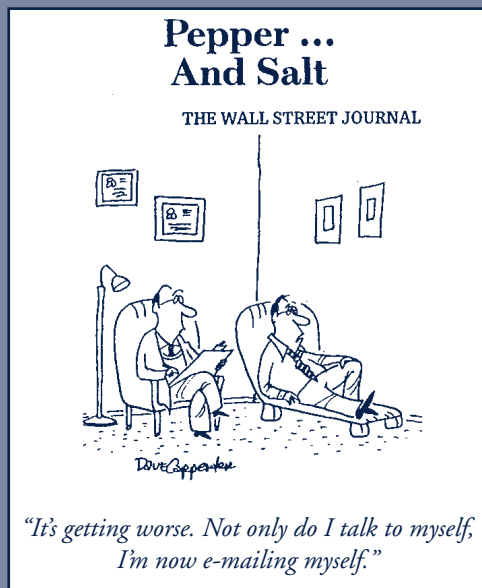
If regulatory risk isn’t enough to deal with, additional challenges for the sector have been the capital markets. For all but the highest rated health care systems, the capital markets are more fickle and volatile than ever, and access is more difficult and less predictable. Investors in hospital debt have come to recognize that health care is no longer a municipal-like investment and the risk in these bonds can be substantial. As a result, hospitals need stronger balance sheets than ever to assure continued access the credit markets. Building cash on the balance sheet while also making the investments in plant, equipment, and technology necessary to remain competitive are daunting tasks for all but the strongest hospital systems.

If the benefits of not-for-profit status are reduced or eliminated by more regulations, uncooperative capital markets, and the economics of an industry that must dramatically increase efficiency, executives and boards may conclude that conversion to for-profit status may be in the best interest of their communities. The hospital sector may be the next wave of conversions. *(Source: Cain Brothers Industry Insights; 10/26/09)*

BRIEFLY NOTED

Long-Term Care

- ... A lack of specific geriatric training as a specialty is causing a widening gap between the number of elderly in our country and the number of physicians trained to care for them. The number of geriatricians in 2010 stands at 3.6 (6,830) per 10,000 population 75 and older (18.9 million). (Source: *Smart Money*; January 2010)
- ... Nearly one third of the U.S. adult population (65.7 million) act as caregivers for at least one person in need of care. Two thirds of caregivers are women. (Source: *Cain Brothers Weekly News*; 12/14/09)
- ... A 44% nationwide decline in senior housing construction occurred when comparing the period 04/01/08 and 04/01/09. Under construction as of 04/01/09 were 12,650 independent living units, 11,175 senior apartments, 6,600 nursing beds, 2,810 memory care units, and 7,790 assisted living units. (Source: *Provider*; December 2009)



Education

- ... Today 58% of all bachelor degrees and 62% of associate degrees are earned by women. At the same time, there has been a 145% rise in unmarried births among college-educated women since 1980. It really is hard to find the right man. (Source: *The Wall Street Journal*; 01/22/10)
- ... Graduating college seniors will have left school in 2008 with an average of \$23,200 in debt, up 6% from 2004. (Source: *The Business Journal*; 01/08/10)
- ... Britain's Cambridge University is considering issuing bonds for the first time in its 800 year history, following a trend set by U.S. Ivy League schools. (Source: *The Wall Street Journal*; 01/04/10)
- ... 58 private U.S. colleges now charge annual tuition in excess of \$50,000. Concern is heightened that potential applicants will not apply to such, which often have substantial scholarship and other funding available to result in a competitive net tuition cost. (Source: *The Chronicle of Higher Education*; 11/06/09)
- ... While the average investment loss in higher education endowments during 2009 was 18.7%, those with endowments greater than \$1 billion averaged 20.5%, and those with endowments less than \$25 million averaged 16.8%. Ten-year average returns for the large category have averaged 6.1%, and for the small portfolios 3.9%. (Source: *Inside Higher Education*; 01/28/10)
- ... One in five Americans who earned a doctorate degree in 2008 attended a community college at some point. (Source: *The Chronicle of Higher Education*; 01/29/10)
- ... In the fall of 2008, 25.3% (4.6 million) of college students took at least one course online. That percentage was only 9.6% in 2002. (Source: *Inside Higher Education*; 01/27/10)
- ... 40 year-old college graduate females are more likely to be married than their high school diploma only counterparts. The reason appears to be that once married, far fewer college graduates will get divorced, seeing marriage not as a source of financial stability, but rather a source of personal fulfillment. (Source: *The Wall Street Journal*; 01/26/10)

Acute Care

- ... The Mayo Clinic raised \$1.35 billion in its first sustained fund raising campaign. It exceeded its goal of \$1.25 billion, doing so in 5, rather than 7 years from 286,000 donors. (Source: *Star Tribune*; 01/26/10)
- ... 96% of all who die in LaCrosse, WI have living wills through a program at the Gundersen Lutheran Hospital. As a result, the cost of care in a patient's last two years of life is lower at Gundersen than in any other hospital in the country. (Source: *The Lutheran*; January 2010)
- ... U.S. healthcare spending grew 4.4% in 2008, the smallest increase in nearly 50 years, as the recession caused consumers and employers to pare medical expenses. (Source: *The Wall Street Journal*; 01/10/10)

BRIEFLY NOTED

Continued from page 5

- ... Radiation therapy for treating cancer is widely accepted, with 2,200 centers operating throughout the country. Proton therapy, capable of delivering a higher dosage in a more concentrated area, is the new kid on the block. Currently there are six such centers, each built at costs of \$150 to \$200 million. (Source: *Industry Insights*; 12/21/09)
- ... Four of the 20 most profitable critical access hospitals for 2007 are located in Wisconsin. Three are in Mississippi and two each in Indiana, New Mexico, and Florida. (Source: *Modern Healthcare*; 12/21/09)
- ... Charitable giving to hospital and health systems grew 2.9% in 2008 despite the financial downturn. (Source: *Modern Healthcare*; 11/02/09)

General

- ... Over 1,000 pedestrians visited emergency rooms in 2008 because they got distracted and tripped, fell, or ran into something while using a cell phone to talk or text. That is double the number in 2007, which was double the accidents reported in 2006. (Source: *The New York Times*; 01/17/10)
- ... Property and casualty insurance companies have turned profitable again in the second half of 2009 which bodes well for the issuers of tax-exempt muni bonds. As of 9/30/09, such insurers held 14.2% of all muni-bonds outstanding. (Source: *The Bond Buyer*; 12/29/09)

- ... Takuo Toda of Japan holds the world's record for the longest flight of a paper airplane (27.9 seconds). (Source: *Associated Press*; 12/28/09)
- ... Norman Borlang, a noble prize winner, passed away at the age of 95 in 2009. Through his genetic engineering of crop seeds and better farming techniques, he is responsible for a six-fold increase in harvest per acre throughout the world. (Source: *TIME*; 12/18/09)



"Fishing for what is biting"

MONITORING DEBT COVENANTS AND WORKING WITH LENDERS IN TRYING TIMES

Taking on or restructuring debt should prompt a review of a hospital's investment portfolio in the context of the revised balance sheet. Too often, however, hospital leaders fail to consider the impact of the investment portfolio on new or newly restructured debt. Failure to build a bridge from the liability side to the asset side creates a dangerous disconnect and the potential to violate promises to maintain financial ratios.

Debt covenants are financial or operational tests a hospital agrees to meet during the life of a financing transaction. They are negotiated during the debt structuring process and are different for every transaction. And the amount of leverage a hospital has in negotiating debt covenants depends on the hospital's financial strength. In good markets, most hospitals tend not to view debt covenants as risks, so they may not think to address them within their investment portfolios. An investment portfolio consisting of volatile asset classes will tend to put the liquidity ratios at a higher risk than a portfolio that is more conservatively allocated. Therefore, investors must be willing to accept slower portfolio growth where covenants exist.

Good relationships with existing lenders must also be maintained, particularly in difficult times. Should a liquidity crisis occur – from a technical debt default, such as tripping a covenant, to actually defaulting on a scheduled payment – it is all too easy to begin to see the lender as an adversary. By doing that, however, you may become counterproductive, and can unnecessarily complicate the situation. In a credit crisis, as much as possible, you should build on your

partnership with the lender so you both perceive that you are working together to resolve the issue.

Until they are absolutely convinced that existing management can't turn the situation around, lenders will work with you. The key is to take proper steps to communicate and to educate them along the way. Trudging through a credit or liquidity issue is never enjoyable. But, should you find your organization in such an experience, approach it as a team with all members involved to yield a more positive and successful outcome. (*Sources: Healthcare Financial Management; July 2009 & November 2009*)



National Association of Health and Educational Facilities Finance Authorities

OFFICERS:

President

Blaine Bandi
Arizona

Vice President

Dr. Maribeth Wright, Ph.D.
Iowa

Secretary

Marianne Remedios
Minnesota

Treasurer

James Parks
Louisiana

DIRECTORS:

Robert Donovan
Rhode Island

Paul Edwards
Washington

Mike Stanard
Missouri

Chris Taylor
North Carolina

Don Templeton
South Dakota