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December 20, 2019

Ms. Margo Michaels, Director  
Determination of Need Program  
Department of Public Health  
250 Washington Street, 6<sup>th</sup> Floor  
Boston, MA 02108

RE: Determination of Need Application – Advocate Healthcare of East Boston, LLC

Dear Ms. Michaels,

The accompanying report is included as relevant additional financial information to assist the department in rendering a decision regarding the proposed construction project of Advocate Healthcare of East Boston, LLC (the "Company").

The report is intended solely for the information and use of management and members of the Company, and the Massachusetts Department of Public Health Determination of Need Program in its review of the Company's Determination of Need application under regulation 100.210 (4) a. It is not intended to be and should not be used by anyone other than these specified parties.

Please contact me should you have any questions or need further information.

Sincerely,

CLA (CliftonLarsonAllen)

Mark Cummings, CPA

Principal

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**ADVOCATE HEALTHCARE OF EAST BOSTON, LLC**

**BENCHMARKING MANAGEMENT'S**

**PROJECTED FINANCIAL ANALYSIS**

**FOR THE INITIAL OPERATING PERIOD**

**NOVEMBER 1, 2019 THROUGH DECEMBER 31, 2019**

**AND FOR THE YEARS ENDING**

**DECEMBER 31, 2020 THROUGH DECEMBER 31, 2024**

**PROCESS OVERVIEW**

**Management’s Projections**

CliftonLarsonAllen LLP (CLA) was requested by the management of Advocate Healthcare of East Boston, LLC to read the financial projections prepared by Advocate Healthcare of East Boston, LLC (“Management” or “AHEB”) for the initial operating period November 1, 2019 through December 31, 2019 and the years ending December 31, 2020 through 2024 and benchmark the stabilized year of Management’s projection.

We have not compiled or examined any of the financial data utilized in the benchmarking analyses and express no assurance of any kind on it. Furthermore, even if the assumptions disclosed herein were to materialize, there will be differences between projected and actual results, because events and circumstances frequently do not occur as expected and those differences may be material. These analyses are intended for the internal use of Management and the Massachusetts Department of Health Determination of Need Program (DoN) and is not intended to be and should not be used or relied on by anyone other than these specified parties.

**BENCHMARK STAFFING AND COST ANALYSIS**

Providers in Suffolk County were used to benchmark Management’s projections. AHEB’s projected initial operating period of November 1, 2019 through December 31, 2019 was compared to Suffolk County Medicare and Medicaid cost report data for the most recent available period of 2018. The data was then projected out to 2024 with an applied 2% revenue inflation factor and 2% expense inflation factor.

**MANAGEMENT’S PROJECTIONS**

**Occupancy/Payer Mix/Revenue per Patient Day**

Projected revenue consists of revenue from operating the skilled nursing facility. Management’s baseline projected revenue for the initial operating period of November 1, 2019 through December 31, 2019 and the year ending 2020 was derived from the interim financial data for 2019, current reimbursement and nursing home regulations and management’s experience in the industry. This information was utilized to project and establish a baseline for the projection. Future years were projected utilizing assumptions for rate increases and operating expenses, and any known changes for operating the renovated facility during the Projection Period.

The following table summarizes the configuration of rooms before renovations and after the proposed renovations:

Resident Room Configuration							
Pre-Renovation - 190 Beds				Post Renovation - 165. Beds			
Type	Capacity	Inventory	Total Beds	Type	Capacity	Inventory	Total Beds
Private	1	21	21	Private	1	28	28
Semi	2	18	36	Semi	2	37	74
Three-Bedded	3	15	45	Three-Bedded	3	21	63
Four-Bedded	4	22	88	Four-Bedded	4	0	0
Total Beds			190	Total Beds			165

**Observations:**

- The plan for this Determination of Need Application is for the replacement of critical systems and fixed equipment, and renovations addressing improved compliance with healthcare construction requirements for resident rooms and related service areas.

**Historical Operations**

Historical Average Occupancy December 31,				
	2015	2016	2017	2018
Occupancy %	76.17%	86.46%	90.73%	90.72%

Historical Average Payer Mix * December 31,				
	2015	2016	2017	2018
Private	3.00%	5.00%	4.00%	3.00%
Medicare	9.00%	12.00%	10.00%	9.00%
Medicaid	86.00%	78.00%	83.00%	84.00%
HMO/Other	2.00%	5.00%	3.00%	4.00%
Total	100.00%	100.00%	100.00%	100.00%

\* Massachusetts' Medicaid Cost Report Data

**Projected Operations**

The following table summarizes AHEB’s 2019 projected data compared to 2018 Suffolk County data for beds and occupancy, payer mix and revenue per patient day. The numbers are then inflated out for Suffolk County to compare to AHEB’s projected year six which is 2024.

	2019	2018			Inflation Adjustment	2024			
	Advocate Healthcare of East Boston	Suffolk, MA 25th percentile	Suffolk, MA 50th percentile	Suffolk, MA 75th percentile		Advocate Healthcare of East Boston	Suffolk, MA 25th percentile	Suffolk, MA 50th percentile	Suffolk, MA 75th percentile
<b>Occupancy~</b>									
SNF/NH Beds	134	83	121	134		144	83	121	134
Occupancy %	91.8%	86.7%	90.4%	93.3%		91.2%	86.7%	90.4%	93.3%
Total SNF/NH Days	^ 7,503	27,479	35,642	42,823		47,914	27,479	35,642	42,823
<b>SNF Payor Mix (% of Days)</b>									
Medicare FFS	10.0%	6.4%	8.7%	12.2%		12.0%	6.4%	8.7%	12.2%
Medicaid	81.0%	48.2%	62.1%	68.3%		79.0%	48.2%	62.1%	68.3%
Other (including MC Advantage)	9.0%	45.4%	29.2%	19.5%		9.0%	45.4%	29.2%	19.5%
<b>Revenue per Patient Day</b>									
Medicare FFS	\$625	\$560	\$633	\$649	2.0%	\$690	\$631	\$713	\$731
Other	\$241	\$228	\$242	\$279	2.0%	\$262	\$256	\$272	\$314

~ Based on active beds

^ November 1, 2019 to December 31, 2019

Projected Average Occupancy  
December 31,

	2019*	2020	2021	2022	2023	2024
Occupancy %	91.80%	91.80%	91.63%	91.16%	91.16%	91.16%

\* November 1, 2019 through December 31, 2019

**Observations:**

- AHEB’s projected occupancy is above the median for the county both before and after the proposed project’s completion
- Members of AHEB’s ownership team have managed the facility since the middle of 2015, as shown in the historical table above, occupancy has steadily increased during that time
- Since 2017 AHEB’s historical occupancy level has been at or above the median. The occupancy is projected to be consistent with these levels throughout the projection period
- AHEB’s Medicare utilization is consistently above the median and is projected to remain at these levels during the projection period
- AHEB has consistently reported a Medicaid mix above the 75<sup>th</sup> percentile, see the historical data above on payer mix for AHEB where they have consistently displayed a higher Medicaid census than any other payer and are projected to continue that trend
- AHEB reports a lower non-Medicare rate due to its higher Medicaid mix

**EXPENSES**

Operating expenses have been projected to be recognized during the month incurred. Management’s baseline projected expenses for the initial operating period of November 1, 2019 through December 31, 2019 and year ending 2020 were derived from interim financial data of the facility (managed by ownership prior to acquisition) for the current period, and Management’s historical experience of operating the facility. This information was utilized to project and establish a baseline for the projection. The specific basis for inflationary increases in major expense categories were formulated by Management.

## Historical Operations

The Following table summarizes the historical cost per patient day by department:

Historical Costs per Patient Day by Department\*  
December 31,

	2017	2018
Administration	\$77	\$75
Plant	23	16
Dietary	18	18
Laundry	4	3
Housekeeping	6	6
Nursing	103	108
Social Services	4	4
Other General Services	4	5
<b>Total Costs</b>	<b>\$239</b>	<b>\$235</b>

\*Massachusetts' Medicaid Cost Report Data

## Projected Operations

The following table summarizes AHEB's projected 2019 data compared to 2018 Suffolk County data expenses by department per patient day. The 2018 Suffolk County numbers are then inflated 2% each year to compare to AHEB's projected year six which is 2024.

	2019				Inflation Adjustment	2024			
	Advocate Healthcare of East Boston	Suffolk, MA 25th percentile	Suffolk, MA 50th percentile	Suffolk, MA 75th percentile		Advocate Healthcare of East Boston	Suffolk, MA 25th percentile	Suffolk, MA 50th percentile	Suffolk, MA 75th percentile
<b>Costs per Patient Day*</b>									
Administration	\$76	\$49	\$63	\$81	2.0%	\$86	\$55	\$71	\$91
Plant	\$16	\$14	\$16	\$20	2.0%	\$19	\$16	\$18	\$23
Dietary	\$19	\$19	\$20	\$24	2.0%	\$20	\$21	\$23	\$27
Laundry	\$3	\$3	\$3	\$4	2.0%	\$5	\$3	\$3	\$5
Housekeeping	\$7	\$6	\$6	\$9	2.0%	\$7	\$7	\$7	\$10
Nursing	\$111	\$93	\$100	\$123	2.0%	\$122	\$105	\$113	\$139
Social Services	\$7	\$3	\$4	\$5	2.0%	\$8	\$3	\$5	\$6
Other General Services	\$4	\$3	\$4	\$6	2.0%	\$4	\$3	\$5	\$7
<b>Total Costs</b>	<b>\$243</b>	<b>\$190</b>	<b>\$216</b>	<b>\$272</b>		<b>\$271</b>	<b>\$213</b>	<b>\$245</b>	<b>\$308</b>

\*AHEB numbers include benefits which are included in Administration. Benchmark data excludes benefits. Additionally, Ancillary expenditures are excluded for both AHEB and the Benchmark data.

## Observations:

- AHEB reports a cost structure between the median and 75<sup>th</sup> percentile both historically (see table above) and in its projections

- AHEB does not anticipate any significant change in cost structure due to the renovations, as their cost in comparison to the median remains consistent
- Plant costs are projected to increase due to projected higher real estate taxes as a result of the increased value of the building. In addition, various cost centers have increased slightly due to the increase in volume
- Historically, AHEB has had slightly higher nursing cost per patient day in comparison to the median for the county. Management projects this trend to continue with no drastic change in the operating structure for care of the patient panel
- For purpose of this observation, It is assumed, with no other information on the future of various healthcare factors or changes, that the facilities in Suffolk County will make no changes in nursing staffing

### **KEY FINANCIAL RATIOS**

In performing this analysis both Medicare and Medicaid cost report data maintained by CMS and the Massachusetts Center for Health Information and Analysis (CHIA) was utilized, with the aid of a proprietary software application. This allowed management the ability to compare key financial ratios with those of similarly located facilities. The ratios below are a common tool used by financial institutions and the health care industry to evaluate the operations of a health care entity.

#### **Earnings before Interest, Depreciation and Amortization (EBIDA) Margin:**

EBIDA is a measure of a company’s operating performance. Essentially, it’s a way to evaluate a company’s performance without having to factor in financing decisions, accounting decisions or tax environments. EBIDA Margin can be a meaningful gauge of a provider’s ability to contain costs, it offers a clearer reflection of operations by stripping out expenses that can obscure how the company is really performing. The EBIDA margin is calculated by dividing EBIDA by total revenue.

The greater a company’s EBIDA Margin, the lower the company’s operating expenses in relation to total revenue. EBIDA margin eliminates the non-operating profitability and cash flow and is important in measuring performance across a single industry with companies of different size and tax situations.

The following chart shows the provider’s projected EBIDA Margin against the Suffolk County Median EBIDA Margin.

	2019	2018			2024			
	Advocate Healthcare of East Boston	Suffolk, MA 25th percentile	Suffolk, MA 50th percentile	Suffolk, MA 75th percentile	Advocate Healthcare of East Boston	Suffolk, MA 25th percentile	Suffolk, MA 50th percentile	Suffolk, MA 75th percentile
<b>EBIDA</b>	7.3%	-3.3%	1.6%	8.8%	7.5%	-3.3%	1.6%	8.8%

#### **Observations**

- AHEB is projecting EBIDA above the Suffolk County median in both 2019 and 2024
- Additionally, for both 2019 and 2024 AHEB’s projected EBIDA is approaching the top quartile
- The EBIDA for Suffolk County was assumed to remain at its 2018 level for purposes of this analysis

## Operating and Capital Budgets

In Benchmarking management’s projected financial analysis, we analyzed and considered AHEB’s past and present operating and capital budgets. Note, AHEB only acquired the license to operate the facility on November 1, 2019 so there are no past operating and capital budgets. Ownership however, did manage the facility prior to acquisition, and the past and present operating budgets are consistent with the results contained in management’s projected financial analysis as indicated by the tables presented previously in the report. Additionally, management has no significant plans at this time to materially alter the operating structure or impact the care of the patient panel.

AHEB does not maintain formal capital budgets. However, except for the first year following construction, a review of past and present capital expenditures indicates that AHEB intends to invest in the built environment of the residents at amounts consistent with or greater than prior spending levels.

	2017	2018	Planned 2024
Capital Expenditures	<u>\$ 55,919</u>	<u>\$ 96,491</u>	<u>\$ 100,000</u>

## Balance Sheets

In benchmarking management’s projected financial analysis, we analyzed AHEB’s balance sheets. As indicated previously AHEB acquired the license to operate the facility on November 1, 2019 and as such there are no prior balance sheets to compare.

## Days Cash on Hand

We analyzed AHEB’s projected days cash on hand ratio for 2019 and the last year of the projection, 2024. The days cash on hand ratio is a liquidity ratio that indicates an entity’s ability to satisfy its current operating expenses with the current cash available.

	2019	2018			2024			
	Advocate Healthcare of East Boston	Suffolk, MA 25th percentile	Suffolk, MA 50th percentile	Suffolk, MA 75th percentile	Advocate Healthcare of East Boston	Suffolk, MA 25th percentile	Suffolk, MA 50th percentile	Suffolk, MA 75th percentile
Days Cash on Hand	25.5	9.7	20.6	91.5	46.7	9.7	20.6	91.5

## Debt Service Coverage Ratio

In Benchmarking management’s projected financial analysis we considered the level of financing necessary to support the proposed project. In doing so, we analyzed the debt service coverage ratio of the applicant. The debt service coverage ratio measures an applicant’s ability to meet its annual debt service requirements. The debt service coverage ratio is an indicator used by lenders to determine an organization’s ability to incur additional financing and service its existing debt.

The following chart shows the applicant’s projected debt service coverage ratio compared to the Massachusetts debt service coverage ratio median:



2019	2018			
Applicant	Massachusetts 25th percentile	Massachusetts 50th percentile	Massachusetts 75th percentile	
Debt Service Coverage (DSC)	1.40	0.40	1.30	4.8

2024*				
Applicant	Massachusetts 25th percentile	Massachusetts 50th percentile	Massachusetts 75th percentile	
Debt Service Coverage (DSC)	1.74	0.40	1.30	4.8

\* Note: The MA 2018 benchmarks were assumed to be the same in 2024 as they were in 2018

- AHEB’s days cash on hand ratio starts slightly higher than the median at December 31, 2019 and is approaching the top quartile by 2024, the last year of the projection
- AHEB’s debt service coverage ratio is slightly higher than the Massachusetts’s state median in 2019 and is improved by .34 in the final year of the projection, 2024