

# **Justification and Senate 579 as filed.**

## **Justification**

### **Senate 579**

#### **An Act to Create A Community Hospital Capital Reserve Fund**

##### **What problem is this Act trying to solve?**

DHCF&P provides quarterly reports on the financial health of the acute hospital sector. While the percentage varies from quarter to quarter, year after year the concluding paragraph remains consistent; “the ability to cover long-term obligations remained a serious concern for (1/4-1/3 varies quarterly) of Massachusetts hospitals.” The significance of this statement: first, it applies to community hospitals, and second, it is a dire warning that the necessary capital that will allow community hospitals to adapt to growing community health needs will either be unavailable or the cost to access capital will be so high that it will add permanent fixed costs to service debt that will crowd out more important expenditures. The DHCF&P statement applies to a significant number of hospitals, but the analysis does not address the implications of low operating margins and the lack of significant endowments across almost all community hospitals as an even greater concern. A lack of access and high cost of capital means that future growth of the health care delivery system will only occur in the high cost teaching sector with devastating results for health care insurance premiums.

##### **How real is the disparity of capital projects between the community hospital sector and the teaching sector?**

Senate 579 is a refilling of Senate 2368, which was filed during the last legislative session. Since Senate 2368 was introduced for consideration, the teaching sector has put into service, received approval for, or initiated planning over \$3B in expansion projects. Conversely, the community hospital sector has virtually no significant inpatient expansion projects, with mostly renovation agendas that total less than \$700M. With over 50% of all admissions going to a teaching model of care versus the national average of 18%, and at a cost in excess of \$1.6B of excessive cost of secondary care provided in a teaching model, we have little chance of mitigating health care cost increases unless we begin to invest in the community hospital sector and recalibrate the balance.

##### **How does Senate 579 contribute to lowering the cost of capital?**

If the moral bond construct follows the success of the Maine experience, these tax exempt bonds issued by HEFA will allow the credit hospital to leverage the Commonwealth’s bond rating, currently AA, at one notch below this rating, which is A. This will have two effects; first, the interest rate will be significantly lower than if the credit entered the market at BBB for example, and second, the cost of bond insurance will be significantly less than if a BBB rated

hospital purchased insurance. The savings will vary by the size of the issue and the degree of strength of the underlying credit, but a random sample of our membership who recently went through a financing, showed savings ranging from \$750,000 to \$1M annually. Over the life of a bond issue such cumulative savings are dramatic. Through the use of a standardized process with standardized documents, a lower interest rate and a lower cost of credit enhancements, it is Wall Street that loses in this proposal.

### **What process has Senate 579 gone through thus far?**

During the last legislative session, separate bills were originally filed in the House and Senate and combined in the Joint Committee on Healthcare Finance where it was approved and sent to the Joint Committee on Bonding, Capital Expenditures, and State Assets. It was approved to go forward and was approved by Senate Ways and Means as Ought to Pass. Throughout the process we have consulted with HEFA and received their support. We solicited input from Hawkins, Delafield & Wood LLP, a national leading bond counsel firm and experts in moral bond issues; Edwards Angell Palmer & Dodge, bond counsel to HEFA; Moody's; and the executive director of Maine HHEFA. We provided educational sessions for legislative committee members and staff, and the Administration. Edwards Angell Palmer & Dodge concluded that the proposed legislation was not in contravention to the state constitution.

### **What if Senate 579 is successful?**

As more hospitals enter the proposed bond program, savings accrue not only to the provider but it begins to take pressure off the state Medicaid budget, which participates in the cost of capital. Eventually, it may be offered to the teaching hospitals as the lowest cost of financing available to them. In the case of Maine, the program is so successful they have been able to offer this financing alternative to very small not-for-profit agencies that never would be able to access credit on their own. This is a program that does not require state funding and is indifferent to the ups and downs of budget cycles. At the end of the day, which could be twenty years from now, cumulative savings could approach \$1B as compared to the current model of financing debt.

**SENATE . . . . . No. 579**

**The Commonwealth of Massachusetts**

PRESENTED BY:

**Robert A. O'Leary**

*To the Honorable Senate and House of Representatives of the Commonwealth of Massachusetts in General Court assembled:*

The undersigned legislators and/or citizens respectfully petition for the passage of the accompanying bill:

**An Act To Create a Community Hospital Reserve Fund.**

PETITION OF:

NAME:	DISTRICT/ADDRESS:
Robert A. O'Leary	Cape and Islands
Susan C. Tucker	Second Essex and Middlesex

**The Commonwealth of Massachusetts**

**In the Year Two Thousand and Nine**

**AN ACT TO CREATE A COMMUNITY HOSPITAL RESERVE FUND.**

*Be it enacted by the Senate and House of Representatives in General Court assembled, and by the authority of the same, as follows:*

SECTION 1. Section 2-10 of chapter 614 of the acts of 1968, as previously amended, is hereby further amended by inserting after subsection (f) the following new subsection:

(g) Community hospital capital reserve fund.

(i) For the benefit of nonprofit community hospitals within the commonwealth licensed by the department of public health, the authority may create and establish one or more special funds,

herein individually referred to as a community hospital capital reserve fund, and to the extent so created, shall pay into each such community hospital capital reserve fund any monies appropriated and made available by the commonwealth for the purposes of such fund, any proceeds of sale of notes or bonds to the extent provided in the resolution, trust agreement, or indenture of the authority authorizing issuance thereof, any other monies or funds of the authority that the authority determines to deposit in the fund and any other monies which may be available to the authority only for the purpose of such fund from any other source or sources.

All monies held in the community hospital capital reserve fund, except as hereinafter provided, shall be used solely for the payment of the principal of bonds of the authority which are secured by such community hospital capital reserve fund as the same mature (which herein shall include becoming payable by sinking fund installment), the purchase of such bonds, the payment of interest on such bonds, or the payment of any redemption premium required to be paid when such bonds are redeemed prior to maturity; provided, however, that, monies in a community hospital capital reserve fund shall not be withdrawn there from at any time in such amount as would reduce the amount of such fund to less than the maximum amount of principal and interest maturing and becoming due in any succeeding calendar year on outstanding bonds which are secured by such community hospital capital reserve fund, except for the purpose of paying the principal of and interest on such bonds maturing and becoming due or for the retirement of such bonds in accordance with the terms of any contract between the authority and its bondholders and for the payment of which other monies pledged to secure such bonds are not available. Any income or interest earned by, or increment to, a community hospital capital reserve fund due to the investment thereof shall be used by the authority for the purposes of such community hospital capital reserve fund.

(ii) The authority shall not issue bonds which are secured by a community hospital capital reserve fund at any time if the maximum amount of principal and interest maturing or becoming due in a succeeding calendar year on such bonds then to be issued and on all other outstanding bonds of the authority which are secured by such community hospital capital reserve fund will exceed the amount of such community hospital capital reserve fund at the time of issuance unless the authority, at the time of issuance of such bonds, shall deposit in such fund from the proceeds of the bonds so to be issued, or otherwise, an amount which, together with the amount then in such fund, will be not less than the maximum amount of principal and interest maturing and becoming due in any

succeeding calendar year on such bonds then to be issued and on all other outstanding bonds of the authority which are secured by such community hospital capital reserve fund.

(iii) To assure the continued operation and solvency of the authority for the carrying out of the public purposes of this act, provision is made in paragraph (i) for the accumulation in a community hospital capital reserve fund of an amount equal to the maximum amount of principal and interest maturing and becoming due in any succeeding calendar year on all outstanding bonds which are secured by such community hospital capital reserve fund. In order further to assure such maintenance of a community hospital capital reserve fund there shall be annually appropriated and paid to the authority for deposit in such community hospital capital reserve fund such sum, if any, as shall be certified by the executive director of the authority to the governor as necessary to restore such community hospital capital reserve fund to an amount equal to the maximum amount of principal and interest maturing and becoming due in any succeeding calendar year on the outstanding bonds which are secured by such community hospital capital reserve fund. The executive director of the authority shall annually, on or before December 1, make and deliver to the governor his certificate stating the amount, if any, required to restore a community hospital capital reserve fund to the amount aforesaid and the amount so stated, if any, shall be appropriated and paid to the authority during the then current fiscal year of the commonwealth.

(iv) For the purposes of this subsection in computing the amount of a community hospital capital reserve fund, securities in which all or a portion of such fund are invested shall be valued at par, or if purchased at less than par, at their cost to the authority, unless otherwise provided in the resolution, trust agreement or indenture authorizing the issuance of bonds secured by the fund.

(v) For the purposes of this subsection, the amount of any letter of credit, insurance contract, surety bond, or similar financial undertaking available to be drawn upon and applied to obligations to which money in the community hospital capital reserve fund may be applied is deemed to be and shall be counted as money in said fund. For the purposes of this subsection, in calculating the maximum amount of interest due in the future on variable rate bonds or bonds with respect to which the interest rate is not at the time of calculation determinable, the interest rate shall be calculated at the maximum interest rate on such bonds or such lesser interest rate as shall be certified by the authority as an appropriate proxy for such variable or nondeterminable interest rate.”

(vi) Bonds secured by the community hospital capital reserve fund shall be issued by the authority

solely for the benefit of nonprofit community hospitals within the commonwealth licensed by the department of public health.

(vii) Notwithstanding any provision of this act to the contrary, no loan shall be made to a nonprofit community hospital by the authority from proceeds of bonds secured by a community hospital capital reserve fund established under this paragraph unless: (a) the project to be financed by the loan has been approved by the secretary of health and human services; and (b) the loan and the issuance and terms of the related bonds have been approved by the secretary of administration and finance. In connection with any loan to a nonprofit community hospital pursuant to this paragraph, the secretary of health and human services and the secretary of administration and finance may enter into an agreement with the authority and the nonprofit community hospital to (a) require that the nonprofit community hospital provide financial statements or other information relevant to the financial condition of the nonprofit community hospital and its compliance with the terms of the loan, (b) require that the nonprofit community hospital reimburse the commonwealth for any amounts the commonwealth transfers to the community hospital capital reserve fund under subparagraph (iii) to replenish the fund as a result of a loan payment default by the nonprofit community hospital, and (c) require compliance by the nonprofit community hospital or the authority with any other terms and conditions the secretaries may consider appropriate in connection with the loan.

(viii) When the authority notifies the secretary of administration and finance in writing that an institution eligible to use the authority under this paragraph is in default as to the payment of principal or interest on any bonds issued by the authority on behalf of such institution, or that the authority has reasonable grounds to predict that the institution will not be able to make a full payment when that payment is due, the secretary of administration and finance shall direct the comptroller to withhold any funds in the comptroller's custody that are due or payable to the institution until the amount of the principal or interest due or anticipated to be due has been paid to the authority or the trustee for the bondholders, or the authority notifies the secretary of administration and finance that satisfactory arrangements have been made for the payment of the principal and interest. Funds subject to withholding under this subparagraph include, but are not limited to, federal and state grants, contracts, allocations or appropriations.

(ix) If the authority further notifies the secretary of administration and finance in writing that no other arrangements are satisfactory, the secretary shall direct the comptroller to make available to the authority without further appropriation any funds withheld from the institution under subparagraph

(viii). The authority shall apply the funds to the costs incurred by the institution, including payments required to be made to the authority or trustee for any bondholders of debt service on any bonds issued by the authority for the institution or required by the terms of any other law or contract to be paid to the holders or owners of bonds issued on behalf of the institution upon failure or default, or reasonable expectation of failure or default, of the institution to pay the principal or interest on its bonds when due.

(x) Concurrent with any notice from the authority to the secretary of administration and finance under this paragraph (g), the authority may notify any other agency, department or authority of state government that exercises regulatory, supervisory or statutory control over the operations of the institution. Upon notification, the agency, department or authority shall immediately undertake reviews to determine what action, if any, that agency, department or authority should undertake to assist in the payment by the institution of the money due or steps that the agencies of the state other than the comptroller or the authority should take to assure the continued prudent operation of the institution or provision of services to the people served by the institution.

(xi) Notwithstanding any general or special law to the contrary, in the event that a nonprofit community hospital fails to reimburse the commonwealth for any transfers made by the commonwealth to the authority to replenish the community hospital capital reserve fund in accordance with subparagraph (iii) within 6 months of any such transfer and as otherwise provided in accordance with the terms of the agreement among the nonprofit community hospital, the authority and the commonwealth authorized under subparagraph (vii), the secretary of administration and finance may, in her sole discretion, direct the comptroller to withhold any funds in the comptroller's custody that are due or payable to the nonprofit community hospital has failed to pay to the commonwealth to reimburse the commonwealth for any such transfers. All contracts issued by the group insurance commission, the health insurance connector authority and MassHealth to any third party for the purposes of providing health care insurance paid for by the commonwealth shall provide that, at the direction of the secretary of administration and finance, the third party shall withhold payments to a nonprofit community hospital which fails to reimburse the commonwealth in accordance with the agreement authorized under subparagraph (vii) and shall transfer the withheld amount to the commonwealth. Any such withheld amounts shall be considered to have been paid to the nonprofit community hospital for all other purposes of law, and the nonprofit community hospital shall be considered to have reimbursed the commonwealth for all or a portion of any such transfers to the community hospital capital reserve fund for purposes of the agreement authorized under

subparagraph (vii).

(xii) For purposes of this paragraph a community hospital excludes any hospital where the ratio of the number of physician residents-in-training to the number of inpatient beds exceeds

0.25.

SECTION 2. Section 2-12 of said chapter 614 of the acts of 1968, as amended, is hereby further amended by striking out the last sentence and inserting in place thereof the following: -

“Except as otherwise permitted pursuant to Section 2-10(g) of this act, the issuance of revenue bonds under the provision of this act shall not directly or indirectly or contingently obligate the commonwealth or any political subdivision thereof to levy or to pledge any form of taxation whatever therefore or to make any appropriation of their payment.”