

# CALIFORNIA HEALTH FACILITIES FINANCING AUTHORITY

## Executive Summary - HELP II Loan Program County of Modoc for the benefit of Modoc Medical Center

June 24, 2010

### Background

As mentioned in the staff report accompanying item 13 on the agenda, representatives from the Department of Finance (DOF), the State Treasurer's Office (STO) and the State Controller's Office (SCO) were recently approached by representatives from the County of Modoc (County) and Modoc Medical Center (MMC) to discuss their pressing financial needs.

The County and MMC appealed to the DOF, the STO and the SCO to temporarily assist the County with its need to immediately restore (as soon as possible pursuant to SCO directive) approximately \$12.5 million in restricted funds to the County treasury. Apparently, the County improperly transferred this sum (and additional sums which have since been restored) to MMC over a period of roughly ten years to finance, in part, operating deficits at MMC. It appears Generally Accepted Accounting Principles (GAAP) were violated when the County allowed MMC to use restricted funds not designated for MMC's use. This violation has contributed to MMC's existing negative cash balances and why, in part, MMC is making its own request for a HELP II loan from the Authority.

Presently, the County is under audit by the SCO. Auditors are preparing to release a revised FY 2006/2007 within the next month and revised FY 2007/2008 and 2008/2009 audits shortly thereafter. The County is simultaneously working to issue a Certificate of Participation (COP) in the amount of approximately \$14 million in August 2010. If successful, some of the COP proceeds may be used to assist MMC with their financial needs. The County Board of Supervisors recently voted to suspend all future funding to the hospital in light of the County's current \$12.5 million deficit. The Board of Supervisors passed a resolution requiring MMC to operate in the black on an on-going basis.

Though MMC has improved efficiencies in their own operations over the last ten months and appears to be operating in the black, MMC anticipates the County may intercept hospital revenues to pay immediate County expenses once the \$12.5 million has been replenished. MMC seeks the maximum amount permitted under the HELP II loan program in the amount of \$750,000 to assist them with their immediate financial needs (roughly \$2.5 million) for the next couple of months. At a minimum, MMC reports that it needs funding for accounts payable and payroll in order to stay in operation.

In August 2010, residents of the County will vote on a measure that, if passed, would allow MMC to become a district hospital. County counsel indicates that formation of a district hospital would formally separate MMC from the County and potentially, free MMC of the debt currently owed to the County. Nevertheless, according to County counsel, all legal responsibility for any debt issued by the Authority to the County on behalf of MMC would flow to the new district, just as any MMC assets would flow to the new district.

MMC is vital to the roughly 10,000 residents of Modoc County. MMC is an acute care facility and the largest medical facility within a three hour drive of the City of Alturas. As of October 2008, MMC was designated as a Critical Access Hospital. Other nearby facilities are located in Klamath Falls, Oregon, and Reno, Nevada, but access for both require travel over major

mountain ranges which are often closed during the winter months. In addition to providing emergency medical services, MMC also operates a rural health clinic and skilled nursing facility.

MMC is currently the second largest employer in the County with approximately 170 full and part time employees. In March 2010, the unemployment rate for Modoc County was 17.7% as compared to the State average of 12.6% and the national average of 9.6%. The poverty rate (in 2007) was 19.6% compared to the State average of 12%.

**Financial Analysis**

MMC’s operating results over the three-year review period were negative – please see the below ratios for a sense of their situation. Generally, MMC’s balance sheet appears to indicate the need for emergency cash to help sustain operations. Though MMC has minimal debt, MMC will be servicing two five year term debts (with a possible interest rate of 11%) to Medicare for approximately \$1.7 million in overpayments made by Medicare to the County for services. According to MMC, this ongoing debt service contributes to their immediate need for operational support.

MMC’s management reports that it has developed a plan to recover from the economic downturn and to stabilize the relationship between revenue and expenses. Indeed, interim numbers for the last ten months (through April) appear to reflect MMC is now operating in the black. MMC appears to have benefited from leadership of an interim chief executive officer whose contract expires at the close of FY 2010 (June 30). The Authority recently learned this contract has not been extended. The continued leadership and path of improvement for MMC is thus uncertain.

MMC and the County have tentatively agreed to secure the proposed HELP II loan request for emergency funding with an intercept of MMC’s Medi-Cal reimbursement payments and potentially with a lien against the County facility (though the Authority awaits confirmation on the latter of these issues). The Authority’s staff is in the process of evaluating the intercept option with the Department of Health Care Services (DHCS).

**Financial Ratios:**

	<b>Proforma (b)</b>	<b>As of June 30 (a)</b>		
		<b>2009 (draft)</b>	<b>2008</b>	<b>2007</b>
Debt Service Coverage (x)	<b>(3.43)</b>	<b>(3.82)</b>	<b>(5.42)</b>	<b>(10.66)</b>
Debt/Unrestricted Net Assets (x)	<b>(0.09)</b>	<b>(0.02)</b>	<b>(0.06)</b>	<b>(1.23)</b>
Margin (%)		<b>(24)</b>	<b>(23)</b>	<b>(32)</b>
Current Ratio (x)		<b>(10.22)</b>	<b>(5.52)</b>	<b>2.11</b>

(a) MMC is currently being audited by the State Controller's Office. FY 2009, FY 2008, and FY 2007 figures are subject to change.

(b) Recalculates 2009 draft audited results to include the impact of this proposed financing.

**Outstanding Issues**

Staff will continue to work on a number of outstanding issues, foremost of which is to continue the review of the complex fiscal challenges faced by MMC and the County to better understand the possible short term and long term consequences of extending a HELP II loan to the County on behalf of MMC. Staff will also focus on appropriate security measures and the remedies the Authority might have in the face of a possible bankruptcy by the County/MMC, transition from a County operated facility to a district hospital, or continuation of the status quo County operation.