

**CHFFA BOND FINANCING PROGRAM  
EXECUTIVE SUMMARY**

<p><b>Applicant:</b> Stanford Hospital and Clinics ("SHC") 300 Pasteur Drive, MC 5554 Stanford, CA 94305 Santa Clara County</p>	<p><b>Amount Requested:</b> \$175,000,000 <b>Date Requested:</b> April 29, 2010 <b>Requested Loan Term:</b> Up to 40 years <b>Resolution Number:</b> 354</p>																
<p><b>Projects Sites:</b> Same as above <b>Facility Types:</b> Acute care Hospital and outpatient care <b>Prior Borrower:</b> Yes (date of last issue 2008)</p>																	
<p><b>Background:</b> SHC operates a licensed acute care hospital and a cancer center in Palo Alto, California, along with numerous outpatient physician clinics in the San Francisco Bay Area, in community settings, and in association with regional hospitals.</p>																	
<p><b>Use of Proceeds:</b> Bond proceeds will be used to current refund previously issued AMBAC/FSA insured fixed rate CHFFA 1998 Series B Bonds. The original bond proceeds were used to refinance prior obligations and finance a new ambulatory care center.</p>																	
<p><b>Type of Issue:</b> Negotiated public offering with fixed rate bonds <b>Credit Enhancement:</b> None <b>Expected Credit Rating:</b> A1/A+/AA- Moody's/S&amp;P/Fitch <b>Financing Team:</b> See Exhibit 1 (page 12)</p>																	
<p><b>Financial Overview:</b> SHC's income statement appears to exhibit solid operating results with positive net income over the review period along with continued revenue growth. SHC's balance sheet also appears solid with strong debt service coverage and growing net assets. Since this is a refunding, SHC's operating proforma debt service coverage remains solid at a 4.47x.</p>																	
<p><b>Net Patient Service Revenue</b> (FYE August 31, 2009):</p> <table style="width: 100%; border-collapse: collapse;"> <thead> <tr> <th style="text-align: left;"><u>Payor Source</u></th> <th style="text-align: right;"><u>Percent</u></th> </tr> </thead> <tbody> <tr> <td>Managed Care – Discounted Fee for Services</td> <td style="text-align: right;">65%</td> </tr> <tr> <td>Medicare</td> <td style="text-align: right;">20%</td> </tr> <tr> <td>Self pay and other</td> <td style="text-align: right;">9%</td> </tr> <tr> <td>Related party</td> <td style="text-align: right;">3%</td> </tr> <tr> <td>Medi-cal</td> <td style="text-align: right;">2%</td> </tr> <tr> <td>Managed Care Capitation</td> <td style="text-align: right;"><u>1%</u></td> </tr> <tr> <td>Total</td> <td style="text-align: right;"><u>100%</u></td> </tr> </tbody> </table>		<u>Payor Source</u>	<u>Percent</u>	Managed Care – Discounted Fee for Services	65%	Medicare	20%	Self pay and other	9%	Related party	3%	Medi-cal	2%	Managed Care Capitation	<u>1%</u>	Total	<u>100%</u>
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<p>*The financing costs are preliminary and are subject to change.</p>																	
<p><b>Legal Review:</b> No information was disclosed to question the financial viability or legal integrity of the applicant.</p>																	
<p><b>Staff Recommendation:</b> Staff recommends the Authority approve Resolution Number 354 in an amount not to exceed \$175,000,000 for Stanford Hospital and Clinics subject to a bond rating of at least an "A" rating by a nationally recognized rating agency. Macias Gini &amp; O'Connell, LLP., the Authority's financial analyst, has reviewed all relevant financial documentation submitted by Stanford Hospital and Clinics and has advised of its concurrence with the Authority's staff recommendations.</p>																	

**STAFF SUMMARY AND RECOMMENDATION**

**Stanford Hospital and Clinics (“SHC”)**

April 29, 2010

Resolution Number: 354

**I. GUIDELINE EXCEPTIONS:**

The Authority adopted bond issuance guidelines in September 2000 which included a minimum debt service coverage of 1.25x. The Authority acknowledged each financing must be reviewed individually and exceptions to these guidelines may be considered. SHC’s Master Indenture dated December 1, 1990, which governs all of its public debt issued since that date, imposes a minimum 1.10x debt service coverage ratio. In consideration of the historical and current financial strength of SHC (its current operating proforma debt service coverage is a healthy 4.47x), staff recommends waiving the minimum debt service coverage requirement ratio of 1.25x thus, allowing SHC to continue to operate in compliance with its existing Master Indenture covenant. The Authority has granted such exceptions to other borrowers with similar Master Indenture covenants on several previous occasions and most notably within the last 24 months.

**II. PURPOSE OF FINANCING:** The refunding will release SHC from certain covenants related to AMBAC/FSA insurance. Additionally, SHC expects to achieve approximately \$5 million in present value savings from the refunding.

***Refunding CHFFA 1998 Series B Bonds* ..... \$170,000,000**

SHC seeks to refund on a current basis<sup>1</sup> all or a portion of its outstanding previously issued AMBAC/FSA insured fixed rate CHFFA 1998 Series B Bonds. The original bond proceeds were used to refinance prior obligations and finance a new ambulatory care center.

***Financing Costs* ..... \*5,000,000**

**Total Uses of Funds..... \$175,000,000**

\*The financing costs are preliminary and are subject to change.

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<sup>1</sup> A current refunding occurs when the (old) refunded issue is retired within 90 days after the refunding (new) issue is sold. Proceeds of the refunding issue are used to purchase the refunded bonds from investors at the maturity date or at a call date prior to the maturity date.

### III. FINANCIAL STATEMENTS AND ANALYSIS:

**Stanford Hospital & Clinics**  
**Consolidated Statement of Activities (\$000's)**

	For the Year Ended August 31,		
	2009	2008	2007
<b>Operating revenues:</b>			
Net patient service revenue	\$ 1,741,856	\$ 1,578,755	\$ 1,459,744
Premium revenue	22,960	20,755	20,205
Other revenue	57,666	51,225	48,788
Net assets released from restriction used for operations	5,195	4,816	4,379
Total operating revenue	<u>1,827,677</u>	<u>1,655,551</u>	<u>1,533,116</u>
<b>Operating expenses:</b>			
Salaries, wages & benefits	787,035	714,856	638,789
Professional fees	22,842	24,713	23,323
Supplies	265,139	235,542	224,996
Purchased Services	434,257	385,273	361,475
Provision for doubtful accounts, net	53,859	51,578	44,733
Depreciation and amortization	73,876	65,812	44,287
Interest	37,921	26,334	22,988
Other	139,385	120,382	99,889
Expenses recovered from related parties	(81,317)	(74,184)	(65,437)
Total operating expenses	<u>1,732,997</u>	<u>1,550,306</u>	<u>1,395,043</u>
Income from operations	94,680	105,245	138,073
Interest and investment income	3,814	21,824	11,108
(Decrease) increase in value of University managed pools	(146,481)	9,720	100,394
Interest rate swaps mark to market adjustments	(48,338)	(42,600)	(1,302)
Loss on extinguishment of debt	-	(17,855)	-
(Deficiency) excess of revenue over expenses	<u>(96,325)</u>	<u>76,334</u>	<u>248,273</u>

(continued)

**Stanford Hospital & Clinics**  
**Consolidated Statement of Activities (\$000's)**

	For the Year Ended August 31,		
	2009	2008	2007
Other changes in unrestricted net assets:			
Transfer to Stanford University	(8,049)	(7,670)	(6,776)
Transfer from (to) Lucile Salter Packard Children's Hospital	288	(2,808)	(14,352)
Change in net unrealized gains (losses) of investments	237	227	(278)
Net assets released from restriction used for:			
Purchase of property and equipment	460	599	1,360
Change in minimum pension liability	(75,101)	(2,212)	3,593
Change in fair value of interest and rate swaps	-	-	438
Decrease (increase) in unrestricted net assets before cumulative effect of change in accounting principle	(178,490)	64,470	232,258
Income (loss) from discounted operations	-	890	(23,869)
Cumulative effect of change in accounting principle	-	-	11,613
Decrease (increase) in unrestricted net assets	(178,490)	65,360	220,002
Change in temporarily restricted net assets			
Transfers from Stanford University	15,167	-	-
Contributions	5,606	8,508	31,240
Investment income	98	586	569
Income and gains on University managed pools	(1,415)	1,161	2,511
Net assets released from restriction for:			
Operations	(5,195)	(4,816)	(4,379)
Purchase of property and equipment	(460)	(599)	(1,360)
Increase in temporarily restricted assets	13,801	4,840	28,581
Changes in permanently restricted net assets:			
Contributions	-	981	1,920
Increase in permanently restricted net assets	-	981	1,920
<b>(Decrease) increase in net assets</b>	<b>(164,689)</b>	<b>71,181</b>	<b>250,503</b>
Net assets, beginning of the period	971,695	900,514	650,011
Net assets, end of period	\$ 807,006	\$ 971,695	\$ 900,514

**Stanford Hospital & Clinics**  
**Consolidated Statement of Financial Position (\$000's)**

	As of August 31,		
	<u>2009</u>	<u>2008</u>	<u>2007</u>
<b>Assets:</b>			
Current assets:			
Cash and cash equivalents	\$ 331,502	\$ 268,869	\$ 39,278
Assets limited as to use, held by trustee	280	504	2,333
Patient accounts receivable, net	253,299	240,989	215,953
Other receivables	11,925	9,912	15,346
Inventories	18,725	20,420	20,636
Prepaid expenses and other	8,553	8,428	5,833
Total current assets	<u>624,284</u>	<u>549,122</u>	<u>299,379</u>
Investments	76,584	60,068	44,674
Investments in University managed pools	533,518	688,644	815,970
Assets limited to use, net current portion	48,828	163,246	331,607
Property and equipment, net	840,955	706,700	511,421
Other Assets	60,715	63,398	83,898
Total Assets	<u>\$ 2,184,884</u>	<u>\$ 2,231,178</u>	<u>\$ 2,086,949</u>
<b>Liabilities and Net Assets:</b>			
Current liabilities:			
Accounts payable & accrued liabilities	\$ 129,750	\$ 143,723	\$ 101,385
Accrued salaries & related benefits	91,835	82,819	72,874
Due to related parties	33,840	23,091	22,252
Third-party payer settlements	19,433	14,704	14,526
Current portion of long-term debt	8,713	7,877	8,033
Debt subject to short-term remarketing arrangements	266,764	249,414	-
Self-insurance reserves	18,303	20,008	21,579
Total current liabilities	<u>568,638</u>	<u>541,636</u>	<u>240,649</u>
Self-insurance reserves, net of current portion	90,811	80,222	86,866
Other long-term liabilities	96,244	54,389	18,217
Pension Liability	65,188	-	-
Long term debt, less current portion	556,997	583,236	840,703
Total liabilities	<u>1,377,878</u>	<u>1,259,483</u>	<u>1,186,435</u>

(continued)

**Stanford Hospital & Clinics**  
**Consolidated Statement of Financial Position (\$000's)**

	As of August 31,		
	2009	2008	2007
Net assets:			
Unrestricted	730,563	909,053	843,693
Temporarily restricted	69,951	56,150	51,310
Permanently Restricted	6,492	6,492	5,511
Total net assets	<u>807,006</u>	<u>971,695</u>	<u>900,514</u>
Total liabilities and net assets	<u>\$ 2,184,884</u>	<u>\$ 2,231,178</u>	<u>\$ 2,086,949</u>

**Financial Ratios:**

	As of August 31,		
	2009	2008	2007
	<b>Proforma (a)</b>		
	<b>FYE August 31, 2009</b>		
Operating debt service coverage (x)	4.47	4.47	6.65
Debt/Unrestricted Net Assets (x)	1.14	1.14	0.93
Operating margin (%)	5.18	6.36	9.01
Current Ratio (x)	1.10	1.01	1.24

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

## **SHC's Management Financial Discussion (Appendix A Disclosures)**

### Historical Performance

For the three years ended August 31, 2009, SHC continued to strengthen its financial position to support investments in the facilities and systems required to remain at the forefront of medicine and to be the provider of choice for complex care in the communities it serves. The cumulative Income from Operations before investment income for the three years ended August 31, 2009 was \$338 million. Cumulative Investment Income for the three years ended August 31, 2009 was \$379 thousand. The cumulative increase in Net Assets for the three years ended August 31, 2009 was \$157 million. Cumulative capital expenditures for the three years ended August 31, 2009 were \$614 million.

### Financial Performance in Fiscal Year 2009

Despite income from operations of \$95 million, the SHC's net assets decreased \$165 million to \$807 million at August 31, 2009. In 2009, SHC generated a \$96 million deficiency of revenues over expenses compared to an excess of revenues over expenses of \$76 million in 2008. Investment income and change in value of Stanford University managed pools decreased by \$174 million, resulting in a loss of \$143 million due to continued negative returns on the SHC investments held through Stanford University.

Net patient revenues increased by 10% to \$1.7 billion in fiscal year 2009. Inpatient revenues, which make up 54% of total revenue, grew by 9% on continuing increases in patient volume. Outpatient revenues increased approximately 12%, accounting for 46% of total revenue.

### Financial Performance in Fiscal Year 2008

SHC's net assets increased \$71 million to \$972 million at August 31, 2008. In fiscal year 2008, the SHC generated \$76 million in excess revenues over expenses compared to \$248 million in fiscal year 2007. Investment income and change in value of Stanford University managed pools decreased to \$32 million, down from \$112 million as a result of negative returns on the SHC investments held through Stanford University.

During fiscal year 2008, SHC sold certain assets and liabilities of its clinical laboratory testing outreach business for \$30 million, plus the assumption of several property leases valued at approximately \$2 million in aggregate. The sales proceeds, net of sales expense and exit costs, were \$21 million.

Net patient revenues increased by 8% to \$1.6 billion in fiscal year 2008. Despite significant capacity limitations, total patient days increased by 2%. Patient discharges were flat compared to fiscal year 2007. Inpatient revenues, which make up 55% of total revenue, grew by 11% on continuing increases in patient volume and favorable negotiations of payor contracts. Outpatient revenues increased approximately 4%, accounting for 45% of total revenues.

### Financial Performance in Fiscal Year 2007

SHC's net assets increased \$251 million to \$901 million at August 31, 2007. In fiscal year 2007, SHC generated \$248 million in excess revenues over expenses, compared to \$169 million in fiscal year 2006. Investment income increased to \$112 million, up from \$54 million as a result of continued excellent returns on SHC's investments held through Stanford University.

Prior to fiscal year 2007, Stanford University had assigned to SHC the right to all revenue related to pediatric and obstetric practices of the School of Medicine faculty. Effective September 1, 2007, Lucile Packard Children's Hospital at Stanford assumed the right to these revenues. In fiscal year 2006 the pediatric and obstetric practices had revenue of \$61 million. Payment for physicians' services related to these services was \$48 million.

Fiscal year 2007 revenues and expenses are compared to fiscal year 2006 excluding the pediatric and obstetric practice services. Income from operations before investment income was \$138 million for the fiscal year 2007, up 20% from \$115 million in fiscal year 2006. Net patient revenues grew 5% to \$1.5 billion in fiscal year 2007, compared to \$1.4 billion in fiscal year 2006. Both patient acuity and volumes slightly increased for the year. Total patient days increased 2%, and patient discharges were up 3% in fiscal year 2007 over fiscal year 2006. Inpatient revenues, which make up 53% of the total revenues, grew by 7% despite existing capacity limitations. Outpatient revenues increased approximately 12%, accounting for 47% of total revenues.

#### **IV. BACKGROUND:**

SHC is a principal teaching affiliate of the Stanford University School of Medicine and provides primary and specialty health services to adults, including cardiac care, cancer treatment, solid organ transplantation services, orthopedics and neurosciences services. SHC, together with Lucile Salter Packard Children's Hospital at Stanford, operates the clinical settings through which the Stanford University School of Medicine (the "School of Medicine") educates medical and graduate students, trains residents and clinical fellows, supports faculty and community clinicians and conducts medical and biological sciences research.

The principal clinical facilities of SHC are the Stanford Hospital, a 613-licensed bed tertiary, quaternary and specialty hospital (the "Hospital"), and the primary, specialty and sub-specialty clinics (the "Clinics" and, together with the Hospital, the "Hospital and Clinics") in which the medical faculty of the School of Medicine provide clinical services. The Hospital and a majority of the Clinics are located on the campus of Stanford University adjacent to the School of Medicine in Palo Alto, California. Other Clinics are located elsewhere on the campus, nearby off-campus and in neighboring communities.

#### **Licensure, Certification and Accreditation**

The California Department of Health Services licenses the Hospital as a general acute care facility. SHC is accredited by The Joint Commission which conducted its last on-site survey in April 2007.

## **Governance**

Pursuant to the bylaws of SHC, the Board of Directors (the “Board”) is comprised of six ex-officio directors and between seven and twenty elected directors as determined by Stanford University. Currently, the Board consists of six ex-officio directors and nineteen directors elected by Stanford University. Elected directors serve for a three-year term commencing on January 1 or on such other date as specified by Stanford University. There are three classes of directors, equally sized to the extent possible, such that the terms of the directors in only one class expire in each year. Term limits were established in July 2001, at which time all previously appointed directors were re-elected. Elected directors may serve up to three consecutive 3-year terms.

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## V. UTILIZATION STATISTICS:

The following table shows utilization statistics of SHC for the fiscal years ended August 31, 2009, 2008 and 2007:

	<b>Fiscal Year Ended August 31,</b>		
	<b>2009</b>	<b>2008</b>	<b>2007</b>
Discharges			
Acute	22,909	22,075	22,063
Behavioral Health	900	797	865
Rehabilitation/Skilled Nursing	0 <sup>(1)</sup>	292	306
Total	<u>23,809</u>	<u>23,164</u>	<u>23,234</u>
Patient Days			
Acute	126,501	122,759	119,683
Behavioral Health	8,590	8,928	8,821
Rehabilitation/Skilled Nursing	0 <sup>(1)</sup>	3,736	4,409
Subtotal	<u>135,091</u>	<u>135,423</u>	<u>132,913</u>
Short Stay Outpatient	<u>6,126</u>	<u>6,620</u>	<u>6,581</u>
Total	<u>141,217</u>	<u>142,043</u>	<u>139,494</u>
Average Daily Census			
Acute	346.6	335.4	327.9
Behavioral Health	23.5	24.4	24.2
Rehabilitation/Skilled Nursing	0 <sup>(1)</sup>	10.2	12.1
Total	<u>370.1</u>	<u>370.0</u>	<u>364.2</u>
Average Length of Stay			
Acute	5.5	5.6	5.4
Behavioral health	9.5	11.2	10.2
Rehabilitation Skilled/Nursing	0 <sup>(1)</sup>	12.8	14.4
Average	<u>5.7</u>	<u>5.8</u>	<u>5.7</u>
Case Mix Index	<u>1.98</u>	<u>1.96</u>	<u>1.89</u>
Emergency Room Visits	<u>48,840</u>	<u>46,156</u>	<u>44,078</u>
Short Stay Outpatient Procedures	<u>24,192</u>	<u>21,940</u>	<u>21,711</u>
Other Outpatient Visits	<u>263,733</u>	<u>256,358</u>	<u>256,196</u>
Surgeries			
Inpatient	11,514	11,453	11,184
Outpatient	<u>11,830</u>	<u>11,179</u>	<u>10,712</u>
Total	<u>23,344</u>	<u>22,632</u>	<u>21,896</u>

<sup>(1)</sup> Reflects suspension of rehabilitation services as of August 31, 2008.

## **VI. OUTSTANDING DEBT:**

As of fiscal year ending August 31, 2009, SHC has approximately \$824 million in outstanding long-term debt, all of which is Authority debt. With this bond financing, SHC outstanding debt is not expected to increase since SHC is refunding existing debt.

## **VII. DUE DILIGENCE:**

Due diligence has been completed with regard to the following items:

- **Section 15438.5(a) of the Act (Savings Pass Through):** SHC properly completed and submitted the “Pass-Through Savings Certification,” in addition to a narrative explaining how it intends to pass through savings.
- **Section 15491.1 of the Act (Community Service Requirement):** SHC properly completed and submitted this certification and indicated that Medi-Cal and Medicare patients are accepted.
- **Compliance with Seismic Regulations:** SHC properly completed and submitted a description of its seismic requirements.
- **Religious Due Diligence.**
- **Legal Review.**

## **EXHIBIT 1**

### **Stanford Hospital and Clinics Financing Team\***

Corporation Counsel: Ropes & Gray LLP  
Bond Counsel: Orrick, Herrington & Sutcliffe LLP  
Senior Underwriter: Morgan Stanley & Company Incorporated  
Co-Underwriter: To be determined  
Underwriters' Counsel: Sidley Austin LLP  
Bond and Master Trustee: Wells Fargo Bank, National Association or  
Union Bank, N.A. or The Bank of New York  
Mellon Trust Company N.A. or Deutsche Bank  
National Trust Company.  
Trustee's Counsel: To be determined

\* SHC is in the process of selecting their financing team.