

CALIFORNIA HEALTH FACILITIES FINANCING AUTHORITY

(CHFFA)

EXECUTIVE SUMMARY

<p>Applicant: Valley Health Team, Inc. (VHT) 21890 Colorado Avenue San Joaquin, CA 93660 (Fresno County)</p> <p>Project site: Kerman Health Center, 449 S. Madera Avenue, Kerman, CA 93630</p> <p>Facility Types: Primary Care Clinic</p>	<p>Amount Requested: \$2,500,000</p> <p>Requested Loan Term: 24 years</p> <p>Date Requested: December 6, 2007</p> <p>Resolution Number: 324</p>																																				
<p>Background: Valley Health Team, Inc. is a California private, not-for-profit corporation with over 30 years of experience in providing a comprehensive range of health services to the indigent, low-income, and multi-cultural residents of the rural communities of western Fresno County and the outlying rural areas.</p>																																					
<p>Uses of Bond Proceeds: Bond proceeds will be used to refund \$710,000 in bonds and refinance \$612,000 in bank loans. The bond refunding will result in a net present value savings of \$41,201 and the bank loan refinancing will result in an estimated interest savings of \$53,921 over the life of the loans. The remaining bond proceeds will be used to relocate, renovate, furnish, equip, and purchase information technology (IT) for the Kerman Health Center.</p>																																					
<p>Type of Issue: Negotiated public offering with a fixed interest rate</p> <p>Credit Enhancement: Cal-Mortgage Insurance – Approved at November 8, 2007 meeting</p> <p>Expected Credit Rating: A+ (Fitch /S&P) based on Cal-Mortgage Insurance rating</p> <p>Senior Underwriter: Altura, Nelson & Co., Incorporated</p> <p>Bond Counsel: Quint and Thimmig LLP</p>																																					
<p>Financial Overview: VHT is currently operating well as a result of their new management’s cost cutting and service expansion measures to encourage financial recovery. The balance sheet reflects potential growth for VHT during its management transition. The proposed financing will reduce overall annual debt payments.</p>																																					
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<p>Legal Review: VHT disclosed four potential legal issues in the Application. These issues were determined not to be material to this financing and do not question the financial viability or legal integrity of the Applicant. (See Due Diligence page 9)</p>																																					
<p>Staff Recommendation: Staff recommends the Authority approve a Resolution in an amount not to exceed \$2,500,000 for Valley Health Team, Inc. subject to financing terms acceptable to the Authority and final Cal-Mortgage Insurance commitment.</p>																																					

STAFF SUMMARY AND RECOMMENDATION

Valley Health Team, Inc. (“VHT”)

December 6, 2007

Resolution Number: 324

I. PURPOSE OF FINANCING:

Bond proceeds will be used to renovate, equip, and furnish the 3,200 square foot Kerman Health Center (KHC) facility owned by VHT. This space will then be used to relocate primary care services from a nearby leased facility. In addition, VHT will use the remaining proceeds to refund approximately \$1.32 million in existing debt, consisting of about \$710,000 in Certificates of Participation and two bank loans totaling about \$612,000. Cal-Mortgage will be providing credit enhancement to the proposed bonds.

Construction/Renovation \$260,000

The renovations include expanding the waiting room and increasing exam rooms from 5 to 10. This will accommodate more patients and allow KHC to offer additional programs and services. The renovation began in 2006, but was delayed due to a lack of funding, to date construction is approximately 65% complete.

Refund/Refinance Existing Debt 1,322,000

Local Medical Facilities Financing Authority \$710,000

The Local Medical Facilities Financing Authority 1990 Certificates of Participation was used to acquire land and construct a 7,300 square foot facility in San Joaquin. The original amount of the serial bonds was \$10,385,000, with an interest rate of with maturities from 2009 to 2020. The net present value savings resulting from this refunding is \$41,201 over the life of the bonds.

United Security Bank Loans \$612,000

One of the United Security Bank loans (balance of \$347,000) was used to purchase the KHC, renovate the 1990 project facility, construct VHT’s Mobile Transportation Building, and purchase additional property. The other United Security Bank Loan (balance of \$265,000) was used to complete the renovations to the KHC. Refinancing these two loans, which each have a fixed interest rate of 7.75% , will result in an estimated interest savings of \$53,921 over the life of the loans.

Purchase Equipment..... 400,000

Items purchased will include an X-ray machine furniture, telephones, and medical equipment. An additional \$165,000 will be used to purchase Mega West Practice Management System software and hardware to support the new system.

Debt Service Reserve 196,625

Financing Costs		242,350
<i>Cost of issuance</i>	<i>\$101,734</i>	
<i>Underwriter's discount.....</i>	<i>24,585</i>	
<i>Bond Insurance</i>	<u><i>116,031</i></u>	
Contingency		291,802
Total Uses of Funds.....		<u>\$2,712,777</u>

Structure of Financing and Terms:

- Negotiated public offering with serial and term bond maturities.
- Fixed interest rates.
- 24-year term with maturities from 2008 to 2031
- Credit enhancement–Cal-Mortgage Insurance.
- Expected Credit Rating: A + (S&P), based on Cal-Mortgage Insurance.
- Debt Service Reserve Fund.
- Contractual obligation to repay, including gross revenue pledge.
- Financial covenants acceptable to the Authority.

II. FINANCIAL STATEMENTS AND ANALYSIS:

Valley Health Team, Inc. Statement of Activities (Unrestricted)

	For the year ended June 30		
	2007	2006	2005
Revenue			
Net patient revenues	\$ 3,253,562	\$ 3,279,555	\$ 3,404,473
Grant revenue	971,590	906,957	914,247
Other operating income	20,159	8,027	14,174
Interest income	12,871	10,600	5,286
Rent income	5,204	5,554	5,554
Total support and revenue	<u>4,263,386</u>	<u>4,210,693</u>	<u>4,343,734</u>
Expenses			
Salaries and wages	2,074,627	2,328,226	2,545,378
Employee benefits	447,909	427,989	459,086
Medical, dental and laboratory consulting fees	480,432	273,419	76,718
Accounting, legal and other outside fees	295,380	80,497	53,412
Medical and office supplies	149,906	278,447	251,094
Repairs and maintenance	43,354	52,433	103,666
Building and equipment rent	49,214	58,484	67,737
Utilities and telephone	147,754	154,110	147,323
Insurance	39,661	35,048	32,533
Travel CME and other education	18,869	26,645	50,918
Postage	6,721	18,521	29,200
Dues and subscriptions	21,835	27,990	33,074
Advertising and marketing	10,281	8,826	6,870
Interest	96,443	104,841	100,481
Depreciation and amortization	134,155	143,053	189,575
Provision for bad debts	214,777	205,687	171,781
Other operating expenses	24,167	27,987	47,168
Total expenses	<u>4,255,485</u>	<u>4,252,203</u>	<u>4,366,014</u>
Change in unrestricted net assets before extraordinary item	7,901	(41,510)	(22,280)
Extraordinary loss on disposal	(334,250)	-	-
Change in unrestricted net assets	(326,349)	(41,510)	(22,280)
Unrestricted net assets at beginning of year	1,470,042	1,511,552	1,533,832
Unrestricted net assets at end of year	<u>\$ 1,143,693</u>	<u>\$ 1,470,042</u>	<u>\$ 1,511,552</u>

Valley Health Team, Inc.
Statement of Financial Position

	As of June 30,		
	2007	2006	2005
<u>Assets</u>			
Cash and cash equivalent	\$ 369,667	\$ 391,938	\$ 396,573
Assets limited as to use to meet current obligations	52,868	49,378	50,133
Patient accounts receivable	394,799	262,016	308,093
Grant and other receivables	71,216	47,398	38,328
Estimated third-party payor settlements	32,554	139,259	74,817
Inventories	17,613	17,511	17,114
Prepaid expenses and other current assets	30,282	11,337	25,025
Total Current Assets	<u>968,999</u>	<u>918,837</u>	<u>910,083</u>
Assets limited as to use	87,251	78,510	99,710
Property and equipment, net	2,165,320	2,038,680	2,105,284
Bond issuance costs, net of accumulated amortization	18,351	19,623	20,895
Total Assets	<u><u>3,239,921</u></u>	<u><u>3,055,650</u></u>	<u><u>3,135,972</u></u>
<u>Liabilities & Net Assets</u>			
Accounts payable and other accrued expenses	\$ 280,198	\$ 55,651	\$ 26,756
Accrued payroll and related liabilities	183,351	109,100	110,499
Deferred revenue	28,500	20,000	20,000
Current maturities of debt borrowings	339,647	413,026	64,789
Total Current Liabilities	<u>831,696</u>	<u>597,777</u>	<u>222,044</u>
Debt borrowings, less current maturities	1,264,532	987,831	1,402,376
Total Liabilities	<u>2,096,228</u>	<u>1,585,608</u>	<u>1,624,420</u>
Unrestricted Net Assets	1,143,693	1,470,042	1,511,552
Total Liabilities & Net Assets	<u><u>\$ 3,239,921</u></u>	<u><u>\$ 3,055,650</u></u>	<u><u>\$ 3,135,972</u></u>

Financial Ratios:

	<u>Proforma (a)</u>			
Debt Service Coverage (x)	1.30	0.47	1.22	1.63
Debt/Unrestricted Net Assets (x)	1.85	1.85	0.97	0.98
Margin (%)		0.19	(0.99)	(0.51)
Current Ratio (x)		1.17	1.54	4.10

(a) Recalculates 2007 audited results to include the impact of this proposed financing.

Financial Discussion:

VHT is currently operating well under their new management's cost cutting and service expansion measures to encourage financial recovery.

VHT is in the process of a financial turnaround under the direction of a new Chief Executive Officer (CEO) and Chief Financial Officer (CFO) who both started in the first quarter of FY 2007. During the 2007 transitional period, VHT went through corporate restructuring, developed and implemented cost controls, and formulated a new recovery strategy. VHT expects to see significant improvement in their financial performance by FY 2008.

Revenues:

VHT revenues have been consistent over our review period, as VHT has received approximately \$4 million in total revenues each of the last three fiscal years. Although outpatient clinic visits have declined 17% from FY 2005 to FY2007, net revenue has remained steady at just over \$3 million over the same period primarily due to annual increases in MediCal PPS and MediCare rates. In addition, new billing staff hired in 2007 improved collection efforts which also added to revenues. According to the independent feasibility study completed for VHT, one full time physician and additional support staff will be added in January 2008. Additionally, patient visits are expected to increase to over 40,000 within the next five years, with projected net patient service revenues increasing to \$4.1 million by FY 2012.

Expenses:

In FY 2007, salary expense was reduced by 11% due to the elimination of administrative positions. Consequently, accounting, legal, and other outside consulting expenses increased due to executive management and administration consultants brought on after CEO, CFO, and other key personnel left VHT. The new CEO, who is currently working as a consultant, will be on contract until August 2009. Medical, dental, and laboratory consulting fees also increased due to medical, optometrist, and dental consultants used to fill in for clinician vacancies or vacation time. Mental health consultants were also brought on for the start of the Wellness Project that was later terminated. Over the review period, total expenses decreased by 2.5% due to cost reductions in usage of medical office supplies, less repairs and maintenance, and other operating expenses.

In FY 2006 and FY 2001 through 2005 audited financial statements were restated to increase the provision for bad debt by \$100,000 for each fiscal year. Financial statements for fiscal years 2004 and 2005 were restated to incorporate errors in calculating the bad debt allowance for patients account receivables. These revisions resulted in net losses for FY 2004, FY 2005, and FY 2006. Current management has implemented measures to improve the handling of collections and bad debts.

Extraordinary Item:

During FY 2006 and FY 2007, VHT developed plans to expand patient care services into a mental health program, called the Wellness Project. However, these plans were determined not to be feasible since VHT was unable to obtain the required financing to proceed with the project. As a result, \$334,250 of costs related to this abandoned project were capitalized as having no value and written off as an extraordinary item in the 2007 audit. Taking this into account, FY 2007 net income prior to the extraordinary item was positive at \$7,901.

The balance sheet reflects potential growth for VHT during its management transition. The proposed financing will reduce overall annual debt payments.

VHT's cash position is solid with \$369,667 in cash and cash equivalents as of June 30, 2007. For FY 2007, total current assets have increased by 5% from 2006. In FY 2007, accounts payable and accrued expenses increased by \$224,547 from 2006 due to the outstanding balances on both the Wellness and KHC Projects. VHT's balance sheet for 2007 is slightly stronger than it was in 2006. With the proposed debt, VHT will remain leveraged with a proforma debt-to-unrestricted net assets ratio of 2.94. However, VHT will use the bond proceeds to refinance existing debt and reduce its overall annual debt service payments. The proposed financing will improve VHT's ability to handle debt as shown by the proforma debt service coverage ratio of 1.30x. Based on the feasibility study, management anticipates the debt service coverage ratio to remain above 1.30x and increase gradually over the period of FY 2008 through FY 2012.

III. BACKGROUND:

Valley Health Team, Inc. is a California private, not-for-profit corporation with over 30 years of experience in providing a comprehensive range of health services to the indigent, low-income, and multi-cultural resident of the rural communities of western Fresno County and the outlying rural areas. These areas are primarily dominated by agriculture and agricultural related interests.

VHT currently operates its clinics out of three locations, two primary care clinics in San Joaquin and Kerman, and an optometry clinic, Kerman Health Centers. Additionally, two mobile services are operated by VHT, dental mobile and transportation van. Services offered by the clinics include clinical lab, dentistry, family practice, health education, nutritional counseling, OB/GYN services, optometry and ophthalmology, pediatrics, pharmacy, radiology/X-ray, podiatry, ultrasound and Women's Health.

Licenses and Contracts: VHT is licensed by the State of California Department of Health Services as a primary care clinic.

IV. UTILIZATION STATISTICS:

Valley Health Team, Inc.			
Year Ended June 30,			
	<u>2007</u>	<u>2006</u>	<u>2005</u>
Payor Mix:			
Medi-cal	46.0%	44.8%	46.6%
Medicare	7.9%	7.9%	6.7%
Other	46.1%	47.3%	46.7%
Outpatient Clinic Visits	31,608	35,928	38,048

V. OUTSTANDING DEBT:

<u>Description</u>	<u>Original Issue Amount</u>	<u>Amount Outstanding as of 06/30/07</u>	<u>Estimated Amount Outstanding after Proposed Financing</u>
<u>Existing Debt:</u>			
Local Medical Facilities Financing Authority, Series 1990, COP	\$1,025,000	\$710,000	\$0
United Security Bank Loan #1	266,300	266,300	0
United Security Bank Loan #2	349,929	347,967	0
CHFFA HELP II, 2002	400,000	279,915	279,915
<u>Proposed Debt:</u>			
CHFFA Bonds		N/A	\$2,500,000
TOTAL DEBT		<u>\$1,604,179</u>	<u>\$2,779,915</u>

*Includes current portion.

VI. DUE DILIGENCE:

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

- Section 15438.5 of the Act (Savings Pass Through): VHT has provided a description of its savings pass through in **Exhibit A**.
- Section 15459 of the Act (Community Service Requirement): VHT has executed this certification and indicated that Medi-Cal and Medicare patients are accepted. A copy of the certification is provided as **Exhibit B**.
- Compliance with Assembly Bill 1341: VHT has provided the necessary documents to show compliance with CEQA requirements of AB 1341.
- Religious Due Diligence.
- Legal Review - VHT disclosed four potential legal issues in the Application.
 - VHT has made a claim against its prior Chief Executive Officer (CEO) regarding collection efforts for over \$400,000 in unapproved bonuses, which could become potential litigation with VHT as the plaintiff.
 - Two related complaints were filed with the Department of Fair Employment and Housing (DFEH) by two former employees both alleging that their employment was terminated for reporting alleged sexual harassment of another employee.
 - The former CEO referenced in the potential litigation mentioned above may be in the process of filing a DFEH complaint.

After Staff and in-house Legal Staff reviewed all the information regarding these issues, they were determined to be not material to this financing and do not question the financial viability or legal integrity of the Applicant.

VII. STAFF RECOMMENDATION:

Staff recommends the Authority approve a Resolution in an amount not to exceed \$2,500,000 for Valley Health Team, Inc. subject to financing terms acceptable to the Authority and final Cal-Mortgage Insurance commitment.