



FY 2016 Annual Operating and Capital Budget

Board of Directors Budget Workshop
June 3, 2015

Agenda

- Executive Summary
- FY 2016 Budget Overview:
 - Key Budget Drivers
 - Inflationary Assumptions
- Key Statistical / Growth Indicators
- Revenue
 - Key Revenue Assumptions / Payer Mix
 - Revenue Trend Analysis
- Salaries, Wages, Benefits & FTEs:
 - 5 Year Salary, Benefits and FTE Trend Analysis
- Non Labor 5 Year Analysis:
 - Supplies / Professional Fees / Purchased Services / Other Direct Expense
- 2016 Annual Budget Summary / EBIDA Recap
- Three Year Capital Planning
- FY16 Budget Summary / Key Take-aways

Executive Summary

- The FY 2016 Annual Budget provides achievable goals for the coming year which continue to put us on a path to successfully executing on our Strategic Financial and Capital Plan (EBIDA growth of \$5 million from Plan) as well as continuing to advance us on the journey toward a Medicare cost profile
- It is the result of a combined effort by administrative and medical staff leadership to absorb inflation and drive greater efficiency in all areas of the organization
- Reflects a concerted effort to hold on all non-essential expenditures
- The operating and capital budgets are aligned with our current year and long term strategic plan initiatives
- The budget process included significant physician leadership engagement to identify reasonable and achievable resource expenditure targets in specific areas



FY 2016 Budget – Key Drivers & Overview

Key Plan Drivers



- Strategic Plan alignment including targeted \$5 million EBIDA growth year over year; this growth is consistent with the long-range Financial and Capital Plan targets
- Continued reimbursement pressures: governmental payer shifts including Medi-Cal Expansion, trend towards capitated contracts, and continued Covered California growth
- Expense management strategies and initiatives include reducing labor costs through our “Patient Throughput” initiative as well as, enhancing supply costs savings through utilization and rate efforts

Patient Throughput Initiative	Supply Exp Reduction Initiative
\$500,000	\$1,700,000

- Examination of outsourcing opportunities and continuation of strategies already in place
- Assessment of service lines and contribution margin profitability
- Continued focus on IT related enhancements and solutions; including revenue cycle opportunities

Key Plan Drivers

KEY DRIVERS

Palomar Health – Baseline Financial Projections (\$ Thousands)

Ratio/Statistic	Projected FYE	Budget	Projections			
	2015	2016	2017	2018	2019	2020
Total Operating Revenue	643,518	666,219	695,082	727,862	766,357	807,058
Operating Income	(24,201)	(19,230)	(18,035)	(14,332)	(7,775)	(805)
PH Calculated Income (Exc. Int. Exp)	6,837	10,443	11,265	14,383	20,225	26,681
Net Income	(7,599)	(2,249)	(1,035)	3,023	10,035	17,574
Cash Flow (Net Inc + Depr)	47,628	54,278	57,092	63,150	72,462	82,401
Unrestricted Cash	159,563	176,518	190,567	210,707	234,215	262,453
<i>Profitability</i>						
Operating Margin	(3.8%)	(2.9%)	(2.6%)	(2.0%)	(1.0%)	(0.1%)
Operating Margin (Exc. Int. Exp)	1.1%	1.6%	1.6%	2.0%	2.6%	3.3%
Excess Margin	(1.2%)	(0.3%)	(0.1%)	0.4%	1.3%	2.1%
Operating EBIDA Margin (Inc. Prop. Tax)	11.7%	12.0%	11.9%	12.0%	12.5%	12.9%
<i>Debt Position</i>						
Debt Service Coverage (x)	2.3	1.9	2.0	2.2	2.4	2.6
<i>Liquidity</i>						
Days Cash On Hand (days)	95.1	102.4	106.2	112.8	120.8	128.9
Cash to Debt	27.2%	30.8%	33.2%	36.7%	40.8%	45.8%
<i>Other</i>						
Days in AR	73.4	71.4	69.4	67.4	65.4	63.4
Average Age of Plant	7.7	8.5	9.3	10.0	10.6	11.2
Compensation Ratio	55.7%	56.5%	56.7%	56.7%	56.6%	56.5%
Expenses per Adjusted Discharges	11,518	11,454	11,572	11,695	11,848	12,007

(1) Moody's: U.S. Not-For-Profit Health Care 2013 Median Ratios. Report issued August 2014.

Prepared by Kaufman Hall and Associates

Inflationary Assumptions

- FY2016 Budget assumes the absorption of a significant amount of industry inflation through utilization and efficiency; several targeted supply management and strategic initiatives were identified
- Pharmaceutical and Implant costs are significant drivers of overall supply costs. As such, the inflation on these two categories will be a key area of focus and pose the most risk

Healthcare Industry Inflation Comparison

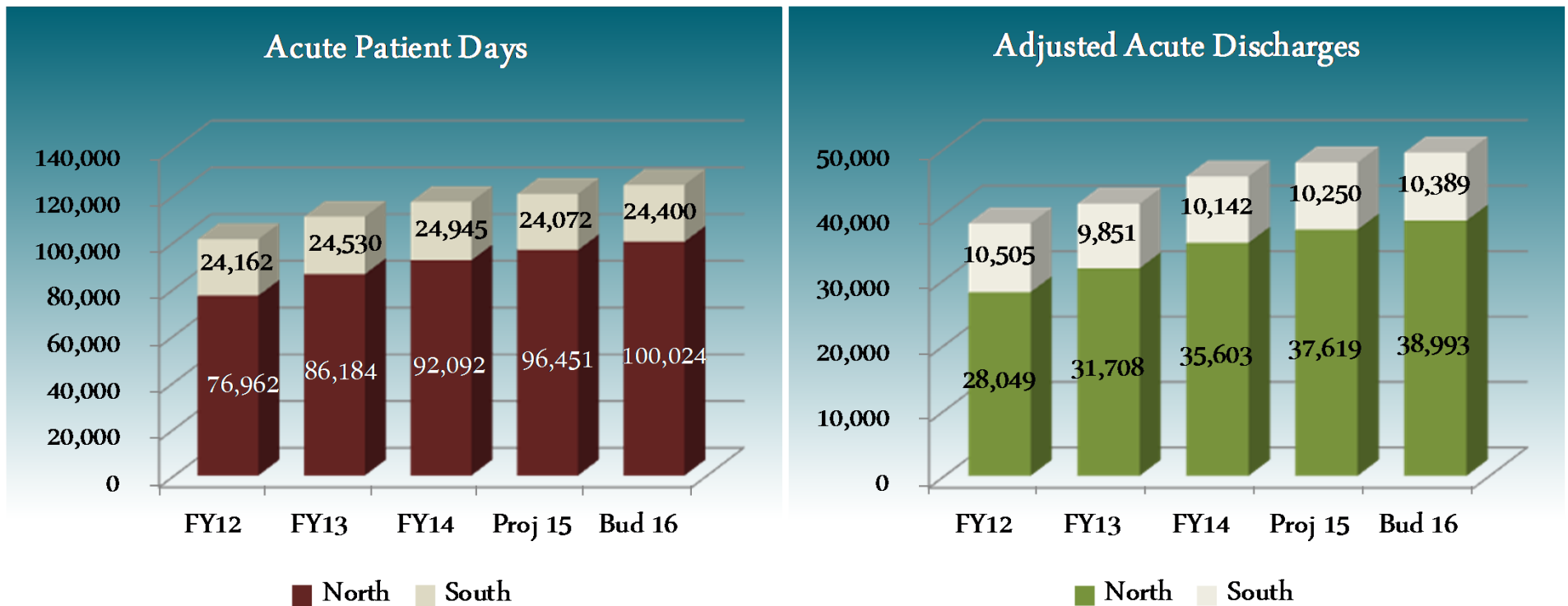
	2016 Budget	Industry Expectations
Implants	0.0%	4.3%
General Surgery Supplies	0.0%	2.1%
Surgical Needles	0.0%	0.0%
Oxygen - Gas	1.5%	3.0%
IV Solutions	3.0%	15.0%
Pharmaceuticals	5.0%	8.0%
Radioactive and X-Ray Material	0.0%	0.5%
Other Medical	0.0%	0.3%
Food / Meat	1.0%	1.3 – 3.5%
Linen	0.0%	0.0%
All Other: Cleaning/Forms/Office/Uniforms	0.0 – 1.0%	0.0 – 4.3%



Key Statistical Indicators

Key Statistical Indicators: INPATIENT

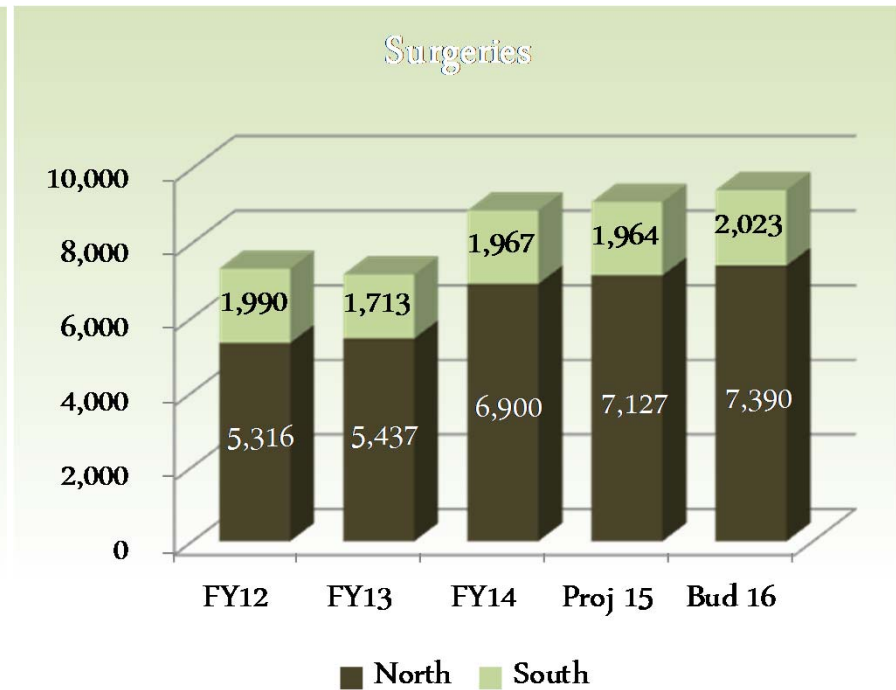
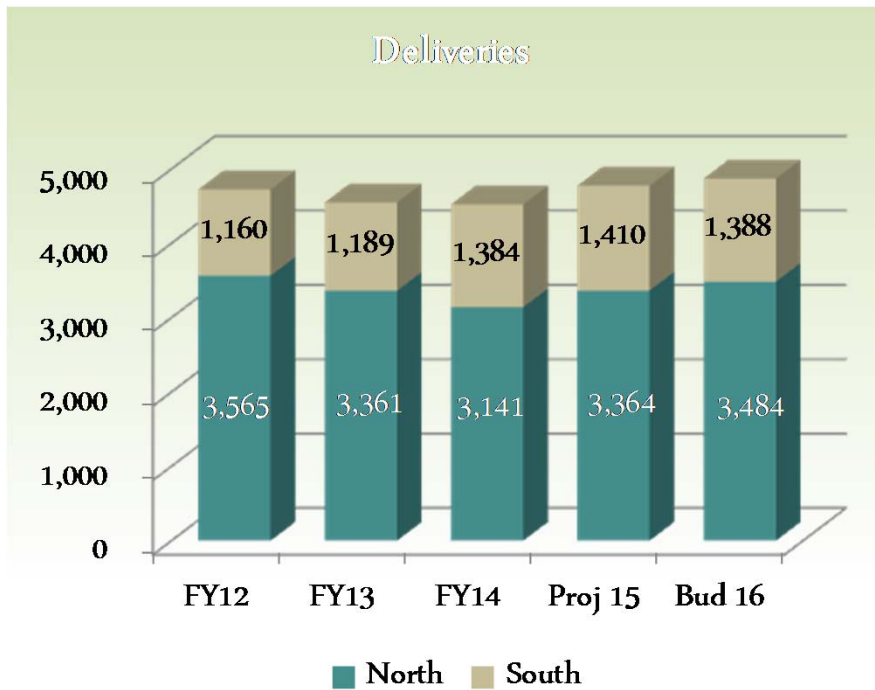
- FY 2016 Planned Acute Patient Days are an increase of 3,901 days or 3.2% year over year
- FY 2016 Adjusted Discharges are 3.2% higher or 1,513 discharges over FY 2015 projected



* North includes Palomar Medical Center (PMC) and Palomar Health Downtown Campus (PHDC); South includes Pomerado Hospital (POM)

Key Statistical Indicators: INPATIENT

- FY 2016 Deliveries are an increase of 98 or 2.1% year over year
- FY 2016 Surgeries are 3.5% higher or 322 over FY 2015 projected

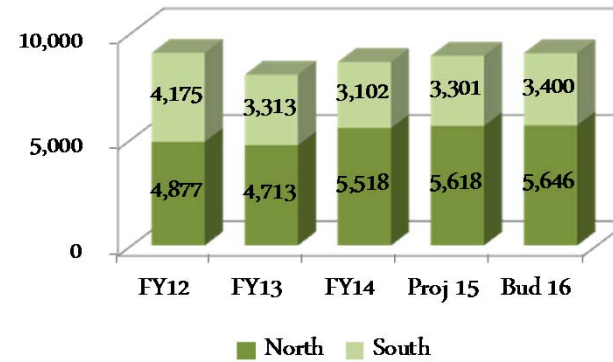


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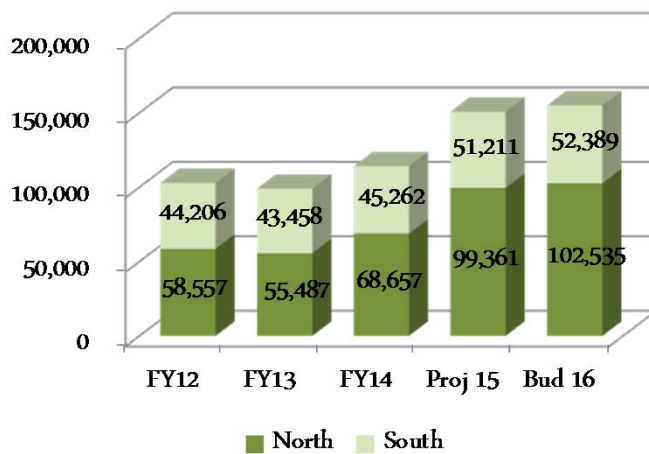
Key Statistical Indicators: OUTPATIENT

- Outpatient Surgeries are increasing 127 or 1.4%
- Emergency Visits are increasing by 5,601 or 4.1%
- Outpatient Registrations are increasing by 4,352 or 2.9%

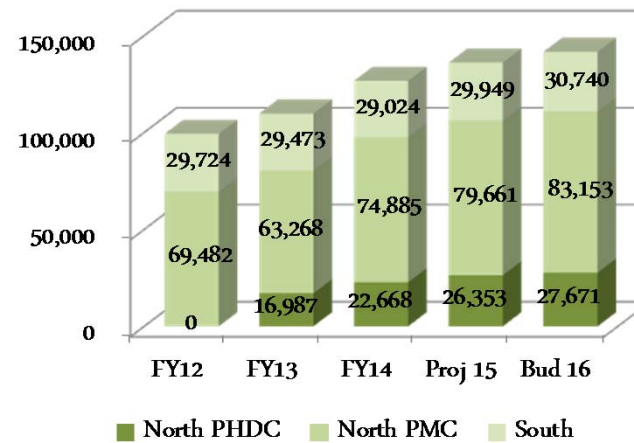
Outpatient Surgery



Outpatient Registration



Emergency Visits





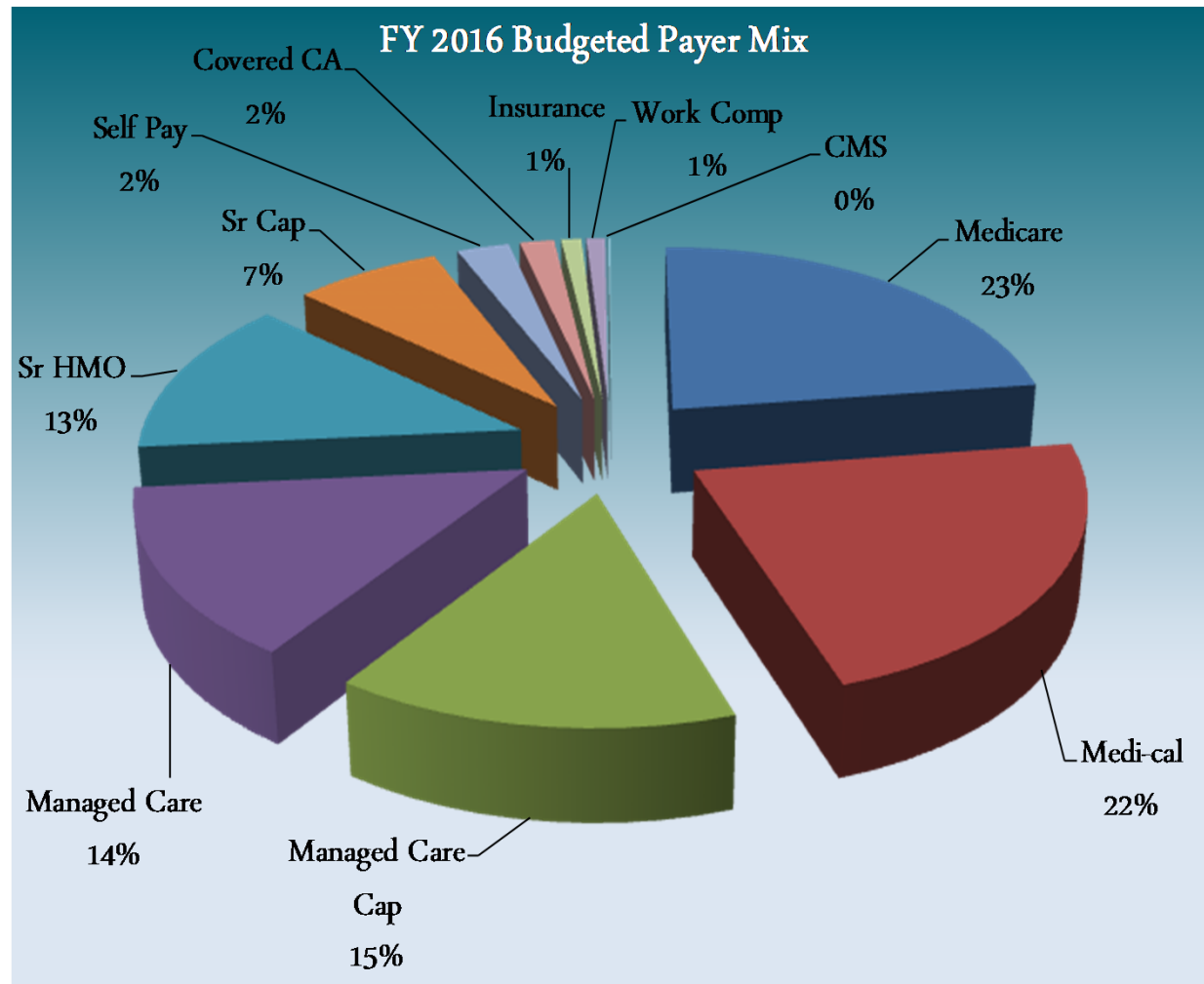
Revenue

Key Gross Revenue Considerations

Assumptions:

- 7.52% overall effective rate increase (targeted 8%)
- Bad Debt and Uncompensated Care 2.4%; FY15 Budget = 4.1%
- Medi-Cal Deductions 9.9%; FY15 Budget = 7.1%

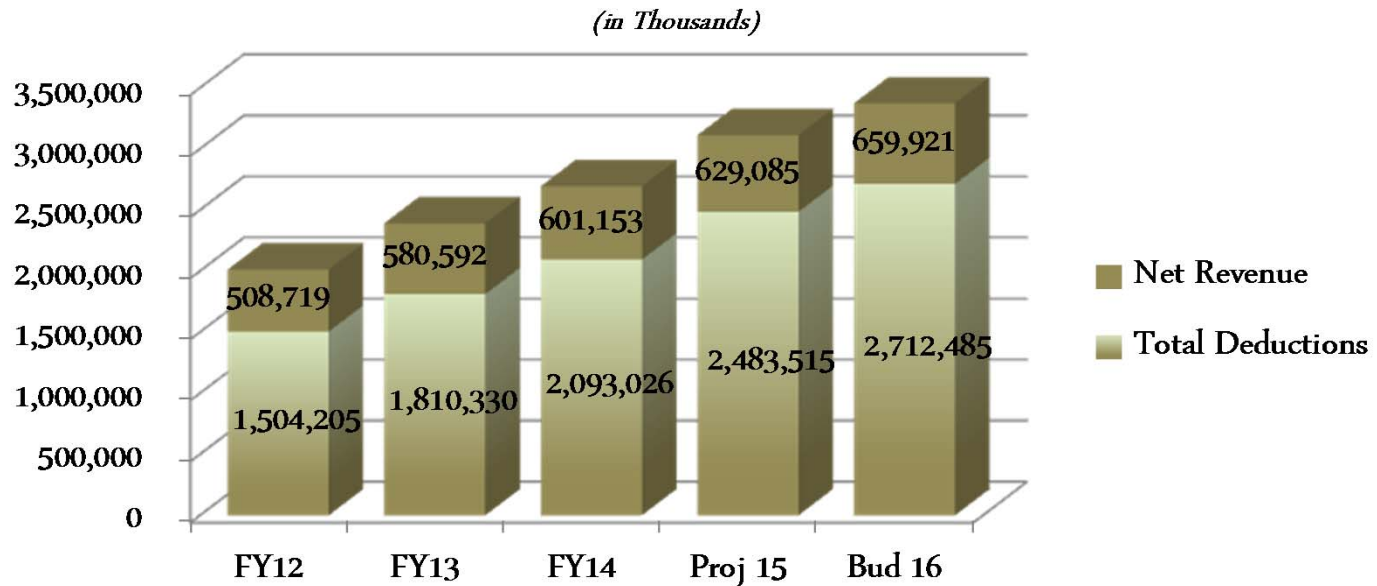
Payer Category	Total CHRGS
Medicare	765,869,468
Medi-cal	744,243,375
Managed Care Cap	488,856,108
Managed Care	471,960,699
Sr HMO	437,911,167
Sr Cap	239,280,065
Self Pay	85,612,004
Covered CA	56,552,969
Insurance	32,931,392
Work Comp	30,994,342
CMS	4,210,962
Total*	3,358,422,551



* Based on Gross Revenue and Excludes Home Health and Clinics

Revenue Trend Analysis

- FY 2016 Gross Revenue is expected to be \$260M or 8% higher than FY 2015
- Net Revenue is anticipated to be \$31M or 5% higher year over year



	FY12	FY13	FY14	Proj 15	Bud 16
Total Deductions *	1,504,205	1,810,330	2,093,026	2,483,515	2,712,485
Net Revenue	508,719	580,592	601,153	629,085	659,921
Total Gross Revenue	2,012,924	2,390,922	2,694,180	3,112,601	3,372,406

*Deductions include net capitation impact



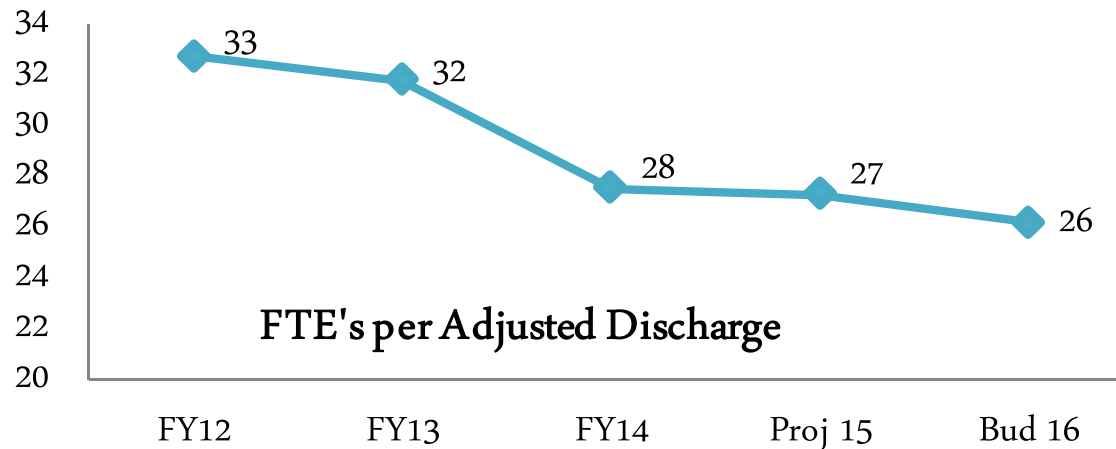
Salaries, Wages, Benefits & FTEs

Labor Analysis – FTE’s

2016 Budgeted FTE Roll Forward		FTE’s
	FY 2015 Paid FTE’s (as of 4/18/2015)	3,578
	FTE’s Added Due to Volume Growth*	87
	Operational Efficiencies & Productivity Standard Adjustments*	(78)
	FTE Reductions	(44)
	FY 2016 Paid FTE’s	3,543

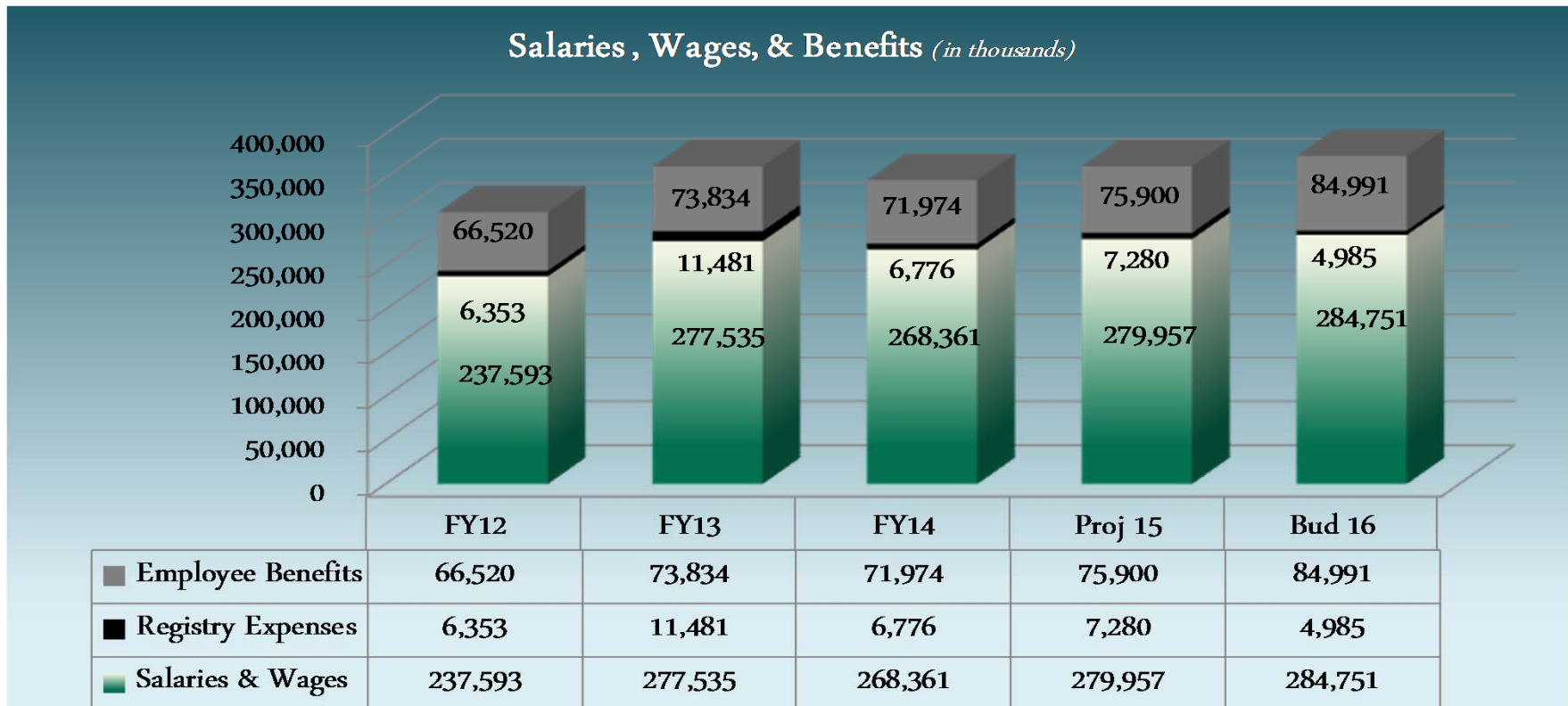
* Productive FTE’s

- Consistent with FY 2015, FY 2016 Budget assumes a reduction in FTE’s on a per Adjusted Discharge basis



Labor Analysis – Salaries, Wages and Benefits

- FY 2016 Total Salaries, Wages and Benefits are increasing \$11.6M or 3.2% primarily driven by a \$9.1M increase in Employee Benefits
- FY 2016 Agency / Registry Expense is expected to continue a 3 year decline by \$2.3M



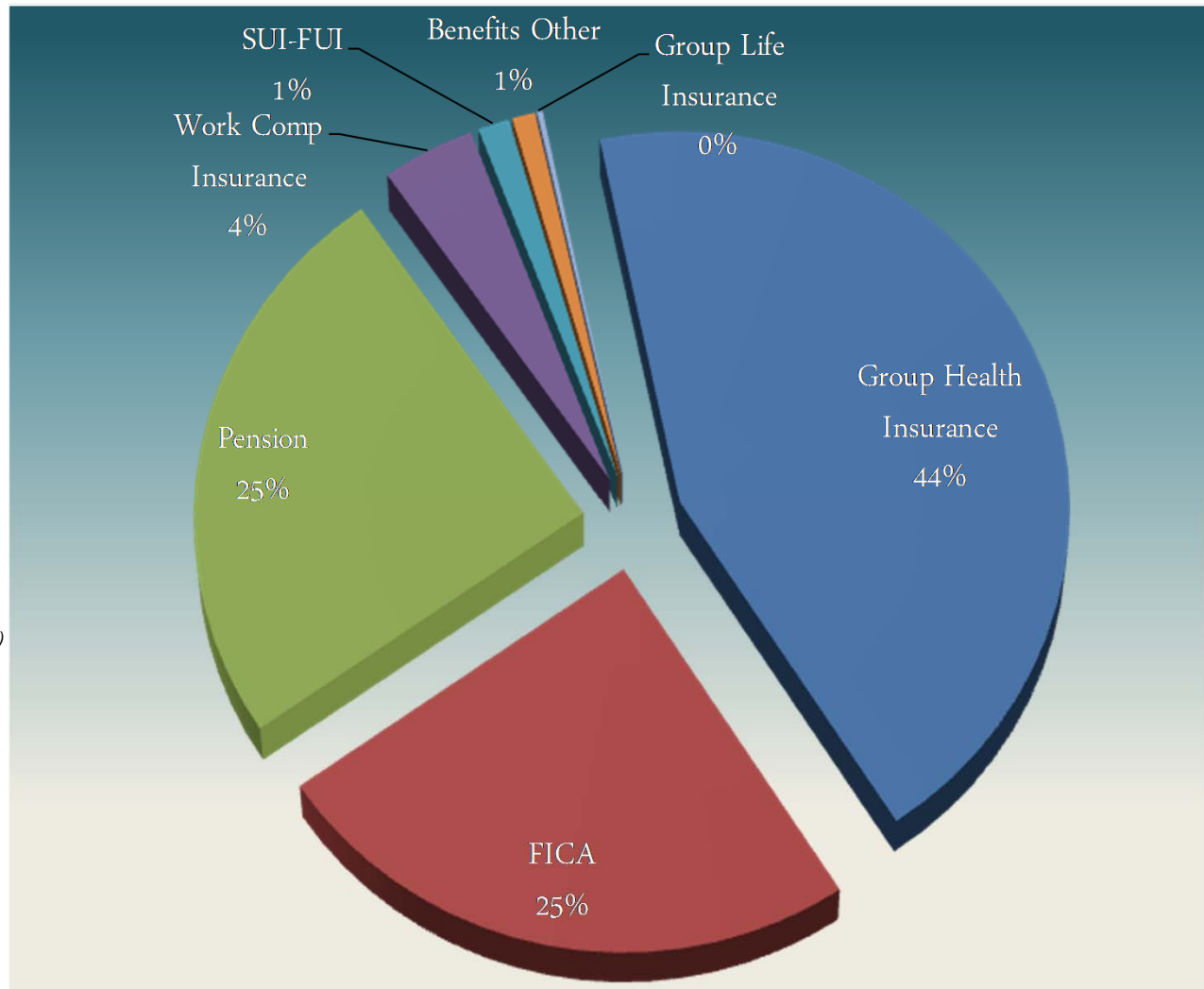
Labor Analysis – Benefits (excluding PTO)

- FY 2016 Employee Benefits are increasing \$9.1M or 12% primarily driven by a \$7M increase in Pension.
- Group Health Insurance has increased by \$2M to provide coverage required under ACA
- Increase of \$750k to provide Paid Sick Leave

(In Thousands)

Bud 16

Group Health Insurance	37,670
FICA	21,000
Pension	21,199
Work Comp Insurance	3,343
SUI-FUI	1,133
Benefits Other	830
Group Life Insurance	213
Total Benefits	85,388

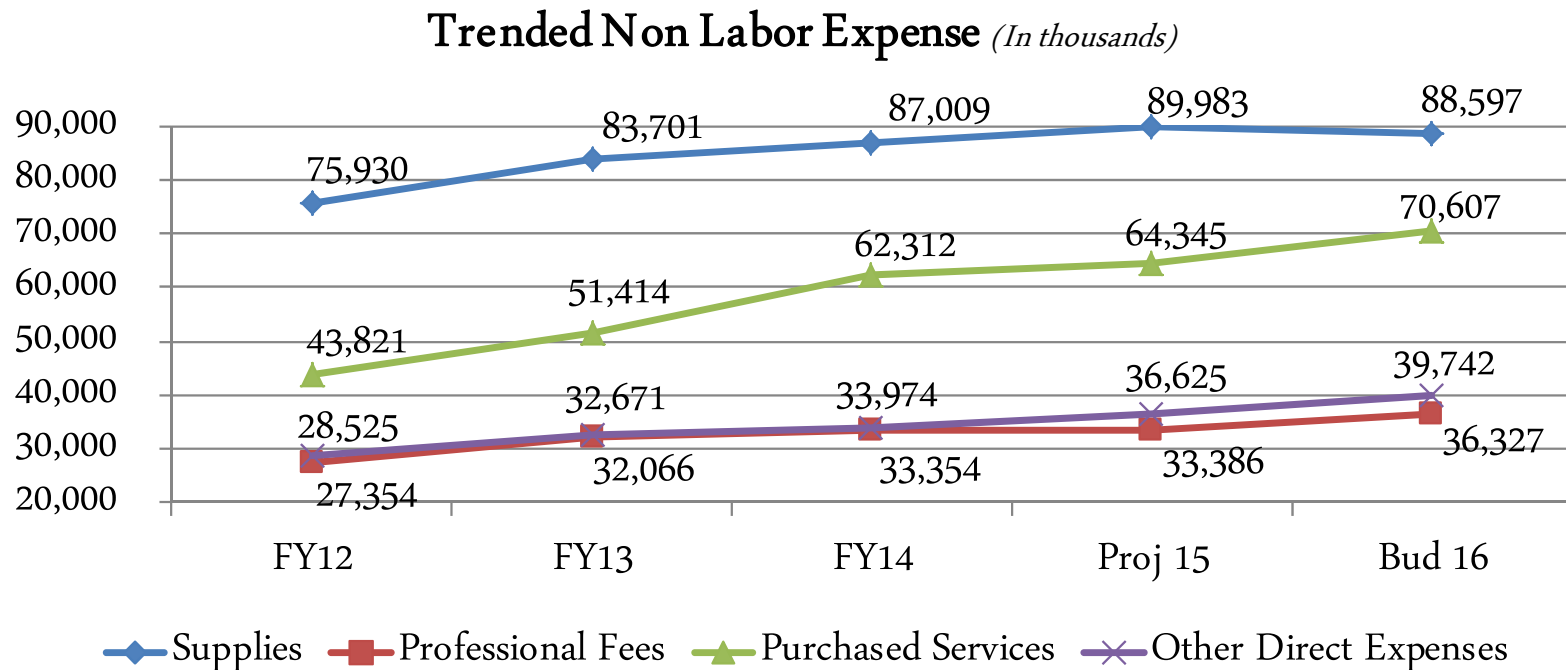




Non Labor Analysis

Non Labor Analysis - Summary

- FY 2016 Non Labor expense is increasing \$10.8M or 3.9%
- However, on a cost per adjusted discharge basis, FY 2016 Non Labor expense is remaining relatively flat to Projected 2015

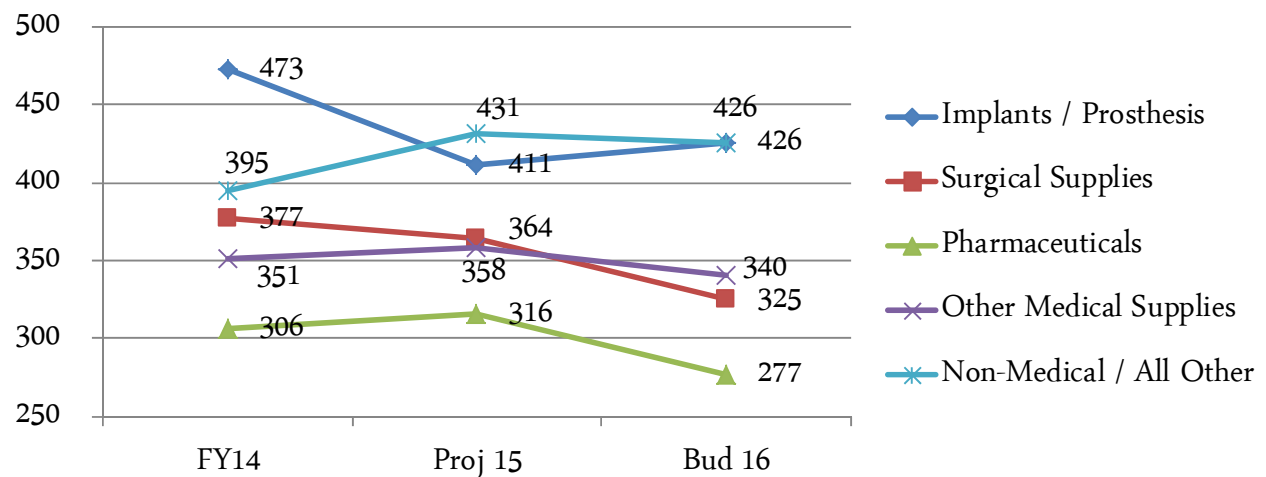


Non Labor Analysis - Supplies

FY 2016 Supply Roll Forward <i>(in thousands)</i>	
FY 2015 Supply Expense (Feb 2015 Projection)	\$89,983
Increases due to Volume and Utilization	625
Inflationary Increases (Net of Absorption)	689
General Supply Management (Efficiency and rate efforts)	(500)
340B Pharmaceutical Savings	(1,000)
Supply Reduction Initiative	(1,200)
FY 2016 Budgeted Supply Expense	\$88,597

- FY16 Budgeted supply management efforts and reduction initiatives total \$1.7M in savings; holding the line on inflation and other increases

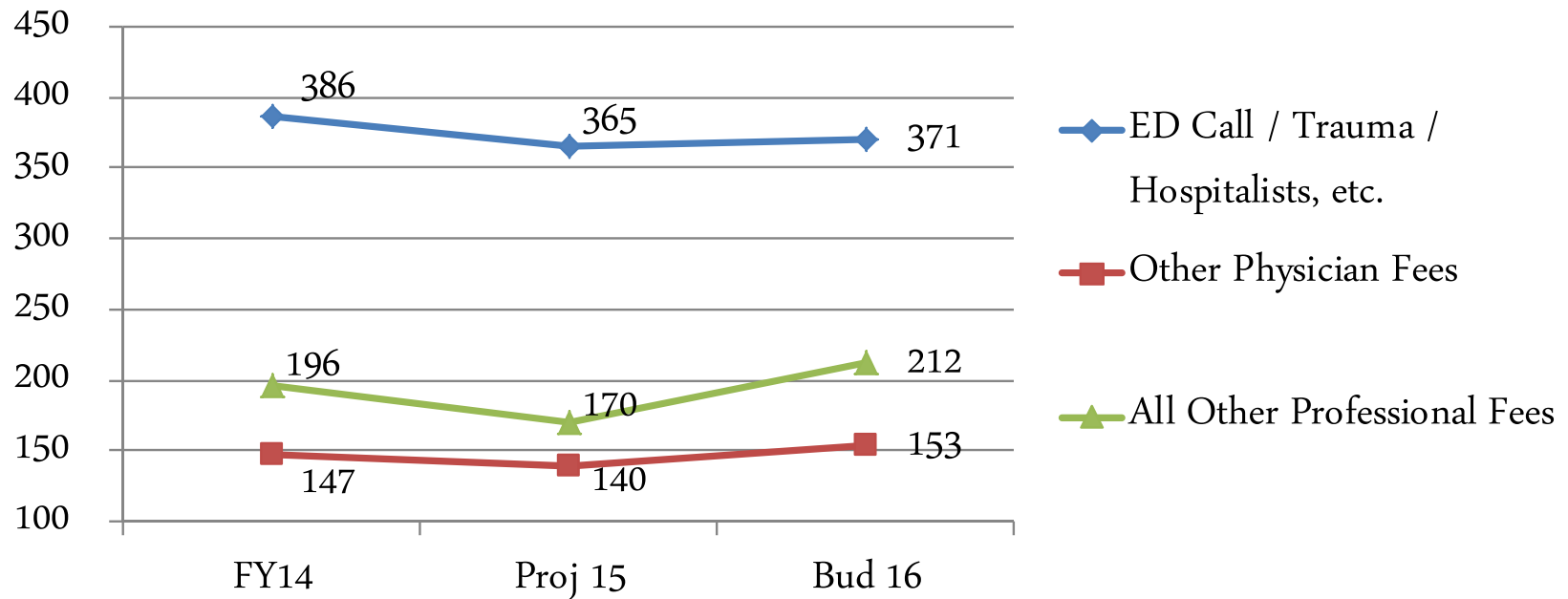
Supplies per Adjusted Discharge



Non Labor Analysis – Professional Fees

- FY 2016 Professional Fees are increasing by \$2.9M or 8.8%
- Professional Fees per adjusted discharge, however, are relatively flat year over year

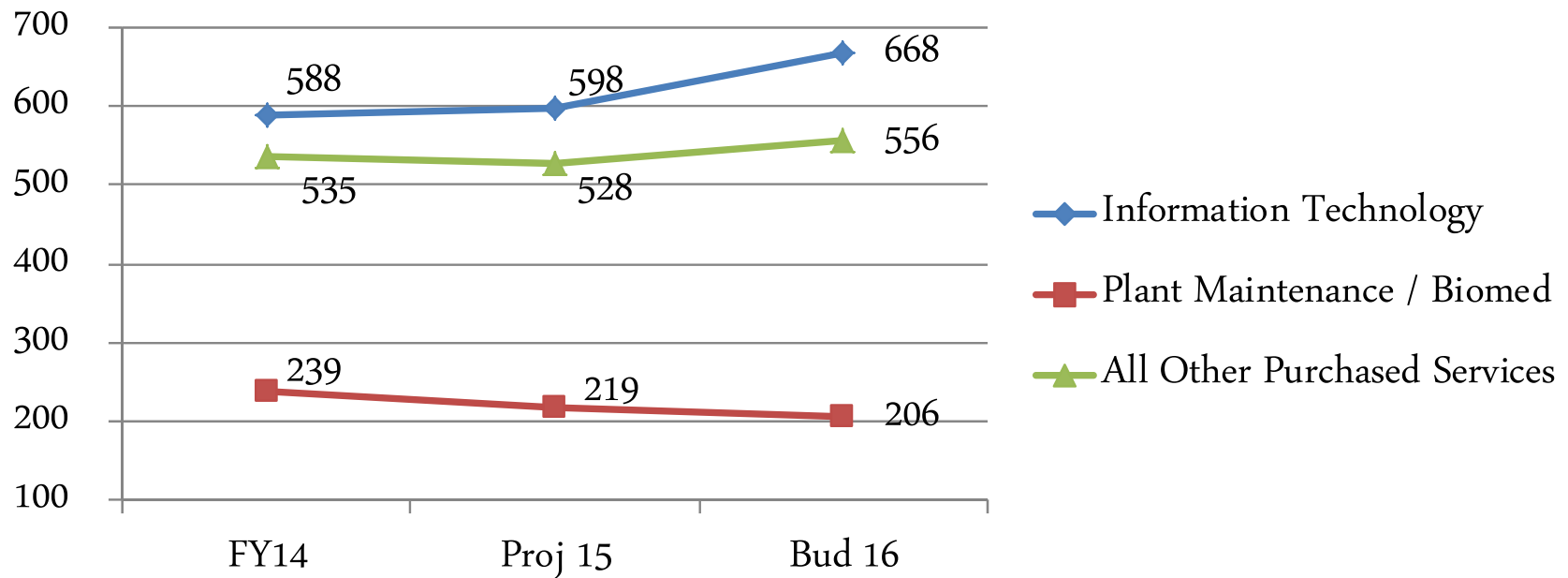
Professional Fees per Adjusted Discharge



Non Labor Analysis – Purchased Services

- FY 2016 Purchased Services are increasing by \$6.3M or 9.7%
- Information Technology increases of \$4.4M are the primary driver

Purchased Services per Adjusted Discharge



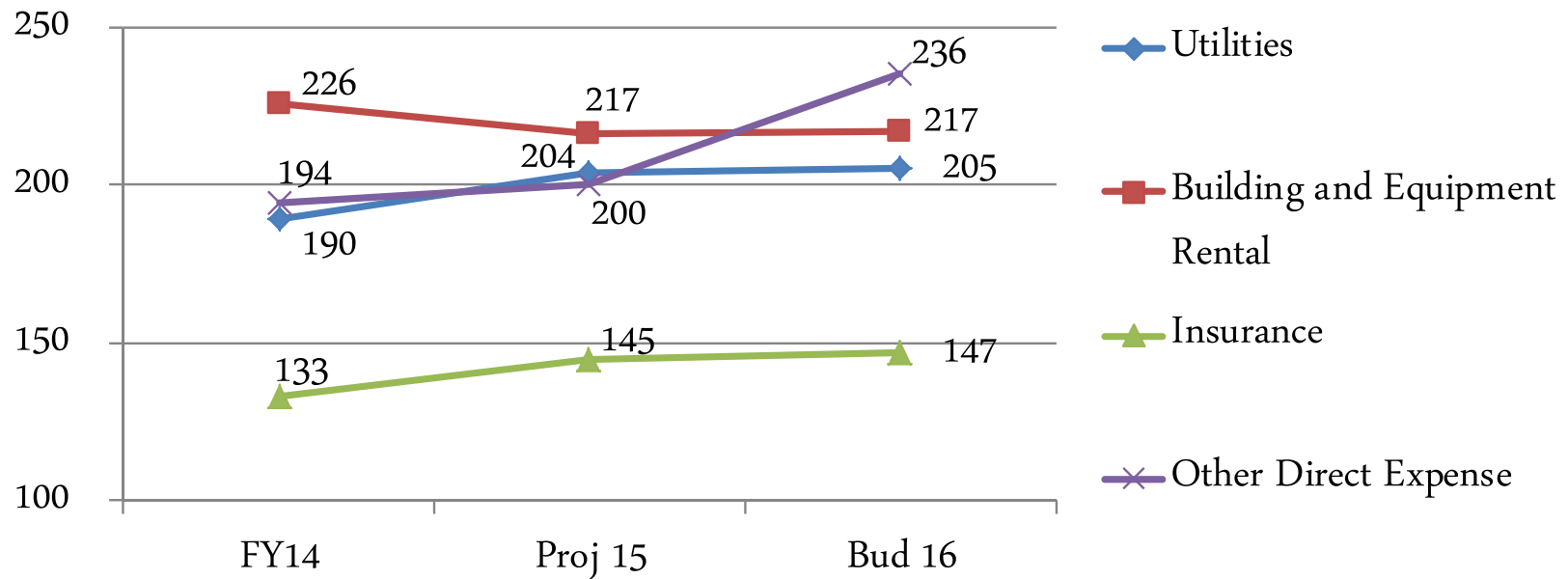
Non Labor Analysis – Purchased Services: IT Roadmap

FY 2015 Accomplishments	
Rehab Services: ARU Inpatient and Outpatient	AirStrip ONE – Patient Monitoring & Imaging
DQR – Document Quality Review	Verdiem (Energy saving software)
Achieved HIMSS Level 6	Phase 1 Wireless Remediation
Axiom Operating Budget system	Physician Wireless Network
LTC – CareTracker system	Emergency Department Dragon Upgrade
Clarity Performance Improvement SCIP Page	Radiology Nuance Upgrade
IT Asset Management System	Core Measures/NHIQM 4.4 Upgrade
FY 2016 Planned Projects	
Population Health Initiative Projects	Crescendo – Home Health system
Info - Contracts Management	Meaningful Use Stage 3
Surgery Physician Documentation Project	ICD-10
Teletracking Orders Interface	Transaction Services - New Claims Scrubber
ED PowerNote 2G	Lighthouse projects (Sepsis & Rapid Response Team)
Lawson – Expense Management	OCR/HIPAA/IT Security Audit



Non Labor Analysis – Other Direct Expense

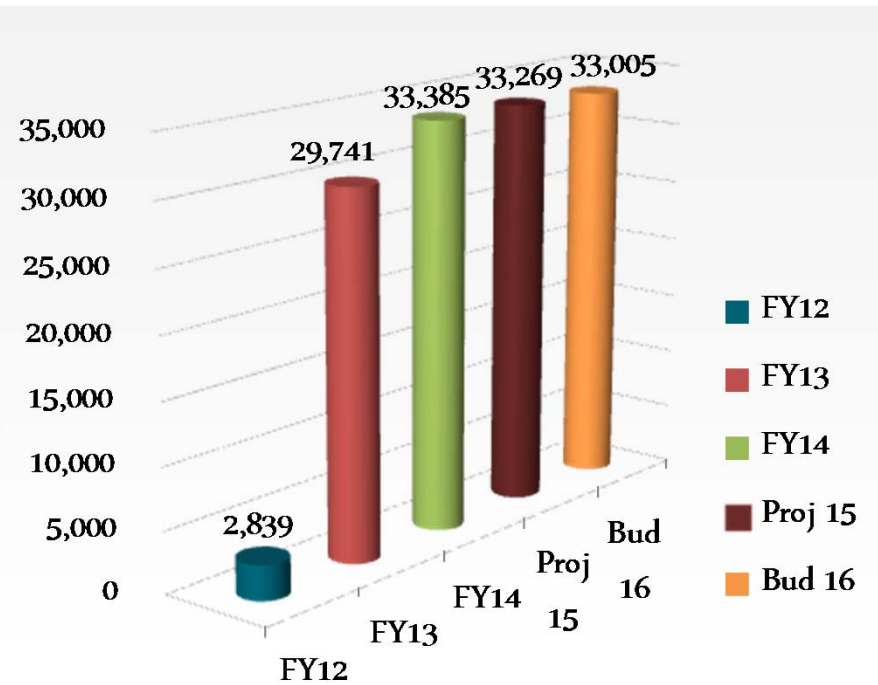
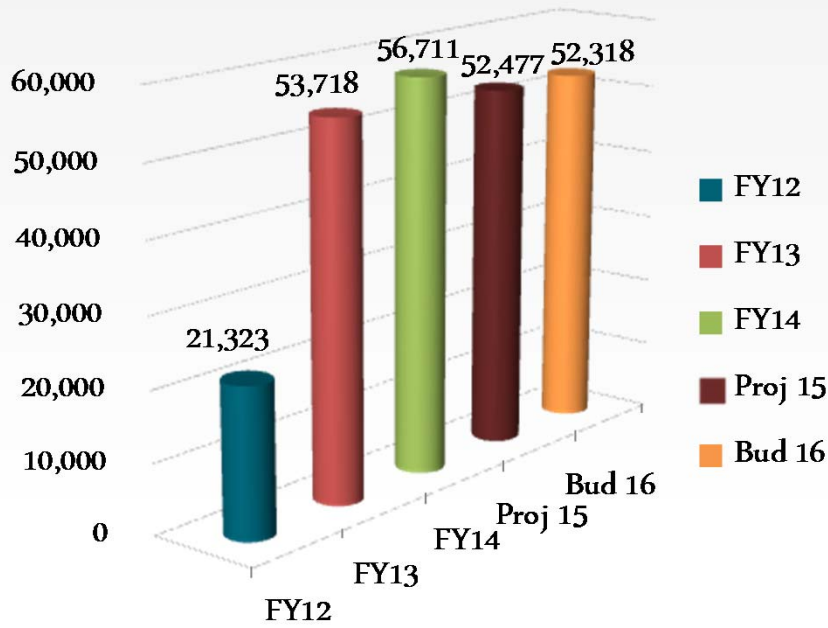
Other Direct Expense per Adjusted Discharge



- FY 2016 Budgeted Other Direct expense is increasing by \$3.1M or 8.5%
- Increases in equipment rental of \$472,000, insurance costs of \$334,000 and utilities of \$386,000 are the primary drivers

Non Labor Analysis – Depreciation and Interest Expense

Depreciation Expense (in thousands)



Interest Expense (in thousands)

- Interest expense reflected for Revenue Bonds only



Annual Operating Budget Summary / EBIDA Recap

Annual Operating Budget Summary and Trend

	Budget FY16	Projected FY15	Results FY14	Results FY13
Revenue:				
Gross Revenue	3,372,405,805	3,112,600,533	2,694,179,906	2,390,922,045
Net Revenue	659,920,567	629,085,362	601,153,488	580,591,690
Other Operating Revenue	12,839,696	15,071,921	13,046,993	13,535,345
Total Operating Revenue	\$ 672,760,262	\$ 644,157,283	\$ 614,200,481	\$ 594,127,035
Expenses:				
Salaries, Wages, Registry, Benefits	374,726,895	363,136,131	347,110,826	362,849,770
Supplies	88,596,912	89,982,812	87,008,983	83,701,324
Depreciation	52,317,549	52,476,711	56,711,438	53,717,757
Other	146,675,906	134,356,791	129,640,252	116,150,300
Total Operating Expense	\$ 662,317,262	\$ 639,952,445	\$ 620,471,499	\$ 616,419,151
Operating Income	10,443,000	4,204,838	(6,271,018)	(22,292,116)
Non-Operating Income	3,686,564	10,786,137	9,772,515	4,400,820
(Interest Expense)	(33,004,734)	(33,269,097)	(33,569,486)	(29,740,802)
Property Tax Revenue	15,099,996	13,900,000	13,451,009	12,913,947
Income (Loss)	\$ (3,775,174)	\$ (4,378,122)	\$ (16,616,980)	\$ (34,718,151)
Net Margin %	-0.6%	-0.7%	-2.7%	-5.8%
OEBIDA Margin (Excl Property Tax Rev)	9.3%	8.8%	8.2%	5.3%
OEBIDA Margin (Incl Property Tax Rev)	11.6%	11.0%	10.4%	7.5%
EBIDA Margin	12.1%	12.6%	12.0%	8.2%
Total Uncompensated Care & Bad Debt	79,560,722	47,582,495	87,221,098	112,188,441
Total Uncompensated Care as % of Gross	2.36%	1.53%	3.24%	4.69%

FY 2016 EBIDA Recap

	Results FY 2012	Results FY 2013	Results FY 2014	Projected FY 2015	Budget FY 2016
Net Income from Ops	13,721	(22,292)	(6,217)	4,205	10,443
<i>Less:</i>					
Depreciation Expense	21,323	53,718	56,711	52,477	52,318
OEBIDA	\$ 35,044	\$ 31,426	\$ 50,494	\$ 56,682	\$ 62,761
OEBIDA Margin (Excl Property Tax Rev)	6.7%	5.3%	8.2%	8.8%	9.3%
OEBIDA Margin (Incl Property Tax Rev)	9.1%	7.5%	10.4%	11.0%	11.6%
EBIDA	52,200	48,740	73,663	81,368	81,548
EBIDA Margin	10.0%	8.2%	12.0%	12.6%	12.1%
Total Uncompensated Care & Bad Debt	97,429	112,188	87,221	47,582	79,561
Total Uncompensated Care as % of Gross	4.84%	4.69%	3.24%	1.53%	2.36%
Net Income/(Loss) after Non-Op Income	\$ 27,935	\$ (34,718)	\$ (16,617)	\$ (4,378)	\$ (3,775)



Capital Plan

Capital Plan

Three Year Capital Budget Summary *(in thousands)*

	FY 2016	FY 2017	FY 2018	Total Project Spend
<u>Routine Capital:</u>				
Equipment	3,000	5,000	5,000	13,000
Facility	3,000	5,000	5,000	13,000
Information Technology	3,000	4,000	4,000	11,000
Total Routine Capital Requests	\$ 9,000	\$ 14,000	\$ 14,000	\$ 37,000
Strategic Capital Reserve	16,000	16,000	16,000	48,000
Consolidated Capital Reserve	\$ 25,000	\$ 30,000	\$ 30,000	\$ 85,000



FY16 Budget Summary & Key Take-Aways

Summary / Key Take-Aways

FY 2016 Budget is achievable and ties to the Strategic Financial & Capital Plan. However, it requires success in the following areas:

- 3% growth in Acute Patient Days
- 3.5% growth in Inpatient Surgeries
- 2% growth in Deliveries
- 5% growth in Net Patient Revenue
- Total expenses year over year on a per adjusted discharge basis are flat
- Execution of Patient Throughput and Supply Initiatives, as well as the other planned expense management strategies included in the budget

Successful Execution will result in:

- Net Income improvement of 14% year over year
- EBIDA of \$81.5M