THE
University of Vermont
MEDICAL CENTER

By Electronic Mail & U.S. Mail

August 15, 2023

Ms. Donna Jerry
Senior Health Policy Analyst
Green Mountain Care Board
144 State Street
Montpelier, VT 05602
Donna.Jerry@vermont.gov

Re: Docket No. GMCB-004-23con, Development of Outpatient Surgery Center on Tilley Drive, Project Cost: $129,640,703
Response to Q.005 – CONFIDENTIAL and UNREDACTED

Dear Ms. Jerry:

The University of Vermont Medical Center Inc. ("UVM Medical Center" or "UVMMC") hereby responds to the Green Mountain Care Board's ("Board") Requests for Additional Information Q.005, dated July 14, 2023, regarding the above-referenced project.

1. Regarding your response to question 4 in Q002: Within the standard financial tables, the FY 2023 budget projects an operating profit of $18.9 million while the FY 2023 projection is $55.7 million. Provide an updated projected operating profit by month to match the FY 2023 projected net operating income shown in the standard financial tables.

Response: Below is a table showing YTD March actual results, monthly actual results of March through June, and monthly projections for July through September. Please see our response to Q.6, below, for a more detailed explanation of the reasons for the increased projected margins.

	FY 2023 PROJECTION							
	FY23 YTD March Actual	Apr-23 Actual	May-23 Actual	Jun-23 Actual	Jul-23 Projection	Aug-23 Projection	Sep-23 Projection	FY203 YRE Projection
Total Gross Patient Service Revenue	2,084,521,674	346,988,525	382,362,222	369,479,278	329,615,371	353,312,636	318,336,882	4,184,616,588
Total Deductions	1,379,692,415	225,628,425	252,718,420	227,022,297	210,648,656	225,835,510	161,060,569	2,682,606,292
Net Patient Service Revenue	704,829,260	121,360,099	129,643,802	142,456,980	118,966,716	127,477,126	157,276,313	1,502,010,296
TOTAL NPSR + FPP + OCV REVENUE	803,026,750	142,994,710	147,898,084	162,670,222	136,367,187	144,877,597	174,676,784	1,712,511,334
Total Other Revenue	164,825,937	27,438,251	30,521,817	30,075,841	24,094,957	26,810,793	23,664,800	327,432,396
TOTAL UNRESTRICTED REVENUE & OTHER	967,852,687	170,432,961	178,419,901	192,746,064	160,462,144	171,688,390	198,341,584	2,039,943,730
Total Salaries	459,276,565	74,207,967	77,428,839	73,367,107	75,179,889	75,498,412	74,417,594	909,376,373
Payroll Tax & Fringe	98,871,684	16,573,439	18,681,004	17,720,036	17,259,041	16,433,976	16,052,342	201,591,522
Salaries, Payroll Taxes, and Fringe Benefits	558,148,249	90,781,406	96,109,842	91,087,143	92,438,930	91,932,388	90,469,936	1,110,967,895
Total Non-Salary Expense	411,593,222	71,088,851	74,973,386	86,203,370	64,308,102	73,086,311	91,993,250	873,246,492
TOTAL EXPENSES	969,741,471	161,870,257	171,083,229	177,290,513	156,747,032	165,018,699	182,463,186	1,984,214,387
NET INCOME (LOSS) FROM OPERATIONS	(1,888,784)	8,562,704	7,336,672	15,455,551	3,715,112	6,669,691	15,878,398	55,729,343

2. Regarding your response to question 10 in Q002: Provide the average inpatient reimbursement rates by service line using the same format as your response to the outpatient reimbursement rates by service line.

Response:

3. Regarding your response to question 11 in Q002: Explain in detail why the 90th percentile is a reasonable benchmark for the OSC.

Response:

4. Regarding your response to question 12 in Q002: Specify the percent of RN positions and RN Perianesthesia positions currently held by Travelers at UVMMC.

Response: Currently, approximately 28% of the RNs working in the UVMMC operating rooms are travelers, and 9% of RNs working in Perianesthesia are travelers.

	FY23 Actual FTEs								
% RN FTEs filled by Travelers	**Oct**	**Nov**	**Dec**	**Jan**	**Feb**	**Mar**	**Apr**	**May**	**Jun**
ORs	26.0%	22.7%	23.3%	24.4%	28.4%	26.9%	24.2%	24.4%	27.8%
Preop & PACU	11.5%	13.9%	10.5%	6.3%	9.1%	9.1%	8.9%	8.6%	8.9%

5. Revise and resubmit financial tables 3, 4, 6, 7, 8 A, B, C to include FY 2028 and 2029 and add an additional column for FY2023 YTD so we may compare FY 2023 projections to actual results thus far. In revising the financial tables, also complete Tables 1 and 2 including debt financing sections and take the site work cost out of the construction line item and include it in the Site Work line item. Also, make any adjustments to the standard financial tables as necessary given your responses to any questions contained in this set of questions.

Response: Please see the revised Tables 1 and 2 submitted in response to the Board's Requests for Additional Information Q.004 (June 19, 2023). Table 1 (rev.) shows Site Work as a separate line item. Table 1 (rev.), line 10 shows the financing cost (capitalized interest). Table 2 (rev.) states the amount of the project cost that we estimate *could* be funded by debt.

Please see the table submitted in response to the above Q.1 for UVM Medical Center's YTD March actual results, monthly actual results of March through June, and monthly projections for July through September.

The financial tables 3, 4, 6, 7, and 8, which we previously submitted, contain information for all of the years required by the Board's rules and its standard tables. Those standard tables require applicants to include financial projections for three project years. The UVM Medical Center has nonetheless also provided the Board with its five-year financial framework, which we submitted in June 2023. As we previously noted, that framework is a much more useful and dynamic tool with which to estimate the impact of this project (or any other) on the overall financial health of the UVM Medical Center in FY 2028 or FY 2029. We were able, through significant staff time and effort, to transpose that financial framework to fit the Board's standard financial tables for project years 1 through 3. As we explained in our prior filing, that transposition was only possible by making assumptions regarding many detailed elements required by the financial tables. Those assumptions grow less reliable in the "out" years, and we are therefore unable to reliably extend the assumptions, and therefore the transposition of our financial framework, for another two years. We remain willing to work with the Board, its staff, and its consultants to utilize the tables and financial framework previously submitted to satisfy the Board's need for financial information regarding this project or the UVM Medical Center.

6. According to the FY 2023 Q2 Bond Disclosure Report, UVMMC's first half net loss from operations was $1.9 million. UVMMC's revised financial tables submitted with Q002 projects a net operating profit of $55.7 million. Describe in detail how a second half profit of $57.4 million will be achieved given a $1.9 million loss in the first half.

Response: Financial results are usually lower the first half of the year due to the seasonal impacts of a few key revenue and expense items. Most importantly, annual cost inflation increases for employed staff occur at the beginning of our fiscal year on October 1, while the majority of payer rate increases to fund cost inflation do not occur until January. This has the effect on the P&L of higher expenses in the beginning of the year for which the revenue to fund flows through the P&L later in the year. The other significant timing item is the supplemental GME Medicaid payment from the State of Vermont, which is recognized on the P&L in September, resulting in a significantly higher monthly margin compared to most other months. Finally, as discussed more fully in our prior responses, in the UVM Health Network's budget narrative, and in response to Q.7, below: All of the UVM Health Network's hospitals have been engaged in extensive and difficult work to reduce expenses and increase operating margins, and those efforts have begun to pay dividends.

The below table, which we have also submitted in response to the above Q.1, shows YTD March actual results, monthly actual results of March through June, and monthly projections for July through September.

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7. Regarding your response to question 3 in Q002, part of the improvement in financial performance is explained by the active recruitment initiative to reduce dependency on contract labor and the margin improvement initiatives. Provide detailed information on these initiatives, a timeline for each, and the estimated financial impact of each initiative.

Response: In 2022, the UVM Health Network identified a number of margin improvement initiatives designed to help improve its financial sustainability over the course of FY 2023. We described those initiatives in detail in our FY 2023 budget narrative and referenced them again in detail in pages 4 -11 of the UVM Health Network's FY 2024 budget narrative. They include:

- Improving the performance of the UVM Health Network Perioperative Services, yielding approximately $47M YTD
- Pharmacy optimization (including implementing the pharmacy automation CON approved by the GMCB), yielding approximately $11M YTD
- Working through pent-up-demand for services, yielding approximately $42M YTD
- Achieving more efficiency in our shared services, yielding approximately $28M YTD

Also among those initiatives has been an effort to reduce reliance on contract labor through increased recruitment and retention of employed providers. While that initiative has not yet produced the savings we have targeted, we continue to work to further reduce the number of so-called travelers necessary to operate our hospitals and skilled nursing facilities. We have also seen significant improvement in our overall spend for travelers for a number of reasons. For instance, across the entire UVM Health Network:

-
- The % of staffing costs attributed to travelers has decreased from high of 16.9% to 11.9%
- The number of traveler FTEs has decreased 8% from high of 802
    - Hospital FTEs have decreased 12% from high of 728
    - But SNF FTEs remain high because we need to maintain post-acute capacity to create access for more acute patients in hospitals

A quarter-by-quarter analysis of those Network-wide traveler costs is below:

These margin improvement efforts, by definition, are never complete, and we have included their anticipated results in our FY 2024 hospital budget submissions.

8. Provide a detailed explanation of the projected net patient revenues rate increases included in the projections for commercial insurance by year for FY 2023-FY 2029.

Response: Consistent with previous rate requests, the projections assume rate increases will fund cost inflation – no more, and no less. In the projections, the model applied future rate increases to fund cost inflation to all payers evenly. Actual rate increases by payer to fund cost inflation are not determined until the annual budget submission and review process by the GMCB. The below table shows the total cost inflation and payer increases to fund cost inflation that were assumed for the projections.

	FY2024	FY2025	FY2026	FY2027
Rate/Revenue Change to Cover Cost Inflation	5.00%	4.00%	4.00%	3.50%

9. Explain in detail how the OSC is projected to drive incremental inpatient surgical volume if inpatient surgical cases already take precedence over outpatient surgical cases when capacity constraints emerge.

Response: The premises of this question are mistaken. It is not true that "inpatient surgical cases already take precedence over outpatient surgical cases when capacity constraints emerge." In the face of constrained capacity, the UVM Medical Center and its providers prioritize cases primarily based on patients' needs. As an example, an elective inpatient surgical case will not always take precedence over outpatient cases.

And the OSC is not projected to "drive" incremental inpatient surgical volume, as the question states. Rather, it is expected to enable UVM Medical Center to accommodate forecasted demand for inpatient surgical services by moving some outpatient procedures that are currently performed in the Main Campus ORs to the outpatient facility. That, in turn, will free up capacity for more inpatient procedures at the UVM Medical Center main campus – volume we project the communities UVM Medical Center serves will need.

UVM Medical Center projects that the percentage of its total cases that are inpatient cases will decline from thirty percent (30%) in FY 2019 to twenty-eight percent (28%) in FY 2030. As we have previously explained, UVM Medical Center projected growth in inpatient surgeries using Sg2 inpatient growth forecasts by service line, which derive from SG2's Impact of Change methodology.

10. Explain in detail how the recent bond rating downgrade by Fitch from an A-plus to an A rating will impact the cost of borrowing the $100 million loan anticipated for this project.

Response: In the annual rating review process, all three rating agencies (S&P Global, Moody's, & Fitch) performed a full review of the UVM Health Network's multi-year financial framework, which included all assumptions and the anticipated $100 million debt issuance included in the OSC CON application.

Below is a summary of the most recent ratings review assessments from all three rating agencies.

S&P Global: "A" Rating, Stable Outlook
Moody's: "A3" Rating, Stable Outlook (A3 is equivalent to A-)
Fitch: "A" Rating, Stable Outlook

Because all of the ratings remain in the "A" category, we do not expect there to be any impact on the cost of borrowing due to Fitch adjusting its rating from "A+" to "A". Given current market conditions and the most recent rating updates, the 5% cost of debt issuance assumed in the CON is still valid. The below table shows estimated interest for different ratings based on current market conditions:

	A	A-	BBB+	BBB	BBB-
Tax Exempt	4.51%	4.61%	4.76%	4.91%	5.06%
Taxable	5.60%	5.75%	5.90%	6.15%	6.45%

11. It is assumed that the funding for this project will be an interest-only loan for five years. Specify the expected term of the interest-only loan and provide an amortization schedule for the loan.

Response: Actual amortization schedules for tax-exempt debt are based on the useful life of the assets being financed, current annual debt service structure of all existing debt, and current market conditions at the time of going to market. We cannot provide the exact amortization schedule until we go to market. What we can share is our current thinking concerning what the general structure of amortization may resemble. Since this is a long-life asset, we anticipate a 25–30-year amortization structure. The first 10 years will mostly be interest only, with interest and principal payments for years 11–25 or 11-30. We will likely target a level debt service structure from year 11 through the end of the term.

12. The application includes population aging as one of the key factors necessitating the development of the OSC project. Explain in detail if and how the payer mix was adjusted

to account for the aging population and whether all applicable financial tables, including the payer mix table, reflect increasing the Medicare payer mix to account for the aging population.

Response: UVM Medical Center continually makes judgments about the value of additional attempted precision in financial modeling for its business planning purposes. Added complexity can produce the false impression that a model is more precise without actually improving its accuracy or value to the planning process, because added complexity can make a model more difficult to understand (and to monitor for robustness) and increase the risk of introducing error. UVM Medical Center's reimbursement model for the proposed OSC factors in forecasted volume by payer type using the payer mix for each service line in FY 2019, and a reduction in Medicare facility reimbursement based on the change in site of service as most recently explained in UVM Medical Center's response to the Board's Q.11 of Q.002 (June 15, 2023).

Modeling the payer mix reimbursement impact of the projected increase in UVM Medical Center's Medicare-eligible patient population would involve making multiple assumptions, including with respect to the percentage of patients aged 65+ who will transition to Medicare from commercial insurance vs. from Medicaid, or uninsured status; and the percentage of patients aged 65+ who will elect a Medicare Advantage plan, or otherwise remain commercially insured for some period of time after they are Medicare eligible.

UVM Medical Center did not attempt to incorporate these variables into the reimbursement model based on analysts' determination that doing so would make the model more complex without materially improving the model's predictive value for its planning purpose.

13. The incremental pro forma expenses do not include inflation for FY 2026. For example, the staff indirect expense is $577,948 for six months in FY 2025. Annualized this is $1,155,896 per year. The FY 2026 expense is $1,152,503, a decline from FY 2025. Given the fixed nature of indirect expenses, it would be expected that this expense item would increase by clinical staff inflation of $4.0%. When converting expense lines to a fixed or variable nature, every expense has less inflation than expected in FY 2026. Please explain in detail.

Response: In preparing the pro forma, we did not perform a straight annualization of all projected FY 2025 half-year expenses to achieve the base FY 2026 expenses, and then apply an inflation factor, as the question proposes. Although we are not certain that we understand the import of the question, we do not believe the approach we employed produces results that are materially different from the approach suggested in the question and are happy to explain our methodology and judgment with respect to these and similar modeling decisions. As exemplified by this exchange, we believe that explanation will be most productive if it takes place conversations with the Board, its staff, its consultants, and interested parties, as we have previously proposed.

14. Provide the math that underlies the outpatient net reimbursement adjustment, showing the number of cases by the amount in dollars per case.

Response:

15. Explain in detail the reason for the difference in net patient revenue between the FY24 hospital budget submission for UVMMC and the financial tables submitted with the OSC CON application.

Response: The University of Vermont Medical Center's five-year financial framework (upon which the financial tables are now based) and its annual hospital budget are two different tools, constructed for different purposes, at different points in time in a dynamic environment. As we have detailed in prior submissions, the financial framework serves as a high-level, multi-year guide for a host of individual financial decisions, including the preparation of hospital budgets. In particular, the financial framework sets margin targets that are necessary to maintain the financial thresholds and relationships that are indicative of a financially healthy organization. Hospital budgets, in turn, are built from the "ground up" each year, based on more detailed and current projections of revenues and expenses.

Each year, each hospital within the UVM Health Network, including the UVM Medical Center, strives to build a budget that meets the objectives of the financial framework, including the margin targets the framework contains. However, the hospital's budget will always differ from the framework in many ways that take account of the individual, and far more granular, factors affecting the hospital's projections at the time the budget is submitted. Similarly, the hospital's actual performance will differ from the budget. Each year, the financial framework is updated to take account of those differences so that it continues to serve as a useful planning tool.

With that context in mind, the FY 2024 hospital budget submission margin differs from the framework margin by approximately $15.3M. The financial framework FY 2024 margin is $81.2M whereas the FY 2024 budget submitted margin is $65.9M. Among many contributing factors, the primary reason the financial framework margin is higher is that it assumes some Hospital Directed Payments that were not built into the FY 2024 hospital budget. Although we continue to discuss increased Hospital Directed Payments with Vermont's Agency of Human Services, such discussions have not yet come to fruition. None of the differences between the financial framework and the FY 2024 hospital budget are significant enough to be material to the Board's decision regarding the pending CON application.

16. Explain in detail whether other recently approved CON projects (Dermatology, da Vinci Surgical Robot, and the CT scanner and construction a pad for a mobile unit) have been incorporated into the projections for UVMMC in the financial tables submitted with Q002. If not, explain in detail.

Response: These projects are included in the overall financial framework assumptions.

17. Confirm whether the reimbursement revenues reflected in the pro forma and the revised financial tables submitted with Q002 reflect the lower reimbursement rates for the OSC recommended by Stroudwater Associates. If not, explain in detail.

Response: Yes, the reimbursement rates for the OSC conform to Stroudwater Associates' recommendations. Please see the response to Q.3 above.

18. Explain in detail UVMMC's contingency plan to cover expenses if revenues are lower than projected.

Response: As we have detailed in our prior filings, no single metric or statistic – including operating margin -- predicts or demonstrates future financial stability. Effective financial management requires a multi-year balanced and integrated approach, and an understanding of the relationship between key financial indicators. Those key financial indicators are Operating Margin, EBIDA Margin, Days Cash on Hand, Capital Spend %, Average Age of Plant, & Long-Term Debt to Capitalization Ratio.

UVMMC nonetheless focuses on achieving the annual margin results necessary to maintain the financial thresholds and relationships set by the financial framework. Should margin performance not meet the objectives outlined in the financial framework, the UVM Medical Center will necessarily adjust its approach to the other factors in the framework to achieve stability. For instance, if the UVM Medical Center does not achieve its budgeted margin, the first "lever" we would pull is reducing capital spending. That action would preserve days cash, but drive up the average age of UVM Medical Center's physical plant.

Of course, if revenues consistently fail to cover operating expenses and produce a positive margin, the UVM Medical Center will be required to further cut operating expenses, which will in turn affect the provision of health care services. Those choices are appropriately addressed in detail in the annual hospital budget process.

19. Specify the current square feet of space and annual associated cost of the space UVMMC currently leases at Fanny Allen. Explain whether UVMMC will continue to lease some or all of this space; the square footage it intends to continue leasing once the OSC is operational, if any; and the annual cost associated with continued lease of space at Fanny Allen.

Response: The UVM Medical Center leases the entire Fanny Allen campus under a single lease on a gross cost basis. The lease does not assign or calculate rent on a per-square-foot basis or assign different rents for different portions of the campus. The campus has a total of approximately 140,444 square feet, and the UVM Medical Center leases it at a cost of $1.158M annually. The Fanny Allen campus currently houses many services, including several specialty clinics within its Medical Office Building, along with the five OR's that are slated to relocate, Urgent Care, Inpatient Rehab, Outpatient Pharmacy, Lab, Radiology, an IT training center, and a chapel. Although the UVM Medical Center has not yet determined exactly how it will re-utilize the relatively small portion of space on the Fanny Allen campus that is vacated after the OSC is operational, it currently anticipates that the entire Fanny Allen campus will remain an integral

part of its outpatient care strategy. Because the current lease expires on September 30, 2026, we are in discussions with the landlord regarding our future occupancy of the site.

20. In a table format, provide the actual percent of payer mix made up by Medicaid each year 2021-2024 for UVMMC's overall payer mix, for current outpatient surgeries, and current inpatient surgeries.

Response:
The table below represents payer mix based on gross patient services revenue for all services through the ORs. There is no actual data for FY2024 to report yet.

	FY21 Actual	FY22 Actual	FY23 Actual YTD June
Medicaid Payer Mix			
Inpatient	15.7%	17.4%	17.1%
Outpatient	17.7%	16.1%	16.0%

Thank you for your attention to UVM Medical Center's application. Please let us know if you have any further questions or need additional information.

Sincerely,

Eric Miller
Sr. Vice President and General Counsel
The University of Vermont Health Network Inc.