Southwestern Vermont Medical Center
Operating Budget
Fiscal Year 2022

A. SUMMARY

Southwestern Vermont Medical Center's (hereafter "SVMC" or "Medical Center" or "Hospital") Operating Budget for Fiscal Year (hereafter "FY") 2022 has a planned operating gain of nearly $3,629,000 or an operating margin of approximately 2.0%. Table #1 provides the high level comparative summary Statement of Operations.

SVMC management would classify this budget as a "Continued Recovery Budget". Pre-pandemic budgets and actual results were typically close to the Green Mountain Care Board (hereafter "GMCB") guidelines for Net Patient Service Revenue (hereafter "NPSR") growth and the Medical Center generated both budgeted and actual operating margins of approximately 3% historically for years. The FY 2022 budget has approximately a 2% operating margin. In July 2020, management prepared the FY 2021 budget in the midst of the pandemic. In the FY 2021 budget management made assumptions related to volumes that were the "best" educated projections in an environment of many unknowns around the pandemic and human behavior related to health care. Comparisons to FY 2019 actual results, the last year before the public health emergency, FY 2021's budget and FY 2021's projected will be made throughout this budget narrative.

Table #1 – Comparative Summary Statement of Operations

	FY 2019 Actual	*FY 2021 Projected*	*FY 2021 Budget*	*FY 2022 Budget*
Net patient service revenues	$163,952,570	$169,481,663	$167,089,128	$177,594,439
Covid-19 Funding		2,847,219		
Other operating revenues	7,408,575	8,066,128	7,505,174	6,797,439
Total operating revenues	*171,361,145*	*180,395,010*	*174,594,302*	*184,388,767*
Operating expenses	*165,778,101*	*175,407,639*	*174,402,372*	*180,760,242*
Operating gain	*5,583,044*	*4,987,371*	*191,930*	*3,628,525*
Non-operating activities	413,312	1,362,242	450,000	(49,235,000)
Excess revenues over expenses	***$5,996,356***	***$6,349,613***	***$641,930***	***($45,606,475)***

The NPSR growth is approximately $8.1 million or a 4.8% increase over FY 2021's projected. Comparing to the FY 2021 approved budget the increase is approximately $10.5 million or a 6.3% increase. Eliminating the conservative estimates of COVID-19 revenues the increase is $9.6 million or 5.7%. The three year increase (FY 2019 actuals is the last non Covid-19 fiscal year) the FY 2022 budget increase is $13.6 million for the three year period. This is an annual increase averaging 2.77% for the three years. Comparing to the FY 2019 budget the three year budget to budget annual increase is averaging 2.5%, annually one percent below the GMCB targets.

The "Continued Recovery Budget" for FY 2022 has many more risks then opportunities which we will describe later in the document. The increase in revenues includes a requested effective net charge master increase of 4.8%, and the anticipation of volumes moving closer to the pre-pandemic run rate but still not to FY 2019 levels. Continued participation in OneCare VT. SVMC management has ***not*** provided any upside or downside risk in this budget related to the OneCare VT model. A provision for lost revenues due to increased retrospective audits and denials from third party payers has been included. Management removed the enhanced reimbursement for COVID-19 patients from Medicare. In FY 2021 outpatient orthopedic surgical and endoscopy volume exceeded budgeted levels and FY 2019 levels. This increase is due to a fully staffed orthopedic practice and improved coverage in the endoscopy service. Management is expecting volumes to continue to increase or hold the current run rate in these services, in the FY 2022 budget.

The budget includes a lower level of COVID-19 laboratory testing volume, revenue and expenses below FY 2021's projections based upon management's best estimates at this time. The budget assumes vaccines will primarily be administered in primary care physician practices, Express Care and at local pharmacies in our region. The Hospital will maintain departments to accommodate patient drive through testing for COVID-19 and for vaccines and flu shots; a Respiratory Evaluation Center for patients with COVID-19 symptoms and patient/visitor screening teams; greater scheduling of patients adding direct and indirect costs to the Medical Center.

SVMC received both federal and state relief funds via the CARES ACT, rural stimulus grant funds, stabilization grant, and Medicaid retainer funds all of which was recorded as revenue in FY 2020 and FY 2021. ***NO*** federal or state relief funds were budgeted in FY 2022. Management is in the process, as of the date of this document, evaluating if the Medical Center qualifies for additional funding. In addition, payment advances were received from Medicare, Medicaid and Blue Cross of Vermont to assist with cash flow issues due to the sharp decline in patient volume/revenue in FY 2020, these funds have been repaid or will need to be fully or partially repaid in the next twelve months.

A listing of the most significant funds received in FY 2020 are in table #2 below:

Table #2 – Schedule of COVID-19 Payments and Advances received in FY 2020

	Amount
HHS Stimulus payment	$9,745,969
Medicaid COVID-19 Retainer	784,501
VT Stabilization Grant	6,457,920
Medicare advance payments	9,470,000
Blue Cross advance payments	1,900,000

In FY 2021, SVMC repaid the Blue Cross advance. Starting in April 2021, Medicare started to recoup the Medicare advance payments. In FY 2022, SVMC will repay the remaining balance which will be an outflow of cash of approximately $7.2 million.

Table #3 is a comparative summary Statement of Cash Flows for the FY 2022 budget. Included on the statement are the material drivers of Medical Center's cash flows. The FY 2022 Operating Budget will generate a positive gain from operations of nearly $3,629,000. After the cash needs, including capital purchases of the organization the expected cash balance will decrease by approximately $3.1 million which represents approximately 7.6 days cash on hand.

Table #3 – Comparative "high level" Statement of Cash Flows

	(as filed)	
Operating gain	*$191,930*	*$3,628,525*
Add: Non-cash activities		
Non-operating gains	450,000	465,000
Increase in line of credit	10,000,000	
Depreciation expense	6,350,000	5,902,441
Pension credit	(600,000)	
Subtotal	*16,391,930*	*9,995,966*
Other operating activities	*(1,370,381)*	*(993,059)*
Cash provided by operations and non-cash activities	*15,021,549*	*9,002,907*
Less: Investing and financing activites		
Capital purchases	(5,750,000)	(6,000,000)
FY 22 ED project spend		(6,400,000)
Transfer from SVHC Foundation		7,741,500
Pension plan funding	(3,000,000)	
Repayment of advances	(8,500,000)	(7,200,000)
Long term debt payments	(464,086)	(250,000)
Cash used for investing and financing activities	*(17,714,086)*	*(12,108,500)*
Net increase (decrease) in cash and equivalents	***($2,692,537)***	***($3,105,593)***

The past few years the Medical Center has invested in itself from cash reserves and investment earnings from its parent organization. The Medical Center reports 42.9 days cash on hand, however, the Medical Center's and its parent organization consolidated day's cash on hand and investments are projected to be approximately 213 days as of September 30, 2022.

Below are summary points of material interest included in the budget:

NO provisions are included in the FY 2022 Budget for a "Surge" or "Shutdown" related to the COVID-19 pandemic, however, provisions are included in the budget to assure the safety of our Patients and Employee's. Additional costs have been provided and will receive constant evaluation. NO Federal or State "Stimulus" funds have been included in the FY 2022 Budget.

Revenue—Rate/Price

- The effective charge master increase of 4.8% is being requested;
- Based upon what management is seeing the commercial insurance volumes are budgeted to increase in FY 2022;
- Included in the budget is an increase in non ACO Medicare reimbursement of 1% for FY 2022;
- Provider reimbursement has not been increased or decreased for FY 2022 due to changes in the wRVU's and proposed fee schedules;
- Vermont Disproportionate Share Payments (hereafter "DSH") are budgeted to decrease slightly;
- Indigent care (bad debt and charity care) is budgeted to increase by approximately $400,000;

Revenue—Volumes/Services

- Increased patient visit volumes, mainly in the primary care setting is the most significant area of in the Medical Group budgeted increase;
- Increased providers and the increased volume in orthopedic surgeries and endoscopy service;
- NO new services are anticipated.

Operating expenses

- A 3% salary increase was included;
- FTE's of 796, 17 FTE's higher than the FY 2021 budget mainly due to direct and indirect COVID-19, needs;
- Provider tax increase of approximately $794,000 from FY 2021 Budget based upon management's estimate and prescribed formula;
- Provisions are included for to maintain safety measures for our Patients and Employees related to COVID-19;
- Inflationary increases are included in supplies and parts of purchased services of approximately 2%;
- OneCare VT participation fees of approximately $1,200,000 for FY 2022 are included.

Capital

The FY 2022 capital budget and investments is $6,000,000. The ED Modernization project capital spend in FY 2022 is estimated to be $6,400,000 of the over $25 million approved.

Other items

In FY 2022, the frozen defined benefit pension plan will be terminated. The defined benefit plan will be fully funded in 2022. This termination process allows greater flexibility for plan participants and no participant will lose any accrued benefit as a result of this termination. It also secures plan and moves the administration of the plan to a highly rated company. The benefit to the Medical Center to terminate the plan it will remove the costs and time to administer the plan.

As a result of the termination there is an estimated $49.7 million non-cash settlement charge on the Statement of Operations. This charge is the estimated accumulated charges which were recorded annually on the balance sheet in unrestricted net assets on the statement of changes in net assets.

Management's Comments

The FY 2022 total NPSR budget was prepared utilizing *"fee for service"* models then split between "*fee for service"* and "*fixed prospective payment"* revenues. The Medical Center has been participating in the Medicare, Medicaid and Blue Cross QHP "risk models". ***The "upside and downside risk" was not considered in the budget preparation.*** No upside revenues were recorded or included in the budget and there were no downside risk reserves recorded as well. The neutral midpoint was included in the budget. However, it is worth noting that Management's philosophy is to conservatively record *actual* results based upon the best information available at the time of the financial statement close.

The FY 2022 Budget is highly dependent on volume and revenue levels reaching budgeted levels. In FY 2021, Inpatient, ER, Outpatient Referred Laboratory Services (non COVID testing) and the Medical Group volumes are not achieving budgeted levels. These area's represent nearly 60% of the Medical Center's NPSR. The operating room, endoscopy services and radiology services are all exceeding plan in FY 2021.

B. YEAR-OVER-YEAR and RECONCILIATIONS

i. Net Patient Revenue and Fixed Prospective Payments (NPR/FPP) Overview

The $177,594,439 of NPSR is an increase of $10,505,311 or approximately 6.3% when compared to the FY 2021 budget. Excluding the FY 2022 COVID-19 related revenues the increase is 5.7%. Comparing FY 2022's NPSR budget to FY 2021's NPSR budget can be somewhat misleading. The FY 2021 budget was prepared with significant uncertainty. COVID-19 had a significant impact on SVMC's operations and volumes in FY 2020 and FY 2021. When compared to the projected FY 2021 the NPSR increase of $8,112,776 is 4.8%.

In the FY 2021 projected there are significant revenues from COVID-19 patients both inpatient and outpatient so comparatives to projected are difficult.

When preparing a NPSR comparison of the FY 2022 budget to the FY 2019 actual NPSR, the FY 2022 budget the annual increase is approximately 2.77% and if the COVID-19 revenues are eliminated the annual increase is approximately 2.5%, a full percentage below the GMCB guidance for that three year period.

FY 2022's budget increase has two high-level components, rate and volume when compared to the FY 2021 budget. The rate change is an increase of approximately $5,130,322 or 3.0% which will be discussed in the charge request section. The "volume" component is an increase of $5,374,989, or approximately 3.3%.

Table #4 will show the components of the budget changes, budget to budget.

Table #4 – FY 2021 NPSR budget rate and volume changes, budget to budget

FY 2021 budgeted NPSR	$167,089,128
Rate increases	5,130,322
Volume increases	5,374,989
FY 2022 NPSR Budget	***$177,594,439***

ii. Net Patient Revenue and Fixed Prospective Payments (NPR/FPP) Utilization

Table #5 below will list the major volume and services changes included in the FY 2022 budget compared to the FY 2021 budget.

Table #5 – Volumes and Service changes, budget to budget

	Amount	***Percent of FY 2022 NPSR***
Inpatient volumes	($2,055,000)	(1.2%)
Emergency room visits	(1,066,000)	(0.6%)
Outpatient surgical volumes	3,299,000	2.0%
Medical Group visit volumes	1,608,000	1.0%
Endoscopy services	1,140,000	0.7%
Medical infusion services	397,000	0.2%
CT Scans	297,000	0.2%
Lab COVID testing revenue	905,000	0.5%
Outpatient volumes and others	850,000	0.5%
Total volume and service changes in revenues	***$5,375,000***	***3.3%***

The original goal preparing the FY 2022 budget was to see if the Hospital realistically could get back to pre-pandemic levels. However, based upon current trends management was not able to achieve that goal. Below will provide explanations on several of the items included in the table above.

1. In the FY 2022 budget total admissions of 3,504 are budgeted to decrease from the FY 2021 budgeted admissions by 226 or 6.0%. This budget projection was based on current trends. The FY 2021 projections are 3,283 and FY 2019 volumes were 3,808.

2. Emergency room visits are budgeted to decrease by 10.0% from the FY 2021 budget. Emergency room volume has been the slowest volume to return to pre COVID-19 levels. Recent average weekly volumes are higher than previous months. The FY 2022 budget reflects a 6.9% increase in visits over FY 2021 projected volume.

3. Outpatient surgical volumes were based on the recent trend. Volume is budgeted to increase 6.6% from the FY 2021 budget. The surgical volumes is mainly due to a fully staffed orthopedic group and additional general surgery capacity based upon the group being fully staffed.

4. Endoscopy volume is budgeted 21% higher than the FY 2021 budget primarily due provider changes in this specialty and 9% greater than projections. This is mainly due to additional physician coverage.

5. Medical group volumes are budgeted at a level more consistent with historic levels in the FY 2022 budget. New providers under contract, at the time of the budget preparation were considered in the budget. Visits are budgeted to be 14% greater than projected and only 1.1% greater than FY 2021 budget. Visits are budgeted below FY 2019 actual.

6. Laboratory COVID-19 testing volume was budgeted at approximately 25% of the FY 2021 projected volume. With 80% of Vermonters being vaccinated it is anticipated that volumes in the areas of the Medical Center where the vaccine will be provided will be minor. Also, no provisions have been included for vaccine boosters.

Management is still uncertain of what will occur related to the volumes in FY 2022 and what effect the pandemic has had on human behavior related to health care.

iii. ***CHANGE IN CHARGE REQUEST***

In this budget we all requesting a gross charge master increase is 4.8%. Physician practice, Physical Therapy and related services charges as well as other identified tests or procedures will not be increased. Approximately 64% of the Hospital charges will be increased. Drugs and medical supplies continue on a cost plus method which will be consistently applied in FY 2022 as in FY 2021 and prior. Realization of the approximately $4.0 million is dependent on commercial insurance, Blue Cross and managed care volumes. The charge increase assumes no impact of COVID-19.

For Medicare and Medicaid payers the increase in gross charges will not directly increase NPSR. Commercial insurers the increase in gross charges will increase NPSR but not on a dollar for dollar basis. Commercial insurance impact varies depending on the individual payer contracts. Bad debt and free care are generally written off at charges therefore a rate increase will increase bad debt and free care by the charge increase amount. The charge increase impact on bad debt and charity care will be approximately $400,000.

Table #6 provides the components that pertain to the rate changes of approximately $5.1 million.

Table #6 – Rate changes included in the FY 2022 budget, budget to budget

	Amount	***Percent of FY 2021 NPSR***
Net realization of the charge increase, ***before*** bad debt and charity care	$4,033,000	2.4%
Commercial payer mix increase	880,000	0.5%
Medicare proposed rate increase	576,000	0.3%
Medicaid proposed rate increase	144,000	0.1%
Medicaid DSH decrease	(103,000)	(0.1%)
Subtotal	*5,530,000*	*3.2%*
Net change in bad debt and charity care	(400,000)	(0.2%)
Total changes in rate	***$5,130,000***	***3.0%***

Below are summary explanations of the above items.

1. Net realization of charge increase before bad debt and charity care--$4.0 million.

2. The FY 2022 budget was prepared with increases in commercial insurance volumes based upon recent trends. The historical volumes SVMC has seen an increase in Medicare volumes and decreases in commercial insurance volumes. This may be a result of COVID-19, the increase in the population, a change in how the population utilizes their health care dollar or it may be short lived in our service area. Management will be monitoring closely.

3. Medicare and Medicaid rate increase – in the budget for all Medicare and Medicaid patients is a 1% rate increase. These are based upon for Medicare the proposed Inpatient Prospective Payment System increases and management's estimates of the Outpatient Prospective Payment System changes. Medicaid is management's estimate.

4. The DSH payments are being reduced based upon the management estimates;

5. The charge increase impact as well as the overall impact of the local economy due to the COVID-19 and others will put additional pressures on the financial assistance policy and the ability for patients to pay their bills for care due to lack of insurance. The overall increase for this combined reduction of NPSR is $400,000 which includes bad debt and charity care

iv. Adjustments (physician transfers and accounting adjustments)

In the FY 2022 SVMC budget there are no physician transfers. In fiscal FY 2020 during the pandemic SVMC had to rebuild its Anesthesia services which until January of 2020 was a contracted service. The service is now part of the PSA agreement with Dartmouth Hitchcock. There are no accounting adjustments included except for the loss of the pension settlement in Non-Operating revenues.

v. Other Operating Revenue and Non-Operating Revenues

Other operating revenues are decreasing by $710,846 or 9.5%. Table #7 below shows the major changes.

Table #7 – Other Operating Revenues, budget to budget

FY 2021 budgeted – Other operating revenues	$7,505,174
340B contract pharmacy revenues – reduction	(1,450,000)
Grant revenue increase	304,000
Dietary revenues increase	79,000
Child Care revenues due to increase	74,000
Other changes, net	282,264
FY 2022 Other Operating Revenues	***$6,794,328***

It is expected that the Medical Center will see decreased volumes related to the 340B contract pharmacy revenues. This is mainly due to the pharmaceutical manufactures deciding to no longer participate in the program. Additionally, insurance plans are requiring patients to go to specialty pharmacies to obtain there pharmaceuticals which reduces SVMC 340B program benefits and NPSR. Later in the document the 340B program will be discussed in greater detail and its impact.

The comparison to the projected other operating is a reduction of nearly $1.3 million. Included in FY 2021 projected revenues are revenues related to the COVID-19 clinic which management believes will not re-occur.

Non-operating revenues are budgeted in FY 2022 to significantly change due to one transaction. The most significant change from budget and projection is an estimated $49.7 million non-cash settlement charge on the Statement of Operations. This charge is the estimated accumulated charges which were recorded annually on the balance sheet in unrestricted net assets on the statement of changes in net assets over the life of the pension plan. This entry is required by the accounting guidance.

vi. Operating Expenses

Operating expenses are budgeted in FY 2022 at $180,760,242 which is greater than the FY 2021 budget by $6,357,870 or 3.6%. Comparisons to the FY 2021 budget with the differences in volumes, COVID-19 activities as well as others is difficult to evaluate and explain the FY 2022 operating expenses. Management will attempt to be complete and brief in it explanations. It is management's opinion comparing to FY 2019's actual operating expense budget is a good starting point. The increase after removing the COVID-19 related expenses the increase is less than 3%, annually.

<u>Salaries, Fringe Benefits, Physician Fees, Contracts</u>

This category of expense on the GMCB reporting is $105,786,588 compared to FY 2021 budget of $100,712,715 or an increase of $5,074,413 or 5%. Below review the components of this expense.

Salaries and wages

Salaries and wages are budgeted at approximately $54,206,235 an increase of approximately $2,930,111 or 5.7% over the FY 2021 budget. The FY 2022 budget includes 795.4 FTE's up from 778.9 FTE's. Below are significant assumptions in the FY 2022 budget:

- Total budgeted FTE's of 795.4 are approximately 17 FTE's higher than FY 2021's budget but just 3 FTE's higher than FY 2021 projected actual FTE's. The budget to budget increase in FTE's is primarily due to new protocols and in the clinical areas;

- In FY 2022, management is providing for the wage increases of an average of 3%;

Table #8 identifies the components to the increase in salary and wage budgeted expense compared to the FY 2021 budget amounts.

<u>Table #8 Components of the Salaries and Wages budget changes</u>

	Amounts *(rounded)*
Compensation increase FY 2022	$1,609,018
FTE increases	1,067,880
Other changes	253,213
Net increase in salary and wage expense	***$2,930,111***

Salaries and wages in FY 2022 are budgeted to increase 1.9% over the projected FY 2021 and comparing to FY 2019 the three year average annual increase is 2.9%.

Employee Benefits

In the FY 2022 budget, the Employee Benefits are increasing by $1,169,221 or nearly 7.4% above the FY 2021 projected actual and the FY 2021 budget. Comparing to the FY 2019 actual and adjusting for the defined benefit credit the annual increase in employee benefits over three years is 1.8%. The employee benefit budget is $16,938,498.

- Health Insurance trends for SVHC/SVMC have been favorable for several years. After consultation with the Hospital's advisors and plan changes to occur at the beginning of the plan year will reduce costs approximately $500,000. Management is budgeting an increase of approximately 7.0% over projected FY 2021 costs in FY 2022.

- Workers compensation plan at SVHC/SVMC an increase in FY 2021 and we anticipate the trend to level off in FY 2022. Costs are budgeted to increase approximately $228,000 in the FY 2022 budget from the current budget. This is attributed to FTE count and some experience.

The other costs in this category are based upon historical and mandated percentage of salaries and wages. They include FICA, Defined Contribution Pension Plan, Life Insurance, and Short and Long-Term Disability.

DH Professional Services Agreement (hereafter "PSA") Costs

This category of expense is budgeted to increase by nearly $1,904,000 or 5.8% in the FY 2022's budget compared to FY 2021's plan. The total cost of $34,641,855 includes salary and wages for the contracted individuals as well as employee benefits, malpractice costs and approximately $400,000 of other support costs. Table #9 below provides FTE details provided via the PSA.

Provider FTE increases are in Primary Care, Anesthesia and Gastroenterology to accommodate anticipated volume increases in those areas.

Table #9 – PSA related FTE's

	FY 2021 Projected	***FY 2021 Budget***	***FY 2022 Budget***
Physician	65.44	64.44	70.00
Assoc. Providers	30.00	29.42	31.22
Total PSA FTE's	***95.44***	***93.87***	***101.22***

Medical/Surgical Drugs and Supplies

Drug costs are budgeted to decrease by $360,988 or 2.3% in the FY 2022 budget over the budgeted FY 2021. Over 80% of the drug costs are incurred in the Cancer Center each year and volumes based on current trends are down. The budget assumes continued drug cost savings in FY 2022 because of initiatives with DH to identify areas for savings and 340B program savings. This savings is at risk.

Health Care Provider Tax

The absolute dollar amount of the increase of over $794,221. The FY 2022 provider tax is budgeted at 6% of the projected FY 2021 revenue with an adjustment for the difference between the State's fiscal year and the Medical Center's fiscal year. The increase in provider tax represents over 12% of the Medical Center's increase.

Depreciation and Amortization Expenses

The depreciation and amortization expense will be budgeted at approximately $5.9 million. This is based upon a FY 2022 Capital Budget of $6,000,000 million and the remaining estimated useful lives of buildings and equipment acquired in FY 2021 and prior.

Interest Expense

Interest expense in FY 2022 is budgeted at $700,000. In order to maintain operating cash balances, repay the non-interest bearing advances as well as others, management is anticipating a slight increase related to utilizing the line of credit with TD Bank in FY 2022. In addition, there are several small capital leases expected to be executed in order to preserve cash in the capital budget.

Other Operating Expenses (Including ACO Participation Fees)

This GMCB category of expense is $58,328,290. Below are the significant components to this grouping of costs.

Supplies

The supplies expense budget is anticipated to increase $873,937 or 7.3% compared to the FY 2021 budget. The Medical Surgical supply expense budget is $12,788,365 compared to $11,914,423. This increase is driven primarily by operating room chargeable supply costs due to increased orthopedic volumes.

An inflation factor of 2% was included in the budget as well as additional costs for Personal Protective Equipment. Additionally, contract savings are currently being explored.

Purchase services, utilities, insurance and other

Included in this section is approximately $1,200,000 of OneCare VT dues. This is based upon FY 2021 actual and does not consider any recent proposals for the dues to be changed since they have not been approved by the OneCare VT Board or GMCB.

This category of expense is budgeted to decrease by $52,161 or -0.2%. Each significant area in this large category will be described. Below in Table #10 will provide details on the changes in the cost composition of this category of expense.

Table #10 – Purchase services, utilities and other significant changes, budget to budget

	Amount
One Care dues	($300,000)
Pulmonary MD locum	254,000
Oncology associate provider locum	263,000
Other changes	(269,161)
Total changes	***($52,161)***

Below are summary explanations of some of the changes in the FY 2022 budget compared to the FY 2021 budget.

Pulmonology MD Locum – The FY 2022 budget includes the purchase of additional locum services to cover for the full-time physician reducing his hours worked;

Oncology MD Locum – The FY 2022 Budget includes a recent contract with a physician locum to cover a vacancy in the Oncology practices

vii. Operating Margin and Total Margin

The FY 2022 proposed “Continued Recovery Budget” assumes approximately a 2% operating margin and a negative 24.7% total margin. Eliminating the settlement charge on the defined benefit pension plan the total margin would be 2.2%.

The FY 2022 operating and total margins are down from the historical performance levels as demonstrated by the table on the following page. SVMC’s goal is to maintain annually 3% operating margin to reinvest in itself and assuring the high level of quality care to the patients we serve. SVMC’s operating performance has been constant over the past several years as demonstrated by the table below.

Table #11 – Operating Margins FY 2016 to present

	Operating Margin Actual	***Operating Margin Budgeted***
Fiscal Year 2016	3.40%	3.00%
Fiscal Year 2017	3.70%	3.00%
Fiscal Year 2018	4.60%	3.90%
Fiscal Year 2019	3.30%	3.60%
Fiscal Year 2020**	2.80%	3.40%
Fiscal Year 2021****	2.70%	0.10%
Fiscal Year 2022		2.00%

*** Includes Federal and State Relief Funds*
***** Includes Federal Relief Funds and is management's projection*

In FY 2020 and FY 2021, if the federal stimulus funding is not included in the operating margin calculation FY 2020 would be a breakeven and FY 2021 would be approximately a 1% operating margin.

The FY 2022 operating budget does not meet SVMC's goal. Management is of the opinion that this "Continued Recovery Budget" is a step in the right direction. FY 2022 will continue the post pandemic recovery, however, we are sure there will be new challenges to achieve the 3% operating margin goal in FY 2023 and beyond.

C. RISKS AND OPPORTUNITIES

SVMC reviews its risks and opportunities routinely with the Board of Trustee's. The items below do not address all the environmental, economical, and political situations. The following will address items that may have a material impact SVMC's operating budget for FY 2022 and into the future.

Risk – SVMC participation in 340B Program -- SVMC is a Sole Community Hospital and Rural Referral Center, the Federal Disproportionate Share Percentage (hereafter "DSH") needs to be 8 percent or greater from the most recently filed Medicare Cost Report as well as meeting other requirements to participate in the program. In the last fiscal year, FY 2019 that was not affected by COVID-19 SVMC's benefit from the program was nearly $6.7 million. Recent trends has seen SVMC's Medicaid inpatient days as a percentage of total inpatient days decline. Higher length of stays due to COVID-19 patients and efforts in managing the care of Medicaid patients are the contributing factors to SVMC's Federal DSH percentage being reduced. SVMC's FY 2021 year to date, Federal DSH percentage through May 31, 2021 is approximately 5.5%. If this trend continues SVMC will not qualify for the 340B program effective April 1, 2022.

On the positive note, SVMC is not alone in this situation. Currently, (as of June 30, 2021) there is both a House bill and a Senate a bill, with bipartisan support, drafted which simply would not use the Federal DSH calculation where the Public Health Emergency was ***not*** in effect, as a result SVMC would continue to participate in the program.

SVMC in FY 2022 has budgeted to be included in the 340B program for the full year.

Risk/Opportunity – Patient Volumes/Payer Mix – as demonstrated by the FY 2021 volumes compared to the FY 2021 budget especially in the inpatient setting and Emergency Room volumes have not achieved target and if you remove the COVID-19 cases the variance is greater. There is upside opportunity if volumes return to pre pandemic levels, however, recent trends are indicating volumes could even be lower than FY 2020's actual.

Included in the budget is an increase in commercial payer mix. Prior to the pandemic SVMC had been seeing increases in Medicare volumes. Since the beginning of FY 2021 commercial volumes have increased. Included in the budget is an additional $880,000 of commercial volumes. If that shifts to the pre-pandemic trend to Medicare the swing in revenues could be nearly $1.5 million lower.

Risk/Opportunity – Payment rates Medicare – Included in the budget is a 1% increase for all Medicare revenues, both fee for service and fixed prospective payment model. The possible 4 to 5% increase for Medicare is still being discussed for the fixed prospective payment models, according to OneCare VT finance team. Each 1% is worth over $200,000 in additional revenues to SVMC in the model.

Opportunity – New Providers and Albany GI – Included in the budget are additional providers. Included in the budget is the historical expected volumes for such providers. If demand increases SVMC is better positioned today than in many years to meet the demand with the increased provider coverage.

Risk/Opportunity continued participation in OneCare VT – CY 2019 SVMC did not perform well and had a negative impact on the financial performance of the Medical Center. Continued negative outcomes could have permanent effect on the Medical Center's financial health. If the demographics' improve and the efforts further improve the health status of the Medicare and Medicaid population exists there is opportunity for SVMC. CY 2020 and to date CY 2021 due to the public health emergency there has been no downside risk for the hospitals. The question is how is the public going to access health care in a post pandemic environment.

Risk – Staff retention and recruitment – included in the budget are pay increases. SVMC's will be monitoring the market closely. No agency staff has been provided in the budget. SVMC's average hourly rate been below the VT averages prior to the pandemic. Additional funds may need to be allocated. The workforce is aging. Recruitment of qualified individuals to replace the aging workforce will create challenges. The risk may be reduced through the arrangements with local colleges and the use of remote working.

Risk – Health Benefits – SVMC's self-insured health plan has had positive claims experience over the past three years. How much of the positive experience is due to the pandemic over the past two years? SVMC is increasing in the budget the cost sharing with employees. Will this impact the use, costs, retention and recruitment?

Risk – Drugs – included in the budget are two inflation factors which are lower than published ranges. Drug costs are budgeted to increase between 5 and 8%. Included in the budget is 5%. In addition, there are additional pressures on the revenue side since several health plans in our region are requiring patients to get their pharmaceuticals from specialty pharmacies and have them delivered to SVMC for administration.

The above are just a few items specifically addressed in the FY 2022 budget. There are many other risks and opportunities facing the healthcare industry and society today.

D. ONECARE VERMONT PARTICIPATION

Currently, SVMC is planning to continue to participate in the Medicare, Medicaid and Blue Cross VT as well as the other minor programs. SVMC reserves the right to withdraw from participation since as of June 30, 2021 the risk corridors both upside and downside have not been agreed to by OneCare VT with the payers to management's knowledge.

SVMC has provided approximately $1.2 million in dues in its budget. As previously discussed this is based what SVMC is currently paying. OneCare VT's finance management has communicated that it is their intent not to increase the dues to SVMC and other participants, however, OneCare VT needs to have this plan approved by its Board and the GMCB which will happen later this year.

The maximum risk liabilities and upside opportunity have not been fully negotiated by OneCare VT with the payers and the table below is to the best of SVMC's knowledge at this time.

Program	***Risk***	***Opp.***
Medicare	2%	2%
Medicaid Traditional	2%	2%
Medicaid Expanded	2%	2%
BCBSVT QHP	0%	3%
MVP QHP	0%	3%

This is SVMC's modeling using the above parameters and the anticipated volumes and revenues. The the estimated downside risk is nearly $2 million and the upside is slightly higher. *These are SVMC's estimates at this time and are subject to change. It is again worth noting these amounts are SVMC's estimates and in preparing this budget management does not include any downside risk or upside opportunity in its budget request.*

The table below provides estimated NPSR breakout by fee for service and fixed payment model.

Total NPSR breakout

Fee for service NPSR	$135,594,439
Fixed prospective payment NPSR	42,000,000
Total NPSR	***$177,594,439***

Fixed Prospective Revenue (est.)

Medicare	$27,000,000
Medicaid	9,800,000
Blue Cross exchange and commercial	5,200,000
Total	***$42,000,000***

SVMC's reserves the right to withdraw from the respective payer plan if the negotiated risk corridors are not acceptable to SVMC's Leadership.

G. CAPITAL INVESTMENT CYCLE

The Medical Center currently has an approved CON for the Modernization of the ED for over $25 million. This CON is for a significant upgrade to the Emergency Room, front entrance, traffic flow and wayfinding. No operating costs associated with the Emergency Room project are included in the FY 2022 operating budget.

In FY 2022 SVMC will submit an estimated $12 to $13 million CON to modernize the Cancer Center.

The capital spend in FY 2022 will be $6.0 million. Consideration on a greater amount for FY 2022 will be evaluated by management and the Board of Trustee's. Most of the remaining FY 2021 and FY 2022 will be routine replacements of aging equipment. SVMC's age of plant exceeds 18 years.

Management in the coming years will be evaluating significant changes to the physical plant of the Medical Center. In addition, we anticipate changes to its current information technology platform, the development of partnership for clinical programs, residency programs, as well as possible corporate affiliations. The evaluation of each continues.

* * * * * *

If there are any questions or comments please do not hesitate to contact Stephen D. Majetich, Chief Financial Officer at 802.447.5011 or Stephen.majetich@svhealthcare.org.