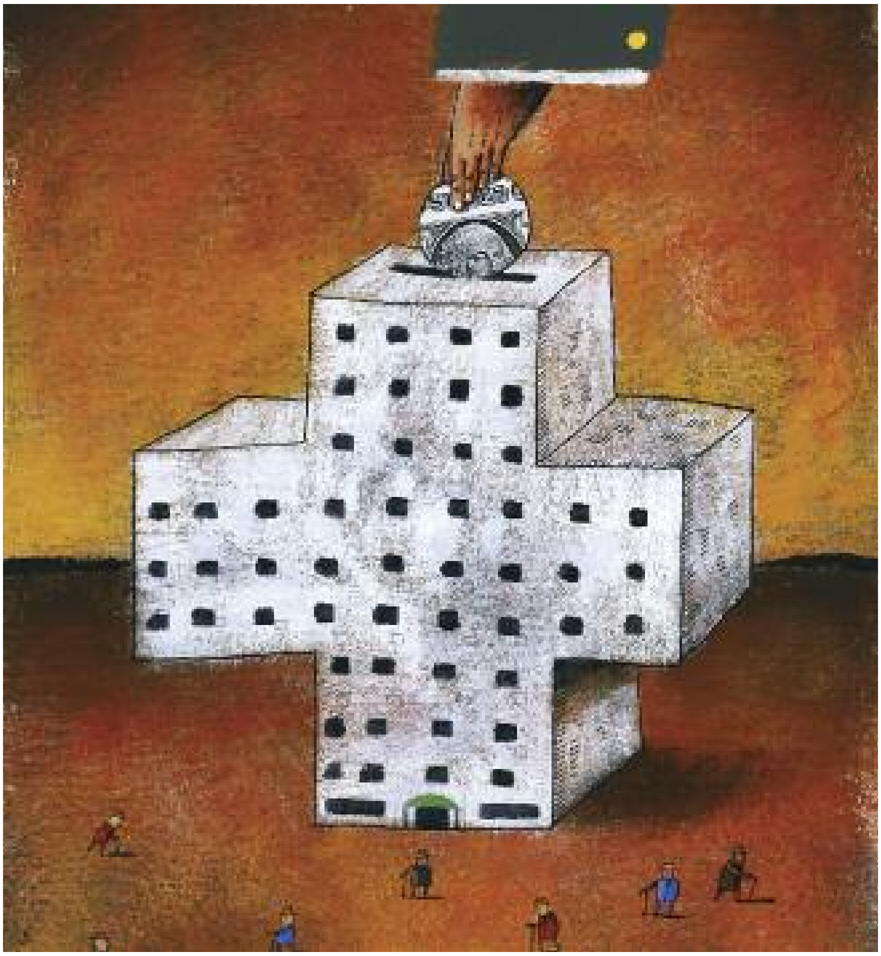
It Takes a Community

To save their hospital and local economy, trustees turned to residents for support

By Alan P. Richman



On Jan. 1, 2011, Effingham Hospital, a 25-bed critical access hospital and nursing home, held a party to celebrate the groundbreaking of its much-anticipated 58,000-square-foot modernization project. The construction expands the facility to accommodate newly acquired, state-of-the-art technology for its emergency department, inpatient and outpatient surgery suites, laboratory and imaging departments, while converting existing space in its nursing facility to a dedicated Alzheimer's unit.

On Jan. 27 of this year, with Georgia's lieutenant governor in attendance, Effingham Hospital's new facility opened six weeks ahead of schedule. During its 13-month construction period, the hospital's modernization project generated $13.4 million in economic impact for the 14,000 residents and businesses of Effingham County, Ga., 30 miles north of Savannah. With the project's completion, the hospital is expected to add 71 new full-time jobs and produce $4.8 million per year of additional revenue to the county.

Like most rural hospitals in recent years, Effingham in 2009 was assessing its continued viability. Ongoing operating losses, coupled with the impact of municipal budget deficits, a recession and insurance cuts, suggested a bleak future for the independently managed county hospital. With its annual county tax pledge of 2 mills (that is, $3.6 million in property tax) scheduled to expire in 2013, the hospital also was facing the prospect of losing its uncompensated care subsidy. The hospital was in dire need of modernization, but the loss of county tax support made financing the project unlikely.

Well-known Threats

Times have not been easy for community hospitals like Effingham. In Georgia, 41 hospitals have closed since 1980, and 62 percent of rural hospitals are in the red. In the last five years, six of these hospitals had turnover in key management positions and three changed ownership. With increasing cuts in Medicaid and rising numbers of uninsured, it is projected that at least 15 Georgia rural hospitals could face a real threat of closure over the next year.

Built in 1969, Effingham Hospital faced its own share of problems. For

IMAGE BY JAMES YANG/SIS

years, its surgical suite had been severely restricted by the size limitations of its physical plant, which couldn't accommodate the installation of long-needed surgical and diagnostic imaging equipment. Out of 13,600 emergency department visits in 2009, Effingham Hospital performed only eight inpatient surgeries. Essentially all candidates for inpatient surgery were triaged and referred to a tertiary care hospital in Savannah. Despite the $3.6 million in annual tax support, the facility was outdated and limited in the services it could provide. The hospital board knew that its hospital was becoming an afterthought in the community and without a major change in its services, it would be on its way to extinction. To change its course, Effingham Hospital would require a sizable loan to fund a comprehensive modernization.

But how could the hospital afford a capital project? How could it borrow funds to finance the project, let alone cover the annual debt service costs with its soon-to-expire tax support? The only option for the hospital appeared to be either a long-term lease to an operator or sale to another hospital. The board deemed both options unacceptable and knew the county commissioners would agree. There was no way an outside entity would take financial control over the hospital. The only party that could responsibly manage the hospital and reinvest in the future of the community was the community itself. As the linchpin of the local economy, the hospital had to maintain local governance and control.

Making the Case

The hospital board knew that a failure to self-finance its needs would result in a sale, merger or closure. As frequent attendees at Georgia Hospital Association meetings, board members were well-aware of the failed mergers, takeovers and external management arrangements of community hospitals both locally and nationwide. Board members knew that the only way Effingham County could count on a future for its hospital would be to remain independent while modernizing the facility. They had confidence that its county residents would support an extension of their tax pledge to finance a modernization project that was designed to revitalize their hospital and local economy. The board still had to convince the county commissioners to change their minds and renew the expiring tax support.

First, hospital board members needed to be certain that they were headed in the right direction. They had to be convinced the project design and scope provided the maximum benefits for the hospital at the minimum cost. So, the board commissioned independent analytical reports: a financial feasibility study to verify the ability to afford a capital loan; a capital markets assessment to determine the most effective financing method for the project; and an economic impact analysis to define the expected contribution to the local economy resulting from the hospital project.

Next, armed with consultants' reports and a comprehensive financing plan, the board was ready to make its case public and advocate for a renewal of the annual tax levy directly with local businesses, residents and county officials.

Third, the hospital needed to convince a lender or credit enhancer that a modernized facility would attract new physicians, support new services and be an attractive credit risk for a $30 million loan.

Fourth, of paramount importance would be the successful recruitment of a new surgeon to tap into the dormant demand for surgical care at Effingham Hospital. Hospital management knew they had to offer a compelling case that its future would be promising if they had an updated hospital.

Getting the Community on Board

An application for Federal Housing Administration Section 242 mortgage insurance to guarantee a $31 million loan to the Effingham County Hospital Authority would need to be submitted to the U.S. Department of Housing and Urban Development no later than Sept. 1, 2010, in order to close the financing by year-end 2010. A 2010 bond closing was essential to finance Effingham's loan with Recovery Zone Economic Development Bonds through a federal stimulus program that was due to expire for new applicants on Dec. 31, 2010. While RZEBs provided a 45 percent federal interest-rate subsidy for eligible borrowers, HUD wasn't expected to approve the application without the commitment of the county commissioners to extend the property tax levy. Getting the county commissioners' consent was essential.

Initially, only one commissioner supported the expansion project and renewed taxes, but there was reason for hope as the others were requesting more information to reconsider their position. Trustees for the Effingham County Hospital Authority were the most effective public and private advocates because they provided an insider's perspective of the value of the project for the health of the hospital and the community. They garnered support for the project through meetings with business leaders at local civic associations, where they displayed the architect's renderings of the construction and explained how the project met the vision and mission of the hospital, according to Norma Jean Morgan, Effingham Hospital CEO.

"The trustees participated in 'lunch and learns,' church breakfasts and community dinners to urge citizens to embrace the hospital expansion project and ask their county commissioners to support it," Morgan adds. Trustees gained the backing of the local newspaper by explaining the merits of the project. Empowered by a community mandate, the eight-member volunteer hospital board of trustees individually lobbied their respective county commissioners.

The Fine Print

County commissioners were concerned about the expansion project's impact on county finances. Could Effingham Hospital service debt of $31 million? How would the financing affect the debt burden and economy of the county? Would HUD and FHA 242 mortgage insurance in any way take control of the hospital away from the board and shift it to Washington?

The hospital chairman was ready to present the case to the county commissioners with support from financial consultants and an economist. In public meetings, the commissioners were provided with a project feasibility study that detailed how the project would recruit new physicians and expand service. One new surgeon could be expected to increase surgeries from eight per year to 100 each month. The project would increase the hospital's case mix, increase market share and enhance operating revenue. By leveraging annual taxes of $3.6 million, the hospital would profitably cover its debt service and cash reserves.

An economist presented a community-impact analysis detailing three scenarios for the hospital and the commissioners to consider:

1. No hospital modernization and ending the annual county tax pledge. Eliminating tax support would force the closure of the hospital within two years and cost the jobs of 283 full-time hospital and nursing home workers. The immediate loss to the county within one year would be $2.4 million and by 2014, the loss would reach $13.6 million. A hospital closure was forecasted to drive down residents' disposable income by $7 million by 2014. The county would lose its only hospital facility and require local residents to travel more than 30 miles for basic acute care.

2. No hospital modernization but maintaining the annual county tax pledge. Even if taxes stayed as they were, without a new facility, the county was merely postponing the hospital's closure. Without the required facility improvements, low utilization and operating inefficiencies would accelerate operating losses that no longer could be offset by current levels of county tax support.

3. Proceed with the capital financing project and extend the annual county tax pledge for 25 years. While stemming out-migration of primary hospital care to Savannah, the new facility would stimulate the economy by adding jobs. Personal income was forecasted to increase $2.8 million per year by 2014 and disposable income by $2.5 million per year.

The board chairman stressed to county commissioners that with an FHA 242 mortgage insured loan, the county taxpayers would not be guaranteeing the hospital's debt. Instead, pursuant to the hospital's loan documents, taxpayers' financial pledge would be limited to the annual 2 mill levy. HUD was looking at the taxes as a supplement to the hospital's revenue and not a guarantee. It would assume the credit risk of Effingham Hospital and its capital project and would not look to the county to bail out any unforeseen future financial shortfall. Limiting the exposure of the county, coupled with a federal interest subsidy and access to AAA borrowing rates due to FHA 242 mortgage insurance and Ginnie Mae (the Government National Mortgage Association), collateral could be expected to result in a borrowing rate to Effingham Hospital below 4 percent.

The case for tax support was too good to refuse, and the commissioners reversed their votes from 1 to 5 against to 5 to 1 in favor of the tax levy for the hospital and the modernization project. According to CEO Morgan, the trustees' powers of persuasion and personal relationships convinced commissioners to get on board in order to complete the financing by Dec. 31, 2010. The project would go foward.

From the momentum of the construction project and physician recruitment, inpatient admissions increased 73 percent, outpatient surgeries rose by 107 percent and outpatient visits were up 3 percent for the last fiscal year. Patient days and profits have increased 59 percent and 33 percent, respectively. In the end, the trustees of Effingham Hospital proved that their hospital could prosper in the hands of their community. **T**

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Carefully Crafted Message

A consistent message from the trustees and management highlighted five ways in which the project and tax pledge would benefit the county:

Demographics: Effingham is one of the fastest-growing counties in Georgia, with a solid job market and well-regarded school system. The average age is 33. Comprehensive hospital services would benefit this community of growing families and encourage relocation from Savannah and elsewhere.

Physician recruitment: The county is underserved by both family practice and specialty physicians. Surgeons in particular require a modern hospital before they will consider operating on a permanent basis. With an expansion under construction, Effingham Hospital could recruit an orthopedic surgeon and a family practitioner within a year.

Tax burden: The tax burden was minimal. The average taxpayer in Effingham would pay $80 per year to support the hospital expansion. Comparatively, the average household pays $168 for garbage pickup.

Financing: Structured to minimize borrowing costs, Effingham Hospital's financing may have resulted in the lowest long-term fixed interest rate loan for any hospital in Georgia. With limited tax support from the county, the combination of Federal Housing Administration Section 242 mortgage insurance and a federal interest subsidy produced a 3.63 percent fixed-rate, 27-year loan.

Right-sized project: Effingham was not building a brand-new hospital. The project was a no-frills renovation and expansion that enhanced the current campus by retaining well-maintained major parts of the existing facility, along with renovating reclaimable space to complement an expansion of the hospital's physical plant. — *A.P.R.*

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