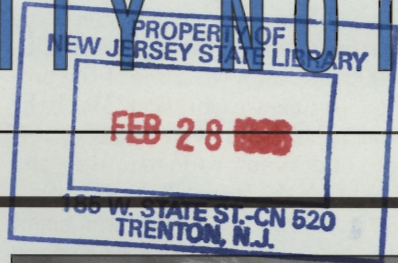


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AUTHORITY NOTES



New Jersey Health Care Facilities Financing Authority

February 1996

AUTHORITY LOWERS FEES

In recognition of borrowers' needs to reduce costs, the Authority recently adopted a new, lower fee schedule. Authority Chairman and Commissioner of Health, Len Fishman, stated that "this is just another step in our ongoing efforts to help borrowers in meeting the challenges they face." The restructured schedule will result in the following:

- Elimination of all initial financing fees;
- Elimination of the project management oversight fee;
- Reduction of the standard annual fee for non-FHA-insured issues to six and one-half basis points (.065%) of the original principal amount of bonds with an annual fee cap of \$50,000; and,
- Reduction of the standard annual fee for FHA-insured transactions to one-half of the non-FHA-insured issues.

The new fee schedule will apply to all transactions for which a Commitment to Finance is received by the Authority on or after January 1, 1996. The Authority also recognized the borrowers who, in anticipation of completing a financing, have executed a Commitment to Finance and have submitted a portion of their initial fees. Both the annual fees for the first year and the balance of the initial fees have been waived for these borrowers. The fees for borrowers whose Authority bond issues are refunded through another issuer will be determined using the standard annual fee and applying it to the amount of bonds outstanding at the time of the refunding (the annual fee will continue as long as the escrow is in existence). For issues completed prior to January 1, 1996, fees will continue to be charged in accordance with the previous fee schedule.

Since its inception, the Authority has charged borrowers both an initial and an annual fee for the professional services rendered in connection with the development and financing of a project and the annual administrative services provided during the term of the bond issue. Project Management Oversight fees were added in 1994 to cover the cost of providing that function. As a result of the elimination of initial fees alone, borrowers will save between \$25,000 and \$70,000 on non-FHA-insured bond financings.



Elizabeth E. Randall, Esquire, of Westwood, was appointed Commissioner of Insurance by Governor Whitman effective December 7, 1995, having served as Acting Commissioner since October 12, 1995. Ms. Randall will serve as a member of the Authority during her tenure as the State Commissioner of Insurance.

At the time of her nomination, Ms. Randall was serving as the State Commissioner of Banking in New Jersey. Prior to her appointment as Banking Commissioner, Ms. Randall was in-house counsel for Bergen County. She also served as a member of the State Assembly representing the 39th Legislative District from 1985 to 1991.

FINANCIAL FEASIBILITY STUDY POLICY MODIFIED

In keeping with its continuing objective to be more responsive to the needs of the state's health care providers, the Authority recently modified its policy on the preparation and submission of financial feasibility studies. The Authority made the modifications following an in-depth examination of its existing policy, the impact on future financings and discussions with the credit community, both nationally recognized credit rating agencies and municipal bond insurance companies. These discussions provided assurances that outside studies do not necessarily confirm a borrower's ability to make debt service payments. In fact, it has recently become standard practice within the credit community to review management projections instead of requiring studies prepared by outside parties because such projections reflect the financial and operating performance of a potential borrower as well as the skill and strategic thinking of its management team. The new policy on feasibility studies reflects the following modifications:

- Borrowers with transactions that receive investment grade ratings, letter of credit commitments, and/or municipal bond insurance will not be required to submit a financial feasibility study;
- Borrowers with nonrated transactions whose projects are not expected to have a material (5% or more) impact on revenues and/or expenses will not be required to submit a financial feasibility study;

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AUTHORITY NOTES has been developed to communicate directly with those who are involved in the financing of New Jersey's health care institutions. It will be published periodically, as needed, to convey changes in Authority policy and practices, tax law and regulations, and to suggest ways to decrease capital expenses and increase revenues. The Authority welcomes your input, ideas and suggestions.

YEAR END REVIEW

At the December Authority Board meeting, Executive Director Edie Behr recapped the Authority's activities and accomplishments for 1995 and set forth some of the projects contemplated for 1996. In her presentation, Ms. Behr noted that, "1995 was a year measured not in terms of new issue volume, but rather, one spent repositioning the Authority to face the challenges of the future."

She noted that a considerable amount of time was spent during the year exploring the needs of the borrowing community. Authority staff met with borrowers, potential borrowers and the industry's trade associations to better understand current financing needs.

And, an improved approach to investing its own funds was adopted by the Authority resulting in the use of investment earnings to support Authority operations and allowing for the reduction of borrower fees (see "Authority Lowers Fees" article on page 1).

The Authority modified its policy on the preparation and submission of financial feasibility studies (see article on page 1). In addition, a policy to negotiate new, stronger covenants into bond issues for hospitals was adopted.

Ms. Behr was especially pleased to report on the success of borrower participation in the financing process and that "we now include borrowers in the selection of bankers for their transactions, asking for their preferences for firms to be interviewed, including them in the interview process, and welcoming their input during our decision making process."

In 1995, approximately \$6.2 million of plant and equipment funds were released to five borrowers. Two collateral substitutions, two waivers, two modifications of project description and one amendment to obligated group definitions were approved.

The Authority was successful in modifying the Capital Asset Program, Series E Issue (see "CAP" article on page 2.)

Authority Note\$, the agency's newsletter, was developed to enhance communication with the industry. The Authority continued its activity on behalf of borrowers in the National Council of Health Care Facilities Finance Authorities.

"We will continue our dialogue with the Federal Department of Housing and Urban Development in an effort to improve and streamline their FHA insurance program", Ms. Behr noted. "Also in 1996, we will be reassessing trustees, credit and liquidity providers, auditors, printers and bankers. We will carry out the new investment policy. We will actively market the Capital Asset Program and we will create a statistical data base for nonacute care borrowers.

"We have explored ways to utilize the \$2 million set aside to support the credit of community health care providers located in the four cities designated by the Governor's Urban Initiative and will make a recommendation to the Board in 1996. Significant progress has been made in the development of a workable structure for the ACCESS Program so that financing for community health care providers can be accomplished early in 1996.

"In addition, the most significant initiative is the pursuit of a legislative expansion which will allow us once again to provide financing for all of the health care needs in New Jersey."

Each of the financings completed during the year represented tangible evidence of the Authority's main objective—to meet borrowers' needs and reduce costs:

- Warren Hospital's bond issue was accomplished with insurance from Asset Guaranty Insurance Company resulting in lower interest rates and greater savings to the borrower;
- The Kennedy Health Facilities transaction represented the first competitively bid FHA-insured bond issue in the country and resulted in 33% savings to the facility;
- The Memorial Hospital of Salem County and New Brunswick Affiliated Hospitals, Inc. transactions were completed utilizing the competitive approach to private placements. The interest rates achieved were significantly lower than those offered initially by investors; and,
- Project Management Oversight, restructured as an in-house program, resulted in savings of \$300,000.

COSTS LOWERED FOR CAPITAL ASSET PROGRAM, SERIES E

The Authority and Morgan Guaranty Trust Company (the "Bank") recently completed negotiations to reduce costs related to the Series E pool and to simplify the loan application procedure. First and foremost, the interest rate on the bonds has been reduced by 24 basis points and the Bank will consider partial rebates to borrowers of loan interest payments on a case-by-case basis. The Bank has also agreed to expanded allowable investments proposed by the Authority which may produce higher yields on the invested funds, thus reducing the loan rate to borrowers. In addition, there is no longer any minimum or maximum loan size. The Bank will perform an independent analysis of each borrower and base the security requirements on the results of its analysis. And, the Authority's recently adopted new fee schedule will result in no filing, application or initial fees being required of the borrower.

Created in 1985 through the sale of a \$100 million bond issue privately placed with the Bank, the Series E Capital Asset Program offers its borrowers cost-effectiveness, efficiency, flexibility and security options. The bonds mature in 2015 and allow for recycling of loans until that time. There are no prepayment penalties to borrowers, simply a 45-day notice of prepayment. Since the tax-exempt bonds were issued prior to the enactment of the 1986 Tax Reform Act, there is no arbitrage rebate calculation; loans for private uses (e.g., parking garages and medical office buildings) can be made more liberally; loans will not limit borrowers with regard to the terms of management contracts; and nonhospital 501(c)(3) organizations are not subject to the \$150 million cap on monies borrowed. In addition, borrowers will not be required to prepare secondary market disclosure information as the sale of the bonds occurred in 1985.

The loans have been used for a wide spectrum of projects including fixed and major moveable equipment, construction/renovations, and leasehold improvements. One financing currently being pursued by the Authority through the Capital Asset Program is for an energy management system.

Potential borrowers interested in applying for a loan or obtaining additional information should contact Suzanne Walton at the Authority's offices. She can be reached at (609) 292-8585, Extension 17.

FINANCIAL FEASIBILITY STUDY POLICY MODIFIED

(continued from page 1)

- If a borrower meets the above guidelines, financial projections prepared by management or its consultant for a prospective five-year period will be acceptable;
- Borrowers with nonrated transactions whose projects are expected to significantly affect the revenues and/or expenses of the borrower will be required to submit a financial feasibility study; and,
- There is no longer a prohibition against using a borrower's auditor as its financial feasibility consultant.

The Authority's new policy will result in savings of \$50,000 to \$100,000 per borrower. Of course, financial feasibility studies required by the terms of certain documents will not be affected by this recent Authority action.

NOTEWORTHY

- A preliminary review of the third quarter 1995 Apollo reports indicates a slight drop in liquidity and profitability for New Jersey hospitals (e.g., median days cash on hand went from 78 to 74 days and median operating margins went from 2.60 to 2.08). A few other indicators suggesting an improvement are: median age of plant is down slightly and median expense per adjusted admission is down.
- Standard & Poor's Corporation has completed its credit review of 22 hospital bond ratings. As a result, 2 were upgraded, 3 were downgraded and 17 ratings were confirmed.
- For those borrowers whose transactions were issued after July 3, 1995, continuing disclosure information must be provided on an annual basis to each nationally recognized municipal security information repository ("NRMSIR") as required by the Securities and Exchange Commission. A current list of NRMSIRs (which can change from time to time) is available from the Authority. Please refer to your Loan Agreement for more specific information or call your account administrator at the Authority's office (609-292-8585) for assistance.
- It was recently reported that a faculty practice plan at University of Pennsylvania Medical System will pay the federal government \$30 million to settle both fines and claims of Medicare billing abuse. The physician members were said to have submitted claims to Medicare for work performed by medical residents; submitted inflated claims to Medicare for inpatient consultation services; and submitted claims for services without adequate documentation. By announcing the settlement, the U.S. Attorney's office is hopeful that the nation's other 1,200 teaching hospitals will closely audit and monitor their own billing practices and voluntarily notify the federal government of any discrepancies. Approximately 70 cases of suspected health care fraud are currently being investigated and the government plans to audit other teaching hospitals.
- The Health Care Administration Board recently adopted a streamlined Certificate of Need ("CN") application and review process which will significantly shorten the process and in some instances, eliminate the necessity for a CN. The Board also adopted amendments to the CN regulations for cardiac diagnostic facilities which will permit

more hospitals to open cardiac catheterization laboratories and will shorten the CN process of applying for one. Among the numerous other services to be impacted by the new rules are lithotripsy services, rehabilitation services, organ transplants, psychiatric beds, alternate family care sponsor agencies and ambulatory care facilities. Legislative action is required for those services being deregulated and for which CN and licensing fee structures will be changed. It is anticipated that the Legislature will address the reform package in the near future.

- The office of Rural Economic and Community Development, through the Rural Housing and Community Development Service, is authorized to make loans to develop community facilities for public use in rural areas and towns of not more than 20,000 people. Eligible borrowers include hospitals, nursing homes, medical rehabilitation centers, and medical or dental clinics. Loan funds can be used for construction, improvements and/or acquisition of equipment. For more information on the loan program or an application, call the Office of Community and Business Programs, at (609) 265-3640.

TAX AND TIMING CONSIDERATIONS RELATED TO ACQUISITIONS

The financial and competitive pressures of the health care industry have resulted in mergers, acquisitions and affiliations of numerous facilities throughout the state. While a number of these ventures are between and among hospital facilities, there have been an increasing amount of non-traditional facility acquisitions, both in the profit and not-for-profit areas. Hospital's considering the acquisition of for-profit facilities need to be aware of tax and timing issues related to these transactions.

When applying for a tax-exemption under 501(c)(3) of the Internal Revenue Service Code, a health care facility must indicate whether or not it will be utilizing tax-exempt bonds to finance its current and/or future activities. In issuing a determination letter to the applicant, the Internal Revenue Service ("IRS") may direct the institution to request a confirmation ruling on the effect the bond financing would have on the institution's exempt status. The IRS determination letter may also instruct the institution to request a confirmation ruling prior to beginning its first tax-exempt bond financing. Hence, the health care facility should be prepared to apply for a ruling as far in advance as possible to avoid a delay in the completion of a tax-exempt bond financing.

There are numerous tax issues that could surface in an acquisition transaction. For example, in the case where a for-profit facility is acquired and all the assets are purchased by a not-for-profit corporation, the obligations of the original owner which are assigned to the new owner may prevent the debt from being advance refunded with tax-exempt bond proceeds. These obligations could include management and physician contracts, specifically the terms of the compensation plans. There are a number of factors which contribute to a determination on the refundability of debt with tax-exempt proceeds. Jim Fearon of DeCotiis, Fitzpatrick & Gluck recommends "that health care facilities arrange to have all documents reviewed by tax counsel prior to entering into a transaction of this type to avoid costly pitfalls and delays in completing a tax-exempt financing."

FINANCING NOTES

The Authority completed two competitively bid private placement bond issues in the last quarter of 1995 for The Memorial Hospital of Salem County and New Brunswick Affiliated Hospitals, Inc. The terms of the two transactions are as follows:

THE MEMORIAL HOSPITAL OF SALEM COUNTY, INC. issue was sold to United Jersey Bank in an aggregate principal amount of \$5,045,000 at a true interest cost of 4.80%. Paul Fredricks, Senior Vice President and Director of Fiscal Affairs at the hospital stated, "I was personally astonished and impressed with the competitive process and certainly pleased with the end results. I didn't anticipate that we could generate the low interest rate without a rating and the hospital will benefit from the 4.80% interest rate for the next seven years." The proceeds were used to refinance a Capital Asset Program loan and was structured for a 7-year term on a level principal basis. Security for the issue consisted of a mortgage on the hospital facilities and a gross receipts pledge on a parity with the existing debt. The bonds are redeemable after November 1, 1999 at 102%, after November 1, 2000 at 101%, and after November 1, 2001 at par.

NEW BRUNSWICK AFFILIATED HOSPITALS, INC.'s \$995,200 Equipment Revenue Note was purchased by Midlantic Bank. The proceeds were used to acquire and install an MRI and related accessories at the Laurie Imaging Center. The Note will be repaid over a 3-year term and the true interest cost was 5.25%. A first lien on the equipment will serve as security for the loan.

The rates originally offered by investors for The Memorial Hospital of Salem County, Inc. and New Brunswick Affiliated Hospitals, Inc. were 6.9% and 6.5% respectively.

NEW FINANCING TECHNIQUES

The Authority has just closed a financing utilizing a surety policy in lieu of a funded debt service reserve fund ("DSRF"). The \$25,735,000 bonds, issued on behalf of Berkeley Heights Convalescent Center/Delaire Nursing and Convalescent Center ("Nursing Homes"), were insured by AMBAC Indemnity Corporation. The surety bond, also provided by AMBAC, provides an unconditional and irrevocable guarantee of the regularly scheduled payment of principal and interest on the bonds and thus provides a high level of comfort to the investors. By obtaining a surety policy, the Nursing Homes were able to reduce the size of their bond issue and to save variable costs and interest payments associated with a traditionally-funded DSRF. Under certain circumstances, surety bonds can be substituted for funded DSRFs. If you're interested in exploring such a substitution for an outstanding bond issue, call June Duggan, Deputy Director, at the Authority's offices. She can be reached at (609) 292-8585.

PROJECT NOTES

- Bayonne Hospital completed construction of a five-deck, 400-space parking garage and held an official opening on November 20.
- Englewood Hospital's multi-level parking garage opened recently with a formal ribbon-cutting ceremony. Doug Duchak, the Chief Financial Officer, reports that the garage has been a great success since opening on December 18 and he was very pleased that the project was completed on time and on budget. The garage's additional 600 spaces increased the hospital's total parking capacity to 1,400 for the hospital's patients and visitors.
- Congratulations to Newark Beth Israel Medical Center on the completion of the Lester Z. Lieberman Center for Ambulatory Care, a 96,680 square foot, six-level building which is connected to the main facility by an overhead bridge and walkway. A preopening reception was held on Sunday, January 21 and guests toured the new center as well as the recently-opened Lester M. Bornstein Center for Emergency Services, the new laboratory building and an outpatient center. The new facilities are part of an \$88.6 million project which will be completed in December, 1996.
- United Healthcare System unveiled its sixth family health center with a ribbon cutting ceremony held on January 23. The United Family Health Center, located at 50 South Clinton Street in East Orange, is a state-of-the-art comprehensive outpatient family health center serving both pediatric and adult patients with a full range of general and specialty outpatient services including speech and hearing, physical therapy and nutritional counseling. As John Dandridge, President and CEO of the System explained, the "facility is equipped to meet all of a families' outpatient healthcare needs under one roof." Designed with the family in mind, the new Center is enhanced by the latest patient registration and scheduling system, a large and secured parking lot, and a modern security system.
- JFK Health Systems recently completed a major expansion project at the Robert Wood Johnson, Jr. Rehabilitation Institute. The project involved approximately 35,000 square feet of new construction at the facility and approximately 38,000 square feet of space is currently undergoing renovation. The expansion represents the completion of Phase 1 of a \$46.5 million construction/renovation project which is scheduled for completion in May 1998.

A FRIENDLY REMINDER When sending correspondence to the Authority through the U.S. Post Office, it is essential to include "CN 366" in the address. The mail that includes the CN number is delivered in a timely manner and permits a prompt response by the Authority staff.

Len Fishman, Chairman • Commissioner of Health
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(Leon Moskowitz, Designee)
William Waldman • Commissioner of Human Services
(Edward Tetelman, Designee)
Noreen P. White • Theodore A. Schwartz
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