

**CALIFORNIA HEALTH FACILITIES FINANCING AUTHORITY (CHFFA)
BOND FINANCING PROGRAM
EXECUTIVE SUMMARY**

| <p>Applicant: Scripps Health (“Scripps”) 4275 Campus Point Center San Diego, California 92121 San Diego County</p> | <p>Amount Requested: \$250,000,000 Date Requested: December 3, 2009 Requested Loan Term: 31 years Resolution Number: 348</p> | | | | | | | | | | | | | | | | |
|--|--|------------------------------------|--------------------------|---------------------------------|-----|---------------|---------------|------------------|---------------|----------|----------------------------|--------------------------|-------------------|-------------------|--------------------------|----------------|--------------------------|
| <p>Obligated Group: Sole Member is Scripps Health, see page 8 for the Obligated Group Facilities</p> | | | | | | | | | | | | | | | | | |
| <p>Project Sites: Various (page 2)</p> | | | | | | | | | | | | | | | | | |
| <p>Facility Types: Acute care, skilled nursing and outpatient facilities</p> | | | | | | | | | | | | | | | | | |
| <p>Background: Scripps, headquartered in San Diego, California is a nonprofit benefit corporation which provides quality, safe and cost-effective health care services. Scripps provides healthcare services through a network of programs at four acute-care hospitals, 22 outpatient clinics, an extensive ambulatory care network, home health care and associated support services.</p> | | | | | | | | | | | | | | | | | |
| <p>Use of Proceeds: Bond proceeds will be used to fund various capital improvement projects at four hospitals on five campuses and an administrative building owned and operated by Scripps. Additionally, bond proceeds will be used to reimburse Scripps for prior capital expenditures at these locations.</p> | | | | | | | | | | | | | | | | | |
| <p>Type of Issue: Negotiated public offering with fixed, intermediate-term put, and/or variable rate bonds</p> <p>Credit Enhancement: Dependent on market conditions, may use a LOC for variable rate bonds from JP Morgan Chase Bank and/or Barclays Capital</p> <p>Expected Credit Rating: A1/A+/A+ Moody’s/S&P/Fitch</p> <p>Senior Underwriter: JP Morgan Securities Inc. Barclays Capital</p> <p>Bond Counsel: Orrick, Herrington, Sutcliffe LLP</p> <p>Financing Team: See Exhibit 1 (page 11)</p> | | | | | | | | | | | | | | | | | |
| <p>Financial Overview: Scripps’ income statement appears to demonstrate increased revenues over the last three fiscal years. Additionally, Scripps appears to exhibit a strong balance sheet with adequate liquidity.</p> | | | | | | | | | | | | | | | | | |
| <p>Net Patient Revenue (FYE September 30, 2008):</p> <table style="width: 100%; margin-left: 40px;"> <thead> <tr> <th></th> <th style="text-align: right;"><u>Percent</u></th> </tr> </thead> <tbody> <tr> <td>Contracted payors</td> <td style="text-align: right;">30%</td> </tr> <tr> <td>Medicare</td> <td style="text-align: right;">23%</td> </tr> <tr> <td>Self pay</td> <td style="text-align: right;">23%</td> </tr> <tr> <td>Medi-Cal</td> <td style="text-align: right;">12%</td> </tr> <tr> <td>Other third party payors</td> <td style="text-align: right;"><u>12%</u></td> </tr> <tr> <td>Total</td> <td style="text-align: right;"><u>100%</u></td> </tr> </tbody> </table> | | | <u>Percent</u> | Contracted payors | 30% | Medicare | 23% | Self pay | 23% | Medi-Cal | 12% | Other third party payors | <u>12%</u> | Total | <u>100%</u> | | |
| | <u>Percent</u> | | | | | | | | | | | | | | | | |
| Contracted payors | 30% | | | | | | | | | | | | | | | | |
| Medicare | 23% | | | | | | | | | | | | | | | | |
| Self pay | 23% | | | | | | | | | | | | | | | | |
| Medi-Cal | 12% | | | | | | | | | | | | | | | | |
| Other third party payors | <u>12%</u> | | | | | | | | | | | | | | | | |
| Total | <u>100%</u> | | | | | | | | | | | | | | | | |
| <table style="width: 100%; border-collapse: collapse;"> <thead> <tr> <th colspan="2" style="text-align: left;"><u>Estimated Sources of Funds:</u></th> <th colspan="2" style="text-align: right;"><u>Estimated Uses of Funds:</u></th> </tr> </thead> <tbody> <tr> <td style="width: 30%;">Bond Proceeds</td> <td style="width: 20%; text-align: right;">\$250,000,000</td> <td style="width: 30%;">Capital Projects</td> <td style="width: 20%; text-align: right;">\$247,000,000</td> </tr> <tr> <td></td> <td style="text-align: right;"><hr style="width: 100%;"/></td> <td style="text-align: right;">Financing Costs</td> <td style="text-align: right;"><u>3,000,000*</u></td> </tr> <tr> <td> Total Sources</td> <td style="text-align: right;"> <u>\$250,000,000</u></td> <td style="text-align: right;"> Total Uses</td> <td style="text-align: right;"> <u>\$250,000,000</u></td> </tr> </tbody> </table> | | <u>Estimated Sources of Funds:</u> | | <u>Estimated Uses of Funds:</u> | | Bond Proceeds | \$250,000,000 | Capital Projects | \$247,000,000 | | <hr style="width: 100%;"/> | Financing Costs | <u>3,000,000*</u> | Total Sources | <u>\$250,000,000</u> | Total Uses | <u>\$250,000,000</u> |
| <u>Estimated Sources of Funds:</u> | | <u>Estimated Uses of Funds:</u> | | | | | | | | | | | | | | | |
| Bond Proceeds | \$250,000,000 | Capital Projects | \$247,000,000 | | | | | | | | | | | | | | |
| | <hr style="width: 100%;"/> | Financing Costs | <u>3,000,000*</u> | | | | | | | | | | | | | | |
| Total Sources | <u>\$250,000,000</u> | Total Uses | <u>\$250,000,000</u> | | | | | | | | | | | | | | |
| <p><i>*Scripps elects to fund the cost of issuance from equity, in which cash additional proceeds would be allocated to Project.</i></p> | | | | | | | | | | | | | | | | | |
| <p>Legal Review: Staff has reviewed the applicant’s responses to the questions contained in the Legal Status portion of the application. The information that was disclosed does not appear to question the financial viability or legal integrity of this applicant.</p> | | | | | | | | | | | | | | | | | |
| <p>Staff Recommendation: Staff recommends the Authority approve a Resolution in an amount not to exceed \$250,000,000 for Scripps Health subject to a bond rating of at least an “A” category rating by a nationally recognized rating agency.</p> | | | | | | | | | | | | | | | | | |

STAFF SUMMARY AND RECOMMENDATION

Scripps Health (“Scripps”)

December 3, 2009
Resolution Number: 348

I. POLICY ISSUES:

The Authority adopted bond issuance guidelines in September 2000 which included a minimum debt service coverage of 1.25x. The Authority acknowledged each financing must be reviewed individually and exceptions to these guidelines may be considered if the applicant demonstrates that such exception is a necessary part of a cost-effective and prudent borrowing strategy. Scripps’ Master Indenture imposes a minimum 1.10x debt service coverage ratio. Additionally, in light of recent market tumult, Scripps desires a minimum debt service coverage ratio of 1.10x to afford Scripps maximum flexibility in a potentially unpredictable marketplace. In consideration of the historical and current financial strength of Scripps (its current proforma debt service coverage is a healthy 5.13x) and the extraordinary market conditions over the last year, staff recommends waiving the minimum debt service coverage requirement of 1.25x and thus, allowing Scripps to adhere to a minimum debt service coverage ratio of 1.10x.

II. PURPOSE OF FINANCING: Scripps seeks to invest up to \$250 million in bond proceeds towards capital improvements at five campus locations throughout San Diego County to provide additional capacity and more efficient service for patients. Bond proceeds will be used to finance the construction, renovation, acquisition and equipping of certain facilities owned and operated by Scripps.

Capital Projects \$247,000,000

Scripps Green Hospital, San Diego

Scripps seeks to construct an approximate 797-space parking structure, renovate and improve buildings, construct a new pharmacy, and expand radiation oncology, operating rooms and supporting facilities, which includes seismic upgrades, as well as the purchase and installation of equipment.

Scripps Memorial Hospital, Encinitas

Scripps seeks to construct an approximate 884-space parking structure, improve buildings, including increase bed capacity, expand the birthing pavilion, provide seismic upgrades as well as purchase and install equipment.

Scripps Memorial Hospital, La Jolla

Scripps seeks to renovate and improve buildings, including a new Cardiovascular Institute, provide seismic upgrades, as well as purchase and install equipment.

Scripps Mercy Hospital, Chula Vista

Scripps seeks to improve buildings, including seismic upgrades, as well as purchase and install equipment.

Scripps Mercy Hospital, San Diego

Scripps seeks to construct an approximate 640-space parking structure and central energy plant, renovate the emergency department and other building improvements, including seismic upgrades, as well as purchase and install equipment.

Campus Point, San Diego

Scripps seeks to acquire and renovate existing and new administrative support buildings.

Scripps expects to finance nearly \$94 million seismic upgrades with bond proceeds over the next five years. Additionally, Scripps will use approximately \$37 million of bond proceeds to reimburse itself for expenditures previously made and future planned seismic upgrades.

| | |
|----------------------------------|-----------------------------|
| <i>Financing Costs</i> | <u>3,000,000</u> |
| Total Uses of Funds | <u>\$250,000,000</u> |

III. FINANCIAL STATEMENTS AND ANALYSIS:

SCRIPPS HEALTH AND AFFILIATES
CONSOLIDATED STATEMENTS OF OPERATIONS
(\$000's)

| | For the Year Ended September 30, | | |
|---|----------------------------------|------------------|------------------|
| | 2008 | 2007 | 2006 |
| Operating revenues: | | | |
| Patient services revenue | \$ 1,667,142 | \$ 1,526,203 | \$ 1,410,946 |
| Capitation premium revenue | 202,116 | 174,224 | 154,704 |
| Other operating revenue | 67,172 | 61,879 | 58,985 |
| Equity released from restrictions used for operations | 17,327 | 18,765 | 19,612 |
| Total operating revenues | <u>1,953,757</u> | <u>1,781,071</u> | <u>1,644,247</u> |
| Operating expenses: | | | |
| Wages and benefits | 868,852 | 782,516 | 702,763 |
| Supplies | 323,662 | 313,894 | 293,474 |
| Services | 489,661 | 442,021 | 411,253 |
| Provision for uncollectible accounts receivable | 73,859 | 61,839 | 66,883 |
| Depreciation and amortization | 74,277 | 65,906 | 56,072 |
| Interest | 14,288 | 14,804 | 15,271 |
| Total operating expenses | <u>1,844,599</u> | <u>1,680,980</u> | <u>1,545,716</u> |
| Operating income | 109,158 | 100,091 | 98,531 |
| Nonoperating gains (losses): | | | |
| Investment income | 25,163 | 63,946 | 27,731 |
| Holding loss on trading portfolio | (118,054) | 47,271 | - |
| Contributions | 1,604 | 11,546 | 2,789 |
| Gain on sale of property | (196) | 794 | 824 |
| Market adjustment on interest rate swaps | (8,028) | 505 | 84 |
| Loss on early extinguishment on debt | (8,903) | (297) | - |
| Other-than-temporary decline in investment | - | - | (165) |
| Excess of revenues over expenses | <u>744</u> | <u>223,856</u> | <u>129,794</u> |

(continued)

SCRIPPS HEALTH AND AFFILIATES
CONSOLIDATED STATEMENTS OF OPERATIONS
(\$000's)
(continued)

| | For the Year Ended September 30, | | |
|--|----------------------------------|---------------------|-------------------|
| | 2008 | 2007 | 2006 |
| Unrestricted net assets: | | | |
| Excess of revenues over expenses | \$ 744 | \$ 223,856 | \$ 129,794 |
| Net unrealized gains on other-than-trading investment | - | 4,132 | 12,438 |
| Reclassification of investment portfolio to trading | - | (47,271) | - |
| Change in fair value of interest rate swaps | - | 188 | 3,902 |
| Net assets released from restrictions used for purchases of property and equipment | 7,689 | 9,162 | 12,213 |
| Other | (621) | (782) | 152 |
| Increase in unrestricted net assets | <u>7,812</u> | <u>189,285</u> | <u>158,499</u> |
| Temporarily restricted net assets: | | | |
| Contributions | 45,373 | 54,968 | 39,990 |
| Investment income | 2,392 | 9,879 | 4,352 |
| Unrealized gains (losses) on investments | (10,515) | 1,875 | 1,043 |
| Net assets released from restrictions used for operations | (17,327) | (18,765) | (19,612) |
| Net assets released from restrictions used to purchase property and equipment | (7,689) | (9,162) | (12,213) |
| Changes in value of deferred gifts | (751) | (96) | 2,338 |
| Other | (1,132) | (675) | 214 |
| Increase in temporarily restricted assets | <u>10,351</u> | <u>38,024</u> | <u>16,112</u> |
| Permanently restricted net assets: | | | |
| Contributions | 373 | 7,840 | 2,911 |
| Change in value of deferred gifts | 51 | (85) | 92 |
| Other | (35) | (178) | 95 |
| Increase in permanently restricted net assets | <u>389</u> | <u>7,577</u> | <u>3,098</u> |
| Total increase in net assets | 18,552 | 234,886 | 177,709 |
| Net assets at the beginning of the year | <u>1,200,920</u> | <u>966,034</u> | <u>799,365</u> |
| Net assets at the end of the year | <u>\$ 1,219,472</u> | <u>\$ 1,200,920</u> | <u>\$ 966,034</u> |

SCRIPPS HEALTH AND AFFILIATES
CONSOLIDATED STATEMENTS OF FINANCIAL POSITION
(\$000's)

| | As of September 30, | | |
|---|---------------------|---------------------|---------------------|
| | 2008 | 2007 | 2006 |
| ASSETS | | | |
| Current Assets: | | | |
| Cash and cash equivalents | \$ 249,144 | \$ 124,267 | \$ 185,691 |
| Accounts receivable, net | 237,730 | 249,962 | 214,923 |
| Assets limited as to use | 10,323 | 10,102 | 9,522 |
| Other current assets | 31,130 | 27,067 | 43,502 |
| Total Current Assets | <u>528,327</u> | <u>411,398</u> | <u>453,638</u> |
| Assets limited as to use | 202,604 | 254,703 | 252,245 |
| Investments | 504,154 | 613,723 | 426,174 |
| Property, plant and equipment, Net | 685,513 | 601,444 | 545,535 |
| Other assets | 96,899 | 107,180 | 69,953 |
| Total Assets | <u>\$ 2,017,497</u> | <u>\$ 1,988,448</u> | <u>\$ 1,747,545</u> |
| LIABILITIES AND NET ASSETS | | | |
| Current Liabilities: | | | |
| Current portion of long-term debt | \$ 59,040 | \$ 13,038 | \$ 12,428 |
| Accounts payable | 96,986 | 98,423 | 98,965 |
| Accrued liabilities | 178,121 | 162,574 | 146,416 |
| Total Current Liabilities | <u>334,147</u> | <u>274,035</u> | <u>257,809</u> |
| Long-term debt | 380,679 | 432,372 | 444,905 |
| Other liabilities | 83,199 | 81,121 | 78,797 |
| Total Liabilities | <u>798,025</u> | <u>787,528</u> | <u>781,511</u> |
| Net Assets: | | | |
| Unrestricted | 996,085 | 988,273 | 798,988 |
| Temporarily restricted | 154,992 | 144,641 | 106,617 |
| Permanently restricted | 68,395 | 68,006 | 60,429 |
| Total Net Assets | <u>1,219,472</u> | <u>1,200,920</u> | <u>966,034</u> |
| Total Liabilities and Net Assets | <u>\$ 2,017,497</u> | <u>\$ 1,988,448</u> | <u>\$ 1,747,545</u> |

Financial Ratios:

Proforma (a)
FYE September, 2008

| | | | | |
|----------------------------------|-------------|-------------|-------------|-------------|
| Debt Service Coverage (x) | 5.13 | 8.22 | 9.41 | 8.96 |
| Debt/Unrestricted Net Assets (x) | 0.69 | 0.44 | 0.45 | 0.57 |
| Margin (%) | 5.59 | 5.62 | 5.62 | 5.99 |
| Current Ratio (x) | 1.58 | 1.47 | 1.47 | 1.76 |

(a) Recalculates FY 2008 audited results to include the impact of this proposed financing.

Financial Discussion:

Scripps' income statement appears to demonstrate increased revenues over the last three fiscal years.

Scripps' income statement appears to exhibit solid profitability over our review period with operating income remaining steady from \$99 million in fiscal year 2006 to \$109 million in fiscal year 2008. In addition, Scripps appears to have shown solid operating margins of 5.99%, 5.62% and 5.59% for fiscal years 2006, 2007 and 2008, respectively. Scripps revenues consist primarily of net patient service revenue accounting for approximately 85% of total revenues in fiscal year 2008. Total operating revenue increased from \$1.6 billion in fiscal year 2006 to \$1.9 billion in fiscal year 2008, an increase of nearly 20%. Scripps attributes the increase to patient volume increases and in hospital discharges, outpatient surgeries and clinic visits as well as in increase in payor reimbursements. Additionally, Scripps experienced an increase in higher capitation rates as well as new patient membership.

Operating expenses increased an average of 10% from fiscal year 2006 to 2008 due to a combination of wage increases, inflation on supplies and services, increased costs of technology, bad debt and depreciation expenses. In fiscal year 2008, Scripps experienced an increase in provisions for uncollectible debt of 19% primarily due to an increase in uninsured patients.

Scripps' also appears to exhibit a strong balance sheet with adequate liquidity.

Scripps' current balance sheet appears to be solid as cash and cash equivalents increased from \$186 million in fiscal year 2006 to \$249 million in fiscal year 2008 due to continued operations and investment income in excess of capital expenditures. Net property, plant and equipment increased by 26%, from \$546 million in fiscal year 2006 to \$686 million in fiscal year 2008, reflecting a substantial investment in various construction and information technology projects. In fiscal year 2008, approximately \$52 million of CHFFA/Scripps variable rate demand bonds (Series 2008 B-G), were classified as current liabilities on Scripps financial statements in accordance with accounting guidance governing short-term liquidity facilities backing variable rate demand bonds. Scripps' current debt service coverage ratio is 8.22x and with the proposed financing, the proforma debt service coverage ratio is a solid 5.13x, indicating that Scripps appears to be able to manage the additional debt.

Fiscal Year 2009

Audit review of results for Scripps at September 30, 2009 is underway. It is expected that the Scripps Health Board will review its audited financial statements on December 10, 2009. Representatives from Scripps attending the CHFFA meeting on December 3, 2009 will be able to respond to questions on the FY2009 results. The 2009 audit and management's discussion will be included in the official statements that will be provided to prospective investors.

IV. BACKGROUND:

Scripps Health, a California nonprofit public benefit corporation, is the core organization of a community-based health care delivery network located in San Diego County, California, that includes four acute-care hospitals on five campuses, 22 outpatient clinic locations, an extensive ambulatory care network, home health care, associated support services and more than 2,750 affiliated physicians. Scripps Health dates back to 1924 when Ellen Browning Scripps founded both Scripps Memorial Hospital (now known as Scripps Memorial Hospital La Jolla) and Scripps Metabolic Clinic in La Jolla, California. Scripps Health has since grown from a single acute care hospital in La Jolla, California to its present county-wide health care delivery system. Today Scripps includes 2 of the 6 designated trauma centers in San Diego County, one of the 10 largest hospitals in California, and one of the oldest and most prestigious multi-specialty clinics in Southern California.

Obligated Group

Scripps Health is currently the sole Member of the "Obligated Group" created pursuant to an Amended and Restated Master Indenture, dated as of May 1, 1998, between Scripps Health and Bank of New York, as Master Trustee. The Obligated Group is the central financing vehicle and credit for Scripps Health and its operating divisions. The Obligated Group facilities are listed below.

Obligated Group Facilities

Scripps Clinics, *Various*
Scripps Green Hospital, *La Jolla*
Scripps Memorial Hospital, *La Jolla*
Scripps Memorial Hospital, *Encinitas*
Scripps Mercy Hospital, *Chula Vista and San Diego*
Medical Office Buildings, *Various*
Scripps Home Healthcare Services, *Various*
Scripps Health Foundation

Licensure, Certification and Accreditation

Each of the hospital facilities is appropriately licensed for the level of care it delivers and is certified to participate in the Medicare and Medi-Cal programs. Each is accredited by The Joint Commission.

Governance

Scripps Health is governed by the Board, which consists of 14 members. Each member serves a term of three years, may be elected to serve a second consecutive term of three years and, following at least one year of not serving on the board, may serve up to two additional consecutive terms of three years each.

V. UTILIZATION STATISTICS:

The following table shows utilization statistics of Scripps Health acute care hospitals operated for the fiscal years ended September 30, 2009, 2008, 2007 and 2006:

| | Fiscal Year Ended September 30, | | | |
|---------------------------------|---------------------------------|-----------|-----------|---------|
| | 2009 | 2008 | 2007 | 2006 |
| Inpatient Activity | | | | |
| Licensed Beds | 1,322 | 1,318 | 1,318 | 1,431 |
| Available Beds | 1,265 | 1,261 | 1,244 | 1,359 |
| Discharges | 70,231 | 68,810 | 67,203 | 66,491 |
| Patient Days | 307,591 | 314,043 | 305,600 | 311,964 |
| Average Daily Census | 843 | 858 | 837 | 855 |
| Average Length of Stay | 4.55 | 4.56 | 4.55 | 4.69 |
| Occupancy Rate (Licensed Beds) | 61% | 63% | 61% | 60% |
| Occupancy Rate (Available Beds) | 65% | 66% | 66% | 63% |
| Inpatient Surgery Cases | 22,362 | 21,772 | 20,889 | 20,261 |
| Outpatient Activity | | | | |
| Hospital Outpatient Total | 466,348 | 460,318 | 447,411 | 436,829 |
| Outpatient Surgery Cases | 28,211 | 27,383 | 27,169 | 26,833 |
| Emergency Room Visits | 124,912 | 125,342 | 123,472 | 118,328 |
| Clinic Office Ancillary Visits | 1,068,794 | 1,044,131 | 1,016,805 | 953,952 |

VI. OUTSTANDING DEBT:

As of December 1, 2009, Scripps has approximately \$399.5 million in outstanding debt of which \$349.5 million is Authority debt. With this bond financing, Scripps' outstanding debt will increase by \$250 million for a total of approximately \$650 million in outstanding long-term debt.

VII. DUE DILIGENCE:

Due diligence has been completed with regard to the following items:

- **Section 15438.5(a) of the Act (Savings Pass Through):** Scripps properly completed and submitted the "Pass-Through Savings Certification," in addition to a narrative explaining how it intends to pass through savings.
- **Section 15491.1 of the Act (Community Service Requirement):** Scripps properly completed and submitted this certification and indicated that Medi-Cal and Medicare patients are accepted.
- **Compliance with Seismic Regulations:** Scripps properly completed and submitted a description of its seismic requirements.
- **Compliance with Section 15455(b) of the Act (California Environmental Quality Act):** Scripps properly submitted documentation to the Authority demonstrating the proposed project has either complied with Division 13 (commencing with Section 21000) of the Public Resources Code, or is otherwise not a project under that division.
- **Religious Due Diligence.**
- **Legal Review.**

EXHIBIT 1

Scripps Health Financing Team

System Counsel: Foley & Lardner LLP
Financial Advisor to System: Kaufman Hall
Underwriter Counsel: Sidley Austin, LLP
Auditor: Ernst & Young LLP
Bond Trustee: U.S. Bank National Association
Bond Trustee Counsel: Dorsey & Whitney
Master Trustee: The Bank of New York Mellon
Trust Company, N.A.