South Dakota Association of Healthcare Organizations

EideBailly CPAs & BUSINESS ADVISORS

ANALYSIS OF THE FINANCIAL IMPACT OF COVID-19 ON SOUTH DAKOTA HOSPITALS – PHASE 2

June 10, 2020

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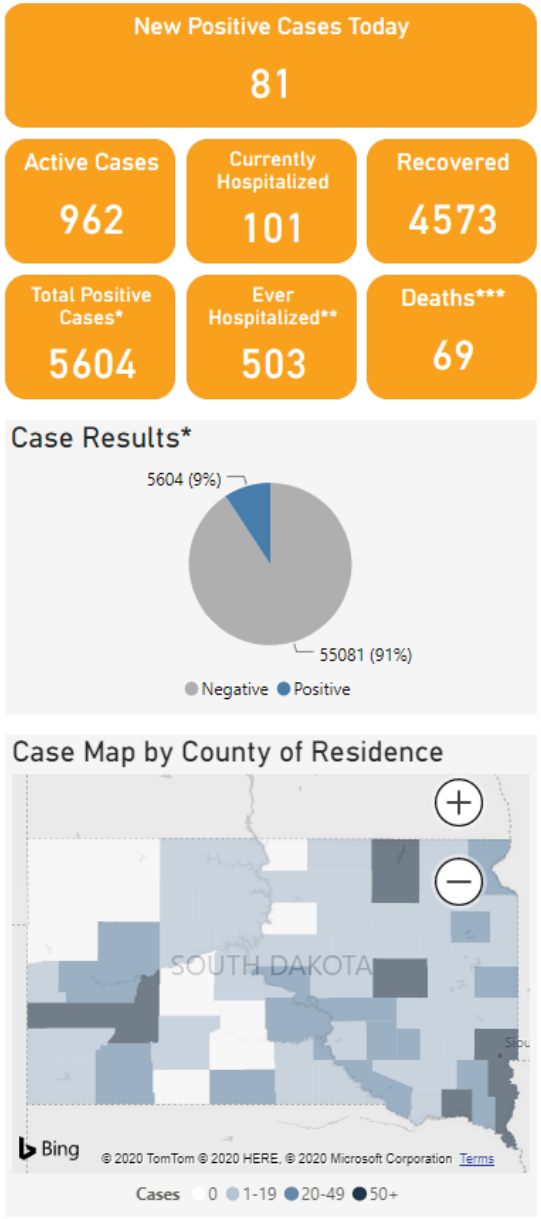
SOUTH DAKOTA COVID-19 IMPACTS[1]



SDAHO engaged Eide Bailly to undergo a multi-phase impact study in order to analyze the devastating financial effects of the novel coronavirus (COVID-19) pandemic on South Dakota healthcare organizations. SDAHO prepared and sent a detailed survey request for financial information to providers across the state. From the data provided, and from summarizing and extrapolating survey results, we have developed initial statewide estimates of financial impacts experienced by South Dakota hospitals.

South Dakota hospitals began experiencing significant operational and financial impacts in mid-March, which coincides with federal, state, and local guidelines recommending limitations of services broadly considered non-emergent in response to the outbreak of COVID-19 nationally.

Our phase 2 estimates presented in this report are based on survey data related to the impacts from the March and April 2020 financial reporting periods. South Dakota providers swiftly put recommended healthcare service limitations in place, but maximum South Dakota hospital case surge remains unknown as state departments of health continue modeling and forecasting cases and hospitalizations while economies slowly reopen and social distancing is relaxed. As expected, April 2020 lost revenue impacts were particularly severe as the entire month saw extensive limitation on non-emergent and elective medical procedures from substantially all providers, while certain geographies began seeing increases in infection and hospitalization rates. Initial reports from providers on May and June activities also note that economic losses will be substantial as providers' volumes remain significantly below capacity. Nursing home providers are now seeing more substantial decreases in resident census as well.

The unknown duration of the ongoing impact of COVID-19 until hospitals and healthcare providers return to normal or historical operations is creating a particularly harsh forecast of financial strain on the state's providers. Significant uncertainty remains regarding the length of time of continuing pandemic effects, maximum impacts of surges in COVID-19 hospitalizations, and the ongoing fluctuation of patient care provided as economies relax restrictions. These factors create both short-term and long-term hospital financial concerns. These economic impacts encountered by South Dakota hospitals not only impact South Dakota's healthcare providers, but the state's economy in total.

[1] South Dakota Department of Health, https://doh.sd.gov/news/Coronavirus.aspx, Updated 6/10/2020, 10:58:14 AM

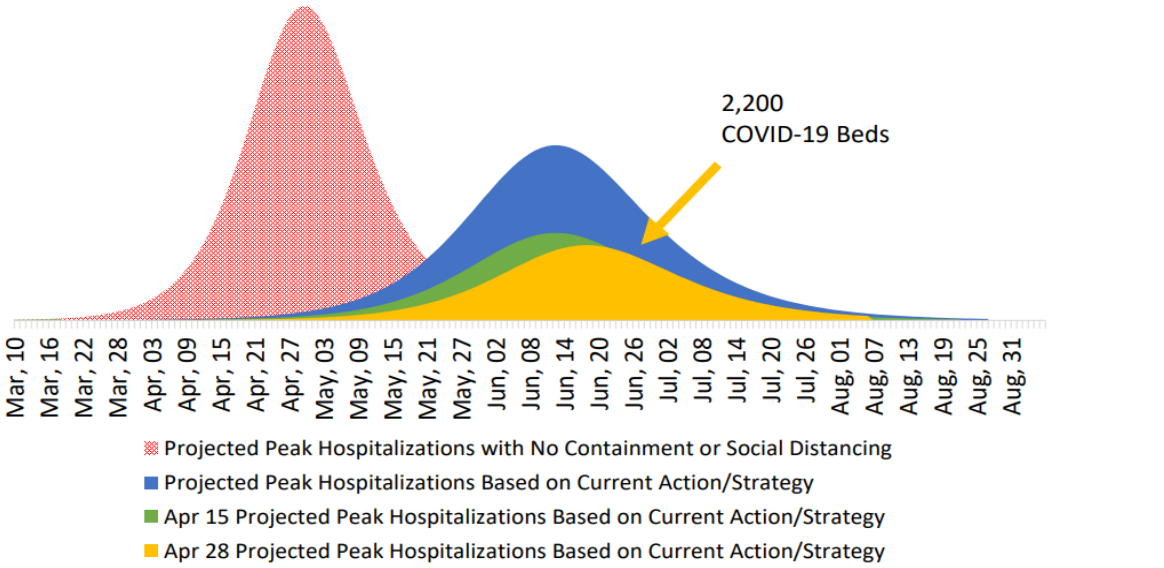
PROJECT OVERVIEW, CONTINUED

Based on our initial analysis, considering the timeline for the current projection of hospitalization surge and pace of expected economic recovery of revenues from non-emergent healthcare services upon the relaxation of suggested limitations of services or COVID-19 inpatient bed reserves, we currently anticipate statewide hospital economic damages from lost revenues, incremental increases in COVID-19 operational and capital costs, and care costs for uninsured or underinsured COVID-19 patients to range from **$5.47 million to $5.83 million on a daily basis** (an approximately 40% negative impact from pre-COVID operations) before any offsetting impacts of federal or state stimulus funds.

Projecting damages for an initial impact period from approximately March 20, 2020 through June 30, 2020, **damages for South Dakota hospitals could exceed $550 million through the quarter ended June 30, 2020.**

SOUTH DAKOTA PEAK HOSPITALIZATION PROJECTIONS [1]

Release Date: April 28, 2020



With South Dakota hospitals and health systems reporting operating margins in total of roughly 2-3% based on available 2018 cost report data or most recent audited financial statements, the COVID losses will place significant strain on operations and in some cases viability of South Dakota providers.

Hospitals and health systems face a more difficult time projecting the second half financial impacts for their calendar year 2020 operations, as the projected need for urgent acute care services, impacts of acute or widespread outbreaks of COVID-19, and consumer choice and social distancing strategy will all play a significant role in the financial results for the last half of the year.

From the CARES Act, South Dakota medical providers' **(including hospitals, clinics, nursing homes, and other medical provider types)** have or will be receiving allocations from the HHS provider relief funds totaling approximately $299 million from general, rural, skilled nursing facility, and rural health clinic allocations to date. This will result in much needed funds to offset economic damages, but our analysis indicates that future allocations from the Provider Relief Fund or other sources will certainly be needed to further mitigate financial impacts. More distributions from the Provider Relief Fund are forthcoming, but it is not yet determined how South Dakota hospitals will be allocated a share of these funds.

[1] https://covid.sd.gov/docs/COVID19_Testing_Slides.pdf, accessed May 4, 2020, 7:58pm

SECTION 2

FINANCIAL DATA HIGHLIGHTS

FINANCIAL DATA HIGHLIGHTS

Patient Volumes

One of the primary drivers of economic damages for hospitals is the impact of decreases in patient revenues driven by limitations of services for both non-emergent or elective medical care. Social distancing limitations and patient behavior have further reduced volume for clinic encounters, emergency room visits, and outpatient surgeries and medical procedures. Inpatient volumes have also been impacted to a lesser degree as hospitals have tried to maintain adequate bed capacity for COVID hospital surge. Urban and larger rural hospital inpatient volumes have been affected as bed capacity has been reserved for planned patient volume surge based on epidemiologic patient flow studies. Recently, skilled nursing census levels have also experienced decreases. Certain South Dakota regions have seen decreases in skilled nursing census approaching 13% in May 2020.

Service Area	Projected Volume Decline
Outpatient	37%
Clinic	48%
Emergency	42%
Surgeries	59%
Inpatient	34%
Skilled Nursing	10%

Lost Revenues

The majority of the economic damages from COVID-19 for hospitals is the lost revenues due to decreases in patient volume. From a review of the latest available Medicare cost report filings for South Dakota hospitals, total net patient revenues were approximately $4.4 billion. Based on initial data obtained from the COVID-19 surveys, South Dakota hospitals are projecting total lost revenue impacts from 32% to 47%, or an average of approximately 40% across providers. Rural providers are seeing significant volatility in lost revenues, but survey respondents have consistently experienced projected lost revenues exceeding 20%. The extent of economic damages related to lost revenues will be most impacted by the duration of the downturn in demand for non-emergent or elective medical care.

Non-emergent "elective" procedures - So-called elective procedures are not considered optional surgeries, but non-emergent. These procedures can alleviate pain, improve quality of life and be otherwise life changing for patients. For some, delaying care could create additional complications later. It remains to be seen what the long-term effects are of delaying care as a result of COVID-19, both in terms of costs for individuals and hospitals, and in terms of health outcomes.

Incremental Expenses

Incremental expenditures have occurred with hospitals including both capital spending for equipment, costs to develop/construct COVID-19 units or screening sites, surge capacity units (including establishing temporary facilities or retrofitting existing medical space), rentals of non-traditional or excess space, expansion of telemedicine, and costs to implement and improve of preventative measures. COVID-19 expenses also include incremental staffing costs due to extraordinary infection control efforts, training costs, incentive or hazard pay scenarios, and other direct increases in costs to care of COVID-19 patients. Supply costs directly attributable to COVID-19 are also significant and include various costs of personal protective equipment, ventilator equipment, and lab and testing materials. Additional incremental expenses will be encountered due to projected increases in uncompensated care related to COVID-19.

Costs Associated with Purchasing Protective Equipment - As noted in a release from the Society for Healthcare Organization Procurement Professionals (SHOPP), estimated costs of certain medical supplies have increased tenfold since the beginning of the pandemic[1].

Costs of Treating Uninsured COVID-19 Patients – According to an April 2020 study by the Kaiser Family Foundation[2], treating the uninsured for symptoms of COVID-19 may cost up to $41.8 billion depending on factors like how prolonged the outbreak is and how many people need the highest levels of care.

[1] http://cdn.cnn.com/cnn/2020/images/04/16/shopp.covid.ppd.costs.analysis_.pdf

[2] https://www.kff.org/uninsured/issue-brief/estimated-cost-of-treating-the-uninsured-hospitalized-with-covid-19/

FINANCIAL DATA HIGHLIGHTS: STIMULUS PROGRAMS

Reference	Program	South Dakota Impacts	Observations
1	CARES Act HHS Provider Relief Fund	As of May 11, 2020, South Dakota healthcare providers have received approximately $117 million from general distributions from this fund, and most recently an additional approximately $164 million in targeted rural relief. Later in May, skilled nursing facilities received approximately $12 million, and rural health clinics received approximately $2.8 million.	These funds will offset losses for South Dakota hospitals, but given financial projections, will fall significantly short of the likely damages for South Dakota hospitals, especially if economic damages persist beyond the June 30, 2020 quarter, which is highly likely even with limited reopening of the economy. In analyzing funds received by South Dakota hospitals, the state's urban facilities and larger rural facilities will likely have the largest shortfall of relief funds received compared to economic damages encountered.
2	Small Business Administration (SBA) – Paycheck Protection Program (PPP)	Smaller hospitals with less than 500 employees in South Dakota have the ability to apply for and receive a loan from the SBA, that can be forgiven if meeting appropriate spending (75% on payroll) over an 8-week period up through June 30, 2020. This will limit layoffs and furloughs for these organizations that would be of higher likelihood due to the significant downturn in patient volumes and revenues.	South Dakota health systems and their affiliates are unable to access SBA PPP funds, due to the number of employees in their organizations under the SBA affiliation rules. The SBA PPP will provide positive relief for recipients, but questions remain regarding the impacts to Medicare cost reporting and rates for critical access hospitals. If any forgiveness of the SBA PPP loan is considered an offset to cost by the Medicare program, the total financial benefit of this program will be limited.
3	Medicare Accelerated Payments	Many South Dakota providers requested accelerated payments from Medicare to receive payment in advance for services to offset significant downturns in cash flows.	Payments received under this program are helping with short-term cash flow, but will need to be repaid or will result in less cash flows as future services are provided and billed.
4	Small Rural Hospital Improvement (SHIP) Grants, Private Grants, and Other Federal and State Grants	South Dakota hospitals have also been recipient to some smaller grant funding sources to offset the costs of COVID-19 preparedness, testing, and treatment.	Current funds from these sources are of benefit, but are not significant in comparison to the economic damages that are projected. South Dakota hospitals continue to actively pursue funding from all possible sources.

FINANCIAL DATA HIGHLIGHTS: OTHER CONCERNS

COVID-19 Background & Remaining Uncertainty

The COVID-19 pandemic has greatly impacted the United States. Confirmed cases exceeded 100,000 by the end of March and over 1 million by the end of April based on reports from the Centers for Disease Control. Beyond the health impacts, the effect of COVID-19 on the American economy has been swift and catastrophic under strict social distancing guidelines. By late March or early April, every state or local government had imposed or recommended restrictions to mitigate the spread of the virus. The pace of economic damage has been stunning as local and national economies have felt the effects of the pandemic. More than 30 million Americans have filed for unemployment insurance since the end of February, with additional increases in unemployment expected as companies navigate running their businesses during this time. After several periods of economic expansion, first quarter gross domestic product contracted by almost 5%. Contraction of the national economy will have many further downstream impacts on healthcare organizations going forward that are not specifically calculated or included this analysis. A few of these economic concerns are discussed below.

Increases in Uncompensated Care

As with prior economic downturn events, such as the Great Recession of 2008 – 2009, hospitals can expect to see an increase in uncompensated care related to all patient services provided. In late 2008, AHA survey results[1] noted a 51% increase in hospitals who saw a moderate or significant increase in uncompensated care in the initial three months after the onset of the 2008 financial crisis. That same report noted that uncompensated care increased 8% comparing 3Q 2008 data to the pre-crisis 3Q 2007 data. A recent AHA study on uncompensated care determined that $41.3 billion of uncompensated care was provided to patients based on the most recent 2018 year cost report filings. If we expect a similar increase related to the COVID-19 pandemic, hospitals can expect an increase of almost $4 billion in uncompensated care. Given the other lost revenue and incremental expense increases from COVID-19, further economic damages will prove costly to continuing to provide healthcare services across the communities of South Dakota.

Other COVID-19 Impacts

Many other unknown impacts exist for hospital and healthcare organizations. Hospitals are faced with uncertainty regarding qualifying for certain government programs such as the 340B drug discount program. Patient volumes fluctuations will impact the minimum disproportionate share (DSH) percentage that is a requirement for participation in the 340B drug discount program. Uncertainties around patient volumes are creating some questions as to a provider's ability to participate in programs such as 340B if calculations like the DSH percentage have significant changes. In addition, COVID-19 has had a significant impact on the financial markets which has caused strain on investment portfolios and liquidity. Many hospitals and health systems obtain credit through public markets and there is a potential for increased interest cost burdens from downgrades to credit ratings and other indirect impacts from the COVID-19 pandemic. Negative impacts in the financial markets will also likely cause increases in pension funding requirements for hospital and health systems, both public and private, that have defined benefit pension obligations. Additional challenges have been experienced by healthcare organizations related to drug shortages and drug procurement, billing and collecting for services provided to patients in non-traditional settings due to rapid increases in telehealth utilization, needs for reallocation of workforce to deal with patient surges, and other impacts adjusting to increased virtual work environments for administrative functions. Many other indirect costs related to the pandemic are expected as time progresses. Skilled nursing facilities are now experiencing lost revenues from decreases in post-surgical care residents and overall decreases in resident census as a result of the impacts of COVID-19.

[1] https://www.aha.org/system/files/content/00-10/081119econcrisisreport.pdf

[2] https://www.aha.org/fact-sheets/2020-01-06-fact-sheet-uncompensated-hospital-care-cost

APPENDIX A

SCOPE OF WORK

SCOPE OF WORK

Scope Overview

- The scope of this analysis is defined as a multi-phase project analyzing at minimum March and April 2020 data specific to lost revenue impacts and incremental expenses and unreimbursed costs of care related to the COVID-19 pandemic.
- Survey data will be gathered from South Dakota hospital providers as month-end data is available to focus this study as much as possible on actual economic impacts, and to reduce the number of variables in projections.
- Actual and projected data will be accumulated and extrapolated if necessary across all hospital providers in the state to determine economic damage.
- The report will be presented at the aggregated level including all of the combined impacts to hospitals in the state.

Lost Revenue Impacts

- Revenues will be evaluated by understanding the baseline impacts to key volume indicators for hospitals including outpatient visits, clinic encounters, emergency room visits, surgeries (including scopes), and inpatient days.
- Summarized revenue information will be obtained and a range of lost revenue will be evaluated by comparing actual patient revenues to three distinct data points including prior year same period revenues, average trailing revenue for the providers fiscal year to date, and current period budgeted results.
- For March and April data submissions, a weighted average daily revenue impact range will be calculated and extrapolated across all providers in the state.
- Additional providers can submit survey data as it becomes available to limit the amount of extrapolation necessary so additional facilities are included in the Phase 2 study as compared to the Phase 1 study.
- Lost revenue impacts will be calculated before any offsetting stimulus impacts for grants and other COVID related programs.

COVID-19 Expense Impacts

- We obtained actual cost information through survey for capital expenditures, staffing and benefits, supplies, and other costs through April 2020. The requested survey data will only include incremental costs of COVID-19 across these categories.
- We also obtained charity care data related to caring for uninsured COVID-19 patients based on the charges forgone and calculated costs of providing the uncompensated care.
- We will use projections as calculated by the Kaiser Family Foundation to determine a possible top range of South Dakota's cost of uncompensated care as limited actual charity information will be likely through survey for March 2020 or April 2020 service periods.
- We will project a daily weighted average expense factor for the costs noted above include both the direct incremental costs of COVID-19 preparedness and patient care, as well as the calculated range of uncompensated care costs for COVID-19 patient care services.
- For April data submissions, an updated weighted average daily cost factor will be calculated, projected, and extrapolated across all providers in the state for reporting in the Phase 2 study document.

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