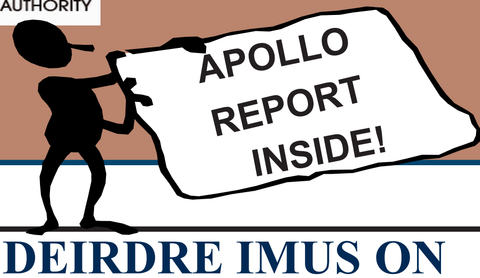
NJHCFFA
NEW JERSEY HEALTH CARE FACILITIES FINANCING AUTHORITY

# AUTHORITY NOTE$




**December '03/January '04**

## A MESSAGE FROM THE GOVERNOR

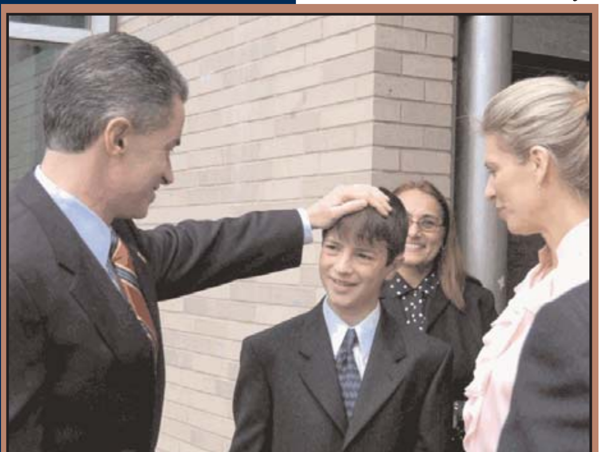
Dear Friends,

I am pleased to report that we are making great leaps in healthcare, as New Jersey moves ahead to lead our nation's battle against cancer. On October 20th, New Jersey's first multidisciplinary cancer center opened in South Jersey, as a member of the elite group of institutions designated by the National Cancer Institute as Comprehensive Care Centers. The Center's opening is a landmark in our future as a leader in cancer eradication.

By investing $5 million of state funds in this branch of The Cancer Institute in New Jersey, we continue to strengthen our state's oncology programs so that they are as good as or better than any others. New Jerseyans will no longer feel the need to go out of state for premier cancer treatment, as one third of our state's sufferers have in the past.

Our investment in cancer care also extends beyond diagnosing and treating the disease. State funding supports studies that will pilot the medical community's understanding of cancer's causes and bring about innovative treatments. For the first time in New Jersey's history, state government is directly funding scientists working to cure cancer.

It is my goal to make New Jersey the nation's medical research capital, and with our abundance of health care organizations, pharmaceutical companies and world-class scientists and researchers, we are in an excellent position to do so.



*Governor McGreevey greeted Corey Furst and Deirdre Imus at Hackensack University Medical Center, at a press conference announcing state funding for cancer research.*

## DEIRDRE IMUS ON "GREENING" NJ HOSPITALS

On October 8, Deirdre Imus enlightened Authority Members and invited guests on the merits of environmentally sound, or "green" health care facilities. Founder and Director of the Deirdre Imus Environmental Center for Pediatric Oncology, located at Hackensack University Medical Center ("HUMC"), Ms. Imus developed a "Greening the Cleaning" movement, in which toxic cleaning materials are replaced with environmentally safe agents. Ms. Imus described the benefits of going green, and described her experience with the HUMC greening the cleaning project.

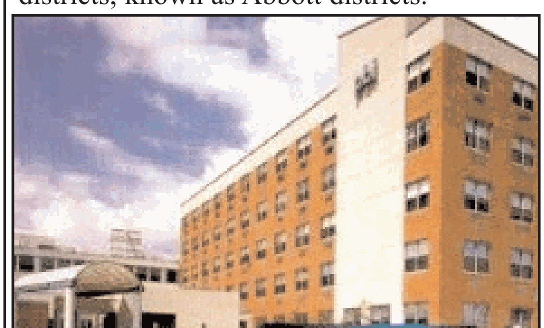
In the spring of 2001, the Deirdre Imus Environmental Center worked with HUMC to reduce the toxicity and waste of its cleaning chemicals. In a four-phase plan involving all levels of hospital personnel, HUMC replaced 18 of their 22 cleaning products/chemicals with safer green replacement products that meet or exceed the effectiveness of the toxic products.

The long-term benefits range from better health among hospital staff to financial savings, since the hospital now buys natural cleaning agents in bulk and dilutes them on-site to specifi- *(continued on page 4)*

## NJHCFFA DOES ITS SCHOOL WORK

The NJHCFFA is now taking its efforts to better communities beyond just the health care arena. The Authority has been working with struggling health care systems to sell financially draining hospital properties for the creation of local public schools. The result is a win-win situation, providing educational facilities for struggling New Jersey communities while strengthening the bottom-lines of the state's health care systems.

On July 18, 2000 the New Jersey Educational Facilities Construction and Financing Act (the "Act") was signed into law, initiating a planned State investment of $8.6 billion in public school construction over the next decade, and providing full funding of all school renovation and construction projects in 30 special needs school districts, known as Abbott districts.



*The Authority helped facilitate Passaic Beth Isreal's move from this building, freeing the property for three new schools and an athletic field .*

Under the Act, the New Jersey Economic Development Authority (EDA) was entrusted to finance, design and construct all of the school facilities projects in these troubled school areas. In July 2002, Governor James E. McGreevey's Executive Order No. 24 directed the EDA's School Construction and Financing Program to be reconstituted as a new subsidiary corporation called the New Jersey Schools Construction Corporation ("SCC"). *(continued on page 4)*

## A MESSAGE FROM THE EXECUTIVE DIRECTOR

*Executive Director Michael T. Kornett*

The end of the calendar is a busy time for the Authority, as health care organizations work to wrap up financings and projects before the coming year. 2003 was no exception, as the Authority closed five separate issues all within December. This year-end rush, though, was compounded with an onslaught of self-insurance and captive program approval requests.

Fortunately, staff was expecting the rush, knowing that many of the Authority's borrowers would be ending malpractice insurance contracts at the close of the year. Staff and Authority Members had been working for several months to create the self-insurance and captive monitoring program currently in place.

With the approval process set, and the document language drafted, the Authority distributed letters to all of its borrowers reminding the chief financial officers of the requirement in the bond documents that all self-insurance programs and/or captives be approved by the Authority. The letter also explained the process for such approval.

At the Authority's November 20, 2003 meeting, staff's outreach efforts were satisfied with requests by six borrowers for approval of self-insurance/captive programs. The presentations were complete and informative and all programs were approved that day.

In December, the Authority hosted its second Advisory Panel roundtable, during which hospital financial executives offered feedback on ways to improve Authority products and services and provided senior staff with an inside look at healthcare's most troubling fiscal hurdles. We welcome the Panel's comments, good and bad, as we advance our mission to make low-cost capital available to New Jersey's health care organizations, improving the health and welfare of all the citizens of the state.

## NEW AUTHORITY PRODUCT: POOLED BONDS PROGRAM

The Authority has officially announced the Pooled Bonds Program, a new product designed specifically to meet borrowers' requests. At the first meeting of the Authority's CFO Advisory Panel, it was clear that borrowers had a need that wasn't yet addressed by any Authority product. Staff responded by creating the Pooled Bonds Program ("PBP"), designed to give borrowers more flexibility to purchase equipment during a capital budget cycle through a tax-exempt line of credit format.

***What can the PBP offer your organization?***

*-An approved line of credit to be drawn down over 12 - 15 months*
*-Low cost variable interest rate debt*
*-Loan terms negotiated directly between the borrower and the credit enhancer*
*-Security provided through equipment liens and/or master indenture notes*
*-Standardized documents to cut drafting time*
*-Straightforward and uncomplicated prepayment terms*
*-Frequent opportunities to enroll, since bonds will be issued annually*

Under the program, a credit-enhancing bank, which will be Commerce Bank for the first issuance, will review applications submitted by potential borrowers and establish a credit line for each. Variable rate bonds issued by the Authority are then used to fund the pre-approved credit lines.

In order to be eligible for the Program, a borrower must be a 501(c)(3) organization, and must get pre-qualified by the Program's credit provider. Also, all proceeds must be used only for equipment or retrofitting for equipment. □

## REDESIGNED: EQUIPMENT REVENUE NOTE PROGRAM

The Authority has officially announced the revamping of its Equipment Revenue Note program ("ERN"), redesigned specifically to address concerns regarding the Program's process.

Like the Pooled Bonds Program, the ERN's new design was spawned at a meeting of the Authority's CFO Advisory Panel, where it was stated that the current product took too long to provide access to capital. Staff responded by modifying the process to offer both an easy and efficient method of financing and refinancing equipment.

Under the new procedure, the Authority approves one request for Negotiated Sale for the year's ERN issues, rather than requiring approval for each borrower and transaction. This modification alone reduces the process time by as much as a month. Additionally, the borrower can bring a bond purchaser to the table if it so desires, eliminating the time necessary to obtain competitive bids by the Authority.

In order to be eligible, the issue size must be $15 million or less, the proceeds must be used only for equipment acquisition costs, and the bonds must not be rated or enhanced.

***What can the ERN offer your organization?***

*-Low cost fixed and/or variable interest rate debt*
*-A negotiated loan term that will likely parallel life of equipment*
*-Security provided through equipment liens and/or master indenture notes*
*-A pre-approved negotiated private placement process that shortens the process by as much as a month*
*-Minimal financing costs*
*-Standardized documents to cut drafting time*

The Authority closed its first bond issuance under the new program design on behalf of Barnert Hospital on December 10th. Details follow on page 3. □

**IF YOU ARE INTERESTED IN BORROWING FUNDS THROUGH THE PBP OR THE ERN, NOTIFY AN AUTHORITY PROJECT MANAGEMENT REPRESENTATIVE AND YOU ARE WELL ON YOUR WAY TO COMPLETING THE ISSUE.**

# FINANCING NOTE$

*JCMC (exterior above left, interior above right),is expected to open its doors early this year.*

On November 20, 2003, the Authority completed a $75,075,000 bond issue on behalf of **Atlantic Health System** ("AHS"). The proceeds of the financing will be used to currently refund the Series 1993 bonds that had been issued on behalf of Mountainside Hospital and to pay for 2003 and 2004 capital budget items.

The AHS bonds are insured by Ambac Assurance Corporation, and were issued in a multi-modal form, which allows AHS some flexibility to react to changes in the interest rate market.

*AHS currently refunded the Mountainside Hospital Series 1993 Bonds.*

The bonds were issued in two maturities of approximately $38 million due in 2014 and $37 million due in 2025. Both maturities have a 7-day auction period. Goldman Sachs, the senior manager, agreed to underwrite the bonds with an interest rate of .9% for the first period.

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On December 11th, the Authority closed a $5.5 million Private Placement on behalf of **Barnert Hospital**. The single investor of the private placement is GE Capital Public Finance, Inc., and the proceeds of the bond issue will be used to purchase various items of equipment ranging from a $450,000 nursing call system to a $750 wheelchair. Proceeds may also be used for various installation costs and to pay the related costs of issuance.

The Barnert transaction is the first issuance under the Authority's newly redesigned Equipment Revenue Note program, which both simplifies and shortens the issuance process for borrowers seeking funds for equipment. For details on the new design, see page 2.

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A $102 million fixed rate transaction on behalf of **Capital Health System** ("CHS") was priced on November 19th, and closed on December 11th. The bonds are rated "BBB" by S&P and "Baa1" by Moody's. Wachovia Bank led the underwriting syndicate and offered to purchase the bonds at yields ranging from 1.75% in 2004 to 5.62% in 2033.

The proceeds of the CHS financing will be used to renovate the ICU/CCU at Helene Fuld, renovate the Emergency Room at Mercer Medical Center, acquire a linear accelerator and construct an Ambulatory Surgery Center in Hamilton Township. The proceeds will also fund 2003 and 2004 capital budget items and refinance more than $30 million in outstanding bonds issued on behalf of Mercer Medical Center.

A second series of bonds for CHS also closed on December 11th. This $30 million series is structured as variable rate demand obligations secured by a Wachovia Bank Letter of Credit. The proceeds will be used for hospital projects and to refund bonds issued under the Authority's Composite Program. The combined all-in-true interest cost for Series 2003A and 2003B is 5.22%.

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The **Jersey City Medical Center** ("JCMC") issuance of $16,440,000 worth of bonds closed on December 17th. The bonds are secured by FHA mortgage insurance, wrapped by municipal bond insurance from AMBAC, all of which provides a "AAA" rating on the bonds. After an order period that generated interest from primarily retail investors, Merrill Lynch, the underwriter for the issue, offered to buy the bonds at yields ranging from 1.35% in 2005 to 4.85% in 2030.

The bonds were issued with an optional call provision beginning in 2011 to match the provision in JCMC's 2001 bond issue. The net interest cost is 4.62%. The proceeds will provide funds for the completion of the construction and equipping of the new Medical Center.

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The Authority also closed a $19,125,000 bond transaction on behalf of the **State of New Jersey Department of Human Services** to complete the final design of the new Greystone Park Psychiatric Hospital in Morris County. The proceeds will also fund the demolition of a former dormitory building and realignment of roadways around the new hospital site. The Department plans, within three years, to open a new, smaller hospital to replace the numerous aging buildings on the Greystone campus, which currently houses and treats about 550 patients.

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Wrapping up the December issues is a $30,600,000 bond transaction on behalf of **Beth Israel Hospital Association of Passaic** ("PBI"), closed on December 30th. The proceeds of the issuance were used to finance the acquisition of The General Hospital Center at Passaic. PBI will move its current operations into the newly acquired facility, while the current PBI location will be used for new schools and athletic fields for the community, funded without taxpayer dollars. □

*The General Hospital Center at Passaic, owned by AHS, was purchased by Beth Israel Hospital Association of Passaic.*

# DEIRDRE IMUS

*(continued from page 1)*

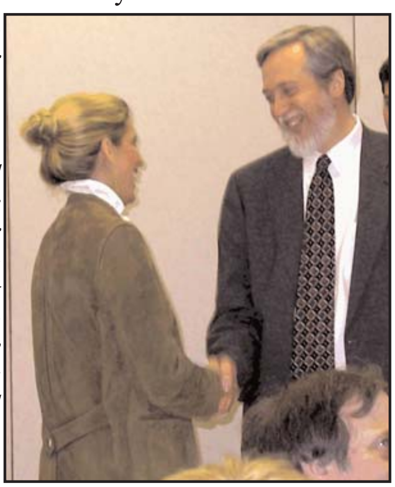
cation, thereby reducing the amount used and product container waste.

Perhaps most important, though, is the fact that a most vulnerable population is no longer surrounded by harmful chemicals that could damage a weakened body.

*Deirdre Imus spoke to Authority Members and guests from the State at the New Brunswick Hyatt.*

In Ms. Imus' words, "the Greening the Cleaning campaign is a perfect fit for hospitals since a facility meant for healing should be as free as possible from poisonous chemicals."

Ms. Imus' organization is also working with HUMC to build the state's first "green hospital" including the use of such products as environmentally safe insulation and air duct systems.



*Commissioner Clifton R. Lacy, M.D. thanked Deirdre Imus for discussing "greening" New Jersey's hospital*

Following the presentation, Ms. Imus answered questions from the audience, during which the attendees demonstrated great enthusiasm for green health care facilities. She then encouraged the attendees to consider the environment, not only in the construction of health care facilities, but also in their own homes.

*For more information about green cleaning or the Deirdre Imus Environmental Center for Pediatric Oncology, visit* http://www.dienviro.com.

# SCHOOL WORK

*(continued from page 1)*

Improving New Jersey's public school facilities would be no small task for the SCC. While the multi-billion dollar budget gave it the financial means to begin its work, improving all the 30+ troubled school districts in New Jersey requires careful financial planning. In addition, the projects require the State to locate property available for school construction in New Jersey's already over developed landscape.

The Authority saw in this the opportunity to help communities by downsizing fiscally troubled hospital systems while helping to free new school property.

Having built solid relationships with New Jersey's health care community, the Authority can communicate with hospitals in the troubled districts that might consider selling property for additional capital. As a facilitator, the Authority can introduce these hospitals to the SCC. The Authority can also coordinate the communications between hospitals, the State Department of Health and Senior Services and the Attorney General's Office.

The Authority began to work pro-actively as liaison and facilitator between troubled school districts, hospitals and the SCC, and with success!

In one such case, the Authority issued bonds on behalf of Beth Israel Hospital Association of Passaic ("PBI"), to help it acquire and relocate to The General Hospital Center at Passaic with the intention of freeing up property for school construction.

The SCC board approved the PBI project and set in motion their efforts to consolidate three new schools and relocate the Passaic Board of Education to the site. The project will result in a new middle school, elementary school & early childhood center, complete with athletic fields, all at the former PBI location. The enabling bond transaction closed on December 30, 2003, and the new schools are expected to be open by fall 2006.

The Authority hopes that the PBI project's success leads to future similar transactions between the hospital community and the SCC. The Authority has already heard from a number of hospitals interested in working with the SCC, including Trinitas Hospital, who has begun to negotiate the sale of the old Elizabeth General Hospital building for the construction of educational facilities. □

# AUTHORITY HOSTS 2nd CFO ADVISORY ROUNDTABLE

Mid-2003, the Authority created a CFO Advisory Panel to offer feedback about Authority products and procedures and to discuss the hot issues concerning Authority borrowers. The first meeting of the Panel led to the creation of a new Authority product, the redesigning of a financing program, and several Authority procedural revisions. Staff was anxious to regroup with the Panel in December to discuss the adjustments and to hear new insights.

The second Advisory Panel meeting, held on December 3rd, was attended by Bill Phillips, Jim Nolan, Rich Keenan, Stella Visaggio and Ron Guy.

The members discussed current **Industry Issues**, including the Authority's self-insurance/captive monitoring program. Panel members found the Authority's criteria to be stringent, including the required high confidence level (95% doubled). Authority staff took note of the feedback and stated that the required funding is *(continued on page 6)*

*Steve Fillebrown, Director of Research and Investor Relations, asked the Panel for feedback on the APOLLO database and reports*

# APOLLO REPORT:

## RESULTS FOR YEAR-END '02 & 2nd QUARTER '03

**By Steve Fillebrown, Director**
**Research and Investor Relations**

Below are some observations on the financial condition of New Jersey's hospitals, based on the Authority's APOLLO reports for the year-end 2002 and second quarter 2003.

### Trends in Statewide Medians

Median operating and profit margins were positive for a third straight year. The median operating margin increased from 1.06% to 1.86% and the median profit margin rose from 1.44% to 1.90%. However, the median debt service coverage ratio fell slightly from 2.80 in 2001 to 2.75 in 2002.

Through the second quarter of 2003, the median operating and profit margins fell to .34% and .98%. These declines were expected as a result of reduced Medicare outlier payments, increasing malpractice insurance costs, labor shortages and the end of one-time disproportionate share payments.

APOLLO numbers reflected continued improvement of median days of unrestricted cash on hand through 2002, rising from 78 to 98 days by year-end. At the same time, median days in accounts receivable continued to drop, from 63 to 56 days, and median days in accounts payable rose by one day to 64. Through the second quarter of 2002, though, median days cash on hand dropped 7 days from year-end. This drop may be explained by the increase of 4 days in median receivables accompanied by a 4-day decrease in median payables.

Leverage ratios increased noticeably in 2002, with the median debt to capitalization rising from 44% in 2001 to 50% in 2002. This increase appears to be in large part due to pension adjustments, as hospitals statewide increased their minimum pension liabilities by $250 million, or about 5% of unrestricted fund balances. Through the second quarter, the median debt to capitalization remained unchanged. Median long-term debt to net fixed assets was also constant, while median cash to debt increased in 2002 (but seems to have leveled off in 2003).

Last year the year-end APOLLO report cautioned that the growing average age of New Jersey facilities and the declining remaining useful life median both indicated a lack of capital spending. In 2002, due to an estimated $945 million in purchases of property, plant and equipment, the trend was reversed. Although average age of plant increased, so did median remaining useful life, rising from 7.5 years to 8.9 years. As a point of reference, in the previous eight years, capital spending was usually in the mid-$600 million range and the previous high was $736 million.

### Differences in Performance

There were some notable differences in trends across the peer groups used in the Apollo System such as bed size, teaching status, location, and income status. For example:

· Gains in liquidity were concentrated among hospitals serving low-income and middle-income populations, which is likely the result of the one-time disproportionate share settlements directed at facilities with high Medicaid and indigent caseloads;

· Low-income and middle-income hospitals showed higher median operating and profit margins than facilities serving high-income populations;

· Major teaching hospitals continued to post weaker medians than either the non-teaching or minor teaching peer groups; and

· As a group, hospitals with under 200 beds posted better medians than other hospitals but the small size of this group (just 10 hospitals) suggests not putting too much emphasis on these differences.

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*APOLLO is an Authority designed and operated database that includes financial information and characteristics on acute care New Jersey hospitals. The Authority uses the data to monitor financial trends among New Jersey's health care providers. Quarterly postings can be viewed on the Authority's website at* http://www.njhcffa.com/reports.htm. □

# SWAPS "IN YOUR OWN WORDS"

The Authority's Advisory Panel agreed that the borrowing community would benefit from further clarification on the swap market. Andrew McKendrick, Senior Managing Consultant at Public Financial Management ("PFM"), answered some questions.

Q: Please define "swap" in layman's terms.

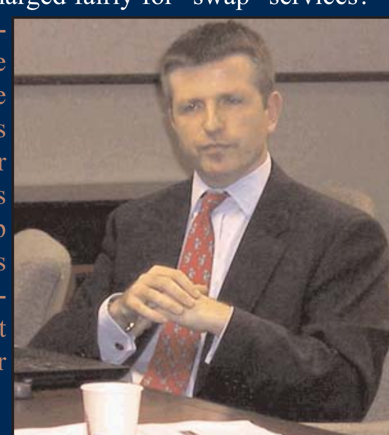
**A:** The typical swap discussed in the financial markets is an interest rate swap, or an agreement between two "counterparties" to exchange interest rate payments at specified points in the future.

Q: Under what circumstances would you most recommend an organization consider a "swap?"

**A:** Interest rate swaps are debt management tools. They are appropriate when prudently used as part of an organization's overall asset and liability management. Most organizations will use swaps for the first time as part of a debt raising effort, when the swap is used to help produce the overall cost of funding.

Q: How can an organization ensure that it is being charged fairly for "swap" services?

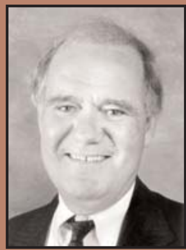
**A:** By far, the largest charge in entering into an interest rate swap is the "bid/offer" spread earned by the financial institution, which acts as counterparty to the swap. This is implicit in the rate at which the swap is executed, but may vary from 1 to 20 basis points per annum or more. A swap advisor can "open" the process to an issuer or make it more transparent. We also keep a database noting where various trades are executed as spreads to mid-market and write a "fair market opinion" to provide comfort that the swap was executed at a fair level and the organization was charged a fair amount.



*Andrew McKendrick (left) taught Authority staff about Swaps*

## Authority Advisory Panel Members at the 2nd Roundtable

*Atlantic City Medical Center*
*James P. Nolan, Jr.*



*Capital Health System*
*Ronald J. Guy*

*Hackettstown Comm. Hosp.*
*Stella Vissagio, CPA*

*Meridian Health System*
*William N. Phillips*

*Society of the Valley Hosp.*
*Richard D. Keenan*

# ADVISORY PANEL

*(continued from page 4)*

only temporary and will be revisited following A.M. Best Company's first round of ratings for the insuring entities.

The Panel also discussed:

- hospital investments in freestanding surgery centers,
- the reclassification of one New Jersey hospital as a "rural center",
- labor market index's negative impact on New Jersey hospitals,
- decreased in-patient psychiatric care; the replacement of psychiatric units,
- RN staffing and the reliance on agencies,
- Tennessee bond issue where a group of doctors were the investors.

Members agreed the new **Pooled Bonds Program**, created in response to the Panel's first meeting, is structured well. Feedback was offered on **APOLLO**, stating that completeness could be sacrificed for a quicker distribution.

The Panel also expressed interest in an **In-Service** tutorial session with a legal expert on Joint Ventures for staff and hospital CFOs.

Staff will process the suggestions and again tweak the Authority accordingly to best fit the needs of its borrowing community.□

## NJHCFFA '03 BONDS ISSUED

| | |
|---|---|
| Catholic Health East | $47,200,000 |
| Meridian Health System | $100,000,000 |
| Pascack Valley Hospital | $51,205,000 |
| Somerset Medical Center | $81,390,000 |
| The Community Hospital Group, Inc. | $20,000,000 |
| The Matheny School and Hospital, Inc. | $3,500,000 |
| Robert Wood Johnson University Hospital | $25,000,000 |
| Saint Clare's Hospital, Inc. | $15,400,000 |
| St. Francis Medical Center | $3,100,000 |
| St. Joseph's Wayne Hospital | $6,500,000 |
| Virtua Health | $11,000,000 |
| Shore Memorial Hospital | $31,205,000 |
| Rahway Hospital | $11,000,000 |
| Atlantic Health System | $75,075,000 |
| Barnert Hospital | $5,500,000 |
| Capital Health System | $131,560,000 |
| NJ DHS (Greystone Project) | $19,125,000 |
| Jersey City Medical Center | $16,440,000 |
| Beth Israel Hospital Assoc. of Passaic | $30,600,000 |
| Total Bonds Issued in 2003: | $684,800,000 |

# PRESENTATIONS BY NJHCFFA STAFF

Authority staff members are often asked to share their insight through presentations at various conferences and seminars throughout the year. On November 12th, Executive Director Michael Kornett spoke at the *Sixth Annual New Jersey Institutional Investors Conference* on the current and future state of health care financing in New Jersey. On November 13th, Jim Van Wart, Director of Authority Operations, spoke at the *Construction Forecast Seminar* on the NJHCFFA's projected financed construction volume for the years 2004 and 2005.

If you would like more information about the presentations, or would like an Authority staff member to present at an event of your own, please contact: Stephanie Zschunke, NJHCFFA Communications Department, szschunke@njhcffa.com. □

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