Hospitals Explain Need For Millions In Bank

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■ Though questioned by some, cash reserves allow non-profits to keep financial ratings healthy.

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How much money does a hospital need to keep in the bank?

Plenty, if you listen to hospital administrators who say they need a healthy reserve of cash and easily sold "liquid" assets. They can use the money to cover bills in a pinch, or as equity when they need to borrow money for expansions and equipment.

"When you don't have any money nobody wants to lend you any," said Richard Showalter, chief financial officer for Mary Hitchcock Memorial Hospital in Lebanon. "We've tried to keep our liquidity high for the credit markets."

The issue came up last week when Optima Health of Manchester tried to obtain tax-exempt bonding to refinance about $70 million in debt. Optima would have saved about $3 million or more over 20 years, depending on where interest rates were when the new bonds were issued.

But they won't be. The Executive Council gave Optima a good going over, saying it hasn't listened to community members who want Catholic Medical Center to remain as a full-scale acute care hospital. It voted 4-0 to deny the company the tax-exempt refinancing.

During discussion, it came out that Optima has reserves of

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$190 million, and ended 1996 with a $19 million surplus.

Documents filed with the state Higher Education and Health Facilities Authority showed that gave Optima 235 days worth of cash on hand.

That may sound like a lot, but it isn't the highest in the state. MHMH has $212.8 million in reserve, enough to fund 368 days of operations, Showalter said.

And according to the document submitted to HEHFA, the Lahey-Hitchcock System has $519 million between New Hampshire and Massachusetts operations. Lahey Hitchcock officials weren't available to discuss the figure, but Showalter said executives there told him their numbers don't agree with the HEHFA document. The system's total net worth is about $660 million, he said.

Craig Carnaroli, a director of the Merrill Lynch health care finance unit, said reserves are a way of judging the risk in lending to a hospital company.

"These companies want to borrow at the lowest interest rates. The way to get that is to have the highest bond rating," he said.

Optima, with its large reserves, has a AA rating, the highest available to a non-profit. "That indicates they are very prudent, and are perceived as very strong," Carnaroli said.

And its 235 days of cash on hand is about in line with the national norm. The U.S. median among non-profit healthcare companies is 224 days, Carnaroli said.

Michael Green, president and chief executive of the Capital Region Healthcare Corp., which operates Concord Hospital, said all not-for-profit hospitals need reserves. But he thinks some companies get carried away.

"In my own perspective you don't need what you used to need. We do need money for equipment replacement, but there has been so much change in health care that very few of us will build a larger hospital in the future. And it will be many years before we build new ones," he said.

Capital Region maintains reserves of $39 million, enough to cover 168 days of operations. Its profit in 1996 was $320,000. Green said the cash-on-hand figure is a measure of a company's liquidity, or ability to pay its bills, especially the interest on bonds. He figures his company has plenty of that.

"I think 150 days ought to be about the limit. If you eat into 150 days of cash on hand, your future is already determined for you," he said.

Capital Region's CFO Bruce Burns said there is no question non-profits need to maintain healthy reserves.

"Otherwise, when it's time to replace dilapidated or outdated facilities, in order to get access to capital, they may need to become affiliated with another organization."

Optima's treasurer, John A. Hession, said the Optima reserve is not as flush with cash as it might seem. The $190 million total includes about $50 million cash, he said. Another $111 million is in the form of investments in property, plant and equipment investments.

How does that come under the heading, "unrestricted liquidity" on Carnaroli's chart?

Hession likened the situation to a couple who own a house worth $100,000 in which they invested $20,000 savings. That $20,000 is their own money and, upon sale of the house, can be invested any way they choose.

He said the $19 million profit Optima made in 1996 was not off the pockets of patients. Most of it, about $13.8 million, came from the sale of securities. Another $5.7 million came from operations, he said.

He said Manchester needs to be sure Optima remains healthy so the decisions made on its future stay in local hands.

"The way things are in managed health care and Medicare, we could have periods of time when we lose substantial sums of money. If we become a weakened system because of reversals in financial results, then we'd have to seek out a white knight. And our neighbors around us would not be large enough," he said.

Alan Sager, a professor at the Boston University School for Public Health, criticized Optima's reserve level.

A staunch advocate for the Save CMC group in Manchester, Sager said Optima's revenues have increased steadily since it was formed from the companies that owned CMC and Elliot Hospital.

"You don't need this much reserve to get a good bond rating. . . . The money they've squireled away is overwhelmingly money raised by charging more than the cost of care. The question is when does that stop, when is it enough and what do they plan on doing with it?" Sager said.

Optima's next big project is a $35 million expansion on its Elliot Hospital campus that will house acute care services now based at CMC.

Sager questioned that, too.

"Optima has proposed and the state's health planning review board has incredibly approved spending $35 million and perhaps much more recreating two good-sized nursing units and the entire cardiac surgery and intensive care units that already exist in fine quarters at CMC. And somehow we call this the elimination of duplication."