

**Spectrum Health**

**Community Commitments Report**

**June 5, 2018**

Dear West Michigan Community,

As part of Spectrum Health's commitment to the community, and as part of our ongoing effort to share openly our compliance with the commitments we made in the Consent Decree, attached please find our demonstration of our financial compliance with (a.) our ongoing commitment to limit margins and (b.) our ongoing commitment to the underserved and medically needy.

Spectrum Health has committed to targeting a five-year rolling average total margin (which includes operating margin and investment income) for the merged system that does not exceed the average of Moody's and Standard & Poor's upper quartile total margins for other health systems nationally. Spectrum Health measures compliance with this commitment by comparing our five-year rolling average total margin to the Moody's Aa3 median total margin for freestanding hospitals, single-state & multi-state healthcare systems. We have included the most recent calculations, which demonstrate our compliance, in the attached report.

Spectrum Health also has committed to establish a fund to provide quality healthcare programs for the underserved in the community, which is budgeted in the amount of \$6.0 million per year. While a separate Community Advisory Committee provides for the ongoing allocation of this fund, we continue to represent that at least \$6.0 million has been included in the 2019 budget for this commitment, and that we have met our annual \$6.0 million spending requirement for the years up to, and including, 2018. We have included our most recent calculations, which demonstrate our compliance, in the attached report.

We take our commitments to the community very seriously and are steadfast in our determination to provide the information necessary for all stakeholders to be confident that their healthcare system has consistently executed the commitments made in the Consent Decree and has demonstrated the value that was anticipated when the merger of Blodgett Memorial Medical Center and Butterworth Health Corporation created Spectrum Health.

Sincerely,

A handwritten signature in black ink, appearing to read "Matthew E. Cox". The signature is written in a cursive, slightly slanted style.

Matthew E. Cox  
Senior Vice President and Chief Financial Officer

## COMMITMENT TO THE UNDERSERVED

Spectrum Health has agreed to establish a fund to provide quality healthcare programs for the underserved in the community. As part of this, Spectrum Health has agreed to increase spending from a pre-merger level of approximately \$2.0 million to \$6.0 million per year.

### Assertions

- Actual spending for programs to the underserved as of March 31, 2018 was \$5.2 million. Annualized to year-end, this level of funding equates to \$6.9 million. Spectrum Health is projecting actual expenditures for fiscal year 2018 will be less than the annualized amount and is anticipating expenditures of approximately \$6.0 million as of June 30, 2018.
- As of March 31, 2018, Spectrum Health has expended funds above the cumulative amounts related to the Commitment to the Underserved. The annual commitment spending of \$6.0 million per year from the merger date through March 31, 2018 totals \$123.0 million compared with actual spending by Spectrum Health for the same period of \$129.1 million resulting in actual spending which is greater than commitments through March 31, 2018 of approximately \$6.1 million.
- The Healthier Communities Department provides services which are not specifically related to one particular program. These services are as follows:

**Direct Program Administration** includes goal and financial management, program oversight, reporting and community-wide committee participation.

**Planning, Development and Management** includes capacity building, program design and management. Administrative expenses primarily include salary and benefits for staff, maintenance expenses and administrative supplies.

**Program Evaluation** includes outcomes measurement for the programs. Rather than giving each program a budget to develop an outcomes measurement function, the function was centralized so that one department would coordinate, monitor and analyze outcomes to provide a more consistent and credible tracking and monitoring system.

Outcomes measurement expenses include salaries and benefits for staff that provide support, education, data collection and analysis to the various programs, along with computer equipment, supplies and evaluation materials.

Total program support, including Program Administration, Planning, Development and Management, and Program Evaluation represented 12.5% of actual total community commitment expenditures in fiscal years 2018 and 2017.

The following summarizes the breakdown between Administration and Evaluation:

	<b>Actual FY 2017</b>	<b>Projected FY 2018</b>	<b>Budget FY 2019</b>
Program Administration	\$139,435	\$125,571	\$127,307
Planning, Development and Management	247,885	223,238	226,324
Program Evaluation	360,846	400,965	402,589
<b>Total Program Support</b>	<b>\$748,166</b>	<b>\$749,774</b>	<b>\$756,220</b>

## **MARGIN COMMITMENT**

Spectrum Health has agreed to target a five-year rolling average total margin for the merged system not to exceed the average of Moody's and Standard & Poor's upper quartile total margins for other health systems nationally.

The source for this benchmark is Moody's Outlook, where the median total margin based on 2016 data for freestanding hospitals, single-state & multi-state healthcare systems with an Aa3 bond rating was used. The worksheet on page five was included in order to demonstrate Spectrum Health's five-year rolling average total margin in comparison with the benchmark.

### **Assertions**

- The actual total margin for Spectrum Health System as reflected in the fiscal year 2018 statements, as of March 31, is 4.9%.
- The five-year average total margin for Spectrum Health System for the period including actual 2014, 2015, 2016, 2017 and year to date 2018 (through March 31, 2018) is 6.1%. The five-year average median Moody's total margin for freestanding hospitals, single-state & multi-state healthcare systems with an Aa3 bond rating is 6.6%.

## **FISCAL YEAR 2019 BUDGET REVIEW**

Our proposed budget and supporting documentation is provided in support of our assertion that the financial commitment to the underserved is incorporated into the fiscal year 2019 budget and that the total margin for the overall system is within the established benchmark per the Margin Commitments.

### **Assertions**

- Spectrum Health attests that \$6.0 million is included in the budget for fiscal year 2019 as part of our commitment to the underserved.
- Spectrum Health's total margin as reflected in the fiscal year 2019 budget is 4.2%. The five year rolling average total margin including actual 2015, 2016, 2017 year to date 2018 (through March 31, 2018) and budget 2019 is 5.4% compared to the five-year average median Moody's total margin for freestanding hospitals, single-state & multi-state healthcare systems with an Aa3 bond rating of 6.6%.

## Spectrum Health System & Affiliates

### Total Margin Calculation - Total System

Through Budget Year Ended 6/30/19

(in thousands)

	<b>Audited 6/30/14</b>	<b>Audited 6/30/15</b>	<b>Audited 6/30/16</b>	<b>Audited 6/30/17</b>	<b>Unaudited Actual Nine Months Ended 3/31/18</b>	<b>Proposed Budget 6/30/19 (A)</b>	<b>Five Year Average Moody's Median (D)</b>	<b>Actual Five Year Average Margin (B)</b>	<b>Budgeted Five Year Average Margin (C)</b>
Total operating revenue	\$ 4,107,828	\$ 4,625,176	\$ 5,220,515	\$ 5,681,179	\$ 4,470,538	\$ 6,386,255		\$ 4,821,047	\$ 5,276,733
Total non-operating income (expense)	188,156	80,036	(57,682)	165,179	92,794	70,878		93,697	70,241
Total revenue	4,295,984	4,705,212	5,162,833	5,846,358	4,563,332	6,457,133		4,914,744	5,346,974
Total operating expenses	3,960,081	4,337,901	4,950,789	5,489,123	4,337,523	6,182,859		4,615,083	5,059,639
Total margin	\$ 335,903	\$ 367,311	\$ 212,044	\$ 357,235	\$ 225,809	\$ 274,274		\$ 299,660	\$ 287,335
Total margin % (E)	7.8%	7.8%	4.1%	6.1%	4.9%	4.2%	6.6%	6.1%	5.4%

(A) Per 2019 Budget

(B) Five year average margin based on actual results for 2014 through March 2018

(C) Five year average margin based on actual results from 2015 through March 2018 plus 2019 Budget

(D) The total margin % (or excess margin as referred to by Moody's) is calculated as follows based on Moody's formula:

(total operating revenue less total operating expenses plus non-operating income) divided by (total operating revenue plus non-operating income).

(E) Moody's represents the median excess margin for freestanding hospitals, single-state and multi-state healthcare systems with an Aa3 rating