Spectrum Health Grand Rapids

Community Commitments Report

November 5, 2019
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 related to the merger of Butterworth Health Corporation (including Helen DeVos Children’s Hospital) and Blodgett Memorial Medical Center (collectively, Spectrum Health Grand Rapids), attached please find our demonstration of our financial compliance with

- our ongoing commitment to limit margins, and
- our ongoing commitment to the underserved and medically needy.

As a result of our decision to change our fiscal year from a June 30 year end to a December 31 year end, the attached report represents the results of the six month bridge period from July 1, 2019 to December 31, 2019, and our attestation to these commitments for the calendar year ending December 31, 2020.

Spectrum Health Grand Rapids has committed to targeting a five-year rolling average total margin (which includes operating margin and investment income) that does not exceed the average of Moody’s and Standard & Poor’s upper quartile total margins for other health systems nationally. Spectrum Health Grand Rapids 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 Grand Rapids 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 calendar year 2020 budget for this commitment. In addition, we have met our annual $6.0 million spending requirement for the years up to the fiscal year ending June 30, 2019 and $3.0 million in the six-month bridge period ending December 31, 2019. 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 Grand Rapids.

Sincerely,

Matthew E. Cox
Chief Financial Officer
COMMITMENT TO THE UNDERSERVED

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

Assertions

- Actual spending for programs to the underserved for the six-month bridge period as of September 30, 2019 was $1.5 million. Annualized to the six-month period, this level of funding equates to $3.0 million. Spectrum Health Grand Rapids is projecting actual expenditures for bridge period 2019 equal to the annualized amount and is anticipating expenditures of approximately $3.0 million as of December 31, 2019.

- As of September 30, 2019, Spectrum Health Grand Rapids 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 September 30, 2019 totals $132.0 million compared with actual spending by Spectrum Health Grand Rapids for the same period of $140.7 million resulting in actual spending which is greater than commitments through September 30, 2019 of approximately $8.7 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 12.0% of actual total community commitment expenditures in the bridge period and fiscal year 2019.

The following summarizes the breakdown between Administration and Evaluation:

<table>
<thead>
<tr>
<th></th>
<th>Actual FY 2019</th>
<th>Projected Bridge Period 2019</th>
<th>Budget 2020</th>
</tr>
</thead>
<tbody>
<tr>
<td>Program Administration</td>
<td>$123,405</td>
<td>$61,352</td>
<td>$126,000</td>
</tr>
<tr>
<td>Planning, Development and Management</td>
<td>219,387</td>
<td>109,070</td>
<td>223,800</td>
</tr>
<tr>
<td>Program Evaluation</td>
<td>376,388</td>
<td>188,984</td>
<td>383,900</td>
</tr>
<tr>
<td><strong>Total Program Support</strong></td>
<td><strong>$719,180</strong></td>
<td><strong>$359,406</strong></td>
<td><strong>$733,700</strong></td>
</tr>
</tbody>
</table>

**MARGIN COMMITMENT**

Spectrum Health Grand Rapids 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 2018 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 Grand Rapids as reflected in the bridge period statements as of September 30, 2019, is 8.9%.

- The five-year average total margin for Spectrum Health Grand Rapids for the period including actual fiscal years 2016, 2017, 2018 and 2019 and projected bridge period ending December 31, 2019 is 6.2%. The five-year average median Moody’s total margin for freestanding hospitals, single-state & multi-state healthcare systems with an Aa3 bond rating is 6.3%.
CALENDAR YEAR 2020 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 calendar year 2020 budget and that the total margin for Spectrum Health Grand Rapids is within the established benchmark per the Margin Commitments.

Assertions

- Spectrum Health Grand Rapids attests that $6.0 million is included in the calendar year 2020 budget as part of our commitment to the underserved.

- Spectrum Health Grand Rapids’ total margin as reflected in the calendar year 2020 budget is 4.8%. The five-year rolling average total margin including actual fiscal years 2017, 2018 and 2019, projected bridge period ending December 31, 2019, and calendar year 2020 budget is 5.1% 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 6.3%.
## Total Margin Calculation
Through Calendar Year Budget Ended 12/31/2020

*(in thousands)*

<table>
<thead>
<tr>
<th></th>
<th>Audited 6/30/16</th>
<th>Audited 6/30/17</th>
<th>Audited 6/30/18</th>
<th>Audited 6/30/19</th>
<th>Projected Bridge Period 12/31/19 (F)</th>
<th>Proposed Budget 12/31/20 (A)</th>
<th>Five Year Average Moody's Median (E)</th>
<th>Actual Five Year Average Margin (B)</th>
<th>Budgeted Five Year Average Margin (C)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total operating revenue</td>
<td>$1,964,264</td>
<td>$1,965,343</td>
<td>$2,073,127</td>
<td>$2,262,335</td>
<td>$1,158,552</td>
<td>$2,319,000</td>
<td>$2,094,138</td>
<td>$2,172,968</td>
<td></td>
</tr>
<tr>
<td>Total non-operating income (expense)</td>
<td>1,435</td>
<td>(726)</td>
<td>113</td>
<td>4,068</td>
<td>989</td>
<td>1,262</td>
<td>$1,306</td>
<td>$1,268</td>
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<tr>
<td>Total revenue</td>
<td>1,965,699</td>
<td>1,964,617</td>
<td>2,073,240</td>
<td>2,266,403</td>
<td>1,159,541</td>
<td>2,320,262</td>
<td>2,095,444</td>
<td>2,174,236</td>
<td></td>
</tr>
<tr>
<td>Total operating expenses</td>
<td>1,776,092</td>
<td>1,864,622</td>
<td>1,983,225</td>
<td>2,146,001</td>
<td>1,078,849</td>
<td>2,208,000</td>
<td>$1,966,398</td>
<td>$2,062,377</td>
<td></td>
</tr>
<tr>
<td>Total margin</td>
<td>$189,607</td>
<td>$99,995</td>
<td>$90,015</td>
<td>$120,402</td>
<td>$80,692</td>
<td>$112,262</td>
<td>$129,047</td>
<td>$111,859</td>
<td></td>
</tr>
<tr>
<td>Total margin % (D)</td>
<td>9.6%</td>
<td>5.1%</td>
<td>4.3%</td>
<td>5.3%</td>
<td>7.0%</td>
<td>4.8%</td>
<td>6.3%</td>
<td>6.2%</td>
<td>5.1%</td>
</tr>
</tbody>
</table>

(A) Per Calendar Year 2020 Budget.
(B) Five year average margin based on actual results for fiscal years 2016 through 2019 and projected results for the bridge period 2019.
(C) Five year average margin based on actual results from fiscal years 2017 through 2019, projected results for bridge period 2019, plus Calendar Year 2020 Budget.
(D) The total margin % (or excess margin as referred to by Moody's) is calculated as follows based on Moody's formula:

\[
\text{Total margin} = \frac{\text{total operating revenue} - \text{total operating expenses} + \text{non-operating income}}{\text{total operating revenue} + \text{non-operating income}}
\]

(E) Moody's represents the median excess margin for freestanding hospitals, single-state and multi-state healthcare systems with an Aa3 rating.
(F) The bridge period represents the six-month transition period, July 1, 2019 through December 31, 2019.