

Truths and Myths in Securing Financing for Rural Hospital Construction Projects



Truths and Myths in Securing Financing

- This is the Iowa Field of Dreams – ***“Build It and They Will Come”***.
- The only reason a small to medium size rural hospital can do a major project is because of the CAH regs, and in all likelihood, as more and more CAH’s invest substantially in their physical plants Congress and Medicare will then change the regs and limit or disallow depreciation and interest expense.
- Should wait a year or two to consider a major project because the financing market is in a state of upheaval due to sub prime mess.

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- The only way a rural hospital can successfully sell tax exempt bonds in this market is to be rated, insured or guaranteed.
- The local bank(s) will want to participate in any long term financing for the hospital.
- Rural hospitals do not need to relocate to major highways since everyone in town knows where the hospital is anyway!

Truths and Myths in Securing Financing (continued)

- HUD 242 loan guarantee application program has been streamlined for CAH's and it is now much more available and easier to acquire.
- USDA is the preferred lender for major rural hospital capital projects.
- Maximum borrowing will rarely exceed 2 times *net revenues*.
- A rural hospital cannot secure financing if their projected debt service coverage is below 1.5.

Truths and Myths in Securing Financing (continued)

- A rural hospital should first spend down their excess cash on major projects so as to avoid excess interest cost and excess loan risk.
- A rural hospital must get *consensus* of stakeholders so as to avoid community disagreements on such a significant community project
- As a rule of thumb it is easier and less expensive to build a new hospital than renovating the present facility.

Truths and Myths in Securing Financing (continued)

- With the pending (current) recession hospital construction costs should decrease so the rural hospitals should hold off on a major project until construction costs are more favorable.
- It is better to renovate and improve your current facility in multiple year phases versus doing it all at once. By doing this, you take less risk.
- A good way to test your thinking is to get a forecast prepared by an experienced health care accounting firm.
- Rural hospitals must have tax support in order to invest substantially in their facilities.

Truths and Myths in Securing Financing (continued)

- If market share has been declining the rural hospital does not have the patient base to invest in a major renovation or total replacement.
- Most rural hospitals cannot build a new facility because people in the rural community would never accept abandoning the present facility.
- By their nature rural hospital boards are conservative thus would never allow the hospital to borrow millions of dollars, of even tens of millions of dollars.

Truths and Myths in Securing Financing (continued)

- You cannot raise significant funds for building projects in most rural communities since they tend to be poor.
- If a neighboring facility has just done a replacement hospital, then you cannot also do one.
- Doctors must be recruited **before** you can embark on a major construction project.
- To have a successful project, this is the order the following project team members should be retained:

Accountants and Attorneys
Construction Manager
Financial Advisor
Underwriter/Banker/Lender
Architect