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Ratings

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Illinois Finance Authority Rush University Medical Center Obligated Group; Joint Criteria; System

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Illinois Finance Authority
Rush University Medical Center Obligated Group; Joint Criteria; System

Credit Profile		
Illinois Fin Auth, Illinois		
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Illinois Fin Auth (Rush Univ Med Ctr Obligated Grp) SYSTEM		
Long Term Rating	A+/Stable	Affirmed
Series 2006B-1		
Unenhanced Rating	NR(SPUR)	Current
Series 2008A		
Unenhanced Rating	A+(SPUR)/Stable	Affirmed
Long Term Rating	AAA/A-1+	Affirmed

Rationale

S&P Global Ratings affirmed its 'A+' long-term rating on the Illinois Finance Authority's series 2015A and 2015B fixed-rate hospital revenue bonds. We also affirmed our 'A+' underlying rating (SPUR) on the authority's series 2008A revenue bonds. At the same time, S&P Global Ratings affirmed its 'AAA/A-1+' rating on the authority's series 2008A variable-rate demand bonds (VRDBs). All bonds were issued for the Rush University Medical Center Obligated Group (Rush). Rush University Medical Center (RUMC) is the largest entity of the obligated group. The outlook, where applicable, is stable.

The 'AAA/A-1+' dual rating on the series 2008A VRDBs is based on our joint criteria, with the 'AAA' long-term component of the rating based jointly on the Northern Trust Co. (AA-/Stable/A-1+) and the SPUR on Rush. The 'A-1+' short-term component of the rating is based on the Northern Trust short-term rating. The letter of credit expires on Sept. 30, 2017.

The 'A+' rating reflects our view of Rush's continued strong cash flow contributing to robust maximum annual debt service (MADS) coverage; good business position, albeit in a very competitive and fragmented market; and improving balance sheet. Rush's unrestricted reserves are down temporarily after a couple years of growth, but we expect this upward trend to return per management expectations and with expected strong cash flow. Rush's strong market and business position continues to be anchored by RUMC, which has benefited from its new patient tower; continued key service-line investments; Rush's integrated approach to research, education, and clinical services; and physician alignment through the Rush Health organization as well as other partnerships. We do view Rush as being on a favorable trajectory with Rush embarking on some key strategic projects, including some specific outpatient projects that we expect will benefit Rush over the medium to long term. However, those projects will likely involve higher capital spending over the next few years and we expect to get clarification on some of the larger projects as well as

funding over the next couple of years. That said, we understand from management that balance sheet metrics will continue to improve over the next couple of years.

The 'A+' rating further reflects our view of Rush's:

- Large operating revenue base of $2.1 billion from three served markets and favorable volumes at the academic medical center along with continued strong market recognition for RUMC as an academic medical center with broad clinical services, extensive education and research capabilities, and an improving market position as a result of its offering of several key service lines in the competitive Chicago-area market;
- Track record of solid financial operations and cash flow that have exceeded budgeted expectations and that management projects will remain consistent with recent years' metrics, as well as robust coverage of more than 5x for the past three and a half years;
- Strengthening balance sheet, which in our view should continue to improve given the track record of healthy cash flow, although capital expenditures will begin to ramp up beginning in 2017; and
- Proactive approach to preparing for the potential reimbursement changes resulting from the health care reform bill through various initiatives, including investing in outpatient strategies and Rush Health, the system's clinically integrated network.

Partly offsetting the above strengths, in our view, are Rush's:

- Location in the highly competitive and fragmented Chicago service area, with RUMC in close proximity to three other hospitals in its immediate service area and with three other academic medical centers as well as community hospitals or health systems providing strong competition for key services;
- Limited income and revenue dispersion (compared with other not-for-profit health care systems) with operating income and revenue coming primarily from RUMC; and
- Moderate concentration of Medicaid revenue in the payor mix and correspondingly moderate reliance on the state provider fee program and disproportionate share funds for solid operating income (however, management has focused on expense management and revenue improvements through service line focus and expansion to provide cushion against any potential stress from these programs and the state).

Rush is an integrated delivery system serving Chicago and primarily the western suburbs but considers its service area as the greater eight-county Chicago metro area. The 'A+' rating is based on our view of Rush's group credit profile and the obligated group's core status. Accordingly, we rate the bonds at the same level as the group credit profile. The obligated group consists of the following entities, whose gross revenue secure the bonds:

- RUMC, which consists of Rush University Hospital (a 679-staffed-bed academic medical center in Chicago), Rush University (a health sciences university with more than 2,500 students and a slightly increased $131 million of annual research that consists of four colleges, including nursing and medical schools), and Rush University Medical Group (a faculty practice plan);
- Rush Oak Park Hospital (ROPH), a 128-staffed-bed acute care center in the neighboring suburb of Oak Park; and
- Rush-Copley Medical Center Inc. (RCMC), which is the parent company of Copley Memorial Hospital Inc. (CMH, a 210-staffed-bed acute care medical center in Aurora, a far southwest suburb of Chicago), Rush-Copley Foundation, Copley Ventures Inc., and Rush-Copley Medical Group NFP.

RUMC (which includes ROPH) is the largest member of the obligated group, accounting for 85% of Rush's net assets, 83% of total revenue, and approximately 76% of operating income as of fiscal year-end June 30, 2015. Rush's total

long-term debt, including capital leases and other financing arrangements, was $679 million as of Dec. 31, 2015, largely in a conservative fixed interest rate mode.

Outlook

The stable outlook reflects our view that the system will continue to generate strong cash flow and coverage while continuing to increase unrestricted reserves. Although we expect possible increased spending over the next two years, we believe that unrestricted reserves should still benefit given the strong cash flow. The outlook also reflects our anticipation that Rush's business position will remain strong and that the system will continue to weather the evolving pressures of the health care industry.

Upside scenario

We could consider a higher rating if Rush is able to continue to increase unrestricted reserves amid increasing capital spending, clarify some of the specifics around the larger capital projects that are likely to begin in the next three years, and demonstrate that the balance sheet could absorb the ongoing heightened spending and any contemplated additional debt at a higher rating. In addition, we would expect that Rush would maintain its strong enterprise profile and market position as well as its healthy operations.

Downside scenario

A lower rating, while not anticipated, could result if capital spending increases and cash flow attenuates, if significant debt is issued to pressure the balance sheet, or if cash flow falls out of line with recent years' trends.

Enterprise Profile

Economic fundamentals

Rush consists of three medical centers in three separate areas in the greater Chicago area. It serves eight counties that have an estimated population of 8.7 million. More specifically, because of the services it provides, RUMC considers its service area the larger eight-county area. RCMC is about 40 miles west of Chicago and has a primary service area (PSA) population of slightly more than 360,000, while ROPH is about eight miles west of RUMC and has a PSA population of 78,000. The system benefits from the diverse local economy of Chicago, but the city's wealth indicators slightly trail national averages. Rush's payor mix has improved slightly in the past two years, but Rush continues to derive 15% of net revenue from Medicaid and has seen modest effects from expansion of insurance in Illinois as well as state-related issues.

Market position

Overall, we view Rush as well positioned with a focus on service lines, clinical integration, and partnerships, and a niche position as a health sciences university with a solid research presence. We do view Rush as slightly less diversified than many of the systems in our portfolio with RUMC contributing the vast majority of income and operating revenue for the system. We take a positive view of the growing outpatient strategy and expect that the strategies will continue to support and enhance Rush's larger business position.

We believe RUMC, located in the Illinois Medical District along with the University of Illinois Medical Center, John H.

Stroger Jr. Hospital of Cook County, and the Jesse Brown VA Medical Center, has a good and growing market position despite its location in a competitive market. RUMC largely competes with other Chicago academic medical centers--Northwestern Memorial Hospital, University of Chicago Hospitals and Health System, Loyola University Health System, and University of Illinois Medical Center--as well as with other large providers that provide similar tertiary care such as Advocate Christ Hospital, part of Advocate Health. Although the market is fragmented, several providers have or are pursuing partnerships with other in-state and out-of-state providers, and we believe these partnerships will continue to intensify competition. Rush is also pursuing various partnerships through its telehealth, stroke, and perinatal networks as well as with other physicians and providers through Rush Health, Rush's clinically integrated network that also includes Riverside Medical Center. We view Rush Health as a good tool to prepare for changes related to health care reform. Rush Health was created to integrate specific services that included managed care contracting, but in recent years has focused on population health and quality improvement strategies. Rush's improving market position is due to the strength of and investment in a number of key services and recent investments in its facilities, both of which have led to favorable volumes, along with its integrated strategy with research and education as well as focus on physician alignment. Rush has a large and growing active medical staff of more than 1,900 physicians. Approximately 600 are employed, with the majority being at RUMC. RUMC also employs 667 medical residents and has a significant research focus along with the university. A majority of the physicians participate in Rush Health and are well engaged with the system's strategic initiatives.

RUMC's market share in its total eight-county service area remained stable at 3.2% in 2015 compared with 2014 but was up from 2.9% in 2012, with the highest individual hospital market share going to Northwestern (4.8%) and second-highest to Advocate Christ (4.2%). The CMH competes with five providers in the area, but has the leading and growing PSA market share of 39.5%, with the second leading provider, Presence Health's Mercy Medical Center, capturing 17.9%. Recent facility investments have benefited CMH in fast-growing Kendall County. We believe the additional investments at CMH, specifically the operating room renovations and expansion, will continue to strengthen CMH's position. RUMC also has a cancer facility in the western suburbs with DuPage Medical Group, one of the largest independent multispecialty physician groups in the Chicagoland area. ROPH also has a leading 22.2% market share in its more limited service area.

Volumes at Rush increased almost across the board through fiscal 2015, but inpatient admissions are down through interim 2016. (Outpatient visits continue to trend upward during the interim period.) Acuity of services provided remains high with Medicare acute case mix index increasing to 1.92 through December from 1.81 at fiscal year-end June 30, 2015. RUMC has several nationally recognized programs, including orthopedics, geriatrics, and nephrology, and captures a good share of the markets for neurosciences, cancer care, heart and vascular, transplant, and high-risk infant and mother services. RCMC and ROPH also benefit from some of these programs. We anticipate that the system's volumes will remain strong in the near term as Rush continues to strengthen its breadth and depth of services and expand patient access partly through its specialty care and outpatient networks.

Table 1

Rush University Medical Center Obligated Group Utilization

	--Six-month interim ended Dec. 31--	--Fiscal year ended June 30--		
	2015	**2015**	**2014**	**2013**
PSA population	N.A.	8,655,312	8,700,000	N.A.
PSA market share %	N.A.	3.2	3.2	N.A.
Inpatient admissions*	22,932	47,282	46,084	45,939
Equivalent inpatient admissions	51,368	103,761	98,192	94,600
Emergency visits	89,286	177,994	162,839	161,160
Inpatient surgeries	8,460	16,907	16,119	15,756
Outpatient surgeries	14,655	29,136	29,459	29,966
Medicare case mix index	1.9200	1.8100	1.8100	1.7900
FTE employees	10,878	10,640	10,144	9,703
Active physicians	1,919	1,902	1,934	N.A.
Top 10 physicians admissions %	N/A	N/A	N/A	N/A
Medicare %§	27	26	26	26
Medicaid %§	15	16	16	13
Commercial/blues %§	52	50	50	52

*Excludes newborns, psychiatric, and rehabiliation admissions. §Based on net revenue. FTE--Full-time equivalent. N/A--Not applicable. N.A.--Not available. PSA--Primary service area.

Management and governance

Rush has a stable and strong management and governance team, in our view, that has improved the organization's competitive and financial position while allowing it to cope with industry trends. Rush also remains focused on research and education and has sustained its investment and growth in both areas.

The executive team consists of well-tenured members that have navigated the evolving pressures of the industry as well as the delayed state payments while investing more than $1 billion in transforming RUMC's campus. One key change is the upcoming retirement of President Peter Butler. However, with succession planning in mind, Rush recruited Michael Dandorph a couple of years ago as chief operating officer (COO) and he will step into the role of president and COO effective July 1, 2016, when Mr. Butler retires. There is also a new role of senior vice president of system integration, filled by the previous chief medical officer (CMO), Dr. David Ansell. The CMO role has been filled by Dr. Omar Lateef, another Rush physician who has been in various leadership roles. There is also a new dean of the medical college, Dr. K. Ranga Rama Krishnan, as well as a couple of other transitions that have been smooth to date.

Long-term forecasts are updated each spring, and management has generally either met or exceeded its budgets during the past several years, indicating its ability to understand its stress points and navigate them. The system is also planning for its next period of strategic investments, which will likely increase capital spending over the next three to five years but will also likely to continue to support and strengthen Rush's presence in the market.

We also take a positive view of Rush's focus on generating strong cash flow through growth as well as expense management and revenue optimization, and we believe that these efforts will serve Rush well as the industry continues to undergo revenue pressures. We take a positive view of Rush's recent investment in its enterprise resource planning (ERP) system and believe it should help Rush implement another wave of efficiencies.

Financial Profile

Financial performance

Rush has posted good operating margins of more than $2 billion in total operating revenue for several years (including after tower completion) as a result of sustained volume growth, expense and clinical resource management efforts, and funding support from supplemental programs. There are always yearly one-time or nonrecurring items, but fiscal 2015 yielded only a net $10 million (compared with about $24 million in the prior year). Cash flow is strong and has considerably strengthened MADS coverage to more than 5x on a fairly consistent basis. Operating results improved in fiscal 2015 and continued to exceed budgeted expectations. While Rush has less revenue dispersion than our typical system, we view all three hospitals contributing to operating income positively. In fiscal years 2015, 2014, and 2013, the system benefited from the state provider tax, which netted approximately $48 million, $44 million, and $21 million, respectively. Operations in fiscal 2016 to date have been good and above budgeted expectations as a result of acuity of services as well as expense management although inpatient volumes are down over the prior-year period for the first time in a few years. Management is optimistic that it will finish ahead of budget in fiscal 2016 (for the 12th straight year) and projects improving cash flow during the next five years as it continues to execute its growth strategies and manage its expense base.

Nonoperating revenue remained steady in recent years, further supporting overall cash flow and MADS coverage. Excess income and EBIDA margins have remained very strong, contributing to robust MADS coverage of more than 5x for the last few years.

Financial flexibility

The system's balance sheet continued to improve as a result of growth in unrestricted reserve (given solid cash flow) and declines in debt as it amortizes. (We adjusted Rush's unrestricted reserves to account for the full self-insurance liability.) All of this should position the organization well for any future spending or investment needs. Despite capital spending surpassing depreciation levels, continued good cash flow and investment gains contributed to the 16% growth in unrestricted reserves in 2015. Some interim declines have occurred as a result of the conversion to ICD-10, a couple of information technology upgrades, the implementation of a large ERP tool, and, to a lesser extent, state delays in payment. However, management expects that Rush should still finish the year with growth in cash on hand. In addition, the system has $530 million endowment for donor-restricted purposes. Rush's investments are largely in fixed income (70%) and cash (23%), with almost all accessible within seven days, which we view as very good liquidity for an organization of this size.

After the completion of the $1 billion, 12-year capital transformation project, capital spending returned to depreciation levels for the past several years. However, we expect increased capital spending will likely resume in 2017 and last for several years. Despite increased capital spending, management expects that strong cash flow will continue to strengthen the overall balance sheet. Key larger capital projects include a new outpatient tower near the main hospital (not likely to begin until 2018), a joint venture orthopedic center in the western suburb of Oak Brook (and not likely to begin until fiscal 2018) and a CMH surgical (and entrance) project. We view these outpatient and surgical projects as positive from a strategic perspective and believe they will help strengthen the obligated group's overall position. Management plans to monitor capital spending while continuing to improve the balance sheet.

Debt and contingent liabilities

We view Rush's debt levels as consistent with rating medians and expect some improvement over the next couple of years as principal amortizes. Total debt increased in fiscal 2015 as a result of refinancing, which contributed about $77 million of premium. We view Rush's mostly fixed-rate debt structure with approximately 14% of debt in variable-rate mode as very conservative. (The inclusion of a swap drops variable-rate debt to about 6%.) Half of Rush's variable-rate bonds are placed with a commercial bank and the other half are issued as VRDBs. Management has announced some larger projects, as indicated above, and while there are no immediate new money debt plans some additional debt will likely be issued as management refines its capital plans. Timing and amount are still under review and a debt issuance may occur in fiscal 2018.

Rush also maintains $100 million in a line of credit as a backup to help manage any unanticipated cash pressures, which we also view as prudent given the state's delay in Medicaid payments.

In addition, given Rush's current credit profile, we don't view its two swaps as a significant concern. Rush was party to two floating- to fixed-rate swaps on a total notional amount of approximately $89.4 million at June 30, 2015. The counterparties on the swaps are Morgan Stanley Capital Services Inc., with a guarantee by Morgan Stanley (A-) and Citibank N.A. (AA). As of June 30, 2015, the mark-to-market value of the swaps was a liability of $18.1 million with no collateral required. Rush is using $50 million of the interest rate swap outstanding to synthetically fix the interest rate on the series 2008A VRDBs, and the remaining swap notional amount is unhedged.

Rush's defined benefit pension plan declined slightly to a still healthy 89% (from 95% in the prior year) at June 30, 2015. The benefit obligation itself has stabilized given some plan changes the organization implemented with employees who had vested but terminated their employment with Rush prior to January 2015. As a result of timing, the system contributed a lower $801,000 relative to its expense of $22.2 million and $51.0 million last year but anticipates contributing $67.3 million in fiscal 2016.

Table 2

Rush University Medical Center Obligated Group Financial Summary

	--Six-month interim ended Dec. 31--	--Fiscal year ended June 30--			'A+' rated health care system medians
	2015	2015	2014	2013	2014
Financial performance					
Net patient revenue ($000s)	934,683	1,811,272	1,719,676	1,592,707	1,539,478
Total operating revenue ($000s)	1,052,838	2,079,914	1,961,188	1,817,739	MNR
Total operating expenses ($000s)	1,009,515	1,994,419	1,887,093	1,761,550	MNR
Operating income ($000s)	43,323	85,495	74,095	56,189	MNR
Operating margin (%)	4.1	4.1	3.8	3.1	2.9
Net non-operating income ($000s)	19,973	33,857	28,598	45,654	MNR
Excess income ($000s)	63,296	119,352	102,693	101,843	MNR
Excess margin (%)	5.9	5.7	5.2	5.5	5.1
Operating EBIDA margin (%)	10.6	11.8	12.0	12.7	10.1
EBIDA margin (%)	12.3	13.2	13.3	14.8	12.0
Net available for debt service ($000s)	131,562	278,933	264,061	276,340	214,196

Table 2

Rush University Medical Center Obligated Group Financial Summary (cont.)

	--Six-month interim ended Dec. 31--	--Fiscal year ended June 30--			'A+' rated health care system medians
	2015	2015	2014	2013	2014
Maximum annual debt service (MADS; $000s)	46,649	46,649	46,649	46,649	MNR
MADS coverage (x)	5.64	5.98	5.66	5.92	4.60
Operating-lease-adjusted coverage (x)	3.96	4.14	4.00	4.26	3.40
Liquidity and financial flexibility					
Unrestricted reserves ($000s)	993,457	1,036,310	894,700	742,625	905,785
Unrestricted days' cash on hand	189.3	202.0	184.9	166.4	190.6
Unrestricted reserves/total long-term debt (%)	146.3	151.7	143.6	116.0	153.4
Unrestricted reserves/contingent liabilities (%)	1,104.6	1,152.3	934.7	736.0	MNR
Average age of plant (years)	13.1	10.7	10.2	8.4	10.1
Capital expenditures/depreciation and amortization (%)	104.6	105.2	83.6	63.5	110.1
Debt and liabilities					
Total long-term debt ($000s)	679,072	683,206	623,244	640,203	MNR
Long-term debt/capitalization (%)	34.3	35.0	32.1	35.6	33.7
Contingent liabilities ($000s)	89,935	89,935	95,720	100,895	MNR
Contingent liabilities/total long-term debt (%)	13.2	13.2	15.4	15.8	MNR
Debt burden (%)	2.17	2.21	2.34	2.50	2.50
Defined benefit plan funded status (%)	N.A.	88.56	95.12	91.17	82.70

MNR--Median not reported. N/A--Not applicable. N.A.--Not available.

Related Criteria And Research

Related Criteria

- USPF Criteria: Contingent Liquidity Risks, March 5, 2012
- USPF Criteria: Not-For-Profit Health Care, June 14, 2007
- USPF Criteria: Assigning Issue Credit Ratings Of Operating Entities, May 20, 2015
- General Criteria: Methodology: Industry Risk, Nov. 20, 2013
- General Criteria: Group Rating Methodology, Nov. 19, 2013
- Criteria: Use of CreditWatch And Outlooks, Sept. 14, 2009
- Criteria: Methodology And Assumptions: Approach To Evaluating Letter Of Credit-Supported Debt, Feb. 20, 2015
- USPF Criteria: Municipal Applications For Joint Support Criteria, June 25, 2007
- Criteria: Joint Support Criteria Update, April 22, 2009

Related Research

- Glossary: Not-For-Profit Health Care Ratios, Oct. 26, 2011
- U.S. Not-For-Profit Health Care Sector Outlook Revised To Stable From Negative, Though Uncertainties Persist, Sept. 9, 2015

- U.S. Not-For-Profit Health Care System Median Ratios Likely To Remain Stable Through 2016 Despite Industry Pressures, Sept. 1, 2015
- Health Care Providers And Insurers Pursue Value Initiatives Despite Reform Uncertainties, May 9, 2013
- Standard & Poor's Assigns Industry Risk Assessments To 38 Nonfinancial Corporate Industries, Nov. 20, 2013
- Health Care Organizations See Integration And Greater Transparency As Prescriptions For Success, May 19, 2014

Ratings Detail (As Of May 5, 2016)

Illinois Fin Auth, Illinois

Rush Univ Med Ctr Obligated Grp, Illinois

Series 2009 A,B,C & D

Long Term Rating	NR	Current

Many issues are enhanced by bond insurance.