



FINANCIAL UPDATE

Summary

- CKHA is projecting an operating deficit of \$3.0 million on hospital operations for the fiscal year ending March 31, 2017. This means that the cost of operating CKHA this year is \$3.0 million more than the revenue we received. This is the amount that is reported to the ESC LHIN and the Ontario Ministry of Health and Long Term Care. When building depreciation/interest is added, the deficit reported in the hospital's audited financial statements would be \$4.5 million. The following table compares last year's actuals to this year's projection:

	March 31, 2016	Projected to March 31, 2017
Hospital Operations – Ministry reporting	-\$1.0	-\$3.0
Building depreciation/interest	-\$1.3	-\$1.5
Sub Total	-\$2.3	-\$4.5
Imagine Project	-\$1.4	0
Surplus (Deficit) – Consolidated	-\$3.7	-\$4.5

This document focuses on financial performance for hospital operations. This is the number reported to the Ministry of Health and Long Term Care through the Hospital Sector Accountability Agreement. This does not include building depreciation or interest expense. Many hospitals prepare financial plans to achieve breakeven at a consolidated level including building depreciation and interest. The immediate priority is to ensure that CKHA achieves a balanced operating position for hospital operations.

- Due to recurring deficits in 6 of the last 7 years and capital expenditures over the years, CKHA has depleted its cash.
- In order to meet its financial obligations including payroll, CKHA increased its bank line of credit from \$4.0 million to \$8.0 million in 2015 and then again to \$10.0 million in March 2016.

Furthermore, it has been necessary to also obtain a cash advance from the Ministry of Health and Long Term Care.

- Preparation of next year’s financial plan is underway. Based on current information the forecast financial gap in fiscal year 2017/18 is in the range of \$3.0 million to \$5.0 million for hospital operations.
- Given how the funding formula works it is not enough to focus on the next fiscal year but rather to develop a multi-year plan that will put CKHA back on a stable financial footing and reduce the negative year-over-year impact of deficit financing.
- Preparation of the financial plan will be informed by benchmarking prepared by external experts that compare CKHA’s performance against other Ontario Hospitals. This is a key aspect of the process – it demonstrates that other organizations have achieved success under the same funding formula. With a collective effort CKHA can achieve similar outcomes.

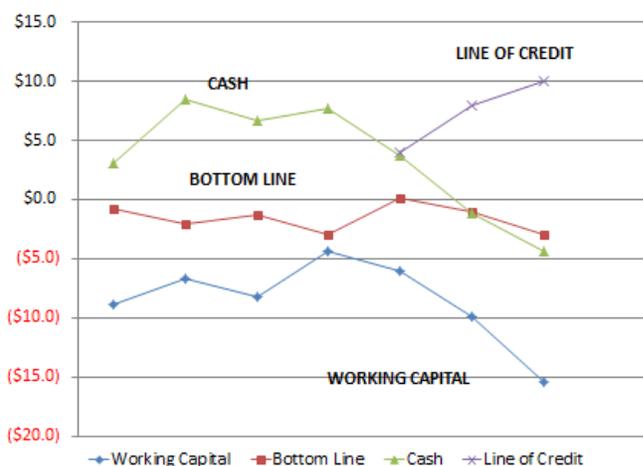
The following pages provide greater detail and a more fulsome explanation of the current situation.

Background

Chatham-Kent Health Alliance is starting to prepare the Fiscal 2017/18 operating and capital budget. In preparing this budget it is important to acknowledge that CKHA is facing a challenging financial situation due to recurring operating deficits over multiple years, negative cash balance, and negative working capital.

An example of the hospital’s serious financial position is the bank line of credit that went from \$4.0 million to \$8.0 million in 2015 to \$10.0 million in March 2016 – in other words, to meet its financial obligations including payroll, CKHA relies on its line of credit. This issue is further magnified given that it was necessary to secure special assistance from the Ministry of Health through a cash advance that will be received in January 2017 because the line of credit would not allow CKHA to meet all of its obligations in the New Year.

The following graph provides CKHA’s performance between F’10/11 and Projected F’16/17:



Bottom Line is the hospital’s financial performance excluding building depreciation and interest expense.

The Bottom Line presented in F’14/15 doesn’t include Post Construction Operating Funding that the Ministry forgave and allowed hospitals to retain.

The line of credit is only shown for F’15/16 and F’16/17.

The Ministry's Health Based Allocation Model (HBAM) cost performance formula indicates that in **F'15/16 CKHA overspent by \$4.0 million**. When compared to the **40th percentile CKHA spent \$5.1 million more than expected** and at the **25th percentile spent \$9.9 million more than expected**.

Comparing CKHA's performance against other hospitals indicates that **CKHA could achieve \$12.3 million in "net" estimated cost improvement opportunities at the 40th percentile** by identifying where efficiencies can be achieved consistent with other hospitals while providing the same level of service to the community.

CKHA's performance under the Provincial Hospital funding formula and its performance compared to other hospitals clearly demonstrate that CKHA has an expense issue given that other Ontario Hospitals are able to deliver service of equal or greater quality at lower cost. Typically hospitals conduct external benchmarking on an annual basis in order to assess relative efficiency and, at the same time, determine how a hospital will perform under the funding formula that rewards efficient hospitals and penalizes inefficient hospitals.

Hospitals are not supposed to operate at a deficit. Having a deficit not only means hospitals are spending more money than they receive and this not only leads to higher debt levels, but under the Provincial funding formula it further reduces future funding levels. In fact, CKHA is **expected to lose funding of \$1.0 million** in the next fiscal year because of the operating deficit in Fiscal 2015/16.

There are three key projects that have been reviewed over the past four months in light of CKHA's financial position that further reflect the need to change the way CKHA manages its financial resources: hospital information system, retail food services, and diagnostic imaging equipment upgrade.

Hospital Information System

Original Plan:

- Partner with the London Hospitals to replace the current McKesson system with the Cerner system used in London and the Thames Valley Hospitals. McKesson had decided that effective March 31, 2018 the system would not be supported by McKesson. The estimated cost of replacing the McKesson system was in the range of \$12 million to \$14 million
- Establish an HIS team to start preparing CKHA for the transition to the Cerner system
- It is important to note that while the organization started to move ahead with this plan, a detailed business case and financial plan for this major investment was never prepared and approved by the Boards

Current Status:

- In September communicated with London that CKHA could not sign a contract by the October date established by London due to CKHA's financial situation and the absence of a financing plan
- Connected with the other hospitals in the region to discuss options

- Reduced the size of the HIS team and shifted focus to support projects relating to plans that support CKHA's transformation under new leadership

Revised Plan:

- Proceed with a third party support option so that CKHA will continue to use the McKesson system after March 31, 2018 and the system will be supported by a third party
- Invest in upgrades to specific software that is considered vulnerable because the current version is outdated, and replace some hardware
- Participate with the other Erie St Clair hospitals in a Request for Proposals that would invite proposals and enable the region to make an informed decision based on competitive bids and value for money
- Based on the results of the RFP develop a detailed business case and implementation plan

Retail Food Services

Original Plan:

- Attract two new retail food service vendors
- Construct an addition to the cafeteria at an estimated cost of \$800 thousand including related renovations
- Close cafeteria service
- Borrow from the bank and use rent and % of sales from retail food service vendors to cover the interest costs and repay the principal

Current Status:

- Attracted one retail food service vendor
- Construction and related renovations now estimated to cost more than \$1.4 million
- Approval to construct an addition as required under the Public Hospitals Act was not obtained from the Ministry of Health and Long Term Care
- Rent and % of sales from single retail food service vendor will not be adequate to cover interest and repay bank loan

Revised Plan:

- Proceed with one retail food service vendor – unused space in the addition will not be completely finished
- Spoke to the Ministry of Health and Long Term Care and declared that CKHA proceeded to build an addition without approval
- Reinstigate cafeteria service on a one-year trial basis in order to determine whether it can operate at a break-even level given the presence of a retail vendor. The cafeteria service is

considering changes to its menu and an increase in some prices. Its success will be determined by sales volume

Diagnostic Imaging

Original Plan:

- Upgrade the suite of diagnostic imaging equipment including the replacement of the current aging CT scanner and ultrasound equipment and the acquisition of SPECT CT
- Approach the Foundation to initiate a fundraising campaign to raise funds

Current Status:

- The DI plan and campaign started without having submitted to the Ministry of Health and Long Term Care the required business case for the replacement of the CT scanner or the acquisition of SPECT CT as per the Ontario *Protocol for the Submission, Review and Approval of CT Designation Requests*
- The fundraising campaign did not plan to cover the total cost of upgrading the suite of diagnostic imaging equipment and did not include estimated renovation costs of \$3.0 million – it is not clear how CKHA planned to finance the total cost of the upgrade as no Board approved business case has been found

Revised Plan:

- Re-scope the DI project (equipment and renovations) within expected available funds from the campaign to date. Priorities are to replace the CT scanner and some ultrasound equipment
- Submitted the required business case for the CT replacement
- Balance of new DI equipment will wait until Foundation fundraising or other funding source is confirmed

Focusing on the Fundamentals

Over the past four months a number of changes have been implemented or are currently underway aimed at strengthening oversight, financial and operational management, and performance. Some changes to date include:

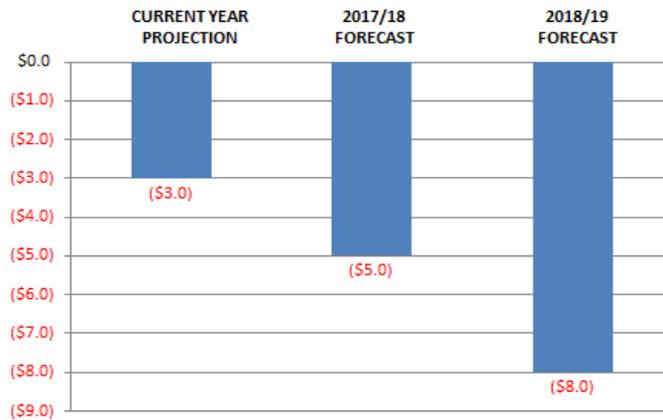
- Introducing improved performance reporting and monitoring;
- Establishing an equipment/facility planning committee;
- Re-introducing program management under which Chiefs/Medical Directors will work with Administrative Directors to provide operational, financial, and strategic oversight to clinical programs and services;
- Engaging the external auditors to review of internal controls in order to ensure the reliability of internal and external reporting, compliance with applicable laws and regulations and internal policies, and safeguard the hospital's resources; etc.

- Strengthen financial reporting, analysis and forecasting at the Finance Committee and Board levels

Through these and other measures CKHA will return to the fundamentals of effective management supported by the appropriate processes, practices and systems.

Moving Forward

Based on current information, the forecast financial gap for fiscal year 2017/18 is \$5.0 million for hospital operations. Our financial planning for Fiscal 2017/18 also needs to consider the longer view and, to the best of our ability, start developing multi-year plans. Based on high level assumptions about revenue and costs, CKHA runs the risk of having significant deficits going forward as illustrated by the following chart.



What differentiates CKHA from other hospitals is the carryforward deficit from the current year (2016/17) and an expected funding reduction due to the deficit in 2015/16.

The financial situation is unsustainable and we need to develop a plan to reduce operating expenses with the goal of achieving a break-even position.

The approach that we are taking is to spend 8 to 10 weeks to figure out what changes can be made to improve operating performance over the next two years.

The question then becomes ‘How will we figure this out’?

- By implementing an organized and systematic process that is expected to start early February and finish the latter part of April, and will be informed by benchmarking results to develop a recovery plan.
 - A Project Management Office will be set up that will provide ongoing support to the recovery plan process by establishing and supporting the work of the Steering Committee; establishing and supporting the four working groups (clinical, diagnostic and therapeutic, administration and support, and management); developing the master work plan and timelines; developing a savings verification methodology, etc.
- By having an organization-wide effort that seeks input from staff and physicians.

- By providing staff, physicians, and the community the opportunity to ask questions about our financial and governance planning through the newly launched website: www.askckha.com.
 - This site will be monitored by Communications and the questions will be acknowledged immediately. Questions will be then directed to the appropriate departments. This site is only for questions regarding our financial and governance plans. Our written communications will also be housed here so the public will have access to them. We welcome comments, questions and ideas to ensure that everyone understands this is a team effort.
- By having meetings throughout all departments to analyze and evaluate strategies and to ensure cross conversations are happening.
 - We acknowledge that a strategy in one department will have an impact on other departments. These conversations will be ongoing to ensure all departments are aware of the strategies being discussed and vetted.
- By bringing in outside expertise to participate in the process, to work with the working groups, and to assist in developing cost improvement plans.

Management is still working out details and these will be communicated in the near future.

In closing we acknowledge that this is a challenging time; however given CKHA's financial situation, action needs to be taken. We ask if you have any cost savings suggestions to please forward these to your direct managers or via www.askckha.com. Our plan will be an organization-wide effort and we will consider all input.