

CONFIDENTIAL

October 14, 2022

The Honorable Morgan McDonald, MD, FACP, FAAP
Interim Commissioner
Tennessee Department of Health
710 James Robertson Parkway
Nashville, TN 37243

Re: Request for a One-Year Extension on the Replacement Capital Plan Submission
Requirement

Dear Commissioner McDonald:

As detailed in our September 19TH letter, not-for-profit health systems throughout the nation have been reporting massive operating losses over the recent reporting periods, further compounded by massive losses on investment reserves due to the volatile market. These losses are having an impact on cash flow, particularly for organizations that must continue to service their debt. From this perspective, Ballad Health is no outlier. The incredibly swift and material impact of inflation, labor shortages, major increases in supply cost and unstable volumes have contributed to financial stress impossible to have been predicted five years ago. These issues make financial forecasting and sustainability planning difficult to do responsibly without recognizing the unpredictability of what lies ahead as these changing conditions are navigated.

Under Section 3.07(b)(ii) of the Tennessee Terms of Certification (“TOC”), Ballad Health is required to submit a replacement capital plan at the end of each three-year period to replace the expiring capital plan. The Tennessee Department of Health (the “Department”) and the Tennessee COPA Monitor do not formally approve the replacement capital plans, but once a capital plan is submitted, there are serious consequences if Ballad Health fails to meet the capital plan it has submitted.

Submitting a realistic and achievable capital plan to the Department is critical for two reasons. First, the consequences of not complying with a submitted capital plan are significant. If, at the end of the three-year period, Ballad Health has spent less than ninety percent (90%) of the

aggregate required spending as set forth in the submitted capital plan, Ballad Health is required to engage a Facilities Consultant to conduct a review of each COPA Hospital where a scheduled Capital Project was not completed in accordance with the Capital Plan (the “Facilities Assessment”). Ballad Health is then required to work with the COPA Monitor to develop and submit to the Department for its approval a new capital plan incorporating the findings from the Facilities Assessment (the “Jointly-Developed Capital Plan”). Thereafter, if Ballad Health does not complete any Capital Project identified in the Jointly-Developed Capital Plan, Ballad Health must deposit the shortfall necessary to cover the cost of such capital expenditure in a separate restricted account until such item is completed. If Ballad Health fails to perform under the Jointly-Developed Capital Plan for an unacceptable period of time, Ballad Health is required to forfeit the lesser of \$2,000,000 or an amount equal to twenty percent (20%) of the amount of the required capital expenditure. The Department may assess additional forfeitures annually if Ballad Health continues in Noncompliance with respect to any Capital Project.

Unfortunately, modifying a capital plan after it has been submitted to the Department is not a simple process. Under Section 3.07(b)(iv), Ballad Health may only request a modification of the existing capital plan in response to material unforeseen circumstances. If the COPA Monitor determines the modification is a material change that necessitates obtaining additional information from an objective third party, Ballad Health is required to engage a Facilities Consultant selected by the COPA Monitor to conduct a Facilities Assessment of the COPA Hospitals affected by the proposed modification. Following the completion of the Facilities Assessment, Ballad Health and the COPA Monitor are required to prepare a Jointly-Developed Capital Plan. If Ballad Health fails to perform under the Jointly-Developed Capital Plan, the same process described above applies. To date, Ballad Health has never been required to engage a Facilities Consultant or prepare a Jointly-Developed Capital Plan, but we know this would be a resource-intensive, time-consuming, and expensive process if this requirement was ever triggered. For these reasons, we believe it is critical that Ballad Health submit a replacement capital plan that is both realistic and achievable for the covered three-year period.

The Ballad Health Board of Directors met on August 30th to discuss the financial state of the organization and the steps that would be necessary to navigate this challenging economic environment. Ballad Health management presented a one-year operating budget and a one-year capital budget to the Ballad Health Board of Directors which was unanimously approved. Given the uncertainty facing our organization, however, the Board of Directors and the Ballad Health management team determined that it would be nearly impossible to prepare a three-year capital budget without a significant degree of speculation, and which would require extensive modification as economic conditions evolve. It would also significantly increase the chances that Ballad Health would trigger the costly requirement to engage a Facilities Consultant and enter into a Jointly-Developed Capital Plan.

Section 8.02 of the TOC permits Ballad Health to notify the Tennessee Department of Health of material unforeseen circumstances and request modifications to the TOC that may be

necessary to address those unforeseen circumstances. We are writing to notify you that the material unforeseen economic circumstances we are experiencing have impacted our ability to prepare a three-year capital plan in 2022 as required under TOC Section 3.07(b)(ii).

In order to allow Ballad Health time to assess the impact of these unprecedented financial challenges and develop a realistic capital plan for the next three years, Ballad Health is requesting a one-year extension on the replacement capital plan submission requirement.

The next twelve months will be critical to understanding whether the rise in inflation, supply costs, and labor costs that we are currently experiencing are short-term challenges or long-term challenges. It will also give our management team time to determine if the many cost-saving measures and revenue improvement efforts we are pursuing are having the desired impact. In place of a three-year capital plan, Ballad Health proposes to submit to the Department the Board-approved one-year capital budget for fiscal year 2023. If economic conditions stabilize over the coming months, Ballad Health's intention would be to provide the three-year replacement capital plan by September 30, 2023. If, however, economic conditions do not stabilize by August of 2023, Ballad Health would notify the Department so that the parties may discuss an additional extension of this requirement.

We greatly appreciate your consideration of this request. The additional time we are requesting will allow our organization to submit a more accurate and realistic replacement capital plan for the next three-year period in furtherance of the goals of the COPA. If we can provide additional insight to assist with your review of this matter, please let us know.

Sincerely,



Alan Levine
Chairman and Chief Executive Officer
Ballad Health

cc: The Honorable Colin M. Greene, MD, MPH
Virginia State Health Commissioner

Jonathan Skrmetti
Tennessee Attorney General and Reporter

Janet M. Kleinfelter
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