Fiscal 2019-2020 Budget Presentation
Residents' Council Meeting
May 20, 2019

Good afternoon. I am Tracy Biesecker, and I am the Chief Financial Officer for Messiah Lifeways. Today I am going to share with you an overview of Messiah Lifeways and the related entities, information on what operating expenses are for Messiah Village, a report on the current year status of finances for Messiah Village, and then present on the next fiscal year budget and plans.

Slide 2: Messiah Lifeways and related entities consist of four separate operating entities:

> Messiah Lifeways, which is a non-profit holding company, and is the parent entity of the other three entities. Messiah Lifeways is often referred to by the acronym ML.
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> Messiah Home, which is doing business as Messiah Lifeways at Messiah Village, is this non-profit continuing care retirement community in Mechanicsburg. Messiah Home is often referred to by the acronym MV.
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> Messiah Lifeways Community Support Service is the non-profit company that provides services to older adults throughout Cumberland and other counties. This entity is often referred to by the acronym CSS.
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> Messiah Family Services, which is doing business as Messiah Lifeways at Mount Joy Country Homes, is a non-profit continuing care retirement community located in Mount Joy, Lancaster County. This entity is often referred to by the acronym MJCH.

Slide 3: Each of the four entities has a business purpose that supports the overall mission, which is "to responsibly enhance the lives of older adults with Christ-like love." ML is the entity that provides shared support services to each of the other three entities. These shared support services include Human Resources, Fiscal Services, Information Technology, Marketing, Compliance, and Donor Development. It also includes the Executive Team. The revenue for ML comes from a management fee that is charged to each of the three entities. The management fee is an allocation of the ML budgeted expenses for the year and is allocated based on the percentage of net revenues.

MV provides Nursing, Enhanced Living (Personal Care), and Housing as well as other related services such as Campus Support Services (Grounds, Maintenance, Dining, etc.), Enrichment Services (which includes Pastoral Care), and Wellness.

CSS provides in-home support services such as companion services, care assistants, drivers, and housekeepers along with two Adult Day centers and a senior center located in Mechanicsburg.

MJCH provides housing to those 55 and better at the Mount Joy campus.

Slide 4: Within MV, there are several areas of operating expenses. Many of the residents are directly impacted by the program expenses based on the area in which they live, as these include those team members, supplies, food, and related care costs. Another area of operating expense that is fairly visible but often not thought of is the building operations. These include utility expenses, service contracts for major equipment such as HVAC and elevators, repairs to buildings and streets, and the cost of various inspections required by regulations. Within operating expenses there are various fees that MV must cover, one of which is the management fee that was discussed on the previous slide. There are also software fees included within operations. Within Administrative expenses are the Nursing Home Assessment Fees (also known several years ago as the granny tax). We do get an offsetting payment from the state which is included in revenue, and as of now we are a "winner" where our receipt is slightly larger than the payment out for the tax.

Slide 5: The last four categories are required operating expenses, but are not always as visible as they are not as tangible. Insurance expense covers the costs of insurance premiums, some of which are required by law such as auto coverage, and others that have become a risk management tool such as cyber insurance. Although MV is a non-profit, it is not fully exempt from paying real estate taxes and must pay them on both the residential living areas as well as a negotiated payment for the nursing and personal care areas. The latter is known as a PILOT (payment in lieu of taxes) agreement, and allows MV to make a payment for real estate taxes at a rate less than the fully assessed value. Interest expense is a result of MV's various debt holdings. Much like a mortgage or car loan, this debt with bond holders and the bank carries an interest rate as the cost of borrowing the funds. Depreciation expense is the cost of our assets that were purchased in the current or prior year, but had a useful life of more than one year. The effect of depreciation expense is the transfer of a portion of the asset's cost from the balance sheet to the income statement during each year of that asset's useful life.

Slide 6: I have found throughout my career that depreciation expense is one of the most misunderstood expenses, as it does not match the cash accounting that we use in our personal lives. This slide illustrates how depreciation expense works when it comes to a business like MV that uses the accrual method of accounting.

Slide 7: <Note that "K" stands for thousand in the following numbers.> The Statement of Operations is the name of the income statement for a non-profit. This slide represents the nine months of activity for MV, which is the time period July 1 through March 31, as compared to the budget for that same time period.

Within Net Resident Services Revenues, the actual results are approximating budget with a variance of $158K or 0.5%. This is the very high level reporting of all the revenue from each of the levels of living, and if we drill down to each area the following variances were noted:

- Net revenues from physical, occupational, and speech therapy was $363K above expectations for the time period. The relatively new therapy company, AdvantageCare, has increased our utilization of therapy through better screening of needs for residents.
- Nursing services were $114K above budget for the nine months. The revenue from the nursing home assessment was $178K higher than budgeted for the time period, due to timing and rates paid by the state as compared to budget. The occupancy within nursing has been quite a bit below budget, which will be shown in a later slide, which has caused daily fees revenue to be below budgeted expectations.

- Enhanced Living revenue is $300K below budgeted expectations, a result of the Hopewell neighborhood being below occupancy expectations for the time period.

Other revenue was $86K or 11% above budget. The revenue from dining is within this area, and specifically catering and Village Square revenue beyond meal plans has been $57K higher than budgeted. Contributions without a restriction also are recorded in this area, and were $28K higher than planned for.

Other expense side, Fees, Purchased Services, and Supplies are trending over budget, and were $404K or 3.4% above what was planned for in the nine months. The main variables in this line were the costs of therapy (a correlation of the revenue above) which were $141K above budget, and the costs within dining which were $263K above budget. These include both the raw food costs and the labor.

Within the Administrative line, as shared previously, is the Nursing Home Assessment tax. This was $155K higher than budgeted for the same time period.

Building Operations and Maintenance was $121K or 6.7% below budget, a result of both the timing of maintenance repairs and grounds expenses, as well as the cost of software fees for electronic health records being lower than expected.

The net operating loss for MV for the nine months ended March 31, 2019 is $2.31 million as compared to a budgeted $2.26 million loss. Thus, the actual net operating loss was anticipated for the year.

Slide 8: The overall budget process is something that lasts quite a few months. The managers responsible for budgets start work as early as January for the next fiscal year. There is a Budget Committee consisting of the CFO, Director of Financial Operations, the Senior Accountant and Staff Accountant that meets with each budget manager and respective Executive Team member. After a few rounds of back and forth with budgets, the Executive Team reviews the final draft. This final draft is then reviewed and approved by the Finance Committee of the Board of Directors, who then in turn review and approve the overall budget. This year that was completed on April 23, 2019.

Slide 9: There are many factors within the budget that must be considered and planned for. We start with the current financial performance to get trends and understand what is impacting the financials. We also plan for strategic initiatives such as growth or technology. We are faced with changing payment systems from Medicare and Medical Assistance, which most often are declines in expected payments. Inflation is a large factor within supplies and food costs. There is a market study done to evaluate our rates for the levels of living to make sure we are not out of alignment with our peer competitors. And finally, we have to factor in the workforce challenges we face including recruitment of team members in a competitive market.

Slide 10: Looking at MV's Operating Budget for Fiscal Year 2020, this slide represents the Operating Expenses for 2020 as compared to the budget for 2019. The shift in Salaries, Wages, and Benefits is a combination of factors. First, there were positions shifted from Messiah Lifeways to MV, as those positions directly impact the operations of MV and not CSS or MJCH. There were also positions added for the opening of Village Square that had not been accounted for previously. These are within the housekeeping area. And there is both an annual increase within salaries and wages for team members as well as positions that have been adjusted due to the market pressures mentioned before.

Fees, Purchased Services and Supplies is increasing due to the increase in the projected therapy costs (with corresponding increases in budgeted revenue), the shift of software fees from building operations, as well as inflationary increases.

Administrative expenses are increasing due to the shift of the electronic health software costs from Building Operations to this line.

Building Operations and Maintenance is lower than the prior year budget as the shift of software fees occurred, offset by inflationary costs within supplies and service contracts.

Slide 11: One of the largest expenses of a service industry like ours is the cost of providing that service through team members. While we do contract out some of that service, from a comparison to other organizations those costs are still included as staffing costs. As we compare the total cost of MV direct team members, campus dining labor, and therapy labor to our total operating expenses, it represents almost half of the cost of operations. This is does not include the cost of services provided by Messiah Lifeways, which would drive that percentage higher. We operate on a pretty thin margin in other expense areas, and believe that this cost of staffing is necessary to provide the high quality of service that we do at MV.

Slide 12: This slide represents the revenue side of the operating budget. There are three major categories of revenue: Net Resident Services Revenue, Other Revenue, and Net Assets Released from Restriction. Net Resident Services Revenue is increasing due to the following:

- Nursing Services is increasing $960K or 4.6% despite a 1% decreased budget occupancy. The increase is mainly due to a payer mix shift, as we plan for more private pay residents and less insurance residents including Medical Assistance. Although rates are going up, the net effect of a 3.5% increase is a 1.8% revenue increase due to adjustments for insurance and Medical Assistance.
- Enhanced Living is increasing $688K or 5.4% although occupancy is budgeted relatively flat between years. The increase is based on a projected higher level of care within the program, which are at higher rates, along with a rate increase.
- Residential Living is increasing $137K or 1.3%. Occupancy is also relatively flat comparatively, and while rates are increasing 3.5%, the budgeted rate in the prior year was unrealistically much higher than the budgeted rate in the current year.

- Net revenue from physical, occupational, and speech therapy is projected to increase $572K, based on the trend previously mentioned.

Other revenues are increasing within the budget based on an increase for contributions/donations, along with increased dining revenue beyond the meal plans.

Net Assets Released from Restriction represents the release from the Endowment fund to support benevolent care, and will be discussed later in the presentation.

Slide 14: The budgeted occupancy assumptions by living area are presented, along with the current actual as of the month of April 2019.

Slide 15: The rate increases are presented, noting that the average increase this year is 3.5%.

Slide 16: Pulling the Statement of Operations together, the fiscal year 2020 budgeted net operating loss for MV is $1.9 million. This is better than the fiscal year 2019 budgeting net operating loss, which was $2.9 million. When Project Envision was modeled out in 2015, we anticipated that fiscal year 2020 would have a $1.7 million dollar loss, and eventually break even in 2023. Therefore, this loss was planned for and is expected to turn around in future years.

Slide 17: Circling back to the consolidation of all four ML entities, the total Net Operating Loss is $1.98 million, which is $1.13 million better than the prior year. Again, this was forecasted, and we will continue to stabilize over the upcoming years. There are non-cash expenses, such as the depreciation expense example, that are impacting the net operating loss, and we are still meeting and exceeding debt covenants. Cash flow is still positive.

Slide 18: Along with the operations budget, we budget for a Capital Budget, which represents those assets we are paying cash for now but have the future life that the cost will be depreciated over. The largest capital expenditure is the expected turnover cost, which is the cost to renovate and prepare a cottage or apartment for the next occupant.

Slide 19 to 21: These slides represent the Benevolent Care and Medicaid costs within our Nursing and Enhanced Living programs. For the nine months ended March 31, MV provided $2.8 million of benevolent care in these two service areas. That represents 10% of the gross revenue that wasn't collected. Benevolent Care is for those who have truly outlived their resources and continue to need the services of MV. In the fiscal 2020 budget, $1.2 million is being shown as "Released from Restriction" to represent the transfer of funds from the Benevolent Care fund to offset uncompensated care.

Questions from the audience:

Question: As part of the cost of salaries, wages, and fringe benefits, has the impact of the proposed change in the minimum wage law been considered?

Answer: Within the fiscal year 2020 budget, there is no specific expense or estimate for the proposed changes. We have discussed the potential impact as an Executive Team. There are certain tiers of employees that would be under the proposed minimum wage, as well as the impact of wage compression. The only way to pay for any change would be to reduce costs or raise rates.

Question: Has the impact of competition been considered for the rates along with the occupancy challenges?

Answer: As part of our budget process, we do evaluate local competitor rates along with other peer communities. The analysis has shown we are at about the middle if not the lower side of the market rates. As far as occupancy, there has been an increase in competition; however, we also are seeing industry wide the impact of a decreased length of stay driven by payment programs. We also see people going home directly from hospitals that in prior years would have gone to short term rehab first.

Question: Were contributions only $28K? It seems like they have been higher this year.

Answer: For clarification, the contributions in the current fiscal year have been $28K higher than budgeted in the unrestricted/Other Revenue line. <The year to date 3/31/19 contributions was $47K.> There have been other contributions received this year that were specifically designated or restricted for a purpose, those are included elsewhere in the financial statements and not deemed part of operating income until the restriction is satisfied.

Question: There was a policy that allowed for 6% of the endowment fund to be used. Is that still in effect?

Answer: The policy is actually both an internal investment policy and a state law that allows for a range of 4-7% to be released. Fiscal year budget 2019 has 6% released, and fiscal year budget 2020 has a release of 7%.