THE UNIVERSITY OF MICHIGAN
REGENTS COMMUNICATION

ACTION REQUEST

Subject: Proposed FY 2013 University of Michigan Hospitals and Health Centers (UMHHC) Operating Budget

Action
Requested: Approval

Background:

UMHHC has completed its annual operating budget process for FY 2013. The activity, revenue and expense projections result in a 0.5% operating margin of $10.8M.

The FY13 Plan is predicated on several key assumptions: (a) significant patient discharge growth associated with capacity activation; (b) improvements to labor efficiency / staff productivity and supply expense per case; (c) Medicare / Medicaid revenue reductions due to sequestration and decreased pool reimbursements; (d) inflationary rate increases; (e) $27M incremental fixed depreciation expense burden associated with strategic investments for the Mott Children’s and Von Voigtlander Women’s Hospitals as well as MiChart.

Consistent with the prior year, UMHHC leadership is developing a broader (36 month) Operating Plan for the FY13-FY15 period. The Operating Plan goal is to return UMHHC to sustained profitability levels necessary to support plans for future strategic and routine capital investments. Leadership has presented expectations to the Operating Units, with goals to positively impact the projected FY13 performance.

We recommend the Regents approve the proposed FY 2013 University of Michigan Hospitals and Health Centers' Operating Budget.

Respectfully submitted,

Timothy P. Stoltz
Executive Vice President and
Chief Financial Officer

Ora Hirsch Pescovitz, M.D.
Executive Vice President for Medical Affairs

June 21, 2012
University of Michigan Hospitals and Health Centers
Operating Budget Assumptions
FY 2012 Forecast to FY 2013 Budget

Activity
• 3.5% growth in discharges
• 13.5% growth in observation cases
• 87.7% occupancy rate, up from 87.4% in FY2012
• 4.0% growth in clinic visits
• 5.3% adjusted case growth

Revenue
• Small decrease in Medicare payment per adjusted case, inflation is offset by federal budgetary reductions
• No change in Medicaid rates expected, other than annualizing FY2012 mid-year changes
• Blue Cross and commercial increase per contracts
• Continued but moderate shift towards government payers
• Risk of additional payment reductions from government payers as state and federal FY2013 budgets unfold
• Revenue Cycle initiatives to improve overall revenue per claim

Expenses
• Maintain competitive salaries
• -2.5% FTE Efficiency / Productivity improvement
• Supply cost per case increase of 2% (commodity inflation and utilization), with gross $33M increase in Supply Costs (volume + inflation)

Margin Target
• 0.5% Operating Margin target
Operating Revenue
Forecast FY 2012 $2,240 M
- Increase in patient activity 116 M
- Changes in payer mix (7) M
- Change in reimbursement rates 41 M

Operating Revenue Budget FY 2013 $2,390 M 6.7%

Total Expense
Forecast FY 2012 $2,252 M
- Payroll 72 M
- Supplies 33 M
- Depreciation 15 M
- Other Expenses 7 M

Total Expense Budget FY 2013 $2,379 M 5.7%
<table>
<thead>
<tr>
<th>Operating Revenue</th>
<th>FY13 Forecast</th>
<th>FY12 Forecast</th>
<th>Y2Y %</th>
<th>FY11 Actual</th>
<th>Y2Y %</th>
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<tbody>
<tr>
<td>Operating Expenses</td>
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<td>Payroll</td>
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