Fair Rental Value System (FRVS) Fundamentals

- Price for use of space irrespective of actual accounting cost
  - Economic value vs. financial accounting value
- Price = Facility value which increases over time based on replacement cost and proper upkeep times a rental rate
- Value based upon professional standards
  - Professional market appraisal
  - Proxy appraisal – Simulated appraisal value using commercial valuation systems such as Marshall Swift/Boeckh or RS Means
Why FRVS? part 1

A well designed fair rental value system will:

- Differentiate reimbursement based upon age/condition
- Provide incentives to generate capital resources for renovation, improvement and replacement
- Encourage investment in physical plant upgrades and renovations
- Impact the physical environment that can result in improvement of resident quality of life
- Simplify administration and allow the State to exert reasonable budget predictability and control
Why FRVS? part 2

- Distinguishes economic value over financial accounting value
- Eliminates concerns for system gaming:
  - DEFRA and COBRA
  - Capital lease issues
  - Related party transactions
- Promotes equity investment
<table>
<thead>
<tr>
<th>States Reimbursed by FRVS</th>
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<tbody>
<tr>
<td>Alabama</td>
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<tr>
<td>Arkansas</td>
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<tr>
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<tr>
<td>Wisconsin</td>
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<td>Virginia</td>
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</table>
Proxy Appraisal = Creation of an appraisal model simulation using standardized values and depreciation factors consistent with commercial valuation systems

- Facility base value established using a standard or actual facility square footage (per bed) and construction cost (RS Means or other)
- Adjusted to include land value and equipment, and sometimes soft costs
- Further adjusted for age and condition using depreciation factor
- Periodically rebased for improvements and replacement cost inflation
Assumptions

- 100 bed facility
- RS Means new bed value of $60,000
- Land value at 10%
- Equipment value at $5,000/bed
- 25 years old
- Depreciation rate of 1.5%/year
- Rental rate of 9.0%
- 33,000 annual patient days
### Gross Fair Rental Example

**New Bed Value**  
$6,000,000

**Equipment**  
$500,000

**Subtotal**  
$6,500,000

**Depreciation**  
0.375  
\[
\begin{align*}
\text{Depreciation} &\quad 0.375 \\
\text{Subtotal} &\quad (2,437,500) \\
\end{align*}
\]

**Subtotal**  
$4,062,500

**Land**  
$600,000

**Rental Value**  
$4,662,500

**Rental Rate**  
9%

**Fair Rental**  
$419,625

**Patient Days**  
33,000

**Fair Rental Rate**  
$12.72
Proposed System Parameters
part 1

- Cost per Square Foot (RS Means) $141.25
- Location Multipliers .76 to .89
- Minimum Square Feet per Bed 350
- Maximum Square Feet per Bed 700
- Land Percentage 15%
- Equipment Allowance per Bed $5,000
- Maximum Age 32.5
- Rental Rate 9.00%
Proposed System Parameters
part 2

- Minimum occupancy: 85%
- Depreciation:
  - Age is $\geq 32.5$: 2.00%
  - Age is $\geq 25$ and $< 32.5$: 1.75%
  - Age is $\geq 17$ and $< 25$: 1.50%
  - Age is $\geq 10$ and $< 17$: 1.25%
  - Age is $< 10$: 1.00%
Georgia Facility Specifics

- Average facility square footage
  330

- Number of facilities less than 350
  208

- Number of facilities greater than 700
  6
Georgia System Values

- Current facility average property rate: $5.31
- FRVS facility average rate: $9.43
- Average rate increase: $4.12
- Cost of FRVS: $38M
- Number of facilities whose rate would decrease: 4
- Plan is to have a hold harmless provision
## Proposed Rate Increase Ranges

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<th>Range</th>
<th>Count</th>
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<tr>
<td>$2.01 to $4.00</td>
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<tr>
<td>$4.01 to $6.00</td>
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<td>$6.01 to $8.00</td>
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<tr>
<td>$8.01 to $10.00</td>
<td>21</td>
</tr>
<tr>
<td>Greater than $10.00</td>
<td>11</td>
</tr>
</tbody>
</table>