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Scope and Limitations

This methodology describes DBRS's approach for rating Canadian public hospitals. The methods described herein may not be applicable in all cases. The considerations outlined in DBRS methodologies are not exhaustive, and the relative importance of any specific consideration can vary by issuer. In certain cases, a major strength can compensate for a weakness, and conversely, a single weakness can override major strengths of the issuer in other areas. Further, this methodology is meant to provide guidance regarding the DBRS methods used in the sector and should not be interpreted with formulaic inflexibility, but understood in the context of the dynamic environment in which it is intended to be applied.

Canadian Public Hospitals

- In Canada, public hospitals are under provincial jurisdiction; DBRS recognizes that health care is a priority of the Canadian population and governments, accounting for 45% to 50% of provincial program spending.
- Hospitals are consolidated within the public accounts of provincial governments.
- There is a high level of monitoring and oversight by provincial governments in Canada over their respective health systems and the hospital sector, with reasonable policies and procedures in place to guide institutions in their management and to prevent major financial issues.
- There is effectively no competition in the sector, and the government acts as the single payer, typically providing more than 90% of hospital operating revenue.
- A provincial government's strong oversight and control over the hospital sector may lead to significant reputational risks to the province and broader public sector entities in the event of a default of a hospital or health network issuer. This could include, but is not limited to, the ability of other broader public sector entities to access capital markets in a timely and cost effective manner to meet their own borrowing needs.

Given these strong institutional and financial ties to provincial governments, DBRS views hospital and health network issuers as being closely linked to the credit profile of their respective provincial governments. As such, the provincial government rating acts as a ceiling on the ratings of hospitals and health networks; under no circumstance can a hospital or health network issuer rating exceed that of its respective provincial government funder.
Essentiality to the Provincial Health-Care System

The primary credit risk factor for DBRS in determining a hospital or health network issuer rating is the institution’s essentiality to the provincial health-care system. A higher level of essentiality of an individual hospital or health network to the provincial health-care system is expected by DBRS to result in a greater likelihood of implicit financial support from the provincial government funder as a result of institutional, fiscal and reputational linkages, despite the distinct legal status of hospitals or health networks. This factor evaluates the strategic position of a hospital or health network within the provincial health-care system and includes consideration of the institution’s profile, geographic location and service area, clinical expertise, and the systemic implications of a disruption in health services.

- Per the following table, those institutions deemed to be highly essential to the broader health-care system will generally be rated in line with the provincial government funder, reflecting the greatest likelihood of implicit support and strongest linkage to the credit profile of the provincial government funder.
- Those institutions deemed to be moderately essential to the broader health-care system will generally be rated one notch below that of the provincial government funder.
- While they are unlikely to access debt capital markets, those institutions considered to be less essential to the broader health-care system will generally be rated more than one notch below the provincial government funder.

<table>
<thead>
<tr>
<th>Hospital/health network profile</th>
<th>Rating in line with provincial government funder</th>
<th>Rating within one notch of provincial government funder</th>
<th>Rating more than one notch below provincial government funder</th>
</tr>
</thead>
<tbody>
<tr>
<td>Highly essential</td>
<td>• Hospital or health network is considered to be a flagship institution with a strong brand and reputation, occupying a highly strategic position within the provincial health-care system.</td>
<td>• Hospital or health network is considered to be an important institution to the provincial health-care system because of its size or role as a regional teaching hospital.</td>
<td>• Hospital or health network is considered less essential to be the provincial health-care system.</td>
</tr>
<tr>
<td>Moderately essential</td>
<td>• Hospital or health network is typically located in a larger urban centre, providing highly specialized/tertiary care to a large geographic area of the province or to a relatively high share of the provincial population.</td>
<td>• Hospital or health network is typically located in a secondary urban centre, or it serves as a primary hospital for a reasonably large geographic area but smaller relative share of the provincial population.</td>
<td>• Hospital or health network is typically located in a smaller population centre or geographically isolated community.</td>
</tr>
<tr>
<td>Less essential</td>
<td>• Hospital or health network provides local community care but does not have specialized clinical expertise or mandates.</td>
<td>• The hospital or health network has some specialized clinical expertise or mandates within a region.</td>
<td>• The hospital or health network would be considered detrimental to a smaller subset of the population within a single community.</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Geographic location and service area</th>
<th>Rating in line with provincial government funder</th>
<th>Rating within one notch of provincial government funder</th>
<th>Rating more than one notch below provincial government funder</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>• Hospital or health network is typically located in a larger urban centre, providing highly specialized/tertiary care to a large geographic area of the province or to a relatively high share of the provincial population.</td>
<td>• Hospital or health network is typically located in a secondary urban centre, or it serves as a primary hospital for a reasonably large geographic area but smaller relative share of the provincial population.</td>
<td>• Hospital or health network is typically located in a smaller population centre or geographically isolated community.</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Clinical expertise</th>
<th>Rating in line with provincial government funder</th>
<th>Rating within one notch of provincial government funder</th>
<th>Rating more than one notch below provincial government funder</th>
</tr>
</thead>
<tbody>
<tr>
<td>The hospital or health network has highly specialized expertise and mandates in numerous clinical areas, along with significant medical research capacity as a leading teaching hospital, or has the highest level of clinical service available in a given province.</td>
<td>• The hospital or health network has some specialized clinical expertise or mandates within a region.</td>
<td>• The hospital or health network provides local community care but does not have specialized clinical expertise or mandates.</td>
<td></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Implication of disruption in health services</th>
<th>Rating in line with provincial government funder</th>
<th>Rating within one notch of provincial government funder</th>
<th>Rating more than one notch below provincial government funder</th>
</tr>
</thead>
<tbody>
<tr>
<td>The disruption of health services at a flagship hospital or health network would be considered highly detrimental to a significant share of the population and/or for numerous clinical mandates.</td>
<td>• The disruption of health services at this hospital or health network would be considered detrimental to a significant share of the population within a given region and/or for some clinical mandates.</td>
<td>• The disruption of health services at this hospital or health network would be considered detrimental to a smaller subset of the population within a single community.</td>
<td></td>
</tr>
</tbody>
</table>
Additional Rating Factors

The additional rating factors discussed below may be very important for certain issuers, depending upon their activities, but they do not necessarily apply to all issuers in the sector.

If a hospital or health network exhibits a material deficiency or weakness in one or more of the following additional rating factors, DBRS may assign a lower rating to a hospital or health network issuer lower than that suggested by its essentiality to the health-care system. These additional rating factors should not be considered exhaustive, and depending on the issuer, other factors may be considered.

**Debt Burden**
- DBRS considers the level of debt, debt structure (i.e., short term versus long term) and servicing arrangements (i.e., provincially supported versus hospital-supported debt) of a hospital or health network, as well as the outlook for borrowing based on current capital plans and operating budgets.
- DBRS expects that a hospital or health network’s debt burden will not consume an unduly high or overly burdensome share of operating revenues, and that debt growth will not evolve rapidly and outside of budget projections over time.
- If an institution’s debt burden is considered to be overly burdensome, with rapidly rising debt levels or debt servicing that is consuming a growing share of revenues with no credible plan to reduce reliance on external financing, additional notching from the rating of the provincial government funder is likely.

**Operating Performance**
- The operating performance of a hospital or health network is considered as an important indicator of emerging issues that may contribute to a rising debt burden or potentially government intervention. DBRS generally expects that institutions will be in a balanced position, on average, over the medium term. DBRS expects that structural deficits will be addressed by management with internal budget measures or additional government support.
- If deficits persist for a prolonged period without an adequate management response, this may result in additional notching from the rating of the provincial government funder.

**Financial Resources and Liquidity**
- The presence of significant financial resources at a hospital or health network in the form of internal liquidity, access to credit facilities and the financial support of affiliated foundations helps to mitigate against the risk of potential shocks, including unforeseen changes in the operating environment (e.g., government funding reductions). DBRS expects that a hospital will have sufficient internal liquidity and access to credit to meet its current obligations in a timely manner.
- The ratings of hospitals or health networks with very limited or rapidly deteriorating internal financial resources, with no external resources in the form of affiliated foundation support, may be subject to additional notching from the rating of the provincial government funder.

**Management and Governance**
- An adequate level of management sophistication and professional board oversight of management activities at hospitals or with health network issuers is expected to avoid and mitigate the emergence of operational, financial and enterprise risks.
- DBRS evaluates hospital or health network issuers using the DBRS Criteria: Evaluating Corporate Governance. Deficiencies in a hospital or health network’s management and governance framework may result in additional notching from the rating of the provincial government funder. In some cases, material issues in corporate governance could even prevent DBRS from being able to rate the issuer.
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