Harris County Hospital District, TX

Issuer: Harris County Hospital District, TX (Harris County, Texas)		
Assigned	**Rating**	**Outlook**
Limited Tax Bonds, Series 2025	AA+	Stable

Methodology

General Property Tax/Assessment Revenue Methodology
U.S. Not-For-Profit Healthcare Rating Methodology
ESG Global Rating Methodology

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Rating Summary: The long-term rating reflects Harris County Hospital District's ("District's" or "Harris Health's") strong and growing ad valorem tax base, large and diversifying underlying economy, and solid bond security features. While KBRA's analysis recognizes the District's mandate to provide essential healthcare services to the County's indigent population and considers its financial operations - including the significant reliance on federal healthcare payments - it is the District's sizable and growing tax base, and the strong limited tax pledge, with ample capacity to raise the ad valorem tax rate, that primarily supports the rating.

Counterbalancing the aforementioned strengths is the District's complex, multi-year capital improvement plan (CIP), which may pressure operating expenses, debt requirements and the tax levy; and the potential operational challenges that significant federal funding cuts to Medicaid would present. Nonetheless, KBRA expects the District's seasoned leadership team to effectively navigate these credit risks at the current rating level.

Proceeds of Series 2025 limited tax bonds (the "Bonds") will fund a portion of the District's nearly $3 billion capital plan to expand, renovate, and replace aging healthcare facilities through 2035. As of February 28, 2025, the District has $59.3 million in parity limited tax bonds outstanding.

The Bonds constitute direct obligations of the District, payable from the levy and collection of an ad valorem tax on all taxable property within the District, which is coterminous with the tax base of the County. The strength of the ad valorem tax pledge is underpinned by the following: (1) Bonds which are secured by voter-approved ad valorem tax assessed on all taxable property within the District; (2) under the Texas Constitution and state law, hospital districts are the only type of local health care providers in Texas that may impose taxes if approved by voters; and (3) a portion of the ad valorem tax (Interest and Sinking or "I&S" tax rate) is designated for the payment of debt service on the Bonds and may not be used for any other purpose.

Article IX, Section 4, of the Texas Constitution as applicable limits the maximum ad valorem tax rate to $0.7500 per $100 of assessed valuation for all purposes. For FY 2025, which began Oct. 1, 2024, the District levied a total rate of $0.1635, with $0.1621 dedicated to operation and maintenance ("M&O" tax rate) and $0.0014 designated for debt service (I&S tax rate). While the total tax rate is limited, there is ample headroom to increase the tax rate to meet the debt requirements on the Bonds. The District also has $197.1 million in outstanding revenue bonds. The revenue bonds are separately secured by a lien on the gross revenues of the District from all sources, other than ad valorem taxes.

The District, established in 1965, is a political subdivision of the State of Texas (the "State"). The County service area has exhibited strong population growth and solid economic indicators, as the County includes the City of Houston, which is the County Seat and the largest city in Texas. Over the last decade, the County population has grown (CAGR 1.1%) at nearly twice the rate of the nation (0.6%), but slightly below that of the State (1.4%)[1]. Income levels are comparable to the State, but the County poverty level (16%), which has trended lower in recent years, remains above the State level (13.7%)[1]. The County's sizeable and growing population and considerable tax base have contributed to a significant rise in property tax values since 2019. The County's total assessed value (TAV) has increased by a CAGR of 6% in the past decade, providing strong revenue support for the District's operations and debt service payments. The District relies on ad valorem property tax revenues (M&O tax levy) to subsidize approximately one-third of operating expenditures, supporting stable financial performance. The County's assessment base is substantial ($608 billion for FY 2025) and lacks concentration in any one taxpayer, with the top ten accounting for a modest 3.7% of TAV for FY 2024. The District's healthcare system includes two acute care hospitals, the Lyndon B. Johnson Hospital (LBJ) with 215 licensed beds, and the Ben Taub Hospital with 402 beds. Ben Taub Hospital is a Level I trauma center for adults, one of only two in the City of

[1] Based upon US Census Bureau data for 2023.

Houston. Harris Health further operates 16 primary care health centers, seven homeless shelter healthcare facilities, an urgent care and other clinics, dental center, and mobile immunization and medial outreach programs. Community support has remained strong for Harris Health, as recently demonstrated by the November 2023 voter-approval of a $2.5 billion bond authorization to fund the District's large capital plan with limited tax bonds.

The Bonds are the first of three planned issuances (aggregate of $2.5 billion) to fund the District's 10-year capital plan of nearly $3 billion. The large capital program is primarily designed to meet growth and upgrade aging facilities. Key capital projects include the construction of a replacement hospital for LBJ with a Level I trauma center, and renovation and expansion of the Ben Taub Hospital Campus, and improvements to numerous health centers and clinics.

As a safety net hospital, Harris Health's payor mix is heavily Medicaid and Medicare funded (at 73% of total cash collections for net patient services for FY 2024, inclusive of charity care). However, KBRA's analysis incorporates the District's strong and growing tax assessment base, and the ample taxing capacity under the $.7500 ad valorem tax rate cap. The current I&S tax rate of $.0014 is projected by the District to peak at $.0240 in fiscal 2030, incorporating the $839.6 million issuance of the Series 2025 Bonds, plus another $830 million in parity limited tax bonds issued in 2026 and again in 2027. Given the County's strong growth in TAV over the past decade along with projected more moderate growth going forward, the M&O tax rate is anticipated to remain relatively flat through 2034. Consequently, the total tax rate, which incorporates the projected M&O and I&S tax rates, should remain well below the taxable limit of $.7500, peaking at roughly $.1875 in 2030, and representing approximately 25% of the total tax limit – maintaining ample flexibility and headroom to increase the I&S tax levy if needed to meet future debt service.

The Stable Outlook reflects KBRA's expectation that the pledged ad valorem tax revenues will continue to grow in line with projections to support the District's operations and debt service. The outlook further assumes that future capital improvements will be completed without necessitating significant increases in the tax rate, which we expect will remain well below the State Constitutional levy limit.

Key Credit Considerations

The rating was assigned because of the following key credit considerations:

Credit Positives

- The District is the primary safety net healthcare provider in the County and plays an essential role within the County's public health mission.
- A growing tax base continues to generate strong property tax revenues for the District, thus supporting voter-authorized debt obligations.
- District's ad valorem tax rate remains well below the Constitutional limit.

Credit Challenges

- Large capital plan will place upward pressure on operating expenses, debt requirements and the tax levy.
- Managing potential operational challenges should federal Medicaid funding materially decline .

Rating Sensitivities

▪ Material growth in the property tax base, which supports the District's revenue and operations and bolsters the taxing capacity within the Constitutional levy limit.	+
▪ Significant secular deceleration or declines in tax base growth pressuring ad valorem tax support. ▪ Trend of sharply increasing operating deficits requiring substantial increases in the M&O tax rate.	-

Key Ratios	
Economic Base and Demographics	
County Population (2023)	4,835,125
CAGR (2013-2023)	1.10%
Income Per Capita (2023)	$39,483
as a % of State	99%
Unemployment Rate (Feb 2025)	4.5%
as a % of US	100%
Poverty Level (2023)	16.0%
Taxable Assessed Value (FY 2025)	$608.1 billion
CAGR (2015-2025)	6.0%
District Ad Valorem Tax	
Constitutional District Tax Limit	$0.7500 per $100 of TAV
FY 2025 Rate	$0.1635 per $100 of TAV

Source: US Census Bureau; Harris County Hospital District POS, Series 2025 Limited Tax Bonds.

Rating Determinants (RD)	
1. Legal Framework	AA+
2. Nature of Property Tax/Assessment Revenue Base	AA+
3. Economic Base and Demographics	AA+
4. Revenue Analysis	AA+
5. Market Position and Operations	A
6. Governance and Management	Satisfactory

RDs 1-4 are from KBRA's General Property Tax/Assessment Revenue Rating Methodology, while RDs 5-6 are from KBRA's U.S. Not-For-Profit Healthcare Rating Methodology.

RD 1: Legal Framework

Harris County Hospital District is a component unit of the County (legally separate from Harris County), established via a countywide election in November 1965. The statutory purpose of the District is to provide medical aid and hospice care to the indigent and needy of the County. The District operates two acute care hospitals (Lyndon B Johnson and Ben Taub) with a total of 617 licensed beds, along with 16 primary care health centers, seven homeless shelter healthcare clinics, an urgent care clinic and varied other clinics, a dental center, and mobile immunization and medical outreach programs.

The Bonds are issued under the Constitution and general laws of the State of Texas, with the approval of the voters of the District, and pursuant to the Bond Resolution adopted by the Board of Directors of the District on March 27, 2025, and the Bond Order adopted by the Commissioners Court of the County (the "Commissioners Court") on April 10, 2025.

The Bonds are direct obligations of the District secured by a continuing and direct ad valorem tax pledge on all taxable property within the District, which is coterminous with Harris County.

Nature and Strength of Pledge

Hospital districts are the only type of local health care jurisdiction in Texas that are able to impose property taxes if approved by voters. The Commissioners Court, which is the elected governing body for the County, acting on behalf of the District, sets the ad valorem tax rate at a level sufficient to pay debt service on the Bonds, in accordance with the Bond Order. The District's ability to issue tax-supported debt is limited by tax rate limitations imposed by the State Constitution; the District's ad valorem tax rate for all purposes cannot exceed $0.7500 per $100 of valuation.

The District currently levies a total tax rate of $0.1635 per $100 of AV for FY 2024, with $0.1621 dedicated to O&M (M&O tax rate) and $0.0014 to debt service (I&S tax levy). The Board may adjust the tax rate subject to the limitation that proposed tax rates resulting in M&O levy growth of more than 8% YoY (excluding the effect of new properties added to the assessment roll) must be brought to a vote whereby the electorate will determine whether or not to reduce the adopted tax rate to within the 8% YoY growth limitation. However, the property tax levy growth limitation does not affect the ability to set an I&S tax rate sufficient to pay debt service on the District's limited tax bonds. Hospital districts are exempt from the Texas Property Tax Reform and Transparency Act of 2019, which limits assessment growth, absent of voter approval, to 3.5% YoY for cities and counties, and 2.5% YoY for school districts. It is the administrative policy of the Attorney General of the State of Texas to limit the I&S levy for hospital districts to two-thirds of the total levy, but this threshold can be exceeded on a "showing of good cause".

Lien Structure

The 2025 Bonds represent the first issuance of debt under an authorization of $2.5 billion approved by the District's voters on November 7, 2023. Revenues collected under the I&S levy pursuant to the voter-approved bond authorizations may only be used for debt service on bonds issued under such authorization.

In addition to the 2025 Bonds, the District has $59.3 million of Certificates of Obligation outstanding, as of February 28, 2025, which are payable from a direct property tax levied by the District subject to the same $0.7500 per $100 limitation. The Certificates are paid from a separate debt service fund and have no claim on the taxes levied for the 2025 Bonds.

The District also has $197.1 million in outstanding revenue bonds, as of February 28, 2025 . The revenue bonds are secured by a lien on the gross revenues of the District from all sources other than ad valorem taxes.

Flow of Funds

Property within the District is generally assessed as of January 1 each year with ad valorem taxes becoming due October 1, and delinquent if unpaid by February 1 of the subsequent year. Taxes are collected by the Harris County Tax Assessor- Collector on behalf of the District. All property taxes collected from the I&S levy for the 2025 Bonds are deposited as collected in the 2025 Bond Debt Service Fund created under the Bond Order.

Debt Service Reserve Fund

The Bonds are not secured by a debt service reserve fund.

Additional Bonds

There is no additional bonds test but additional bonds payable from the same pledge of ad valorem taxes would be subject to the same authorization requirements as the current issue. After the issuance of the 2025 Bonds the District will have approximately $1.65 billion remaining under the November 2023 authorization.

Bankruptcy Assessment

KBRA has consulted outside counsel on bankruptcy matters and the following represents our understanding of the material bankruptcy issues relevant to the District and the Bonds.

Eligibility to be a Debtor

To be a debtor under the municipal bankruptcy provisions of the U.S. Bankruptcy Code (i.e., Chapter 9), a local governmental entity must, among other things, (i) qualify under the definition of a "municipality" in the Bankruptcy Code and (ii) be specifically authorized to file a bankruptcy petition by the state in which it is located.

The District is a political subdivision or public agency or instrumentality of the State of Texas and thus is a "municipality" as defined under the Bankruptcy Code.

As to authorization, Texas state law specifically authorizes any municipality in the State that has the power to incur indebtedness through the action of the municipality's governing body to file a Chapter 9 petition. The District, as a municipality under Texas law, has the authority to incur indebtedness, and, hence, it is specifically authorized under Texas law to file a Chapter 9 petition, subject to the further threshold requirements in Federal law (i.e., the Bankruptcy Code) for commencement of a Chapter 9 case.

Liens and Pledges that Survive a Chapter 9 Filing

Chapter 9 provides for post-petition recognition of (i) security interests represented by a pledge of specific special tax revenues, municipal enterprise revenues, or a special excise tax imposed on a particular activity or transaction (each "special revenues") and (ii) statutory liens on revenues pledged for municipal obligations. By contrast, the pledge of general *ad valorem* property taxes for general purpose obligations of a municipality is not recognized as a security interest or lien that continues following the filing of a petition under Chapter 9.

The Bonds are secured by and payable from the levy and collection of a continuing, direct *ad valorum* tax, levied on all taxable property within the District.

Because (i) the funds pledged to pay the Bonds are not from a separate, dedicated and restricted source of revenues that meets one of the definitions of "special revenues" under Chapter 9, and (ii) there is no statutory lien imposed on the funds pledged to pay the Bonds, the bondholders, assuming proper presentation and argument, should be treated as unsecured creditors in a Chapter 9 bankruptcy proceeding of the District.

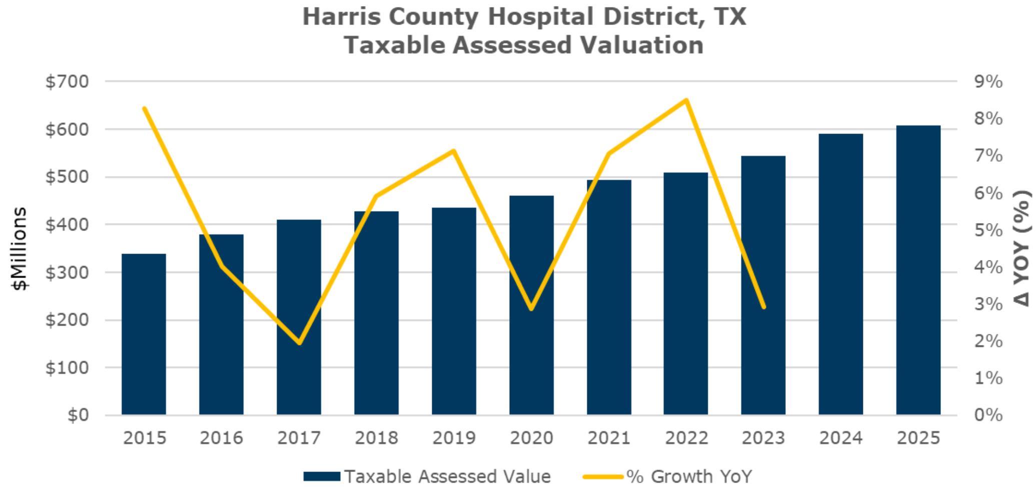
RD 2: Nature of Property Tax/Assessment Revenue Base

KBRA views the nature of the pledged ad valorem revenues as strong given that the property tax levy is assessed on all taxable property in the District, which encompasses all of the County's tax base, and includes the large and growing City of Houston, TX.

The tax base is diverse with real residential property accounting for the largest share (56.5%), followed by real commercial and industrial property (22.8%).

The County's tax assessment base is very large reflecting a population of 4.8 million. The TAV in the County has increased considerably over the past decade, from $339.6 billion in 2015 to $608.1 billion in FY 2025, reflecting a strong 10-year CAGR of 6.0% (Figure 1).

Figure 1



Source: Harris County Hospital District, Annual Continuing Disclosure.

Tax Base Concentration

The District's ten largest taxpayers are fairly diverse, and in aggregate all ten comprise only 3.7% of the County's total assessed value in fiscal 2024 (Figure 2), which is down from 4.1% YoY.

Figure 2

Ten Largest Taxpayers - Harris County FY 2024				
	Taxpayer	**Property Type**	**TAV [1] ($000s)**	**% of Total TAV**
1	Centerpoint Energy, Inc.	Electric Utility	5,967,413	0.98%
2	Exxon Mobil Corp.	Oil & Gas	4,911,227	0.81%
3	Chevron Chemical Co.	Oil & Gas	3,367,710	0.55%
4	Equistar Chemicals LP	Chemical Mfg.	1,678,743	0.28%
5	Lyb Channelview POTBA LLC	Chemical Mgg.	1,396,026	0.23%
6	HEB Grocery Co. LP	Retail Store	1,124,061	0.18%
7	Palmetto Transoceanic LLC	Business Park	1,062,329	0.17%
8	Walmart	Retail Store	1,031,573	0.17%
9	Liberty Property	Retail Store	989,562	0.16%
10	Lyondell Chemical Co.	Chemical Plant	942,111	0.15%
	Total		**$22,470,755**	**3.70%**

[1] Taxable Assessed Valuation, Harris County.
Source: Harris County Hospital District

RD 3: Economic Base and Demographics

The District's economic base, which is located in and coterminous with Harris County is sound, characterized by a large and growing population as well as an increasingly diversified economy. Harris County remains the most populous county in Texas, and the County Seat – Houston - is the largest city in Texas and the fourth largest city in the nation.

Population

The Harris County population is sizeable at 4.8 million (2023) and has increased at a 1.1% CAGR between 2013 and 2023, somewhat slower than the State (+1.4%) but nearly twice as quickly as the nation (+0.6%). The strong population growth exhibited within the County has necessitated that the District take steps to expand capacity and services, which will be financed primarily through the $2.5 million bond authorization.

Income

County per capita income estimated at $39,483 as of 2023 was solid, equivalent to 99.3% of the State ($39,775) and 91.2% of the US ($43,313) averages. The County incidence of poverty (16.0%) exceeds that of both the State (13.7%) and nation (12.5%) reflecting its urban character.

Employment

Harris County's employment base is fairly diverse with a degree of concentration relative to the U.S. overall in professional & business services as well as trade and construction. Twenty-six Fortune 500 companies are headquartered in the Houston MSA.

The County unemployment rate has trended generally above the State and national averages since 2016, although as of February 2025, it stood at 4.5%, comparable to the US level (4.5%) and above the State (4.3%). Employment growth has been favorable, recording a 10-year CAGR through 2024 of 1.2%, outpacing that of the US (+1.0%), but lagging the rapid growth of the State overall (+2.0%).

Figure 3

Total Employment (Not Seasonally Adjusted) (In Thousands)								
	Harris County, Texas	% Δ	Houston-The Woodlands-Sugar Land, TX	% Δ	Texas	% Δ	United States	% Δ
2004	1,699	0.8%	2,413	1.5%	10,370	1.7%	139,252	1.1%
2005	1,737	2.2%	2,481	2.8%	10,625	2.5%	141,730	1.8%
2006	1,792	3.2%	2,554	2.9%	10,847	2.1%	144,427	1.9%
2007	1,832	2.2%	2,619	2.5%	11,027	1.7%	146,047	1.1%
2008	1,860	1.5%	2,674	2.1%	11,211	1.7%	145,362	-0.5%
2009	**1,840**	-1.1%	**2,652**	-0.8%	**11,116**	-0.8%	139,877	-3.8%
2010	1,896	3.1%	2,740	3.3%	11,264	1.3%	**139,064**	-0.6%
2011	1,935	2.1%	2,800	2.2%	11,476	1.9%	139,869	0.6%
2012	2,007	3.7%	2,907	3.8%	11,777	2.6%	142,469	1.9%
2013	2,055	2.4%	2,985	2.7%	11,986	1.8%	143,929	1.0%
2014	2,110	2.7%	3,076	3.1%	12,304	2.7%	146,305	1.7%
2015	2,121	0.5%	3,104	0.9%	12,446	1.2%	148,834	1.7%
2016	2,118	-0.1%	3,117	0.4%	12,650	1.6%	151,436	1.7%
2017	2,134	0.8%	3,153	1.2%	12,890	1.9%	153,337	1.3%
2018	2,168	1.6%	3,220	2.1%	13,176	2.2%	155,761	1.6%
2019	2,195	1.2%	3,281	1.9%	13,433	1.9%	157,538	1.1%
2020	2,072	-5.6%	3,119	-4.9%	12,880	-4.1%	147,795	-6.2%
2021	2,151	3.8%	3,238	3.8%	13,513	4.9%	152,581	3.2%
2022	2,252	4.7%	3,390	4.7%	14,160	4.8%	158,291	3.7%
2023	2,334	3.6%	3,514	3.6%	14,609	3.2%	161,037	1.7%
2024	2,387	2.3%	3,669	4.4%	14,971	2.5%	161,346	0.2%
Δ 2014 to 2024		**13.1%**		**19.3%**		**21.7%**		**10.3%**
10 Year CAGR (2024)		**1.2%**		**1.8%**		**2.0%**		**1.0%**

Source: U.S Bureau of Labor Statistics

Bold = trough during the Great Recession (2008-2012)

RD 4: Revenue Analysis

KBRA views the pledged ad valorem tax revenues as providing a strong source of debt service repayment for the District's limited tax bonds. The service area has exhibited strong property tax base appreciation, providing a stable source of revenue for the District's operations and payment of debt service on the limited tax bonds.

Trend in Ad Valorem Tax Revenues

The TAV has grown by a CAGR of 6.0% for the past ten years (2015-2025), and along with the pandemic-related federal funding have allowed the total tax rate to trend lower through FY 2024, to $.1434 per $100 TAV from $.1700 in fiscal 2020. With the pandemic related funding fully exhausted, the District has returned to more typical operating performance, and the total tax rate is up YoY for FY 2025 to $.1635, which remains well below the taxing capacity of $.7500 per $100 TAV and continues to support healthy operating performance.

Figure 4

Assessed Value, Tax Rate, and Levy History									
Fiscal Year Ends 9/30 (1)	Taxable Assessed Value ($000)	*YoY % Chg*	Total Tax Rate (2)	Distribution: Operation & Maintenance	Distribution: Interest & Sinking Fund	Tax Levy ($000) (3)	% Current Collections (3)	% Total Collections (3)	GO Tax Debt Outstanding ($000) (3)
2020	461,641,802	*5.9%*	0.1700	0.1700	-	643,566	94.90%	99.50%	55,005
2021	494,523,765	*7.1%*	0.1667	0.1649	0.0018	824,430	93.18%	93.76%	81,540
2022	508,749,755	*2.9%*	0.1622	0.1605	0.0017	825,768	94.93%	94.56%	76,385
2023	544,607,133	*7.0%*	0.1483	0.1468	0.0015	834,222	98.31%	97.60%	70,970
2024	590,883,077	*8.5%*	0.1434	0.1421	0.0014	897,274	98.08%	96.87%	65,285
2025	608,079,477	*2.9%*	0.1635	0.1621	0.0014	1,059,033	95.69%	95.06%	898,865

(1) The District changed its fiscal year end from February 28th to September 30th, effective 3/1/2022.

(2) Per $100 of assessed valuation; includes the O&M and I&S tax rates.

(3) Reflects projections for FY 2025; includes limited tax debt outstanding as of 2/28/2025 plus proposed Series 2025 issuance; tax collections thru 3/31/2

Source: Harris County Hospital District, Preliminary Official Statement Series 2025, Limited Tax Bonds.

The District's debt burden is relatively low at 18.3% of total capitalization for FYE2024, with limited new debt requirements for the past five years. Outstanding limited tax bonds totaled $59.3 million as of February 28, 2025. Post issuance of the 2025 Bonds, pro forma debt service requirements are generally flat, with MADS of approximately $54.8

million in FY 2043, and a final maturity of 2055. Including the District's additional limited tax borrowings anticipated in 2026 and 2027, annual debt service is projected to levelize at about $161 million, with MADS of $170 million in FY 2030.

RD 5: Market Position and Operations

KBRA views Harris Health as an essential health care provider for its patient population that is primarily uninsured and underinsured in the higher poverty areas of the County, with its operations supported by tax revenues. The substantial size of the County, strong population growth and urban poverty levels support ongoing demand for indigent healthcare services in the County.

The District's principal medical facilities - the LBJ and Ben Taub acute care hospitals - provide a full range of medical services and specialties, in concert with an extensive network of clinics, health centers and telemedicine capabilities to serve the indigent population in the County. Ben Taub Hospital is one of two Level I trauma hospitals in the County[2] for adult patients. With continued strong population growth, the District is adding another Level 1 trauma hospital at the LBJ complex. The new replacement hospital is under construction and anticipated to be completed in 2028.

The District levies property taxes to generate sufficient revenues to meet the healthcare needs of its target population. Approximately 35% of FY 2024 total revenues were derived from ad valorem tax revenues, and the rest (65%) from general non-tax revenues. Harris Health's property tax revenues continue to outpace its operating losses, supporting stable operating performance, with a net position that has grown to $1.2 billion in FY 2024 from $492 million in FY 2021. Liquidity is solid at 231 days cash on hand for fiscal 2024, up from 167 days cash in the prior year. All COVID-19 related federal funds will be exhausted by 2026.

Payor Mix and Reimbursement

As a safety net provider, the District serves a large volume of Medicare (11% of patients) and Medicaid (19%) patients, as well as uninsured (charity care) patients (44%). Consequently, net patient revenues, excluding the property tax revenues, rely on significant federal and other supplemental funding.

Figure 5

Harris Health Payor Mix					
Based on Cash Collections	**FY2024**	**FY2023** [1]	**FY2022**	**FY2021**	**FY2020**
Commercial	6.6%	6.1%	11.4%	7.4%	8.4%
Medicare	14.4%	15.1%	28.6%	29.8%	31.5%
Medicaid	5.3%	6.0%	9.5%	11.0%	17.3%
Medicaid Supplemental & Other Oper Income	72.9%	71.9%	39.4%	37.6%	34.0%
Self-Pay	0.3%	0.3%	9.8%	9.9%	4.4%
Other Cost Reimbursement	0.5%	0.6%	1.3%	4.2%	4.4%
Total	**100.0%**	**100.0%**	**100.0%**	**100.0%**	**100.0%**

[1] Reflects 12-month period ended Sept. 30th, 2023. The District changed its fiscal year-end from February 28th to Sept. 30th, as of 3/

Source: Harris County Hospital District, Preliminary Official Statement, Series 2025 Limited Tax Bonds.

According to the fiscal 2024 audit, Medicare, Medicaid and managed Medicaid supplemental programs accounted for 73% of total cash collections for net patient service revenues; similar to the prior fiscal year at 75%. While KBRA views the reliance on supplemental funding as relatively high, it is manageable and expected given the District's role as a safety net provider and its tax-supported operations. Harris Health's historical payor mix, based upon cash collections, is noted in the table below. KBRA will continue to monitor Federal actions as it relates to Medicaid funding throughout the nation.

Utilization and Market Share

Following the pandemic-related utilization decline in FY 2020, inpatient, specialty care, emergency room and surgical case have all recovered significantly through fiscal year 2024 (see Figure 6).

While market share data is limited, the District noted that Harris Health maintains an estimated 7.4% of the adult inpatient market, and it rises to 15.4% of the adult Medicaid-served market. Harris Health operates in the greater Houston area which is a hub for medical and life sciences, and it includes one of the largest healthcare providers in the US, Memorial Hermann Health System, which operates 15 hospitals in the area. In KBRA's view, the competitive pressure is moderated by the District's nature of its payor mix, its role of serving as the County's safety net provider, and its tax-supported operations with demonstrated community support (voter-approval) for its continued operations.

[2] The second Level I trauma center for adults is the Red Duke Trauma Institute at Memorial Hermann – Texas Medical Center. There is also a children's Level 1 trauma center at Texas Children's Hospital.

Figure 6

Utilization - Harris County Hospital District					
Fiscal Year ended 9/30 [(1)]	**2021**	**2022** [2]	**2022** [3]	**2023** [4]	**2024**
Year-end Beds in Operation	654	670	693	686	705
Inpatient Admissions	24,626	26,919	17,223	31,530	30,757
Observation Cases	11,855	13,643	7,755	10,074	11,476
Total Patient Days	179,686	209,126	127,737	229,819	239,811
Average Length of Stay	5.99	6.22	5.97	6.24	6.51
Average Percent Occupancy	75.3%	85.5%	87.7%	91.8%	92.9%
Primary Care Clinic Visits	691,711	668,781	383,520	656,222	637,640
Specialty Care Visits	161,495	228,773	144,518	244,898	244,782
Emergency Room Visits	132,514	147,496	91,453	155,570	165,526
Surgical Cases	15,744	18,207	11,962	20,704	22,022

(1) Harris County Healthcare District changed its fiscal year from Feb. 28th to Sept. 30th as of 3/1/2022.

(2) 12-month period ended Februanry 28, 2022.

(3) 7-month period ended September 30, 2022.

(4) 12-month period ended September 30, 2023.

Source: Harris County Healthcare District, FY2024 Continuing Disclosure Series 2016 Revenue and Refunding Bonds.

Payment Methodologies and Regulatory Factors

The Bonds are secured from ad valorem revenues of the District, and not from Medicaid, Medicare or other revenues received by the District. Like other urban hospital districts in Texas that operate under the Texas Indigent Health Care and Treatment Act, the provision of services to the uninsured requires the levy of health care ad valorem taxes for maintenance and operations purposes.

Texas is among 12 states that have not expanded Medicaid under the Affordable Care Act ("ACA"). Since federal fiscal year 2012, Texas hospitals have continued to receive supplemental federal funding and expanded Medicaid managed care pursuant to a waiver program (the Medicaid Section 1115 waiver). The waiver program, which has been renewed by CMS through September 30, 2030, provides for State and federal government funding of the Uncompensated Care ("UC") Pool and the Delivery System Reform Incentive Payment ("DSRIP") Pool in lieu of upper payment limit payments to hospitals. These two pools provide supplemental payments to providers to partially offset the cost of uncompensated care provided to Medicaid and uninsured patients. UC funding requires the District to provide a State match (through the State Health and Human Services Commission), which is then matched by federal funding. The DSRIP program expired on September 30, 2021. The Centers for Medicare and Medicaid Service developed alternative directed payment programs to transition hospitals away from the DSRIP.

Texas is one of 11 states with no certificate of need laws or caps. The lack of state regulatory approval of major healthcare capital expenditures may make it easier for the District to expand its facilities as needed.

Scope of Operations & Medical Staff

Harris Health offers an extensive suite of healthcare services at its 2 main hospitals and via numerous (37) clinics and healthcare centers throughout the County. In addition to its recognized Level I and Level III trauma centers at Ben Taub and LBJ hospitals, respectively, Harris Health offers medical services which include intensive care, surgical, obstetrics, neonatal, psychiatric inpatient services, and a wide range of outpatient clinical services.

Ben Taub and LBJ Hospitals are each teaching facilities associated with Baylor College of Medicine and McGovern Medical School at UTHealth, respectively. The District notes that Harris Health is a recognized leader in the areas of cardiology, stroke, trauma, neonatology and community healthcare.

RD 6: Governance and Management

Governance

The governance of the District is vested in a nine-member Board of Trustees (the "Board") appointed by the Commissioners Court to serve staggered two-year terms. The Board selects a chairman, sets District policy, appoints a Chief Executive Officer (CEO) and submits an annual budget to the Commissioners Court for approval. The Chief Executive Officer manages the day-to-day operations of the District and its health care facilities. The Commissioners Court, which is the elected governing body for the County, is responsible for setting the District's ad valorem tax levy, which funds the debt service on the Bonds and also approves the District's debt obligations.

Management Experience and Track Record

The District's senior leadership team is comprised of seasoned, highly knowledgeable executives, with decades of experience in healthcare administration, including in settings that provide care to a large, indigent care population. In addition, several leaders have served at the District for many years and have taken on roles of increasing responsibility over time. Depth of experience and tenure, in KBRA's view, better positions management to effectively navigate potential operational and financial challenges that may arise as the District implements its complex, multi-phase CIP.

The President and CEO of the District, Dr. Esmaeil Porsa (MD; MPA; MPH; CCHP-A) has been at Harris Health for five years, following the retirement of the prior CEO. Dr. Porsa's healthcare experience spans 28 years, previously as the Executive Vice President and Chief Strategy and Integration Officer at Parkland Health & Hospital System, another large hospital system in Dallas, TX.

The Chief Financial Officer, Victoria Nikitin (MBA, CPA) has been the District's Executive Vice President and CFO for the past three years but has worked in varying capacities at Harris Health since 2004. Ms. Nikitin has twenty-five years of financial experience in complex healthcare environments including primary, secondary and tertiary care. She joined the District in 2004 and was directly involved with the development of Harris Health's change strategy, resulting in over 220% growth in the District's operations to a $2.5 billion enterprise today. She also served as a co-architect of the District's $370 million multi-year strategic capital program that included the construction of two outpatient towers, two new clinics and eligibility centers, and expansion of the Ben Taub and LBJ hospital platforms.

Financial Policies and Procedures

The District's maintains sound financial policies and procedures, and its budget process generally coincides with the County's budget calendar -- both are based on a fiscal year end of September 30th. The District is required by law to prepare an annual budget for approval by the Board, which then submits the budget to the Commissioners Court for final approval.

Projections of tax receipts are based on the Harris Central Appraisal District's Certified Estimate of TAV for the applicable tax year. The District's budget process begins in January and provides a proposed budget for approval by its Board of Trustees in August. The Commissioners Court then reviews the proposed budget for approval, and in September sets the new tax levy for the District and all component units, for use in the new fiscal year beginning Oct. 1st.

The District is monitoring the budget performance on a monthly basis and reports actual performance relative to budget on a quarterly basis to the County. The District has the ability to adjust the budget during the year, with the approval of the Board and the Commissioners Court. The District has a goal of adopting a budget each year which incorporates a 2% total margin, which the District has exceeded each of the last five years.

Enterprise Risk Management

The District maintains insurance policies including property and casualty insurance, cyber insurance, and liability insurance covering officers and directors. The District also carries a managed-care liability insurance policy that covers Community Health Choice, Inc., with respect to errors and omissions and liability. Under Texas law the maximum liability for professional and general liability claims is generally $100,000 per individual and $300,000 in aggregate per occurrence.

Strategic Planning

The District's maintains a strategic plan that is updated every five years and approved by the Board. The current strategic plan (2021–2025) focuses on six pillars: quality and patient safety; people; one Harris Health; population health management; infrastructure optimization; and diversity, equity and inclusion. Through the plan the District is addressing varied goals, including: the need to replace aging infrastructure at its LBJ and Ben Taub hospitals; improve system reliability; eliminate "never" events; and address the need for care in underserved communities and specialty care for the indigent and uninsured population of the County. The District is in the midst of developing the successor plan for the 2026–2030 period which focuses on the key themes of quality and patient safety; people; financial resiliency; health promotion and disease prevention; infrastructure optimization; and access.

Capital Planning

The District's comprehensive 10-year capital plan totals just under $3 billion through 2035. The vast majority of the capital plan (roughly 87%) will be debt funded via the issuance of the 2025 limited tax Bonds and the projected two subsequent parity bond issuances. The rest of the capex funding is anticipated to be funded internally ($300 million) and via philanthropic support ($100 million).

The LBJ Campus plan is estimated at $2.0 billion and includes a replacement hospital to increase patient capacity in multiple areas; position the hospital as a level 1 trauma facility; and transform legacy facilities to address critical service gaps and provide increased outpatient access. The LBJ capital projects are scheduled for completion in phases through 2024-2031, with the new Level I trauma hospital completion anticipated in late 2028.

The Ben Taub projects, totaling $410 million is slated for completion in 2030 and expected to extend the facility's lifespan by 15 years; adding capacity through the addition of a new inpatient tower with approximately 120 incremental patient rooms. The final aspect of the capital program includes $504.5 million investment in new ambulatory care facilities in three precincts of the District to provide greater patient volumes at the existing sites.

The District implemented a thorough demand planning process in developing the plans for the new LBJ facility, which commenced in 2021-2023 with the design phase to determine initial capacity levels for full build out as well as shelled areas for future use. Phases 2 through 4 will continually revise the capacity plan through consultation with Capital Healthcare and the UT Health Science Center to determine final staffing projections and operating needs for Day 1 based on projected demand.

Investment Management

The District is required to conservatively maintain investments in compliance with the Texas Public Funds Investment Act (PFIA), which can include obligations of the United States or its agencies, direct obligations of the State or its agencies, certificates of deposit, and repurchase agreements.

The District's governing Board adopted a formal investment policy in accordance with state law which is reviewed and approved annually. The investment policy includes a list of authorized investment instruments, a maximum allowable stated maturity by fund type, and the maximum weighted-average maturity of the overall portfolio. The policy also establishes guidelines for diversification and risk tolerance, as well as minimum acceptable credit ratings for certain investment instruments. In practice, the District's investments are limited to obligations of the United States or its instrumentalities, federal agencies, fully collateralized repurchase agreements, commercial paper, municipal obligations rated "AA" or higher, and money market mutual funds.

ESG Management

KBRA typically analyzes Environmental, Social, and Governance (ESG) factors through the lens of how issuers plan for and manage relevant ESG risks and opportunities. More information on KBRA's approach to ESG risk management in public finance ratings can be found here. Over the medium-term, public finance issuers will likely need to prioritize ESG risk management and disclosure with the likelihood of expansions in ESG-related regulation and rising investor focus on ESG issues.

KBRA analyzes many sector- and issuer-specific ESG issues but our analysis is often anchored around three core topics: climate change, with particular focus on greenhouse gas emissions; stakeholder preferences; and cybersecurity. Under environmental, as the effects of climate change evolve and become more severe, issuers are increasingly facing an emerging array of challenges and potential opportunities that can influence financial assets, operations, and capital planning. Under social, the effects of stakeholder preferences on ESG issues can impact the demand for an issuer's product and services, the strength of its global reputation and branding, its relationship with employees, consumers, regulators, and lawmakers, and, importantly, its cost of and access to capital. Under governance, as issuers continue to become more reliant on technology, cybersecurity planning and information management are necessary for most issuers, regardless of size and industry.

Environmental Factors

The State of Texas regulates the management of medical waste, defined as waste from health care-related facilities. The District is compliant with the state's medical-waste treatment requirements. HCHD follows protocol and provides training to employees in the proper handling and management of hazardous materials and waste.

Given the District's location near the Texas Gulf Coast, it is susceptible to severe weather events including high winds, heavy rain, flooding, hurricanes, tropical storms, and winter storms. If a weather event were to cause damage within the District resulting in a significant decline in the assessed value of property, the tax revenues securing the bonds may be impacted and could necessitate an increase in the District's tax rate.

The District's capital plan includes the construction of a Central Utility Plant to provide on-site power generation using a natural gas cogeneration system, for which all primary systems are above the 500-yr flood plain. The District reports that plant will reduce carbon emissions versus grid power by approximately 34%.

Social Factors

HCHD serves as a safety-net hospital with the purpose of providing medical and hospital services to the indigent and lower income residents of Harris County, regardless of payor source. The District is an essential healthcare system and includes two hospitals (one of only two level I trauma centers in the County and the busiest level III trauma center in the State) and a large network of sixteen community health centers, seven homeless shelter clinics, five specialty clinics, among other facilities.

The District's strategic plan contains initiatives partnering with community-based organizations to address social and economic determinants of health including but not limited to food insecurity, housing and transportation, income, and health literacy.

Governance Factors

The District maintains a comprehensive cybersecurity program, which includes various network security measures, employee training and awareness, and periodic independent third-party assessments, along with cyber-insurance coverage. The District's cybersecurity team meets monthly with the corporate compliance team to evaluate and monitor all cyber-risk management activities of the District. The District also conducts periodic assessments of its cybersecurity measures, utilizing an independent consultant to identify potential vulnerabilities and any necessary remediation efforts to address.