

**EVALUATION OF THE CERTIFICATE OF NEED APPLICATION SUBMITTED ON BEHALF OF KENNEWICK PUBLIC HOSPITAL DISTRICT dba KENNEWICK GENERAL HOSPITAL PROPOSING TO RELOCATE 74 OF ITS EXISTING ACUTE CARE LICENSED BED CAPACITY TO A NEW CAMPUS AT THE SOUTHRIDGE AREA OF KENNEWICK**

**PROJECT DESCRIPTION**

Kennewick Public Hospital District (KPHD) dba Kennewick General Hospital (KGH), a public hospital located in the city of Kennewick, within Benton County provides Medicare/Medicaid acute care services to residents of Benton and Franklin counties and surrounding areas. KGH is currently licensed for 101 acute care beds and holds a three year accreditation from the Joint Commission on Accreditation of Health Care Organizations. In addition to the hospital, KPHD also owns and operates Kennewick Home Health Services, Benton Franklin Elder Services and KGH Medical Mall. Inpatient services currently provided at KGH include medical-surgical services, emergency services, basic pediatric services, obstetrical services, ICU and CCU, progressive care unit, neurological services, diagnostic services, and physical therapy.

Upon Completion of the project, the Southridge campus would provide critical care, medical and surgical beds, emergency department, operating rooms, diagnostic imaging, pharmacy, administrative, and support services. The Auburn campus would provide women and children's services, (maternity, pediatric, and nursery services) ambulatory services, physician practices, ultrasound, urgent care, satellite lab, limited imaging, hospital support services, and some administrative services. The Medical Mall would continue to offer ambulatory services, physician practices, outpatient surgery, outpatient imaging, G.I. services, and pharmacy..

For this project, KGH is proposing to construct a facility at its Southridge campus and transfer 74 acute care licensed beds and supporting services from its existing Auburn campus leaving 27 beds and supporting services at the Auburn campus. The new campus known as KGH Southridge, will provide inpatient medical/surgical and intensive care services, emergency services, and a full complement of ancillary services. Obstetrical and pediatric care will continue to be provided at the existing Auburn campus.

The total capital expenditure associated with this project is \$112,378,100 of which approximately \$94,378,100 or 83.5% is related to construction/site preparation costs.

**APPLICABILITY OF CERTIFICATE OF NEED LAW**

This project is subject to Certificate of Need Review as the establishment of a new health care facility under the provisions of Revised Code of Washington (RCW) 70.38.105(4)(a) and Washington Administrative Code (WAC) 246-310-020(1)(a).

## **APPLICATION CHRONOLOGY**

April 30, 2008	Letter of Intent submitted
July 07, 2008	Application submitted
July 08, 2008	Department's Pre-Review Activities
September 12, 2008	Screening Responses Received
September 19, 2008	Department begins review of application
November 5, 2008	Public hearing conducted on this project
November 5, 2008	End of public comment on application
January 5, 2008	Department's anticipated decision due
January 6, 2009	Department extends Review period for 30 days
February 4, 2009	Department's actual decision date

## **AFFECTED AND INTERESTED PERSONS**

The following entities sought and received affected person status under WAC 246-310-010:

- Larry Chapman located in the city of Richland in the Public Hospital District within Benton County
- Robert Williamson located in the city of Richland in the Kennewick Public Hospital District within Benton County.
- Ray Robinson located in the city of Richland in the Public Hospital District, within Benton County.

## **SOURCE INFORMATION REVIEWED**

- Kennewick General Hospital's June 28, 2008, Certificate of Need Application.
- Kennewick General Hospital's supplemental information (September 12, 2008)
- Community member's comments received throughout the public comment period
- Documents and comments received from community members at the November 5, 2008 public hearing
- Kennewick General Hospital's rebuttal comments (November 21, 2008)
- Comprehensive Hospital Abstract Reporting System (CHARS) data obtained from the Department of Health's Office of Hospital and Patient Data Systems
- Population data obtained from the Office of Financial Management based on year 2000 census Published January 2007.
- Department of Health's Office of Hospital and Patient Data Systems
- Healthcare cost and utilization project (HCUP) database of Oregon State Hospital discharge data 2006.
- Historical charity care data obtained from the Department of Health's Office of Hospital and Patient Data Systems (2003, 2004, 2005 summaries)
- Data obtained from Kennewick General Hospital's website
- Southridge Sub-Area Plan, April 2005, City of Kennewick

- November 5, 2008 letter from Foster Pepper PLLC Re: Proposal to Finance and Develop New Hospital Facilities.
- Hospital licensing and survey data provided by the Department of Health's Office of Health Care Survey

### **CRITERIA EVALUATION**

To obtain Certificate of Need approval, KGH must demonstrate compliance with the criteria found in WAC 246-310-210 (need), 246-310-220 (financial feasibility), 248-310-230 (structure and process of care), and 246-310-240 (cost containment)<sup>1</sup>.

### **CONCLUSION**

For the reasons stated in this evaluation, the application submitted by Kennewick General Hospital District on behalf of Kennewick General Hospital proposing to relocate 74 acute care licensed beds and construct a new facility is consistent with applicable criteria of the Certificate of Need Program and a Certificate of Need should be issued provided the applicant agrees to the terms and condition stated below:

### **TERMS**

- 1) Within 30 days of finalizing the Ground Lease Agreement, the applicants will submit to the Certificate of Need Program the executed Ground Lease. The final Ground Lease will be consistent with the draft agreement provided in Exhibit 3 of the application.
- 2) Within 30 days of finalizing the Facility Lease Agreement, the applicants will submit to the Certificate of Need Program the executed Facility Lease. The final Facility Lease will be consistent with the draft agreement provided in Exhibit 4 of the application.
- 3) Within 30 days of finalizing the Regulatory Agreement with HUD, the applicants will submit to the Certificate of Need Program the executed document.
- 4) Within 30 days of finalizing the Approval Covenants for HUD Section 242 Mortgage Insurance document, the applicants will submit to the Certificate of Need Program the executed document.
- 5) Within 30 days of finalizing the Rider to Regulatory Agreement for HUD Section 242 Mortgage Insurance, the applicants will submit to the Certificate of Need Program the executed document.
- 6) Prior to commencement, KGH must submit a copy of the approval letter or other documentation to show adoption of the previous environmental impact statement (EIS) as referenced in the letter dated 8/26/08 from the City of Kennewick.

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<sup>1</sup> Each criterion contains certain sub-criteria. The following sub-criteria are not discussed in this evaluation because they are not relevant to this project: WAC 246-310-210 (3), (4), (5), (6).

## **CONDITION**

Kennewick General Hospital will provide charity care in compliance with the charity care policies reviewed and approved by the Department of Health. Kennewick General Hospital will use reasonable efforts to provide charity care in an amount comparable to or exceeding the average amount of charity care provided by hospitals in the Central Washington Region. Currently, this amount is 1.79% of gross revenue and 4.21% of adjusted revenue. Kennewick General Hospital will maintain records documenting the amount of charity care it provides and demonstrating its compliance with its charity care policies.

The proposed capital expenditure for this project is \$112,378,100

**A. Need (WAC 246-310-210)**

Based on the source information reviewed and with the applicant's agreement to the condition on page 4, the department determines that the applicant has met the need criteria in WAC 246-310-210(1) and (2).

1. The population served or to be served has need for the project and other services accessible to meet that need.

1987 Washington State Health Plan as guidance for projecting need for acute care beds. The 74 beds in this project to be relocated to the Southridge campus are currently licensed and in operation at the Auburn campus and patients are being admitted to these beds. Therefore, both Kennewick General Hospital and the department included them as CN approved beds and not as new beds being added to the existing supply. Therefore the department concludes that while a new health care facility would be established, it would not result in licensed acute care beds being added to the CN approved bed supply; therefore the numeric acute care bed need methodology is not applicable to this project.

a. In the case of a reduction, relocation, or elimination of a service, the need the population presently served has for the service, the extent which the need will be met adequately by the proposed relocation or by alternative arrangements, and the effect of the reduction, elimination, or relocation of the service on the ability of low-income persons, racial and ethnic minorities, women, handicapped persons, and other underserved groups and the elderly to obtain needed health care.

Since the applicant is proposing to move 74 beds and associated ancillary services approximately 3 miles from the existing Auburn campus, this criterion is relevant to the applicants proposed project. The applicant is moving the services from a downtown location in the City of Kennewick to a less developed urban growth area for the City of Kennewick. The applicant states that a primary characteristic of the Southridge property is its close proximity to two major highways serving the area. The applicant states that access to the new facility will be improved due to its location at the junction of the two major highways serving Benton County, Highway 395 and I-82. The project is also located within a 2,300 acre urban growth area for the city of Kennewick. This will provide easy access for patients using their personal vehicles. This area is currently served by the Ben Franklin Public Transit which provides van transportation for handicapped persons. KGH has submitted information that the project will be located in a growth area for Kennewick and that transportation access will be improved for all persons using the hospital facility. The Department concludes that the relocation of these hospital services is not expected decrease the accessibility of the services to patients currently served by KGH. This sub-criterion is met.

b. In the case of health services or facilities proposed to be provided, the efficiency and appropriateness of the use of existing services and facilities similar to those proposed;

KPHD is included in the Benton/Franklin Hospital Planning Area. KGH has defined its service area based upon the boundaries defined for the Kennewick Public Hospital

District. Included with KGH in the Benton/Franklin Hospital Planning Area are Kadlec Medical Center and Prosser Memorial in Benton County and Lourdes Medical Center in Franklin County. Kadlec Medical Center is licensed for 189 acute care beds, Prosser Memorial (critical access hospital) is licensed for 25 acute care beds, and Lourdes Medical Center (critical access hospital) is licensed for 25 acute care beds. In 2007 Benton County residents generated 61,625 acute care patient days. Of these patient days, 50,065 (81.2%) were provided in by the hospitals located in Benton/Franklin counties. The rest of the patient days, 11,560, (28.8%) were provided by hospitals located outside of the Benton/Franklin hospital planning area. In 2007 Franklin County residents generated 11,790 acute care patient days. Of these patient days, 6,855 (58.1%) were provided in hospitals located in Benton/Franklin Counties. [Source: CHARS data] The rest of the patient days 4,935 (41.8%) were provided by hospitals located outside of the Benton/Franklin hospital planning area. The retention of patients in Benton County is fairly high but there are additional patient days provided by hospitals outside the hospital planning area that the applicant could attract. There are additional patient days in Franklin County that the applicant could also attract to meet it patient day projections. The applicant has submitted data that would support some growth in patient days due to the population growth. The applicant has not demonstrated that the entire growth will occur due to population increase. When looking at a longer trend of KGH's historical patient days it shows a non linear trend. To achieve an annual average growth rate of 4.1 % the data would suggest that the applicant may have to increase their market share by up to 3%. There appears to be sufficient patient days provided by hospitals outside of the Benton/Franklin planning area to support an increase in market share. The Department concludes that KGH's patient day projections are obtainable. This sub-criterion is met.

2. All residents of the service area, including low-income persons, racial and ethnic minorities, women, handicapped persons, and other underserved groups and the elderly are likely to have adequate access to the proposed health service or services.

The Admission Policy provides the overall guiding principles of the facility as to the types of patients that are appropriate candidates to use the facility, and any assurances regarding access. The admission policies provided by the applicant demonstrate that patients would be admitted to the facility for treatment without regard to age, color, religion, sex national origin, handicap, or sexual preference, and will be treated with respect and dignity. [Source: KGH application Exhibit 7] All residents of the service area including low-income, racial, and ethnic minorities, handicapped and other underserved groups currently have access to services at KGH. The relocation of a part of the hospital is not expected to change this access.

To determine whether low income residents would have access to the proposed services, the department uses the facility's Medicaid eligibility or contracting with Medicaid as the measure to make that determination. To determine whether the elderly would have access to services, the department uses Medicare certification as the measure to make that determination. The facility is currently Medicare certified and Medicaid eligible. A review of the financial pro formas indicates that the project will not change this status

For charity care reporting purposes, the OHPDS, divides Washington State into five regions: King County, Puget Sound (less King County), Southwest, Central, and Eastern. KGH is one of 20 hospitals located within the Central Region. According to the 2003, 2004, and 2005 Charity Care Reports obtained from OHPDS, KGH has generally provided annual charity care less than the Central Region average for the respective years.

**Table 1  
EHMC Charity Care Comparison**

	<b>3-Year Average for Central Region</b>	<b>3-Year Average for KGH</b>
<b>% of Gross Revenue</b>	1.79%	1.29 %
<b>% of Adjusted Revenue</b>	4.21%	2.74%

The applicant’s pro forma revenue and expense statements indicate that the hospital will provide charity care at approximately 2.29% of gross revenue, or 5.50 of adjusted, which is higher than the average charity care provided in the region. RCW 70.38.115(2)(j) requires hospitals to meet or exceed the regional average level of charity care. [Source: July 7, 2008 Application, Exhibit 10]

KGH has historically provided significantly less charity care than the regional average. Because KGH does propose to exceed the regional average as identified above, a charity care condition for the hospital is necessary to approve the project.

KGH will provide charity care in compliance with the charity care policies provided in this Certificate of Need application, or any subsequent polices reviewed and approved by the Department of Health. KGH will use reasonable efforts to provide charity care in an amount comparable to or exceeding the average amount of charity care provided by hospitals in the Central Washington Region. Currently, this amount is 4.21% of adjusted revenue. KGH will maintain records documenting the amount of charity care it provides and demonstrating its compliance with its charity care policies.

With the applicant’s agreement to this condition, the department concludes this sub-criterion is met.

**B. Financial Feasibility (WAC 246-310-220)**

Based on the source information reviewed and with the applicant’s agreement to the terms on page 3, the department determines that the applicant has met the financial feasibility criteria in WAC 246-310-220

1. The immediate and long-range capital and operating costs of the project can be met.

Kennewick General Hospital is a District Hospital. The December 31, 2007 audited financial report for KGH shows:

**Table 2**  
**Kennewick Public Hospital District 2007 Actual**

<b>Assets</b>		<b>Liabilities</b>	
Current	\$22,368,552	Current	\$10,856,215
Board Designated	\$11,075,718	Long Term Debt	\$19,541,080
Prop./Plant/Equip.	\$29,941,461	Other	-
Other	\$7,206,240	Equity	\$40,194,676
<b>Total</b>	<b>\$70,591,971</b>	<b>Total</b>	<b>\$70,591,971</b>

[Source: CHS/Hospital and Patient Data Systems Dec 15, 2008 Report]

**Table 3**  
**Kennewick Public Hospital District 2014 Projected**

<b>Assets</b>		<b>Liabilities</b>	
Current	\$27,043,000	Current	\$14,383,000
Board Designated	\$43,277,000	Long Term Debt	\$109,142,000
Prop./Plant/Equip.	\$115,038,000	Other	-
Other	\$21,100,000	Equity	\$82,932,000
<b>Total</b>	<b>\$206,458,000</b>	<b>Total</b>	<b>\$206,457,000</b>

[Source: CHS/Hospital and Patient Data Systems Dec 15, 2008 Report]

**Table 4**  
**Kennewick-Southbridge**

Capital Expenditure	\$112,378,100
Beds/Stations/Other Unit	\$1,518,623
Total Capital per Unit	\$1,518,623
Percent of Total Assets	159.2%
Percent of Board Designated Assets	1,014.6%
Percent of Equity	279.6%

[Source: CHS/Hospital and Patient Data Systems Dec 15, 2008 Report]

“Kennewick General Hospital capital expenditure is projected to be \$112,378,100 or 159.2% of 2007 FYE total assets. The applicant indicates it will finance this project with a Washington Health Care Facilities Authority bond backed by the United States Department of Housing and Urban Development (HUD) using Section 242 (242 program) of the Title II National Housing Act. Due to rules of the 242 program, Kennewick must receive approval of the project from certain legal entities which include the C of N Program, before the 242 program can be used. Thus, there is no approval from HUD that can be included in the discussion and in addition the project has not been reviewed by the WHCFA. The analysis provided by HPDS staff assumes approval of the financing. Table 2, 3, and 4 illustrate the impact of this project on the Kennewick Public Hospital District” [Source: CHS/Hospital and Patient Data Systems Dec 15, 2008 Report]

“Review shows that while this project will have considerable impact on the hospital; this project will not adversely impact the financial health of the hospital if the patient volume is realized.” [Source: CHS/Hospital and Patient Data Systems Dec 15, 2008 Report] In the need section, the department evaluated the patient day projections because of the impact on the hospital if KGH does not achieve the projected patient volume and determined the projected patient days were obtainable.

“HPDS staff has also reviewed various ratios that can give a picture of the financial health of the hospital and the project. These ratios are shown in Table 5. The A means it is better if the hospital number is above the State number and B means it is better if the hospital number is below the state number. This part of the review assumes KGH patient day projections can be met. KGH long-term debt to equity ratio at the end of the 2007 fiscal year is 0.486 which is better than the 2007 state average of 0.527 as calculated using CHS/Hospital and Patient Data. The projections for this ratio are above the average which can happen with a major new project coming on line”.

**Table 5  
Kennewick General Hospital’s Financial Ratios**

Financial Ratio	Trend	State 07	KPHD07	Projected Year 1	Projected Year 2	Projected Year 3
Long Term Debt to Equity	B	0.527	0.486	1.539	1.490	1.316
Curr. Assets/Curr. Liab.	A	2.135	2.060	1.871	1.878	1.880
Assets Funded by Liab.	B	0.420	0.431	0.632	0.626	0.598
Oper. Exp./Oper. Rev.	B	0.948	0.962	1.027	1.010	0.990
Debt Service Coverage	A	6.199	3.862			

Long Term Debt to Equity	Long Term Debt/Equity
Current Assets/Current Liab.	Current Assets/Current Liabilities
Assets Funded by Liabilities	Current Liabilities +long term Debt/Assets
Oper. Exp./Oper. Rev.	Operating Expense/Operating Revenue
Debt Service Coverage	Net Profit+Depr. and Interest Exp. /Current Mat. LTD and Interest Exp.

The ratios are appropriate for a project like this. The Hospital will initially show a major shift in the ratios due to the capital expenditure, but the ratios should show a steady improvement in years 2 and 3 after the opening. Kennewick is projected to have a 1% profit margin in Year 3, which is acceptable. Kennewick financial health overall is average compared to other hospitals in Washington State [Source: CHS/Hospital and Patient Data Systems Dec 15, 2008 Report]. Based on the above analysis, this sub-criterion is met.

2. The costs of the project, including any construction costs, will probably not result in an unreasonable impact on the costs and charges for health services.

“Kennewick is similar to the statewide average”. [Source: CHS/Hospital and Patient Data Systems Dec 15, 2008 Report] Kennewick projections are included in Table 6:

**Table 6 Kennewick Southridge**

Rate per Various Items	2012 Con year 1	2013 Con year 2	2014 Con year 3
Patient Days	23,869	24,895	25,966
Adjusted Patient Days	52,830	54,753	56,751
Gross Revenue	\$264,156,000	\$273,778,000	\$283,762,000
Deductions From Rev.	\$154,315,000	\$159,904,000	\$165,702,000
Net Patient Billing	\$109,841,000	\$113,874,000	\$118,060,000
Other Oper. Revenue	\$2,972,000	\$3,039,000	\$2,816,000
Net Operating Revenue	\$113,967,000	\$118,101,000	\$122,100,000
Operating Expense	\$117,091,000	\$119,258,000	\$120,917,000
Operating Profit	(\$3,124,000)	(\$1,157,000)	\$1,183,000
Other Revenue	\$2,253,000	\$2,715,000	\$6,305,000
Net Profit	(\$871,000)	\$1,558,000	\$7,488,000
Operating Revenue per Patient Day	\$4,775	\$4,744	\$4,702
Operating Expense per Patient Day	\$4,906	\$4,790	\$4,657
Net Profit per Patient Day	(\$36)	\$63	\$288
Operating Revenue per Adj. Patient Days	\$2,079	\$2,080	\$2,080
Operating Expense per Adjusted Patient Days	\$2,216	\$2,178	\$2,131
Net Profit per Adj. Patient Days	(\$16)	\$28	\$132

[Source: CHS/Hospital and Patient Data Systems Dec 15, 2008 Report]

“Review of the data does not show unreasonable impact to the hospital or the community. The project costs to the patient and community are similar to current providers”. [Source: CHS/Hospital and Patient Data Systems Dec 15, 2008 Report]

This sub-criterion is met.

3. The project can be appropriately financed.

The applicant states tax exempt bonds would have been the best financing alternative for the project. However, in November of 2007, KGH went to the voters requesting approval of a 37-year levy to pay for operations and facilities so the hospital’s direct revenues could pay off \$132 million in revenue bonds to finance and build a 220,000 square-foot, 101 bed hospital at Southridge. The total cost of the replacement hospital excluding land, was estimated at \$140 million. Following the failure of the Bond issue, KPHD determined another attempt at voter approval would likely result in the same outcome.

After the levy failure, KGH immediately re-engaged in a process to define how much it could borrow absent voter obligated debt. Their analysis, supported by Merrill Lynch suggested that using FHA 242 financing KGH could support \$112 million in debt. After capitalized interest and debt service reserve requirements, this equated to approximately \$94 million; which was estimated to be sufficient to construct 168,000 square feet of

space - enough for 74 beds and the required ancillary and support services. This type of financing would result in the best rates for the hospital and the largest amount of funds available for actual construction. Accordingly, they downsized the project and now propose to relocate the medical/surgical services and ICU to the Southridge campus along with the establishment of a new emergency department. Women's and Children's services (27 beds) would remain at the Auburn location. The applicant has down sized the project from previous proposals submitted to the voters for tax funded debt.

The applicant is proposing to fund this current proposal using the FHA 242 mortgage program in conjunction with bonds issued by the Washington Health Care Authority for 90% of the project. The remaining 10% will be funded by hospital reserves. The FHA backed mortgage will allow the hospital district to issue AAA rated bonds. This is the first time this type of funding has been used by a Public Hospital District in Washington State. The applicant's legal counsel provided the following information regarding the method of funding for this project.

*“The District is specifically authorized under RCW 70.44.240 to establish a nonprofit corporation with another party and to lease its property to such nonprofit corporation. Mid Columbia is a nonprofit corporation under Washington state law created by the Foundation. Its purpose is to finance and develop health care facilities that will be leased to and operated by the District. While the District appoints up to two representatives to the Mid-Columbia board of directors, its representation constitutes a minority of the board.*

*The Foundation was formed in 1974 to engage in fundraising and related support activities for the Hospital and the District. While it supports the District's purposes, the Foundation is independent of the District and has a self-perpetuating board. The Foundation supports the District's plans to renovate and expand the Hospital, and offered to establish Mid-Columbia and provide other assistance in the ongoing operations of Mid-Columbia.*

*Mid Columbia as a nonprofit corporation has all of the powers granted under the Washington Nonprofit Corporation Act, Chapter 24.03 RCW. Specifically, these powers include the authority to mortgage property under RCW 24.03.035. Nothing in Chapter 70.44 RCW or Chapter 24.03 limits or restricts Mid-Columbia from engaging in the actions proposed. If the legislature intended to restrict the powers of an entity created under RCW 70.44.240, it would do so explicitly. For example, public hospital districts are authorized to join with other public agencies to create nonprofit corporations under the Interlocal Cooperation Act, Chapter 39.34 RCW. Nonprofit corporations created jointly under the Interlocal Cooperation Act, unlike those created under RCW 70.44.240, are limited to exercising the powers that both public agencies involved in their creation have the authority to exercise [RCW 39.34.030]. RCW 70.44.240 includes no such limitation. Given the specific authority granted to Mid-Columbia under RCW 24.03.035 and the lack of limitations placed on an entity authorized under RCW 70.44.240, any limitations on a public hospital district's ability to mortgage property do not apply to Mid-Columbia.” [Source*

November 5, 2008 letter from Foster Pepper PLLC Re: Proposal to Finance and Develop New Hospital Facilities].

In order to comply with state regulations and to facilitate completion of the HUD section 242 financing application for the Southridge hospital, several documents have been established. The following documents were provided in draft form as part of the application.

Ground Lease Agreement (Attachment 2)

This draft agreement is between Kennewick Public Hospital District (lessor) and Mid-Columbia Regional Healthcare (lessee). This draft agreement outlines the roles and responsibilities of each entity related to the lease of the Southridge facility and the new construction planned for the Southridge project. The duration of the lease is 25 years, with provisions for an extension of up to 10 years, and the lease amount is one dollar (\$1.00) a year for the duration of the lease.

Facilities Lease Agreement (Attachment 3)

This draft agreement is between Mid-Columbia Regional Healthcare (landlord) and Kennewick Public Hospital District dba Kennewick General Hospital (tenant). This is the leaseback agreement between the two entities. The leaseback agreement allows the hospital district to maintain operations and oversight of the hospital. It further outlines the obligation of Mid-Columbia to maintain the Southridge campus and to finance and construct a new hospital. The agreement is designed to be a ‘absolute net lease’ whereas all costs that Mid-Columbia realizes through performing its obligations as landlord (i.e.: insurance premiums, loan payments, financing costs) be passed through to the tenant for payment.

Given that these documents are in draft format, if this project is approved, the department would include a term that will require the applicant to provide a copy of all final, signed documents.

Mid-Columbia was registered with the Washington Secretary of State in December, 2008. In order for Mid-Columbia to be awarded the financing for the construction of the new hospital, several documents will need to be compiled upon approval of the Certificate of Need. The following documents will be necessary to be considered for the proposed financing.

Regulatory Agreement–US Department of Housing and Urban Development

The draft Regulatory Agreement is used by the US Department of Housing and Urban Development (HUD) as a loan application and is required by HUD to be completed before borrowing any funds. It outlines the roles and responsibilities of the borrower (Mid-Columbia) and lender (HUD). The final document is notarized and filed by the Federal Housing Commission. No draft Regulatory Agreement was included as part of this application.

Approval Covenants for HUD Section 242 Mortgage Insurance

The Covenants Approval document is used by HUD as an attachment to the Regulatory Agreement (above). It further outlines the roles and responsibilities of the borrower (Mid-Columbia) and lender (HUD). Attachments to the document include the hospital's 2008 balance sheet and statement of operations. Both of these financial documents are provided in the application and used by the applicant as a basis for preparing pro forma documents. No covenants were included as part of this application.

#### Rider to Regulatory Agreement for HUD Section 242 Mortgage Insurance

The draft Rider document is required to be added to the Regulatory Agreement (above) and outlines further responsibilities of the borrower (Mid-Columbia). It provides direction to the borrower for subsequent mergers, any affiliate transactions, and requires the establishment of a mortgage reserve fund. It further requires submission of specific annual financial reports, biannual business plan/consultant reports, quarterly construction reports, and annual independent audit reports. No covenant rider was included as part of this application.

Given that these documents are necessary for approval of the proposed financing, the applicant is tasked with completing the necessary application process to gain HUD approval for the proposed financing. If this project is approved, the Department would include terms that will require the applicant to provide a copy of all final, signed documents related to the HUD Section 242 financing outlined above.

Based on the documentation provided by the applicant during the review of this project, the following conclusions can be reached related to this sub-criterion.

- Mid-Columbia Regional Healthcare is a non-profit corporation as required under RCW 70.44.240.
- The Mid-Columbia Board of Directors includes representatives of the hospital district.
- The ground and facility lease agreements between the hospital district and Mid-Columbia are structured to ensure KPHD's ownership interest in the land and the new hospitals are protected.
- The district will maintain operational authority of the existing Auburn facility and intends to be responsible for the proposed Southridge facility.

After review of the information submitted by applicant and with agreement to the terms listed above the department concludes the form of financing is appropriate. This sub-criterion is met.

### **C. Structure and Process (Quality) of Care (WAC-246-310-230)**

Based on the source information reviewed, the department determines that the applicant has met the need criteria in WAC 246-310-230.

1. A sufficient supply of qualified staff for the project, including both health personnel and management personnel, are available or can be recruited.

The applicant reports that implementation of this project will require the addition of 9.9 positions and the reduction of 4.3 other positions associated with efficiencies related to the new physical plant. The applicant does not anticipate any difficulty in recruiting this small number of staff since KGH offers an excellent wage and benefit package that is competitive with other health care providers in the Tri-Cities and they also offer a number of training opportunities in conjunction with local colleges.

Based on the information provided in the application and the small number of additional staff required for implementation of this project, the department concludes that KGH will be able to recruit and retain the staff necessary for the new facility. [Source: Application pp40-42]. This sub-criterion is met.

2. The proposed service(s) will have an appropriate relationship, including organizational relationship, to ancillary and support services, and ancillary and support services will be sufficient to support any health services included in the proposed project.

The existing Auburn facility was originally constructed in 1952 with additions in 1977 and 1988. Beginning in 2005, KGH engaged in a nearly two year intensive planning process to calculate its space needs and plan for the future. In Early 2007, their architects determined that the current physical plant was 75% too small for even current volume levels. These size deficiencies by department are shown in Table 7.

**Table 7 2006 Space Shortages**

<b>Department</b>	<b>Percent Undersized for Current Volume</b>
Emergency	60 %
ICU	250%
Imaging	112%
Catheterization Laboratory	144%
Surgery	261%
Respiratory Therapy	71%
Laboratory	198%
Pharmacy	57%
Med./Surgical Inpatient Units	167%
Family Birth Center	102%

[Source: Application pg 20]

The new facility will double the space available to the hospital and those services with the greatest need for space will be moving to the new facility. Additionally, this will free up space in the existing facility for the Family Birth Center.

The applicant currently operates two separate facilities (Auburn campus and the KGH Medical Mall) as an integrated system under a single hospital license. These facilities are

located on two separate campuses and the Southridge project would be the third location under the same license. The ancillary and support services are currently designed to support not only the needs of the two inpatient facilities, but also the physician clinics, walk-in clinics, and urgent care operated by the Hospital District. The applicant is proposing to keep some of the departments at the existing Auburn campus and some will be transferred to the Southridge campus, but regardless of location the department will serve all of the other facilities. [Source: Application p42 and September 12, 2008 supplemental material pp6-7]. The information submitted by KGH demonstrates the need for improved ancillary and support services and that the project will address the relationship of these services to the overall project. This sub-criterion is met.

3. There is reasonable assurance that the project will be in conformance with applicable state licensing requirements and, if the applicant is or plans to be certified under the Medicaid or Medicare program, with the applicable conditions of participation related to those programs.

KGH will continue to provide Medicare and Medicaid acute care services to the residents of the service area. KGH had a Joint Commission inspection on August 11, 2008 and was accredited for 18 months. The facility was re-licensed in November 2008 based upon the successful completion of the Joint Commission inspection [Source: ILRS data provided by Office of Health Care Survey]. KGH also operates a Medicare certified home health agency under the hospital license. The home health agency is also JCAHO accredited. Within the last two years, the Department of Health's Office Health Care Survey (OHCS), which surveys hospitals within Washington State, has completed one compliance Survey for the hospital. The hospital survey revealed minor non-compliance issues typical of a hospital, and KGH submitted a plan of correction for the non-compliance issues within the allowable response time. Documentation provided by the applicant and DOH's Office of Health Care Survey indicates there is reasonable assurance that the project will be in conformance with applicable licensing and certification requirements. This sub-criterion is met.

4. The proposed project will promote continuity in the provision of health care, not result in an unwarranted fragmentation of services, and have an appropriate relationship to the service area's existing health care system.

With this project, KGH anticipates that it will improve the overall operation of the hospital by providing replacing double bed rooms with single bed rooms, increasing the size of ancillary and support services to current standards to better serve the patients and accommodate new technology, and to more efficiently coordinate inpatient and outpatient services provided by the hospital. The applicant currently shares services between the various physician offices and other facilities operated by the Hospital District and the improvements to the ancillary services provided by the KGH should be of benefit to all the providers in Kennewick area. This project will promote the continuity of care provided in the applicant's facility. This sub-criterion is met

5. There is reasonable assurance that the services to be provided through the proposed project will be provided in a manner that ensures safe and adequate care to the public to be served and in accord with applicable federal and state Laws, rules, and regulations.

This sub-criterion is addressed in sub-section 3 above.

#### **D. Cost Containment (WAC 246-310-240)**

Based on the source information reviewed and with agreement to the term on page 3 of this analysis, the department determines that the applicant has met the cost containment criteria in WAC 246-310-240.

1. Superior alternatives, in terms of cost, efficiency, or effectiveness, are not available or practicable.

The applicant evaluated two other different options before selecting the option of moving 74 existing beds and constructing a new facility for part of the inpatient services.

The first option was going back to the voters for the funding to build an entire replacement hospital. This option has been voted down twice and follow-up information gathered by the applicant indicated that this process was not likely to succeed.

The second option which the applicant reports that was explored thoroughly by their architect and hospital planning team had a number of significant draw-backs. The current Auburn site is land locked and not of suited for further expansion, the option was estimated to cost substantially more (\$144,000,000 for construction excluding financing costs) than the option chosen in this application. There is a potential in this option for major disruption to the provision of services during the remodeling and new construction activities. The facility will require upgrading of space and structural requirements to new building code requirements [Source November 21, 2008 letter from Peterson Kolberg & Associates, A.I.A., P. C.].

The third option was various configurations of a two campus 101 bed hospital. The advantages to the third option based on the information provided by the applicant are:

- Lower projected construction costs for this alternative versus remodeling
- Lower site preparation costs versus using the Auburn campus
- Consistent useful life span for building using this alternative
- Relocating the new facility to a larger site offering more flexibility for future development. [Source Nov. 21, 2008 letter from Peterson Kolberg & Associates, A.I.A., P. C.]

Based on the information submitted the Department concludes the third option is the best available alternative. This sub-criterion is met.

2. In the case of a project involving construction:

a. The costs, scope, and methods of construction and energy conservation are reasonable;

The total capital cost for the 74 beds at Southridge is \$112,378,100 which results in a cost per bed of \$1,518,622.97. HPDS staff report that this cost per bed is comparable to past construction costs reviewed by their office. Construction costs can vary quite a bit due to type of construction, quality of material, custom versus standard design, building site and other factors. KGH will fully evaluate alternative methods of energy consumption to determine the safest, most reliable, and most economical method available over the long-term. [Source: application pg. 49].

This project requires either an environmental impact statement (EIS) or a declaration of non-significance. The applicant has submitted a letter dated August 28, 2008 from the City of Kennewick with the following information:

“An Environmental Impact Statement was prepared for the Southridge Sub-area and approved by Resolution 07-02, Southridge Sub-area Mitigation Documents for ED 07-18. Since your proposed project consistent with the Southridge Sub-area plan it will be possible to adopt the previous Environmental Impact Statement to satisfy SEPA requirements.”

This information and with the applicant’s agreement the term below, the department concludes the Certificate of Need EIS requirements will be met.

Prior to commencement, KGH must submit a copy of the approval letter or other documentation to show adoption of the previous environmental impact statement (EIS) as referenced in the letter dated 8/26/08 from the City of Kennewick.

Based on the information reviewed and with the above term, the Department concludes this project’s construction costs are reasonable. This sub-criterion is met.

b. The project will not have an unreasonable impact on the costs and charges to the public of providing health services by other persons.

Kennewick General Hospital while noting that having two campuses will cause some duplication of effort, stated that the new facility will be designed from the beginning to have functional and operational efficiencies. This sub-criterion is also evaluated within the financial feasibility criterion under WAC 246-310-220(2). This sub-criterion is met.