

**EVALUATION OF THE CERTIFICATE OF NEED APPLICATION SUBMITTED
ON BEHALF OF KENNEWICK HOSPITAL DISTRICT PROPOSING TO LEASE
HOSPITAL PROPERTY TO MID-COLUMBIA REGIONAL HEALTHCARE,
WHILE RETAINING KENNEWICK GENERAL HOSPITAL AS THE
LICENSED OPERATOR OF THE FACILITY**

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's current facility is located at 900 South Auburn and is licensed for 101 acute care beds. KGH holds a three year accreditation from the Joint Commission on Accreditation of Health Care Organizations. In addition to the Auburn facility, KPHD owns and operates Kennewick Home Health Services, Benton Franklin Elder Services, and the KGH Medical Mall. Inpatient services currently provided at KGH include medical-surgical services, emergency services, pediatric and obstetrical services, intensive and critical care units, neurological services, diagnostic services, and physical therapy.

Currently, KGH has a separate application under review which proposes to construct a second hospital (Southridge) in the planning area. This separate application proposes to construct a Southridge campus and to transfer 74 acute care licensed beds from the Auburn campus. Upon completion of that 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 continue to provide women and children's services, (maternity, pediatric, and normal newborn Level I nursery services¹) urgent care, speech pathology, physical therapy, and outpatient education. The Medical Mall would continue to offer ambulatory services, physician practices, outpatient surgery, outpatient imaging, GI services, and pharmacy. [Program records; Application, p8]

The application reviewed in this evaluation proposes to lease the current real hospital property held by KPHD to Mid-Columbia Regional Healthcare (Mid-Columbia); who will then sub-lease the facility back to KGH as the licensed operator. Mid-Columbia has been established by the Kennewick General Hospital Foundation as a separate legal entity. The separate Ground and Facilities leases obligate Mid-Columbia to maintain the Auburn facility and to construct the proposed Southridge campus described above. The arrangement will result in Mid-Columbia holding a lease to the land held by KPHD for two separate hospital sites while retaining KGH as the licensed operator of each facility. There is no capital expenditure associated with this project. [Application, p2]

APPLICABILITY OF CERTIFICATE OF NEED LAW

This project is subject to Certificate of Need (CN) review because it is the lease of an existing hospital under Revised Code of Washington (RCW) 70.38.105(4)(b) and Washington Administrative Code (WAC) 246-310-020(1)(b).

¹ As detailed in DOR 08-23 released April 23, 2008

CRITERIA EVALUATION

To obtain Certificate of Need approval, Kennewick Hospital District must demonstrate compliance with the criteria found in WAC 246-310-210 (need); 246-310-220 (financial feasibility); 246-310-230 (structure and process of care); and 246-310-240 (cost containment).²

APPLICATION CHRONOLOGY

May 30, 2008	Letter of Intent Submitted
October 1, 2008	Application Submitted
October 2, 2008 through December 17, 2008	Department's Pre-Review Activities <ul style="list-style-type: none">• Screening responses
December 18, 2008	Department Begins Review of the Application
January 7, 2009	End of Public Comment / No Public hearing
February 12, 2009	Department's Anticipated Decision Date
February 4, 2009	Department's Decision Date

AFFECTED AND INTERESTED PERSONS

Throughout the review of this project, no entities sought or received affected person status under WAC 246-310-010.

SOURCE INFORMATION REVIEWED

- Kennewick Hospital District's Certificate of Need Application submitted October 1, 2008
- Kennewick Hospital District's supplemental information dated December 8, 2008
- Comments received at the Certificate of Need Program office
- Historical charity care data report and supplemental obtained from the Department of Health's program of Hospital and Patient Data Systems (2004, 2005, and 2006 summaries)
- Financial feasibility and cost containment evaluation prepared by the Department of Health's Office of Hospital and Patient Data Systems received January 26, 2009
- Licensing and/or survey data provided by the Department of Health's Office of Health Care Survey
- Data obtained from the internet regarding Kennewick Hospital District (www.kennewickgeneral.com)
- Data obtained from the internet regarding the Washington State Health Care Facilities Authority (www.whcfa.wa.gov)
- Data obtained from the internet regarding FHA section 242 (<http://portal.hud.gov> & www.raconline.org)

² 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(1), (3), (4), (5), (6) and WAC 246-310-240(2) and (3).

CONCLUSION

For the reasons stated in this evaluation, the application submitted by Kennewick Public Hospital District dba Kennewick General Hospital proposing to enter into an arrangement with Mid-Columbia Regional Healthcare to lease the hospital at 900 Auburn Street 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 following terms and condition stated below.

There is no capital expenditure proposed for this project.

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.

CONDITION

- 1) KGH will provide charity care in compliance with the charity care policies provided in this Certificate of Need application, or any subsequent policies 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 1.79% of gross revenue and 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.

A.Need (WAC 246-310-210)

Based on the source information reviewed and with the applicant's agreement to the condition on page 3, the department determines that the applicant has met the need criteria in WAC 246-310-210(2).

- (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.

KGH is currently a provider of health care services to residents of Washington State, including low-income, racial and ethnic minorities, handicapped and other underserved groups. As an acute care hospital, KGH also currently participates in the Medicare and Medicaid programs. To determine whether all residents of the service area would continue to have access to an applicant's proposed services, the department requires applicants to provide a copy of its current or proposed admission policy. 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 to treatment.

To demonstrate compliance with this sub-criterion, KGH provided a copy of its current Patient Rights and Responsibilities and its Non-Discrimination Policy that would also be used at Southridge. The policy states the process that KGH will use to admit patients for treatment or care at the hospitals. The policy also states that any patient requiring care will be accepted for treatment at KGH without regard to race, ethnicity, religion, national origin, citizenship, age, sex, pre-existing condition, physical or marital status, insurance status, economic status, or the ability to pay for medical services. [Application, Exhibit 6]

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 or continue to have access to the proposed services, the department uses Medicare certification as the measure to make that determination.

KGH currently provides services to Medicare and Medicaid eligible patients. Documents provided in the application demonstrate that KGH intends to maintain this status. For this project, a review of the policies and data provided for KPHD facilities identifies the financial resources as including both Medicare and Medicaid revenues [Application, p18 & December 8, 2008 Supplemental Information, Appendix 7]

A facility's charity care policy should confirm that all residents of the service area including low-income, racial and ethnic minorities, handicapped and other underserved groups have, or would have, access to healthcare services of the applicant. The policy should also include the process one must use to access charity care at the facility.

KGH demonstrated its intent to continue to provide charity care to residents by submitting its charity care policy that outlines the process a patient would use to access this service. Further, Kennewick Hospital District included a 'charity care' line item as a deduction from revenue within the pro forma financial documents for Kennewick. [December 8, 2008 Supplemental Information, Appendix 6 & 7]

For charity care reporting purposes, the Department of Health’s Hospital and Patient Data Systems program (HPDS), divides Washington State into five regions: King County, Puget Sound (less King County), Southwest, Central, and Eastern. Kennewick is located in Richland County and one of 21 hospitals located within the Central Washington Region. According to 2004-2006³ charity care data obtained from HPDS, Kennewick has historically provided significantly less than the average charity care provided in the region. Kennewick’s most recent three year percentage of charity care for gross and adjusted revenues is detailed in Table 1 below. [HPDS 2004-2006 charity care summaries]

**Table 1
Kennewick Public Hospital District Charity Care Comparison**

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

The applicant’s combined 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. [December 8, 2008 Supplemental Information, Appendix 7]

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 policies 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 that all residents, including low income, racial and ethnic minorities, handicapped, and other under-served groups would have access to the services provided by the hospital. 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), (2), and (3).

³ Year 2007 charity care data is not available as of the writing of this evaluation.

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

This project proposes a lease and lease-back arrangement. The estimated capital expenditures are expected to be zero. To assist the department in its evaluation of this sub-criterion, Office of Hospital and Patient Data Systems (HPDS) provided a review of the project. Below is the HPDS summary of the December 31, 2007 audited financial report for KPHD and a projection of the balance sheet for 2014. [HPDS analysis, p2]

Table 2
Kennewick Public Hospital District 2007 Actual ⁴

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

Table 3
Kennewick Public Hospital District 2014 Projected ⁵

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

As HPDS reiterates, “The applicant indicates that the overall construction project related to this CN will be financed with a Washington Health Care Facilities Authority (WHCFA) 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 includes CN, before the 242 program can be used. Thus there is no approval from HUD that can be included in the discussion. The WHCFA has not ruled on this application either. The applicant, based on their balance sheet projections on it retaining the assets within the District and not the Mid-Columbia non profit corporation. The applicant plans to use Mid-Columbia as a carrier of the debt and little else. The District will make lease payments to Mid-Columbia that equal the debt payment and Mid-Columbia will make the debt payment. This analysis assumes the legality of this plan. This analysis also assumes the financing will be approved”. HPDS also notes that, while this project will have a considerable impact to the hospital, this project will not adversely impact the financial health of the hospital if the patient volume is realized. [HPDS analysis, p2]

⁴ Audited 2007 Kennewick Public Hospital District Report

⁵ Compiled from CN application end of 3rd yr

To further assist in the review, HPDS provides a summary of the short and long-term financial feasibility of the project, which includes a financial ratio analysis. The analysis assesses the financial position of an applicant, both historically and prospectively. The financial ratios utilized are 1) long-term debt to equity ratio; 2) current assets to current liabilities ratio; 3) assets financed by liabilities ratio; 4) total operating expense to total operating revenue ratio; and 5) debt service coverage ratio. If a project's ratios are within the expected value range, the project can be expected to be financially feasible.

For Certificate of Need applications, HPDS compares the applicant's projected ratios with the most recent year's financial ratio guidelines for hospital operations. For this project, HPDS uses 2007 data for comparison.

As described by HPDS, "This part of the review assumes Kennewick patient day projections can be met. Kennewick Hospital Long-Term Debt to Equity Ratio at the end of 2007 fiscal year is .486 which is better than the 2007 state average of .527 as calculated by CHS⁶/Hospital and Patient Data". HPDS also reviewed various ratios that can give a picture of the financial health of the hospital and the project. Important ratios used by Certificate of Need are listed below. The ratios are for Kennewick Hospital District as a whole. [HPDS analysis, p3]

Table 4
Kennewick Public Hospital District Projected Debt Ratios ⁷

Ratio Category	Trend	State07	KPHD07	2012 CONy1	2013 CONy2	2014 CONy3
Long Term Debt to Equity	B	0.527	0.486	1.539	1.490	1.316
Current Assets/Current Liabilities	A	2.135	2.060	1.871	1.878	1.880
Assets Funded by Liabilities	B	0.420	0.431	0.632	0.626	0.598
Operating Expense/Operating Revenue	B	0.948	0.962	1.027	1.010	0.990
Debt Service Coverage	A	6.199	3.862			

As HPDS summarizes, "The ratios are appropriate for a project like this. Kennewick is projected to have 1% profit margin in Year 3, which is acceptable. Kennewick's financial health overall is average compared to other hospitals in Washington State".

Based on the information above, the department concludes that the immediate and long-range operating costs of the project can be met and 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.

As stated in the project description section of this evaluation, KPHD intends to initially maintain all current services at KGH after the lease. After the completion of the Southridge campus, 74 beds will be moved from the Auburn facility and a number of services will be

⁶ Center for Health Statistics

⁷ 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.

redistributed between the two campuses. As indicated in the projections below in Table 5, KPHD does not intend to increase charges for health services to make a net profit in year three. HPDS determined the costs and charges are reasonable and comparable. [HPDS analysis, p4]

**Table 5
KPHD Patient Rates Forecast**

Rate per Various Items	2012 CONyr1	2013 CONyr2	2014 CONyr3
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 Revenue	\$ 154,315,000	\$ 159,904,000	\$ 165,702,000
Net Patient Billing	\$ 109,841,000	\$ 113,874,000	\$ 118,060,000
Other Operating 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. Pat Days	\$ 2,079	\$ 2,080	\$ 2,080
Operating Expense per Adj. Pat Days	\$ 2,216	\$ 2,178	\$ 2,131
Net Profit per Adj Pat Days	\$ (16)	\$ 28	\$ 132

Based on the information provided above, the department concludes that the cost of the project will not result in an unreasonable impact on the costs and charges for health services within the service area. This sub-criterion is met.

(3) The project can be appropriately financed.

There is no estimated capital expenditure for this project. Financing for the project will be obtained by Mid-Columbia and operation of the hospitals will continue to be by KGH through a lease with Mid-Columbia; described in more detail below. This arrangement allows the hospital district to continue operations and oversight of the hospitals. The lease arrangement also allows Mid-Columbia to obtain funding for the project from the Washington Healthcare Facilities Authority. Under this proposal, the funds would be FHA insured during the duration of the loan.

The applicant provided a legal review of the proposed financing package which addressed uncertainty regarding a public hospital district's authority to grant a mortgage on its ownership interest in real property. The arrangement described in this evaluation is intended

to allow Mid-Columbia to finance a significant portion of the construction for the Southridge campus through tax exempt bonds issued by the Washington Healthcare Facilities Authority.⁸ The bond issue is to be secured through a mortgage loan insured by the U.S. Department of Housing and Urban Development acting through the Federal Housing Commissioner pursuant to Section 242 of the National Housing Act.⁹ The inclusion of Mid-Columbia, under controlling interest by KGH, is intended to allow compliance with state limitations on the mortgaging of hospital district property¹⁰ and to comply with HUD 242 program rules. [HUD website; Application, p2; December 8, 2008 Supplemental Information, Attachment 1]

The legal review of the proposed financing arrangement states,

“Under the proposed financing plan, The [Washington Healthcare Facilities] Authority will issue tax-exempt bonds and loan the proceeds of the bonds to Mid-Columbia to be used by Mid-Columbia to pay the costs of the project”. The review continues, “Due to uncertainty regarding a public hospital district’s authority to grant a mortgage on it’s ownership interest in real property, the Kennewick General Hospital Foundation created Mid-Columbia for the purpose of leasing the Southridge land and the Auburn land and improvements, financing the construction of new improvements at Southridge using the FHA 242 Program and leasing the existing and new improvements back to the district for its operation of the Hospital. This structure promotes the development and maintenance of hospital facilities of public agencies, provides certain protection to the leasehold mortgage while the debt is outstanding and preserves the public agency’s ultimate ownership in the land and improvements”. [December 8, 2008 Supplemental information, Attachment 1]

In addition to evaluating whether the project can be appropriately funded as required under this sub-criterion, an evaluation of whether the proposed funding arrangements are appropriate is also necessary. Revised Code of Washington (RCW) 70.44.240 allows a hospital district to enter into a contract with another entity to acquire, own, operate, manage, or provide hospital services. If this type of contract is executed, it must do so through a legally established non-profit corporation. The governing body of the non-profit corporation must include representation from the hospital district, which may include commissioners. Further, if this type of contract is executed, the non-profit entity may sell or lease property to another legal entity to carry out the hospital’s mission.

To comply with RCW 70.44.240 above, the hospital district entered into a contract with Mid-Columbia. Mid-Columbia is a Washington State Non-profit Corporation governed by 5-member board of directors with direct ties to KPHD. The applicant included documentation from Benton County establishing KPHD’s ownership of the site. [Application, p1 & Exhibit 3; December 8, 2008 Supplemental Information, Addendum to responses]

⁸ The Washington Health Care Facilities Authority was created by Legislature in 1974 to provide a new source of capital funding for modern, well equipped, and reasonably priced health care facilities. The goal of minimizing capital costs is accomplished by offering tax exempt financing to nonprofit health care facilities.

⁹ The purpose of this Federal Housing Administration 242 program is intended to provide hospitals access to affordable financing for capital projects. Uses may include new construction, refinancing, modernization, remodeling, equipment, and expansion.

¹⁰ Applicable portions of RCW 70.44

The legal review also addresses whether hospital districts have the authority to execute the lease and leaseback transaction. A portion of the summary pertinent to this project is restated below. [December 8, 2008 Supplemental Information, Attachment 1]

“The district has determined that it is in the best interests of the residents of the district to modernize and expand the hospital. In order to complete the project in the most economical manner while protecting district assets, the district intends to lease the land and existing improvements to [Mid Columbia], which will mortgage its leasehold interest in order to finance and build the needed improvements. The District and [Mid Columbia] have the explicit authority to execute these transactions pursuant to Revised Code of Washington 70.44.240 and 24.03.035 respectively.”

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

Ground Lease Agreement (Exhibit 3)

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 Auburn 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 (Exhibit 4)

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 Auburn 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.

Based on the information provided above and with the applicants' agreement to the terms outlined above, the department concludes that the project can be appropriately financed. 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 structure and process (quality) of care criteria in WAC 246-310-230(1), (2), (3), (4), and (5).

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

The proposed project does not anticipate an elimination of any services or staff as a result of this project. The applicant outlines a redistribution of services among the two facilities that will result, and that support and technical services will be able to effectively support all of the hospital facilities. [Application, Exhibit 4; December 8, 2008 Supplemental Information, p5-6]

KPHD maintains a 7-member Board of Commissioners to oversee the governance of the hospital and has provisioned a 5-member Board of Directors to oversee operations of Mid-Columbia Regional Healthcare. [Application, p42; December 8, 2008 Supplemental information, Addendum to responses]

Based on documents provided in the application, the department determines 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 applicant states “KGH has community linkages that are long standing and well developed. KGH staff have historically worked with patients, family members and physicians to keep them informed of other services”. The applicant continues, “KGH also has a proven history of collaborating and working closely with the two other acute care hospitals in the Tri-Cities – Lourdes and Kadlec to address regional healthcare needs”. KPHD does not anticipate any change in these relationships as a result of this financing arrangement. [Application, p23]

The department concludes that there is reasonable assurance that Kennewick Hospital District will continue to maintain the necessary relationships with ancillary and support services to provide healthcare in the communities. Approval of this project would not negatively affect these relationships. 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.

Kennewick General Hospital will continue to provide Medicare and Medicaid services to the residents of Benton County and surrounding communities.

The Department of Health’s Office of Health Care Survey (OHCS) last completed a survey at the Auburn facility in 2007.¹¹ There were minor policy and procedure issues noted and a correction plan was presented and approved by the department. [Facility survey data provided by the Office of Health Care Survey]

Based on the historical compliance history of Kennewick General Hospital, there is reasonable assurance that the existing hospital would continue to operate in conformance with applicable state and federal licensing and certification requirements. This sub-criterion is met.

¹¹ Survey completed March 22, 2007.

- (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.

Kennewick General Hospital is a 101-bed hospital in Benton County. The hospital provides acute care and general health care services to the residents of Benton County and the surrounding communities.

Continuity in the provision of health care will be accomplished with the continued operation of Kennewick General Hospital at 900 Auburn Street throughout the efforts to secure this financing proposal as well as after the proposed Southridge campus is constructed. Further continuity will be accomplished after the new facility is operational as it will offer the same services in an updated environment. [Application, p23]

Based on the above information, the department concludes that Kennewick General Hospital will continue to promote continuity in the provision of health care services in the community. 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, the department determines that the applicant has met the cost containment criteria in WAC 246-310-240 (1).

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

The applicants provided the background information related to the proposed construction of a new Southridge facility. After an unsuccessful effort to have the residents within the district vote to back a bond issue with tax-payer funds, KPHD considered two alternatives.

- (a) Make a second attempt to gain voter approval for the funds necessary for a replacement hospital or a smaller partial replacement project.
- (b) Delay the project until market conditions and/or KGH's financial position allow for an improved AAA rating without the FHA guarantee.

In reference to alternative (a), the applicant states, "KGH respects the decision of the voters. Follow-up interviews and public comment demonstrated that while the voters overwhelmingly understood the need and are supportive of KGH, they were unwilling to obligate themselves to a tax of the scope and length needed to support a project of the size that is required". KGH also states that the deterioration of the economy since the original vote would make it even more difficult to gain voter approval.

In the applicant's analysis of alternative (b), KGH considered the current needs of the community. KGH concluded, "Our facility has surpassed its useful life and does not meet current care delivery standards". They continue, "Because of the limitations of the current

site, many departments that should be adjacent to each other for both optimal patient care and efficiency are not (i.e.: emergency and surgery). Every nursing unit and nearly every ancillary department is undersized for current volumes. The hospital's infrastructure (heating, cooling, ventilation, etc.) is beyond its useful life, and the building configuration and original construction types make it cost prohibitive in some instances to remodel for new medical technology and equipment". The applicant included an internal analysis of the current physical plant and determined that it was too small for current volumes. The analysis includes a look at specific departments of the facility and concludes that the current physical plant is 75% too small to accommodate current volumes. As a result, the applicant concluded that without the Southridge campus, the hospital's financials will stagnate making it difficult to obtain the rating necessary to secure the funds for the expansion.

With these factors considered, the project proposed in this application is viewed by the Department to be the best available option. With acceptance of the conditions above, this criterion is met.