

IN THE MATTER OF

BEFORE THE

CARROLL HOSPITAL CENTER

MARYLAND HEALTH

DOCKET NO. 12-06-2330

CARE COMMISSION

REQUEST TO MODIFY CERTIFICATE OF NEED

I. INTRODUCTION

Approved Project

In June of this year, Carroll Hospital Center (“CHC”) was authorized to make a capital expenditure to develop a comprehensive community oncology center connected to and including renovated space in the existing Richard N. Dixon Building which is connected to the hospital. The project will involve new construction of 42,546 square feet (“SF”) in a structure which will connect to the Dixon Building at the first floor level and renovation of 25,555 SF of Dixon Building space on this level. Conference and education space and space for CHC’s Complementary Health Program (a suite of services including massage, meditation, and other therapies and healing practices often referred to as “alternative medicine”) will be accommodated in portions of the renovated space included in this project. The project will have a ground floor of new construction totaling 12,340 SF that will house mechanical and electrical systems, receiving and storage, and service space. It will also include a small second floor space (3,184 SF) with an elevator lobby and 1,900 SF of shell space.

The replacement facility will concentrate radiation and hematology/oncology treatment in the new construction component, which will include a replacement linear accelerator and a second linear accelerator vault and a CT simulator for radiation therapy. It will contain 18 spaces for infusion therapy, physician offices, a pharmacy, nine exam rooms, and staff support offices, locker, lounge, and support spaces. The main lobby, reception, and waiting area will also be included in the new construction. The renovated space adjoining the new construction will primarily house the Wellness/Education Center facilities being added and space for use in providing complementary health services,

This project replaces the 13,250 SF Carroll Regional Cancer Center operated by CHC at 555 South Center Street.

The total approved cost of the project is \$27,975,000, consisting of \$26,482,776 in capital costs, an inflation allowance of \$1,442,224, and \$50,000 in consulting fees. CHC identified two funding sources for this project in its approved application: \$17,975,000 in cash and \$10 million in donated funds.

The project was approved with four conditions:

1. Carroll Hospital Center will not finish the shell space without giving notice to the

Commission and obtaining all required Commission approvals.

2. Carroll Hospital Center will not obtain or request an adjustment in rates or its revenue cap by the Health Services Cost Review Commission (“HSCRC”) that includes depreciation or interest costs associated with construction of the proposed shell space until and unless Carroll Hospital Center has filed a CON application involving the finishing of the shell space, has obtained CON approval for finishing the shell space, or has obtained a determination of coverage from the Maryland Health Care Commission that CON approval for finishing the shell space is not required.
3. The HSCRC, in calculating future rates or revenue caps for Carroll Hospital Center and its peer group, shall exclude the capital costs associated with the shell space until such time as the space is finished and put to use in a rate-regulated activity. In calculating any rate that includes an accounting for capital costs associated with the shell space, HSCRC shall exclude any depreciation of the shell space that has occurred between the construction of the shell space and the time of the rate calculation (i.e., the rate should only account for depreciation going forward through the remaining useful life of the space). Allowable interest expense shall also be based on the interest expenses going forward through the remaining useful life of the space.
4. Any future change to the financing of this project involving adjustments in rates or revenue caps set by the Health Services Cost Review Commission must exclude \$976,287 associated with the excess construction cost, and portions of the contingency and inflation allowance estimated for the project.

Modified Project

CHC now estimates that the capital costs of this project will be \$3 million more than the approved \$26.5 million, based on discussions with contractors as it moves toward issuance of a Request for Proposals from contractors seeking a guaranteed maximum price contract. It cites two causes for this 11.3% increase in capital costs. First, final material selections and construction plans have increased the cost estimate. CHC states that the CON application cost estimate was based on concept drawings “still going through design changes.” Secondly, CHC states that an Interior Design Team working on the design of the project “decided it was important to select substantial finish materials that provided a longer life expectancy and required less maintenance than the materials we (CHC) have used on past projects.” The team and CHC leadership concluded “that the additional cost was an investment that would provide sustained quality, reduced maintenance costs and improved patient safety and comfort.”

Staff asked CHC to provide more specifics with regard to the longer-term savings associated with this decision for more expensive finish material choices. The hospital’s response is appended to this report.

The new estimate of the project cost totals \$30,975,000, consisting of \$29,482,776 in

capital costs, the same inflation allowance of \$1,442,224, and the same \$50,000 in consulting fees. The same two funding sources for this project are anticipated with \$20,975,000 in cash being provided by the hospital and \$10 million in donated funds.

No significant changes in the physical plant design approved for the project have been identified.

II. STAFF REVIEW AND ANALYSIS: PROPOSED MODIFICATION

Requirements for Project Modification

Commission regulations at COMAR 10.24.01.10 and .17 require Commission approval of changes to projects approved through the Certificate of Need program. Specifically, Commission approval is required if any of five specified changes to a project is proposed before project implementation. These changes are:

- (1) Significant changes in physical plant design;
- (2) Capital cost increases that exceed the approved capital cost inflated by an amount determined by applying the Building Cost Index published in *Health Care Cost Review* from the application submission date to the date of the filing of a request for approval of a project change;
- (3) Total expense or revenue increases which exceed the approved expenses or revenues inflated by 10 percent per year;
- (4) Changes in the financing mechanisms of the project; and/or
- (5) A change in location or address of the project.

COMAR 10.24.01.17C describes three types of changes to a project that are impermissible, and would require Commission review and approval as a new CON project:

- (1) A change in the fundamental nature of facilities or services to be provided in the facility from those that were approved by the Commission;
- (2) An increase in the total licensed bed capacity or medical service categories from those approved; and
- (3) Changes requiring extensions of time to meet the applicable performance requirements specified under Regulation .12, except as permitted under Regulation .12E of this chapter.

In this case, CHC is proposing a change in the approved capital cost that exceeds the approved capital cost inflated by an amount determined by applying the Building Cost Index published in *Health Care Cost Review* from the application submission date to the date of the filing of a request for approval of a project change. This index would only allow a cost increase of approximately \$220,000 for this recently approved project. That is the only change in the project requiring Commission approval. No impermissible changes are proposed

Construction Costs

At the time of the CON approval, Commission Staff analyzed the original proposed construction costs compared to building cost benchmarks derived from Marshall Valuation Service (MVS) guidelines, as required by COMAR 10.24.10. These comparisons indicated that the proposed cost per square foot for the new construction, as appropriately adjusted for certain characteristics of the project, were above the MVS benchmark for a project of this type by \$21.49 per square foot. (See Condition #4 as outlined in the Introduction.)

Commission Staff compared the modified costs to current costs for comparable new construction in the applicable region of Maryland according to MVS. Only costs associated with the design and construction of the buildings are used in calculating project costs for MVS purposes and adjustments are allowed for extraordinary costs. This analysis indicates that the new estimated cost per square foot for the new construction continues to be above the MVS benchmark for a hospital project of this type, by \$49.71

The State Health Plan, at COMAR 10.24.10, requires that all construction costs that exceeds the SHP standard for hospital construction cost be financed by means other than rate increases. For this reason, the June, 2012 CON included a condition excluding the \$976,287 in excess construction costs from any future rate adjustment by the HSCRC. That condition should be modified, as follows, based on the modified project cost:

Any future change to the financing of this project involving adjustments in rates or revenue caps set by the Health Services Cost Review Commission must exclude \$2,306,775 associated with the excess construction cost, and portions of the contingency and inflation allowance estimated for the project.

III. SUMMARY AND STAFF RECOMMENDATION

Carroll Hospital Center has requested Commission approval of a modification to its Certificate of Need (Docket No. 12-06-2330), effective June 21, 2012.

Essentially, this is a project approved at a point in time when final design and finish decisions had not yet been finalized. It appears very likely, given the history of this project, that if more such decisions had been made earlier and their cost impact incorporated in the project cost estimates at the time this project was reviewed in the Spring of 2012, the CON would have still been approved. This finding rests on the fact that the benefits identified for this project, which included an appropriate upgrade of radiation therapy equipment and needed additions of space for cancer therapies based on growth in patient volume, would have still been present and the marginally higher construction cost estimate would only have had the effect of altering the excess cost excluded for purposes of any future request for project-related rate adjustment (or, in the case of this hospital, an increase in its revenue cap). At the time this project was reviewed, it appeared unlikely that any path to action by HSCRC to assist in paying for this project was likely to become available and that is still the case. There are no changes in the financing plan for this project: all cash, from hospital reserves or donations. No debt financing is proposed.

HSCRC staff review concluded, at the time of the June 2012 CON review, that the project was financially feasible, based on the reasonableness of the assumptions used by the hospital and its analysis of the financial ratios. These financial ratios included a projected 157 days of cash on hand in 2015 and 2016 after project implementation compared to HSCRC's target value of 115 days. CHC financial projections submitted with this modification request indicate no change in revenues and only a small decrease in operating income. MHCC staff analysis of these projections along with the projections submitted to HSCRC indicates that the days of cash on hand are only likely to decrease to 151 days in 2015 and 152 days in 2016 as a result of the increased cash contribution to this project.

Staff concludes that the requested modifications are permissible under COMAR 10.24.01.17 and recommends that the Commission **APPROVE** the proposed modifications subject to the following conditions:

1. Carroll Hospital Center will not finish the shell space without giving notice to the Commission and obtaining all required Commission approvals.
2. Carroll Hospital Center will not obtain or request an adjustment in rates or its revenue cap by the Health Services Cost Review Commission ("HSCRC") that includes depreciation or interest costs associated with construction of the proposed shell space until and unless Carroll Hospital Center has filed a CON application involving the finishing of the shell space, has obtained CON approval for finishing the shell space, or has obtained a determination of coverage from the Maryland Health Care Commission that CON approval for finishing the shell space is not required.
3. The HSCRC, in calculating future rates or revenue caps for Carroll Hospital Center and its peer group, shall exclude the capital costs associated with the shell space until such time as the space is finished and put to use in a rate-regulated activity. In calculating any rate that includes an accounting for capital costs associated with the shell space, HSCRC shall exclude any depreciation of the shell space that has occurred between the construction of the shell space and the time of the rate calculation (i.e., the rate should only account for depreciation going forward through the remaining useful life of the space). Allowable interest expense shall also be based on the interest expenses going forward through the remaining useful life of the space.
4. Any future change to the financing of this project involving adjustments in rates or revenue caps set by the Health Services Cost Review Commission must exclude \$2,306,775 associated with the excess construction cost, and portions of the contingency and inflation allowance estimated for the project.

IN THE MATTER OF	*	BEFORE THE
	*	
CARROLL HOSPITAL CENTER	*	MARYLAND HEALTH
	*	
DOCKET NO. 08-18-2248	*	CARE COMMISSION
	*	

FINAL ORDER

Based on the analysis and findings in this Staff Report and Recommendation, and the record in this review, it is this 20th day of December, 2012, **ORDERED**:

That the request by Carroll Hospital Center to modify its Certificate of Need, Docket No. 12-06-2330, is **APPROVED** subject to the following conditions:

1. Carroll Hospital Center will not finish the shell space without giving notice to the Commission and obtaining all required Commission approvals.
2. Carroll Hospital Center will not obtain or request an adjustment in rates or its revenue cap by the Health Services Cost Review Commission ("HSCRC") that includes depreciation or interest costs associated with construction of the proposed shell space until and unless Carroll Hospital Center has filed a CON application involving the finishing of the shell space, has obtained CON approval for finishing the shell space, or has obtained a determination of coverage from the Maryland Health Care Commission that CON approval for finishing the shell space is not required.
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MARYLAND HEALTH CARE COMMISSION

December 20, 2012

December 12, 2012

Paul Parker
Chief, Certificate of Need
Maryland Health Care Commission
4160 Patterson Avenue
Baltimore MD 21215

Re: Carroll Hospital Center Cancer Center Certificate of Need (Matter No. 12-06-2330)

Dear Mr. Parker:

This letter is in response to your e-mail of December 7, 2012 requesting additional information pertaining to our request for an increase in the approved costs for the above referenced CON. In our original letter we stated that this increase was due in part to selecting finish materials that would provide sustained quality, reduced maintenance costs and improved patient safety and comfort.

Below we have provided you with examples that we hope address the clarification you need to have our request presented at the December 20th Commission meeting.

Reduced Maintenance

Flooring:

1. Vinyl composite tile (VCT) maintenance costs are estimated to be \$1.44 per sq. ft. (based on \$0.21 per sq. ft. for labor and \$1.23 per sq. ft. for materials). To maintain the tile per manufacturer recommendations you need to strip and wax the floors three times per year, it would cost \$4.32 per sq. ft. per year. Vinyl composite tile material cost is \$1.75 per sq. ft.

2. Linoleum:

- Made from natural raw materials, including linseed oil, pine rosin and wood flour; it is biodegradable and environmentally friendly.
- It naturally strengthens over time –it starts with a psi of 450 and over its life cycle it will double (VCT has a psi of 75).
- Inherently anti-static and anti-bacteriostatic – Inhibits the growth of many micro-organisms, including dust mites, MRSA and C-difficile.
- Repels dust and dirt.
- Occupancy ready finish – Topshield only needs to be reapplied as needed, which could be every two or three years. There is no need for initial maintenance or chemicals.
- Has better long term appearance retention.

200 Memorial Avenue
Westminster, MD 21157

410.848.3000
From Baltimore: 410.876.3000
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www.CarrollHospitalCenter.org

3. Sheet Vinyl:

- Sheet vinyl is treated with a high-quality, cross- linked polyurethane reinforcement that is UV cured allows for a low cost, polish-free maintenance regime for the lifetime of the flooring.
- Recycled content.
- Outstanding acoustic possibilities.
- Durable – Up to 2,500 psi. Fiberglass reinforced backing for a semi-rigid construction that resists tears, gouges, cracks and indentations.

4. Rubber Sheet:

- PVC-free and made from rapidly renewable sustainable raw materials.
- Increased coefficient of traction that reduces slips and falls.
- Ergonomic – very comfortable under foot.
- Great acoustical properties that rival commercial carpets.
- Very durable.
- Low maintenance – requires no waxing.
- Inherently bacteriostatic and anti-static – Is resistant to fungi and micro-organisms.

5. Linoleum tile, solid vinyl tile, and rubber sheet flooring maintenance costs are estimated to be \$0.43 per sq. ft. (based on \$0.21 per sq. ft. labor and \$0.22 per sq. ft. for materials). To maintain linoleum tile, solid vinyl tile, and rubber sheet flooring per manufacturer recommendations you are only required to apply a floor sealer once every two years, it would cost \$0.43 per sq. ft. every two years.

Linoleum tile material cost is \$4.25 per sq. ft.

Solid vinyl tile material cost is \$5.25 per sq. ft.

Rubber sheet flooring material cost is \$6.65 per sq. ft.

Life expectancy for all of these products is between 20 – 40 years.

Below is an illustration of cost differentiation and estimated maintenance savings for a 50,000 sq. ft. project.

Floor Type	Material Costs	Initial Material Costs	Material Cost Difference	Year 1 Maintenance	Year 2 Maintenance	Total 2-Yr Maintenance	Maintenance Savings (Every 2 Yrs)
VCT	\$1.75	\$87,500	\$0	\$216,000	\$216,000	\$432,000	\$0
Linoleum	\$4.25	\$212,500	\$125,000	\$0	\$21,500	\$234,000	(\$198,000)
Solid Vinyl	\$5.25	\$262,500	\$175,000	\$0	\$21,500	\$284,000	(\$148,000)
Rubber Sheet	\$6.65	\$332,500	\$245,000	\$0	\$21,500	\$354,000	(\$78,000)

It is also important to note that although we do not plan to have our project Leadership in Energy and Environmental Design (LEED) certified we thought it important to keep with industry standards and use products that would comply with LEED certification criteria, which these products do.

Improved Patient and Staff Safety and Comfort

- The ceiling systems we will be using are manufactured by Armstrong. They offer an acoustical value that will absorb as well as block sounds providing a more quiet environment and enhancing patient privacy and comfort.

Below is an illustration of a cost analysis for a 50,000 sq. ft. project. Cost at an estimated 50,000 sq. ft.:

Standard Tiles		Armstrong Tiles		Difference
Per Sq. Ft	Total	Per Sq. Ft	Total	
\$.56	\$28,000	\$2.66	\$133,000	\$105,0000

While we are not able to put a cost benefit over the life of the project for each finish we selected, we do want to provide you with the following information on how these selections affect patient safety and comfort.

- Flooring (as also described above):
 - Inherently anti-static and anti-bacteriostatic – Inhibits the growth of many micro-organisms, including dust mites, MRSA and C-difficile.
 - Repels dust and dirt.
 - Ergonomic – very comfortable under foot.
 - Great acoustical properties that rival commercial carpets.
- The two story concourse will have sound absorbing micro perforated wall panels providing a quieter environment.
- The glass used for the interior storefront in the concourse will be a decorative glass that will provide natural light and a welcoming environment for patients and visitors.
- To provide an environment that is calming and comfortable for patients and visitors, keeps with consumer expectations and keeps pace with industry standards, a fireplace with RealStone Veneer product will be installed in the cancer center waiting room and a two-story water feature will be added to the main lobby with a seating area to provide patients and visitors with a well-appointed area in which to relax and enjoy refreshments while waiting for patients to receive treatments. This area also will have wireless service.

I hope the above information provides you with the clarification you need. Should you need any additional information in order to evaluate this request, please let me know.

We thank you for your time and consideration.

Very truly yours,

A handwritten signature in black ink, appearing to read "John Sernulka", with a stylized flourish at the end.

John Sernulka, FACHE
President and CEO