

IN THE MATTER OF:
WALDORF NURSING &
REHABILITATION CENTER
DOCKET NO. 11-08-2325

*** BEFORE THE**

*** MARYLAND HEALTH**

*** CARE COMMISSION**

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REQUEST TO MODIFY CERTIFICATE OF NEED

I. INTRODUCTION

On December 4, 2012, Mid-Atlantic Waldorf, LLC (“Mid-Atlantic”) filed a request for modification of a Certificate of Need (“CON”) approved on April 19, 2012 to build a new 67-bed comprehensive care facility (“CCF”) to be known as Waldorf Nursing and Rehabilitation Center, to be developed in combination with a 90-bed assisted living (“AL”) facility in Charles County. The modification request includes a change in the physical plant design of the project. The applicant proposes to proceed with development of a free-standing 67-bed nursing home, delaying development of the assisted living component. Thus, the proposed facility is being changed from one with multiple levels of care to a proposed facility that will initially only offer CCF services.¹ This change will require an increase in CCF square footage. The modification request also includes a request to increase the project cost of the CCF. This change is primarily related to an increase in space allocated to the CCF that had formerly been allocated to the AL facility.

Background

On September 16, 2010, the Maryland Health Care Commission (“MHCC or Commission”) authorized Mid-Atlantic Waldorf, LLC to build a new 67-bed CCF, to be developed in combination with a 90-bed assisted living (“AL”) facility at 3735 Leonardtown Road in Waldorf (Charles County). The CCF, more commonly known as a nursing home, was to consist of a one-level structure totaling 34,693 square feet composed of two nursing units, one nursing unit with 35 beds (15 private and 10 semi-private rooms) and the other with 32 beds (all private rooms). The CCF was to include two interior courtyards and share an entrance, therapy, support, and ancillary areas with the assisted living component of the project. The AL portion of the new construction was to connect directly to the CCF and would be situated on the proposed site in such a manner as to permit future expansion of the AL component of the project. The AL facility was designed as a three-story structure containing 65,337 square feet featuring 70 private and 10 semi-private rooms, with access to an exterior courtyard. The estimated cost of this project was \$24,895,642 of which \$9,574,535 was attributable to the CCF beds.

¹ Assisted living services, bed capacity, and cost are not subject to CON review and approval

On August 10, 2011, Mid-Atlantic Waldorf filed a new CON application seeking approval to change the site because the owner of the original site failed to move forward with construction of the storm water management facilities and indefinitely suspended development work on the site. The new site is Lot 1, Part of Parcel AA, Fairway Village in St. Charles Communities, located off of Demarr Road near the Intersection with St. Charles Parkway in Waldorf (Charles County), Maryland, approximately 3.7 miles from the original site. All other features of the project remained the same.

On April 19, 2012, The Commission approved the new CON at the new site. The project cost estimate for the new site was \$26,062,330, of which \$9,862,847 was attributed to the CCF, the portion of the project subject to CON review. The source of funding for the entire project was anticipated to include \$6,967,161 in cash, a mortgage loan of \$17,708,169, a working capital loan of \$800,000, and a loan of \$587,000 to purchase furniture, fixtures, and equipment.

The approval was issued with the following two conditions that had been included in the first CON:

At the time of first use review, Waldorf Nursing and Rehabilitation Center shall provide the Commission with a completed Memorandum of Understanding with the Maryland Medical Assistance Program agreeing to maintain the minimum proportion of Medicaid patient days required by Nursing Home Standard COMAR 10.24.08.05A.(2); and

At the time of first use review, Waldorf Nursing and Rehabilitation Center shall provide to the Commission information that demonstrates that it has established collaborative relationships with other types of long term care providers to assure that each resident has access to the entire long term care continuum, as required by Nursing Home Standard COMAR 10.24.08.05A(9); and appropriate transfer referral agreements.

Request for Modifications to Approved CON

Mid-Atlantic Waldorf is requesting a modification of the latest CON approval, delaying the assisted living component, which is not subject to CON review, and limiting construction at this time to the 67 CCF beds and common and support areas. This change requires the allocation of some common and support space and cost to the 67 CCF beds that was to be spread over the total of 157 CCF and AL beds. Mid-Atlantic Waldorf states that the decision to delay the assisted living component of the project is a result of continued weakness in the housing market in Charles County. This weakness is a concern for the applicant because prospective residents of AL facilities often rely on the proceeds from the sale of their primary residence to help pay the monthly expenses of an assisted living facility. As market conditions improve, Mid-Atlantic Waldorf intends to construct the AL portion of the project at a later date after the CCF is opened and stabilized.

With the construction limited to the CCF, the spaces that were originally allocated and shared between the CCF and the AL components (e.g., “shared spaces” such as main entry, service entry, beauty shop, wellness & rehabilitation spaces, staff lounge and meeting room, central supply, central mechanical/engineering-maintenance, laundry/housekeeping, kitchen, gift

shop, family dining, medical records, and the offices for business, administration, activities, and social worker) must now be constructed and allocated solely for use in the CCF. Another change in the design of the facility is that the design of eight resident rooms designated for use by bariatric patients have increased by 100 square feet, and the design of 20 patient rooms include private showers. Therefore, the total building square footage allocable to the CCF will increase from 34,693 square feet to 43,712 square feet, an increase of 9,019 or 26.0%.

The layout of the CCF to be known as Waldorf Nursing & Rehabilitation Center (“WNRC”) will remain generally the same as previously approved. The facility will remain a single story building with courtyards: the facility design will accommodate a connection for the future addition of an AL component. The CCF will continue to operate with two Nursing Units, with Unit 1 containing 34 beds (26 private and 4 semi-private rooms) and Unit 2 designed with 33 beds (21 private and 6 semi-private rooms). Unit 1 will include a cluster of eight beds surrounding the nursing station that will treat more medically complex cases, including ventilator dependent patients who are non-ambulatory. The CCF will configure these beds for more intense monitoring, observation and interaction with the staff.

The following table summarizes key differences and similarities in the approved project and the modified project now proposed.

**Table 1: Comparison of Approved and Proposed Modified Construction Project
Waldorf Nursing & Rehabilitation Center CCF Beds**

	Approved Project April 12, 2012	Proposed Modified Project
New construction gross square feet ("GSF")	34,693	43,712
Project budget estimate	\$9,862,847	\$11,897,178
Sources of Funds		
Cash	\$2,421,633	\$2,947,178
Mortgage	\$6,521,225	\$7,750,000
Working Capital Loan	\$500,000	\$600,000
FFE Loan	\$419,989	\$600,000
Total CCF Beds	67	67
Private rooms (on completion)	47	47
Semi-private rooms (on completion)	10	10

Source: Original CON and Project Modification Request, Waldorf Nursing & Rehabilitation Center

The resulting changes in the design and construction of the CCF will increase the total square footage and project costs for the proposed WNRC. The modification will not change the total number of licensed CCF beds operating in the proposed facility after completion of this modified project.

II. STAFF REVIEW AND ANALYSIS

Requirements for Project Modification

COMAR 10.24.01.17 sets forth five changes that require Commission action and three impermissible changes that would require a new CON. The three impermissible changes are: (1) changes in the fundamental nature of the facility or the services to be provided in the facility from those that were approved; (2) increases in the total bed capacity or capacity of medical service categories from those approved; and (3) changes requiring extensions of time to meet applicable performance requirements, except as permitted by regulation. This modification request does not include any impermissible modifications. This modification does not change the fundamental nature of the approved services or facilities, which was limited to the CCF component of the project because the AL component is not subject to CON review. The applicant states that its plan continues to be the construction of a 67-bed CCF in Charles County but with AL facility development occurring in a second project phase, at an undetermined future date. The proposed changes will not increase the total bed capacity or services offered. The Applicant has not indicated that the proposed change will change the current project schedule.

The five changes that require Commission action are (1) any significant changes to the 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 projected operating expenses or revenue increases that exceed the projected expenses or revenues in the approved Certificate of Need Application, inflated by 10 percent per year; (4) a change in the project financing mechanism; and (5) a change in location or address of the project. The requested modification does not include a change in location or a change in financing mechanism. This proposed modification requires Commission approval because of the significant physical plant design changes (the delay in the construction of the assisted living component part of the project and the associated increase in the CCF square footage over what was approved) and the significant increase in CCF project costs primarily associated with the increase in CCF space.

Significant changes in physical plant design

The changes in the design include re-designing the facility as a freestanding CCF, and incorporating space that was previously shared with the assisted living facility such as building entrances (both main and service), administrative offices, therapy space, laundry, and kitchen. The Applicant calculated that these changes in design and re-allocation of space will add 6,214 square feet ("SF") to the CCF. Other physical plant design changes will add 2,805 SF as follows: enlargement of eight patient rooms for bariatric patients adding 800 SF; adding private showers to 20 rooms adding 300 SF; and the addition of tub rooms, extra clean/soiled laundry spaces and thicker walls to comply with recent regulatory changes, which in total will add 1,705 SF.

While the proposed change is a permissible modification, staff is concerned with the relatively small bed capacity of the project as a freestanding nursing home. The modified facility will be over 650 SF per bed for the 67 CCF beds. By way of comparison, Staff notes that the recently approved Magnolia Center replacement project, as currently designed, will be approximately 560 SF. per bed for a 130-bed facility. Staff's concern is not with the small facility size per se, but with the impact on cost per patient day and reimbursement rates. The impact on reimbursement rates is addressed below under the section on projected increases in revenue and expenses. Regarding the relationship of cost per patient day and size of facility, staff analyzed operating expenses per patient day as reported on the Commission's 2011 Long Term Care Survey and found that the expenses per patient day decreased as the size of freestanding nursing homes increased from an average daily census of ("ADC") of 30 – 59 through the ADC range of 150 - 179. After that, average expenses per day increased slightly, but the number of facilities in these larger size ranges is small, as detailed in the table below.

Table 2
Comparison of FY 2011 Operating Expense
Per Patient Day by
Facility Size Measured by
Average Daily Census

Average Daily Census	Number of Facilities	Total Operating Expenses Per Patient Day
30-59	18	\$347
60-89	31	\$314
90-119	53	\$281
120-149	51	\$281
150-179	18	\$275
180-209	6	\$286
210-239	2	\$287
240-269	4	\$321
270+	3	\$304

Source: MHCC Long Term Care Survey 2011 and
Medicaid Cost Reports

At a projected ADC of 62, WNRC would fall in the second group (60 – 89), but its projected expenses per patient day at \$344.33 is closer to the first group of smaller facilities with the lowest average daily census range (30 – 59).

While staff is concerned with the impact of the reduced scale of the project on operating expenses, staff recognizes that there is no statutory or regulatory minimum size of a nursing home project. (Staff recommends that establishing such regulatory guidance be considered in the next update of the nursing home chapter of the State Health Plan.) Moreover, the 67 CCF beds were approved because they met a need for CCF beds that was projected by the Commission for Charles County in 2007. Staff recognizes that building the CCF before building the AL component can arguably be a more financially prudent approach if the timing of project development does result in a higher AL facility vacancy rate during the early years of operation. The applicant has presented pro forma projections of revenues and expenses which indicate the

ability to reach profitability as a 67-bed freestanding CCF using acceptable assumptions, even with fairly conservative assumptions with respect to payer mix. Finally, the applicant has had a recent history of operating relatively small nursing homes profitably, including Chapel Hill Nursing and Rehabilitation Center, with an ADC in FY 2011 of 58, Fairfield Nursing and Rehabilitation (2011 ADC of 81), and Oakland Nursing and Rehabilitation (2011 ADC of 86). While these are not new facilities, which typically present a more difficult profitability challenge because of higher capital cost, this track record does suggest that the applicant has familiarity with the challenges of managing for cost control at lower patient census levels. Therefore, staff concludes that the proposed change in physical plant design, related to changes in the development schedule for the complete campus, is an acceptable approach to achieving the objective of fulfilling the bed capacity need identified for Charles County.

Incurring 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

Mid-Atlantic has provided a revised Project Budget to reflect the costs associated with the modified project plan, as summarized below.

**Table 3: Changes in the Uses of Funds
Approved and Proposed Modified Construction Project
Waldorf Nursing & Rehabilitation Center**

USE OF FUNDS	As Approved April 19, 2012	Requested Modification	Change	Percent Change
Building	\$5,830,664	\$7,210,000	\$1,379,336	23.7%
Land Purchase	507,568	585,386	77,818	15.3%
Site preparation	325,934	360,000	34,066	10.5%
Architect/engineering fees	291,681	350,000	58,319	20.0%
Permits (buildings/utilities)	72,487	150,000	77,513	106.9%
Major Movable Equipment	551,156	550,000	(1,156)	-0.2%
Minor Movable Equipment	419,989	600,000	180,011	42.9%
Contingencies	234,108	580,000	345,892	147.7%
Interest	190,202	226,042	35,798	18.8%
Total Current Capital	\$8,423,789	\$10,611,428	\$2,187,639	26.0%
Inflation Allowance	\$676,027	\$392,000	(\$284,027)	-42.0%
TOTAL CAPITAL COSTS	\$9,099,816	\$11,003,428	\$1,903,612	20.9%
Loan Placement Fees	\$163,031	\$193,750	\$30,719	18.8%
Other Fees & Costs	100,000	100,000	0	0.0%
FINANCING/ OTHER COSTS	\$263,031	\$293,750	\$30,719	11.7%
Working Capital/Startup	\$500,000	\$600,000	\$100,000	20.0%
TOTAL USE OF FUNDS	\$9,862,847	\$11,897,136	\$2,034,289	20.6%

Source: Project Budget in Staff Report dated April 12, 2012 for original CON and Project Budget in Request for Modification, dated December 4, 2012, pages 8-9

In reviewing the changes in the project budget, Staff applied the allowable inflationary increases applicable to this project. Specifically, Commission regulations at COMAR 10.24.01.17B(2), require Commission approval for 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. Capital cost increases under that amount do not require Commission approval.

To confirm that the requested increase in capital cost exceeds the allowable inflation and requires Commission approval, Staff applied the allowable inflationary increases that would be applicable to this project and confirmed that the proposed modification clearly requires Commission approval because the increase in costs exceeds the allowable inflation target. While this cost increase is significant, it is not an impermissible modification and the increase is generally justified by the reasonable increase in the size of the building for the CCF that results from the elimination of the Assisted Living component in the first phase of campus development and the added amenities of larger rooms and enhanced bathroom facilities.

When total projected operating expenses or revenue increases exceed the projected expenses or revenues in the approved Certificate of Need Application, inflated by 10 percent per year

Mid-Atlantic has provided a revised Revenue and Expense Statement to reflect the costs associated with the modified project.

**Table 4: Changes in the Proposed Revenues & Expenses for Second Year
Waldorf Nursing & Rehabilitation Center**

Revenue	As Approved April 19, 2012	Requested Modification	Change	Percent Change
	Dollar Amount	Dollar Amount		
Total Projected Operating Revenue	\$7,406,000	\$8,084,000	\$678,000	9.2%
Total Projected Operating Expenses	\$6,929,000	\$7,747,000	\$818,000	11.8%
Salaries, Wages & Benefits	\$4,035,000	\$4,383,000	\$348,000	8.6%
Other Including Contract Services & Supplies	\$2,233,000	\$2,540,000	\$307,000	13.7%
Project Interest, Depreciation & Amortization	\$661,000	\$824,000	\$163,000	24.7%

Source: CON Application (p. 22) and Waldorf Nursing & Rehabilitation Center
Project Modification Request (p.16)

Table 4 indicates that the construction of the CCF component will increase total projected operating revenues by 9.2%, less than the 10% increase that would require Commission action. However, the Total Projected Operating Expenses are projected to increase by 11.8%. The

increase in projected revenue is attributable to a small increase in projected patient days (1.1%) and a substantive increase in projected Medicare days (9.9%), as well as increases in assumed Medicaid and Medicare rates based on actual experience between the time the approved CON application was submitted and the time that this modification request was filed. The increases in projected operating expenses are primarily a result of the reduction in the size of the project as a result of the deferral of the Assisted Living component to a later date. This change not only eliminated the ability to spread project capital cost across more beds but also eliminated the ability to spread some personnel costs, such as administrative, food service, housekeeping, and maintenance staff, and other costs such as utilities and property taxes across the two components. Operating expenses are also projected to be higher particularly for therapies and prescription drugs due to the increase in projected Medicare days.

Regarding the impact of the proposed change on reimbursement rates, Medicare reimbursement rates are not set on a facility specific basis so Medicare rates will not be impacted by the proposed change in cost. Regarding the impact on Medicaid rates, the nursing home portion of the project exceeded the Medicaid capital appraisal limits when it was part of the larger project and the project capital costs will continue to exceed these limits. Therefore, the increase in project costs will not have any impact on the facility's Medicaid rate. However, Mid-Atlantic has estimated that the projected increases in expenses in other areas will increase Medicaid rates approximately \$19 per day for each of the four payment levels. This increase is a result of the reallocation of costs that would have been shared by the Assisted Living component and are reasonable and justified by the need for CCF beds to serve Charles County as projected by the Commission in 2007.

At this point in time, the applicant has reported closing on purchase of the project site, at an expenditure of \$507,568.

Change in the Project Financing Mechanisms

This CON modification request does not involve any significant changes in the project funding plan that would fundamentally alter an approved "mechanism of financing." The financing plan is still comprised of a cash contribution, a mortgage loan, and other loans. The first of the two other loans will provide working capital for the startup of WNRC, and the second for the purchase of furniture, fixtures, and equipment. Mid-Atlantic will finance the changes in constructing the freestanding CCF by increasing the cash equity contribution and by borrowing more, as detailed in Table 5.

**Table 5: Changes in the Proposed Sources of Funds
Waldorf Nursing & Rehabilitation Center**

USE OF FUNDS	As Approved April 12, 2012	Requested Modification	Change	Percent Change
	Dollar Amount	Dollar Amount		
Cash	\$2,421,633	\$2,947,178	\$525,545	21.7%
Mortgage	\$6,521,225	\$7,750,000	\$1,228,775	18.8%
Working Capital Loans	\$500,000	\$600,000	\$100,000	20.0%
Loan - Furniture, Fixture & Equipment	\$419,989	\$600,000	\$180,011	42.9%
TOTAL SOURCE OF FUNDS	\$9,862,847	\$11,897,178	\$2,034,331	20.6%

Source: Project Budget in Staff Report dated April 12, 2012 for original CON; Project Budget in Submission dated December 4, 2012

Table 5 shows that the applicant will increase the cash contribution for the project by almost 21.7% from \$2,421,633 to \$2,947,178, and increase the amount of the mortgage loan by approximately 18.8% from \$6,521,225 to \$7,750,000. The working capital loan for WNRC will increase from \$500,000 to \$600,000, an increase of 20%, while the loan used to purchase furniture, fixtures, and equipment will increase from \$419,989 to \$600,000, an increase of 42.9%. This modification will not change the financing mechanisms used by the applicant, only the dollar amount contributed by each source of financing. Waldorf provided an opinion letter from Leonard Sacks, CPA/CFF, CVA, CIRA, dated December 3, 2012, attesting that, based on his experience working with the principal, sufficient available assets exist to meet the equity contribution for the project. Susquehanna Bank also provided a letter, dated November 30, 2012, expressing interest in financing the construction of the 67 bed CCF.

Change in Location or Address of the Project

This CON modification does not involve a change in the location or address of the project.

III. SUMMARY AND STAFF RECOMMENDATION

Mid-Atlantic Waldorf has requested Commission approval of a modification to its approved Certificate of Need Docket No. 11-08-2325), issued on April 19, 2012. Mid-Atlantic Waldorf seeks to increase the building space and cost of the approved 67-bed CCF, primarily as a result of its' decision to postpone construction of the Assisted Living component of the project, that was originally presented to the Commission as being developed in a single phase with the CCF. The reason given for this change is continued weakness in the housing market in Charles County.

The requested modification includes no changes to the fundamental nature of the facility or the CCF services to be provided by the proposed facility from those subject to and approved by the Commission. Staff finds that there are no impermissible modifications requested, and that

the facility design changes proposed and the cost increases that result from the design changes are permissible under Commission regulations at COMAR 10.24.01.17. While staff is concerned with the reduced size of the project and its impact on per diem expenses, the 67 CCF beds were approved because they met a need for CCF beds that were projected by the Commission. In addition, the proposal to open and stabilize the CCF component of the originally planned project before initiating work on the AL component may improve the project's financial viability if the applicant's read on the difficulties it could face in marketing AL units during the next few years is correct. Therefore, staff concludes that the project, with the proposed modifications, is an acceptable approach to moving forward with the CCF bed capacity MHCC has identified as needed in Charles County. The applicant has demonstrated, with reasonable assumptions, that it can feasibly develop and operate this small CCF project as a freestanding facility and it still plans to develop a larger scale of operation in the future by building AL facilities as a later phase of campus development. For these reasons, Staff recommends that the Commission **APPROVE** the proposed modification to the Mid-Atlantic Waldorf Certificate of Need physical plant design and capital cost increase with the two conditions attached to the original CON approval.

IN THE MATTER OF:

**WALDORF NURSING &
REHABILITATION CENTER**

DOCKET NO. 11-08-2325

*** BEFORE THE**

*** MARYLAND HEALTH**

*** CARE COMMISSION**

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FINAL ORDER

Based on the analysis and findings in this Staff Report and Recommendations, it is this 16th day of May, 2013, **ORDERED**

That the request by Mid-Atlantic Waldorf, LLC to modify the Certificate of Need approved under Docket No. 11-08-2325, on April 19, 2012 by increasing the CCF building space and increasing the project cost to \$11,897,178 is **APPROVED** with the following conditions.

At the time of first use review, Waldorf Nursing and Rehabilitation Center shall provide the Commission with a completed Memorandum of Understanding with the Maryland Medical Assistance Program agreeing to maintain the minimum proportion of Medicaid patient days required by Nursing Home Standard COMAR 10.24.08.05A.(2); and

At the time of first use review, Waldorf Nursing and Rehabilitation Center shall provide to the Commission information that demonstrates that it has established collaborative relationships with other types of long term care providers to assure that each resident has access to the entire long term care continuum, as required by Nursing Home Standard COMAR 10.24.08.05A(9); and appropriate transfer referral agreements.

MARYLAND HEALTH CARE COMMISSION

May 16, 2013