

**MARYLAND HEALTH CARE COMMISSION**4160 PATTERSON AVENUE – BALTIMORE, MARYLAND 21215
TELEPHONE: 410-764-3460 FAX: 410-358-1236**MEMORANDUM**

TO: Donna Kinzer, Executive Director, HSCRC
Jerry Schmith, Deputy Director, HSCRC

FROM: Frances B. Phillips *Frances B. Phillips*
Commissioner/Reviewer

DATE: August 31, 2015

RE: Relocation of Washington Adventist Hospital and Establishment of a Special Hospital Psychiatric on the Existing Takoma Park Campus
CON Docket No. 13-15-2349

As you know, Adventist HealthCare, Inc. (AHC) has submitted a Certificate of Need (“CON”) application to replace and relocate most of the acute care services currently provided by Washington Adventist Hospital (“WAH”) on its Takoma Park campus, to a new 48.9 acre general hospital campus site in the White Oak area of Silver Spring in Montgomery County, approximately 6.6 miles from the current campus. AHC’s application proposes that existing behavioral health services, including 40 psychiatric beds that would be licensed as a Special Hospital – Psychiatric, would remain on the Takoma Park campus and would be operated by Adventist Behavioral Health. The final version of this CON application was filed on September 29, 2014.

HSCRC has previously received copies of the original and replacement applications, as well as comments on the applications and responses, and staff’s completeness questions and responses. This memorandum formalizes the Maryland Health Care Commission’s request for HSCRC review that was made when MHCC staff delivered those materials. If there are additional materials you want to review, you should be able to find them at the following link (or MHCC staff can bring you copies, upon your request):
http://mhcc.maryland.gov/mhcc/Pages/hcfs/hcfs_con/hcfs_con_washington_adventist_hospital.a.spx.

The proposed Takoma Park campus also will include special hospital medical rehabilitation services licensed as Adventist Rehabilitation Hospital of Maryland for 87 beds¹

¹ Adventist Rehabilitation Hospital of Maryland operates both a campus in Rockville and the Takoma Park under a single license

including 32 beds on the Takoma Park Campus. In addition to the psychiatric and rehabilitation services, AHC plans to partially renovate and modify space on the Takoma Park campus for alternate uses including an urgent care center, outpatient clinics, a Federally Qualified Health Center, and a maternity clinic serving low income women.

The estimated project cost for the relocation and replacement of the general hospital to White Oak is \$330,829,524. The estimated cost for renovations to existing space for the Special Hospital-Psychiatric on the Takoma Campus is \$5,223,506. AHC has budgeted an additional \$13,245,772 for the other renovations to the Takoma Park Campus. AHC proposes to finance the relocation of the hospital to White Oak with approximately \$244.8 million in debt, \$50.6 million in cash, \$20 million from contributed gifts, \$11 million in contributed land, and \$4.5 million in interest income. AHC plans to debt finance the combined \$18.5 million in improvements to the Takoma Park campus, including the improvements to the inpatient psychiatric nursing unit.

I request that HSCRC staff review the financial projections and the assumptions upon which these projections are based, as provided in the replacement CON application² submitted on September 29, 2014 (Exhibit 1, Tables J, K and L, and Exhibit 37), and comment on the proposed project's financial feasibility and the reasonableness of the assumptions.

In providing the requested comments, it would be very helpful if you could answer the following questions:

1. Are the sources of funds assumed by the applicant appropriate? In your opinion, is the equity contribution and the proportion of other non-debt sources of project funding adequate?
2. As you know, one of the applicant's assumptions is that it will obtain a 7% increase in the hospital's global budget revenue to account for the increased capital costs resulting from this project. In your opinion, is this increase necessary for this project to be feasible and for the replaced and relocated WAH to be financially viable? If, in your opinion, this increase is not necessary for project feasibility and the viability of WAH, please provide the basis for this opinion.
3. Based on your analysis and the experience of HSCRC to date in implementing the new payment model for hospitals, what is the ability of the proposed replacement hospital to be competitively priced, when compared with general hospitals in its region of the state and when compared with similar (peer-group) hospitals throughout the state, if the project is implemented as proposed and the applicant's utilization projections are realized?

Because AHC is proposing to change the form of its provision of acute inpatient psychiatric services in eastern Montgomery County through this proposed project, from a general hospital unit at WAH to a special hospital-psychiatric, thus changing the manner in which charges for this service will be regulated by HSCRC, I would also like to receive comments on

² The cover sheet for the September 29, 2014 application, additional volumes containing exhibits, and subsequent exhibits refer to "Modification of Application for Certificate of Need".

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the financial feasibility of providing acute psychiatric hospital services in Takoma Park as a 40-bed special hospital. The project budget, five year pro forma schedule of revenues and expenses, and assumptions for this proposed special hospital were submitted on December 12, 2014. Note that the project budget erroneously indicated that the source of funds for renovating space for behavioral health would be cash. The correct source of funds is debt, as specified in Exhibit 6 of the September 29, 2014 replacement application. This was confirmed by WAH in its response to my April 29, 2015 request for additional information.

With respect to utilization projections (see Exhibit 1, Table I of the September 29, 2014 replacement application), I am not requesting that HSCRC analyze the feasibility of this project with alternative utilization projections. However, with respect to my previously noted request that HSCRC staff review the assumptions used by AHC in this application and comment on the reasonableness of these assumptions, you may, of course, offer your opinions on the reasonableness of utilization projections employed by AHC.

Finally, Laurel Regional Hospital, and MedStar Montgomery Medical Center submitted an analysis of the impact of the relocation on their discharges and the impact of such a reduction in volume on their revenues and bottom line. While I do not necessarily agree with the hospitals' assessments of the impact on volume and I am not asking for your opinion on their calculation of the expected loss in discharges, I would like your comments on the methodology used to convert such losses in volume to reductions in revenue and impact on the hospitals' bottom line (the relevant analysis submitted by the interested parties on May 29, 2015 is attached).

I understand that HSCRC staff has been considering and reviewing the materials regarding AHC's application for some period of time. I hope that, under these circumstances, it will be possible for HSCRC staff to provide comments on AHC's financial projections and these more specific questions by Friday, October 2, 2015. I value HSCRC's input on these matters.

Attachment

cc: Ulder Tillman, M.D.
Montgomery County Health Officer
Ben Steffen, MHCC
Paul E. Parker, MHCC
Kevin McDonald, MHCC
Joel Riklin, MHCC
Suellen Wideman, AAG
Howard L. Sollins, Esquire
John J. Eller, Esquire
Kurt J. Fischer, Esquire
Marta D. Harting, Esquire
Thomas C. Dame, Esquire
Ella R. Aiken, Esquire
Susan C. Silber, Esquire
Kenneth Sigman, Esquire
Catherine S. Tunis, President, SOSCA

Dimensions LRH \ Medstar MMC
Impact of Lost Volume Due to WAH Proposed Relocation
2014 Dollars

	Dimensions LRH	Medstar MMC	Note
1) Projected Discharge Reduction	(582)	(284)	(1)
2) FY 2014 Average Charge Per Discharge	\$ 9,056	\$ 9,712	(2)
3) Inpatient Revenue Reduction (A)	\$ (5,271,000)	\$ (2,758,000)	(3)
4) Outpatient Revenue to Inpatient Revenue	84%	91%	(4)
5) Outpatient Revenue Reduction (B)	\$ (4,415,000)	\$ (2,511,000)	(5)
6) Total Revenue Reduction (A + B)	\$ (9,686,000)	\$ (5,269,000)	(6)
7) Total FY 2014 Actual Revenue	\$ 104,230,000	\$ 166,918,000	(7)
8) Percentage Revenue Change / Lost Revenue Percentage Due to WAH Relocation	-9.29%	-3.16%	(8)

Note (1): Source - KPMG Demand Assessment Impact, LRH Comment Letter, Exhibit 4; Detailed excel worksheets provided in the attached filing. Represents lost discharge volume due to WAH relocation.

(2): Source - HSCRC Inpatient Abstract Data Set for the twelve months ended June 30, 2014 & computation is total inpatient charges divided by total actual discharges

(3): Line 3 equals Line 1 (discharges) times Line 2 (average charge per discharge)

(4): Source - HSCRC Inpatient and Outpatient Abstract Data Set for the twelve months ended June 30, 2014. Computation is Outpatient Revenue divided by Inpatient

(5): Line 3 (Inpatient Revenue Reduction) times Line 4 (Outpatient revenue percentage) to compute the corresponding outpatient revenue impact of volume loss.

(6): Line 6 equals Line 3 plus Line 5 to represent estimated total revenue loss due to WAH relocation

(7): Source - HSCRC Inpatient and Outpatient Abstract Data. The total inpatient and outpatient revenue for the twelve months ended June 30, 2014. Data excludes LRH's Speciality Unit revenue.

(8): Percentage change in revenue is the amount on Line 6 divided by total actual revenue on Line 7.

Dimensions LRH \ Medstar MMC
Impact of Lost Volume Due to WAH Proposed Relocation
2014 Dollars (\$ 000's Deleted)

	Dimensions LRH	Medstar MMC
Projected Revenue Reduction	\$ (9,686,000)	\$ (5,269,000)
Expected HSCRC Market Share Adjustment Factor	50%	50%
Expected Collection Ratio ⁽¹⁾ Net Revenue Impact (A)	<u>85%</u> <u>\$ (4,101,000)</u>	<u>86%</u> <u>\$ (2,257,000)</u>
Projected Revenue Reduction	<u>\$ (9,686,000)</u>	<u>\$ (5,269,000)</u>
Expected Collection Ratio ⁽¹⁾	85%	86%
Composite Variable Cost Assumption Net Expense Change (B)	<u>36%</u> <u>\$ (2,978,000)</u>	<u>29%</u> <u>\$ (1,305,000)</u>
Net Impact on Operating Margin (A-B)	<u>\$ (1,123,000)</u>	<u>\$ (952,000)</u>

Source (1): FY 2014 HSCRC Annual Filing RE Schedule

Dimensions LRH \ Medstar MMC
Variable Cost Factors
Under Various Volume Change Scenarios

	Percentage Volume Change		
	0% - 4%	5% - 10%	10%+
Patient Care	50%	60%	70%
ER\Clinic\SDS\OBV	50%	60%	70%
Ancillaries	20%	30%	40%
Medical Supplies	50%	60%	70%
Drugs	50%	60%	70%
Patient Care O/H	20%	30%	40%
Other Overhead	10%	15%	20%
CFA	0%	0%	0%

Laurel Regional Hospital
Computation of Composite Variable Cost Factors
2014 Dollars (\$ 000's Deleted)

FY 2014 Actual Costs	Percentage Volume Change					
	0% - 4%		5% - 10%		10%+	
	Factor	Cost	Factor	Cost	Factor	Cost
\$ 18,774	50%	\$ 9,387	60%	\$ 11,265	70%	\$ 13,142
ER\Clinic\SDS\OBV	50%	4,831	60%	5,797	70%	6,764
Ancillaries	20%	4,643	30%	6,964	40%	9,285
Medical Supplies	50%	3,271	60%	3,925	70%	4,580
Drugs	50%	1,952	60%	2,342	70%	2,733
Patient Care OIH	20%	2,724	30%	4,086	40%	5,448
Other Overhead	10%	2,302	15%	3,453	20%	4,604
CFA	0%	-	0%	-	0%	-
Total		\$ 29,110		\$ 37,832		\$ 46,555
Composite Variable Cost Factor		28%		36%		45%

Source: HSCRC Annual Filing Schedule M

Montgomery Medical Center
Computation of Composite Variable Cost Factors
2014 Dollars (\$ 000's Deleted)

FY 2014 Actual Costs	Percentage Volume Change					
	0% - 4%		5% - 10%		10%+	
	Factor	Cost	Factor	Cost	Factor	Cost
\$ 19,068	50%	\$ 9,534	60%	\$ 11,441	70%	\$ 13,348
ER\Clinic\SDS\IOBV	50%	6,063	60%	7,276	70%	8,488
Ancillaries	20%	4,301	30%	6,451	40%	8,602
Medical Supplies	50%	5,983	60%	7,179	70%	8,376
Drugs	50%	5,066	60%	6,079	70%	7,092
Patient Care OIH	20%	3,188	30%	4,782	40%	6,376
Other Overhead	10%	2,266	15%	3,399	20%	4,533
CFA	0%	-	0%	-	0%	-
Total		\$ 36,401		\$ 46,608		\$ 56,814
Composite Variable Cost Factor		29%		37%		45%

Source: HSCRC Annual Filing Schedule M