




MARYLAND HEALTH CARE COMMISSION

4160 PATTERSON AVENUE – BALTIMORE, MARYLAND 21215
TELEPHONE: 410-764-3460 FAX: 410-358-1236

MEMORANDUM

TO: Commissioners

FROM: Kevin R. McDonald
Chief, Certificate of Need 

DATE: March 18, 2021

SUBJECT: Sheppard Pratt at Elkridge
Docket No. 15-13-2367

Enclosed is the staff report and recommendation concerning a request for Project Change After Certificate of Need Approval filed by Sheppard Pratt Health System. The project involves the relocation of a Special Hospital- Psychiatric 4100 College Avenue in Ellicott City, to a 39.1-acre site located at the intersection of Route 103 and Route 1 in Elkridge.

The applicant is requesting an increase in the approved cost of the project, which was previously approved by the Commission on September 20, 2016, at a total project cost of \$96,532,907. Sheppard Pratt requests a \$9,105,505 increase (9.4%) in the approved cost of the budget, bringing the total estimate for the project to \$105,638,412.

Sheppard Pratt states that construction bids came in higher than originally anticipated as a result of: (1) increased costs for building materials; (2) increased costs attributable to the COVID pandemic, and (3) design changes that added materials cost; and (4) increased architect and engineering costs due to the associated design adjustments and extension of the project timeline.

Sheppard Pratt states that the additional funds required will be covered by an additional \$9 million in philanthropy.

Staff recommends that the Commission APPROVE the proposed change to the authorized cost of this project.

**IN THE MATTER OF
SHEPPARD PRATT
AT ELKRIDGE
Docket No. 15-13-2367**

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**BEFORE THE
MARYLAND
HEALTH CARE
COMMISSION**

**STAFF REPORT
REQUEST FOR PROJECT CHANGE AFTER
CERTIFICATE OF NEED APPROVAL**

I. INTRODUCTION

Background

The applicant, Sheppard Pratt Health System, Inc. (Sheppard Pratt), is a private non-profit psychiatric institution founded in 1891. It is Maryland’s largest private provider of mental health, special education, and substance abuse treatment services, with more than 2,700 employees and 34 programs in 38 locations.¹ Among Sheppard Pratt’s facilities and programs are two hospitals specializing in the provision of psychiatric services, The Sheppard and Enoch Pratt Hospital, a 322-bed special psychiatric hospital located in Towson (Baltimore County) and Sheppard Pratt at Ellicott City, a 78-bed special psychiatric hospital located in Ellicott City (Howard County).

On September 20, 2016, the Maryland Health Care Commission (Commission) awarded a Certificate of Need (CON) to relocate and replace the Ellicott City special hospital to Elkridge (Howard County). Sheppard Pratt is constructing a three-level replacement special hospital with 85 beds. It is designed to provide five distinct programs of service based on patient age and patient conditions. The hospital will serve adolescents, young adults, the general adult population, adults with co-occurring conditions (i.e., adults with a primary psychiatric diagnosis and a secondary substance use disorder), and adults with psychotic disorders. The hospital configuration was described, when the project was approved, with five corresponding units, each with 16 rooms and 17 beds.

As approved, the special hospital would include 155,507 square feet (SF) of new construction on a 39 acre campus located at the intersection of Routes 103 and Route 1 in Elkridge. The approved project cost is \$96,532,907 with four funding sources; \$66.7 million in debt, \$14.86 million in cash, \$7.5 million in philanthropic gifts, and \$7.5 million in State grant funding.

Sheppard Pratt projects that the replacement hospital will open on June 28, 2021

¹ Sheppard Pratt’s website is located at <https://www.sheppardpratt.org/about/history/sheppard-pratt-health-system-today/>

Summary of Requested Project Change

Sheppard Pratt requests that the Commission approve a \$9,105,505 increase (+9.4%) in the approved cost of the project, bringing the total cost estimate for the project to \$105,638,412. Sheppard Pratt states that construction bids came in higher than originally anticipated as a result of increased costs for building materials and cost increases attributable to the COVID pandemic. In addition, certain design changes added to the cost of materials and the associated design adjustments, and extension of the project timeline resulted in additional costs for architectural and engineering fees. These increased project costs will be partially offset by reductions in other line items, described later in this staff report.

Sheppard Pratt states that the additional funds required will be covered by an additional \$9 million in philanthropy.

II. APPLICABLE REGULATIONS

COMAR 10.24.01.17B provides that certain “changes that would place the project at variance with its Certificate of Need ... shall receive approval from the Commission” Sheppard Pratt seeks to make a permissible modification.² This project change requires Commission action because it would incur “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” as provided in COMAR 10.24.01.17B(2).

Under COMAR 10.24.01.17D(3), the Commission may approve the requested change, approve it in part or with conditions, deny approval of the change for stated reasons, or require a complete CON review because of the scope of the requested change.

III. COST INCREASE AND FINANCIAL IMPACT OF THE REQUEST

Current Request Compared with the Original CON Approved Budget

Table 1, on the following page, compares the approved costs of this project with the applicant’s current cost estimate, reflecting the construction bids received. Sheppard Pratt explained the increase in the estimated project cost as follows.

1. Rising cost of materials and construction. The building costs increased by approximately 30% from those estimated at the time of the CON approval due to the underestimation of certain construction elements. Additional construction cost increases resulted from the COVID-19 pandemic and the related extension of the project timeline. Original estimates were based on preliminary plans that were prepared in 2016, and this requested project change is based on construction bids received.
2. Changes to the project. Changes made to the building façade increased materials costs by \$2.3 million. Two elements not included in the original cost estimates were added; metal doors and frames, adding \$3.3 million to project cost, and gypsum board shaft assemblies,

² Sheppard Pratt’s modification request does not involve an impermissible modification to the project (i.e., a change that would require submission and approval of a new CON application).

adding \$4.8 million.

3. Architect and engineering fees. Design adjustments and the extended timeline of the project increased these costs by approximately \$1 million.

These project cost increases are partially offset by decreases in costs for permits, site preparation, moveable equipment, technology, financing costs, and legal fees. See Table III-1, below

**Table III-1: Original Project Budget and Current Project Cost Estimate
Sheppard Pratt at Elkridge**

A. Uses of Funds				
	2016 CON	Current Estimate	Variance	% Change
New Construction				
Land Purchase	\$ 2,837,150	\$ 2,837,150	--	--
Building	52,383,532	68,135,607	\$15,752,075	30.1%
Site and Infrastructure	315,000	133,500	(181,500)	(57.62%)
Architect/Engineering Fees	5,048,863	6,066,099	1,006,236	19.9%
Permits	1,059,000	731,552	(327,448)	(30.9%)
Subtotal – New Construction	\$58,806,395	\$75,055,758	\$16,249,363	27.6%
Moveable equipment	\$ 5,590,000	\$ 5,439,788	(\$510,212)	(8.60%)
Contingency Allowance	9,578,370	9,578,370	-	-
Interest	2,355,972	2,355,972	-	-
Other*	11,119,920	8,780,813	(2,339,107)	(21.0%)
Total Current Capital Costs	\$90,647,807	\$104,047,841	\$13,400,034	14.8%
Inflation Allowance	\$3,885,100	0	(\$3,885,100)	(100%)
Total Capital Costs	\$94,532,907	\$104,047,841	\$9,514,934	10.1%
Financing Cost and Other Cash Requirements				
Loan Placement Fees	\$1,400,000	\$800,982	(\$599,018)	(42.7%)
Bond Discount	300,000	0	(300,000)	(100%)
Legal Fees	250,000	114,079	(135,921)	(54.4%)
Non-Legal Consultant Fees	50,000	134,500	84,500	169.0%
Total Uses of Funds	\$96,532,907	\$105,638,412	\$9,105,505	9.4%
B. Sources of Funds				
	Original CON	Currently Anticipated	Variance	% Change
Cash	\$14,857,500	\$14,963,005	\$ 105,505	0.1%
Philanthropy	7,500,000	16,500,000	9,000,000	120.0%
Bonds	66,675,407	66,675,407	-	-
State Grants	7,500,000	7,500,000	-	-
Total Sources of Funds	\$96,532,907	\$105,638,412	\$9,105,505	9.4%

Source: Table 1, Project Budget, from 2016 CON application and the 2021 Request for Project Change.

* Other charges include technology costs and miscellaneous campus development fees including permitting and engineering for capital costs outside of the new construction, security, landscaping, roads, and parking lots.

The Change in Project Cost Exceeds the Inflation Allowance

Sheppard Pratt projects that the project will require an additional expenditure of approximately \$9.1 million. CON regulations provide for inflation in approved project costs that reflect published estimates of inflation in health care facility construction costs. Increases that exceed this index require Commission approval. The inflation allowance is calculated using the building cost indices published on a quarterly basis by IHS Global Insight in *Healthcare Cost Review*. (https://mhcc.maryland.gov/mhcc/pages/hcfs/hcfs_con/documents/con_cap_cost_index_20200127.pdf).

Using the building cost inflation index noted above, the allowable inflation allowance for this project is approximately \$6.1 million, below the estimated cost increase being proposed. Thus, the regulations require Commission approval of the proposed cost increase.

Impact on Financial Performance

Sheppard Pratt plans to fund the additional project cost with additional philanthropic donations, avoiding higher ultimate project costs by not adding more long-term debt. Sheppard Pratt states that it has already raised \$13.5 million of the anticipated \$16.5 million dollar philanthropy goal for the project. Sheppard Pratt notes its strong record of fundraising, which lends support to its belief that it can raise the additional funds for the project. Sheppard Pratt has the funds available to cover the remaining \$3 million if the philanthropy goal is not met.

The following table summarizes and compares the projected operating results for the Sheppard Pratt project as originally approved and as in the proposed modification. The sole effect on the facility’s financial results will be a \$428,209 increase in annual depreciation expense, which reduces the facility’s projected net income in its first full year of operation from \$2.17 million to \$1.74 million.

**Table III-2: Projected Utilization and Financial Statistics – First Year of Operation
2016 Application and 2021 Project Change Request Projections
Sheppard Pratt at Elkridge**

	Project as Originally Approved	Project with Requested Change
Utilization Statistics		
Discharges	3,580	3,580
Patient Days	27,930	27,930
Average Length of Stay (Days)	7.8	7.8
Financial Statistics		
Net Operating Revenue	\$37,632,707	\$37,632,707
Total Operating Expenses	\$35,462,232	\$35,890,441
Net Income	\$2,170,475	\$1,742,266

IV. ANALYSIS AND RECOMMENDATION

The increased project cost would be paid for by philanthropy donations. Thus, the sole effect of these changes projected for the operating budget of the special hospital is an increase of \$438,000 in annual depreciation expense. Despite that additional expense, Sheppard Pratt still projects the ability to achieve an operating margin of 4.8 percent. Staff concludes that the applicant

can sustain this increased capital cost without difficulty.

In addition, staff concludes that the proposed project change entails no material changes to the nature of the project, its location, or its capacity. . Nor does it change the findings that the Commission made in 2016 concerning the need for and the positive impact of relocating the Sheppard Pratt facility to Elkridge. For these reasons, staff recommends that the Commission approve Sheppard Pratt's request for project changes after Certificate of Need approval.

IN THE MATTER OF

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SHEPPARD PRATT

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AT ELKRIDGE

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HEALTH CARE

Docket No. 15-13-2367

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COMMISSION

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FINAL ORDER

Based on Commission staff’s analysis of the request by Sheppard Pratt Health System, Inc. for project change after Certificate of Need approval, it is this 18th day of March, 2021, **ORDERED** that:

The request by Sheppard Pratt Health System, Inc. for changes to its September 20, 2016 Certificate of Need to relocate and replace the existing Sheppard Pratt special psychiatric hospital in Ellicott City to a site in Elkridge at a total project cost of \$105,632,412 is hereby **APPROVED**,

MARYLAND HEALTH CARE COMMISSION