February 16, 2024

VIA E-MAIL

Ella Aiken, Esq.
Alison Lutich, Esq.
Gallagher Evelius & Jones Attorneys at Law
218 North Charles Street, Suite 400
Baltimore, MD 21201

Re: **Completeness Questions from the Health Services Cost Review Commission Regarding Docket No. 23-24-EX017**
Request for Exemption from Certificate of Need Review – Merger and Consolidation of University of Maryland Rehabilitation and Orthopaedic Institute and University of Maryland Medical Center

Dear Ms. Aiken and Ms. Lutich,

At the request of staff at the Maryland Health Care Commission (MHCC or Commission), the Maryland Health Services Cost Review Commission (HCSRC) has reviewed the December 29, 2023, request of James Lawrence Kernan Hospital, Inc. d/b/a University of Maryland Rehabilitation and Orthopaedic Institute (UMROI) and University of Maryland Medical Center, LLC (UMMC) for an exemption from Certificate of Need (CON) review of the proposed merger and consolidation of acute inpatient rehabilitation and chronic care beds from UMROI to UMMC. Based on their review of the information contained in this request, HSCRC has the following observations and questions, requiring additional information or clarification:

Table E (Project Budget):

1. The capital costs tally $203.2 M, and the financing costs tally $4.1 M for a total budget of $207.3 M. Table G reflects annual depreciation/ amortization expense of $25.5 M which implies an average life of 8.1 years. This is judged unreasonable.

   The average depreciable lives of assets and amortization life of the bonds used in the Greenebaum Comprehensive Cancer Center (GCCC) project was 22.8 years and yielded an average annual depreciation/amortization expense of $11.8 M, as reflected in Tables E and G, and as submitted 08/16/2023. This was judged reasonable using approximate lives of 35 years of building, 20 years of fixed equipment, 10 years of moveable equipment, and 30 years of bond life.

Please provide average useful lives expected by asset class and bond amortization life expected so as to support a reasonableness test of annual depreciation/amortization and tie Table E costs to Table G expense.

2. The capitalized interest during construction is $14.9 M. Please provide a term sheet for proposed bonds (start date, rate, duration) and relate it to the construction timetable and opening to support the reasonableness test of capitalized interest on project financing.

3. The contingency allowance is $10.6 M and the inflation allowance is $10.7 M, combined this represents 10.5% of budgeted capital costs. Given that the capital cost for the GCCC project rose from $193.9 M to $266.3 M (an increase of 37%) as reflected in Table E as submitted August 2023. Please provide the reasons for supporting the sufficiency of a 10.5% combined allowance for this project.

4. The bonds are measured at $148.8 M in Table E. Assuming such bonds are to have an amortization of 30 years, its first year's interest (2024) is approx. $7.4 M and its fourth year's interest (2027 when project construction is finished and open for business) is approx. $7.1 M. Table G reflects annual interest of $15.6 M and falling. Please provide the assumed terms sheet for proposed bonds and relate it to the timetable for construction and opening so to support the reasonableness of annual expensed interest on project financing and tie Table E costs to Table G expense.

5. Other financing costs and cash requirements are $1,963,600. Please define.

6. Interest earned from bonds proceed is $3.6 M. Please provide assumptions on spend down of bond proceeds and earnings rate on proceeds and relate to the construction timetable and bond financing timetable so as to support the reasonableness test of interest earnings.

7. Authorized bonds are $148.8 M. Does this represent new borrowing, and allocation of existing borrowing, or a combination of both?

8. State Grants/Appropriations are $55 M. To date how much has been realized in cash, and how much more has been pledged?

9. How much of the $207.3 M budget is supported by binding contracts, if any? How much is supported by vendor estimates?

Table F (Statistics Entire Facility/Services):

10. Total discharges grow at an average rate of 0.9% for the 6 projected years ending FY29. However, FY27 reflects growth of 3.8%, What assumptions are driving the growth in non-acute care in FY27 and beyond?

11. Total patient days grow at an average rate of 2% for the 6 projected years ending FY29. However, FY27 reflects growth of 10%, What assumptions are driving the growth in non-acute care in FY27 and beyond?

Table G (P&L Uninflated Entire Facility/Services):

12. Gross patient service revenues (GPSR) grow at an average rate of 0.5% for the 6 years ending FY29. However, FY27 reflects growth at 4.2%. What assumptions are driving the growth in FY27 and beyond? Please relate to GBR value and assumed growth rate.

13. Table J reflects FY27 growth in GPSR of $65,765 K due to the transfer of beds, while Table G reflects $87,863 K. Given both are uninflated what other assumptions are impacting the UMMC growth rate for FY27 and beyond?

14. The contra revenues to GPSR are consistently 14.9% for the 6 years projected ending FY29. However, such is not consistent with Table H, which reflects 14% for the 3 years ended FY26 and 13.8% for the 3 years ended FY29. Please reconcile the change in assumption.

15. Payroll expenses for FY23 and FY29 do not tie to the same expense for these periods in Table L. Please reconcile.

16. Interest Expense on Current Debt for FY21 through FY23 is inconsistent with the same as presented on the audited financials by the Hospital. ($24,523, $21,080, and $20,782 per Table G versus $16,839, $13,205, and $18,088 per Audit for FY21, FY22, and FY23 respectively). Please reconcile and confirm the presentation format referenced per audit. Also, please explain the source and format for interest projected through FY29.

17. Interest Expense on Project Debt for FY26 through FY29. See point #4 above.

18. Project Depreciation projected for FY26 through FY29 appears to be inconsistent with text on page 11 of CON and inconsistent with Table E. See point #1 above. It is assumed that amortization of project financing should be reflected here as well.

19. Total Operating Expenses reflect an average annual growth of 0.3% for the 6 years ended FY29 implying volume changes in costs. While Total Operating Income reflects an

average annual growth of 0.1% for the 6 years ended FY29 implying volume changes at a slower pace. Please comment on this pre-inflation negative measure of operations planning, and the strategy to mitigate going forward.

Table H (P&L Inflated Entire Facility/Services):

20. The contra revenues to GPSR are less conservative than that of Table G. See Point #14 above.

21. Payroll expenses for FY23 and FY29 do not tie to the same expense for these periods in Table L. See Point #15 above.

Table J (P&L Uninflated New Facility/Services):

22. The contra revenues to GPSR are consistently 13.6% for the 3 years projected ending FY29. However, such is not consistent with Table G.

23. Interest on Project Debt is not consistent with the same item on Table G. Please reconcile.

24. Project Depreciation is not consistent with the same item in Table G. Please reconcile.

Table K (P&L Inflated New Facility/Services):

25. The contra revenues to GPSR are consistently 13.6% for the 3 years projected ending FY29. However, such is not consistent with Table H.

26. Interest on Project Debt is not consistent with the same item in Table H. Please reconcile.

27. Project Depreciation is not consistent with the same item in Table H. Please reconcile.

Please submit four copies of the responses to the above questions and the requests for additional information within ten working days of receipt. Also submit the response electronically, in both Word and PDF format, to Ruby Potter (ruby.potter@maryland.gov) and to mhcc.confilings@maryland.gov. If additional time is needed to prepare a response, please let us know at your earliest convenience.

As with the request itself, all information supplementing the request must be signed by person(s) available for cross-examination on the facts outlined in the supplementary information, who shall sign a statement as follows: "I hereby declare and affirm under the penalties of perjury that the facts stated in this application and its attachments are true and correct to the best of my knowledge, information, and belief."

If you would like a hard copy of this document, the Excel document from which these questions were developed, or should you have any additional questions, please feel free to contact Bob Gallion via phone at (410) 764-5595 or via email at Bob.Gallion@Maryland.gov.

Sincerely,

Rachel Bervell
Program Manager, CON, MHCC

cc: Jerry Schmith, Principal Deputy Director, Hospital Rate Revenue and Regulations, HSCRC
Bob Gallion, Associate Director, Revenue and Regulation Compliance, HSCRC
Allan Pack, Principal Deputy Director, Quality and Population-Based Methodologies, HSCRC
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