



STATE OF WASHINGTON  
DEPARTMENT OF HEALTH

May 1, 2012

CERTIFIED MAIL # 7011 1570 0002 7802 6036

Scott W. Bosch, President & Chief Executive Officer  
Harrison Medical Center  
2520 Cherry Avenue  
Bremerton, Washington 98310

Dear Mr. Bosch:

RE: CN12-10

We have completed review of the Certificate of Need application submitted on behalf of Harrison Medical Center proposing to amend Certificate of Need #1463. For the reasons stated in this evaluation, the application submitted by Harrison Medical Center is consistent with applicable criteria of the Certificate of Need Program, provided Harrison Medical Center agrees to the following in its entirety.

**Project Description:**

Harrison Medical Center is approved to add 50 new medical surgical beds to the Silverdale campus in two phases.

Phase One: Establishment of a new 24-bed medical/surgical unit designed and equipped to specifically address orthopedic care. These beds are expected to be operational in June 2013.

Phase Two: Establishment of a new 26 bed medical/surgical unit. These beds are expected to be operational in December 2015.

At project completion the total number of licensed acute care beds for Harrison Medical Center will be 347. The breakdown of the licensed acute care beds is shown in the table below.

Type of Service	Licensed Beds - Bremerton	Licensed Beds - Silverdale
General Acute Care	242	94
Psychiatric	11	0
<b>Total</b>	<b>253</b>	<b>94</b>



**Conditions:**

1. Approval of the project description as stated above.
2. Harrison Medical Center will provide charity care in compliance with the charity care policies reviewed and approved by the Department of Health. Harrison Medical Center will use reasonable efforts to provide charity care in an amount comparable to or exceeding the average amount of charity care provided by hospitals in the Puget Sound Region. Currently, this amount is 1.95% of gross revenue, and 4.73% of adjusted revenue. Harrison Medical Center will maintain records documenting the amount of charity care it provides and demonstrating its compliance with its charity care policies.

**Approved Costs:**

The approved capital expenditure for the Certificate of Need portion of the project is \$24,963,634.

You have two options, either accept or reject the above in its entirety. If you accept the above in its entirety, your application will be approved and a Certificate of Need sent to you. If you reject any provision of the above, you must identify that provision, and your application will be denied because approval would not be consistent with applicable Certificate of Need review criteria. Please notify the Department of Health within 20 days of the date of this letter whether you accept the above in its entirety.

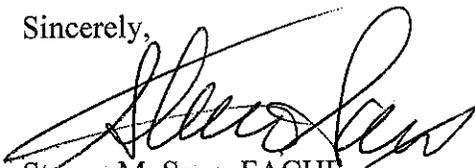
Your written response should be sent to the Certificate of Need Program, at one of the following addresses.

Mailing Address:  
Department of Health  
Certificate of Need Program  
Mail Stop 47852  
Olympia, WA 98504-7852

Other Than By Mail:  
Department of Health  
Certificate of Need Program  
111 Israel Road SE  
Tumwater, WA 98501

If you have any questions, or would like to arrange for a meeting to discuss our decision, please contact Janis Sigman with the Certificate of Need Program at (360) 236-2955.

Sincerely,



Steven M. Saxe, FACHE  
Director, Health Professions and Facilities

Enclosure

**EVALUATION DATED MAY 1, 2012 OF THE CERTIFICATE OF NEED APPLICATION  
SUBMITTED BY HARRISON MEDICAL CENTER (HMC) PROPOSING TO AMEND  
CERTIFICATE OF NEED #1463**

**APPLICANT DESCRIPTION**

Harrison Medical Center (HMC) is a not-for-profit hospital serving the residents of Kitsap County. HMC includes two campuses under one license. The Silverdale campus is located in the city of Silverdale and Bremerton campus is located in the city of Bremerton within Kitsap County. HMC provides Medicare/Medicaid acute care services to residents of Kitsap County and surrounding areas. HMC is currently licensed for 297 acute care beds. The current breakdown of beds is shown below

**Harrison Medical Center  
Current Acute Care Bed Breakdown**

<b>Type of Service</b>	<b>Licensed Beds Bremerton</b>	<b>Licensed Beds Silverdale</b>
General Acute Care	242	44
Psychiatric	11 <sup>1</sup>	0
<b>Total</b>	<b>253</b>	<b>44</b>

HMC was surveyed in 2010 and has an active accreditation from The Joint Commission effective through 2012. In addition to the hospitals, HMC also owns and operates a Medicare certified home health agency and an outpatient clinic in Port Orchard that provides urgent care, imaging, and primary specialty care.

Inpatient services currently provided at campus located in Bremerton include: medical-surgical services, orthopedic services, emergency services, critical care services, cardiovascular services including open heart surgery, rehabilitation services, oncology services, behavioral health, pain management, sleep center, and inpatient dialysis. Inpatient services currently provided at the campus located in Silverdale include mother/baby care, women’s services, outpatient surgery, rehabilitation, and emergency services.

**BACKGROUND INFORMATION**

On November 3, 2008, HMC submitted an application to add 92 beds to its Silverdale campus by transferring 42 beds from the Bremerton campus and adding 50 new beds. At project completion HMC would have been licensed for a total of 347 acute care beds; the Bremerton campus would have 200 acute care beds and 11 psychiatric beds and the Silverdale campus would have 136 acute care beds.

The addition of beds at the Silverdale campus was part of a larger construction project that included completion of a new 6 story patient tower. Construction of the patient tower was expected to commence in January 2009 with the offering of services planned by March 2012. Because of the size

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<sup>1</sup> HMC reported in the September 2009 progress report related to the “Intent To Issue a Certificate of Need” that the 11 psychiatric beds had been closed and converted to medical/surgical use. On December 2, 2009, the Certificate of Need Program notified HMC that these dedicated psychiatric beds could not be converted without a Certificate of Need.

of the construction project, HMC was required to obtain a conditional use permit. The department is precluded from issuing a Certificate of Need until an applicant obtains a conditional use permit. As a result, on June 1, 2009 the department issued an “Intent to Issue” a Certificate of Need for the project. On, February 9, 2012, HMC provided the department with a copy of its conditional use permit from the Kitsap County Department Community Development. As a result, Certificate of Need #1463 was issued to HMC on February 24, 2012. [Source: Amendment Application, pp3 & 8]

### **PROJECT DESCRIPTION**

After the department’s June 1, 2009 Intent to Issue CN approval; HMC began to secure the Conditional Use Permit. During this time, the economy fell into a recession, affecting health care utilization and access to capital for all hospitals. These two issues resulted in HMC re-evaluating the project as originally proposed. After nearly a year of re-evaluation, HMC determined that the size of the original project (\$205 million in total for the construction of a 6 story tower) needed to be scaled back because of land use issues and access to capital. [Source: Amended application, p9]

With this application, HMC proposes to amend CN#1463 with the following changes:

1. Reduce the number of beds to be added to the Silverdale campus from 92 to 50 beds. The 50 beds would be ‘new’ beds and no beds would be transferred from the Bremerton campus. The Bremerton campus will remain at 242 medical/surgical beds and 11 psychiatric beds, and the Silverdale campus will have 94 medical/surgical beds (50 new and 44 existing) for a total licensed acute care bed capacity of 347. [Source: Amended application, p12]
2. Reduce the CN capital expenditure from \$69,044,583 to \$24,963,634. Since the construction project has been modified and the number of beds reduced, the capital expenditure was reduced by approximately 64%.

### **APPLICABILITY OF CERTIFICATE OF NEED LAW**

This project is subject to review under WAC 246-310-570(1)(c) because the number of beds to be added to the Silverdale site will decrease, the capital costs of the project are reduced, and the timing of the project has changed.

### **CRITERIA EVALUATION**

WAC 246-310-200(1)(a)-(d) identifies the four determinations that the department must make for each application. WAC 246-310-200(2) provides additional direction in how the department is to make its determinations. It states:

*“Criteria contained in this section and in WAC 246-310-210, 246-310-220, 246-310-230, and 246-310-240 shall be used by the department in making the required determinations.*

*(a) In the use of criteria for making the required determinations, the department shall consider:*

- (i) The consistency of the proposed project with service or facility standards contained in this chapter;*
- (ii) In the event the standards contained in this chapter do not address in sufficient detail for a required determination the services or facilities for health services proposed, the department may consider standards not in conflict with those standards in accordance with subsection (2)(b) of this section; and*

- (iii) *The relationship of the proposed project to the long-range plan (if any) of the person proposing the project.*

In the event WAC 246-310 does not contain service or facility standards in sufficient detail to make the required determinations, WAC 246-310-200(2)(b) identifies the types of standards the department may consider in making its required determinations. Specifically WAC 246-310-200(2)(b) states:

*“The department may consider any of the following in its use of criteria for making the required determinations:*

- (i) Nationally recognized standards from professional organizations;*
- (ii) Standards developed by professional organizations in Washington state;*
- (iii) Federal Medicare and Medicaid certification requirements;*
- (iv) State licensing requirements;*
- (v) Applicable standards developed by other individuals, groups, or organizations with recognized expertise related to a proposed undertaking; and*
- (vi) The written findings and recommendations of individuals, groups, or organizations with recognized expertise related to a proposed undertaking, with whom the department consults during the review of an application.”*

The review for an amendment project is limited to only those criteria that would be affected by the amendment, provided that the amendment does not significantly alter the project. While HMC’s initial project was significantly delayed and the cost of the project is decreasing; the number of new beds to be added to the Silverdale campus remains at 50. The department’s review will focus on applicable portions of financial feasibility (WAC 246-310-220) and cost containment (WAC 246-310-240).<sup>2</sup>

Certificate of Need #1463 was issued with a condition related to the provision of charity care to be provided at HMC as required under WAC 246-310-210(2)(b). Given the significant time that has lapsed between the initial approval (June 1, 2009) and the issuance of CN #1263 (February 24, 2012), this condition will be re-evaluated to incorporate the most recent charity care data.

If this amendment project is approved, the department would include the updated charity care condition as previously described.

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<sup>2</sup> Each criterion contains certain sub-criteria. The following sub criteria are not relevant to this project: WAC 246-310-210(1), (3), (4), (5) and (6) and WAC 246-310-230.

## **APPLICATION CHRONOLOGY**

<b>Action</b>	<b>HMC</b>
Letter of Intent Submitted	April 7, 2011
Application Submitted	October 7, 2011
Department's pre-review Activities including screening and responses	October 8, through December 17, 2011
Beginning of Review <ul style="list-style-type: none"><li>public comments accepted throughout review (no public comments were submitted);</li><li>no public hearing conducted under the expedited review rules</li></ul>	December 18, 2011
End of Public Comment	January 4, 2012
Rebuttal Comments due	January 20, 2012
Department Declares Pivotal Unresolved Issue (PUI)	February 13, 2012
Applicant Submits PUI documents	February 21, 2012
Public Comments on PUI Documents	March 12, 2012
Rebuttal Comments Submitted for PUI Documents <sup>3</sup>	March 27, 2012
Department's Anticipated Decision Date	April 26, 2012
Department's Actual Decision Date	May 1, 2012

## **AFFECTED PERSONS**

Washington Administrative Code 246-310-010(2) defines "*affected person*" as:

"...an "*interested person*" who:

- (a) *Is located or resides in the applicant's health service area;*
- (b) *Testified at a public hearing or submitted written evidence; and*
- (c) *Requested in writing to be informed of the department's decision.*"

Throughout the review of this project, no entities sought and received affected person status under WAC 246-310-010(2).

## **SOURCE INFORMATION REVIEWED**

- Harrison Medical Center's Certificate of Need amendment application submitted October 7, 2011
- Harrison Medical Center's supplemental information received December 8, 2011
- Harrison Medical Center's PUI Supplemental Information received on February 21, 2012
- The department's May 20, 2009, initial evaluation approving Harrison Medical Center's addition of 92 beds to the Silverdale campus and reduction of 42 beds at the Bremerton campus
- "Intent to Issue CN" dated June 1, 2009
- Certificate of Need #1463 issued on February 24, 2012

<sup>3</sup> Public comments on the PUI documents were due on March 12, 2012. There were no comments submitted, therefore the applicant did not provide any rebuttal comments.

**SOURCE INFORMATION REVIEWED (continued)**

- Quarterly Progress Reports completed and submitted by Harrison Medical Center related to the Intent to Issue [Reports submitted quarterly beginning in September 2009, and each quarter thereafter for years 2010 through October 2011]
- Financial Feasibility and cost containment evaluation prepared by the Department of Health’s Hospital and Patient Data Systems dated January 10, 2012
- Joint Commission website [www.jointcommission.org]

**CONCLUSIONS**

For the reasons stated in this evaluation, the application submitted by Harrison Medical Center proposing to amend Certificate of Need #1463 because of a decrease in the number of beds to be added to the Silverdale campus, a reduction in the capital costs of the project, and a change in the timing of the project is consistent with applicable criteria of the Certificate of Need Program, provided Harrison Medical Center agrees to the following in its entirety.

**Project Description:**

Harrison Medical Center is approved to add 50 new medical surgical beds to the Silverdale campus in two phases.

- Phase One: Establishment of a new 24-bed medical/surgical unit designed and equipped to specifically address orthopedic care. These beds are expected to be operational in June 2013.
- Phase Two: Establishment of a new 26 bed medical/surgical unit. These beds are expected to be operational in December 2015.

At project completion the total number of licensed acute care beds for Harrison Medical Center will be 347. The breakdown of the licensed acute care beds is shown in the table below.

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General Acute Care	242	94
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<b>Total</b>	<b>253</b>	<b>94</b>

**Conditions:**

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2. Harrison Medical Center will provide charity care in compliance with the charity care policies reviewed and approved by the Department of Health. Harrison Medical Center will use reasonable efforts to provide charity care in an amount comparable to or exceeding the average amount of charity care provided by hospitals in the Puget Sound Region. Currently, this amount is 1.95% of gross revenue, and 4.73% of adjusted revenue. Harrison Medical Center will maintain records documenting the amount of charity care it provides and demonstrating its compliance with its charity care policies.

**Approved Costs:**

The approved capital expenditure for the Certificate of Need portion of the project is \$24,963,634

#### **A. Need (WAC 246-310-210) and Acute Care Bed Forecasting Method**

Based on the source information reviewed and the Harrison Medical Center's agreement to the condition identified in the "Conclusion" section of this evaluation, the department determines that the application is consistent with the applicable need criteria in WAC 246-310-210.

- (1) The population served or to be served has need for the project and other services and facilities of the type proposed are not or will not be sufficiently available or accessible to meet that need.

#### **HMC's Initial Evaluation Summary**

In its May 20, 2009, initial evaluation supporting the "Intent to Issue" CN and CN#1463, the department concluded that this sub-criterion was met based on the following factors:

- 1) The department's numeric hospital bed need methodology outlined in the 1987 Washington State Health Plan projected a need for 50 additional acute medical/surgical beds in Kitsap County.
- 2) HMC provided the documentation that they were the only hospital in the Kitsap planning area and were qualified to accomplish the project.

#### **HMC Amendment Application Review**

With this amendment, HMC proposes to add 50 new beds to the Silverdale campus and not relocate any beds from the Harrison campus. Since this amendment project does not propose to revise the number of new beds to be added in the planning area (Kitsap County), the department concludes **this sub-criterion remains met.**

- (2) All residents of the service area, including low-income persons, racial and ethnic minorities, women, handicapped persons, and other underserved groups and the elderly are likely to have adequate access to the proposed health service or services.

#### **HMC's Initial Evaluation Summary**

- 1) The department concluded that this criterion was met with the condition that HMC meet the 2005 to 2007 three year charity care average for the Puget Sound Region.
- 2) HMC provided their admissions policy, and documentation of Medicare certification, Medicaid eligibility, and charity care policy confirming their accessibility to the above populations.

#### **HMC Amendment Application Review**

As previously stated, the department obtained updated charity care data for 2008, 2009 and 2010. For charity care reporting purposes, the Department of Health's Hospital and Patient Data Systems (HPDS), divides Washington State into five regions: King County, Puget Sound (less King County), Southwest, Central, and Eastern. Located in Kitsap County, HMC is one of 18 hospitals in the Puget Sound Region. According to 2008-2010<sup>45</sup> charity care data obtained from HPDS, HMC has historically provided less than the average charity care provided in the region based on total revenue and more than the average based on adjusted revenue. HMC's most recent three years (2008-2010) percentages of charity care for gross and adjusted revenues are 1.80% and

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<sup>4</sup> Year 2011 charity care data is not available at this time.

5.31%, respectively. The 2008-2010 average for the Puget Sound Region is 1.95% for gross revenue and 4.73% for adjusted revenue. [source: HPDS 2008-2010 charity care summaries]

**Table 1  
HMC Charity Care Comparison**

	<b>3-Year Average for Puget Sound Region</b>	<b>3 Year Average for HMC</b>
<b>% of Gross Revenue</b>	1.95%	1.80%
<b>% of Adjusted Revenue</b>	4.73%	5.31%

RCW 70.38.115(2)(j) requires hospitals to meet or exceed the regional average level of charity care. Since HMC’s historical percent of gross revenue is currently less than the average for the region and HMC projects to provide less than the regional average the department will need to condition this project. The department concludes that all residents, including low income, racial and ethnic minorities, handicapped, and other underserved groups would have access to the services provided by the hospital; provided that HMC agrees with the condition related to charity care. **This sub-criterion is met.**

**B. Financial Feasibility (WAC 246-310-220)**

Based on the source information reviewed and the Harrison Medical Center’s agreement to the conditions identified in the ‘Conclusion section of this evaluation, the department determines that the applicant has met the financial feasibility criteria in WAC 246-310-220.

*(1) The immediate and long-range capital and operating costs of the project can be met.*

WAC 246-310 does not contain specific WAC 246-310-220(1) financial feasibility criteria as identified in WAC 246-310-200(2)(a)(i). There are also no known recognized standards as identified in WAC 246-310-200(2)(a)(ii) and (b) that directs what the operating revenues and expenses should be for a project of this type and size. Therefore, using its experience and expertise the department evaluates if the applicant’s pro forma income statements reasonably project the proposed project is meeting its immediate and long-range capital and operating costs by the end of the third complete year of operation.

**HMC’s Initial Evaluation Summary**

In its initial application HMC proposed a much larger overall project (\$204,975,927) and also a larger Certificate of Need project (\$69,044,583). In its May 20, 2009, initial evaluation supporting the “Intent To Issue” CN and issuance of CN #1463, the department concluded that this sub-criterion was met based on the following factors:

- 1) a review of HMC’s projected utilization based on acute care days. This review included proposed revenues, expenses, and net profit for its first three years of operation—2013, 2014, and 2015 following completion of the project; and
- 2) a review of HMC’s historical audited financial reports filed with HPDS. [Source: Initial evaluation pp9-10]

The department concluded that the proposed project would have a considerable impact on the hospital, but it would not adversely impact the financial health of the health of the hospital if the projected patient volume was realized

**HMC Amendment Application Review**

To comply with this sub-criterion HMC provided its assumptions, forecasted pro forma income statements, and forecasted balance sheets. [Source: December 8, 2011, Supplemental Information, Attachment 1]

To determine if the facility would meet its immediate and long range operating costs with this project, the department reviewed the assumptions used as a basis for its financial projections. Additionally, the department reviewed HMC’s financial statements for its first three full years of operation. Summarized below are the assumptions used by HMC as the basis for projecting number of patients and patient days it expects.

- HMC reduced its projected number of patients and patient days for the amendment based on the decline in utilization experienced in 2009 and 2010. HMC is anticipating that growth in utilization will be slower than previously projected.
- HMC is not expecting any change in anticipated sources of revenue by payor
- HMC is anticipating reduced operating costs and capital costs for the amended project

The table below shows a summary of the projected number of beds, patients and number of patient days based on the assumptions above.

**Table 2  
HMC Utilization Projection Years 2013-2018**

	<b>2013</b>	<b>2014</b>	<b>2015</b>	<b>2016</b>	<b>2017</b>	<b>2018</b>
# of Beds	336	336	336	336	336	336
# of Patients	16,084	17,511	18,881	20,327	21,769	22,012,
# of Patient Days	62,729	68,294	73,635	79,275	84,900	85,848
% Occupancy	51.1%	55.7%	60.0%	64.6%	69.2%	70.0%

Revenue and expense statements for years 2013-2018, based on the projected number of patient days. [Source: December 8, 2011, Supplemental Information, Attachment 1] For this amendment project, HMC also revised its revenue and expense statements based on the reduced patient days and project changes. The table on the following page is a summary of the revenue and expense statement for phase one of the project.

**Table 3A**  
**Harrison Medical Center**  
**Phase One Years 2013 – 2015**  
**Revised Revenue and Expense Statement Summary**

	<b>2013</b>	<b>2014</b>	<b>2015</b>
<b>Net Revenue</b>	<b>\$403,684,000</b>	<b>\$439,497,000</b>	<b>\$473,868,000</b>
Operating Expenses	\$389,107,000	\$417,545,000	\$442,728,000
<b>Net Profit or (Loss)</b>	<b>\$14,577,000</b>	<b>\$21,953,000</b>	<b>\$31,140,000</b>

Source: HPDS Analysis p4

The ‘net revenue’ line item in table 3A is the result of gross revenue minus any deductions plus other revenue. The ‘total expenses’ line item includes staff salaries/wages and other direct expenses. As shown in Table 3A HMC projects a net profit the first three years of operation (Phase One) with 336 beds. When compared with the initial project, HMC projected a net loss in years one and two, and a profit in year three.

The table below is a summary of the revenue and expense statement for phase two of the project.

**Table 3B**  
**Harrison Medical Center**  
**Phase two Years 2016 – 2018 Revised Revenue and Expense Statement Summary**  
**Phase 2**

	<b>2016</b>	<b>2017</b>	<b>2018</b>
<b>Net Revenue</b>	<b>\$510,164,000</b>	<b>\$546,363,000</b>	<b>\$552,464,000</b>
Operating Expenses	\$468,738,000	\$494,432,000	\$498,731,000
<b>Net Profit or (Loss)</b>	<b>\$41,426,000</b>	<b>\$51,931,000</b>	<b>\$53,733,000</b>

Source: HPDS Analysis p4

The ‘net revenue’ line item in table 3B is the result of gross revenue minus any deductions plus other revenue. The ‘total expenses’ line item includes staff salaries/wages and other direct expenses. As shown in Table 3B with the assumed reduction in patient days updated expenses, and cost allocations for HMC, the revised statements show a net profit in the first three years of phase two.

In addition to reviewing the projected statement of operations, the department reviews the most current hospital balance sheet. HPDS staff reviewed the 2010 balance sheet for HMC and also evaluated this project against various assets of the hospital in the 2010 balance sheet. A summary of the 2010 Balance sheet is shown on the following page.

**Table 4  
HMC 2010 Actual  
Balance Sheet**

<b>Assets</b>		<b>Liabilities</b>	
Current Assets	\$79,214,097	Current Liabilities	\$39,381,129
Board Designated Assets	\$110,113,464	Long Term Debt	\$87,396,615
Property/Plant/Equip.	\$109,153,430	Other	\$39,259,724
Other	\$47,960,302	<b>Equity</b>	<b>\$180,403,825</b>
<b>Total Assets</b>	<b>\$346,441,293</b>	<b>Total Liabilities and Equity</b>	<b>\$346,441,293</b>

The table below shows the comparison of this project with the various assets of HMC at 2010 fiscal year end

**Table 5  
Harrison Medical Center  
Certificate of Need portion of project**

Capital Expenditure	\$24,963,634
Percent of Total Assets	7.2%
Percent of Board Designated Assets	22.7%
Percent of Equity	13.8%

As shown in Table 5 the project will have a minimal impact on the assets of the hospital. The CN portion of the project is only 22.7% of Board designated assets and 13.8% of equity. The overall project submitted in the amendment application is much smaller (\$35,000,000) and the Certificate of Need project (\$24,963,634) is also much smaller.

Since the project continues to have two phases, HPDS also reviewed the 2018 balance sheet which is 3 years after completion of Phase two.

**Table 6  
HMC 2018 Projected  
Balance Sheet**

<b>Assets</b>		<b>Liabilities</b>	
Current	\$104,850,000	Current	\$48,983,000
Board Designated	\$392,253,000	Long Term Debt	\$92,005,000
Property/Plant/Equip.	\$110,613,000	Other	\$24,400,000
Other	\$1,416,000	<b>Equity</b>	<b>\$443,744,000</b>
<b>Total Assets</b>	<b>\$609,132,000</b>	<b>Total Liabilities and Equity</b>	<b>\$609,132,000</b>

Table 6 contains the projected balance sheet for third year of phase 2 of the project. The data in Table 6 indicates that HMC is projecting to have a minimal increase in long term debt and a substantial increase in their equity.

HPDS also reviewed various ratios that can give a snap shot of the financial health of HMC as of 2010. Also detailed are the first six years of the project at the project level. State 2010 ratios are included as a comparison and are calculated from all community hospitals in Washington State whose fiscal year ended in 2010. The data is collected by the Washington State Department of Health Hospital and Patient Data section of the Center for Health Statistics. This information is shown in the tables below.

**Table 7A  
Current and Projected HPDS Debt Ratios for HMC  
Phase One**

Category	Trend <sup>6</sup>	State	HMC	Projected		
		2010	2010	2013	2014	2015
Long Term Debt to Equity	B	0.554	0.484	0.470	0.416	0.357
Current Assets/Current Liabilities	A	2.281	2.011	2.176	2.151	2.152
Assets Funded by Liabilities	B	0.366	0.366	0.366	0.345	0.318
Operating Expense/Operating Revenue	B	0.947	0.946	0.964	0.950	0.934
Debt Service Coverage	A	5.892	7.150	4.475	4.830	5.761
<b>Definitions:</b>	<b>Formula</b>					
Long Term Debt to Equity	Long Term Debt/Equity					
Current Assets/Current Liabilities	Current Assets/Current Liabilities					
Assets Funded by Liabilities	Current Liabilities + Long term Debt/Assets					
Operating Expense/Operating Revenue	Operating expenses / operating revenue					
Debt Service Coverage	Net Profit+Depr. and Interest Exp/Current Mat. LTD and Interest Exp					

**Table 7B  
Projected HPDS Debt Ratios for HMC  
PHASE Two**

Category	Trend <sup>7</sup>	State	Projected		
		2010	2016	2017	2018
Long Term Debt to Equity	B	0.554	0.030	0.248	0.207
Current Assets/Current Liabilities	A	2.281	2.144	2.141	2.138
Assets Funded by Liabilities	B	0.366	0.289	0.258	0.232
Operating Expense/Operating Revenue	B	0.947	0.919	0.905	0.903
Debt Service Coverage	A	5.892	6.639	7.640	7.780
<b>Definitions:</b>	<b>Formula</b>				
Long Term Debt to Equity	Long Term Debt/Equity				
Current Assets/Current Liabilities	Current Assets/Current Liabilities				
Assets Funded by Liabilities	Current Liabilities + Long term Debt/Assets				
Operating Expense/Operating Revenue	Operating expenses / operating revenue				
Debt Service Coverage	Net Profit+Depr. and Interest Exp/Current Mat. LTD and Interest Exp				

Tables 7A and 7B show that while this project will have an impact to the hospital; it will not adversely impact the financial health of the hospital if the patient volume is realized. The 2010

<sup>6</sup> A is better if above the ratio, and B is better if below the ratio.

<sup>7</sup> A is better if above the ratio, and B is better if below the ratio.

current asset to current liabilities is the only ratio for HMC that is out of range. However, the difference is not substantial. Long-Term Debt to Equity Ratio at the end of 2010 fiscal year is 0.484 which is better than the 2010 state average of 0.554 as calculated by HPDS staff. The ratios for Certificate of Need year 2018 for HMC as a whole are better than the state average or are within a reasonable range. Long Term Debt to Equity and the Debt Service Coverage are improving each year. These ratios are normally going to be out of range for a new project due to the new debt added for this project. The hospital is breaking even by the end of the sixth year. [Source: HPDS analysis, p3]

Based on the information above, the department concludes that the immediate and long-range operating costs of the project can be met. **This sub-criterion is met.**

- (2) The costs of the project, including any construction costs, will probably not result in an unreasonable impact on the costs and charges for health services.

WAC 246-310 does not contain specific WAC 246-310-220(2) financial feasibility criteria as identified in WAC 246-310-200(2)(a)(i). There are also no known recognized standards as identified in WAC 246-310-200(2)(a)(ii) and (b) that directs what an unreasonable impact on costs and charges would be for a project of this type and size. Therefore, using its experience and expertise the department compared the proposed project's costs with those previously considered by the department.

#### **HMC's Initial Evaluation Summary**

In its May 20, 2009, evaluation supporting the "Intent To Issue" CN and the issuance of CN #1463, the department concluded that this sub-criterion was met based on the following factors:

- 1) HMC's basis for establishing its construction costs for the project; and
- 2) construction cost analysis provided by HPDS dated March 26, 2009.

[Source: Initial evaluation, p18]

#### **HMC Amendment Application Review**

In this amendment application, HMC has reduced the scope of overall project substantially. The Certificate of Need portion of the project has also been reduced by approximately 50%. This reduction in the size of the project lessens the impact of this project on HMC's costs and charges

HMC submitted a non-binding construction cost estimator letter stating that the proposed construction costs for this project are reasonable. [source: February 21, 2012, Supplemental Information, Attachment 3] The construction cost analysis provided by HPDS staff states the construction costs are reasonable when compared to similar projects previously reviewed. [Source: HPDS analysis, pp3 & 4]

Based on the information above, the department concludes **this sub-criterion remains met.**

- (3) The project can be appropriately financed.

WAC 246-310 does not contain specific source of financing criteria as identified in WAC 246-310-200(2)(a)(i). There are also no known recognized standards as identified in WAC 246-310-200(2)(a)(ii) and (b) that directs how a project of this type and size should be financed. Therefore, using its experience and expertise the department compared the proposed project's source of financing to those previously considered by the department.

**HMC’s Initial Evaluation Summary**

In its May 20, 2009, evaluation supporting the “Intent To Issue” CN and the issuance of CN #1463, the department evaluated HMC’s funding for the project. In the initial application, HMC intended to fund the project through bonds. The department concluded that this method of funding was reasonable and this sub-criterion was met based on the following factors:

- 1) HMC’s basis for establishing its construction costs for the hospital; and
  - 2) HMC’s historical financial analysis provided by HPDS staff analysis dated March 20, 2009.
- [Source: Initial evaluation, pp14 & 15]

**HMC Amendment Application Review**

In the initial application, HMC identified a capital cost for the Certificate of Need portion of the project of \$69,044,583 and intended to fund the project with bonds. For this amendment project, HMC states that the project will be funded through two sources:

- Phase One - non taxable bonds
- Phase Two hospital reserves

In addition to the information submitted by HMC, the department has obtained a copy of HMC’s application for financial assistance submitted to the Washington Health Care Facilities Authority (WHCFA). During the review of this amendment project, the department unable to reconcile the information provided to WHCFA with the information provided in this amendment application. Therefore, the department declared a Pivotal Unresolved Issue on February 14, 2012. HMC was directed to send information clarifying the differences in financing between the two applications and identify the correct amounts. In the response to the PUI, HMC submitted the information summarized in the table below.

**Table 8  
Financing Comparison  
Certificate of Need Application and WHCFA Loan Application**

	C of N Application			WHCFA Loan Application		
	Phase One	Phase Two	Total	Phase One	Phase Two	Total
Land Improve	\$1,322,518	\$0	\$1,322,518	\$1,322,518	\$0	\$1,322,518
Bldg. Construct.	\$10,212,844	\$3,583,645	\$13,796,489	\$11,053,953	\$3,583,645	\$14,637,598
Equipment	\$3,734,803	\$986,386	\$4,751,189	\$4,520,054	\$986,386	\$5,506,440
Architect/Eng.	\$1,147,986	\$0	\$1,147,986	\$1,605,081	\$0	\$1,605,081
Consulting Fees	\$30,000	\$0	\$30,000	\$30,000	\$0	\$30,000
Site preparation	\$250,000	\$112,501	\$362,501	\$250,000	\$112,501	\$362,501
Supervision.	\$85,028	\$0	\$85,028	\$92,031	\$0	\$92,031
Debt Costs	\$314,286	\$0	\$314,286	\$416,009	\$0	\$416,009
Interim Interest	\$1,363,033	\$0	\$1,363,033	\$1,358,963	\$0	\$1,358,963
Sales Tax	\$1,315,183	\$430,003	\$1,745,187	\$1,465,390	\$430,003	\$1,895,393
Other Costs	\$45,418	\$0	\$45,418	\$45,418	\$0	\$45,418
<b>Total</b>	<b>\$19,851,099</b>	<b>\$5,112,535</b>	<b>\$24,963,634</b>	<b>\$22,159,417</b>	<b>\$5,112,535</b>	<b>\$27,271,952</b>

Source: February 21, 2012 Response to PUI

HMC reported that the differences in costs between the two applications are due to timing and refinements in the design of the planned facility. The Certificate of Need application was

completed in October of 2011 and the WHCFA application was completed in January of 2012. The WHCFA application represents more refined cost estimates for construction and equipment.

One major cost change encountered by HMC is additional costs to remodel the sterile processing area which does not require Certificate of Need review. During the course of the building plan review, HMC determined that their current sterile processing area meets Joint Commission and Department of Health requirements; its configuration was not adequate to meet HMC's newer infection control standards without significant work a rounds. The detailed work planning work on this amendment project will begin in March and is expected to be completed with the improvements by the end of 2012. [Source: February 21, 2012 Response to PUI, p3]

Other cost changes are due to improvements to the facility plan. HMC is expanding the size of the waiting room, creating additional space for medical equipment storage, and making upgrades to the building heating system from reheat to hydronic, and added other functional and aesthetic architectural improvements.

HMC also addressed the difference in financing costs raised by the two applications. The costs for financing within the Certificate of Need application include interim interest payments of (\$1,363,033) as well as an estimated portion of the costs for securing for securing the bond (\$314,286). The amount listed on the WHCFA application includes a more current estimate of the costs of issuance (\$700,000) and is consistent with the costs associated with the full \$35,000,000 bond (larger than the Certificate of Need project). The Certificate of Need portion of the \$700,000 cost of issuance is estimated to be \$416,009. HMC notes that normally the bond process would occur after the Certificate of Need process and thus not having the issue of different numbers. [Source: February 21, 2012 Response to PUI, p2]

The department concludes that HMC demonstrated a financial commitment for this project and it can be appropriately financed. The project as amended has substantially less impact on assets of the hospital, and given the recent economic conditions, appears to be a better solution for the needs of the hospital and the community. **This sub-criterion is met.**

### **C. Cost Containment (WAC 246-310-240)**

Based on the source information reviewed and provided that Harrison Medical Center agrees to the conditions identified in the 'conclusion' section of this evaluation, the department determines that the application has met the cost containment criteria in WAC 246-310-240.

- (1) Superior alternatives, in terms of cost, efficiency, or effectiveness, are not available or practicable. WAC 246-310 does not contain specific WAC 246-310-240(1) as identified in WAC 246-310-200(2)(a)(i). There are also no known recognized standards as identified in WAC 246-310-200(2)(a)(ii) and (b) that directs what superior alternatives, in terms of cost, efficiency, or effectiveness should be for a project of this type and size. Therefore, using its experience and expertise the department assessed the materials contained in the application.

To determine if a proposed project is the best alternative, the department takes a multi-step approach. Step one determines if the application has met the other criteria of WAC 246-310-210

thru 230. If it has failed to meet one or more of these criteria then the project is determined not to be the best alternative, and would fail this sub-criterion.

If the project met WAC 246-310-210 through 230 criteria, the department would move to step two in the process and assess the other options the applicant or applicants considered prior to submitting the application under review. If the department determines the proposed project is better or equal to other options the applicant considered before submitting their application, the determination is either made that this criterion is met (regular or expedited reviews), or in the case of projects under concurrent review, move on to step three.

Step three of this assessment is to apply any service or facility specific criteria (tie-breaker) contained in WAC 246-310. The tiebreaker criteria are objective measures used to compare competing projects and make the determination between two or more approvable projects which is the best alternative. If WAC 246-310 does not contain any service or facility criteria as directed by WAC 246-310-200(2)(a)(i), then the department would look to WAC 246-310-240(2)(a)(ii) and (b) for criteria to make the assessment of the competing proposals. If there are no known recognized standards as identified in WAC 246-310-200(2)(a)(ii) and (b), then using its experience and expertise, the department would assess the competing projects and determine which project should be approved.

### **HMC's Initial Evaluation Summary**

In its March 20, 2009, initial evaluation supporting the issuance of CN #1463, the department concluded that this sub-criterion was met based on the following factors:

- 1) a review of the options considered by HMC before submitting the initial application; and
- 2) the numeric hospital bed need methodology outlined in the 1987 Washington State Health Plan projected a need for additional acute medical/surgical bed capacity in Kitsap County.

As a result, the department concluded HMC's project was the best alternative for Kitsap County, and HMC's bed addition project for the Silverdale campus was approved. [Source: Initial evaluation, pp 22 & 23]

### **HMC Amendment Application Review**

To evaluate HMC's amendment project, the department begins with the three steps identified above.

#### **Step One**

For this project, HMC has met the applicable review criteria under WAC 246-310-210 and WAC 246-310-220. Therefore, the department moves to step two below.

#### **Step Two**

HMC is proposing to add the 50 new acute care medical/surgical beds proposed in the initial application. The applicant reports that recent historical patient days at HMC have decreased and thus they have re-evaluated the projected patient days for this project. HMC has substantially reduced the scope and cost of this project to better serve the community in a more cost efficient manner. Reviewing the information provided by HMC, the department is in agreement with HMC that this project is a better alternative at this time.

Step Three

This step is used to determine between two or more approvable projects which is the best alternative. This step does not apply to this amendment project.

Based on the information above, the department concludes this project is the best available alternative for the residents of Kitsap County. **This sub-criterion is met.**

(2) In the case of a project involving construction:

(a) The costs, scope, and methods of construction and energy conservation are reasonable; and

This sub-criterion is evaluated within the financial feasibility criterion under WAC 246-310-220(2). Based on that evaluation, the department concludes that **this sub-criterion is met.**

(b) The project will not have an unreasonable impact on the costs and charges to the public of providing health services by other persons.

This sub-criterion is evaluated within the financial feasibility criterion under WAC 246-310-220(2). Based on that evaluation, the department concludes that **this sub-criterion is met.**