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NO. 95967-6

SUPREME COURT OF THE STATE OF WASHINGTON

SIGNATURE HEALTHCARE SERVICES, LLC,

Petitioner,

v.

WASHINGTON STATE DEPARTMENT OF HEALTH,

Respondent, and

SPRINGSTONE, LLC,

Respondent Intervenor.

STATE'S ANSWER TO PETITION FOR REVIEW

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I. INTRODUCTION

The Legislature enacted Revised Code of Washington (RCW) 70.38 to contain health costs by limiting the establishment of new healthcare facilities to those necessary to meet community need. The Washington State Department of Health (Department) implements RCW 70.38 by issuing Certificates of Need (CN) to applicants who prove they satisfy all criteria for obtaining a CN. The Petition for Review (Petition) filed by applicant Signature Healthcare Services, LLC (Signature) attempts to manufacture issues of substantial public interest, but this is nothing more than a routine Administrative Procedures Act (APA) judicial review in which Signature failed to meet its burden of proof because it submitted a deficient application and failed to satisfy all the criteria for obtaining a CN.

Signature's Petition does not present an issue of substantial public interest, nor does the Court of Appeals' unpublished opinion conflict with a decision of the Supreme Court. Rules of Appellate Procedure (RAP) 13.4(b)(1), (4). The Court of Appeals fully considered the facts and the law before concluding the Department properly (1) required Signature to provide a draft 20-year lease to establish sufficient interest in its proposed hospital facility when the project it proposed included a lease; (2) required the draft lease to include all costs; and (3) concluded that Signature failed to prove its project was financially feasible and would foster cost

containment when it submitted a deficient draft lease. The new and modified theories that Signature offers to justify its failure in its Petition are unavailing.

II. COUNTERSTATEMENT OF THE ISSUES

If this Court were to accept review, the issues would be:

1. Did the Department properly treat parent corporations as "applicants" where CN applications and supplemental submissions identified those parent corporations as "applicants?"
2. Did the Department properly conclude that a CN applicant who submits only a 5-year hospital lease with no option to renew fails to demonstrate sufficient site control where the Department requires a lease for at least five years with options to renew for at least 20 years if a CN applicant proposes to lease a hospital facility from a separate legal entity?
3. Did the Department properly require a CN applicant to submit a draft lease for at least five years with options to renew for at least 20 years where the CN applicant proposed a project where it would own the land, but not the hospital facility to be built on the land by a separate legal entity, and where a subsidiary of a CN applicant planned to rent the facility from the separate legal entity that would own the hospital building?
4. Did the Department properly deny the CN application where the Department requires a lease with all associated costs but the applicant submitted a lease that did not include monthly or annual rent, or a methodology for calculating the rent?

III. COUNTERSTATEMENT OF THE CASE

A. Background

1. The CN application process

Under RCW 70.38 and Washington Administrative Code (WAC) 246-310, healthcare providers must obtain a CN from the Department before establishing a new healthcare facility. RCW 70.38.105(4)(a), .025(6). To obtain a CN, the healthcare provider submits an application "in such form and manner and containing such information as the department has prescribed and published as necessary to such a certificate of need application." WAC 246-310-090(1)(a); RCW 70.38.115. The Department screens the application to determine if it is complete. WAC 246-310-090(2)(a). If incomplete, the Department may request supplemental information through screening questions. WAC 246-310-090(2). If more than one provider submits applications to provide services in the same planning area, the Department reviews the competing applications concurrently. RCW 70.38.115(7); WAC 246-310-110(2)(d).

A CN applicant has the burden of satisfying certain criteria including, but not limited to, financial feasibility and cost containment. WAC 246-310-220, -240. Failure to meet the criteria will result in denial of the application. An aspect of satisfying financial feasibility is proving site control, and the Department's CN application requires applicants to submit

documentation to establish that the applicant can use the location for the stated purpose and relevant period of time. Administrative Record (AR) at 1821, WAC 246-310-090(1)(a). The Department may deny a CN application when an applicant fails to submit required or necessary information. RCW 70.38.115(6); WAC 246-310-090(1)(a), (c),-490(1)(b)(ii).

2. Clark County concurrent review applications

Signature applied for a CN to establish a psychiatric hospital in Vancouver, Clark County. AR at 1811-2104. The application identified four separate entities in its organizational structure: Signature, Vancouver Life Properties, LLC (Vancouver Life Properties), Vancouver Behavioral Healthcare Hospital, LLC (Vancouver Behavioral Health), and another corporation that is not relevant to this matter. AR at 1865, 2121-22. According to Signature's application, Signature would own the land underlying the hospital facility; Vancouver Life Properties would own the hospital facility; and Vancouver Behavioral Healthcare (a wholly-owned subsidiary of Signature) would rent the facility from Vancouver Life Properties to operate the hospital. AR at 1865, 1881-1906, 2121-22. Dr. Soon K. Kim owns all the entities, either directly or as the owner of Signature. AR at 1865.

To establish site control, Signature provided a purchase and sales real estate agreement for the land that would underlie the facility. AR at 1881-1906. Signature did not submit a copy of the lease agreement between the Vancouver Life Properties and Vancouver Behavioral Health. In screening questions, the Department's CN Program (Program) requested that Signature provide a copy of the lease between Vancouver Life Properties and Vancouver Behavioral Health that identified all costs associated with the agreement. AR at 2196-97. Signature provided a draft lease agreement that was for five years and did not include a renewal option. AR at 2207-2246 (AR at 2209-10 term provision). It did not include the amount of the rent or the methodology for calculating the rent. AR at 2211-12.

Shortly after receiving Signature's application, the Program also received Springstone's CN application to establish a psychiatric hospital in the same area as Signature's proposal. AR at 2458-2641. Springstone's application identified Rainier Springs, LLC, a newly formed subsidiary, as the applicant. AR at 2461. Before the end of the screening process, Springstone submitted a revised draft lease agreement between Rainier Springs and the lessor, Propstone, which is another Springstone subsidiary. AR at 3059-3073. The revised lease was for an initial term of 10 years with options to renew for two additional five-year terms; the lease

included the methodology to calculate rent. AR at 3059 (rent), 3057 (term and renewal options).

The Program concurrently reviewed Signature and Springstone's applications, then issued its decision granting a CN to Springstone and denying Signature's application. AR at 3650-3713. Because Signature failed to establish sufficient site control and the lease failed to include essential costs, the Program denied Signature's CN application for failure to satisfy financial feasibility in WAC 246-310-220. AR at 3650-52. Because it failed the criteria for financial feasibility, it also failed the cost containment criteria in WAC 246-310-240. AR at 3650-52.[1]

B. Procedural History

Signature requested adjudicative proceedings to contest the CN granted to Springstone and denial of its CN application. AR at 1-186, 191-281. On cross motions for summary judgment, the Presiding Officer issued an Initial Order affirming the Program's decision. AR at 1512-52. Following Signature's Petition for Administrative Review, the Department's Review Officer upheld the Initial Order. AR at 1641-83.

On January 13, 2017, Signature petitioned for judicial review in Thurston County Superior Court. Clerk's Papers (CP) at 4-257. On the

[1] An applicant that does not satisfy applicable CN criteria, including financial feasibility, automatically fails WAC 246-310-240(1), cost containment, and the review ends. AR at 3650-52.

Department's Motion, Thurston County Superior Court certified the case for direct review under RCW 34.05.518. On May 26, 2017, the Court of Appeals accepted the matter for direct review under RCW 34.05.518-522 and RAP 6.3.

In an unpublished opinion, the Court of Appeals affirmed the Department's Final Order. *Signature Healthcare Services, LLC v. Wash. State Dep't Health,* No. 501090-1-II, 2018 WL 2215462, at *12 (Wash. Ct. App. May 15, 2018) (unpublished). The Court disagreed with Signature's arguments that the Department misinterpreted and misapplied the law in requiring Signature to submit a draft lease with a 20-year total term to show site control. *Signature Healthcare Services, LLC,* 2018 WL 2215462, at *4-6. The Court held that Signature failed to demonstrate sufficient interest in its proposed hospital because it failed to provide the draft lease with the required term. *Id.* at *6. The Court also determined the Department properly applied the law in requiring lease costs in the draft lease agreement. *Id*. at *6-7. The Court found that Signature failed to demonstrate financial feasibility because the lease did not provide monthly or annual lease costs for Vancouver Behavioral Health. *Id*. at *7. With regard to Springstone's CN application, the Court of Appeals found that there was no genuine issue of material fact concerning the true applicant because Springstone was the parent company wholly owning Rainier Springs, and parent companies are

considered the applicant for CN application purposes. *Signature Healthcare Services, LLC,* 2018 WL 2215462, at *9-10.

Signature petitioned for review by this Court.

IV. REASONS WHY THE COURT SHOULD DENY REVIEW

The Court should deny review because the Court of Appeals' decision does not conflict with any Supreme Court decision, and the Petition for Review does not involve an issue of substantial public interest that warrants further review by the Supreme Court. RAP 13.4(b)(1), (4). Signature incorrectly argues that the Department's denial of a single deficient CN application is a matter of substantial public interest. RAP 13.4(b)(4). Not so. As the Court of Appeals found, the Department complied with the law and fairly exercised its discretion when considering and denying Signature's application, where Signature failed to provide necessary documentation to establish financial feasibility and cost containment.

A. The Department Was Not Required to Treat Dr. Kim as the True CN "Applicant"

Signature argues that the Department and Court of Appeals should have recognized Dr. Kim as the "applicant" because Dr. Kim owned the array of business organizations described in Signature's proposal. Petition for Review (Pet.) at 8-11. At the outset, the Court should decline to consider this argument as it was raised for the first time during oral argument before

the Court of Appeals even though Signature could have raised this at any point in the application process by naming Dr. Kim as the applicant, amending the application, or otherwise notifying the Department that Dr. Kim should be treated as the applicant. *See Int'l Ass'n of Fire Fighters, Local 46 v. City of Everett*, 146 Wn.2d 29, 37, 42 P.3d 1265 (2002) (courts decline to consider new legal theories under RAP 2.5(a) unless question raised affects important public policy issues).

More to the point, Signature's fact-specific argument that the Department should have treated Dr. Kim as the true CN applicant fails because Signature's CN application did not identify Dr. Kim as the applicant, and Signature has never asserted that Dr. Kim is in fact the individual "proposing to engage in any undertaking subject to review under chapter 70.38 RCW . . . ." WAC 246-310-010(6). Instead, Signature's application identified *itself* as the applicant and explained that its Clark County hospital would do business as Vancouver Behavioral Health. AR at 1814, 1816. The application relied on *Signature's* past performance to support its proposal. *See* AR at 1814, 1856, 2192-94. And the application identified Dr. Kim only as an owner of four business entities identified in Signature's proposal. *See* AR at 1865. Accordingly, the Department properly recognized Signature as the applicant. *See* AR at 2117 (Signature's response to the Department's first screening letter with no correction to the

statement clarifying that Signature is the applicant). Signature cites no authority—and the Department is aware of none—requiring the Department to affirmatively designate a person as the CN applicant.

Signature argues that because the definition of "applicant" in WAC 246-310-010(6) *could* include someone like Dr. Kim, the Department was required to treat him as one. Pet. at 10; WAC 246-310-010(6) ("applicant" includes a person who owns ten percent of more of an entity seeking to engage in an "undertaking subject to review under 70.38 RCW"). But Signature has not cited any WAC or other authority requiring the Department to ferret out every potential entity or person who may qualify as an "applicant." Instead, the WACs contemplate that "applicants" are persons or entities that submit a CN application and any other relevant documentation to the Department. *See, e.g.*, WAC 246-310-080 (prior to applying, applicant must submit a letter of intent to the Department); WAC 246-310-120(2)(a) (applicant undergoing concurrent review must submit copies of application to Department). Notably, an applicant may amend an application to change the name of the applicant. *See* WAC 246-310-100. And the Department is limited to considering information requested from and submitted by the applicant. *See* WAC 246-310-090(1)(a)(iii). Here, there is no evidence that Dr. Kim submitted a letter of intent or an application; prepared or submitted

information or responded to requests from the Department; attempted to amend the application to include himself; or participate in the adjudicative proceeding or this appeal. *See* WAC 246-310-610(1) ("An applicant denied a certificate of need . . . has the right to an adjudicative proceeding").

By contrast, the Department properly treated Springstone as the true applicant after Springstone specifically clarified that it was the owner of Rainier Springs and should be treated as the applicant. AR at 2653. Signature's argument that the Department arbitrarily treated Signature differently than Springstone by recognizing Springstone, the parent company of Rainier Springs, as the "applicant" (Pet. at 11) ignores the context in which the Department made its determinations. *See* WAC 246-310-090(1)(a)(i) (information required by Department "shall vary in accordance with and be appropriate to the category of review or the type of proposed project . . . .").

Moreover, just because the Department may treat a parent company such as Springstone as the true applicant does not mean it must treat a sole shareholder as a true applicant. Instead, by acknowledging the primary or parent corporation (Signature and Springstone) as the applicants instead of the secondary or subsidiary business entity (Vancouver Behavioral Health and Rainier Springs), the Department treated the applicants alike. Neither the Department nor the Court of Appeals arbitrarily treated the competing

proposals differently with regard to identifying the applicant. *Signature Healthcare Services, LLC,* 2018 WL 2215462, at *9-10 (finding there was no genuine issue of material fact regarding the true applicant in Springstone's application because the evidence presented to the Department showed that Springstone entirely owned Rainier Springs).

Signature's fact-specific argument that the Department and the Court of Appeals erred by failing to identify Dr. Kim as an applicant does not warrant this Court's review, and instead is a post hoc, untimely attempt to resurrect its failed project, which this Court should reject. RAP 2.5, RAP 13.4(b)(1), (4).

B. Signature's Failure to Show Sufficient Interest in the Proposed Hospital Is Not an Issue of Substantial Public Interest

Signature incorrectly argues that its real estate purchase and sale agreement for the undeveloped site where Vancouver Life Properties would build a hospital facility should have been sufficient to show site control because the CN application states that the applicant must have interest in the site *or* facility. Pet. at 11-14. The Court of Appeals correctly afforded deference to the Department's interpretation of its own application requirements to reject this argument.

The Court of Appeals noted that RCW 70.38.115(6) "clearly provides that the Department may require whatever information it deems reasonably necessary to review a CN application." *Signature Healthcare*

Services, LLC, 2018 WL 2215462, at *5. In other words, the Department has the authority to set forth certain requirements in its CN application, and its interpretation of those requirements is entitled to deference. *See D.W. Close Co., Inc. v. Dep't of Labor & Indus.,* 143 Wn. App. 118, 129, 177 P.3d 143 (2008) ("agency acting within the ambit of its administrative functions normally is best qualified to interpret its own rules, and its interpretation is entitled to considerable deference by the courts"); *Signature Healthcare Services, LLC,* 2018 WL 2215462, at *5 (properly finding that because the Department "acts within the scope of its administrative functions in assessing CN applications, we give the Department deference in construing the requirements of its CN application form"). Signature's citation to cases involving interpretation of *statutes or regulations* are inapposite. *See* Pet. at 11-12. Signature cites no authority contravening the rule of deference to the Department's interpretation of its CN application.

Here, the CN application states in relevant part:

> 8. Provide documentation that the applicant has sufficient interest in the site or facility proposed. Sufficient interest shall mean one of the following:
>
> a) Clear legal title for the proposed site; **or**
>
> b) Lease for at least five years with options to renew for no less than a total of twenty years in the case of a hospital or

> psychiatric hospital, tuberculosis hospital or rehabilitation faculties; or
>
> …
>
> d) Legal enforceable agreement to give such title or such lease in the event that a Certificate of need is issued for the proposed project.

Signature Healthcare Services, LLC, 2018 WL 2215462, at *5 (emphasis added); AR at 1821-22 (emphasis added).

As the Court noted, it is undisputed that Signature structured its CN application so that its hospital operator, Vancouver Behavioral Health, did not own the hospital facility; instead, Vancouver Life Properties owned and would lease the facility to the operator. *Id.* at *5; AR at 1908, 1865.

> Because Signature provided that its proposed hospital would lease its facilities, the Department requested that Signature provide . . . a lease with a 20-year total term. Consequently, Signature was required to provide . . . a 20-year lease to demonstrate sufficient interest, but Signature provided a lease agreement with only a five-year term.

Id. at *6; *see* AR at 2207-2246 (lease agreement).

Thus, the Court of Appeals fully considered statutory authority and the undisputed facts before properly holding that Signature failed to demonstrate sufficient interest in its proposed facility because it failed to provide required documentation of an up to 20-year lease. *Id*. at *6. The fact that Signature did not comply with an explicit requirement that its

competitor, Springstone, did comply with is not an issue of substantial public interest.

C. The Court of Appeals' Decision Does Not Conflict With a Decision of the Supreme Court Concerning the Common Law Principle of Annexation of Fixtures to Real Property

Signature argues for the first time to this Court that Vancouver Life Properties was merely the "builder" of the proposed hospital facility and that Signature, as the owner of the underlying land, would be the "true owner" under the common law principle of annexation of fixtures to real property. Pet. at 14-17. Signature further asserts that a written agreement is necessary to sever a facility from the land. Pet. at 15. Because Court of Appeals did not consider this theory, this Court should reject it under RAP 2.5(a).

In any case, the Court of Appeals' decision that Signature was required to submit a draft lease is not in conflict with any decision of this Court, and the cases Signature relies on to support its argument are not persuasive because of the way Signature structured its project. AR at 1865. Signature cites *Union Elevator & Warehouse Co. v. State ex rel. Department of Transportation*, but this case articulates a test to determine whether *personal property* becomes a fixture and is thus irrelevant. *Union Elevator & Warehouse Co., Inc.,* 144 Wn. App. 593, 603, 183 P.3d 1097 (2008) (discussing annexation of personal property (machinery)). Signature

also relies on *Ballard v. Alaska Theater Co*. for the general rule that permanent structures erected on the land by the owner become part of the realty in the absence of contrary intent. *Ballard,* 93 Wash. 655, 665, 161 P. 478 (1916). However, *Ballard* primarily discussed whether chattel (e.g a pipe organ, opera chairs) were trade fixtures or part of the realty and is thus distinguishable. *Id*. at 662-63.

Signature's reliance on cases involving whether personal property are fixtures to real property are inapplicable to this project. The Court of Appeals' decision did not implicate fixtures law, nor did the Court of Appeals hold that a landowner does not own structures on the land absent contrary intent. In this case, the Department reasonably relied on Signature's application to understand that the land and hospital facility would be separately owned. Signature structured its project so it would not own the yet un-built hospital facility. AR at 1865, 2121-22. Signature, through Vancouver Behavioral Healthcare Hospital, proposed leasing the hospital facility from Vancouver Life Properties—the builder/owner, and Signature's legal right to use the hospital was secured through a lease with Vancouver Life Properties. AR at 1660, 1673, 1865. In other words, under the project that Signature proposed, there would not be common ownership of both the land and the hospital facility, and the landowner would lease the facility from the facility owner. AR at 1865. Under these circumstances, the

Department requires a 20-year lease to establish site-control. AR at 1821; WAC 246-310-090(1)(a).

Signature would have the Department and Court of Appeals second guess the structure of Signature's own proposal, but the Department is aware of no authority requiring such an inquiry. *See, e.g.*, AR at 1865 (Signature project structure). Thus, the Court of Appeals correctly affirmed the Department's determination that when faced with a CN application where the hospital operator proposes to lease a facility owned by a separate legal entity, a lease for a sufficient term that contains all necessary information is required for the Department to evaluate if a project is financially feasible. *Signature Healthcare Services, LLC*, 2018 WL 2215462, at *13.

D. Signature's Failure to Submit a Lease With the Necessary Rent Information Is Not an Issue of Substantial Public Interest

Signature argues that providing a rent amount in its pro forma revenue and expense statement should have been sufficient for the Department to determine the costs of the lease, arguing for the first time that the Department rejected the lease "only" because the lease reflected triple net costs. Pet. at 17-19. This argument does not present an issue of substantial public interest; it is another attempt to misdirect away from Signature's failure to submit a 20-year lease with all essential terms.

The Court of Appeals considered then correctly rejected Signature's arguments that the Department misapplied the law by requiring the draft lease to include annual and monthly lease costs. *Signature Healthcare Services, LLC,* 2018 WL 2215462, at *6-7. The Court noted that a CN applicant must submit an application "'in such form and manner and containing such information as the [D]epartment has prescribed and published as necessary to such a [CN] application.'" *Id.* at *5 (quoting WAC 246-310-090(1)(a)). The Court further observed that WAC 246-310-200(1) requires a CN applicant to demonstrate that its proposed hospital is financially feasible, meaning that an applicant must show that the immediate and long-range capital and operating costs of the proposed hospital will be met. *Id.* at *6.

The Court acknowledged that Signature's application noted an annual rental payment of approximately $2 million, but did not include a lease agreement. *Id*. (The amount appeared in Signature's Pro Forma Income Statement that projects expenses and revenues in the first three years of operation. AR at 1909-1913). Signature failed to supply any additional information after the Department specifically requested Signature provide the monthly and annual lease costs of its proposed hospital. The Department sent a second screening letter requesting the

information and Signature provided a draft lease agreement that still did not include the monthly or yearly rent amount.

As the Court of Appeals noted, "[t]he Department requires a copy of a lease agreement that includes annual and monthly lease costs to determine whether a proposed hospital is financially feasible." *Signature Healthcare Services, LLC,* 2018 WL 2215462, at *15-16. Because the lease Signature finally submitted did not include monthly or annual rent, or a methodology for calculating the rent, the Court of Appeals correctly held that Signature failed "to show that the Department misapplied the law in denying CN application for failing to demonstrate financial feasibility." *Id.*

V. CONCLUSION

The Department required a hospital lease to establish site control because Signature structured its project so another company would own the hospital and lease it to Signature. Signature eventually submitted a hospital lease to the Department but it was for too short a time and did not identify all costs associated with the lease. As a result, its application failed to satisfy financial feasibility and, consequently, cost containment. The Court of Appeals' decision affirming the Department's Final Order denying Signature's application does not conflict with a decision of this Court and presents no issues of substantial public interest. The substantial public interest in the outcome of this case is ensuring that critically needed

psychiatric services are available, which Springstone stands ready to provide. This Court should deny review.

RESPECTFULLY SUBMITTED this 15th day of August, 2018.

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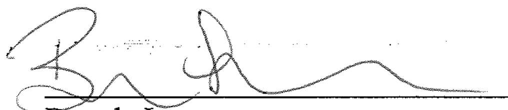
I certify under penalty of perjury under the laws of the state of Washington that the foregoing is true and correct.

DATED this 15th day of August 2018, at Olympia, Washington.



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