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No. 52393-1-II

**IN THE COURT OF APPEALS
OF THE STATE OF WASHINGTON
DIVISION II**

HERITAGE GROVE, PRESTIGE CARE, INC., CARE CENTER
(YAKIMA), INC. AND YAKIMA VALLEY VENTURES, LLC,

Appellants,

v.

DEPARTMENT OF HEALTH, STATE OF WASHINGTON, SELAH
CARE AND REHABILITATION, LANDMARK CARE AND
REHABILITATION, EMERALD CARE, GOOD SAMARITAN
HEALTH CARE CENTER, WILLOW SPRINGS CARE AND
REHABILITATION, CRESCENT HEALTH CARE, INC., AND
SUMMITVIEW HEALTHCARE CENTER,

Appellees.

REPLY BRIEF OF APPELLANTS

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I. INTRODUCTION

The Department of Health's Response brief argues first that this appeal must be dismissed, alleging that the case is moot. The Department then urges that substantial evidence supports the Final Order's findings, particularly Findings of Fact 2.20 and 2.23 on financial feasibility. The nursing home Respondents' Response Brief follows suit, but reverses the order of the Department's Brief, arguing first that substantial evidence supports the Department's determination in the Final Order and, second, that the case is moot.

To reach these conclusions, the Respondents were required to infer added language into the operative statute, RCW 70.38.115(13)(b), and to ignore key facts and challenges by the Appellant's Opening Brief. In the course of that process, the Respondents attempted to support a new standard for financial feasibility of replacement project in the special type of certificate of need review at issue in this case.

The Appellant replies that the critical Findings on financial feasibility of the Heritage Grove project, Findings of Fact 2.20 and 2.23, are the result of application of a single fact that is irrelevant to the Heritage Grove project, the county average Medicaid occupancy percentage at the existing facilities, when there is no evidence that (a) Heritage Grove is required by any review standard to have a Medicaid occupancy percentage of 60% or 69% or (b) that such percentages are unlikely because the new facility will concentrate on short-term

rehabilitation patients after discharge from the hospitals. To reach the statements in Findings of Fact 2.20 and 2.23 the Final Order had to ignore the plain language of WAC 246-310-220(1), the bulk of the testimony on financial feasibility, and the experience and expertise of the Department's Certificate of Need Program ("Program"), which accepted the assumptions for the financial projections in the application as reasonable.

These errors and omissions are precisely why the Final Order must be reversed. It commits the same errors as espoused by the Respondents.

II. STANDARDS OF REVIEW

A. Administrative Procedure Act.

King County Public Hospital District No. 2 v. Washington State Department of Health, 178 Wn.2d 363, 371-72, 309 P.3d 416 (2013) summarizes the standards of review applicable to Certificate of Need cases such as the present case:

The standards of review in certificate of need cases stem from the Administrative Procedure Act (APA). RCW 70.38.115(10)(a); *Providence Hosp. of Everett v. Dep't of Soc. & Health Servs.*, 112 Wn.2d 353, 355, 770 P.2d 1040 (1989) (referring to former RCW 34.04.130 (1977), re-codified as RCW 34.05.570). "The agency decision is presumed correct and the challenger bears the burden of proof." *Providence*, 112 Wn.2d at 355, 770 P.2d 1040 (citing *In re All-State Constr. Co.*, 70 Wn.2d 657, 659, 425 P.2d 16 (1967)). This court sits in the same position as the superior court and applies the APA standards directly to the record before the agency. *Tapper v. Emp't Sec. Dep't*, 122 Wn.2d 397, 402, 858 P.2d 494 (1993). Under the error of law standard, the court may substitute its interpretation of the law for that of the agency, but it substantially defers to the agency's interpretation, particularly where the agency has special expertise. *Providence*, 112 Wn.2d at 356, 770 P.2d 1040 (citing

Franklin County Sheriff's Office v. Sellers, 97 Wn.2d 317, 325, 646 P.2d 113 (1982)). The court affirms an agency's factual findings unless they are not supported by substantial evidence. RCW 34.05.570(3)(e); *Tapper*, 122 Wn.2d at 402, 858 P.2d 494. The court may also grant relief from an agency order that is arbitrary and capricious, meaning that "the decision is the result of willful and unreasoning disregard of the facts and circumstances." *Providence*, 112 Wn.2d at 356, 770 P.2d 1040 (citing *Barrie v. Kitsap County*, 93 Wn.2d 843, 850, 613 P.2d 1148 (1980)).⁴ We review an administrative law judge's evidentiary decisions for abuse of discretion. See *UWMC*, 164 Wn.2d at 104, 187 P.3d 243.

The Court reviews de novo whether a decision is arbitrary and capricious. *Karanjah v. Dep't of Social and Health Services*, 199 Wn. App. 903, 924, 401 P.3d 381 (2017).

This record shows that: (1) substantial evidence does not support the Findings of Fact 2.20 and 2.23, which are the basis for all of the Findings as to WAC 246-310-240, cost containment, and the adverse conclusions of law, (2) that the decision is the result of willful and unreasoning disregard of the facts and circumstances, and (3) that the Final Order considered need in reversing the earlier decisions granting CN #1557, despite that criterion having been eliminated as applicable to this case.

B. Certificate of Need Review Criteria; Need is not an Issue.

Only three of the four criteria normally used in review of applications for a Certificate of Need are applicable in this case, namely, WAC 246-310-220 (financial feasibility), WAC 246-310-230 (structure

and process of care),¹ and WAC 246-310-240 (cost containment). The prohibition on considering the usual first criterion, need (WAC 246-310-210), is contained in RCW 70.38.115(13)(b), which provides:

RCW 70.38.115(13)(b):

(b) When an entire nursing home ceases operation, the licensee or any other party who has secured an interest in the beds may reserve his or her interest in the beds for eight years or until a certificate of need to replace them is issued, whichever occurs first. However, the nursing home, licensee, or any other party who has secured an interest in the beds must give notice of its intent to retain the beds to the department of health no later than thirty days after the effective date of the facility's closure. Certificate of need review shall be required for any party who has reserved the nursing home beds except that the need criteria shall be deemed met when the applicant is the licensee who had operated the beds for at least one year, who has operated the beds for at least one year immediately preceding the reservation of the beds, and who is replacing the beds in the same planning area.

[Emphasis added]

This statute has never been construed by an appellate court, until now. Heritage Grove qualified for treatment under the exception above. (Final Order, p. 7; AR 2448) Because need is “deemed met,” the criteria related to need and found in WAC 246-310-210 and WAC 246-310-360 through -390 and as usually applied in the Department’s review process are irrelevant to this decision as a matter of law.

The Final Order concludes RCW 70.38.115(13)(b) is “clear and

¹ No issues regarding WAC 246-310-230 are presented in this case. The Final Order rules in favor of the Appellant on that criterion.

unambiguous on its face and that the Appellant met the criteria for application of that statute. AR 2448. The Department urges that the statute “does not exempt the former licensee from any CN criteria other than the need criteria concerning the number of beds.” As noted in the Final Order, the Department in its earlier briefs has previously argued that “the plain language of the statute obligates the Department to consider the need as met when considering Heritage Grove’s application” AR 2448. The statute has no words limiting its exemption to only those criteria “concerning the number of beds.” It uses the term “need criteria,” so any standard relating to need “is deemed met.”

Hence, need was not an issue for this review, and consequently evidence related to need as a criterion is irrelevant. This is critical to analysis of Appellant’s qualification for a CN, as it highlights that this is a limited review of the application and that need considerations may not creep into the three other criteria that are within the scope of the review. Findings of Fact 2.20 and 2.23, based upon the average Medicaid occupancy of the old existing facilities, fail to recognize that considering what is occurring at the other facilities is a part of need analysis and erroneous for that reason.

The Department’s brief sets forth four misleading arguments about the review standards on pp. 20-23 that are simply erroneous. First, it asserts that CN decisions are discretionary. Br. p. 20. This is plainly erroneous. As stated in *Swedish Health Services v. The Department of Health of the State of Washington*, 189 Wn. App. 911, 916, 388 P.3d 1243

(2015): “The plain text of the Department’s regulations establishes that its standards are mandatory.” WAC 246-310-200(1) provides:

(1) The findings of the department’s review of certificate of need applications and the action of the secretary’s designee on such applications shall, with the exceptions provided for in WAC 246-310-470 and WAC 246-310-480 be based on determinations as to:

- (a) Whether the proposed project is needed;
- (b) Whether the proposed project will foster containment of the costs of health care;
- (c) Whether the proposed project is financially feasible; and
- (d) Whether the proposed project will meet the criteria for structure and process of care identified in WAC 246-310-230.²

(Emphasis added)

Second, the Department argues, Br. at p. 22, that the Department evaluates the applicant’s financial projections by examining the number of likely patients and the mix of likely patients in the planning area, citing Mr. Russell’s testimony (AR 4860-61). Actually, Mr. Russell testified that such an examination is part of need analysis in a review where need is at issue. Of course, no need analysis was done as to Heritage Grove, so he did not have “any kind of analysis” he could use to evaluate the Heritage Grove financial projections. (TR 777: ll. 4-8; AR 4861)

Third, the Department argues that *King County Public Hospital District No. 2 v. Washington State Department of Health*, 178 Wn.2d 363,

² WAC 246-310-200(2) is also mandatory in requiring decisions to be based upon standards.

377-78, 309 P.3d 416 (2013), stands for the proposition that the Department uses average daily census to determine if a proposal will meet capital and operating costs. *King County* is not apposite to this case and has been distinguished in *Swedish Health Services v. The Department of Health of the State of Washington*, 189 Wn. App. 911, 916. It involves a review of a hospice agency application, which had to be filed before the Department issued its hospice need numbers. Also, the case says nothing of nursing home financial feasibility which differs from the hospice special standards, including average daily census, to determine the need and financial feasibility of the proposed hospice agency. See WAC 246-310-290(6). This rule and the *King County* case apply only to hospice applications.

Fourth, the Department's brief, Br. 23, argues that the Department has a practice of comparing an applicant's projected payer mix with the existing payer mix in the planning area. There is no evidence of such a practice, much less any review standard in the rules related to this non-existent "practice." Further, Appellant can find no rule or practice to this effect in the Department decisions on applications where need is deemed met. See, e.g., *Seattle University*, CN 14-02 (AR 587-641), which pre-dates this case and uses the same format and considerations as in the Heritage Grove application Evaluation. (AR 2743 – 2769)

The Department and Appellant agree that an "agency order is supported by substantial evidence if there is a sufficient quantity of evidence to persuade a fair-minded person of the truth or correctness of

the order.” *Hardee v. State, Dep’t of Soc. & Health Services*, 172 Wn.2d 1, 7, 256 P.3d 339 (2011).

We disagree that there is a sufficient quantity of evidence to support the Final Order’s FF 2.20 and 2.23, and the other Findings which are based primarily on Findings of Fact 2.20 and 2.23, because the county-wide Medicaid census average at the existing facilities is irrelevant to analysis of the Appellant’s application.

A fair-minded person must reject these findings and the findings on containment under WAC 246-310-240 that are based upon them, and the conclusions of law that the Final Order draws. It is a classic example of the old saying: “If you start with a false premise, your conclusion is bound to be wrong.”

III. ANALYSIS

A. **Findings of Fact 2.20 and 2.23 are based solely upon the county average Medicaid consensus percentage for existing facilities.**

1. Findings of Fact 2.20 and 2.23 must be rejected for lack of substantial evidence?

The last sentence of FF 2.20 sums up its finding:

Thus, the record contains no evidence of whether Heritage Grove could satisfy the financial feasibility criteria in light of the historic (sixty-nine percent) Medicaid occupancy rate in Yakima County, or even the reduced number (60 percent) as asked by the program in the screening questions). (AR 2465-66.)

FF 2.20 gives no justification for considering the county-wide average Medicaid census applicable to this application, or even that it shed any light on the review of the application .

In its answer to screening question No. 7, pertaining to need, Heritage Grove gave the first of many reasons why the county average Medicaid census was irrelevant: “we [applicant] do not believe Heritage Grove will experience 60% Medicaid occupancy.”³ This is based upon the evidence as to Appellant’s project discussed below. The project is not designed or intended to be like the eleven existing nursing homes in Yakima County and is expected to have the Medicaid census incorporated into the financial projections in the application. FF 2.7 provides no support for the application of the county average Medicaid census to Appellant’s financial projections in FF 2.20 and 2.23.

The second factual basis for the summary statement in FF 2.20, is a statement that “Mr. Russell [the Department’s reviewing analyst] further testified that he performed no testing of Heritage Grove’s financials to see what would happen to them if they had a higher-than-anticipated percentage of Medicaid patients. Final Order p. 24; AR 2465. However, FF 2.20 fails to explain the reason for no testing. Mr. Russell actually testified that he performed no “stress testing,” “Because revenue would be easy to evaluate...but the change in cost due to variable and fixed cost would be much more difficult to make a reasonable evaluation of that.” (TR 795; AR 4879) The facts as found in Mr. Russell’s testimony support only a decision by him not to do any analysis using a higher Medicaid

³ Partially quoted in FF 2.7 (AR 2465). The question was asked as a part of questions under the need criteria. The Appellant’s response was confirmed in the testimony and submissions of the representatives of the Respondent Nursing Homes, discussed below.

census due to the complexity of coming up with a reasonable conclusion. They do not support the claim that “the record contains no evidence of whether the Heritage Grove could satisfy the financial feasibility...” (AR 2465)

B. The Record contains all the evidence that is relevant to this application and needed to satisfy the WAC 246-310-220 criteria.

The statement in FF 2.20 that the record contains no evidence of whether Heritage Grove could satisfy the financial feasibility criteria must be rejected under the substantial evidence standard and the result of arbitrary and capricious refusal to consider the evidence in the Record. Abundant and sufficient evidence submitted by the applicant and even testimony from the Respondent Nursing Homes but ignored by the Final Order establishes the falsity of the statement in FF 2.20 and the error of the conclusion of law in FF 2.23 that there is “insufficient evidence to determine whether Heritage Grove’s projected revenues and expenses are reasonable, the costs of the project will have an unreasonable impact on the costs and charges for health services appropriately financed.” (AR 2466-67)

In applying WAC 246-310-220 to the facts, the Final Order must construe “agency rules in a “rational, sensible” manner, giving meaning to the underlying policy and intent.” *Odyssey Healthcare Operating BLP v. Washington State Department of Health*, 145 Wn. App. 131, 143, 185 P.3d 652 (2008).

To meet the standards of WAC 246-310-220, determination of financial feasibility, the applicant must show:

(1) The immediate and long-range capital and operating costs can be 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.

(3) The project can be appropriately financed.

[Emphasis added]

WAC 246-310-220(1) does not require or even suggest that average county-wide Medicaid census in other facilities must be considered as a part of the review. The Certificate of Need program does not consider it in doing reviews. Russell, TR 770: ll. 23-25 – 771: ll. 1-2; AR 4854-55). Program specifically rejected information related to occupancy in this review, because it is linked to evaluation of the need criteria. TR 778: ll. 24-25 – 779: ll. 13-20; AR 4862-63)⁴ Thus, the Final Order in basing FF 2.20 and 2.23 on Medicaid census at other facilities applies a standard not part of WAC 246-310-220 and is erroneous as a matter of law. The Final Order may not create a new standard or add words to the regulation it is applying.⁵

⁴ Mr. Russell did nothing with occupancy information submitted at the public hearing because “I wasn’t doing a need analysis.”

⁵ *Providence Physician’s Services Co. v. Washington State Department of Health*, 196 Wn. App. 709, 726, 384 P.3d 658 (2016), relying upon *Failor’s Pharmacy v. Department of Social and Health Services*, 125 Wn.2d 488, 886 P.2d 147 (1994) (“If, however, an agency adds a new requirement to an already well defined regulation, that requirement will be

C. The Nursing Home Respondents have conceded that they will lose patients and revenue to Heritage Grove.

The word “can” in the WAC 246-310-220(1) is important. Its plain meaning is that if there is a way to achieve at least a break-even on the operations, the criterion is satisfied. The Final Order has no language that the decision applied the regulation as it is written.

The evidence in the record is that Heritage Grove can attract and serve sufficient Medicare and other higher revenue/heavier care rehabilitation patients. The project “can” and will meet the regulatory standard. Norm Hyatt, who testified as an expert for the Nursing Home Representatives of the Nursing home Respondents, agreed that the new Heritage Grove facility will be attractive to private, Medicare and state (Medicaid) patients⁶ and that he was concerned that patients would go to Heritage Grove rather than the Nursing Home Respondents’ facilities. (TR 445: ll. 1-7; AR 4528)

Mr. Hyatt also testified that (1) the patients at Heritage Grove were only going to come from one place, the existing facilities (TR 486: ll. 12-16; AR 4569), and (2) he and Chris Bosworth developed the table⁷ showing the revenue that would be gained by Heritage Grove

deemed a rule subject to the formal rule-making procedures.”)

⁶ Elsewhere in his testimony, Mr. Hyatt listed all types of payors involved in his calculations of the revenues that Heritage Grove would gain from patients choosing the new facility, so he probably was not excluding Managed Care and PPO patients from the people who would be attracted to the Heritage Grove facility.

⁷ AR 3059-60. Table of forecasted losses to the existing facilities when Heritage Grove is operational, attached to her letter submitted at the public hearing and prepared by Norm Hyatt and Chris Bosworth.

(\$11,052,000)⁸ and lost by the existing facilities because the patients had gone to Heritage Grove (\$11,234,217). (TR 453: ll. 3-10; AR 4536) The calculations were based upon the assumptions in the Heritage Grove application financial projections. (TR 486: ll. 12-16; AR 4569).

Molli Harrington, representing Crescent Healthcare, affirmed Mr. Hyatt's statement:

Last year I [Crescent] had a perfect survey, so word of mouth gets around in Yakima. But a lot of people are drawn to a brand-new facility, a fancy facility regardless of what the quality of care is.

She also stated in her public hearing letter that she expected an annual lost revenue of \$719,000 to Crescent if Heritage Grove was built. (AR 2665)⁹

All of this testimony and evidence appears to have been disregarded in the Final Order.

D. Substantial evidence supports Heritage Grove's compliance with WAC 246-310-220.

1. Program's Evaluation and Mr. Russell's testimony.

Each of the sub-criteria under WAC 246-310-220 was examined in detail by Program, using the Program's experience and expertise, to come to conclusions of compliance with the specific requirements of WAC 246-

⁸ This is a rounded revenue number for Heritage Grove corresponding to the 11,051,901 Mr. Hyatt used in his calculations (AR and found in the projected revenues of Heritage Grove (AR)).

⁹ Gloria Dunn also testified that her facility, Landmark facilities would lose revenue to Heritage Grove. (TR 101: ll. 24-25; AR 4183-84). Each of the Respondent Nursing Homes representatives ascribed to the table of Heritage Grove revenues found at 3059-60, including Mike Hoon (AR 2675), Chris Bosworth (AR 2668), Taylor Hall (AR 2670) and Carol Hyatt (AR 2668).

310-220. The Final Order relies on the county-wide Medicaid census average as the basis for all of its conclusions as to financial feasibility.

Program in its Evaluation of the Heritage Grove application found that it was reasonable to expect that new facility would exceed break even, that is, be profitable, by the second year of operation. (AR 2754) It came to this conclusion based upon its experience and expertise:

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)(i) and (b) that directs what the operating revenues and expenses should be for 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.

(Evaluation, AR 2754)

The Evaluation first reviewed the assumptions used in the application to determine the number of admissions, patient days and occupancy of Heritage Grove. It notes that the Heritage Grove project is not like the old facilities presently operating in Yakima County. It also accepted as a guideline for the financial performance calculations the census data breakdown for facilities of similar design and opening within the prior three years, and specifically the Medicaid census at Manor Care Salmon Creek and Manor Care Lacey as a guideline for the Medicaid percent occupancy. (AR 2754) In such acceptance, Program accepted that Heritage Grove was going to be a different kind of facility from the

old existing facilities.

Bob Russell, the Department Analyst in the Certificate of Need Program who reviewed the Heritage Grove application, testified that:

“We [Program] concluded that the project was financially feasible.” (TR 782: l. 18; AR 4866).

He further testified that the basis for Program’s determination was:

“The financial information submitted by the applicant is the basis for making that determination. We accepted his projection – patient days projections in the financial statement and we evaluated the other information submitted as far as financial information....” (TR 782: ll. 23-25 – 783: ll. 1-4; AR 4866-4867)

Mr. Russell also testified that in connection with financial feasibility:

- In the review need was deemed met and the Department does not do an analysis of need in this kind of review. (TR 767: ll. 1-9; AR 4851) There is no dispute that the projections show that Heritage Grove’s project will be profitable by the second year of operation, specifically, by \$671,632.00. (AR 2756)
- The Department has no criteria for a facility taking a “fair share” of Medicaid patients and consequently any particular number of Medicare and Medicaid patient days. (TR 770: ll. 17-25 -771: ll. 1-2; AR 4854-4855)
- With regard to the assumptions used to generate projected patient days, a factor in need analysis, Mr. Russell found that the response to Screening Question No. 5 was a “fairly good

response to my question.” AR 4857) (TR 772: ll. 24-25 - 773: ll. 1-15; AR 4856-4857). In other words, he accepted that the specific type of facility proposed by Heritage Grove could generate the revenues stated.

- He also accepted the Appellant’s response to Screening Question 7 regarding serving Medicaid patients. (TR 773: ll. 19-22)
- As to sub-criterion WAC 246-310-220(2), Mr. Russell testified that he looked at the proposed capital expenditure, a letter from the applicant’s contractor verifying the costs and financial statement to ascertain the applicant has the financial capability or commitment to finance the project. (TR 781; ll. 16-25; AR 4865) The Final Order does not discuss this.
- WAC 246-310-220(3), as analyzed in the Evaluation, was not in issue in the hearing.
- Program found that the application met each of the sub-criteria for financial feasibility, based upon the evidence in the Record. (AR 2754 -2758). This portion of the record is substantial evidence of financial feasibility of the Heritage Grove project, including that the assumptions used by Mr. Ulrich were reasonable. (AR 2754, 2757)

2. The Final Order errs

Mr. Russell’s testimony was clear that Program did not do a need

analysis:

“We didn’t look at need, therefore, I did not have any kind of analysis I could use to evaluate these revenue projections.” (TR 777: ll. 6-8; AR 4861)

He accepted the projections as reasonable based on the assumptions being reasonable. (AR 2757) Mr. Ulrich testified at length on the detailed process using actual reported results from DSHS and application of his professional judgment that went into developing the numbers.¹⁰

Mr. Russell was correct in applying the normal factors under WAC 246-310-220 that are used in this type of review where need is deemed met. As he testified, (TR 777: ll. 13-20; AR 4861):

“We look at the first three years – full years of operation in the facility for evaluating the financial feasibility and our criteria – or our standard for that is by projected year three, the applicant needs to be profitable, in other words, needs to be making more revenue over expenses. They may run a deficit in year one and two as long as they achieve profitability in year three for the project.”

Mr. Russell also testified that reviewing “the overall average occupancy in the planning area” would “involve looking at need, if I was to use that material,” so the information provided at the public hearing related to occupancy was not used in his analysis. (TR 778: ll. 24-25-779; ll. 1-2; AR 4862-63)

Thus, the Final Order’s reliance on county-wide average Medicaid census is a factor not found in this type of review, and there is no evidence

¹⁰ TR 551: ll. 16-25 – 555: l. 21; AR 4635-4639; TR 598; ll. 17-20; AR 4682). The Medicaid census assumptions in his projections were determined from DSHS data.

of it in this Record except for the Respondents submissions at the public hearing. As discussed below, the Final Order is without legal authority to create new standard without rulemaking. It violates both the APA and the requirement of WAC 246-310-200(1) and (2) that the decision on the Heritage Court application “shall” be based upon the criteria as found in the regulations.

In an apparent attempt to justify FF 2.20, the Department for the first time on appeal claims, Br. 24, that “the analyst [Bob Russell] incorrectly concluded that RCW 70.38.115(13)(b) implicates both numeric need and payer mix.” Program followed RCW 70.38.115(13)(b) and certainly did not consider need in reviewing the Heritage Grove projections. AR 4861. But Mr. Russell was not mistaken, nor did he come to any incorrect conclusions about what could and could not be used as evidence in Program’s review. The error was that of the Final Order in applying the county average Medicaid census for non-comparable facilities to the analysis of Heritage Grove, violating both RCW 70.38.115(13)(b) and its own ruling that evidence related to the need principles was outside the scope of this review.

Mr. Russell’s testimony was clear that Program did not do a need analysis, which involves looking census:

“We didn’t look at need, therefore, I did not have any kind of analysis I could use to evaluate these revenue projections.” (TR 777: ll. 6--8; AR 4861)

Program’s Evaluation accepted the projections as reasonable based on the

assumptions being reasonable. (AR 2757) The Record was built on the conclusion of law in Pre-Hearing Order No. 6 that need was deemed met and that evidence relating to issue of need or based upon need principles was irrelevant to this kind of facility review and excluded.¹¹

Mr. Russell was correct in applying the factors under WAC 246-310-220 that are used in this type of review where need is deemed met. As he testified, (TR 777: ll. 13-20; AR 4861):

“We look at the first three years – full years of operation in the facility for evaluating the financial feasibility and our criteria – or our standard for that is by projected year three, the applicant needs to be profitable, in other words, needs to be making more revenue over expenses. They may run a deficit in year one and two as long as they achieve profitability in year three for the project.”

Mr. Russell also testified that reviewing “the overall average occupancy in the planning area” would “involve looking at need, if I was to use that material,” so the information provided at the public hearing related to occupancy was not used in his analysis. (TR 778: ll. 24-25-779; ll. 1-2; AR 4862-63) The very standard that is central to the Final Order findings on financial feasibility is prohibited in this case by RCW 70.38.115(13)(b).

The Final Order is correct in affirming the Pre-Hearing Order No. 6.¹² RCW 70.38.115(13)(b) says nothing of “numeric” need, and the

¹¹ Pre-hearing Order No. 6 (AR 1614-1625, at 1615). Excluding from the hearing and pre-hearing discovery all evidence “relating to the issue of numeric need or that is based upon the need principles;” ruling affirmed in the Final Order. (AR 2448)

¹² AR 1614-1625.

Presiding Officer and the Final Order both gave the statute its plain meaning: any evidence or argument relating to need is not allowed in this case.¹³

Appellant's opening brief details the substantial evidence to support compliance of the application with WAC 246-310-220, including:

- The financials showing profitability by the end of the second year of operation (\$671,632.00);
- The assumptions are based upon actual operating results of facilities operated by the management company for Heritage Grove and two similar, nearly new facilities serving the same clientele mix;
- The Heritage Grove project is highly different from the existing Yakima nursing homes based upon age, design, equipment, concentration on post-acute rehabilitation patients and proximity to the hospitals;
- As noted above Respondent nursing homes admit that the Heritage Grove facility will attract patients to go to Heritage Grove and revenues now flowing to the existing facilities will come to Heritage Grove.

What is missing from the record is any substantial evidence of:

- That the location of the Heritage Grove project in Yakima County makes it any different from operationally from those in Clark County or Thurston County.
- Any review standard that would require Heritage Grove to accept Medicaid residents at the county average Medicaid census in 2013 (69%) or even 60 percent;
- Any relationship between the county average Medicaid census level of 69% or 60% and the expected census mix in a new and

¹³ The need criteria are contained in WAC 246-310-210 and WAC 246-310-360 through 390. "Numeric need" is not a term found in the regulations.

highly different facility serving primarily short term rehabilitation residents.

A review of the substantial evidence supporting each element of the financial feasibility criteria, all of which was ignored or disregarded, supports reversal of the Final Order as unsupported by substantial evidence, contrary to law and arbitrary and capricious.

3. Substantial evidence supports compliance of the Heritage Grove project with WAC 246-310-220(2)

WAC 246-310-220(2) requires a showing that “the costs of the project, including any construction costs, will probably not result in an unreasonable impact of the costs and charges for health services. Program’s Evaluation of the Heritage Grove application found that this criterion was met. AR 2757-58. Like its analysis of WAC 246-310-220(1), the Evaluation used Program’s experience and expertise because “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. (AR 2757)

The Final Order in Conclusion 3.12 (AR 2480) concludes that all three of the WAC 246-310-220 financial feasibility sub-criteria are failed because of FF 2.18-2.23. The refusal to consider the matters actually addressed in the regulation’s sub-criteria as part of those findings and the ample evidence against FF 2.20 and 2.23, including the costs of the project (Evaluation, AR 2757), must be considered arbitrary and capricious. *Karanjah v. Dep’t of Social and Health Services*, 199 Wn. App. 903, 924-257, 401 P.3d 381 (2017) (disregard or not considering the facts and

circumstances underlying the decision is arbitrary and capricious).

4. Substantial evidence compliance of Heritage Grove with WAC 246-310-220(3)

This sub-criterion requires that the project can be appropriately financed. Again, because there are no known recognized standards that direct how a project of this type and size should be financed, the Department used its experience and expertise and compared the proposed project source of financing (Banner Bank) to those previously considered by the Department. (AR 2758) The Department found this sub-criterion was met as well. (AR 2758).

5. The Final Order does not perform any analysis of the criteria of WAC 246-310-240.

FF 2.41 and FF 2.42 (AR 2475-76), and the Conclusion 3.16 (AR 2482) are based entirely on the Findings related to financial feasibility. Those findings are contrary to law rulings in this case and arbitrary and capricious. The analysis in the Evaluation, AR 2768-69, is based upon the record and correct. Mixing the financial feasibility findings with WAC 246-310-240 is unlawful in failing to follow the directive in WAC 246-310-200 that the decision must be based upon the criteria in each of the applicable regulations. It is also arbitrary and capricious in this case to render a decision based upon facts related to determinations of need.

E. THIS CASE IS NOT MOOT

1. Petitioners' rights to a Certificate of Need are not "moot."

The Respondents argue that this case is moot because the eight-

year period in RCW 70.38.115(13)(b) continues to run even after a CN has been issued to the applicant.

This argument is both procedurally and substantively wrong. The language of the statute itself plainly states:

When an entire nursing home ceases operation, the licensee ... may reserve his or her interest in the beds for eight years or until a Certificate of Need to replace them is issued, whichever comes first.

[Emphasis added]

In this case the Department of Health issued CN #1557 on August 3, 2015. Final Order FF 2.8, AR 2460; AR 2771-73) When a CN is issued, there is no more bed banking, for an obvious reason: the banked bed rights have been converted into the right to build a replacement facility, and the rights of the party that banked the beds are governed by the certificate of need or any appeal thereof.

This appeal is governed by the APA, as were the previous appeals by Nursing Home Respondents. *King County Public Hospital District No. 2 v. Washington State Department of Health*, 178 Wn.2d at 371. The remedies sections of the APA in RCW 34.05.574(1) and (4) provide ample authority for correction of the Final Order's errors.

The Department fails to point out that Pre-Hearing Order No. 5, AR 1612, tolls the commencement of CN #1552 "until the conclusion of this proceeding." We are still in the proceeding. The Final Order did not disturb that ruling, which was not in issue on Administrative review. No case cited by the Department holds that a party that has fulfilled the time

requirements of a statute and earned a CN for the replacement facility can have its rights taken away merely by the passage of time after it has appealed an adverse decision.

The Department's decision on a CN application is not discretionary, though the Department alleges that it is (Br. p. 20), citing RCW 70.38.105 and RCW 70.38.115. Neither statute states that the Department's decision on a CN application is discretionary. WAC 246-310-200 and *Swedish Health Services v. The Department of Health of the State of Washington*, 189 Wn. App., supra at 916, state that it is mandatory that the Department apply the criteria. The Court has the authority to order "an action required by law."

IV. CONCLUSION

The Court must conclude from this Record that the Final Order's new standard for financial feasibility review where need is not part of the criteria. Creation of that standard (county-wide Medicaid average census) without resort to the APA rulemaking procedures is unlawful. Refusal to consider evidence from the Respondents that they expect the Heritage Gove facility to have revenue as stated in the application can only be characterized as willful disregard of the facts and circumstance. This Court has the authority under RCW 34.05.574 to "order an agency to take an action required by law," which in this case means a decision reversing the Final Order, reinstating Appellant's interests in the CN #1557 issued by the Department and the affirmation that the decision in the Initial

Decision was correct.

Appellant renews its request for attorneys' fees under the EAJA under the principles this court discussed in *Karanjah v. Dep't of Social and Health Services*, 199 Wn. App. 903, 926-27, 401 P.3d 381 (2017). The Final Order is not "substantially justified," based upon its lack of substantial evidence for Findings of Fact 2.20 and 2.23, errors of law and arbitrary and capricious decision-making.

Respectfully submitted this 15th day of April, 2019.

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DECLARATION OF SERVICE

I declare that on this 15th day of April, 2019, I caused to be served the foregoing document on counsel for Respondents, and the named court reporters, as noted, at the following addresses:

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Dated this 15th day of April, 2019.

Place: Seattle, Washington

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