

No. 340651
No. 340864
(Consolidated)

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Division III
State of Washington

COURT OF APPEALS, DIVISION III
OF THE STATE OF WASHINGTON

KADLEC REGIONAL MEDICAL CENTER, and
KENNEWICK PUBLIC HOSPITAL DISTRICT,

Appellants,

v.

WASHINGTON STATE DEPARTMENT OF HEALTH,
Respondent.

**KENNEWICK PUBLIC HOSPITAL DISTRICT'S
REPLY BRIEF**

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Kennewick Public Hospital District, formerly doing business as Kennewick General Hospital and now doing business as Trios Health (“KGH” for purposes of this proceeding), respectfully submits this reply to the response/opposition brief of the Department of Health Certificate of Need Program (“Department” or “CN Program”), in this consolidated judicial review action involving the Department, Kadlec Regional Medical Center, and KGH.¹

I. INTRODUCTION

This reply brief addresses the arguments raised by the Department in its response/opposition to the pending consolidated appeals concerning the 2009 Certificate of Need applications of Kadlec and KGH. The Department correctly notes that KGH does not contest the 55 beds that were awarded to Kadlec in 2009, and that if the Court of Appeals reaches the same conclusion as the CN Program, the Health Law Judge, the Secretary of Health’s Review Officer, and the Benton County Superior Court — and upholds the Department’s decision to award only 55 beds to

¹ This is consolidated judicial review action. KGH and Kadlec submitted CN applications in 2009 that were concurrently reviewed by the Department. KGH intervened as a party to the adjudicative proceeding commenced by Kadlec. AR 72-74. Kadlec intervened as a party to the adjudicative proceeding commenced by KGH. AR 219-23. The adjudicative proceedings were consolidated (AR 251-55), as were the proceedings before the Benton County Superior Court and these consolidated appeals (No. 340651 and No. 340864).

Kadlec based on Kadlec's 2009 application — then KGH accepts that decision and the Department's corresponding decision to deny KGH's 25-bed application.

In other words, KGH requests that the Court affirm the Department's denial of Kadlec's 2009 requests for 75 or 114 beds beyond the 55 beds Kadlec already received. Given the passage of time, this litigation is not the appropriate procedural mechanism to make decisions for the Benton/Franklin planning area based on stale data more than six years out-of-date. However, if the Court is inclined to take the extraordinary measure of changing the outcome of more than six years of proceedings and litigation before the Department, the Health Law Judge, the Secretary of Health's Review Officer, and the Benton County Superior Court, and if additional need for beds beyond the 55 beds approved six years ago is found in connection with or stemming from this judicial review proceeding, then KGH respectfully requests the approval of KGH's request for 25 acute care beds, and that the Department issue a CN awarding KGH up to 25 additional beds. KGH's application was reasonable and well-founded when it was submitted in 2009, and when examined with Kadlec's 2009 application in context based on the information available at that time, KGH's application for 25 beds should have been approved.

II. ARGUMENT

A. Argument Overview.

The Department's response brief addressed the Kadlec and KGH 2009 CN applications, which were reviewed by the Department together. This Court's review is limited to whether the Department's decisions about the 2009 CN applications were appropriate based on the then-existing record.² This action is not about the current conditions in the Benton-Franklin planning area. Numerous developments have taken place in the Benton-Franklin planning area since Kadlec and KGH submitted CN applications in 2009. But facts and circumstances regarding the present conditions of the planning area are outside the scope of this proceeding. As a result, as the underlying litigation proceedings have

² As explained in KGH's Opening Brief at p.4, this judicial review proceeding is based upon the Administrative Record ("AR"), which contains the Application Record ("App.R") and the adjudicative hearing transcript ("Hrg. Tr."). The Application Record was created in 2009-2010. *See* Initial Order at AR 2383 ("the Presiding Officer finds that the relevant evidence is the evidence available before the initial decision maker (Program)... This ruling helps prevent a revolving door of remands to obtain even more accurate, current data upon which to make a decision."); Secretary of Health Review Officer's Final Order at AR 2706 ("the administrative review is based entirely upon the record and determines whether the Initial Order was appropriate based solely on the information available during the application process."); Benton County Superior Court Order attaching Ruling Transcript at Clerk's Papers ("CP") 141-142 ("this court's decision as to whether the Department's actions were arbitrary and capricious is based on the record available at the time the decision was made and that action was taken."); *see also University of Washington Medical Center v. Department of Health*, 164 Wn.2d 95, 103-104, 187 P.3d 243, 246-247 (2008) (affirming limitation of evidence to a snapshot in time).

demonstrated time and again, the current conditions in the planning area and what is best for the planning area today cannot and should not be evaluated in this proceeding.

Rather than apply for additional beds based on current data, Kadlec seeks through this litigation to retroactively double the number of acute care beds it was awarded by the Department in 2009-2010. Instead of the 55 beds Kadlec received then (a significant 31% increase in Kadlec's licensed bed capacity, from 176 to 231 acute care beds), Kadlec asks this Court to add — more than six years after the fact — 59 additional beds for a total of 114 beds. Kadlec's excessive request was based on unprecedented speculation, assumptions, overstatements, and an inflated need analysis that necessarily relied on an extended 10-year planning horizon to justify its proposal. Kadlec's request for additional beds beyond the 55 beds it received six years ago was properly denied — by the CN Program, by the Health Law Judge, by the Secretary of Health's Review Officer, and by the Benton County Superior Court. KGH respectfully requests that this Court do the same. However, if bed need beyond the 55 beds previously approved is somehow determined from this judicial review proceeding based on 2009 data, then KGH respectfully requests the approval of its request for 25 acute care beds as a reasonable, rational and fair result.

B. KGH Concurs with the Department's Conclusion Regarding Kadlec's Application.

KGH concurs with the Department's conclusion that Kadlec should not have been approved in 2009-2010 for more than 55 beds. The record is clear that the Department's use of the medium-series population projection and a seven-year planning horizon were appropriate at the time the decisions were made on the 2009 CN applications.

The parties in this case (including Kadlec) agreed that the State Health Plan ("SHP") methodology was the proper standard to use for projecting need for acute care beds in the Benton-Franklin planning area. Further, the parties agreed that the Office of Financial Management ("OFM") was the best and most accurate predictor of population growth. The question therefore is whether the Department reasonably adhered to the State Health Plan standard requiring use of the most accurate population forecasts "available at the time of forecasting" in 2009-2010. AR 4262 (SHP at p. C-30).

KGH and the Department agreed that OFM medium series projections were properly applied as the most accurate forecasts at the time of use in 2009-2010. The medium series contained specific forecasts broken down by age cohorts. The OFM high series did not. These cohort breakdowns were critical in applying the State Health Plan methodology.

Age is a material factor in projecting bed need because the 65+ population uses hospital inpatient services (patient days) at a rate that is five times that of the 0-64 population. The impact of over-projecting the 65+ population therefore is a dramatic increase in need forecasts. The only way Kadlec could generate numbers in support of its 114 bed proposal was to derive its own hybrid analysis of the 65+ cohort – not available from OFM and which could not be replicated by the other parties to this proceeding – and to extend the time horizon out 10 years. The Department used the appropriate population series and seven-year planning horizon in this case. The evidence did not support using Kadlec’s cherry-picked data. To the contrary, substantial evidence supported the use of the medium series with the age cohort breakdowns.³ Kadlec’s request for more beds beyond the 55 it received was properly denied.

³ See Health Law Judge’s Initial Order at pp. 12-13 (AR 2364-65) (noting that Kadlec’s methodology calculations relied on information that was not in the record, did not provide sufficient data to allow the replication of the calculations, and did not support substituting Kadlec’s calculations for the State Health Plan methodology using the OFM medium series); Review Officer’s Final Order at pp. 5-8 (AR 2708-2711) (concluding at AR 2710 that “[b]ased on the record, the Program’s reliance on OFM’s 2007 medium series was reasonable.”); Superior Court Judge Cameron Mitchell’s Order Affirming Department of Health’s Final Order (CP 130-131 and 140) (concluding there is “substantial evidence in the record to support the Department’s decision to use the OFM medium series”).

1. **Substantial Evidence Supported the Department's Decision on Kadlec's 2009 Request for 114 Beds, As Affirmed by the Health Law Judge, the Review Officer and the Superior Court.**

Substantial evidence in this case supported the Department's finding that the State Health Plan methodology was the proper standard for projecting need for acute care beds in the Benton-Franklin planning area. RCW 34.05.570(3)(e); WAC 246-310-210. The State Health Plan states that "[t]he most accurate population forecasts available at the time of forecast should be used" and that OFM forecasts, including age specific forecasts, should be "the basic forecast used." AR 4262 (SHP at p. C-30) (underline emphasis added).

a. **The OFM medium series.**

The OFM medium series met the State Health Plan's accuracy requirements in this case. OFM is the State's chief demographer, and OFM develops the population projections, not the Department. AR 4533-4534 (Hrg. Tr. 149:13-150:20). Acting as the state's expert in the area of population forecasting, OFM's demographers recommended the medium series as the most likely to occur. RCW 43.62.035; *see also* AR 4716 (Hrg. Tr. 331:5-20) (Kadlec's expert noting that "OFM population data is considered much more reliable than commercially available data" and that "OFM has a much more robust forecast methodology that focuses on state level variables and parameters and it also calibrates based on local

variables and parameters, and so you have a lot more local sensitivity in the OFM forecast than you would with an organization such as Claritas”); AR 2097 (CN Program noting that “it is reasonable for the Department to defer to OFM’s expertise in the area of population forecasts.”).

The Department reasonably adhered to the State Health Plan standard requiring the most accurate population forecasts “available at the time of forecasting” in 2009-2010. AR 4262 (SHP at p. C-30) (underline emphasis added). Substantial evidence in the record supported the conclusion that the OFM medium series projections were properly applied as the most accurate forecasts at the time of consideration. The Benton-Franklin planning area has a long history of significant population fluctuations, both up and down. AR 3864 (App.R 1127); AR 4441 (Hrg. Tr. 57:6-17). In light of these complicating factors, the OFM expert demographers recommended the medium series as the “most likely” scenario. AR 4817-4818 (Hrg. Tr. 432:24-433:3).

In addition, the Department performed appropriate diligence in this instance regarding whether the medium series offered the most accurate forecast at the time. OFM recognized that its 2002 projections did not accurately predict the growth in the Benton-Franklin planning area. It evaluated the actual growth in the planning area and adjusted its 2007 projections to reflect this higher rate of growth. AR 4015 (App.R 1277).

The Department and KGH independently contacted OFM to inquire about these adjustments and whether the medium series, as recently adjusted, was still the most appropriate population projection. AR 3890 (App.R 1153); AR 4901-4903 (Hrg. Tr. 515:22-517:14). Kadlec did not. AR 4806-4807 (Hrg. Tr. 421:24-422:17). OFM indicated that it was aware of the high growth rate in the planning area and that its adjustments in 2007 addressed that high rate of growth. AR 4439-4441 (Hrg. Tr. 55:20-57:17); AR 3864 (App.R 1127). In short, substantial evidence supported the conclusion that the Department reasonably relied on OFM's representations, and that the Department's decision was not arbitrary or capricious. AR 4533-4534 (Hrg. Tr. 149:13-150:20); Review Officer's Final Order at AR 2710 ("Based on the record, the Program's reliance on OFM's 2007 medium series was reasonable."); Superior Court Order at CP 140 (noting substantial evidence for OFM medium series).

b. The age cohort breakdown in projecting bed need.

The State Health Plan requires use of the most accurate population forecast available, and that forecasts prepared by OFM, including age specific forecasts, should be the used. AR 4261 (SHP at p. C-29) ("[f]or the group of people being considered, patient day forecasts should to the extent to which it is practical and to which available, be calculated

separately for those age and sex groups which have significantly different use rates”); AR 4262 (SHP at p. C-30) (“[p]opulation forecasts prepared by the [OFM], including age and sex specific forecasts, should be the basic forecasts used”); AR 4443-4444 (Hrg. Tr. 59:20-60:24).

The medium series was the only population projection that met the standard of including age specific projections. *Id.* The OFM medium series projection contains age specific forecasts, on a county by county basis, and the high series does not. AR 4525 (Hrg. Tr. 141: 16-24); AR 2098-2099. Age is a material factor in projecting bed need because the 65+ population uses inpatient hospital services at a rate five times that of the 0-64 population. AR 4527-4528 (Hrg. Tr. 143:2-144:7); AR 2759 (App.R 41) (Kadlec’s CN Application noted that “residents over age 65 utilize inpatient healthcare at a rate over five times that of the residents ages 0-64”); AR 4543 (Hrg. Tr. 159:2-25) (CN Program citing to State Health Plan standards at C-30 regarding use of OFM age specific forecasts). The impact of over-projecting the 65+ population therefore has a dramatic increase on need forecasts. AR 4920 (Hrg. Tr. 534:1-15) (“the 65-plus drives the bed need methodology”); AR 4925 (Hrg. Tr. 539:4-22) (“impact on bed need is over 30 beds”).

In this matter, Kadlec requested that the Department apply an OFM population forecast that lacks these vital breakdowns. To

compensate for the lack of age cohort breakdown in the high series, Kadlec unilaterally made a series of assumptions to manufacture this information. The Department took the proper course in relying on the medium series in this instance. *See* AR 2708-2711 (Review Officer's Final Order at pp. 5-8).

Simply stated, Kadlec's estimates were not based on either the 2007 OFM medium or high series. Instead, Kadlec came up with its own analysis, interweaving assumptions about population growth rates and age cohort breakdowns, and grafting them on to the OFM high series. Kadlec's self-created hybrid forecast is inconsistent with the State Health Plan, because it was not the "most accurate" nor was it even "available." Kadlec's analysis, assumptions and calculations were not available or reasonably capable of being independently tested and verified. *See* Health Law Judge ("HLJ")/Presiding Officer's Initial Order (AR 2364-65); AR 4791 (Hrg. Tr. 406:1-17); AR 4999-5000 (Hrg. Tr. 613:6-614:3) (noting that Kadlec's analysis could not be replicated because OFM doesn't provide sufficient data for high series and noting that "how you move a very young community in a very short time frame to that kind of aging is unprecedented"); AR 5007 (Hrg. Tr. 621:6-20) (Kadlec's numbers can't be replicated). The overinflation of the 65+ age cohort population figures and growth rate is important, because that age group uses health care

services at five times the rate for the younger cohort. Thus, any inflation of the older population has a compounding effect on projected patient days and planning area need. AR 4934-4935 (Hrg. Tr. 548:1-549:1).

Moreover, even if the high series forecast had been used, both the Health Law Judge and the Review Officer determined that the result would have been the same. The Health Law Judge concluded that “even if the high OFM high population forecast was the appropriate forecast, the Presiding Officer finds that the percentage of the age 65 figure should be the one for the Benton/Franklin County planning area, and not the state average as used by Kadlec.” AR 2365; *see also* AR 2712-13 (Review Officer concluding that “[t]he most accurate population forecast available at the time of the CN applications was OFM’s 2007 medium series”); Superior Court Judge Cameron Mitchell’s Order Affirming Department of Health’s Final Order (CP 130-131 and 138-140)(concluding there is “substantial evidence in the record to support the Department’s decision to use the OFM medium series.”).

c. A seven-year, not ten-year planning horizon was appropriate.

The Department applies a seven-year horizon for expansion projects. The State Health Plan standards are clear that “for most purposes bed projections should not be made for more than seven years into the future.” AR 4262 (SHP at p. C-30). It is only for major policy questions, such as whether a community should have a hospital or additional

hospitals, should long-range projections be prepared. AR 4262 (SHP at p. C-30). No matter how characterized by Kadlec, as an expansion project on an existing hospital, the case simply did not meet this standard. AR 4431-4433 (Hrg. Tr. 47:17-49:7).

Moreover, this matter involved a review of two CN applications, and the same rules applied to both applications. The Department stated at the outset of its review process in 2009 that the planning horizon was seven years, and KGH relied on that representation. AR 3415 (App.R 687) (Department's Evaluation at 11); AR 4262 (SHP at p. C-30) ("because in general long-range forecasts are unreliable, forecasts should go only as far into the future as needed to answer the type of policy questions being asked").

Kadlec itself acknowledged the Department's use of a seven-year horizon in its CN application in November 2009. AR 2769-2770 (App.R 51-52) ("In determining bed need, the Department uses a 'target year,' defined as seven years after the last full year of actual patient day statistics."). It was only much later that Kadlec changed its position and proposed a ten-year horizon in its rebuttal submission. AR 3387 (App.R 661). However, this would be inconsistent with the State Health Plan's guidance regarding hospital expansion projects. The Department used the

appropriate planning horizon in this case. *See* AR 2711 (Review Officer's Final Order at p. 8).

2. **The Department's Decision on Kadlec's 2009 Request for 114 Beds Was Not Arbitrary and Capricious.**

Kadlec asserts that the denial of its 114 bed request based on the population forecast and time planning horizon was "arbitrary or capricious." RCW 34.05.570(4)(c)(iii). In other words, Kadlec must show that that the Department's decision on these two issues with respect to Kadlec's 2009 CN application was the result of "willful and unreasoning disregard of the fact and circumstances." *Overlake Hosp. Ass'n v. Dep't of Health*, 170 Wn.2d 43, 57, 239 P.3d 1095 (2010). Based on the foregoing and the robust record supporting the denial of Kadlec's 114 bed request, Kadlec did not and cannot meet this standard. CP 140 ("the Department did not act in an arbitrary and capricious manner").

3. **Kadlec's Inflated Need Assertions.**

The Department of Health concluded that Kadlec's 2009 request for 114 beds should not have been approved. KGH concurs with that conclusion. To the extent Kadlec asserts that out-of-date information about its occupancy statistics and complex care support its need calculation for 114 beds, those assertions are not supported in the record.⁴

⁴ Kadlec has repeatedly chosen to pursue litigation in this matter, but that has never been Kadlec's only option. Even with litigation pending,

The record reflects that Kadlec would not have implemented more than 55 beds by 2014 anyway under any scenario. AR 4682-4684 (Hrg. Tr. 297:11-299:1); AR 4682-4684 (App.R 112-115).

In addition, Kadlec's service mix is not unique, and adding 55 beds to Kadlec would have addressed capacity issues as Kadlec increased its bed count and lowered its average occupancy. The record demonstrated that the vast majority of planning area patient days was for general acute care services as opposed to tertiary services. AR 3710-3712 (App.R 977-979). Granting Kadlec more beds, up to its proposal of 114 beds, would have only served to permit Kadlec to grow at its leisure over a 10 year planning horizon while ensuring no expansion opportunities for KGH's future growth. Moreover, internal need is not a standard for CN approval of more beds in a planning area. *See* AR 1913-1919.

Kadlec's data, based on the available information at the time, indicated that it ran at a 70% average midnight occupancy based on full

nothing has prohibited Kadlec from submitting a new CN application containing current population and occupancy data to support its assertions – which would then be subject to appropriate scrutiny and rebuttal by interested and affected parties. Had Kadlec submitted a new application based on current facts, the Department would have rendered its decision on that new request by now. Kadlec's assertion in effect that the result would have been the same assumes a multitude of unknown facts and circumstances outside the record which make this judicial review process incapable of determining current needs based on facts that are more than six years stale.

year data in 2009. At the time of the application, Kadlec operated 176 acute care beds. At 70% occupancy, Kadlec had, on average, over 50 acute care beds empty per day. AR 4611 (Hrg. Tr. 227:15-20). That figure jumped to over 100 empty beds per day after Kadlec received the additional 55 bed grant. AR 4675-4674 (Hrg. Tr. 290:25-291:17). With this amount of unused capacity at Kadlec alone, any grant of additional beds would have been unwarranted at that time. AR 4433-4436 (Hrg. Tr. 49:9-52:19); AR 4506-4508 (Hrg. Tr. 122:8-124:15) (Department analyst explaining that the addition of the approved 55 beds would change Kadlec's occupancy calculation, and that approval of 114 beds would put Kadlec in a different minimum occupancy class entirely).

Furthermore, the record showed that the majority of inpatient services needed in the planning area were not complex cases requiring specialized beds. Highly complex services available at Kadlec were limited and patient days for those types of highly complex services were very low. Once NICU (neonatal intensive care unit) discharges were removed, for cases in the top 30 Diagnosis Related Groups (DRGs) cited by Kadlec that would be treated in an acute care bed, Kadlec had 57 discharges for all of 2008. AR 2745 (App.R 27). That equates to an average of just 3 patients per day. AR 3710 (App.R 977). As clarified in the testimony at the hearing, even when the definition of "complex" is

expanded beyond the top 30 DRGs to include a wide range of tertiary services, tertiary services accounted for only 13% of the planning area patient days in 2008 and over half of those patient days were provided in hospitals outside the planning area (outmigration). AR 3702, 2710 (App.R 970, 977); AR 5004-5005 (Hrg. Tr. 618:21-619:24) (“in rebuttal, we actually even enlarged the definition of tertiary. And what Kennewick concluded is it is not the driver of bed need in the community. There is about 13 percent of all of the days that are, quote, ‘tertiary.’ So 87 percent of the activity in that community is for the kinds of medical/surgical, OB, ped business that both hospitals do.”).

C. KGH’S Application Met The CN Criteria

1. KGH’s Application Met the Financial Feasibility Criteria (WAC 246-310-220).

The Department relies on the Presiding Officer’s finding that KGH did not meet all the financial feasibility criteria, such as the capital and operating costs criterion of WAC 246-310-220(1). However, substantial evidence in the record supports the conclusion that KGH’s application was and is financially feasible, and the immediate and long-range capital and operating costs of KGH’s project could be met. KGH operates its Southridge campus and its Auburn campus under a single license. KGH’s

capital costs for the project would only be \$519,215, with funds coming out of budgeted capital, and no new construction.⁵

KGH also had sufficient reserves for its project. In the Department's evaluation in 2010, the Department specifically found that KGH "will use Board Designated reserves for the project that are available now." AR 3431 (App.R 703) (Evaluation at 27) (underline emphasis added). The Department also found that KGH "will use a small percent of the assets of the hospital for the reserve financing." AR 3431 (App.R 703) (Evaluation at 27). The Department further noted that "[t]he hospital also expects to expend up to \$6 million of reserves during the same time frame of this project for capital expenditures. This project is included in the \$6 million. The pro-forma data supports funds being available for the entire capital expenditures." AR 3431 (App.R 703) (Evaluation at 27, citing HPDS) (underline emphasis added). The consideration of anticipated future depreciation and profits do not change this reasonable conclusion made at the time the application was submitted.

⁵ Substantial evidence in the record supports KGH's satisfaction of the CN financial feasibility criteria. *See, e.g.*, AR 4879-4890 (Hrg. Tr. 493:14-504:2); AR 5026-5035 (Hrg. Tr. 640:25-649:12); AR 3497-3503 (App.R 767-773) (KGH Application); AR 3683-3692 (App.R 951-960) (KGH Supplemental); AR 4035-4040 (App.R 1297-1302); CP 320-352.

Likewise, KGH's financial ratios and HPDS data sufficiently supported the financial feasibility of the 25-bed project. As noted above, the Department's evaluation cited to the HPDS data in concluding that reserves would be sufficiently available. AR 3431 (App.R 703). The Presiding Officer cited to no new evidence that would change that reasonable conclusion. In addition, the Department had just approved the Southridge Hospital less than a year earlier, and KGH's 25-bed application was predicated on the same financials that had been previously approved by the Department. Substantial evidence supports the financial feasibility of KGH's project.

In addition, as with Kadlec' application, KGH's 25-bed application must be evaluated in context of the then-existing conditions in 2009-2010. As explained in the Department's February 4, 2009 Southridge decision at p. 9 (AR 2004, Attachment 3), new hospital construction typically results in a short-term deterioration of financial position and financial ratios outside state averages are routinely approved for these type of projects.⁶

⁶ In approvals involving other new hospitals, the Department similarly determined that, despite ratios below the average, the projects met financial feasibility standards because the hospitals projected positive financial growth and improving ratios each year. *See* Department's January 25, 2010 *PeaceHealth* decision at p. 18 (AR 2033), and the Department's March 14, 2004 *Franciscan Health System* decision at p. 17 (AR 2073) (attached as Attachments 4 and 5 to KGH Post-Hearing Brief, demonstrating examples of approvals where financial ratios were outside state averages). In this case, the Department noted positive financial

See also AR 4882-4885 (Hrg. Tr. 496:22-499:17) (Carona) (discussing financial ratios and noting that a capital expenditure of about \$500,000 would not jeopardize a hospital's long or short-term financial commitments, particularly when it would generate net revenue improvements as shown on the pro-formas); *see also* AR 3683-3692 (App.R 951-960) (pro formas); AR 5030-5031 (Hrg. Tr. 644:11-645:19) (Marshall) (noting improving financial ratios).

KGH's pro-formas for the Auburn facility demonstrated that 25 beds would improve the financial condition of that facility, and that KGH's projections were reasonable and appropriate under the circumstances. AR 3684 and 3686 (App.R 952 and 954). In addition, the pro formas demonstrated that the addition of the beds at Auburn resulted in an improved financial condition of the hospital as a whole. Auburn wouldn't be operating as a stand-alone facility, and as reflected in the consolidated pro formas provided by KGH, the addition of 25 beds would improve the financial performance of the hospital. AR 3688 and 3691 (App.R 956 and 959) (showing financials with and without the 25 bed project); *see also* AR 5027-5030 (Hrg. Tr. 641:5-644:10) (Marshall) (\$3.2 million operating income with 25 bed project); AR 4885-4888 (Hrg. Tr.

growth and improving ratios for KGH. The Department's denial of KGH's application in this case is inconsistent with those past decisions.

499:23-502:22) (Carona) (considerable financial improvement at KGH with addition of 25 beds); AR 5022 (Hrg. Tr. 636:5-17) (Marshall) (projected growth); AR 3705-3706 (App.R 972-973) (KGH strong growth). In short, substantial evidence in the record supports the financial feasibility of KGH's project, and there was not substantial evidence for a finding to the contrary.

2. **KGH's Application Met the Structure and Process of Care Criteria (WAC 246-310-230).**

In the Department's original evaluation of the applications in 2009-2010, the Department concluded that KGH met all the structure and process of care criteria, except for WAC 246-310-230(4), due to the purported potential for the project to over-extend the financial standing of the organization. AR 3436-3441 (App.R 708-713). Substantial evidence contained in the record, however, supports KGH's satisfaction of the structure and process of care criteria, and does not support a finding to the contrary. AR 4890-4895 (Hrg. Tr. 504:3-509:15); AR 3504-3508 (App.R 774-778) (KGH Application).

KGH met the structure and process of care and cost containment criteria when the project financials are appropriately considered. *See also* AR 4131-4153 (KGH Expert Report (Carona) at pp. 5-7 and Table 2). KGH's campuses would operate under a single, integrated license, and any internal patient transport issues would be handled accordingly by KGH.

Moreover, capital improvements would not be required for the 25 beds to be added, because the Auburn campus would be operating at smaller capacity. AR 5053-5058 (Hrg. Tr. 667:24-672:8) (Marshall).

3. KGH's Application Met the Cost Containment Criteria (WAC 246-310-240).

Substantial evidence contained in the record supports KGH's satisfaction of the cost containment criteria, and does not support a finding to the contrary. AR 3509-3511 (App.R 779-781); AR 4895-4899 (Hrg. Tr. 509:16-513:16). Once an application is deemed to meet WAC 246-310-210 and/or WAC 246-310-220 standards, it typically comes into compliance automatically with WAC 246-310-230 and 240. KGH met the cost containment criteria when the project financials are appropriately considered. In addition, KGH's operating expenses would be lower than Kadlec's. AR 5034-5035 (Hrg. Tr. 648:1-649:11).

4. KGH's Application Was the Superior Alternative.

The Department's assertion that Kadlec's proposal for additional beds was the superior alternative is the product of circular reasoning, particularly if need beyond 55 beds is somehow retroactively determined more than six years after the fact. Kadlec was not the superior alternative under WAC 246-310-240(1), because there was no planning area need for Kadlec's exorbitant bed request, KGH's costs for its 25-bed project were lower, and approving 114 beds would have unnecessarily precluded

growth of other hospitals in the Tri-Cities for many years by allocating all the beds to Kadlec before there was demonstrable need.

In addition, Kadlec would not have implemented more than 55 beds by 2014 anyway under any scenario. AR 4682-4684 (Hrg. Tr. 297:11-299:1); AR 2830-2833 (App.R 112-115). Kadlec's service mix is not unique, and adding 55 beds to Kadlec would have addressed any capacity issues as Kadlec increased its bed count and lowered its average occupancy. The evidence in the record showed that the vast majority of planning area patient days (and the growing element of patient days) was for general acute care services rather than for tertiary services. AR 3710-3712 (App.R 977-979).⁷

Any contention that KGH could have reallocated beds is also misplaced and does not change the analysis. KGH has already implemented a reduction in the number of women's and children's beds from 41 to 27 with the opening of the Southridge Hospital. AR 5050

⁷ The record established that the majority of inpatient services needed in the planning area were not complex cases requiring specialized beds. Highly complex services available at Kadlec were limited and patient days for those types of highly complex services were very low. *See, e.g.*, AR 2745 (App.R 27); AR 3710 (App.R 977) (average of just 3 patients per day); AR 3702, 2710 (App.R 970, 977); AR 5004-5005 (Hrg. Tr. 619:20-22) ("87 percent of the activity in that community is for the kinds of medical/surgical, OB, ped business that both hospitals do.").

(Hrg. Tr. 664:13-16) (Marshall). Southridge had been approved based on a separate application and separate proceeding, and KGH's 25-bed request was appropriate and supported by substantial evidence on its own merits. KGH's 2009 application for 25 additional beds was proportional, appropriate, financially feasible, and the superior alternative to allocating all beds to Kadlec based on the then-existing facts and circumstances contained in the record.

III. CONCLUSION

Kadlec received 55 beds from the Department based on its 2009 application. The Court should affirm the Department's denial of Kadlec's alternate requests for up to 114 beds. However, if additional need for beds beyond the 55 beds approved six years ago is found in connection with or stemming from this judicial review proceeding, then KGH respectfully requests the approval of KGH's request for up to 25 acute care beds.

DATED this 5th day of August, 2016.



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CERTIFICATE OF SERVICE

I certify that I am a citizen of the United States of America and a resident of the State of Washington, over the age of eighteen years, and competent to be a witness herein.

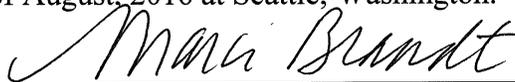
On the date designated below I caused to be served the foregoing document via U.S. Mail and e-mail, pursuant to the parties' e-service agreement, upon designated counsel:

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