

**MISSISSIPPI STATE DEPARTMENT OF HEALTH
DIVISION OF HEALTH PLANNING AND RESOURCE DEVELOPMENT
MAY 2010**

**CON REVIEW HP-CO-0310-015
MISSISSIPPI CHILDREN'S HOME SOCIETY
COST OVERRUN TO CON #R-0767
(CONSTRUCTION OF AN ARTS AND EDUCATION
BUILDING AND COTTAGES FOR THE BENEFIT OF
CARES CENTER, INC.'S PSYCHIATRIC RESIDENTIAL
TREATMENT FACILITY)
APPROVED CAPITAL EXPENDITURE: \$5,548,066
ADDITIONAL CAPITAL EXPENDITURE: \$990,466
REVISED CAPITAL EXPENDITURE: \$6,538,532
LOCATION: JACKSON, HINDS COUNTY, MISSISSIPPI**

STAFF ANALYSIS

I. PROJECT SUMMARY

A. Applicant Information

Mississippi Children's Home Society is a not-for-profit Mississippi corporation dedicated to providing compassionate solutions for children and families. The entity consists of a 34-member governing board. CARES operates a 44-bed psychiatric residential treatment facility (PRTF) for children and adolescents ages 6 through 17, an accredited school providing special education and related services to 120 children and adolescents, and a group home for adolescents ages 13 through 18 who suffer from substance abuse and serious emotional distress. Mississippi Children's Home Society (MCHS), an affiliated of CARES, owns the property and leases same to CARES. CARES had a 99.15 percent occupancy rate with an average daily census of 43.51 for FY 2007.

B. Project Background

Mississippi Children's Home Society obtained CON authority for construction of an Arts and Education Building and cottages for CARES Center, Inc.'s PRTF project by Certificate of Need No. R-0767, effective June 26, 2008. On December 8, 2009, MCHS was approved for a six-month extension on CON No. R-0767. This extension period will terminate June 26, 2010.

Mississippi Children's Home Society states in the original application that the applicant acquired 21 acres of land located at 200 North West Street in Jackson, and after much consideration and evaluation, determined that the best use of the property would be to expand the CARES Center campus by building cottage-style housing for 30 residents attending Grades 1 through 6 in CARES school (the "CARES Elementary School"). CARES school provides education not only to the residents of CARES' PRTF but also to other children in elementary school within a 50-mile radius

of Jackson, who have severe emotional and behavioral problems. MCHS indicates that CARES Elementary School will continue to serve the same population of children.

The applicant states that simultaneously with the filing of MCHS' original project, CARES Center filed a CON Amendment and Cost Overrun requesting authority to amend CON #R-0651 to allow CARES to locate 16 of the PRTF beds that it is relocating from Harrison County to the expanded CARES campus. MCHS will construct the cottages that will house the 16 PRTF beds and CARES will lease the cottages from MCHS.

MCHS asserts that in order to keep cost down. MCHS will construct all the buildings covered by both projects with an allocation of 77 percent to this project and 23 percent of cost to the CARES' CON amendment and Cost Overrun project (2008). The expanded CARES campus located at 2000 North West Street ("Expanded CARES Campus") will be developed to include initially three (3) residential cottages for the residents of the PRTF, each consisting of 4,754 square feet of space and capable of housing 10 residents, and the CARES Elementary School. Upon completion of the project submitted by MCHS and this CON Amendment, the Expanded CARES Campus, with its three (3) cottages, will be capable of housing 30 PRTF residents. The existing CARES campus will continue to be capable of housing up to 44 residents, depending on the ages and acuity levels. Residents at the existing CARES Campus will be of a higher acuity level than those housed in the cottages. The three (3) cottages on the Expanded Campus will be designated as follows: one cottage for up to 10 younger children ages 6 through 11; one cottage for 10 adolescent girls who are at a lower acuity level; and one cottage for up to 10 adolescent boys who are at a lower acuity level. The applicant submits that at no time will the residents of CARES Center exceed 60 in number.

The Division of Health Facilities Licensure and Certification approved the site for the project.

C. Project Description

Mississippi Children's Home Society now requests Certificate of Need authority for a cost overrun to its CON No. R-0767. Mississippi Children's Home Society asserts that the proposed cost overrun is necessary to complete the original project. According to the applicant, the capital expenditure approved in the original CON is \$5,548,066 and the additional costs for this cost overrun proposal are \$990,466 resulting in a revised capital expenditure of approximately \$6,538,532 for the project. This cost overrun project does not change the scope of the original project.

According to the MCHS, the construction contract, which included site preparation cost, was in an amount greater than had been estimated by the architect in his cost estimate contained in the original application. Reasons for such increase include the fact that the site itself required more preparation than originally anticipated, an increase in the cost of materials, and changes to the project requiring change orders.

The increase in non-fixed equipment is primarily the result of the need for additional and higher quality furnishings than had been anticipated to create the homelike environment sought by utilizing the cottage concept. Another reason for the increase in cost is that MCHS determined that some of the furniture and furnishings initially anticipated to be used needed to be upgraded to provide for longevity.

The increase in architectural fees results from the greater than estimated cost of construction and the change orders.

Capitalized interest was greater than originally anticipated primarily because the architect's cost estimate was lower than the actual cost of the project. The applicant states, however, that because of the manner in which the closing was structured, there is interest earned on deposits to offset such capitalized interest.

The contingency reserve estimated by the architect in his cost estimate contained in the original application was determined by calculating 10 percent of the cost of the architect's cost estimate. However, because the project is essentially complete, such contingency reserve has been lowered. The applicant asserts that although the costs of the MCHS project are no longer simply estimates, a contingency reserve in the amount of \$231,000 is included in an abundance of caution.

According to Mississippi Children's Home Society, 99 percent of the project is completed. The applicant states that MCHS has expended \$5,357,585 with respect to this project.

The applicant asserts that Mississippi Children's Home Society CON No. R-0767 authorized construction of arts and education building and cottages for CARES Center, Inc.'s PRTF. Together the projects (MCHS and CARES) were approved for a total capital expenditure \$7,996,556.43. As noted in the filing of this cost overrun regarding both projects, \$7,743,259 has been expended toward completion of both the MCHS and CARES projects.

According to the MCHS, in order to conserve financial resources and realized cost efficiencies, Phase II of the CARES project and the MCHS project are being

constructed at the same time, pursuant to one contract for construction and on agreement with the architect. Therefore, the MCHS project and the CARES project are intertwined.

The applicant asserts that the architect's cost estimate for the construction of both projects was \$5,540,947.20, the actual construction contract with Evan Johnson, the contractor that was selected after a competitive bidding process, was in the amount of \$6,567,000 for both projects, and the estimated contingency fee in the amount of \$600,839.38 will not be sufficient to absorb the difference. Also, the higher construction cost results in higher architects' fees. Additionally, the cost estimated for non-fixed equipment (\$280,500) for the MCHS project will be insufficient to cover the actual cost of the non-fixed equipment, the cottages that will house 16 of the PRTF beds, and all the equipment, furniture, and furnishings for the arts and education building.

II. TYPE OF REVIEW REQUIRED

The original project was reviewed under the applicable statutory requirements of Section 41-7-191, subparagraph (1) (j), Mississippi Code of 1972, as amended.

The State Health Officer reviews all projects for cost overruns in accordance with duly adopted rules, procedures, plans, criteria and standard of the Mississippi State Department of Health.

In accordance with Section 41-7-197(2) of the Mississippi Code or 1972 Annotated, as amended, any affected person may request a public hearing on this project within 20 days of publication of this staff analysis. The opportunity to request a hearing expires on June 7, 2010.

III. CONFORMANCE WITH THE STATE HEALTH PLAN AND OTHER ADOPTED CRITERIA AND STANDARDS

A. State Health Plan

The original project was in substantial compliance with the *FY 2007 State Health Plan*, in effect at the time the original application was submitted. This cost overrun project continues to be in substantial compliance with the *State Health Plan*.

B. General Review Criteria

The original project was in substantial compliance with the *Certificate of Need Review Manual, 2008 revision*, in effect at the time of submission. This application continues to be in compliance with applicable general review criteria and standards contained in the *Manual*.

IV. FINANCIAL FEASIBILITY

A. Capital Expenditure Summary

	<u>Approved Capital Expenditure</u>	<u>Revised Capital Expenditure</u>	<u>Increase (Decrease)</u>
New Construction	\$4,252,896	\$5,064,408	\$811,512
Renovation	0	0	0
Capital Improvements	0	0	0
Land	0	0	0
Site Work	0	0	0
Fixed Equipment	0	0	0
Non-Fixed Equipment	280,500	469,878	189,378
Architectural/Engineering Fees	389,399	439,937	49,538
Contingency Reserve	462,646	231,000	(231,646)
Capitalized Interest	143,375	263,179	119,804
Other Cost (accounting, closing costs for bond issuance)	19,250	70,130	51,880
Total	\$5,548,066	\$6,538,532	\$990,466

As previously mentioned, the capital expenditure approved in the original CON is \$5,548,066 and the additional costs for this cost overrun proposal are \$990,466 resulting in a revised capital expenditure of approximately \$6,538,532 for the project. This cost overrun project does not change the scope of the original project.

The applicant states that MCHS has expended \$5,357,585 with respect to this project. This project is about 99 percent complete.

B. Method of Financing

Mississippi Children's Home Society is financing and constructing the cottages and the arts and education building and acquiring the non-fixed equipment using proceeds from the issuance of an obligation bond by Mississippi Business Finance Corporation in the principal amount of \$8,000,000, having the following terms: 5.12 percent annual interest, ten-year term, and 20-year amortization with respect to annual interest rate.

The applicant asserts that the CARES will lease all three of the cottages and the arts and education building from MCHS and all of the furnishings and equipment for the cost of the MCHS financing, approximately \$400,000 per year. The lease cost is lower than originally anticipated because MCHS has been successful in paying down the debt, thus lowering CARES' lease payments.

C. Effect on Operating Cost

Revised Projected Operating Statement
For the First Full year of Operation
After Completion of this Project

Revenue	
Allocations from United Way	\$140,000
Contributions	281,877
Special Events	282,000
Legacies and Bequests	17,000
Fees and Grants	9,430,460
Program Fees and Net Incidental Revenue	80,440
Investment and Rental Income	1,225,982
Total Revenue	\$11,458,259
Expenses	
Salaries	\$4,591,888
Benefits	1,026,014
Professional Fees	1,430,334
Program Supplies and other Expenses	403,607
Telephone	93,244
Postage and Shipping	33,150
Occupancy	955,495
Rental and Maintenance	118,017
Printing and Publications	27,231
Travel	907,422
Conferences and Meetings	45,426
Specific Assistance to Individuals	23,324
Membership dues	15,723
Insurance (other than employee benefits)	121,647
Interest and Miscellaneous	21,398
Depreciation	476,709
Other	1,018,665
Total Operating Expense	\$11,309,294
Net Income (Loss)	\$ 148,965

D. Cost to Medicare/Medicaid

The applicant asserts that because Medicaid reimburses psychiatric residential treatment facilities based on a pre-established fair bed value basis and not on a capital cost basis, the effect of this CON cost overrun on Medicaid, if any, is minimal.

V. RECOMMENDATION OF OTHER AFFECTED AGENCIES

The Division of Medicaid was provided a copy of this cost overrun to CON #R-0767 for review and comment.

VI. CONCLUSIONS AND RECOMMENDATION

This project continues to be in substantial compliance with the overall objectives of the FY 2007 *State Health Plan; Certificate of Need Review Manual; Revised 2008*; and all adopted rules, procedures, and plans of the Mississippi State Department of Health in effect at the time of approval.

The Division of Health Planning and Resource Development recommends approval of the application submitted by Mississippi Children's Home Society for a cost overrun to CON #R-0767 (construction of an arts and education building and cottages for the CARES Center Inc.'s PRTF beds).