THE University of Vermont MEDICAL CENTER

By Electronic Mail and U.S. Mail

January 20, 2022

Donna Jerry
Senior Health Policy Analyst
Green Mountain Care Board
144 State Street
Montpelier, Vermont 05620
Donna.Jerry@vermont.gov

Re: Conceptual Development Phase Certificate of Need Application, and Certificate of Need Application

Dear Ms. Jerry:

The University of Vermont Medical Center Inc. ("UVM Medical Center") hereby submits 1) a Certificate of Need application for the relocation of outpatient Dermatology and Ophthalmology practices to an unoccupied building at 350 Tilley Drive in South Burlington, which UVM Medical Center will purchase from Pizzagalli Properties, at a total capital cost of $35,246,100 (the "Project"); 2) a Conceptual Development Phase Certificate of Need Application for certain outstanding pre-construction Project planning activities and expenditures; and 3) a request for relief from sanctions pursuant to Green Mountain Care Board Rule 4.700(f).

1. **Certificate of Need Application**

We are pleased to submit the following materials supporting UVM Medical Center's Certificate of Need Application:

1. Letter of Intent, requesting expedited review;
2. Certificate of Need Application.

We will submit a Verification under Oath, signed by Stephen Leffler, M.D. next week. Since we are requesting expedited review, we understand that your office will provide public notice in accordance with 18 V.S.A. §§ 9440(c)(2)(B) and 9440(c)(5)(A).

2. Conceptual Development Phase Certificate of Need Application

UVM Medical Center conceived this Project in 2018 with the intent to lease the 350 Tilley Drive building. Project planners determined that the contemplated lease would be an "operating lease" under the then-prevailing Financial Accounting Standards Board ("FASB") lease classification rules; as a result, the Project's capital costs would be well under $30 million; and UVM Medical Center could therefore complete pre-construction planning activities without obtaining a Conceptual Development Phase Certificate of Need ("CCON").

Project planning proceeded on those assumptions until UVM Medical Center reevaluated the Project in September – November 2021; decided it makes financial sense under current market conditions to buy the 350 Tilley Drive building rather than lease it; and further determined that the previously contemplated lease is a capital lease under an amended FASB rule that UVM Medical Center adopted in October, 2019.

Today, the Project's capital costs will exceed $30 million whether UVM Medical Center buys or leases the building, and a CCON is therefore required for planning activities and expenditures. UVM Medical Center has completed the project planning necessary to support its CON application, but additional pre-construction planning remains incomplete. UVM Medical Center therefore submits the following materials in support of a CCON application for approval to finish the outstanding pre-construction planning work:

1. Letter of Intent, requesting expedited review;
2. Conceptual Development Phase Certificate of Need Application.

The proposed additional planning expenditures, if approved, will allow UVM Medical Center to complete its planning while the Board considers its Certificate of Need application, thereby allowing us to more quickly provide improved access to outpatient ophthalmology and dermatology services if the Board grants the requested CON.

We will submit a Verification under Oath, signed by Stephen Leffler, M.D. next week. Since we are requesting expedited review, we understand that your office will provide public notice in accordance with 18 V.S.A. §§ 9440(c)(2)(B) and 9440(c)(5)(A).

3. Request for Relief from Sanctions

Finally, pursuant to Green Mountain Care Board Rule 4.700, UVM Medical Center submits a request for relief from sanctions for conducting some Project planning activities in good faith without first obtaining a CCON.

We look forward to working with you during the review process. Please contact me if you have any questions concerning our application materials.

Sincerely,

Eric Miller
Senior Vice President and General Counsel
The University of Vermont Health Network

cc. Stephen Leffler, M.D.

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January 20, 2022

Donna Jerry
Senior Health Policy Analyst
Green Mountain Care Board
144 State Street
Montpelier, Vermont 05620
Donna.Jerry@vermont.gov

Re: Letter of Intent for Conceptual Development Phase Certificate of Need

Dear Ms. Jerry:

The University of Vermont Medical Center Inc. ("UVM Medical Center") files this Letter of Intent and the attached Conceptual Development Phase Certificate of Need ("CCON") application to undertake planning activities and expenditures related to the relocation of its outpatient Dermatology and Ophthalmology practices from the UVM Medical Center Main Campus and 462 Shelburne Road to 350 Tilley Drive in South Burlington, an unoccupied building awaiting fit-up (the "Project").

UMV Medical Center is seeking expedited approval of the CCON without a hearing and with such other abbreviated process as the Green Mountain Care Board (the "Board" or "GMCB") finds appropriate. The Board may grant expedited review of a CCON application pursuant to Certificate of Need Rule 4.304(1)(d). We respectfully request that the Board issue written notice granting a CCON without any further process.

In accordance with 18 V.S.A. § 9440(c)(2) and Certificate of Need Rule 4, we provide the following information about the Project, which we further discuss in the attached application:

Project Scope: The Project involves planning for the relocation of outpatient Dermatology and Ophthalmology practices from UVM Medical Center's Main Campus and 462 Shelburne Road to 350 Tilley Drive in South Burlington. UVM Medical Center will purchase the 350 Tilley Drive building from Pizzagalli Properties, fit-up 24,115 department gross square feet (DGSF) on the first floor and 25,032 DGSF on the second floor, and build a 2,220 sq. ft. addition for staff entry, elevators, loading area, and space for storage and waste management.

Project Rationale and Objectives:	The relocation of outpatient Dermatology and Ophthalmology will address the current and projected rising demand for Dermatology and Ophthalmology services and procedures, driven largely by the healthcare needs of the region's growing and aging population. Both practices have outgrown the spaces they now occupy and expansion at their existing locations is not possible. The relocation will allow for the addition of 14 clinical spaces for Dermatology and 5 for Ophthalmology, facilitate scheduling optimization and workspace efficiencies, and enable the practices to attract and accommodate additional providers. The relocation aligns with the UVM Medical Center Ambulatory Master Facility Plan. The Master Plan identifies Dermatology and Ophthalmology as highly ambulatory services that "Make More Sense Off-Campus" in contrast to other services that support emergent and inpatient care and are best located on the Main Campus. The Master Plan also includes a strategy for phased relocation of services from leased space at 1 South Prospect Street in Burlington, and this project will allow Neurology to move from South Prospect Street to space that will be vacated on the Main Campus.
Need to be Addressed:	The relocation of Dermatology and Ophthalmology to 350 Tilley Drive responds to the needs of patients in our service area for increased access to outpatient Dermatology and Ophthalmology services and enables the future relocation of outpatient Neurology to the Main Campus Ambulatory Care Center as a part of UVM Medical Center's Masterplan to improve our outpatient patient care facilities.
Cost, Access, Quality:	The relocation of Outpatient Dermatology and Ophthalmology to 350 Tilley Drive will improve access to quality care in the right environment, which will in turn promote positive health outcomes that reduce long term costs of care.
Location:	UVM Medical Center has established an outpatient campus in the vicinity of 350 Tilley Drive, which currently includes outpatient cardiology, endocrinology, orthopedics and rehabilitation, pain management, physical therapy, and radiology clinics, and may include an outpatient surgery center in the future.

Service Area: UVM Medical Center Hospital Referral Region

Projected Expenditures: $92,020 for planning prior to fit-up of the space and construction of the addition. As explained in UVM Medical Center's Request for Relief from Sanctions filed January 20, 2022, UVM Medical Center has already spent $452,499 on project planning in reliance on its good faith projection that the capital costs of the relocation would be well under the $30 million jurisdictional threshold for a CCON, which was reasonable based on a totality of the underlying facts and circumstances.

We look forward to working with you during the review process for this application.

Sincerely,

Eric Miller
Senior Vice President and General Counsel
The University of Vermont Health Network

STATE OF VERMONT
GREEN MOUNTAIN CARE BOARD

CONCEPTUAL DEVELOPMENT PHASE CERTIFICATE OF NEED APPLICATION

by

THE UNIVERSITY OF VERMONT MEDICAL CENTER INC.

for

PLANNING EXPENDITURES RELATED TO RELOCATION OF OUTPATIENT DERMATOLOGY AND OPHTHALMOLOYGY TO 350 TILLEY DRIVE, SOUTH BURLINGTON

January 20, 2022

CONCEPTUAL DEVELOPMENT PHASE
CERTIFICATE OF NEED APPLICATION

The University of Vermont Medical Center Inc. ("UVM Medical Center") submits this Conceptual Development Phase Certificate of Need Application to the Green Mountain Care Board (the "Board") pursuant to 18 V.S.A. 9434(c) and Board Rule 4.206. We request expedited issuance of a Conceptual Development Phase Certificate of Need (a "Conceptual CON") approving the expenditure of $92,020 on planning activities in the conceptual development phase of a project to relocate outpatient Dermatology and Ophthalmology practices from the UVM Medical Center Main Campus and 462 Shelburne Road to 350 Tilley Drive in South Burlington (the "Project"). A Conceptual CON is required because the capital cost of the Project is expected to exceed $30 million.

The Board "shall grant" a Conceptual CON if it finds that:

(a) The cost of the proposed planning activities is reasonable and the applicant can afford such cost;
(b) The project appears to meet an identifiable, existing or reasonably anticipated need which is appropriate for the applicant to provide; and
(c) If the project includes or comprises the purchase or lease of health information technology, the project is consistent with the most current Vermont Health Information Technology Plan.[1]

Board Certificate of Need Rule 4.206.

The following Part I demonstrates that the Project will "meet an identifiable, existing or reasonably anticipated need," and Part II shows that the proposed costs are reasonable and affordable.

I. The Project Meets an Identifiable Need

There is a clear and identifiable need for the project. The current demand for Dermatology and Ophthalmology services is strong and projected to increase as the region's population ages. The two practices are currently housed in multiple separate spaces that cannot be expanded or renovated to meet the growing demand. The new location will add needed clinical and support space, and increase efficiencies. In addition, the relocation of these practices is consistent with the UVM Medical Center Master Facility Plan, as it appropriately locates ambulatory services outside the Main Campus, while freeing up limited space on the Main Campus for services that support inpatient and emergent care.

II. The Costs of the Proposed Planning Activities are Reasonable and Affordable

[1] The Project does not involve the purchase or lease of health information technology. Rule 4.206(c) is therefore inapplicable.

As explained in UVM Medical Center's Request for Relief from Sanctions filed January 20, 2022, UVM Medical Center has already spent $452,499 on project planning in reliance on its good faith projection that the Project's capital costs would be well under the $30 million jurisdictional threshold for a CCON, which was reasonable based on a totality of the underlying facts and circumstances. The planning conducted to date is sufficient to support UVM Medical Center's Certificate of Need application filed January 20, 2022. The proposed additional planning expenditures, if approved, will allow UVM Medical Center to complete its planning while the Board considers its Certificate of Need application, thereby allowing us to more quickly provide improved access to outpatient ophthalmology and dermatology services if the Board grants the requested CON.

UVM Medical Center requests a CCON approving the expenditure of $92,020 on completion of pre-construction planning activities generally as follows:

Architectural Design and Planning: UVM Medical Center has retained the services of Scott + Partners Architects to serve as the Architect for this project. Halsa Advisors has been selected to complete the programming for the project. Scott + Partners and Halsa will complete programming, operational planning and design for the fit-up of the space and for the proposed construction of a 2,200 sq. ft. addition to the building.

Permitting: Permitting for the building as currently constructed has been completed by the building's owner. Final additional local and state permitting for the project will be completed for a proposed 2,200 sq. ft. addition to the building.

LEED Certification*:* UVM Medical Center is committed to using sustainable best practices in its operations and construction projects to reduce or mitigate social and environmental impacts and will seek Leadership in Energy and Investment Design (LEED) certification for the interior fit-up portion of the Project. A LEED professional will be engaged to ensure the Project will meet certification criteria. We also intend to achieve an Energy Star score of 75 for this project.

Commissioning: The Project design will be governed by the *2018 Guidelines for Design and Construction of Health Care Facilities* published by The Facility Guidelines Institute (FGI), and must be commissioned to meet current design standards. A commissioning agent has facilitated the development of the "Owner's Project Requirements" and will complete development and execution of the commissioning plan to support the design and fit-up of the space.

Pre-construction Services: A qualified Construction Manager, ReArch Construction, has been retained to work with UVM Medical Center and the design team during planning and design development. ReArch Construction is advising the UVM Medical Center and its architects on construction means and methods to be employed during construction as well as materials selection and construction logistics, scheduling and phasing. The Construction Manager will provide on-going construction cost estimating and value analysis, which is an essential part of the planning and design process.

UVM Medical Center believes this work is reasonable and necessary based on our experience with similar construction projects. The estimated outstanding costs of this work, totaling $92,020, are set out in Table I attached hereto. These costs are included in UVM Medical Center's budgets, and they are affordable.

III. Conclusion

For all the foregoing reasons, the Board should approve UVM Medical Center's application and issue a Conceptual CON as requested.

TABLE 1

Pre-Construction Planning Expenses		
Costs	**Invoiced**	**Outstanding Expenditures**
Design Fees (Architectural, Engineering, Other Related Design Services)	$344,702.00	$82,045.00
Other Consultant Fees	$107,797.00	$9,975.00
Total	$452,499.00	$92,020.00

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Re: Requests for Relief from Sanctions

Dear Ms. Jerry:

The University of Vermont Medical Center Inc. ("UVM Medical Center") requests relief from sanctions for conducting certain pre-construction planning activities for the relocation of outpatient Dermatology and Ophthalmology practices to 350 Tilley Drive in South Burlington (the "Project") without first obtaining a Conceptual Development Phase Certificate of Need ("CCON). As outlined in UVM Medical Center's CCON application filed January 20, 2022, UVM Medical Center has already spent $452,499 on pre-construction Project planning, and requests approval to spend $92,020 on additional planning activities.

Full relief from sanctions is merited under Green Mountain Care Board ("Board") Rule 4.700, which requires the Board to consider the following mitigating factors in determining appropriate sanctions for violations of the Certificate of Need laws:

(c) whether the project will cause an increase in costs to the health care system;
(d) whether the project is likely to reduce or contain the cost of health care services;
(e) whether the project is otherwise consistent with Certificate of Need criteria; [and]
(f) in the case of a facility that incorrectly projects it would not exceed monetary jurisdictional thresholds, whether the erroneous projection was reasonable based on a totality of the underlying facts and circumstances;

Board Rule 4.700.

UVM Medical Center engaged in Project planning activities and expenditures without first obtaining a CCON in good faith, with the intent to lease the 350 Tilley Drive building, and

based on its determination that capital costs would be well below the $30 million jurisdictional threshold.[1] This determination was correct until Financial Accounting Standards Board ("FASB") lease classification rules[2] changed approximately two years after Project planning began (unbeknownst to Project planners); and then UVM Medical Center reevaluated the Project in September - November 2021, and decided it should purchase the 350 Tilley Drive building. Today, Project capital costs will exceed $30 million in either scenario – whether UVM Medical Center buys or leases the building.

UVM Medical Center began planning the Project in 2018 with the intent to lease the 350 Tilley Drive building from Pizzagalli Properties for a 13-year term with an option to purchase. At that time, Project planners applied the then-effective FASB rules for lease classification to determine that lease costs would be an operating expense because the Net Present Value of rent payments was less than 90% of the building's Fair Market Value.[3] Project planners periodically confirmed that lease payments would be an operating expense per this formula, and the Project's

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[1] *See* 18 V.S.A. § 9434(c) (conceptual development phase certificate of need required when capital expenditures in excess of $30 million are anticipated).

[2] Vermont's CON law defines a "capital expenditure" to include "an expenditure for the plant or equipment that is not properly chargeable as an expense of operation and maintenance and includes acquisition by . . . lease that is treated as capital expense in accordance to the accounting standards established for lease expenditures by the Financial Accounting Standards Board, calculated over the length of the lease for plant or equipment. . . ." 18 V.S.A. § 9432(5).

[3] In 2018, the applicable rule was FASB statement no. 13, *Accounting for Leases*, which provided in relevant part as follows:

"Criteria for Classifying Leases (Other than Leveraged Leases)

7. The criteria for classifying leases set forth in this paragraph derive from the concept set forth in paragraph 60. If at its inception (as defined in paragraph 5(b)) a lease meets one or more of the following four criteria, the lease shall be classified as a capital lease by the lessee. Otherwise, it shall be classified as an operating lease. (See Appendix C for an illustration of the application of these criteria.)

a. The lease transfers ownership of the property to the lessee by the end of the lease term (as defined in paragraph 5(f).

b. The lease contains a bargain purchase option (as defined in paragraph 5(d)).

c. The lease term (as defined in paragraph 5(f)) is equal to 75 percent or more of the estimated economic life of the leased property (as defined in paragraph 5(g)). However, if the beginning of the lease term falls within the last 25 percent of the total estimated economic life of the leased property, including earlier years of use, this criterion shall not be used for purposes of classifying the lease.

d. The present value at the beginning of the lease term of the minimum lease payments (as defined in paragraph 5(j)), excluding the portion of the payments representing executory costs such as insurance, maintenance, and taxes to be paid by the lessor, including any profit thereon, equals or exceeds 90 percent of the excess of the fair value of the leased property (as defined in paragraph 5(c)) to the lessor at the inception of the lease over any related investment tax credit retained by the lessor and expected to be realized by him. However, if the beginning of the lease term falls within the last 25 percent of the total estimated economic life of the leased property, including earlier years of use, this criterion shall not be used for purposes of classifying the lease. A lessor shall compute the present value of the minimum lease payments using the interest rate implicit in the lease (as defined in paragraph 5(k)). A lessee shall compute the present value of the minimum lease payments using his incremental borrowing rate (as defined in paragraph 5(l)), unless (i) it is practicable for him to learn the implicit rate computed by the lessor and (ii) the implicit rate computed by the lessor is less than the lessee's incremental borrowing rate. If both of those conditions are met, the lessee shall use the implicit rate."

capital costs remained well under $30 million, as planning activities and negotiations with Pizagalli Properties proceeded over the next few years.[4] The Project was shown as a major project in UVM Medical Center's hospital budget submissions to the Board since FY2019 with capital costs under $30 million, and lease costs included as an operating expense.

In September – November 2021, UVM Medical Center reevaluated the Project, and decided it makes sense to purchase the 350 Tilley Drive building rather than lease it on the terms negotiated with Pizagalli Properties, based in part on a cash flow analysis showing that purchasing the property will save $2.3 million over twenty years.[5] The Project's total capital cost is $35,246,100 if UVM Medical Center buys the building, as proposed in the CON application filed January 20, 2022.

When UVM Medical Center's in-house accountants evaluated the purchase option, they also advised Project planners that UVM Medical Center had adopted a revised FASB standard for lease classification effective October 1, 2019,[6] and the contemplated 350 Tilley Drive lease is a capital lease under this new standard. If UVM Medical Center were to lease the building on the agreed terms as previously planned, the Project's capital costs would be $32,775,161, of which $13,630,754 is attributable to lease costs. In short, the capital costs of the project rose by over $13 million solely as the result of the change in the FASB rule.

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[4] In January 2018, UVM Medical Center signed a Letter of Intent to lease the building for a 13-year term with an option to buy. In May 2019, UVM Medical Center signed a lease agreement contingent on regulatory approval, but terminated it in April 2020 at the onset of the COVID-19 pandemic. In July 2020, UVM Medical Center revisited the Project and signed an Option Agreement for a 13-year lease with an option to buy. UVM Medical Center renegotiated the Option Agreement in the fall of 2021 after determining that purchasing the property is preferable to leasing it under current market conditions, as well as in light of the organization's concurrent plans for other investments in the Tilley Drive area, including development of an outpatient surgery center.

[5] *See* Exhibit A hereto.

[6] The revised standard is ASU 2016-02 *Leases (Topic 842)*, which provides in relevant part:

"**8.3.3 Lease Classification Criteria**
ASC 842-10
25-2 A lessee shall classify a lease as a finance lease . . . when the lease meets any of the following criteria at lease commencement:

a. The lease transfers ownership of the underlying asset to the lessee by the end of the lease term.
b. The lease grants the lessee an option to purchase the underlying asset that the lessee is reasonably certain to exercise.
c. The lease term is for the major part of the remaining economic life of the underlying asset. However, if the commencement date falls at or near the end of the economic life of the underlying asset, this criterion shall not be used for purposes of classifying the lease.
d. The present value of the sum of the lease payments and any residual value guaranteed by the lessee that is not already reflected in the lease payments in accordance with paragraph 842-10-30-5(f) equals or exceeds substantially all of the fair value of the underlying asset.
e. The underlying asset is of such a specialized nature that it is expected to have no alternative use to the lessor at the end of the lease term.

25-3 When none of the criteria in paragraph 842-10-25-2 are met:

a. A lessee shall classify the lease as an operating lease . . . ."

The revised FASB standard is similar in most relevant respects to the predecessor standard that was applied to classify the lease as an operating lease in 2018. The Present Value of lease payments relative to the building's Fair Market Value remains relevant. The revised standard includes a new term, however, which provides that a lease is a "finance lease," and lease costs are capital costs, if the lease grants the tenant an option to purchase and the tenant is "reasonably certain" to exercise that option. Implementation Guidance interpreting the standard provides that "reasonable certainty" is assessed based on all the relevant "contract-based, asset-based, market-based, and entity-based" factors.[7]

In-house accountants advised that the previously contemplated 13-year lease with an option to purchase is a "capital lease" because UVM Medical Center is "reasonably certain" to exercise the option. Consistent with the new FASB Rule and guidance, multiple factors inform this conclusion, including a cash flow analysis showing purchasing the property will save $2.3 million over twenty years, and potential plans for other long-term investments in the Tilley Drive area, including development of an outpatient surgery center.

The Board should not sanction UVM Medical Center for making Project planning expenditures without first obtaining a CCON because UVM Medical Center's determination that capital costs would not exceed the jurisdictional threshold was "reasonable based on a totality of the underlying facts and circumstances." *See* Board Rule 4.700(f). Project planners made a good faith and initially accurate calculation that capital costs would be well under $30 million, and planning progressed on that basis. Planners were not aware that capital costs would exceed $30 million until the Project was reevaluated in the fall of 2021, they were advised of the FASB rule change and its implications with respect to the lease option, and UVM Medical Center decided to purchase the 350 Tilley Drive building.

Relief from sanctions is also merited because the Project is fully consistent with all applicable CON criteria, as outlined in UVM Medical Center's CON application. *See* Board Rule 4.700 (c)-(e).

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[7] The guidance states:

> At the commencement date, an entity assesses whether the lessee is reasonably certain to exercise or not to exercise an option by considering all economic factors relevant to that assessment—contract-based, asset-based, market-based, and entity-based factors. An entity's assessment often will require the consideration of a combination of those factors because they are interrelated. Examples of economic factors to consider include, but are not limited to, any of the following: a. Contractual terms and conditions for the optional periods compared with current market rates, such as: 1. The amount of lease payments in any optional period 2. The amount of any variable lease payments or other contingent payments, such as payments under termination penalties and residual value guarantees 3. The terms and conditions of any options that are exercisable after initial optional periods (for example, the terms and conditions of a purchase option that is exercisable at the end of an extension period at a rate that is currently below market rates). b. Significant leasehold improvements that are expected to have significant economic value for the lessee when the option to extend or terminate the lease or to purchase the underlying asset becomes exercisable. c. Costs relating to the termination of the lease and the signing of a new lease, such as negotiation costs, relocation costs, costs of identifying another underlying asset suitable for the lessee's operations, or costs associated with returning the underlying asset in a contractually specified condition or to a contractually specified location. d. The importance of that underlying asset to the lessee's operations, considering, for example, whether the underlying asset is a specialized asset and the location of the underlying asset.

ASC 842-10-55-26.

Thank you for your consideration. Please do not hesitate to contact me if you have questions or need additional information.

Sincerely,

Eric Miller
Senior Vice President and General Counsel
The University of Vermont Health Network

cc. Stephen Leffler, M.D.