

Memorandum to the Commissioner

APPLICANT:

Advocate Healthcare of East Boston
111 Orient Avenue
East Boston, MA 02128

PROJECT NUMBER: DoN 19120215-CL (Significant Change)

Filing DATE: June 9, 2021

Introduction

This memorandum presents, for Commissioner's Review, the Determination of Need (DoN) Program's recommendation pertaining to a request by Advocate Healthcare of East Boston, for a Significant Change to its previously approved DoN. The Amendment is for an incremental increase in the maximum capital expenditure of \$7,408,778 (+73.4%), resulting in an increase of \$74,087.78 in the community health initiatives (CHI) contribution to DoN 19120215-CL. As described further herein, the Applicant seeks approval for the increase in the Maximum Capital Expenditure without a change in scope.

This Amendment request falls within the definition for Significant Change that includes "...Any increase or decrease in the maximum Capital Expenditure over 10% of the inflation adjusted originally approved total expenditure. An increase shall be allowed only for contingencies that could not have been reasonably foreseen, that are not reasonably within the control of the Holder, as determined by the Commissioner, and will be reviewed pursuant to 105 C.M.R. 100.635(A), which requires that the proposed change falls within the scope of the Notice of Determination of Need and is reasonable." The Department has received no public comment on this request for Significant Change.

Background

In April 2020, Advocate Healthcare of East Boston, LLC (Advocate) f/n/a Don Orione Nursing Home, received approval of a Conservation DoN¹ for renovations to restore its 190-bed long term care facility, located at 111 Orient Ave., East Boston. The approved capital expenditure for the project was \$10,087,722. Through this Amendment, the Applicant seeks approval for an increase in the capital expenditure for the Project to \$17,496,500.00 (May 2021 Dollars).

¹ Conservation Project, which means "Construction that consists solely of a project(s) that would Sustain or Restore a Health Care Facility or service for its designated purpose, and to its original functionality, without Modernization, Addition, or Expansion." Pursuant to 105 CMR 100.210(B)(2), Staff reviewed the Application in the context of Factors 3- Compliance, 4- Financial Feasibility, and 6- Community Health initiatives and was delegated by the Department for review and Final Action by the Commissioner.

Because of its age, much of the facility’s infrastructure and systems, and two of the nursing units were approved to be brought into compliance with current healthcare building standards and restored to its original functionality. The Applicant had determined that the entire facility could not be renovated at once and had taken a “targeted approach” that would result in improvements in residents’ overall quality of life and provide material benefits for the Facility. Renovations approved by the Department in April 2020 include replacing “critical systems” that are beyond their useful lives including:

- the 60+ year old boiler
- electrical panels
- fire alarm system
- emergency generator; and
- a majority of the windows.

The April 2020 approval also includes the following components impacting the two nursing units on the first floor:

- Removal of community bathrooms;
- Plumbing replacement, including new toilets, sinks, showers and tubs;
- Addition of new systems, including:
 - HVAC
 - Fire protection
 - Lighting systems
 - Nurse call systems
- Renovations that include
 - asbestos remediation
 - new casework, handrails, flooring
- Removal of cinderblock walls;
- Expansion common nursing space/nursing stations;
- Renovations of the resident common area; and
- Replacement of furniture and fixtures

Proposed Amendment:

The Holder states that it does not seek to materially change the scope or gross square feet of the approved Project but that “The primary basis for this Significant Amendment is the material increase in the cost of the Project.” Staff has reviewed the Amendment request to determine whether it falls within the scope of the original Approval. The Holder reports that following DoN project approval in April 2020 it received Part I DPH Plan Review approval on June 3, 2020, submitted Part II DPH Plan Review on Oct. 23, 2020, and received a response on Dec. 31, 2020. Revised plans were submitted on March 8, 2021 addressing DPH Plan Review concerns. Simultaneous to submission for Plan Approval, the Applicant began seeking financing. All funding options, private or Government sources, included substantial contingencies requiring additional modifications. The Applicant determined the best financing option was through the U.S. Department of Housing and Urban Development (HUD).

As described by the Applicant and summarized by Staff below, the cost increases occurred as a consequence of four significant unforeseen interrelated circumstances, two of which are related to their decision to get U.S. Department of Housing and Urban Development (HUD) funding,

including: 1) the uncovering of additional required work during development of detailed architectural and engineering plans submitted for the Department’s Plan Review process and for contractor bids; 2) the COVID-19 pandemic-related disruptions to the supply chains leading to cost increases; 3) the additional repairs and/or replacements required to secure HUD financing (detailed below); and, 4) the use of the prevailing wage rates, also required to secure HUD financing.

The Holder provided the following explanation of their efforts to secure financing:

“At the time of the filing of the DoN and the development of the Project projections, the Applicant was contemplating using traditional bank financing. After receipt of the DoN, it explored the option of HUD insured financing and it was well underway with the HUD application process, having completed many third-party reviews and reports, when it became apparent that the HUD prevailing wage requirement would have a significant impact on contractor bids. The Applicant then sought financing from local banks and one national bank where it learned that most were just not interested in being involved in lending projects in the long-term care industry at this time and the few that would provide financing, would only do so with significant terms the Applicant found unacceptable. With the lack of other acceptable options, the Applicant continued with the HUD process.”

These four unforeseen circumstances described above lead to additional work that extended the construction timeframe which in turn added further cost increases. The Holder is seeking authorization for these additional requirements and their associated costs as part of this amendment, since the increases are not a change in scope. Staff has described them in detail below.

Impact on Cost

The regulation requires that a Holder submit a description of the proposed change along with associated cost implications. As the chart below shows, with this Proposed Project, the Applicant seeks to increase its capital expenditures by 73.4% which is greater than the minimum threshold for filing an amendment of 10%. This is for the construction, and renovations necessary for the implementation of the originally approved project, and to secure acceptable financing.

The Holder provided the following explanation and citations regarding increases in construction costs.

There are many factors affecting construction costs.² For example, “Steel prices jumped significantly towards the end of 2020 and the beginning of 2021, in some cases as much as 25% to 50% in raw material value.”³ Lumber has increased 112%.⁴ Other factors include

² How U.S. Trade Policy Helped Construction Materials Costs Go Through the Roof by Scott Lincicome posted March 18, 2021 11:11AM. [Article on CATO Institute webpage.](#)

³ Domestic Material Price Trends [Article on Cumming Group webpage.](#)

⁴ Thinking of a new wooden deck for spring? It may bust your budget. Published Wed. Feb. 10, 2021 at 11:50 AM,

suppliers incorrect estimate that demand would decline with Covid-19 limiting production; material increase demand for home improvement, renovations and construction due to more time spent at home increasing the demand; import tariffs and government policies; supply and manufacturing material shortages such as copper and crude oil,⁵ and significant increases in labor costs.

The Holder provided the table below of the increases in costs with the percentage increases by line item below. Staff has summarized each expense category in sequence.

Comparison of Approved and Requested Capital Expenditures⁶

Category of Expense	Approved (April 2020 Dollars)	Request (May 2021 Dollars)	Difference	% Change
Land Costs	\$0	\$0	\$0	\$0
A. Construction Contract	\$8,175,023	\$14,051,044	\$5,876,021	71.9%
B. Fixed Equipment	0	474,276	474,276	100.0%
C. Architectural Cost	663,790	908,500	244,710	36.9%
D. Pre-Filing Planning Costs	145,000	169,000	24,000	16.6%
Post-Filing Planning Costs	40,000	180,000	140,000	350.0%
E. Net Interest Construction	276,695	664,258	387,653	140.1%
Major Movable Equipment	628,909	629,000	91	0%
Total Construction Cost	\$9,929,417	\$17,076,078		
F. Financing Costs	158,305	420,422	262,177	165.6%
TOTAL	\$10,087,722	\$17,496,500	\$7,408,788	73.4%

A. Construction Contract increases were reported by the Holder and are summarized below (items 1-16 below are included in the construction contract). The main reasons for cost increases fall into three categories, 1) more extensive work discovered during investigation required for detailed engineering and construction plans, 2) additional work required as a result of HUD financing (described below, the main HUD related changes include replacement, demolition and removal of boilers, replacement and repairs to electrical panels, façade and stairwell repairs, refurbishment of elevators, labor, additional inspections, and financing costs), and 3) increased cost of supplies and labor.

updated Wed. at 18:28 PM EST by Diana Olick.

[Diana Olick article on CNBC webpage](#)

⁵Why Are Prices Skyrocketing in Wire & Cable Products? Posted Feb. 17, 2021. [_Article on Lapp Tannehill webpage](#)

⁶ The Center for Information and Analysis reviews these in detail when determining the LOCF capital cost adjustments.

1. Mechanical costs were originally estimated at \$979,845. The current projected cost is \$2,617,419, an increase of \$1,638,574. During the investigation required for detailed engineering and construction plans, it was determined that costs would be much higher because certain low ceiling heights required extensive routing of the ductwork (for supply and return air) from the ERUs to the individual rooms, and for the routing of refrigerant piping for heating and air-conditioning from the two new roof-mounted energy recovery heat pumps to the individual rooms.
2. Roofing must now be done in phases to coordinate with mechanical systems installation, which significantly increases the costs. The initial roofing estimate was \$244,778; the current is \$314,220, is an increase of \$69,442.
3. Glass & Glazing- The initial estimate for the replacement windows needed in order to achieve temperature uniformity for resident comfort and energy efficiency was \$995,044. Current estimates are \$1,309,221, an increase of \$314,177. Testing showed that the old window caulking contains asbestos, making the replacement process slower, more complex, and labor intensive. It includes processes to assure safety in staff and resident areas.
4. Drywall- The initial budget was \$414,164. This increased to \$1,126,014, an increase of \$711,850. These cost increases are primarily attributed to an increase in the cost and amount of materials needed for (i) added soffits, drywall and ceilings; (ii) patient room and common area walls; (iii) the extensive fire rated shaft walls required to wrap mechanical systems that extend through the building; and (iv) an increase in labor costs on a multi-phase process which was not fully reflected in the initial cost estimate.
5. Wall Protection/Accessories -The original projected cost for this was \$153,957. The revised estimate is \$346,088, an increase of \$192,131. This work is for the application of protection devices such as corner guards, door kick plates, interior signage, cubicle curtains and tracks; towel racks and toilet paper holders, metal lockers, and window shades. The areas identified where wall protection was required were much greater than originally estimated and also accessory costs have increased materially.
6. Hazardous Material Abatement -The original estimate for asbestos abatement was \$200,844. The current estimates are projected at \$333,153, an increase of \$132,309. The increase in hazardous material abatement costs is associated with additional areas, discovered during inspections, requiring asbestos removal including the flooring and window caulking materials, along with the need for increased testing, monitoring, inspections and air clearance costs not reflected in prior estimates
7. Demolition Costs -The original estimate was \$95,269; and the current is \$288,892. The increase is associated with routing of mechanical duct work and refrigeration piping through concrete block walls; increased plumbing and drainage piping replacements

including cutting of the concrete floor slab at the Garden Level; and demolition and removal of four existing boilers, required by HUD. The Applicants has three active and one inactive boiler. Given their age HUD strongly recommended replacement of the three active ones which the Applicant agreed to and as a result, HUD required their removal despite there being sufficient space for the new unit in the same location. (See also B. *Fixed Equipment Not In Contract*, below) which was not anticipated. As a result, changes were made in the plans for plumbing, electrical, HVAC and other system access throughout building further increasing the demolition required.

8. Plumbing- The initial cost for plumbing was \$768,390; current estimates are \$1,174,841, an increase of \$406,451. The increase is primarily related to the larger amount of existing plumbing and drainage piping throughout the building that requires replacement and or re-routing. As much of the plumbing is hidden behind walls, it was only identified as more extensive engineering evaluations were performed to develop construction level plans.
9. Electrical -The initial cost estimate of this extensive work was \$1,222,961. It is now estimated to be \$1,775,208, which is an increase of \$552,247. It is a result of increases in supply costs, the required addition of a replacement emergency generator, and the increase in repairs and replacements of electrical panels and rewiring identified by HUD and during the development of final construction plans. Replacement of and upgrading electrical systems to current standards was a material component of the capital expenditures for this Project as the wiring and systems in the facility have not been addressed in decades.
10. Contractor's General Requirements -The estimates developed for the DoN included contractor overhead or general requirements of \$104,005. With construction level plans now available, the current estimate is \$181,266, an increase of \$77,261. The increase is a result of the additional necessary work identified, and the required phasing needed which will extend the construction timeline.
11. Contractor's General Conditions Labor Costs -As a consequence of the increase in the scope of work and the subsequent longer construction period. The Contractor's General Conditions Labor Costs increased. Initial Contractor Labor Costs were estimated at \$489,762. The current proposed amount is \$857,924, an increase of \$368,162.
12. Contractor's Fee -The initial estimated Contractor Fee was \$209,898; with the increased length of time for construction and the additional work required, the contractor currently estimates a fee of \$362,695, a \$152,797 increase in the original DoN approved costs.
13. Permits & Fees -The original 2019 estimate of the permits and fees was \$75,966. The latest proposals have increased this to \$142,843, an increase of \$66,877. Local permitting is based on subcontractor trade costs and thus reflect the increases discussed above.
14. Contractor's Insurance -The DoN projected budget allocated \$69,971 for the Contractor's insurance. The current estimate is \$142,902, an increase of \$72,931. This is partially a

result of increased subcontractor trade costs. In addition, experts in the industry are indicating that “due to increasing losses and poor investment returns [by insurance companies], rates for most lines of coverage are increasing, capacity is declining and underwriters are being more selective on which accounts they will even consider.”⁷ This article projected increases in all types of insurance required by the contractor and specifically it projected up to 10% on Builder’s Risk policies in 2021.

15. Payment & Performance Bond –This cost has risen from the prior estimate of \$69,966 to \$119,531, an increase of \$49,565. The underlying reason is that these fees relate to the subcontractor costs, which when the insured amount increased the cost of the policy also does. Additionally this type of insurance is more costly today than in 2019.
16. Owner’s Project Management -When the original DoN estimates were obtained, the Applicant felt that it would be able to manage the Project with existing staff. However, as the Project has become more complex, with multiple phases and events requiring coordination with facility operations, it was determined that a professional project manager (PM) with knowledge of long-term care facility construction was required for managing the design process, obtaining the permits and construction approvals, making required regulatory filings, monitoring contractor performance and expenditures, negotiating and finalizing contracts and assuring compliance with their terms. The PM will also to focus on ensuring minimal impact on the residents and the ongoing operation of the nursing home. The current estimate for these services is \$275,000.
17. Façade Repairs – Initial reviews indicated that while there were some issues with the façade, nothing required immediate attention. However, as more detailed inspections were performed by city inspectional officials and HUD, it was determined that repairs are required including: failed and spalling bricks at various exterior lintel locations at the rear stairwell, treads and building corners. It is also required that replacement bricks needed to be compatible and properly blend with the existing bricks meaning that “off the shelf” brick cannot be used. This work is now necessary due to inspections and HUD related findings, and are general safety requirements. The cost of this work is \$248,082 and was not in the original budget.

B. Fixed Equipment Not in Contract

The HUD physical plant inspection identified repairs and/or replacement and removal to certain fixed equipment amounting to \$474,276 required of the Applicant to qualify for the HUD insured financing. Prior to submitting the DoN Application the Applicant had consulted with the various service vendors and consultants that had indicated that such work might be required in the future, but was not necessary for the Project completion.

⁷ The Insurance Market: What Contractors Can Expect in 2021 by Jeffrey Cavnac published Tuesday, January 5, 2021. [Article on Construction Executive Webpage](#)

First, a complete overhaul of both the passenger and the freight elevator was required as safety and efficiency measures and is projected to be \$174,276.00

Second, as explained above under A7 *Demolition*, the HUD inspection strongly recommended replacement, and then required removal of the three (3) operating boilers that had passed their useful life and showed significant deferred maintenance, raising concerns. It also required removal of a fourth, older inactive boiler and the underground fuel tanks. This resulted in additional Fixed Equipment Costs not included in the Construction Contract of another \$300,000.00.

- C. Architectural Costs increased from \$663,790 to \$908,500 (an increase of \$244,710). They are for the modifications to construction level drawings, and additional design and engineering support required as a result of the extension of the construction period from 52 to 72 weeks, to meet final project requirements described throughout.
- D. Pre and Post Filing Planning and Development Costs are for permits and approvals and many are levied as a percent of the total. Therefore, with the large increase in project costs there was an increase in certain permits or approvals. The Post-Filing costs are projected to increase by \$140,000.00 or 350%.
- E. Net Interest Expense originally was \$276,695, based on a 16-month construction period and a total borrowed amount of \$8,042,000.00. The amount for this amendment is \$563,320, an increase of \$286,625.00. It is based on total borrowing of \$15,450,000 with the construction period now extended as explained herein.
- F. Financing Costs -Originally, the approved cost to secure financing is \$158,305. With the changes in the lender, HUD, and the amount to be borrowed, the cost is now estimated to be \$420,432. It is for the HUD application fees, additional third-party reports and inspections, and a loan placement fee.

Impact on Community Health Initiative Funding

The DoN Regulation states that (c) For a Proposed Project on behalf of a Long-term Care Facility, which is deemed a Conservation Project by the Department, funding shall be 1% of the total Capital Expenditure of the proposed Conservation Project. (105 CMR 100.210(6)).

One percent of the originally approved DoN amount is \$100,877.22. The Holder had opted to make two equal payments of the required CHI contribution. The first was due within 30 days of approval (May 27, 2020) and the second on the first anniversary of DoN approval (April 27, 2021). Following DoN Approval, the first payment of \$50,438.61 was not received.

Since the proposed project entails an incremental increase in the Capital Expenditure of the project, the community health initiatives (CHI) contribution will increase from \$100,877.22 by \$74,087.78 to a total of \$174,965.

As required, within 30 days of approval of this Amendment, the Holder must submit payment for the unpaid amount of \$50,438.61 and the incremental increase of \$37,043.89 for a total of

\$87,482.50. The second payment of \$87,482.50 must be submitted on the Anniversary of the approval of this Amendment.

Staff Summary and Findings

Staff reviewed the 2020 Staff Report and Decision Letter of Approval to determine whether the request falls within the scope of that Approval. Staff determined that there are no additional gross square feet, service or programmatic changes that would change the scope of the project. Staff also finds that the proposed changes could not have been reasonably foreseen given the well documented impact of the COVID-19 pandemic on the health care industry and also on the costs of materials and labor in the construction industry, as well as the need to secure HUD funding, or the subsequent increase in scope required by HUD. Therefore Staff finds that the Holders changes to the Approved DoN fall within the scope of an Amendment and Staff recommends approval of this request.

Based upon the information submitted, with additional staff analysis the Department can find that the “the proposed change or modification falls within the scope of the Notice of Determination of Need as previously approved by the Department, and ... is reasonable” 105 C.M.R. 100.635(A) which are requirements for approval of an Amendment.

The total approved capital expenditure is increased to \$17,496,500.00 (May 2021 Dollars) and the total approved CHI is \$174,965.

Other Conditions to the DoN

1. To reflect the amended MCE increase, the total CHI contribution will be \$174,965 paid in two equal payments of \$87,482.50 with the first payment due at the time of receipt of a duly-approved Notice of Determination of Need (or upon receipt of a payment letter from DPH), and the second, on the first anniversary of the Notice.

Within thirty (30) days from the date of this Notice of Approval of approval of this Amendment, to comply with the obligation to contribute to the Massachusetts Healthy Aging Fund, the Holder must submit a check for \$87,482.50 to Health Resources in Action, the fiscal agent for the Massachusetts Healthy Aging Fund. The Holder must promptly notify DPH (CHI contact staff) when the payment has been made.

Payment should be sent to:
Health Resources in Action, Inc., (HRiA)
2 Boylston Street, 4th Floor
Boston, MA 02116
Attn: Ms. Bora Toro