

IN THE SUPERIOR COURT FOR THE STATE OF ALASKA

THIRD JUDICIAL DISTRICT AT ANCHORAGE

SOUTH ANCHORAGE AMBULATORY )  
SURGERY CENTER, )  
 )  
Appellant, )  
 )  
STATE OF ALASKA, DEPARTMENT OF )  
HEALTH AND SOCIAL SERVICES, )  
 )  
Appellee. )  
\_\_\_\_\_ )

Case No. 3AN-07-10738 CI  
OAH No. 06-0152-DHS

**Decision on Appeal**

A certificate of need is required to spend more than a million dollars on construction of a health care facility,<sup>1</sup> and the Department of Health and Social Services is charged with evaluating whether a proposed expenditure is needed to maintain good health for Alaskans.<sup>2</sup> A joint venture of medical care providers sought a CON to build a new surgery center in Anchorage, and an administrative law judge found that the quality of medical care could suffer if the application were denied.<sup>3</sup> The Commissioner, however, concluded that the regulations<sup>4</sup> did not allow for use of the trend analysis relied upon by the ALJ, and so denied the application.<sup>5</sup> The joint venture appealed,<sup>6</sup> and the parties argued their positions two weeks ago.<sup>7</sup>

<sup>1</sup> AS 18.07.031. (An automatic increase of \$50,000 per year in the triggering amount began 7/1/05.)

<sup>2</sup> AS 18.07.041.

<sup>3</sup> Decision and Order, 5/24/07; R. 189-208.

<sup>4</sup> See 7 AAC 07.025.

<sup>5</sup> Decision and Order, 7/5/07; R. 45-48.

## Decision of the Administrative Law Judge.

These proceedings began with a letter of intent written in late 2004; the JV hoped to be operational with four new operating rooms by 2006.<sup>8</sup> After some delay,<sup>9</sup> the Commissioner denied the application,<sup>10</sup> and a hearing was requested.<sup>11</sup> Commission staff examined the need-related data under both the standard criteria and using “trend analysis,”<sup>12</sup> and the distinction between the two is at the heart of this appeal.

Under the standard methodology, the need for additional surgery suites

is calculated using prescribed formulas in which projected population and general surgery use rates are the variables that dictate whether anticipated demand for surgery services might outpace supply. The general surgery use rate is an average from the three preceding years and remains static throughout the projection. Projected future growth in surgery demand is solely a function of growth in overall population. The standard methodology, therefore, does not take into account whether other factors, such as an aging population or changed approaches to medical care, cause the three year average to underestimate likely future rate of usage for surgery services.<sup>13</sup>

The parties agree that use of this methodology showed a surplus rather than a deficit of operating suites, while the trend analysis showed a need for 3½ suites by 2011.<sup>14</sup> Chief ALJ Thurbon concluded, however, that trend analysis “is a more

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<sup>6</sup> Brief of Appellant [At. br.] filed 1/30/08, Brief of Appellee [Ae. br.] filed 4/1/08, and Reply filed 4/21/08.

<sup>7</sup> Media 3DIA08-93, 2:27-3:27 (6/20/08).

<sup>8</sup> R. 1229.

<sup>9</sup> See At. br. at 6-8.

<sup>10</sup> R. 1150.

<sup>11</sup> R. 1149; 7 AAC 07.080.

<sup>12</sup> R. 191.

<sup>13</sup> R. 191-92 (internal footnotes omitted); see At. br. at 10-11.

<sup>14</sup> R. 193, 196.

reliable predictor of future need than the standard methodology.”<sup>15</sup> The information was developed during the agency appeal process, which Chief Judge Thurbon described as a means “to allow the executive branch decisionmaker an opportunity to correct errors” at the agency level, with “errors” defined loosely to mean anything that gets in the way of reaching the correct result.<sup>16</sup> Accordingly, the evidence on trend analysis was evaluated to see if “the availability, quality, or accessibility of existing healthcare services creates an unreasonable barrier to services.”<sup>17</sup> The ALJ concluded that there were several such barriers:

- Scheduling for routine procedures can be difficult because block time is in short supply and reliance on hospital suites increases the likelihood of routine procedures being postponed to accommodate emergencies.

- Procedures take longer than necessary, in part because of the time spent changing equipment and surgical teams, and because non-specialized support personnel are less efficient.

- Procedures that do not require a hospital must still be performed there.

- The risk of infection may be greater in a hospital setting and increases if a wound must be left open due to a delay in surgery.

- Exposure to unnecessarily high levels of general anesthesia occurs more often in hospitals than ambulatory surgery centers, where specialists rely more heavily on regional blocks.

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<sup>15</sup> R. 196.

<sup>16</sup> R. 200-202.

<sup>17</sup> *Id.*, citing 7 AAC 07.025(b).



•Operating at 90% of capacity in a hospital setting is taxing and operating above 85% can be a problem. Providence Alaska Medical Center's general surgery suites now operates at 98% of capacity.<sup>18</sup>

Chief ALJ Thurbon found that "Collectively, these facts show that more likely than not some patients' medical care is being adversely affected by current limitations on surgery suites available for non-hospital outpatient procedures."<sup>19</sup> She therefore concluded that the JV had shown that barriers existed to receiving a desirable quality of health care, that the barriers were unreasonable, and that application of trend analysis justified making an exception to the standard methodology.<sup>20</sup> The trend analysis demonstrated that the rate of surgical procedures has been increasing and is likely to continue to do so, and, as noted earlier, Judge Thurbon concluded that the linear regression analysis was a more reliable predictor of future need than the standard methodology.<sup>21</sup> Also noted were potential problems in using a dedicated endoscopy suite for general surgery,<sup>22</sup> scheduling difficulties and a perception that patients simply do better in an outpatient surgery center than in a hospital.<sup>23</sup>

#### **The Commissioner's decision.**

Commissioner Jackson began by stating that "(1) the findings and conclusions in the May 24, 2007 decision and order are hereby adopted, except as

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<sup>18</sup> R. 205, citing the record in internal footnotes 81-88.

<sup>19</sup> R. 206.

<sup>20</sup> *Id.*

<sup>21</sup> R. 196.

<sup>22</sup> See At. br. at 11-12 for record citations.

<sup>23</sup> R. 196-97. See also At. br. at 17-19 (discussing qualitative advantages of proposed suites).

provided in (2) and (3) below.”<sup>24</sup> Neither of the conclusions which followed disputed the ALJ’s findings, but part (2) rejected the conclusion “that an exception can be allowed under 7 AAC 07.025 to use of the standard methodology for calculating need for general surgery services.”<sup>25</sup> The Commissioner determined that the department did not intend to allow exceptions to the methodologies, but only the standards, even though the language, read literally, might suggest otherwise.<sup>26</sup> She acknowledged that, “Over time, more methodologies might be authorized,” but at present there was only the one.<sup>27</sup>

The Commissioner did not address Chief Judge Thurbon’s reasoning that a methodology is an inseparable part of the standard itself.<sup>28</sup> The regulation incorporates by reference a 40 page document titled *Alaska Certificate of Need Review Standards and Methodologies*, dated December 9, 2005,<sup>29</sup> which does distinguish between the two terms.<sup>30</sup> The general standard is set forth on page 2, and speaks to whether the applicant has documented the need for the project, coordination with other stakeholders, anticipated impact, accessibility and the like,<sup>31</sup> while the review methodology is specific for each type of medical care being evaluated. And indeed the methodology for surgical care employs the

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<sup>24</sup> R. 51.

<sup>25</sup> *Id.*

<sup>26</sup> R. 52.

<sup>27</sup> R. 52-53.

<sup>28</sup> R. 203. *See also* Reply at 13-14.

<sup>29</sup> *See* R. 348 and <http://www.hss.state.ak.us/publicnotice/PDF/133.pdf>.

<sup>30</sup> *Id.* at 1, 3.

<sup>31</sup> *Id.* at 2.

formula recited by the parties in their briefing,<sup>32</sup> and described by the ALJ<sup>33</sup> as inferior to trend analysis in meeting the statutory goal.

#### **Standard of review.**

There are four different standards of review:

(1) the “substantial evidence” test applies to questions of fact; (2) the “reasonable basis” test applies to questions of law involving agency expertise; (3) the “substitution of judgment” test applies to questions of law where no expertise is involved; and (4) the “reasonable and not arbitrary” test applies to questions of about agency regulations and the agency’s interpretation of those regulations.<sup>34</sup>

The State emphasizes the second of these,<sup>35</sup> and indeed there certainly would appear to be agency expertise involved in the lengthy and complicated regulation at issue. But the real question may be whether the regulation as interpreted by the State is consistent with and reasonably necessary to implement the statutes under which it is authorized.<sup>36</sup> As the Alaska Court of Appeals put it (in a different context),

To the extent that a regulation is inconsistent with statutory law, the executive branch agency that promulgated the regulation has exceeded the rule-making power delegated by the legislature. Thus “when a regulation conflicts with a statute, it is the regulation which must yield.”<sup>37</sup>

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<sup>32</sup> *Id* at 30-31; At. br. at 10-11, Ae. br. at 5-6.

<sup>33</sup> See text accompanying note 13, *supra*.

<sup>34</sup> *Lakloey, Inc. v. University of Alaska*, 157 P.3d 1041, 1045 (Alaska 2007).

<sup>35</sup> Ae. br. at 16, citing *Rose v. Commercial Fisheries Entry Commission*, 647 P.2d 154, 161 (Alaska 1982), *Lauth v. State*, 12 P.3d 181, 184 (Alaska 2000), and *State v. Greenpeace*, 96 P.3d 1056, 1061 (Alaska 2004).

<sup>36</sup> *Wilber v. State, Commercial Fisheries Entry Commission*, \_\_ P.3d \_\_, 2008 WL 2551082 (Alaska 6/27/08), citing *Grunert v. State*, 109 P.3d 924, 929 (Alaska 2005). See also AS 44.62.030.

<sup>37</sup> *Frank v. State*, 97 P.3d 86, 91 (Alaska App. 2004), quoting *Gudmundson v. State*, 763 P.2d 1360, 1363 (Alaska App. 1988)(other footnotes omitted).



Although agency expertise is implicated in the regulation, there are parallels between the issue posed in this case and that presented in *O'Callaghan v. Rue*.<sup>38</sup> As in that case, the issue of whether the regulation is consistent with the law is one of statutory construction, which a court may decide using independent judgment, while whether the regulation is necessary to implement it involves fundamental policy determinations, which are reviewed on a rational basis standard.<sup>39</sup> The “reasonable not arbitrary” review is also deferential.

**Is 7 AAC 07.025 as applied by the Commissioner consistent with the statute?**

There is no dispute about the agency’s authority to promulgate the regulation;<sup>40</sup> the question is whether it is consistent with the legislative directive, when construed to exclude application of trend analysis as it has been in this case. And of course we reach this issue only if the regulation is interpreted in the manner that Commissioner Jackson did, which is in conflict with the decision of Chief Judge Thurbon. It makes sense to begin with what the evidence revealed about application of the standard methodology.

The JV emphasizes that the uncontested facts show a need for more surgery suites,<sup>41</sup> while the result produced by the standard method is that there are 7½ too many already.<sup>42</sup> The witnesses agreed that Alaska, like the rest of the country, was getting older, and that this, and a new approach to certain medical problems, were

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<sup>38</sup> 996 P.2d 88, 94 (Alaska 2000).

<sup>39</sup> *Id.* at 94-95.

<sup>40</sup> See Ae. br at 18, Reply at 5.

<sup>41</sup> See also R. 689 (21 needed by 2011).

<sup>42</sup> R. 193; Ae. br. at 9.

resulting in much more use of day surgery that can be done in an ambulatory center.<sup>43</sup> Appellant argues that the result of the standard method is flawed because you can't use an average rate of surgery when it is apparent that the rate is accelerating rapidly,<sup>44</sup> and it notes that the Department's own expert agreed that the alternative methodology was superior for this reason.<sup>45</sup> The JV's expert, Professor Goldsmith, was, naturally enough, even more definite, calling use of the standard method a mistake, inappropriate and misleading.<sup>46</sup> And, as noted, Chief Judge Thurbon found this evidence compelling.<sup>47</sup>

The Department defends the standard methodology in several ways. First of all, it was developed by a task force charged with increasing efficiency and objectivity in the CON process, putting everyone on the same footing.<sup>48</sup> Secondly, the Department viewed the increase in the surgery rate as resulting from its own previous allowance of CONs—if you build it they will come.<sup>49</sup> Third, the methodology seemed to work in a recent Fairbanks application.<sup>50</sup> It perceives the issue as simply “whether the regulation can be excepted or waived...a legal question to which much of the testimony is not relevant. The court should not be enticed by the JV's statements and inferences in looking at these simple and

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<sup>43</sup> See At br. at 20-22 (quoting testimony).

<sup>44</sup> See example in At. br. at 13.

<sup>45</sup> Tr. 213-14, 267-71; see R. 637, 688-89.

<sup>46</sup> Tr. 300-302.

<sup>47</sup> R. 196-97.

<sup>48</sup> Ae. br. at 3-4.

<sup>49</sup> Ae. br. at 13-14.

<sup>50</sup> *Id.*



straightforward legal issues.”<sup>51</sup> And, it points out, a properly adopted regulation is presumed to be valid.<sup>52</sup>

But although the Department eventually gets around to stating the issue directly,<sup>53</sup> it never responds to the Joint Venture’s argument that the standard methodology is fatally flawed, calling its position “sour grapes,” and an end-around that would cause the process to lose neutrality and predictability.<sup>54</sup> It then concludes that the regulation is valid and moves on to the issue that it believes this appeal “begins and ends with”—is the standard methodology subject to an exception or waiver. If no, end of story and decision below affirmed.<sup>55</sup> It took the same approach at oral argument.

But while I find the two views of the regulatory language intriguing, I disagree that this is the key issue raised in this appeal. That issue is instead whether the regulation, read as the Commissioner did, is consistent with the statute. And the State has at no time explained how a method that fails to take into account an increasing rate of surgical procedures satisfies a statute that commands issuance of a CON “if the availability or quality of existing...resources is less than the current or projected requirement...to maintain the good health” of Alaskans.<sup>56</sup> While consistency and objectivity are laudable goals for an administrative agency,

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<sup>51</sup> *Id.* See also Ae. br. at 16.

<sup>52</sup> Ae. br. at 17, citing *Interior Alaska Airboat Ass’n v. State Board of Game*, 18 P.3d 686, 689 (Alaska 2001).

<sup>53</sup> Ae. br. at 19.

<sup>54</sup> Ae. br. at 21.

<sup>55</sup> Ae. br. at 22.

<sup>56</sup> AS 18.07.041.

the main idea is to serve the statute, to get the job done. The mathematical argument here is not complex, and if the regulation needs to be rewritten to meet conditions on the ground, then this will have to be done. Having adopted all of the findings made by the ALJ,<sup>57</sup> the Department cannot defend its regulation without showing that it yields a result that is consistent with the law as written by the legislature. It has not even attempted to do that in this case.

The Department is entitled to deference on the interpretation of its regulation, and it has determined that what appears to be a relief valve in 7 AAC 07.025(b) is unavailing to the JV. But in closing this door, it has left itself open to the argument that the regulation is not consistent with the statute. The goal is to predict health care needs,<sup>58</sup> and the regulation as construed fails to do this under the facts of this case. Based on the uncontested evidence accepted by the Commission, the JV is entitled to a certificate of need.

### **Conclusion.**

The parties also litigated the question of whether, if the JV prevailed, it could “shell in” another two suites for possible use later.<sup>59</sup> It appears that this matter was settled at oral argument. The JV recognizes that a CON is required to construct surgery suites,<sup>60</sup> and that it cannot be heard to argue estoppel or waiver of some sort if it builds space ultimately rejected in a future application. It further recognizes that it can’t argue that if the additional cost to convert the space to an

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<sup>57</sup> R. 51, Ae. br. at 11.

<sup>58</sup> Ae. br. at 20.

<sup>59</sup> At. br. at 40-42, Ae. br. at 30-33, Reply at 18-20.

<sup>60</sup> R. 208.

operating room is less than the \$1.2 million, or whatever threshold is applicable at the time, that it would not require a CON to add two more suites. With the agreement that it will have to re-apply should it seek to convert the space, it appears that the parties no longer have any dispute in this regard.

The Commissioner's decision is reversed and remanded with instructions to grant the certificate of need.

Dated: 7/2/08

Fred Torrisi  
Fred Torrisi, Judge



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