



December 22, 2018

**UPDATE TO THE SEPTEMBER 1, 2018 LEGISLATIVE REPORT
Under HB 4038 (2018)**

**Report on the Progress of Establishing the Roseburg Oregon Veterans' Home
(Update on Increased Construction Costs)**

Background

House Bill 4038 (2018) directed the Director of the Oregon Department of Veterans' Affairs (ODVA) to “study the progress of the establishment of the Roseburg Oregon Veterans’ Home authorized under ORS 408.385 and shall report the findings of the study to the Legislative Assembly no later than September 1, 2018.”

On September 1, 2018, ODVA submitted the “Report on the Progress of Establishing the Roseburg Oregon Veterans’ Home” (Report) to the Oregon legislative Assembly. The Report is attached as Attachment A and may also be found here: <https://www.oregon.gov/odva/Connect/Pages/Reports.aspx>.

In the Report, ODVA made a recommendation to the Legislative Assembly that the Roseburg Oregon Veterans’ Home be built on the grounds of the Roseburg campus of the Roseburg Veterans Affairs Health Care System. The United States Department of Veterans Affairs (USDVA) has agreed to transfer more than 13 acres on the campus to the State of Oregon for the purpose of siting the new Veterans’ Home, a skilled nursing facility, which would be adjacent to the new main hospital the USDVA is building on the campus.

Purpose of the Update: Increased Construction Costs

The purpose of this update is to provide new information on the potential costs of the Roseburg Oregon Veterans’ Home (Roseburg Home). As stated in the September 1, 2018 Report, The Roseburg Home would be based on the Edward C. Allworth Veterans’ Home, located in Lebanon (Lebanon Home), which is a state-of-the-art skilled nursing facility that is organized around the idea of an intentional community or neighborhood.

The very rough cost estimates in the September 1, 2018 Report were based in part on the initial grant application ODVA submitted to the USDVA for a State Home Construction Grant in 2012 to build a third veterans’ home and in part on the costs of the Lebanon Home that was completed in 2014.

Since the September 1, 2018 report, ODVA has been able to refine and more accurately estimate the future hard and soft construction costs that include cost escalations; more expensive and restrictive USDVA design requirements and state building requirements; and an additional three years of projected future cost escalation. Note that the project will take roughly four years to complete all aspects of financing, grant application and approval, and construction.

The September 1, 2018 Report estimated the costs as follows:

Oregon Department of Veterans' Affairs has done a very rough estimate of the costs of a Roseburg Veterans Home based on the costs of the Lebanon Home. It is important to note that the \$40 million for the Lebanon Home was based on costs of construction in 2012 for a 154 bed skilled nursing facility.

Assuming \$40 million in total costs for a skilled nursing facility in Roseburg based on the Lebanon Home model:

- *To build a \$40 million skilled nursing facility with construction beginning in 2018, the project would need to be scaled back to 126 beds. (A 150 bed facility would be roughly \$45 million)*
- *Based on current trends in costs of construction, for each year of delay in construction after 2016, the construction escalation costs will be 6 percent per year.*

The Federal VA will donate the land, parking lots, and some of the infrastructure costs (utilities). Therefore, the ODVA will need to pay additional costs that are unknown at this time.

As stated, the U.S. Department of Veterans Affairs will only provide 65 percent of the costs of construction and the state will need to match with 35 percent of the costs through state, local and county funding. Assuming \$40 million for the total costs:

- *USDVA would provide approximately \$26 million (65%)*
- *The state and local partners need to provide \$14 million: \$10.5 million in approved capital construction bonds, leaving an additional \$3.5 million needed in additional funds (35%)*

This update will describe the rationale and analytics driving the increased construction costs.

Roseburg Home Construction Cost Update

History

In 2012, ODVA submitted a grant application to the USDVA for a State Home Construction Grant to build a third Oregon veterans' home. The State Home Grant Program is a partnership between the USDVA and the States to construct skilled nursing facilities and for renovations to existing homes. USDVA may participate in up to 65 percent of the cost of construction; the remaining 35 percent of constructions costs are provided by state and local funds and must be in place before consideration of a grant application. Grant funds may be used only for construction costs; they may not be used for land acquisition.

In 2012, total project costs were estimated to be between \$37 and \$40 million, with the expected Federal grant request projected to be \$24 to 26 million, representing 65% of the project cost. The remaining 35% of the costs, estimated to be between \$13 and \$14 million, was expected to come from either state or local match funding. (See ODVA letter to Emergency Board, requesting approval to submit USDVA grant application)

At that time, estimates for the size of the facility (154 beds), layout and cost (\$37 to \$40 million) were based on rough costs estimates to the planned Lebanon Home, which was not yet under construction.

The Legislature also authorized \$10.5 million in bonding authority to be used to partially meet the required state/local matching funds for the Roseburg Home. The amount of state/local matching funds was intended to mirror the original local match amount provided by Linn County and Lebanon for the Lebanon Home, which was \$10.5 million.

To date, the bonds have not been issued because the status of the Roseburg Home has not been finalized.

Impact of Construction Cost Escalation to Overall Costs of the Roseburg Home

In 2012, the initial estimated total cost of the Roseburg Veterans' Home was approximately \$37 million; including \$29 million in hard costs (actual construction costs) and \$8 million in soft costs (architectural, engineering, equipment, etc.). The current proposed project timeline estimates construction of the Roseburg home to begin in 2021 to 2022.

The impact of six years of cost escalation (from 2012 to 2018), more expensive and restrictive USDVA design requirements and state building requirements, and an additional three years of projected future cost escalation (2018 to 2021) will likely increase hard costs from \$29 million to \$38 million. **Total project costs, including hard and soft costs, will likely increase the original cost estimates from \$37 million to \$48 million.**

To mitigate some of the costs, the total proposed number of beds for the Roseburg Home was reduced from 154 beds to 126 beds. This reduction of 28 beds lowered the overall cost; however, the need for a storage building and activity rooms at each neighborhood eliminated any cost savings that would be realized from a reduced bed count.

In addition, ODVA applied lessons learned from the Lebanon Home construction to this project. These lessons included the need for additional square footage to some of the ancillary spaces in each neighborhood and in the community center, and a covered portico for the front entrance.

Rationale and Analytics Used to Estimate Future Cost Escalation

- Long term construction cost inflation is normally about double consumer price inflation (CPI). Since 2000, taking out the two worst years of recession (-8% to -10% total for 2009-2010), the 20-year average inflation is 4.2%.

- In times of rapid construction spending growth, construction inflation averages about 8%. Nonresidential building inflation has averaged 3.7% since the recession bottom in 2011; and it has averaged 4.2% for the last four years. Although inflation is affected by labor and material costs, a large part of the change in inflation is due to change in contractors/suppliers margins. When construction volume increases rapidly, margins increase rapidly. Construction inflation can be very different from one major sector to the other and can vary from one market to another. It can even vary considerably from one material to another.
- Construction analytics from respected industry estimating groups, forecast nonresidential building spending in 2018 will reach the fastest rate of growth in three years, which historically leads to accelerated construction cost inflation. Anticipated construction inflation for nonresidential building for 2018 and 2019 will be between 4.5% to 5.5%, rather than the long term average of 3.5% to 4.0%. This trend in cost escalation is projected to continue for the next 4 to 5 years.

Impact of Cost Increases to the ODVA Grant Application Submitted to the USDVA

As stated, ODVA submitted a grant application to the USDVA for a State Home Construction Grant in 2012 to build the Roseburg Home. The application was based on the best cost estimates at that time.

The Code of Federal Regulation (CFR) Title 38 Part 59, which governs veteran home construction, only allows a 10% increase in construction costs for a project. Based on the significant increases in costs, the USDVA central office advised ODVA that the best course of action would be to resubmit all documents for the Roseburg Home. ODVA is currently assembling the required documents for that resubmission.

Summary of Cost Estimates for a Veterans Home in Roseburg as of December 22, 2018

Project:

- 126 bed skilled nursing facility in Roseburg, Oregon
- Veterans Home based on the Lebanon Home model
- The Federal VA will donate the land, parking lots, and some of the infrastructure costs (utilities). (May be additional unknown infrastructure costs)

Costs:

- Hard and soft construction costs \$48.0 million
- USDVA Construction Grant 65% \$31.2 million
- State and local match to cover 35% \$16.8 million
 - State capitol construction bonds \$10.5 million
 - Additional funds required \$ 6.3 million
\$16.8 million