



**EMANUEL
MEDICAL CENTER**

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November 17, 2017

Sent by Electronic Mail wendi.horwitz@doj.ca.gov and FedEx

Wendi A. Horwitz
Deputy Attorney General
State of California Department of Justice
Office of the Attorney General
300 South Spring Street, Suite 1702
Los Angeles, California 90013

Dear Ms. Horwitz:

This letter serves as a request by Doctors Medical Center of Modesto, Inc., doing business as Emanuel Medical Center ("EMC" or the "Hospital"), pursuant to California Code of Regulations, title 11 ("Regulations"), section 999.5, subdivision (h), to modify Condition VII set forth in the "Conditions to the Proposed Sale of Emanuel Medical Center and Approval of the Asset Purchase Agreement by and between Emanuel Medical Center, Inc. and Doctors Medical Center of Modesto, Inc." issued by your office on January 10, 2014 (the "Attorney General Consent Letter"). Pursuant to Regulations section 999.5, subdivision (h) (2), a "request for an amendment shall include a description of each proposed amendment, a description of the change in circumstance requiring each such amendment, a description of how each such amendment is consistent with the Attorney General's consent or conditional consent to the transaction, and a description of the efforts of the entity making the request to avoid the need for amendment." We address such requirements in this letter below.

I. Summary

In connection with EMC's acquisition of Emanuel Medical Center in 2014, your office approved the transaction subject to the conditions described in the Attorney General Consent Letter. Condition VII of the Attorney General Consent Letter ("Condition VII") requires that the Hospital provide Charity Care (as defined in the Attorney General Consent Letter) of at least \$3,212,054 annually (which amount is prorated for any partial years, and which amount has an annual CPI adjustment) for six fiscal years following the closing of the transaction. That dollar amount was determined using the five-year average of the Hospital's cost of charity care for fiscal years 2008 through 2012, which methodology was recommended by Medical Development Specialists, LLC (now Vizient, Inc.) ("Vizient") in its healthcare impact report for the transaction dated May 20, 2013 (the "2013 Vizient Report") issued to your office. As described below in this letter, the implementation of the Patient Protection and Affordable Care Act (the "ACA") has resulted in a dramatic increase in the Hospital's charity care patients who have become eligible for Medi-Cal or other coverage.

Emanuel
Cancer Center

Emanuel
Family Practice

Emanuel
Rehabilitation Center

Emanuel
Specialty Care

Ruby E. Bergman
Women's Diagnostic
Center

Stanford Emanuel
Radiation Oncology
Center

Despite the Hospital's good faith efforts to comply with Condition VII, and by virtue of the intended, but unknown consequences of the ACA (such consequences being unknown at the time of the 2013 Vizient Report), the Hospital has experienced a corresponding, dramatic reduction in the number of patients who qualify as charity care patients, resulting in a decline of the need for charity care in our community, and the Hospital being unable to provide charity care anywhere near the amount required by Condition VII.

As a result, we are submitting this request that Condition VII be modified to adopt a methodology for the recalculation of the Minimum Charity Care Amount (as defined below) for the fiscal year ending December 31, 2016 to reflect the charity care needs of the local community served by EMC based on available data for the hospitals serving the local community for fiscal years ended 2013 through 2016. This methodology would provide a more accurate representation of our community's need for charity healthcare while preserving the State of California's interest in maintaining a commensurate level of charity care to the local community served by EMC. The details of our modification request are set forth below in this letter.

II. Transaction Background

As you know, EMC acquired substantially all of the assets comprising the Hospital pursuant to an Asset Purchase Agreement dated as of February 20, 2013, as amended, by and between Emanuel Medical Center, Inc., a California nonprofit religious corporation, and Doctors Medical Center of Modesto, Inc., a California corporation (the "APA"). The transaction contemplated by the APA was consummated by the parties thereto on July 31, 2014 ("the "Closing"), effective as of August 1, 2014.

Condition VII requires, for six fiscal years from the Closing (that is, until July 31, 2020), that EMC provide an annual amount of Charity Care (as defined in the Attorney General Consent Letter) at the Hospital equal to or greater than \$3,212,054 (defined in Condition VII as the "Minimum Charity Care Amount" and which amount has an annual CPI adjustment). For this purpose, "charity care" means the amount of charity care costs (not charges) incurred by EMC in connection with the operation and provision of services at the Hospital. The definition and methodology for calculating "charity care" and the methodology for calculating "costs" shall be the same as that used by the California Office of Statewide Health Planning and Development ("OSHPD") for annual hospital reporting purposes.

III. Changes in the Healthcare Marketplace

As you are well aware, most hospitals and the communities that they serve have been positively impacted by the ACA. At its core, the ACA was intended to drive a massive and dynamic series of healthcare reforms, including enhanced quality and a better healthcare delivery system. Broader coverage via Medicaid and state/federal exchanges have facilitated improved access to quality medical care (including primary care and a medical home) and concurrent improvements in the overall health for tens of millions of previously uninsured people. The hospital industry has fully supported and implemented various reforms under the ACA based upon these fundamentals and long-term improvements in healthcare delivery and population health.

Moreover, hospitals also supported over \$300 billion in future reductions across a range of programmatic and payment system changes, including with respect to hospital readmissions, hospital-acquired conditions and payments based upon performance for outcomes and quality measures. With California opting fully for Medi-Cal expansion, the ACA’s broad scope and effect has been more evident here (as compared to other states which did not opt for Medicaid expansion) and while some trends may have been anticipated, the degree to which those trends would impact hospitals and other stakeholders was unknown at the time of the Closing.

Through programs like Medi-Cal expansion and Covered California, more people have access to quality healthcare than ever before. In 2016, California’s uninsured rate reached a historic low of 7.1% according to estimates from the National Health Interview Survey (compared to a California uninsured rate of 17% in 2013). California’s Central Valley hospitals have experienced significant expansion in coverage and dramatic decreases in the level of charity care provided.

This decrease has been further accelerated as more patients have become educated about the opportunities afforded by the ACA. For instance, consistent with the goals of the ACA, the Hospital has continued to play an active role in educating the public about such opportunities afforded by the ACA, enrolling patients in available coverage, and working with community organizations. In fact, the Hospital has five full-time-equivalent eligibility counselors who assist patients in determining what type of program the patients may be eligible for, including ensuring that those patients who can be enrolled in Medi-Cal are enrolled in Medi-Cal.

IV. Emanuel Medical Center’s Situation

At Emanuel Medical Center, we have experienced the same dramatic shift in charity care and Medi-Cal: that is, a large decline in our charity care, with a corresponding increase in our Medi-Cal population. The data in the table below compares the Hospital’s charity care costs prior to the implementation of the ACA (*i.e.*, 2013) to 2014, 2015 and 2016. As shown, the Hospital experienced the sharpest decrease in the level of charity care costs in 2014 (*i.e.*, the first year post-ACA) and a continued decrease through 2016 (the “2016 Period”).

<u>Emanuel Medical Center</u>	<u>2013</u>	<u>2014</u>	<u>2015</u>	<u>2016</u>
Charity Write-Offs	\$63,376,160	\$24,260,513	\$15,157,469	\$12,106,611
Cost/Charge Ratio	15.77%	15.79%	13.40%	11.71%
Cost of Charity Care	\$9,994,420	\$3,831,924	\$2,031,101	\$1,417,684

This decrease in charity care costs is attributable to a correspondingly drastic increase in Medi-Cal coverage for our patient population. In fact, Vizient acknowledges in its November 17, 2016 report to your office that the expansion of Medi-Cal and increased enrollment in health insurance coverage has resulted in a significant increase in the number of Medi-Cal patients utilizing services at EMC since FY 2013 (*i.e.*, pre-ACA), resulting in the decreased number of charity care patients served by EMC and a correspondingly sharp decline in charity care costs.

The tectonic shift in how patients are classified, resulting from the intended, but unknown consequences of the implementation of the ACA, has made it impossible for the Hospital to deliver the same amount of charity care as currently defined by Condition VII. Nevertheless, the Hospital continues to care for all patients that choose the Hospital for their healthcare needs – it is just that they are being classified differently.

Further, since the Closing, the Hospital has continued to have in place the same charity care policy that was in place at the Hospital immediately prior to the Closing. The Hospital has also continued to devote resources towards ensuring that the community served by the Hospital is aware of the Hospital’s charity care policy. This has included having the Hospital’s five full-time-equivalent eligibility counselors (as described above) assist patients in determining whether they are eligible for charity care, and making available on the Hospital’s website information concerning its charity care policy.

V. Requested Amendment to Condition VII

In the spirit of our continued commitment to serving all patients, including low-income and indigent, the uninsured and the underinsured, and recognizing the dramatic impact that Medi-Cal expansion has had in accordance with the ACA as described above in this letter, we are requesting that Condition VII be modified to adopt an alternative methodology for calculating the Minimum Charity Care Amount. The current Minimum Charity Care Amount has been calculated utilizing the five-year average of the Hospital’s cost of charity care for fiscal years 2008 through 2012, as recommended in the 2013 Vizient Report. Insofar as a significant number of patients who would otherwise have been classified as charity care patients pre-ACA are now covered by Medi-Cal or other coverage, we propose the methodology for calculating the Minimum Charity Care Amount be modified in the following manner (the “Proposed Methodology”):

1. Using Hospital Annual Financial Disclosure reports from OSHPD for fiscal years ended 2013 through 2016 (the latest information available), calculate the charity care costs for each fiscal year for all hospitals within the community served by EMC. Costs are determined by multiplying a hospital’s charity care write-offs by the hospital’s cost-to-charge ratio.
2. Document the percentage change from 2013 to 2016 for these hospitals in the community served by EMC and apply the percentage change to the Minimum Charity Care Amount to compute a community-wide reduction amount.
3. Deduct the reduction amount from EMC’s Minimum Charity Care Amount to determine a modified Minimum Charity Care Amount.
4. For ease of reference, the calculation described above is also depicted as follows:

Minimum Charity Care Amount (a)	Community-based Reduction Percentage	Reduction Amount (a * b = c)	Modified Minimum Charity Care Amount (a + c)
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5. The modified Minimum Charity Care Amount would be applicable for EMC's fiscal year ended in 2016. Future fiscal years would adhere to conditions pursuant to the Attorney General Consent Letter.

This Proposed Methodology would provide a more accurate representation of our community's need for charity healthcare by taking into account the effect of the previously unknown consequences of the ACA into the calculation.

Attached as Exhibit A is a table containing calculations of the Proposed Methodology as it applies to EMC. For the 2016 Period, EMC's Minimum Charity Care Amount is \$3,348,377. The percentage change from 2013 to 2016 of charity care costs for the hospitals within the community served by EMC is 79.2%. By applying this community-based reduction percentage to EMC's Minimum Charity Care Amount, the modified Minimum Charity Care Amount for the 2016 Period under the Proposed Methodology would be \$689,937. For reporting periods subsequent to 2016, this modified Minimum Charity Care Amount would be subject to annual CPI adjustments in accordance with the terms of the Attorney General Consent Letter.

This letter is consistent with Regulations section 999.5, subdivision (h)(1), which states that an entity may request approval of any amendment of the terms and conditions of any agreement or transaction for which the Attorney General has given conditional consent, based solely on "a change in circumstances that could not have reasonably been foreseen at the time of the Attorney General's action." The terms of Condition VII specifically acknowledges the ACA "may cause a reduction in future needs of charity care" and that any such reduction will be considered "unforeseen" for purposes of Regulations section 999.5, subdivision (h). Consistent therewith, Vizient stated in its 2013 Vizient Report that it could not foresee the impact that the ACA would have on EMC as it pertains to charity care. Specifically, on page 38 of such report, Vizient stated that "while these [ACA-related] initiatives may result in more individuals with health insurance, it is unknown if this will result in less charity care and bad debt, especially in a service area like Hospital's where a high percentage of the population is medically indigent." Accordingly, EMC was not in a position to be able to foresee, or to control, the changes that the implementation of the ACA would have upon charity care and our Medi-Cal population.

Thank you for your consideration of the request set forth in this letter. We are committed to ensuring that each person in our community has access to quality healthcare and we take pride in our continuing to care for all types of patients regardless of their ability to pay. We believe that the Proposed Methodology set forth in this letter is consistent with the principles contained in the Attorney General Consent Letter and appropriately takes into account how the ACA has dramatically changed the landscape of how healthcare is delivered to our patients.

If you need additional information, please contact me at (209) 664-5090, or at sue.micheletti@tenethealth.com.

Sincerely,

A handwritten signature in black ink, appearing to read "Susan C. Micheletti". The signature is fluid and cursive, with a large initial "S" and "M".

Susan C. Micheletti
Chief Executive Officer
Emanuel Medical Center

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Exhibit A

Proposed Methodology – EMC Calculations

<u>Charity Write-Offs</u>	<u>2013</u>	<u>2014</u>	<u>2015</u>	<u>2016</u>
Memorial Medical Center	\$75,569,313	\$28,887,578	\$13,324,431	\$14,066,568
Doctors Medical Center	\$219,893,770	\$176,950,204	\$36,356,240	\$28,459,023
Oak Valley	\$1,038,604	\$1,473,073	\$891,546	\$900,340
Emanuel Medical Center	\$63,376,160	\$24,260,513	\$15,157,469	\$12,106,611
Mercy Merced	\$30,955,273	\$27,708,684	\$21,301,927	\$17,471,304

<u>Cost/Charge Ratio</u>	<u>2013</u>	<u>2014</u>	<u>2015</u>	<u>2016</u>
Memorial Medical Center	21.45%	21.61%	23.10%	24.45%
Doctors Medical Center	12.44%	11.90%	11.96%	11.83%
Oak Valley	24.75%	29.45%	30.54%	33.79%
Emanuel Medical Center	15.77%	15.79%	13.40%	11.71%
Mercy Merced	24.32%	23.44%	25.77%	24.18%

<u>Cost of Charity Care</u>	<u>2013</u>	<u>2014</u>	<u>2015</u>	<u>2016</u>
Memorial Medical Center	16,209,618	6,242,606	3,077,944	3,439,276
Doctors Medical Center	27,354,785	21,057,074	4,348,206	3,366,702
Oak Valley	257,054	433,820	272,278	304,225
Emanuel Medical Center	9,994,420	3,831,924	2,031,101	1,417,684
Mercy Merced	7,528,322	6,494,916	5,489,507	4,224,561
Total	61,344,200	38,060,340	15,219,035	12,752,449

Note: All data using OSHPD reports

% Change vs '13		38.0%	75.2%	79.2%
Emanuel Charity Commitment		1,338,356	3,250,599	3,318,862
Emanuel's Updated Commitment with Community-Based Adjustment		830,368	806,449	689,937
Emanuel's 2016 Charity Care				1,417,684
Variance				727,747