

June 29, 2018

VIA EMAIL AND OVERNIGHT MAIL

Mr. Scott Chan
Deputy Attorney General
California Department of Justice
Office of the Attorney General,
Charitable Trusts Section
455 Golden Gate Avenue, Suite 11000
San Francisco, CA 94102

Re: St. Joseph Health System (“SJHS”) and St. Mary Medical Center: Request for Amendment to June 21, 2016 Conditions to Approval of Health System Combination Agreement

Dear Mr. Chan:

By this letter, SJHS and St. Mary Medical Center, a California nonprofit corporation, (collectively referred to herein as “SMMC”) respectfully request that the Attorney General amend Section IX of its June 26, 2016 Conditions to the Approval of the Health System Combination Agreement between SJHS and Providence Health & Services (the “**Conditional Consent**”). Section IX of the Conditional Consent requires SMMC to provide an annual amount of charity care equal to or greater than \$7,772,603 (plus an annual cost of living adjustment) at St. Mary Medical Center, the general acute care facility located in Apple Valley, California (the “**Hospital**”).¹

We note at the outset that SMMC seeks only a temporary, limited amendment to the Attorney General’s charity care requirements with respect to the Hospital, covering only the period of charity care provided by SMMC between July 1, 2016 and June 30, 2017 (the “**FY 2017 Reporting Period**”). As described further below, SMMC’s request for a limited amendment is based on the Affordable Care Act’s (the “**ACA**”) substantial effect on the need for charity care within the Hospital’s service area – and particularly the significant expansion of Medi-Cal coverage to the previously uninsured under the ACA – which resulted in significantly diminished charity care usage at the facility. In fact, the impact of the ACA and corresponding expansion of Medi-Cal coverage within SMMC’s service area rendered it impossible for SMMC to provide the annual amount of charity care required by the Conditional Consent during the FY 2017 Reporting Period.

This enormous shift in the Hospital’s payer mix – from uninsured patients (receiving charity care) to Medi-Cal eligible patients – and the unachievable level of charity care set forth in the Hospital’s Conditional Consent (which was based on historical charity care volumes that no longer exist) is demonstrable through several fundamental facts:

¹ The amount of SMMC’s annual charity care requirement is extraordinary given the size of the hospital. SMMC is a 212-bed acute care facility located in Apple Valley, California. In comparison, SJHS-affiliated facilities St. Joseph Hospital of Orange (463 beds), St. Jude Medical Center (350 beds), and Queen of the Valley Medical Center (208 beds) have annual charity care requirements of \$9,243,620, \$7,401,427, and \$2,975,000, respectively.

- Due to the ACA, the California uninsured rate has dropped from 17.2% in 2013 to 7.4% in 2016;
- Within the Hospital’s approximate service area, the number of certified Medi-Cal eligible patients increased by 81% from 2012 through 2014², and Medi-Cal patient volume at the Hospital also substantially increased during the same period;
- At hospitals in San Bernardino County (where the Hospital is located), there was a corresponding 81% decrease in reported annual charity costs from 2013 through 2016 (as cited by the Attorney General’s consultant³);
- At the Hospital itself, charity care patient volume (measured in discharges) dropped by over 70% from FY 2013 through FY 2017 (from 398 discharges in FY 2013 to 114 discharges in the FY 2017 Reporting Period); and
- In order for the Hospital to have reached the charity care level set forth in the Conditional Consent during the FY 2017 Reporting Period, the Hospital would have been required to treat **an additional 1,138 charity care patients** (669 inpatients and 469 outpatients), a number impossible to reach given that the Hospital was effectively at full occupancy during that same time period.

Not only was the charity care level set forth in the Conditional Consent unattainable, but SMMC also suffered a substantial loss – in excess of \$7 million dollars⁴ – during the FY 2017 Reporting Period in connection with the care it provided to the increasing number of Medi-Cal patients seeking treatment at the Hospital.

In light of these circumstances, to require SMMC to pay over \$5 million dollars (representing the amount of SMMC’s charity care shortfall) to other entities, when SMMC – an organization providing more charity care and Medi-Cal services than any other provider in the High Desert area of San Bernardino County – already faithfully continues to fully serve the poor and vulnerable residents within its service area, would be fundamentally unfair and does not serve the best interests of the affected communities.

SMMC’s request for an amendment is submitted pursuant to Section 999.5(h)(2) of Title 11, California Code of Regulations. Section 999.5(h)(2) requires a request for amendment to describe the following:

² Research and Analytics Study Division: Medi-Cal Statistical Briefing, August 2015, available at dhcs.ca.gov.

³ Vizient’s February 23, 2018 Report on USC Verdugo Hills Hospital’s Request for Amendment, at p. 9.

⁴ This figure accounts for a normalized QAF revenue component (the average annual QAF revenue recognized by SMMC over the six year period between FY 2012 and FY 2016), given the inconsistent timing of QAF program payments. Excluding these QAF payments, which payments bear no connection to the Medi-Cal services provided during the periods in which the QAF payments are received, SMMC suffered a loss of over \$41,000,000 on Medi-Cal patients during the FY 2017 Reporting Period.

- The proposed amendment;
- The change in circumstances requiring the amendment;
- How the amendment is consistent with the Attorney General's conditional consent to the transaction; and
- The efforts of the entity making the request to avoid the need for the amendment.

We discuss each of these categories in turn below.

(1) The Proposed Amendment

During the FY 2017 Reporting Period, SMMC provided \$2,269,481 in annual charity care (at cost) at the hospital. Due to the significantly reduced volume of charity care patients at the hospital during that reporting period – when charity care patient volumes were over 70% less than the volumes during FY 2013 – it was effectively impossible for SMMC to provide additional charity care to the residents within its service area, much less meet the charity care levels set forth in the Conditional Consent. In light of these circumstances, SMMC requests that the Attorney General relieve SMMC from having to achieve an unreachable charity care level set forth in the Conditional Consent, and to set SMMC's "Minimum Charity Care Amount" at the same level as its actual charity care costs during the FY 2017 Reporting Period (*i.e.*, \$2,269,481).

In order to demonstrate SMMC's continuing commitment to the communities served by the Hospital and the residents of its service area, should the Attorney General decide to grant SMMC's request for relief, SMMC will dedicate \$1 million dollars (in total) over the next twelve (12) months to the following Hospital programs in order to enhance the access and availability of health care services within the community:

- **Bright Future Mobile Health Services:** Bright Futures Mobile Health Services helps uninsured or low to moderate-income families get health care for adults and children. This program's mobile van brings health care services directly to residents within the Hospital's service area.
- **Healthy Beginnings/ADELANTO Clinic:** Adelanto Clinic is located approximately 11 miles from SMMC, in a designated Medically Underserved Area. The population of Adelanto is approximately 32,000 people and 32% of households live below the federal poverty line. The clinic is the only prenatal care provider in Adelanto, and also provides primary and pediatric care. Additional funding would be used to expand the clinic.

The financial support provided to these programs by SMMC would be provided in addition to the community benefit program payments and charity care cost requirements set forth in the Conditional Consent.

This proposed amendment would allow SMMC, the provider serving the most Medi-Cal and uninsured patients within its service area (and an organization that provided over \$5,781,539 of community benefit services during the FY 2017 Reporting Period to its community – an amount almost \$1 million in excess of the amount required by the Conditional Consent) – to continue to marshal and dedicate its full set of resources to serving its charitable mission.

(2) The Change in Circumstances Requiring the Amendment

As noted above, the ACA led to the extensive expansion of Medi-Cal eligibility throughout California. The impact of the ACA, both in terms of reducing the uninsured patient population and substantially increasing the Medi-Cal patient population in California, has been specifically recognized by numerous public sources. As explained in a report recently prepared for the Attorney General:

“According to the U.S. Department of Health and Human Services, the California uninsured rate has dropped from 17.2% in 2013 to 7.4% in 2016. This steep decline in the uninsured rate has resulted in a dramatic reduction in charity care across California. [...] Prior to the implementation of the ACA, many patients who were categorized as indigent and needing charity care, now receive care supported by Medi-Cal or an insurance plan. As the number of patients that are medically indigent has gone down, so has the need for charity care.”⁵

With respect to Hospital’s service area and its specific patient population, these statements are particularly appropriate. From June 2012 through October 2016, the number of certified Medi-Cal eligible persons within the Hospital’s service area increased by 81% (from 130,202 to 235,144). And, as recently recognized in a report prepared for the Attorney General, annual charity care costs across all hospitals in San Bernardino County (where the Hospital is located) have dropped by approximately 81% during the same time period (FY 2013 through FY 2016).⁶

This dramatic shift in the patient population within the Hospital’s service area – where vast numbers of uninsured patients (who would have been eligible for charity care at the Hospital) received health care coverage instead through the Medi-Cal program – rendered it impossible for SMMC to attain the charity care level set forth in the Conditional Consent. In this regard, the number of patients eligible for charity care at the Hospital (measured in discharges) dropped from 398 patients in FY 2013, and a six-year high of 440 patients in FY 2014, to 114 patients in FY 2017, reflecting an over 70% decrease in charity care patients from pre-ACA periods to FY 2017. In order to meet the Conditional Consent’s requisite charity care level, SMMC would have been required to treat more than 1,100 additional charity care-eligible patients at the Hospital during the FY 2017 Reporting Period⁷ – a number which was impossible to achieve given that the Hospital was operating at effectively full occupancy during this time period, including through its provision of care to a substantially increased number of Medi-Cal patients.

Moreover, the Hospital’s rising Medi-Cal population also had a substantial negative impact on SMMC’s financial performance during the FY 2017 Reporting Period. As noted by the Attorney General’s consultant in a recent health care impact report concerning SMMC (in connection with

⁵ Vizient February 23, 2018 Report to the Attorney General on USC Verdugo Hills Hospital’s Request for Amendment, at p.16.

⁶ Vizient’s February 23, 2018 Report on USC Verdugo Hills Hospital’s Request for Amendment, at p. 9.

⁷ This figure is based on the current average length of stay and average cost of Inpatient and Outpatient services at the Hospital.

SJHS's combination with Providence Health & Services), the Hospital is a substantial provider of Medi-Cal services, and is the market share leader with respect to such services within its service area. This report also specifically recognized the potential impact of the ACA on the Hospital's Medi-Cal population:

"With the implementation of the ACA and the statewide expansion of Medi-Cal, the percentage of the State of California's population that is currently eligible for Medi-Cal has greatly increased, reporting a historic increase to more than 12 million enrollees in the Medi-Cal program in 2016. Based on St. Mary Medical Center's service area income demographics and San Bernardino County's percentage of Medi-Cal eligible residents, a large percentage of the service area residents qualify for coverage under the ACA expansion."⁸

This impact was borne out during the FY 2017 Reporting Period, when the Hospital's total Medi-Cal patient discharges rose to 6,174 discharges, a figure which had increased year-over-year from 4,454 Medi-Cal patient discharges in FY 2013 (representing an approximate 37% increase from pre-ACA periods to FY 2017). In connection with providing care to this larger Medi-Cal patient population, SMMC suffered a loss of over \$41,000,000 during the FY 2017 Reporting Period. Even including Quality Assurance Fee (QAF) revenue received by the Hospital – despite the fact those funds are attributable to Medi-Cal services provided in prior years, and were unaffected by Medi-Cal expansion – SMMC's losses exceeded \$7 million dollars during the FY 2017 Reporting Period.

In light of these circumstances, where the change in payer mix at the Hospital due to the ACA (and out of the Hospital's control) has both rendered it impossible for SMMC to provide the level of charity care set forth in the Conditional Consent and caused SMMC to suffer a substantial negative financial impact, it would be wholly inequitable for the Attorney General to require SMMC to pay additional funds (to other entities) for failing to reach an unattainable requirement.⁹ This is particularly true here, where those funds would be better served if they remained with SMMC, as SMMC – which is among the largest health care providers in the High Desert and has continually provided, consistent with its charitable mission, substantial health care services and community benefits to the poor and vulnerable residents within its community – is uniquely positioned to utilize and allocate its full resources in the best interests of the communities it serves.

Finally, in its Conditional Consent, the Attorney General specifically recognized that the ACA might cause a reduction in the future need for charity care, although the impacts of the ACA were not fully known at the time the Conditional Consent was issued. As a result, the Conditional Consent specifically states that:

⁸ Vizient/MDS's March 28, 2016 Report re: Effect of the Proposed Change in Control and Governance of St. Joseph Health System and Providence Health & Services on the Availability and Accessibility of Healthcare Services to the Communities Served by St. Mary Medical Center (the "HICR"), at p. 57.

⁹ It is also worth noting that the charity care amounts set forth in the Conditional Consent applicable to SMMC were set based on historical charity care costs and volumes that included a majority of pre-ACA and Medicaid expansion time periods, and were already declining when the Conditional Consent was issued. As noted in the Attorney General's Health Care Impact Report for SMMC, "St. Mary Medical Center's charity care costs have decreased from approximately \$9.6 million in FY 2011 to \$4.3 million in FY 2015." HICR, at pp. 45 and 46.

"The 2010 Federal Patient Protection and Affordable Care Act may cause a reduction in future needs of charity care. Any actual reduction will be considered "unforeseen" for the purposes of Title 11, California Code of Civil Procedure, section 999.5, subdivision (h)."

Accordingly, the substantial change in circumstances described above clearly meet the requirements of Title 11, California Code of Regulations, Section 999.5(h)(1).

(3) The Requested Amendment is Consistent with the Attorney General's Conditional Consent; Efforts of SMMC to Avoid the Need for Amendment

The charity care requirements set forth in the Attorney General's Conditional Consent were designed so that SMMC would continue to provide levels of charity care that were consistent with the hospital's historical charity care experience and the corresponding needs of the community. Consistent with the spirit and intent of Section IX of the Conditional Consent, SMMC has continued to provide charity care at levels that match the needs of the communities it serves.

Due to the uncertainties related to the ACA – and the changes being made at the federal level that may adversely affect the ongoing success of the program in reducing the number of uninsured – we have limited our request for an amendment to SMMC's charity care requirements to this single year. Should the need for uninsured charity care increase in the future, we are fully prepared to provide such care consistent with our religious and charitable mission and with the AG's conditions of consent.

SMMC's proposed – and limited – amendment does not alter the spirit or intent of Section IX or any other terms of the Conditional Consent. To the contrary, SMMC's proposed amendment, which includes a commitment from SMMC to support an additional \$1 million in Hospital programs (an amount of support to be provided over and above the community benefit and charity care services already provided by SMMC pursuant to the Conditional Consent), will enhance access and availability of health care services within the communities served by the Hospital.

As described in detail above, the dramatic effects of the ACA on the need for charity care within SMMC's service area made it impossible for the Hospital to provide the requisite levels of charity care set forth in the Conditional Consent. As a result, this request for amendment was necessary, and unavoidable.

In light of the foregoing, SMMC respectfully requests that the Attorney General grant SMMC's request for amendment. If you have any questions about this correspondence, please let me know.

Sincerely,



Deputy General Counsel
St. Joseph Health System