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USC Verdugo Hills Hospital's Request for Amendment of Condition VII

Prepared for the Office of the California Attorney General

February 23, 2018

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Introduction & Purpose

On January 4, 2018, pursuant to Title 11, California Code of Regulations, Section 999.5, subdivision (h), the University of Southern California (USC) Verdugo Hills Hospital submitted a request to amend Condition VII set forth in the California Attorney General's July 2013 "Conditions to Sale of Verdugo Hills Hospital, Verdugo Hills Health Services, and Verdugo Hills Support Services to USC Verdugo Hills Hospital LLC, a wholly-owned subsidiary of University of Southern California." Condition VII requires USC Verdugo Hills Hospital to provide a certain level of charity care[1] for five years after closing date of the transaction as set forth below:

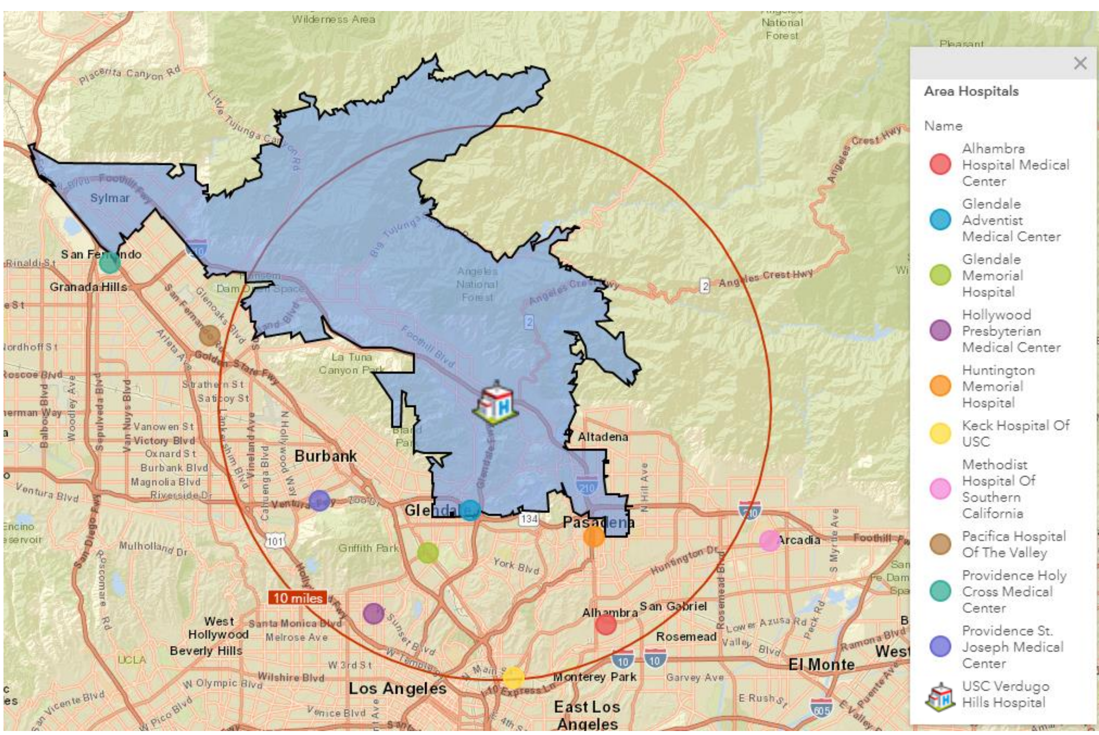
VII.

> For five years from the closing date of the transaction, Buyers shall provide an annual amount of Charity Care (as defined below) at Verdugo Hills Hospital equal to or greater than $1,978,848 (the "Minimum Charity Care Amount". For purposes hereof, the term "Charity Care" shall mean the amount of charity care costs (not charges) incurred by Buyers in connection with the operation and provision of services at Verdugo Hills Hospital. The definition and methodology for calculating "charity care" and the methodology for calculating "cost" shall be the same as that used by the California Office of Statewide Health Planning and Development (OSHPD) for annual hospital reporting purposes. Buyers shall use charity care and collection policies that comply with Federal and California law.
>
> Buyers' obligation under this condition shall be prorated on a daily basis if the closing date of the transaction is a date other than the first day of Buyers' fiscal year.
>
> For the second fiscal year and each subsequent fiscal year, the Minimum Charity Care Amount shall be increased (but not decreased) by an amount equal to the Annual Percent Increase, if any, in the "12 Months Percent Change: All Items Consumer Price Index for All Urban Consumers in the Los Angeles-Riverside-Orange County Consolidated Metropolitan Statistical Area Base Period: 1982-84=100" (CPI-LA, as published by the U.S. Bureau of Labor Statistics).
>
> If the actual amount of Charity Care provided by the Buyer at Verdugo Hills Hospital for any fiscal year is less than the Minimum Charity Care Amount (as adjusted pursuant to the above referenced Consumer Price Index) required for such fiscal year, Buyers shall pay an amount equal to the deficiency to a tax-exempt entity for direct medical care to residents in the Verdugo Hills Hospital service area, as defined on page 24 of the Health Care Impact Statement. Such payment shall be made within nine (9) months following the end of such fiscal year.

[1] Charity care is free or discounted care that hospitals provide to patients under the hospital's financial assistance policy. The Office of Statewide Health Planning and Development (OSHPD) defines charity care by contrasting charity care and bad debt. According to OSHPD, "the determination of what is classified as ... charity care can be made by establishing whether or not the patient has the ability to pay. The patient's accounts receivable must be written off as bad debt if the patient has the ability but is unwilling to pay off the account."

Vizient Inc. was retained by the Office of the California Attorney General to analyze USC Verdugo Hills Hospital's request to reduce its charity care obligation as set forth in Condition VII. In preparation of this report, Vizient Inc. performed the following:

- A review of USC Verdugo Hills Hospital's request to amend Condition VII dated January 4, 2018, and submitted to the Office of the California Attorney General;
- Research on the effects of the ACA on the uninsured and their need for charity care, and the impact of the Emergency Medical Treatment and Active Labor Act (EMTALA) on access for the uninsured to emergency medical care and the subsequent cost of charity care;
- An analysis of financial, utilization, and service information provided by the California Office of Statewide Health Planning and Development (OSHPD); and
- A review of trends to determine if similar charity care and payer mix patterns are occurring at other comparable area hospitals as well as those in Los Angeles and other Southern California counties. USC Verdugo Hills Hospital's service area, as defined on page 24 of the Health Impact Statement, includes approximately 320,000 residents. There are three comparable hospitals located within USC Verdugo Hills Hospital's service area and seven additional comparable hospitals located just beyond the service area that are also important providers of healthcare services to service area residents.



Background & History

Verdugo Hills Hospital (the Hospital) began as Behrens Memorial Hospital, which was established in 1947. Instead of attempting to expand the Behrens facility, a new hospital was built on the hilltop land donated by the Greene family. In 1972, the Hospital was created as an independent, general acute care hospital serving patients in the cities of Glendale and La Cañada Flintridge, as well as the surrounding Foothill communities of Southern California.

In 1991, the Hospital opened an 18-bed Transitional Care Unit that provides skilled nursing services. In 1994, the Hospital opened a 24-bed, licensed, acute inpatient psychiatric program. All 24 beds are designated as geropsychiatric, are contained in a locked unit, and can care for involuntary patients under Welfare and Institutions Code sections 5150 and 5250[2]. The Hospital also operates a geropsychiatric program called "Stepping Stones at Verdugo Hills Hospital" that provides hospital-based intensive outpatient psychiatric services.

From January to October 2010, the Strategic Planning Committee of the Hospital's Board of Directors (Board) discussed the costs associated with upgrading facilities due to seismic concerns; various capital needs, including emergency department expansion; and the need to review options for establishing a more strategic business relationship with physicians. In April 2011, Board established an Options Committee to discuss opportunities and risks of affiliation and other options.

In May 2011, the Hospital retained legal counsel and the services of a consulting firm to assist with the review process. In November 2011, Board voted to enter into discussions with area hospitals and explore possible affiliation, merger, or other arrangements that would be compatible with the strategic priorities of the Hospital. In March and April 2012, Board established an Affiliation Oversight Committee and approved a process for considering affiliation and partner selection criteria. In June 2012, the Affiliation Oversight Committee reviewed and discussed the three proposals that had been received and recommended commencing negotiations with USC. The Board approved the recommendation. In July 2012, the Hospital's medical staff hired its own consultant to determine whether the Hospital needed to find a partner and whether the Hospital used an appropriate partner selection process. The Hospital

[2] Under Welfare and Institutions Code section 5150, a person can be held involuntarily for 72 hours if a police officer, clinician, or professional person "has probable cause to believe that the person is, as a result of mental disorder, a danger to others, or to himself or herself, or gravely disabled." Under California Welfare and Institutions Code section 5250, if the patient is brought to a facility under section 5150, the patient can be provided no more than 14 days of intensive treatment related to the mental disorder or impairment related to chronic alcoholism, under specific conditions.

selected "the best proposal submitted," namely USC. In August 2012, the Board reviewed the Letter of Intent from USC and authorized its execution. In November 2012, the Board established a Definitive Agreement Review Committee to work with the Hospital's legal counsel and consultant and to provide feedback on agreement provisions and drafts. In early March 2013, the Asset Purchase Agreement was presented to the Board and was approved. On March 11, 2013, the parties entered into the Asset Purchase Agreement. On March 22, 2013, written notice of the sale of Verdugo Hills Hospital was submitted to the Office of the California Attorney General.

On March 25, 2013, Verité Healthcare Consulting, LLC was retained by the Office of the California Attorney General to prepare a healthcare impact statement to describe the possible effects that USC's acquisition of the Hospital could have on the availability and accessibility of healthcare services to the communities served by the Hospital. On May 16, 2013, the healthcare impact statement was issued. On July 5, 2013, the California Attorney General issued her decision granting conditional consent to the proposed sale of the Hospital. The Asset Purchase Agreement closed on July 16, 2013.

Today, the Hospital is licensed for 158 beds and services include a 24-hour emergency room, a primary stroke center, bariatric and minimally invasive surgery, OB-GYN and infant services, acute inpatient geropsychiatry, orthopedic surgery, occupational, physical and speech therapy, cardiac rehabilitation and imaging and diagnostic services to the over 320,000 residents living in the Hospital's service area.

Charity Care Costs

USC Verdugo Hills Hospital

The table below details the Hospital's annual historic charity care costs from Fiscal Years (FY) 2014 – 2017 and the difference between the historic annual charity care cost and the minimum annual charity care amount required by Condition VII.

CHARITY CARE COSTS: FY 2014 - 2017			
FY Year	**Charity Care Costs**	**Charity Care Cost Requirement**	**Difference**
2017[1]	$421,518	$2,073,564	-$1,652,045
2016[2]	$1,741,292	$2,030,914	-$289,623
2015[2]	$2,018,836	$1,998,636	$20,199
2014[3]	$1,794,255	$1,897,525[4]	-$103,270

Source: OSHPD Disclosure Reports, FY 2013-2016

[1]From an unaudited OSHPD Disclosure Report. All other years are from audited reports

[2]FY 2015 is from 7/1/2014 to 5/28/2015 and FY 2016 is from 5/29/2015 to 6/30/2016. USC Verdugo Hills Hospital LLC transferred ownership of the Hospital to the University of Southern California on 5/29/2015, resulting is a shortened fiscal period in 2015, and a lengthy fiscal period is 2016.

[3]FY is from 7/16/2013 to 6/30/2014. The sale of Verdugo Hills Hospital to USC Verdugo Hills Hospital LLC closed 7/16/2013.

[4]Prorated per Condition VII as the first fiscal year after the transaction closed was only 350 days in length.

In FY 2015, the Hospital exceeded the minimum charity care cost required by Condition VII by approximately $20,000. However, as shown in the table below, in FY 2014, FY 2016, and 2017 the Hospital's charity care costs were approximately $103,000, $290,000, and $1.65 million, respectively, less than the minimum amount required in Condition VII. The Hospital is asking the Attorney General to modify the required charity care obligation for FY 2017 and forward as follows:

A. 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 the Hospital within the community it serves. Costs are determined by applying the charity care write-offs, multiplied by the hospital's cost-to-charge ratio.

B. Document the percentage change from 2013 to 2016 for all of the hospitals in a specific community for the unique group that has undergone a sale or transfer of not-for-profit facilities during a window of time experiencing the tremendous change that has affected the health care industry (as discussed below) and apply the percentage change to the AG specified charity care cost target to compute a community-wide reduction amount.

C. Deduct the reduction amount from the AG specified charity care cost target to determine a modified minimum charity cost target.

D. The following is an example[3] provided in the September 8, 2017, letter from California Hospital Association to Melanie Fontes Rainer, Special Assistant to Attorney General Xavier Becerra:

AG Required Charity Cost Target (a)	Community-based Reduction Percentage (b)	Reduction Amount (a * b = c)	Modified Minimum Charity Cost Target (a+c)
$15,000,000	(40.0%)	$6,000,000	$9,000,000

E. The following is an application of the Hospital's charity care calculation, under the formula in item D above:

AG Required Charity Cost Target for the Hospital (a)	**Community-based Reduction Percentage (b)**	Reduction Amount (a * b = c)	**Modified Minimum Charity Cost Target (a+c)**
$1,978,848	(45%)	$890,481.60	$1,088,366.40

[3] Verdugo Hills Hospital's formula for the modified minimum charity cost target should read "a-c" not "a+c". The community based reduction percentage of 45% was based upon the total net charity care change from 2013 to 2016 for four nearby hospitals (Glendale Memorial, Glendale Adventist, Methodist Hospital, and Huntington Memorial).

When this methodology is applied, it results in a reduction percentage of 45% and modified charity cost of $1,088,366 versus the required amount of $1,978,848.

F. The modified minimum charity care target would be applicable for the Hospital's FY ended in 2015 and future subsequent fiscal years would adhere to conditions pursuant to the AG Decision.

USC Verdugo Hills Hospital Compared to Other General Acute Care Hospitals Serving the Area

The table below compares charity care costs at service area general acute care hospitals from FY 2013 to FY 2016. FY 2017 charity care cost data was not available for all area hospitals at the commencement of this report. Since Calendar Year (CY) 2012[4], charity care costs at the Hospital have decreased by 24% from approximately $2.3 million to approximately $1.7 million in FY 2016. A decrease in charity care costs is consistent across almost all of the area hospitals. Six of the area hospitals have seen decreases in their charity care costs of over 50%, including Glendale Memorial Hospital, Hollywood Presbyterian Medical Center, Huntington Memorial Hospital, Methodist Hospital of Southern California, Pacifica Hospital of the Valley, and Providence St. Joseph Medical Center. Two of the area hospitals, Glendale Adventist Medical Center and Keck Hospital of USC, have seen increases in their charity care costs between FY 2013 and FY 2016 of 3% and 88% (from $216,115 to $407,006), respectively. Collectively, there was a 45% decrease in charity care costs among area hospitals from FY 2013-2016.

AREA HOSPITAL COST OF CHARITY CARE: FY 2013-2017

Hospital	FY 2013	FY 2014	FY 2015	FY 2016	% Change (FY 2013-2016)	% Change (FY 2015-2016)
USC Verdugo Hills Hospital	**$2,304,739***	**$1,794,255**	**$2,018,836**	**$1,741,292**	-24%	-14%
Alhambra Hospital Medical Center	$1,482,841	$548,064	$448,278	$900,093	-39%	101%
Glendale Adventist Medical Center	$4,791,931	$1,939,561	$1,345,613	$4,919,161	3%	266%
Glendale Memorial Hospital	$6,008,281	$3,373,925	$7,120,911	$2,206,170	-63%	-69%
Hollywood Presbyterian Medical Center	$3,480,178	$2,685,412	$1,059,080	$688,488	-80%	-35%
Huntington Memorial Hospital	$4,397,373	$9,163,058	$2,868,935	$1,658,642	-62%	-42%
Keck Hospital Of USC	$216,115	$508,731	$726,399	$407,006	88%	-44%
Methodist Hospital Of Southern California	$1,997,114	$953,448	$632,759	$705,700	-65%	12%
Pacifica Hospital Of The Valley	$1,766,070	$1,417,739	$2,126,789	$711,287	-60%	-67%
Providence Holy Cross Medical Center	$18,307,529	$15,554,983	$10,093,378	$12,483,334	-32%	24%
Providence St. Joseph Medical Center	$9,932,881	$7,337,725	$4,040,756	$3,614,310	-64%	-11%
Total	**$54,685,053**	**$45,276,900**	**$32,481,734**	**$30,035,484**	**-45%**	**-8%**

Source: OSHPD Disclosure Reports, FY 2013-2016

* From CY 2012. After USC acquired Verdugo Hills Hospital in 2013, the beginning of the fiscal year end changed from December 31 to June 30.

[4] After USC acquired the Hospital, the Hospital moved the beginning of its fiscal period from January to July. For purposes of comparison, the CY 2012 is shown instead of FY 2013 as it represents the most recent full year fiscal period as compared to FY 2013, which is approximately 6 months in length.

Los Angeles County Compared to Other Southern California Counties

The table below compares charity care costs for general acute care hospitals across five counties in Southern California from FY 2013-2016. Since FY 2013, charity care costs in Los Angeles County have decreased by 58% from $388 million in FY 2013 to approximately $163 million in FY 2016. Charity care costs have also decreased in Orange County, Riverside County, San Bernardino County, and Ventura County by 53%, 97%, 81%, and 40%, respectively. Four of the five counties have seen decreases in their charity care costs of over 50%, including Los Angeles County, Riverside County, and San Bernardino County. Collectively, there has been a 63% decrease in charity among the five counties between FY 2013 and FY 2016.

Vizient also studied the trend in charity care costs across all California general acute care hospitals for the same period. Over this four-year period, California's charity care costs dropped by 57%, from $1.6 billion in 2013 to $675 million in 2016.

COUNTY COST OF CHARITY CARE: FY 2013 - 2016						
County	FY 2013	FY 2014	FY 2015	FY 2016	% Change (FY 2013-2016)	% Change (FY 2015-2016)
Los Angeles	$387,530,570	$268,100,285	$204,675,902	$163,395,908	-58%	-20%
Orange	$82,141,850	$84,128,021	$57,191,768	$38,717,132	-53%	-32%
Riverside	$56,363,472	$47,246,921	$15,722,421	$1,608,453	-97%	-90%
San Bernardino	$103,273,098	$55,098,265	$43,564,654	$19,384,918	-81%	-56%
Ventura	$37,891,771	$34,261,634	$18,307,957	$22,626,673	-40%	24%
Total	**$667,200,761**	**$488,835,125**	**$339,462,702**	**$245,733,084**	**-63%**	**-28%**

Source: OSHPD Disclosure Reports, FY 2013-2016

Conclusion

The Hospital's charity care costs decreased by 24% between FY 2013 and FY 2016. Between FY 2013 and FY 2016, nine of the eleven area general acute care hospitals showed a decrease in charity care costs of between 24% and 80%. The majority of the decrease in charity care costs occurred between FY 2013 and FY 2015. Charity care costs for the areas' hospital's overall decreased by only 8% from FY 2015 to FY 2016. Additionally, charity care costs across five counties in Southern California have collectively decreased by 63% from FY 2013 to FY 2016, and 28% from FY 2015 to FY 2016.

Payer Mix Trends

USC Verdugo Hills Hospital

In support of its request, the Hospital cited the January 1, 2014 commencement of the 2010 Federal Patient Protection and Affordable Care Act (the ACA) as the reason for the drop in charity care costs. The impact of the ACA has resulted in a substantial increase in the number of Medi-Cal beneficiaries and a substantial reduction in the number of indigent patients without insurance. Between CY 2012 and FY 2017, the Hospital had an increase of 193% for its Medi-Cal inpatient discharges and increase of 13% for its Medi-Cal outpatient visits. Between CY 2012 and FY 2017, the Hospital had a decrease of 72% for its indigent inpatient discharges and a decrease of 94% for its indigent outpatient visits.

USC VERDUGO HILLS HOSPITAL: MEDI-CAL AND INDIGENT PATIENT PAYER MIX						
	CY 2012*	FY 2014	FY 2015	FY 2016	FY 2017	% Change (CY 2012-FY 2017)
Medi-Cal Inpatient Discharges	208	383	482	666	609	193%
Medi-Cal Outpatient Visits	9,000	11,087	13,656	10,164	10,164	13%
Indigent Inpatient Discharges	148	155	131	52	42	-72%
Indigent Outpatient Visits	5,248	4,419	5,091	2,509	333	-94%

Source: OSHPD Disclosure Reports, FY 2012-2016

* From CY 2012. After USC acquired Verdugo Hills Hospital in 2013, the beginning of the fiscal year end changed from December 31 to June 30.

USC Verdugo Hills Hospital Compared to Other General Acute Care Hospitals Serving the Service Area

The tables on the following pages compare payer mix trends for the area general acute care hospitals from FY 2013 – 2016 for Medi-Cal patients and indigent patients.

A. Indigent Patients:

Between FY 2013 and FY 2016, all area hospitals showed a decrease in inpatient and outpatient indigent encounters with the exception of outpatient visits at Alhambra Hospital Medical Center (13% increase), Glendale Adventist Medical Center (114% increase), and Glendale Memorial Hospital (166% increase). Additionally, between FY 2013 and FY 2016, inpatient and outpatient indigent encounters decreased by a combined 70% and 55% respectively.

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AREA HOSPITALS: INDIGENT INPATIENT DISCHARGES AND OUTPATIENT VISITS										
	FY 2013		FY 2014		FY 2015		FY 2016		% Change (FY 2013-2016)	
Hospital	Inpatient Discharges	Outpatient Visits	Inpatient Discharges	Outpatient Visits	Inpatient Discharges	Outpatient Visits	Inpatient Discharges	Outpatient Visits	Inpatient Discharges	Outpatient Visits
USC Verdugo Hills	**148***	**5,248***	**155**	**4,419**	**131**	**5,091**	**52**	**2,509**	**-65%**	**-52%**
Alhambra Hospital Medical Center	125	1,165	87	1,256	26	96	7	1,321	-94%	13%
Glendale Adventist Medical Center	184	222	53	150	108	288	167	475	-9%	114%
Glendale Memorial Hospital	23	498	81	5,622	66	7,723	13	1,327	-43%	166%
Hollywood Presbyterian Medical Center	48	1,461	49	941	19	812	40	674	-17%	-54%
Huntington Memorial Hospital	238	980	262	4,616	117	1,185	65	801	-73%	-18%
Keck Hospital Of USC	5	89	10	53	0	0	0	0	-100%	-100%
Methodist Hospital Of Southern California	223	892	118	562	33	274	42	293	-81%	-67%
Pacifica Hospital Of The Valley	45	127	35	124	32	380	10	3	-78%	-98%
Providence Holy Cross Medical Center	955	15,259	601	6,488	343	4,941	159	5,482	-83%	-64%
Providence St. Joseph Medical Center	360	11,329	22	662	95	1,707	141	4,038	-61%	-64%
Total	**2,354**	**37,270**	**1,473**	**24,893**	**970**	**22,497**	**696**	**16,923**	**-70%**	**-55%**

Source: OSHPD Disclosure Reports, FY 2013-2016

* From CY 2012. After USC acquired Verdugo Hills Hospital in 2013, the beginning of the fiscal year end changed from December 31 to June 30.

B. Medi-Cal Patients:

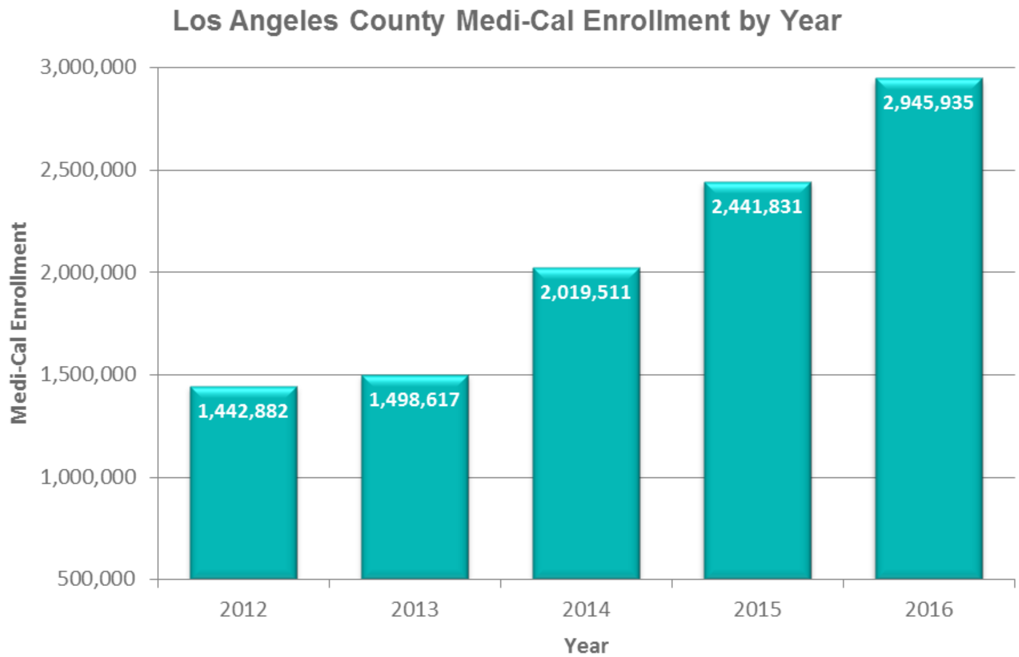
Between FY 2013 and FY 2016, all area hospitals showed an increase in inpatient and outpatient Medi-Cal encounters with the exception of inpatient discharges at Glendale Memorial Hospital (0%), Hollywood Presbyterian Medical Center (-2%), and Pacifica Hospital of the Valley (-15%) and outpatient visits at Providence St. Joseph Medical Center (-32%). As shown in the table below, between FY 2013 and FY 2016 inpatient and outpatient Medi-Cal encounters increased by a combined 19% and 42%, respectively.

AREA HOSPITALS: MEDI-CAL INPATIENT DISCHARGES AND OUTPATIENT VISITS										
	FY 2013		FY 2014		FY 2015		FY 2016		% Change (FY 2013-2016)	
Hospital	Inpatient Discharges	Outpatient Visits	Inpatient Discharges	Outpatient Visits	Inpatient Discharges	Outpatient Visits	Inpatient Discharges	Outpatient Visits	Inpatient Discharges	Outpatient Visits
USC Verdugo Hills	**208***	**9,000***	**383**	**11,087**	**482**	**13,656**	**666**	**10,164**	**220%**	**13%**
Alhambra Hospital Medical Center	1,121	6,587	1,532	8,033	2,116	10,602	2,407	10,917	115%	66%
Glendale Adventist Medical Center	5,940	28,288	6,083	32,720	6,023	55,995	6,594	52,456	11%	85%
Glendale Memorial Hospital	4,162	22,633	3,531	26,812	3,756	31,008	4,175	38,318	0%	69%
Hollywood Presbyterian Medical Center	7,530	21,031	7,156	26,809	7,540	28,017	7,403	30,351	-2%	44%
Huntington Memorial Hospital	3,152	14,855	3,974	17,638	4,408	22,847	4,912	22,599	56%	52%
Keck Hospital Of USC	1,126	11,590	1,398	10,774	1,959	15,428	1,717	17,170	52%	48%
Methodist Hospital Of Southern California	1,939	12,129	2,603	16,630	2,540	21,054	2,574	21,098	33%	74%
Pacifica Hospital Of The Valley	3,550	7,420	3,178	5,751	3,070	8,506	3,022	8,814	-15%	19%
Providence Holy Cross Medical Center	4,745	37,370	5,938	48,686	6,315	52,154	6,617	63,579	39%	70%
Providence St. Joseph Medical Center	3,650	44,325	3,672	30,644	3,820	26,067	4,255	30,295	17%	-32%
Total	**37,123**	**215,228**	**39,448**	**235,584**	**42,029**	**285,334**	**44,342**	**305,761**	**19%**	**42%**

Source: OSHPD Disclosure Reports, FY 2013-2016

* From CY 2012. After USC acquired Verdugo Hills Hospital in 2013, the beginning of the fiscal year end changed from December 31 to June 30.

The table below shows Medi-Cal managed care enrollment in Los Angeles County between CY 2012 and CY 2016:



Source: California Department of Health Care Services

Since 2013, Medi-Cal enrollment in Los Angeles County has more than doubled to almost 3 million enrollees.

Los Angeles County has a Two-Plan Model for managed care that offers Medi-Cal beneficiaries a "Local Initiative" and a "commercial plan." L.A. Care Health Plan is the Local Initiative plan for Los Angeles County. Medi-Cal beneficiaries can choose L.A. Care Health Plan or one of the contracting partners that include Blue Cross of California, Care 1st, Community Health Plan, and Kaiser Permanente. The second Medi-Cal plan in Los Angeles County is a private commercial plan provided by Health Net Community Solutions, Inc. in partnership with Molina Healthcare.

Conclusion

Between FY 2013 and FY 2016, indigent inpatient and outpatient encounters decreased significantly at most of the area's general acute care hospitals including at USC Verdugo Hills Hospital. A drop in indigent inpatient and outpatient encounters has a direct correlation to a drop in charity care costs.

Between FY 2013 and FY 2016, inpatient and outpatient Medi-Cal encounters increased significantly at most of the area general acute care hospitals. At the Hospital, the Medi-Cal inpatient discharges and

Medi-Cal outpatient visits increased. An increase in inpatient and outpatient Medi-Cal encounters has a direct correlation to a drop in charity care costs.

Bad Debt

The table below shows the annual provision for bad debt[5] at the Hospital from CY 2012-2017. There has been a 95% and a 167% decrease in bad debt at the Hospital between CY 2012 - FY 2016 and CY 2012 - FY 2017 respectively.

USC VERDUGO HILLS HOSPITAL BAD DEBT: CY 2012 to FY 2017							
	CY 2012*	FY 2014	FY 2015	FY 2016	FY 2017	% Change (CY 2012-FY 2016)	% Change (CY 2012-FY 2017)
Provision for Bad Debt	2,892,941	2,677,856	1,808,487	134,199	(1,941,809)[1]	-95%	-167%

Source: OSHPD Disclosure Reports, FY 2013-2016

* After USC acquired Verdugo Hills Hospital in 2013, the beginning of the fiscal year end changed from December 31 to June 30.

[1] In 2017, the hospital reached a settlement with a 3rd party payor for 2.4 million dollars, some of which was previously considered uncollectable in prior years. The portion that was previously considered uncollectable was adjusted in FY 2017.

The table below shows the annual provision for bad debt for area general acute care hospitals from FY 2013-2016.

USC VERDUGO HILLS HOSPITAL & AREA HOSPITAL PROVISION FOR BAD DEBT: FY 2013 - 2016					
Hospital	FY 2013	FY 2014	FY 2015	FY 2016	% Change (FY 2013-2016)
USC Verdugo Hills Hospital	**$2,892,941***	**$2,677,856**	**$1,808,487**	**$134,199**	**-95%**
Alhambra Hospital Medical Center	$4,472,256	$10,389,288	$2,471,886	$1,833,922	-59%
Glendale Adventist Medical Center	$7,977,162	$14,905,803	$27,621,243	$6,366,547	-20%
Glendale Memorial Hospital	$29,694,507	$24,892,103	($3,486,003)	$10,000,810	-66%
Hollywood Presbyterian Medical Center	$30,308,274	$8,936,329	$5,039,477	$3,424,964	-89%
Huntington Memorial Hospital	$19,338,197	$4,219,528	$22,162,786	$16,039,052	-17%
Keck Hospital Of USC	$25,562,366	$26,631,579	$31,553,389	$19,209,950	-25%
Methodist Hospital Of Southern California	$13,691,440	$14,178,412	$3,359,497	$6,719,488	-51%
Pacifica Hospital Of The Valley	$6,100,188	$1,873,672	$4,435,020	$1,570,071	-74%
Providence Holy Cross Medical Center	$12,272,226	$20,469,631	$10,388,684	$25,987,322	112%
Providence St. Joseph Medical Center	$11,816,302	$13,934,640	$15,755,709	$12,077,907	2%
Total	**$164,125,859**	**$143,108,841**	**$121,110,175**	**$103,364,232**	**-37%**

Source: OSHPD Disclosure Reports, FY 2013-2016

* From CY 2012. After USC acquired Verdugo Hills Hospital in 2013, the beginning of the fiscal year end changed from December 31 to June 30.

[5] The amount of accounts receivable that are determined to be uncollectible due to the patient's unwillingness to pay. This amount is charged as a credit loss against gross patient revenue. Bad debts are classified as deductions from revenue and not included in operating expenses.

Bad debt at Alhambra Hospital, Glendale Memorial, Hollywood Presbyterian, Methodist Hospital of Southern California and Pacifica Hospital of the Valley decreased by over 40% between FY 2013 and FY 2016. However, between FY 2013 and FY 2016, bad debt increased by 2% and 112% at Providence Holy Cross Medical Center and Providence St. Joseph Medical Center, respectively. Overall, the area general acute care hospitals have seen a combined decrease in bad debt of 37%.

Conclusion

Between FY 2013 and FY 2016, bad debt decreased significantly at most of the area's general acute care hospitals. During this time period, bad debt at the Hospital decreased by 95%, indicating that the decrease in charity care costs could not be explained by an increase in bad debt (e.g., did the newly insured, often enrolled in high deductible health plans, have difficulty paying co-pays leading to increased bad debt at the Hospital).

Analysis of the Request by USC Verdugo Hills Hospital to Amend Condition VII

The methodology requested by the Hospital to be used for a modification of charity care cost may not be a good predictor of future charity care needs in the specific community because of the following:

1. It assumes the changes to insurance coverage that have resulted in a decrease of charity care due to the ACA from FY 2013-2016 will continue in the future. Currently, proposed federal healthcare policy changes affecting the "individual mandate" and funding of health plans on the health insurance marketplace are likely to result in increases, instead of decreases, to the number of uninsured patients and, thus, increases in charity care;

2. It assumes the changes to insurance coverage that have resulted in a decrease of charity care due to the ACA from FY 2013-2016 will continue in the future. Uncertain funding and federal policies regarding Medicaid may lead to decreases, instead of increases, in covered Medi-Cal lives and thus increases in charity care;

3. Basing future charity care obligations on the percent of charity care decreases for FY 2013-2016 is not accurately predictive of the future as evidenced by the 8% decrease of charity care costs for area hospitals from FY 2015 to FY 2016 compared to that of prior years;

4. The Hospital requests calculating a modified minimum charity care target that would be applicable for the Hospital's commitment that remains constant for future years. However, the community's need for charity care has not been constant in the past and is unlikely to be in future; and

5. While there has been a significant decline in charity care, there is no consistent percentage that can be applied to individual hospitals. For example, while the regional average charity care cost reduction for the ten area hospitals was 45% from FY 2013-2016, the individual hospitals reported a range from an increase of 88% to a decrease of 80%. A "community-based reduction percentage" that includes a community does not account for variations in the changing local community dynamics regarding demographics, payer mix, healthcare service availability, access, and competition. Not only is health care very local, but most charity care for a hospital is for

patients that have presented in the emergency department and most patients utilize the emergency department closest to their home. The Emergency Medical Treatment and Labor Act (EMTALA) is a federal law that requires Medicare participating hospitals to screen and provide stabilizing treatment to anyone coming to an emergency department regardless of their insurance status or ability to pay. Hospitals with specialized capabilities must also accept appropriate transfers to provide stabilizing treatment regardless of ability to pay. The law does not require hospitals to continue treating patients once they are stable. The law was enacted in 1986 in order to prevent improper care of patients, and avoid the "dumping"[6] of Medicare, Medicaid, and uninsured patients. Since then it has remained an unfunded mandate thus resulting in charity care for those unable to pay and within federal poverty level policies. Hospitals found in violation of the law face a potential $50,000 civil fine per incident and can be barred from the Medicare and Medicaid programs.

Summary

The ACA led to the expansion of Medi-Cal in California and the creation of a healthcare marketplace (Covered California) for individuals to be able to purchase subsidized health insurance plans. As a result of expanded health insurance coverage, the number of uninsured in California has decreased. 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 of charity care across California. Charity care is free or discounted care that hospitals provide to patients under the hospital's financial assistance policy. Most patients that are medically indigent access hospital care through the emergency department and the largest source of charity care cost is for those indigent patients that are admitted. The second largest charity care cost is for indigent patients that are seen in the emergency department and then released without being admitted. 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.

The ACA led to the expansion of Medi-Cal and increased enrollment in subsidized health insurance plans. Between FY 2013 and FY 2016, indigent inpatient and outpatient encounters decreased

[6] A statutorily imposed liability that occurs when a hospital capable of providing the necessary medical care transfers a patient to another facility or simply turns the patient away because of the patient's inability to pay for services. Hospitals that knowingly, willfully, or negligently fail to comply with legislation prohibiting this practice are subject to various monetary penalties as well as suspension of their Medicare provider agreements.

significantly and Medi-Cal inpatient and outpatient encounters increased significantly at almost all of general acute care hospitals near the Hospital. As a result, the number of charity care patients served has continued to decrease both at the Hospital and at many area general acute care hospitals, resulting in a sharp decline in charity care costs.

Vizient Inc. analyzed the Hospital's request to amend Condition VII. While it is based on significant declines in the service area's charity care needs, the methodology suggested may lead to inaccurate predictions of future charity care needs for the Hospital's community.

If the California Attorney General approves a recalculation of the required minimum charity care amount, Vizient Inc. recommends that the required amount be determined by a rolling average of charity care costs using available data for the time period after the implementation of the ACA. Because of the uncertainty regarding future healthcare reform and its effect on charity care, Vizient recommends using the three most recent fiscal years of data, if available. For example, for FY 2016, the Hospital would only be required to provide $1,906,545 taking an average of its charity care costs for FY 2014 and FY 2015. Additionally, for FY 2017, the Hospital would be required to provide $1,851,461, taking an average of its charity care costs for FY 2014, FY 2015, and FY 2016. This methodology provides a more accurate representation of the Hospital's community's current needs for charity healthcare. Because it uses more recent data on a rolling average basis, the required amount of charity care will be adjusted as changes occur to the ACA and the healthcare marketplace.