

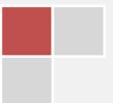


MUNICIPAL SERVICE REVIEW
AND SPHERE OF INFLUENCE STUDY

for the

Palm Drive Health Care District

FINAL REPORT



Contents

| | |
|--------------------------------------------------------------------------|----|
| I. Introduction | 1 |
| Role and Responsibility of Lafco..... | 1 |
| Purpose of a Municipal Service Review | 1 |
| Purpose of a Sphere of Influence..... | 2 |
| Organization of the MSR..... | 3 |
| Special Notes Regarding This Study..... | 4 |
| II. Agency Profile..... | 6 |
| Formation of the District..... | 6 |
| History Since Formation..... | 7 |
| District Governance, Staff, and Facilities..... | 8 |
| District Boundaries..... | 8 |
| Affected Agencies..... | 9 |
| III. Municipal Service Review Factors..... | 12 |
| Factor 1 – Growth and population..... | 12 |
| Determinations | 12 |
| Discussion..... | 12 |
| Factor 2 – Disadvantaged Unincorporated Communities | 13 |
| Determinations | 13 |
| Discussion..... | 13 |
| Factor 3 – Capacity and adequacy of public Facilities and Services | 14 |
| Determinations | 14 |
| Discussion..... | 15 |
| Factor 4 – Financial Ability to Provide Services | 18 |
| Determinations | 18 |
| Discussion..... | 19 |
| Factor 5 – Opportunities for Shared services and Facilities | 32 |
| Determinations | 33 |
| Discussion..... | 33 |
| Factor 6 – Accountability, Structure And Efficiencies | 33 |
| Determinations | 34 |
| Discussion..... | 35 |

| | |
|-----------------------------------------------------------------------------------------------------------------|----|
| Factor 7 – Commission Policy Considerations | 38 |
| Determinations | 38 |
| Discussion | 38 |
| Iv. Sphere of Influence | 39 |
| V. Attachments..... | 40 |
| 1. Sonoma LAFCO: Scope of MSR for Palm Drive Health Care District..... | 40 |
| 2. Sonoma LAFCO: Formation Resolution for Palm Drive Health Care District..... | 40 |
| 3. Palm Drive Health Care District, Financial Audit 2014/15, | 40 |
| 4. Palm Drive Health Care District, Proposed Bankruptcy Settlement Plan..... | 40 |
| 5. Coastal Valleys EMS Agency: Patient Destination/Point of Entry Policy 7007 | 40 |
| 6. Sonoma LAFCO: Financial Analysis of PDHCD (Annotated Excel Spreadsheet)..... | 40 |
| 7. North Sonoma County Healthcare District: Letter Dated May 11, 2016, Regarding Financial Information | 40 |
| 8. Sonoma LAFCO Request for Information to the District and District Response. | 40 |
| 9. MSA between the District and Sonoma West Medical Center..... | 40 |

List of Figures

| | |
|--------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|----|
| Figure 1: Palm Drive Health Care District Boundary Map | 10 |
| Figure 2: District Debt Obligations by Type..... | 19 |
| Figure 3: Bankruptcy Plan, Adjusted Debt Obligations | 20 |
| Figure 4: District Expenses Using District Projections | 22 |
| Figure 5: District Expenses Adjusted for Higher, Long-Term Hospital Subsidies | 23 |
| Figure 6: Income, Expenses and Reserves, Unadjusted | 23 |
| Figure 7: Income, Expenses and Reserves Adjusted for Higher, Long-Term Hospital Subsidies | 24 |
| Figure 8. Income, Expenses and Reserve Projections Post-Detachment (District Expense Projections with Lower Community Health Program Expenses) | 25 |
| Figure 9: Income, Expenses and Reserve Projections Post-Detachment (Adjusted for Higher, Long-Term Hospital Subsidies and Lower Community Health Program Expenses) | 26 |
| Figure 10: Available Funding for Hospital Subsidies, Post-Detachment | 27 |

I. INTRODUCTION

ROLE AND RESPONSIBILITY OF LAFCO

The Cortese-Knox-Hertzberg Local Government Reorganization Act of 2000, as amended (CKH Act) (California Government Code §§56000 et seq.), is LAFCO’s governing law and outlines the requirements for preparing Municipal Service Reviews (MSRs) for periodic Sphere of Influence (SOI) updates.

MSRs and SOIs are tools created to empower LAFCO to satisfy its legislative charge of “discouraging urban sprawl, preserving open-space and prime agricultural lands, efficiently providing government services, and encouraging the orderly formation and development of local agencies based upon local conditions and circumstances” (§56301).

CKH Act Section 56301 further establishes that “one of the objects of the commission is to make studies and to obtain and furnish information which will contribute to the logical and reasonable development of local agencies in each county and to shape the development of local agencies so as to advantageously provide for the present and future needs of each county and its communities.”

Based on that legislative charge, LAFCO serves as an arm of the State: preparing and reviewing studies and analyzing independent data to make informed, quasi-legislative decisions that guide the physical and economic development of the state (including agricultural uses) and the efficient, cost-effective, and reliable delivery of services to residents, landowners, and businesses.

While SOIs are required to be updated every five years, they are not time-bound as planning tools by the statute, but are meant to address the “probable physical boundaries and service area of a local agency” (§56076). SOIs, therefore, guide both the near-term and long-term physical and economic development of local agencies within their broader county area, and MSRs can provide the near-term and long-term time-relevant data to inform LAFCO’s SOI determinations.

PURPOSE OF A MUNICIPAL SERVICE REVIEW

As described above, MSRs are designed to equip LAFCO with relevant information and data necessary for the Commission to make informed decisions on SOIs. The CKH Act, however, gives LAFCO broad discretion in deciding how to conduct MSRs, including geographic focus, scope of study, and the identification of alternatives for improving the efficiency, cost-effectiveness, accountability, and reliability of public services.

The purpose of a MSR in general is to provide a comprehensive inventory and analysis of the services provided by local municipalities, service areas, and special districts. A MSR evaluates the structure and operation of the local municipalities, service areas, and special districts and discusses possible areas for improvement and coordination.

A MSR is intended to provide information and analysis to support a sphere of influence update. A written statement of the study's determinations must be made in the following areas:

1. Growth and population projections for the affected area.
2. The location and characteristics of any disadvantaged unincorporated communities within or contiguous to the sphere of influence.
3. Present and planned capacity of public facilities, adequacy of public services, and infrastructure needs or deficiencies including needs or deficiencies related to sewers, municipal and industrial water, and structural fire protection in any disadvantaged, unincorporated communities within or contiguous to the sphere of influence.
4. Financial ability of agencies to provide services.
5. Status of, and opportunities for, shared facilities.
6. Accountability for community service needs, including governmental structure and operational efficiencies.
7. Any other matter related to effective or efficient service delivery, as required by commission policy.

This MSR is organized according to the determinations listed above. Information regarding each of the above issue areas is provided in this document.

PURPOSE OF A SPHERE OF INFLUENCE

In 1972, LAFCOs were given the power to establish SOIs for all local agencies under their jurisdiction. As defined by the CKH Act, "sphere of influence" means "a plan for the probable physical boundaries and service area of a local agency, as determined by the commission" (§56076).

SOIs are designed to both proactively guide and respond to the need for the extension of infrastructure and delivery of municipal services to areas of emerging growth and development. Likewise, they are also designed to discourage urban sprawl and the premature conversion of agricultural and open space resources to urbanized uses.

The role of SOIs in guiding the State's growth and development was validated and strengthened in 2000 when the Legislature passed Assembly Bill (AB) 2838 (Chapter 761, Statutes of 2000). The bill was the result of two years of labor by the Commission on Local Governance for the 21st

Century, whose members and staff traveled up and down the State taking testimony from a variety of local government stakeholders.

The Commission assembled an extensive set of recommendations to the Legislature to strengthen the powers and tools of LAFCOs to promote logical and orderly growth and development and the efficient, cost-effective, and reliable delivery of public services to California's residents, businesses, landowners, and visitors.

The requirement for LAFCOs to conduct MSR was established by AB 2838 as an acknowledgment of the importance of SOIs and recognition that regular periodic updates of SOIs should be conducted on a five-year basis (§56425(g)) with the benefit of better information and data through MSRs (§56430(a)).

Pursuant to Sonoma LAFCO policy, an SOI includes an area adjacent to a jurisdiction where development might be reasonably expected to occur in the next 20 years. A MSR may be conducted prior to, or in conjunction with, the update of a SOI and can provide the foundation for updating it. Sonoma LAFCO has adopted a policy that if an agency is not seeking to amend its sphere or if the Commission determines that no change is needed, the sphere can be "confirmed" absent the preparation of an MSR.

When establishing, amending, or updating a SOI for any local agency, LAFCO is required to make five written determinations that address the following (§56425(c)):

1. The present and planned land uses in the area, including agricultural and open-space lands.
2. The present and probable need for public facilities and services in the area.
3. The present capacity of public facilities and adequacy of public services that the agency provides or is authorized to provide.
4. The existence of any social or economic communities of interest in the area if the commission determines that they are relevant to the agency.
5. For an update of an SOI of a city or special district that provides public facilities or services related to sewers, municipal and industrial water, or structural fire protection, the present and probable need for those public facilities and services of any disadvantaged unincorporated communities within the existing sphere of influence.

ORGANIZATION OF THE MSR

This MSR has been organized in a checklist format to focus the information and discussion on key issues that may be particularly relevant to the subject agency while making required MSR and SOI determinations.

The checklist questions are based on the Cortese-Knox-Hertzberg Act, the LAFCO MSR Guidelines prepared by the Governor's Office of Planning and Research, and adopted Sonoma LAFCO local policies and procedures.

This report includes:

- A description of the subject agency
- MSR determinations for public and Commission review
- Discussion that supports the MSR determinations
- Identification of any other issues that the Commission should consider

The report, in the form of a "public review draft," will be distributed to affected agencies and interested parties for comment.

SPECIAL NOTES REGARDING THIS STUDY

The current circumstances of the Palm Drive Health Care District (PDHCD or District) and, in particular, the operation of the hospital in Sebastopol by the Sonoma West Medical Center (SWMC), make an analysis of the District challenging. The hospital has only recently reopened and is being managed by a contracted operator for the first time in the District's fifteen-year history.

District representatives have opined that analyzing the operations of the hospital during a start-up phase would not paint a reasonable picture of the ongoing viability of the District's mission.

Nevertheless, Sonoma LAFCO has concluded that a narrowly-focused study of the District, which would not attempt to discern the long-term viability of the hospital operation, would be valuable not only as the Commission adjudicates an application for detachment of Russian River communities but as a foundation for other potential LAFCO actions. These actions could include sphere of influence amendments or other organizational changes to the District.

The Commission, over a series of discussions at meetings in 2015, agreed to a scope for this Municipal Service Review (Attachment 1). Notably, the scope acknowledged that some components of a typical MSR would have little or no relevance to a study of a health care district and that to comprehensively study the hospital operation itself is not within the purview of a LAFCO review.

Staff notes that there may be a plethora of issues that are pertinent to the public's evaluation of the Palm Drive Health Care District's operations and viability, particularly with regard to the likely sustainability of the hospital operation in Sebastopol. However, this MSR focuses narrowly on the District.

Finally, the Sonoma West Medical Center is clearly facing challenges in reopening the hospital and is beset with staffing changes, staff recruitment and retention challenges, and, above all else, financial difficulties. SWMC has been almost wholly reliant on financial contributions from a single donor, to begin and attempt to sustain operations.

With the acknowledgment that the situation at SWMC is very fluid, staff notes that this analysis of the District's operations and viability may very well be overtaken by near-term events. However, this analysis may form a "baseline" from which the Commission can direct further analysis as needed to support any future LAFCO determinations.

The overarching responsibility for judging the capabilities of the District to meet its stated mission and the needs of West County communities falls on District constituents and the directors they elect to represent them on the board. While the Sonoma Local Agency Formation Commission can make changes to the District's sphere of influence and otherwise amend its boundaries or even consider dissolution, more substantive changes can occur only through a partnership between the District and its public constituency.

II. AGENCY PROFILE

Palm Drive Hospital was originally established in 1941 as a private, for-profit operation. In 1998, the then-owner Columbia/HCA decided to close the hospital, and the West County Health Care Foundation was formed to preserve operations.

The Foundation conducted a fund-raising campaign to allow the community to purchase the hospital. However, it was not possible to raise sufficient funds to provide for both the operation and purchase of the building. A limited liability corporation, 35 for Palm Drive (LLC), was formed to purchase the property.

FORMATION OF THE DISTRICT

In 1999, registered voters in the area submitted a petition to LAFCO to form a health care district. A petition for the formation of a District needs to comply with the signature requirements of the principal act. The principal act for the formation of a health care district requires that 12% of the registered voters residing within the boundary of the proposed district sign the petition.

The Registrar of Voters found that, of a total of 31,083 registered voters residing within the proposed district, 3,842 verified registered voter signatures were included on the petition, slightly more than the required 12% (3,730).

The Commission approved the formation of the Palm Drive Health Care District on November 3, 1999, and called for an election (Attachment 2). The special election was held on April 11, 2000, with a ballot calling for the formation of the District as well as the approval of the bonds necessary to fund the District.

The District formation measure (Measure F) received 91.1% approval and the bond measure (Measure G) received 90.7% approval.

Although California Health and Safety Code Section 1250 and Section 32000 et seq. authorize health care districts to provide a wide variety of services, the District is only authorized to provide “emergency, acute care and other medical services.”

The appropriations limit, or the amount of funds that the District can spend, was established by the Commission’s resolution and Measure F to be \$500,000. The District has the responsibility for reviewing and reauthorizing its appropriations limit annually.

The District was officially formed on May 1, 2000, using the boundary lines of nine West County elementary school districts. School district boundaries were used to provide definite and certain established boundaries. The District encompasses approximately 200 square miles.

HISTORY SINCE FORMATION

Measure G, passed in 2000, called for the establishment of a tax levy as follows:

An election will be held in the Palm Drive Health Care District (the "District") on April 11, 2000, to authorize the sale of up to \$5,900,000 in general obligation bonds of the District to finance the acquisition of Palm Drive Hospital, make seismic safety retrofits and upgrades and the modernization, improvement, construction and renovation of health care facilities. If such bonds are authorized and sold, the principal thereof and interest thereon will be payable from the proceeds of tax levies made upon the taxable property in the District. The following information is provided in compliance with Sections 9400-9404 of the California Elections Code.

A portion of the funds from the sale of the bond was used to purchase the hospital from 35 for Palm Drive (LLC), at their cost of approximately \$2,800,000. The remainder of the funds was used to purchase a building addition for the CT scan and other capital improvements. The general obligation bond was backed by ad valorem taxes rather than a direct charge or parcel fee. The ad valorem tax rate is assessed against property values.

In 2001, the voters of the Palm Drive Health Care District were asked to approve a tax levy with Measure D:

Shall the Palm Drive Health Care District levy a special tax on each parcel within the District, not to exceed \$60.00 per parcel per year for five (5) years to ensure access to locally owned and operated community hospital services and to be used for medical services, including emergency, medical/surgery, intensive care, and outpatient services, and for no other purpose and correspondingly increase the District's appropriations limits by the revenue raised by the tax?

Measure D passed with 82.9% approval.

In 2004, the District issued Series A and Series B Notes in the amount of \$1,312,500 and \$1,300,000, respectively.

In 2005, the voters of the Palm Drive Health Care District were asked to consider another tax levy in Measure W:

To ensure survival of Palm Drive Hospital and access to local emergency, acute care, medical and physician services, and provide for ongoing expenses, repair and improvements to equipment and technology, shall Palm Drive Health Care District repeal its existing tax and levy a special tax up to \$155.00 on each taxable parcel in the District

(excluding low value parcels) while assuring independent fiscal oversight and financial accountability?

Measure W passed with 69.4% approval (2/3 approval required).

Subsequently, the District issued \$9,800,000 in Parcel Tax Revenue Bonds, the proceeds of which were used in part to pay off the outstanding 2004 notes.

In 2007, the District filed for Chapter 9 bankruptcy protection. During the course of the District's bankruptcy proceeding, it continued to make regularly scheduled 2005 bond payments, thereby avoiding default.

In 2008, the District issued a "2008 Series A" note for \$2,905,000 which was purchased by the Sonoma County Treasury. At that time, the note was secured by the District parcel tax and was part of a consensual court-approved plan to allow the District to exit Chapter 9 bankruptcy. These notes have since been repaid in full by the District.

In 2010 the District exited its first bankruptcy, using \$11 million in funds raised through issuance of Certificates of Participation, secured by parcel tax revenues.

On April 7, 2014, the District filed for Chapter 9 bankruptcy protection. In a subsequent action at its April 28, 2014, meeting, the District Board also voted to close the Palm Drive Health Care medical facilities.

On April 15, 2014, the District requested that the County provide financial assistance in the amount of up to \$1,800,000 to support the orderly wind-down of its operations. The County approved the request. The assistance is in the form of two notes purchased by the County General Fund secured by the District's parcel tax revenues through a bankruptcy court order.

DISTRICT GOVERNANCE, STAFF, AND FACILITIES

The District is governed by a five-member board, elected on staggered four-year terms. Staff includes a part-time Executive Director and one administrative position, augmented by contracted support services (e.g. legal and financial/accounting services).

District offices are located in leased space directly across from the District-owned hospital facility, located at 501 Petaluma Avenue in Sebastopol.

DISTRICT BOUNDARIES

The District serves western Sonoma County (West County), including the communities of Sebastopol, Graton, Forestville, Bodega Bay, Carmet, Salmon Creek, Jenner, Duncans Mills,

Guerneville, Occidental, Freestone, Rio Nido, Monte Rio, Guerneville Park, Summerhome Park, and Mirabel Heights (Figure 1).

PDHCD's boundaries were set using the existing boundaries of nine school districts:

- Forestville Union School District
- Gravenstein Union School District
- Guerneville School District
- Harmony Union School District
- Monte Rio Union School District
- Oak Grove Union School District
- Sebastopol Union School District
- That portion of Shoreline Unified School District within Sonoma County
- Twin Hills Union School District

AFFECTED AGENCIES

Per Government Code Section 56427, a public hearing is required to adopt, amend, or revise a sphere of influence. Notice must be provided at least 21 days in advance and mailed notice is to be provided to each affected local agency or affected County and to any interested party who has filed a written request for notice with the executive officer.

Per Government Code Section 56014, an affected local agency means any local agency whose territory overlaps with any portion of the subject agency boundary or SOI (including proposed changes to the SOI).

All affected agencies and interested parties were sent a Notice of Preparation of an MSR and, subsequently, a Notice of Availability of a Public Review Draft. Additionally, copies of the MSR were mailed to the affected agencies and interested parties and made available on the Commission's website.

The affected local agencies for this MSR are:

County and Cities:

County of Sonoma (various departments)
City of Sebastopol
County Service Areas (CSAs)
 CSA No. 40 (Fire Services), representing:
 Bodega Volunteer Fire Company
 Valley Ford Volunteer Fire Company
 Bloomfield Volunteer Fire Company
 Camp Meeker Volunteer Fire Company
 CSA No. 41 (Multi-Services)

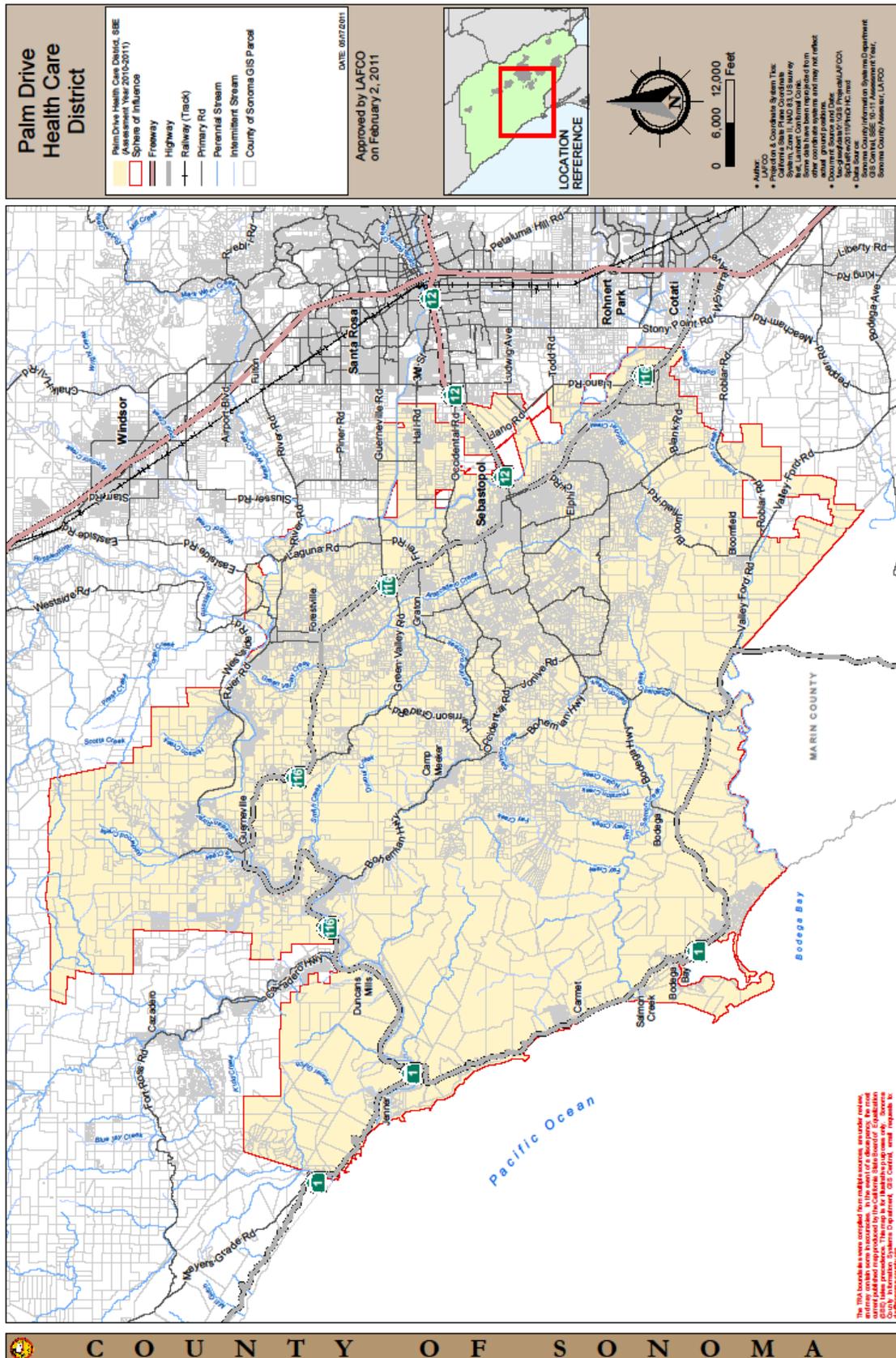
Special Districts:

Cazadero Community Services District
Graton Community Services District
Occidental Community Services District
Green Valley Cemetery District
Bodega Bay Fire Protection District
Forestville Fire Protection District
Gold Ridge Fire Protection District
Graton Fire Protection District
Monte Rio Fire Protection District
Rancho Adobe Fire Protection District
Roseland Fire Protection District
Rincon Valley Fire Protection District
Russian River Fire Protection District
Goldridge Resource Conservation District
Sonoma Resource Conservation District
Bodega Bay Public Utility District
Forestville Water District
Russian River Water District
Sweetwater Springs Water District
Camp Meeker Recreation and Park District
Russian River Recreation and Park District
Monte Rio Recreation and Park District

Multi-County Districts:

Marin-Sonoma Mosquito and Vector Control District

Figure 1: Palm Drive Health Care District Boundary Map



III. MUNICIPAL SERVICE REVIEW FACTORS

State law requires LAFCOs review and make determinations on seven factors as part of a Municipal Service Review. In each of the following factor sub-sections, a checklist notes whether the factor has relevance. Immediately following the checklist are the determinations relating to the factor, followed by discussion that supports the determinations.

FACTOR 1 – GROWTH AND POPULATION

| Growth and population projections for the affected area | YES | MAYBE | NO |
|----------------------------------------------------------------------------------------------------------------------------------------------------|-----|-------|----|
| a. Is the agency's territory or surrounding area expected to experience any significant population change or development over the next 5-10 years? | | | X |
| b. Will population changes have an impact on the subject agency's service needs and demands? | | | X |
| c. Will projected growth require a change in the agency's service boundary? | | | X |

Determinations

- The growth and population projections for the area served by the District do not significantly impact the District's ability to provide health care services through its traditional model (operation of an acute care hospital with emergency room capabilities).
- Potential increases in difficult-to-serve and underserved populations (elderly residents, and under- or uninsured) may impede the ability of the hospital operation to maintain financial viability and, in turn, the ability of the District to meet its mission through that service model.

Discussion

The West County region served by the District includes only one incorporated city (Sebastopol), and both it and the remaining unincorporated areas are expected to have little growth in the future due to land use restrictions and lack of municipal infrastructure (water and sewer).

Further, population growth has not and is not expected to necessarily drive use of the health care services at the hospital that the District subsidizes. Over 75% of County residents access health care services through insurers and major health care providers not aligned with the four regional hospitals associated with a health care district (Sonoma Valley, Healdsburg, Petaluma, and SWMC).

The composition of both existing and future populations in the West County may be more predictive of the health care service needs that might need to be supported by the District – notably the proportion of difficult-to-serve and under- or uninsured residents. These populations require high levels of service, and government-sponsored insurance and grant programs do not fully cover the costs of providing for these needs.

Rather than population growth resulting in a need for PDHCD to increase its ability to provide services, the District has determined that attracting business from out-of-area residents is important to sustain the financial condition of the hospital operation.

The District has no plans to seek an expansion of its territory or sphere of influence due to projected growth.

FACTOR 2 – DISADVANTAGED UNINCORPORATED COMMUNITIES

| The location and characteristics of any disadvantaged unincorporated communities within or contiguous to the sphere of influence. | YES | MAYBE | NO |
|----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|-----|-------|----|
| a. Does the subject agency provide public services related to sewers, municipal and industrial water, or structural fire protection? | | | X |
| b. Are there any “inhabited unincorporated communities” (per adopted Commission policy) within or adjacent to the subject agency’s sphere of influence that are considered “disadvantaged” (80% or less of the statewide median household income)? | X | | |
| c. If “yes” to both a) and b), it is feasible for the agency to be reorganized such that it can extend service to the disadvantaged unincorporated community? (If “no” to either a) or b), this question may be skipped.) | | | |

Determinations

- While the District is nominally providing health care services to two disadvantaged unincorporated communities that are within its service territory, because health care services are not considered to be “municipal,” the dictates of SB 244 do not apply.

Discussion

Senate Bill (SB) 244 (Chapter 513, Statutes of 2011) made changes to the CKH Act related to “disadvantaged unincorporated communities” (DUCs). A DUC is inhabited territory containing 12 or more registered voters where the annual median household income is less than 80 percent of the statewide annual median household income.

DUCs are recognized as social and economic communities of interest for purposes of recommending SOI determinations pursuant to Section 56425(c). In particular, SB 244 regulates how municipal services (i.e., water, sewer, emergency services, etc.) are provided to DUCs.

PDHCD does not provide municipal services that may trigger the provisions of SB 244 and a subsequent LAFCO determination regarding any disadvantaged unincorporated communities within or adjacent to the agency's sphere of influence.

It is otherwise noted that two Disadvantaged Unincorporated Communities are located within the boundary of the District. These communities are Guerneville and Monte Rio. Additionally, Cazadero, also classified as a DUC, is adjacent to the District's boundary to the northwest.

FACTOR 3 – CAPACITY AND ADEQUACY OF PUBLIC FACILITIES AND SERVICES

| Present and planned capacity of public facilities, adequacy of public services, and infrastructure needs or deficiencies including needs or deficiencies related to sewers, municipal and industrial water, and structural fire protection in any disadvantaged, unincorporated communities within or contiguous to the sphere of influence. | YES | MAYBE | NO |
|----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|-----|-------|----|
| a. Are there any deficiencies in agency capacity to meet service needs of existing development within its existing territory? | | | X |
| b. Are there any issues regarding the agency's capacity to meet the service demand of reasonably foreseeable future growth? | | | X |
| c. Are there any concerns regarding public services provided by the agency being considered adequate? | X | | |
| d. Are there any significant infrastructure needs or deficiencies to be addressed? | | | X |
| e. Are there changes in state regulations on the horizon that will require significant facility and/or infrastructure upgrades? | | X | |
| f. Are there any service needs or deficiencies for disadvantaged unincorporated communities related to sewers, municipal and industrial water, and structural fire protection within or contiguous to the agency's sphere of influence? | | | X |

Determinations

- PDHCD has had difficulty meeting what the District considers its primary mission: supporting a viable and sustainable hospital with emergency services for the West County area.

- The necessity of providing acute care and emergency care services is tenuous, given the protocols for patient destination/point of entry issued by the Coastal Valleys Emergency Medical Services (EMS) Agency and the healthcare services landscape in the County.
- The District is advised to at least consider other service models as a contingency exercise, should the hospital/emergency room focus becomes unsustainable.
- Options for continued support of West County communities might include other medical services such as:
 - Urgent care clinic(s)
 - Community health clinic(s)
 - Other community health initiatives
 - Funding of ambulance or other emergency response services (providing or subsidizing these services would require exercise of the District's latent powers, subject to approval by LAFCO)

Discussion

As discussed in the review of population growth, the capacity of the District to provide acute, emergency, and other medical services to the West County area is not being driven by development or population, but rather by demographics and the choices residents and visitors make regarding where they seek medical services.

The capacity of the District to meet service needs adequately can be evaluated on two criteria: the District's selection of which services to offer and in what fashion. In particular, is the District's sole focus on supporting a hospital with emergency room functions an appropriate one, given its financial resources and the policies that drive the use of emergency rooms in the County?

To be sure, the genesis of the District was driven by very strong community support in 2000 to reopen Palm Drive Hospital and, in particular, to preserve emergency room capability, and the District has consistently held that as its primary mission throughout its decade-and-a-half existence.

Nevertheless, the District has had difficulty in meeting this "primary mission" and, with its funding resources reduced due to debt obligations and resolution of a pending bankruptcy filing, it can be asserted that meeting this mission will be more difficult in the near-term (see the following section).

Emergency Room Services

There has been discussion within the West County community, both in the Russian River area and more broadly, regarding the necessity of maintaining an emergency room capability at the hospital. In part, this discussion has been triggered by the opening of Sutter Regional Hospital at River Road and Highway 101 and, in part, due to the tenuous financial condition of SWMC.

Some of these discussions have centered on claims regarding which hospital emergency room (Sutter or SWMC) is closest for a given community, and there is evidence that Sutter is somewhat closer in travel time than SWMC for portions of the Russian River area communities.

Basing these discussions solely on geographical proximity fails to acknowledge two issues:

- For the vast majority of transports to emergency rooms, the patient chooses the facility to which he or she is taken.
- There are other predictors of emergency response success, including response time and capabilities of first responders.

Note: At the direction of the Commission, an addendum has been attached to this report describing the licensing and certification of SWMC's emergency room operations and how the availability of services is reported.

Directing Emergency Transports

The Coastal Valleys EMS Agency has the responsibility of assigning and managing emergency medical response agencies and has adopted the "Patient Destination/Point of Entry" protocol that describes how patients are transported and directed to local area hospital emergency rooms.

When a patient's condition is unstable or life threatening, the protocol indicates that the patient should be transported to the "closest appropriate hospital." However, several other factors may be considered in determining the patient's destination, including patient or family member request, or the patient's physician's preference or request.

There are also extensive protocols for directing major trauma patients (for half hour or shorter transports, to Santa Rosa Memorial), pediatric trauma patients (by helicopter to Oakland) and other types of trauma patients.

In practice, the majority of transports are directed by patients, generally to Sutter, Kaiser, or Memorial.

SWMC has accepted emergency patients since its reopening in 2015, and having emergency capabilities is certainly of some benefit to the West County community. However, SWMC's emergency capabilities are somewhat limited in that the hospital operates a "Standby" facility, and has had an intensive care unit that has been open intermittently. (A "Standby" emergency

room indicates that doctors and other technicians are not staffing the emergency room full time but are available “on call.”)

Emergency service providers in the coastal areas of West County (notably the Bodega Bay Fire Protection District) value having the ability to direct patient transports to SWMC because the patient admitting process can be much shorter than at the three major hospitals (Kaiser, Memorial, and Sutter), allowing crews to return to the coast to resume coverage more quickly.

PDHCD also notes that the hospital in Sebastopol is the only major medical facility in the County west of Highway 101 with emergency room capability, perhaps making it critically important in the event of a region-wide disaster such as a major earthquake.

Fundamentally, patients who have a doctor/health plan/facility relationship with SWMC or have no health care plan affiliation (i.e., uninsured, or from outside of the region/state/country) are most likely to access emergency services at SWMC. Otherwise, patients with serious trauma or who have doctor/health plan/facility relationships with the three major hospitals in the County, are very unlikely to use SWMC.

With the Coastal Valley EMS Agency protocols in mind, it becomes clear that patient proximity is only one factor in the decision by patients and emergency response providers to choose to access emergency services at the hospital in Sebastopol.

Predictors of Emergency Success: Proximity, Availability, and Capability of First Responders

The public generally equates the availability of emergency room access as the most important factor in predicting the outcome of emergency medical calls. This viewpoint would clearly indicate that having emergency room services at the hospital in Sebastopol would be of primary importance.

It should be noted that at least three other important predictors of the success of emergency services provision are the availability, proximity, and capabilities of first responders.

In simplistic terms, it is perhaps less important how long it takes to get to hospital emergency services compared to the time it takes for first responders to get to patients in the first place. First responders often point out that they convert “incidents” into “patients.”

This assertion by no means diminishes the relative importance of having emergency room services available in the West County, but it may provide a better context for evaluating what mix of “acute, emergency, and other medical services” PDHCD might consider providing or subsidizing now and in the future.

FACTOR 4 – FINANCIAL ABILITY TO PROVIDE SERVICES

| Financial ability of agencies to provide services | YES | MAYBE | NO |
|------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|-----|-------|----|
| Does the organization routinely engage in budgeting practices that may indicate poor financial management, such as overspending its revenues, failing to conduct commission independent audits, or adopting its budget late? | | X | |
| Is the organization lacking adequate reserve to protect against unexpected events or upcoming significant costs? | X | | |
| Is the organization's rate/fee schedule insufficient to fund an adequate level of service, and/or is the fee inconsistent with the schedules of similar service organizations? | | | X |
| Is the organization unable to fund necessary infrastructure maintenance, replacement and/or any needed expansion? | | X | |
| Is the organization lacking financial policies that ensure its continued financial accountability and stability? | X | | |
| Is the organization's debt at an unmanageable level? | | X | |

Determinations

- The District has proposed a bankruptcy plan to the court and creditors; if the plan is approved, the District will pay on the order of \$800,000 per year to creditors over the next seven years, and some debt will be restructured.
- If the District's bankruptcy plan is approved, the District will have just over \$1 million per year for the seven-year period to devote to hospital subsidies and community health programs. If the District continues to consider hospital subsidy payments a priority, it will likely be unable to support additional expansion of community health services during the bankruptcy repayment period.
- In overarching terms, during the bankruptcy repayment period, the District will be devoting on the order of three quarters of its revenue to debt payments, with only a quarter available to meet its mission.
- The District is facing the potential detachment of Russian River area communities. Although landowners in the detachment area would still pay their portion of the debt burden of the District if detachment is granted by LAFCO (including bankruptcy plan payments), the District would experience a decrease of about 40% of revenue that can be devoted to non-debt purposes (i.e. District operation costs and financial contributions to the hospital and community health initiatives).

- If detachment of the Russian River communities is granted, the District would need to identify new funding sources, seek additional debt financing, identify expense cuts, or some combination thereof if it wishes to provide the planned subsidies to the hospital. The District would otherwise be unable to provide full, planned subsidies beginning as early as 2018.
- The District retains the authority to seek additional revenue from the community, to support hospital subsidies or other public health programs, by proposing a raise in the parcel tax amount, which would have to be authorized by voters. The District also has the right to seek additional debt financing, using the hospital facility and/or future tax revenues as collateral, although loan terms would very likely be quite onerous given the existing debt burden and the lack of a credit rating for the District.
- The District should consider preparing capital plans for the hospital facility and for equipment to better predict the need for subsidies to the existing or future hospital operator and should consider retaining direct responsibility and oversight of funding devoted to these expense categories.

Discussion

Financial Ability: Overview

The analyses of the District's financial circumstances presented here applies a framework of predicting District income, debt service obligations and District operating expenses, and subsequently determining what remaining financial resources the District can expect to have to support the District's mission.

District financial reports are the foundation of the analysis; in particular, the audited financial results for the District in 2014 and 2015 and the District's proposed bankruptcy settlement plan.

*Note: The District's proposed bankruptcy settlement plan has **since been withdrawn**, and subsequent negotiations with creditors are taking place. However, for the purposes of this review, the settlement plan represents a valid proxy for how the bankruptcy payments will affect District finances, and the other budgetary projections in the plan remain valid.*

This section also attempts to identify relevant risks to the financial viability of the District, where appropriate, to examine alternative scenarios to predict potential outcomes if these risks come to pass, and to suggest actions the District could take to ameliorate their effects.

District Income: Tax Receipts

The District revenue figures presented later in the financial analysis are taken from District projections and include a transfer of reserve funds to the revenue account in 2016 of \$2.3

million. Tax revenues are very predictable given that they are parcel tax-based rather than property tax-based (which would fluctuate based on property value assessments).

If the District identifies that additional revenue is required to meet its mission, with the priorities that it has decided to pursue, it would be advisable to weigh seeking an increase in the parcel tax assessment compared to seeking additional debt financing. Seeking a parcel tax increase has the advantage of allowing District residents to directly indicate their support or lack of same for the priorities that the District board has chosen.

Pre-Bankruptcy District Debt

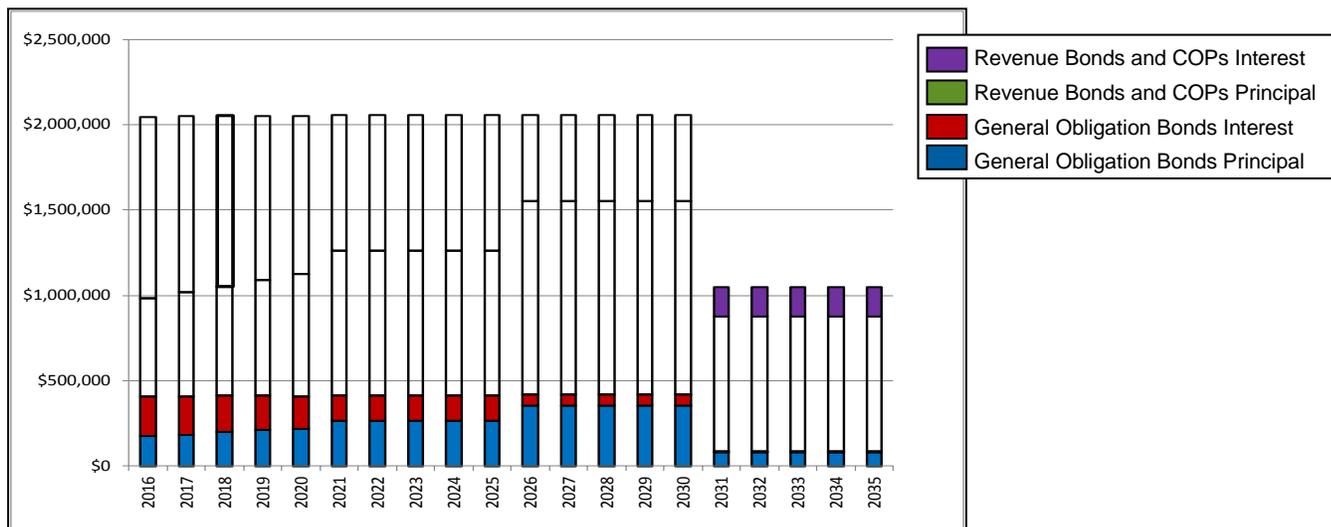
The District has three sets of debt obligations:

- General obligation bonds that were encumbered in 2000 (to purchase the hospital from a citizens group that had secured it in hopes of forming a health care district to reopen the facility)
- Parcel tax revenue bonds issued in 2005 (future parcel tax receipts are pledged to pay the debt service)
- Parcel tax “Certificates of Participation” (COPs) issued in 2010 (again, future parcel tax revenues are pledged to pay the debt service; a portfolio of bonds was issued with varying maturities and interest rates)

According to the District’s financial audit conducted for 2014 and 2015, the three classes of debt incurred by the District total \$20,800,000. The District also entered into capital leases for equipment with short-term maturity dates, in the amount of just over \$1,800,000. These obligations are included in the District’s bankruptcy filing.

Figure 2 projects the current debt service obligations of the District through 2035.

Figure 2: District Debt Obligations by Type



It should be noted that the debt service payments are structured so as to be very consistent, with payments of approximately \$2,055,000 annually through 2030, followed by payments of approximately \$1,047,000 per year for five years beginning in 2031.

As part of Assembly Bill 582, which passed in June 2014 and was specifically directed at PDHCD, the District was granted the authority to refinance debt, while at the same time providing a “statutory lien” against future tax revenue to secure the debts.

The District has not refinanced debts, and, due to reporting lapses, has forfeited a bond rating that would enable it to do so now. The current bankruptcy also precludes the possibility of refinancing or restructuring debt.

With debt financing at 7.5% and 5% (depending on issuance) and current bond rates significantly lower, it is unfortunate that the District did not restructure existing debt, which would have resulted in lower payments and therefore more funding available to support the District’s ongoing mission.

Bankruptcy Settlement Plan

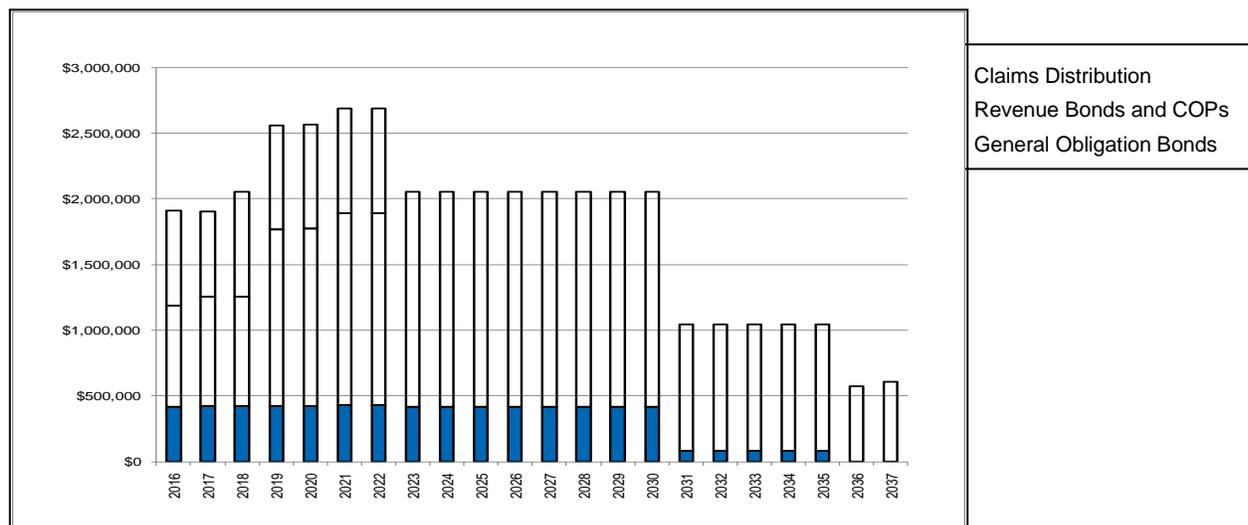
The District has filed a bankruptcy settlement plan with the court and is seeking acceptance of the plan by seven classes of creditors. It is reasonable to conclude that the plan represents the minimum that the District will be ordered to pay as a settlement; there is some risk that one or more creditor classes will not accept the plan or that the court may impose a more costly settlement.

The District’s bankruptcy plan treats each creditor class differently and includes write-offs of owed amounts, varying payment schedules over a seven-year period, and restructuring of some

existing debt (including a short-term freeze on payments of some principal and interest and an extension of debt service payments to “out” years).

For the purposes of the financial analysis prepared for this report, the District’s bankruptcy settlement plan has been used to project bankruptcy payments as well as payments for

Figure 3 Bankruptcy Plan, Adjusted Debt Obligations



restructured debt. As noted above, these projections are a “floor” – if there is a risk, it is that the ordered bankruptcy payments will be higher or that the payment terms would be shorter.

Figure 3 illustrates the District’s debt structure if the bankruptcy plan is approved.

Potential Increase in Debt

The District has not indicated that it is considering issuing new debt that might be secured against real assets (the hospital facility) or future tax income. A number of residents of the District are concerned that the District may seek additional debt financing in the future, encumbering constituents with additional long-term debt payments.

While the current District board cannot be expected to rule out seeking additional debt financing in the future, or to preclude a future board from doing so, the District might consider adopting a policy describing potential avenues for seeking additional debt financing and under what conditions the District might consider that option.

District Operation Costs

District operation costs include administrative staff costs and costs for conducting District business, including consulting fees for legal and financial services.

The District has proposed an operational cost budget through 2022 in its bankruptcy settlement proposal. For the financial analysis presented here, the annual District operation budget of \$350,000 in 2022 has been projected through 2035 with an escalation rate of 3%. This projection assumes that the District has appropriately budgeted for staffing and administration costs, including long-term employee obligations such as retirement and health care obligations.

It should be noted that the District's operation costs through 2020 are quite high due to projected costs for legal and accounting services support, nominally due to bankruptcy-related activities. Beginning in 2021, District operation costs return to a nominal level to support ongoing staff functions.

Health Care Funding

The District has traditionally devoted all remaining financial resources, after debt payments and District operation costs, to subsidies for the hospital operation but, since 2015, provides a modest subsidy to a community health program in the Russian River area. The District is also proposing to fund additional community health programs.

For the financial analysis presented here, the health care funding levels presented in the District's bankruptcy settlement plan are used through 2022. Interestingly, the District projects funding levels of \$1 million per year for the hospital through 2020, then \$500,000 per year thereafter. We have conducted financial projections using the District's projections (reflected in Figure 4) but also have run an analysis with \$1 million per year in hospital subsidies through the entire study period, reflected in Figure 5.

For funding for community health programs, our analysis uses the District's projections through 2022, then applies a 3% annual escalation factor for out years.

Summary of District Expenses Analysis

Figure 4 illustrates the totality of projected District expenses through the study period based on the projections made in the bankruptcy settlement filing, including:

- Debt servicing and bankruptcy settlement payments
- District expenses
- Hospital subsidy payments (which decrease from \$1 million per year to \$500,000 per year beginning in 2021)
- Community health program expenses

Figure 4 – District Expenses Using District Projections

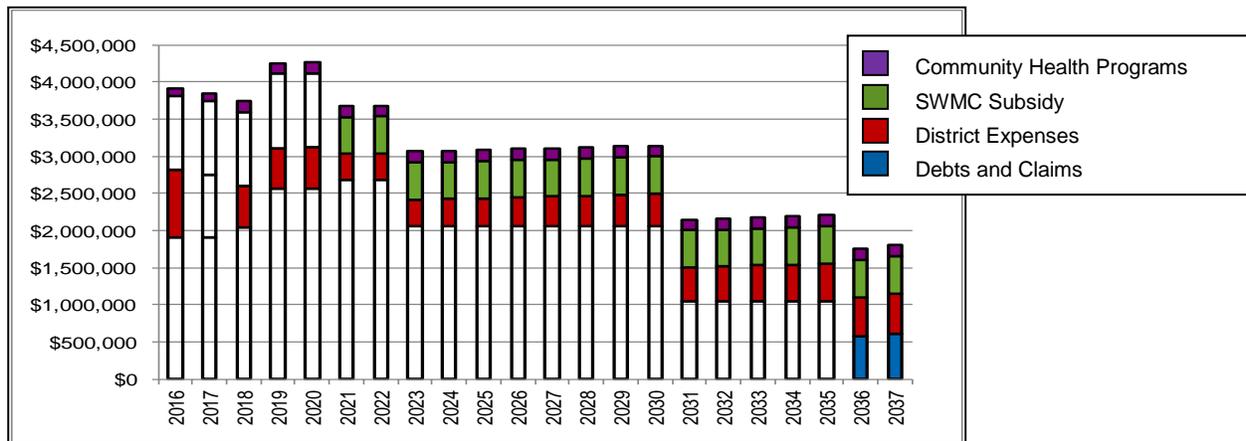
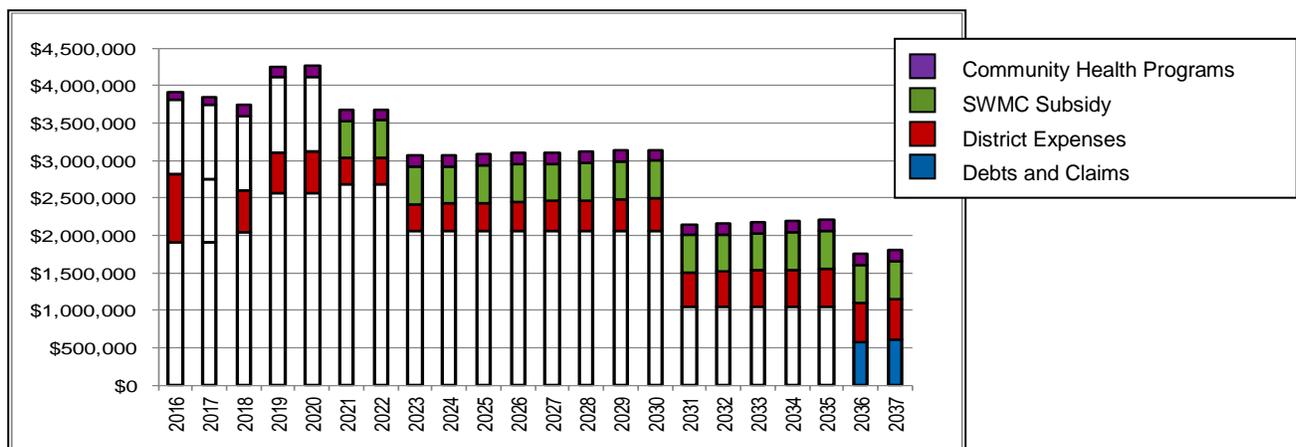


Figure 5 simply adjusts these projections by assuming that the District will continue to subsidize the hospital operation at \$1 million per year throughout the study period.

Figure 5: District Expenses Adjusted for Higher Long-Term Hospital Subsidies



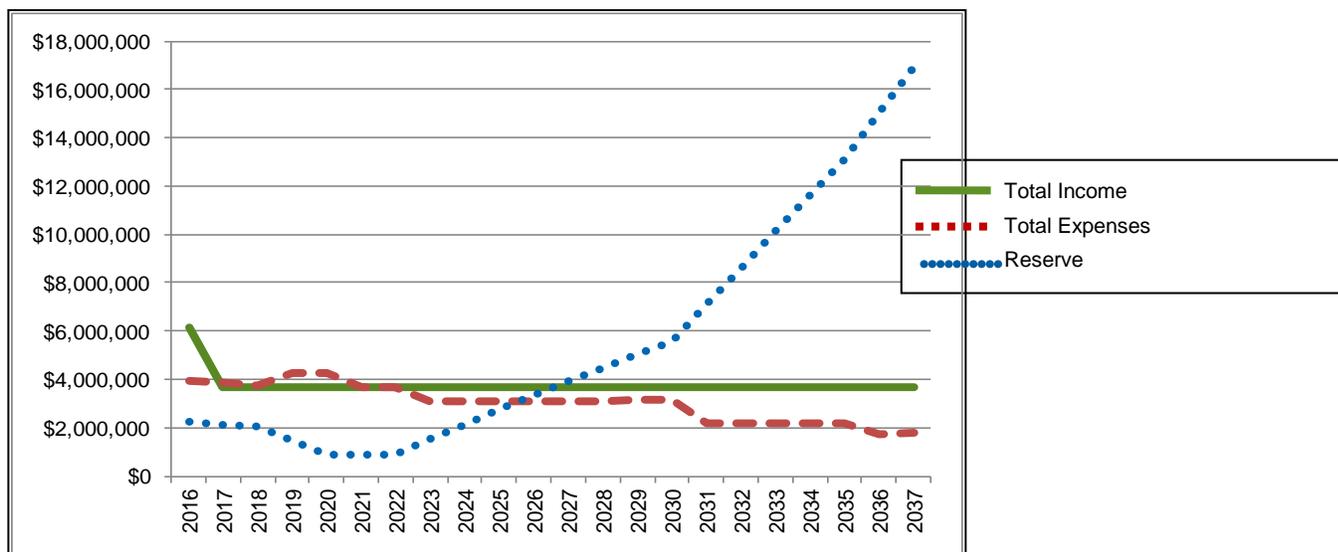
Income vs. Expenses and Reserves: District Projections

For the final graphs showing the overall financial projection for the District, we have plotted District revenue and predicted resultant reserve levels. The definition of “reserve” for this analysis differs from that typically used by the District. The District considers funds available after paying District expenses (debt payments, and District operations) to be “reserves,” which can then be used to supplement hospital operations.

For this analysis, projected payments to the hospital are considered expenses, and therefore “reserves” represent amounts left over, if any, after paying for all District expenses. The reserve figures indicate whether the District is able to “stay ahead” of expenses over time.

Figure 6 shows the revenue and expense comparison and resultant reserve levels based on unadjusted projections from the District.

Figure 6: Income, Expenses, and Reserves, Unadjusted



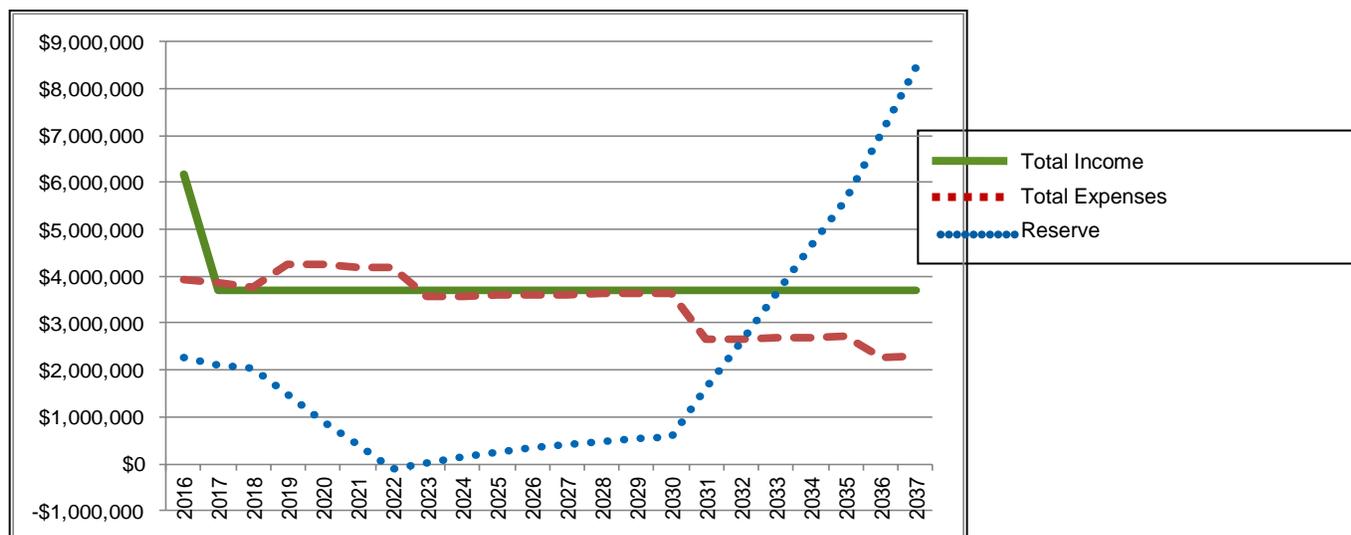
There are several items to note about these resulting projections:

- The bankruptcy settlement plan, combined with the transfer of \$2.3 million from reserves made in 2016, enables the District to meet its projected payment stream of \$1 million per year for hospital operations over the next five years (although expenses exceed income for 2017 through 2020).
- District reserves decline to just below \$900,000 in 2020, 2021, and 2022.
- District reserves then recover significantly and climb at a high rate when debt service payments drop dramatically beginning in 2031.

Income vs. Expenses and Reserve: Alternate Scenario

Our “alternative” analysis, which simply considers an ongoing subsidy of \$1 million to the hospital throughout the study period, results in the projections shown in Figure 7.

Figure 7: Income, Expenses and Reserves Adjusted for Higher, Long-Term Hospital Subsidies



The “takeaway” from this set of projections is that the District would have higher expenses than income beginning next year through 2022; reserves would decline precipitously, falling to \$500,000 or below for an eight-year period beginning in 2021 (and actually going negative in 2022). Reserve levels don’t recover appreciably until 2031.

Impact of Detachment of Russian River Area Communities

Other than the overarching concern regarding the financial stability and viability of the hospital operation, which is discussed in the following section, the other significant risk to the District is the potential detachment of Russian River area communities.

An application for detachment of the Monte Rio, Guerneville, and Forestville Union School District areas from the District has been filed with LAFCO and will be considered beginning in September 2016.

It should be noted that, if any areas are detached from the District, property owners within those areas will remain responsible for a portion of the debts incurred by the District prior to the detachment.

Nevertheless, detachment of any areas from the District will result in a loss of funding that could be devoted to a hospital subsidy or other expenditures which the District would like to make in support of its mission.

For our financial analysis of the Russian River area detachment, the income, expense, and reserve projections are repeated under the two scenarios (one with District projections for hospital subsidies, the other with a \$1 million per year subsidy throughout the projection period).

It should be noted that we also reduced projected expenses for community health programs to a nominal level (\$25,000 per year throughout the projection period). The District has indicated that it expects community program expenditures to be directed almost solely to the Russian River area, and that if that area were to detach from the District, the District would no longer pursue those initiatives.

The District has offered some funding support for programs in other communities, such as support for equipment purchases by the Bodega Bay Fire District. Funding for these efforts doesn't appear to be accounted for in the District's expense projections and is not accounted for in our analyses.

Figure 8: Income, Expenses and Reserve Projections Post-Detachment (District Expense Projections with Lower Community Health Program Expenses)

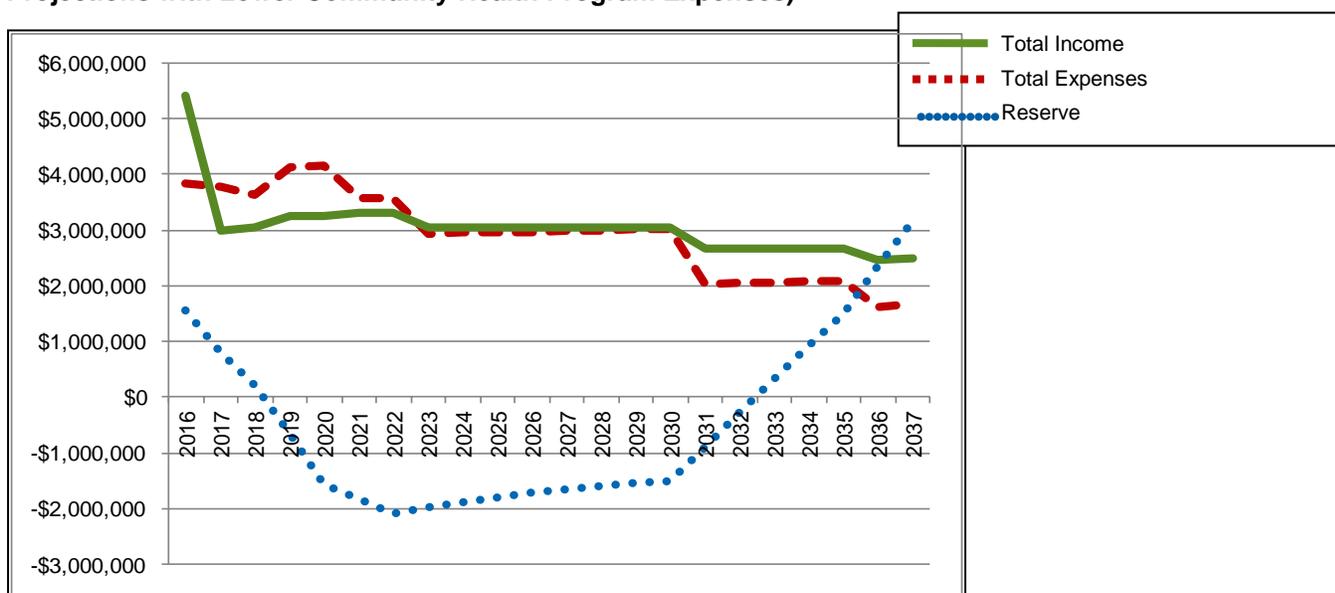


Figure 8 summarizes the projected fiscal conditions for the District if the Russian River area communities are detached.

The significant reduction in tax receipts that would occur post-detachment would preclude the District from providing subsidies for hospital operations at the levels projected by the District, beginning in 2018, when reserves would fall to zero.

During this period the District would have to consider securing additional sources of revenue (e.g., an increase in the parcel tax assessment or further debt financing) or would have to cut the projected subsidy level to the hospital.

It should be reiterated that the District would not become insolvent in the event of detachment – it simply wouldn't have the resources to devote to hospital subsidies as planned.

Beginning in 2023, the District would again have sufficient resources to make projected hospital subsidy payments (at the projected rate of \$500,000 per year), on a cash flow basis.

Post-detachment, the District would be unable to sustain continued annual subsidy payments of \$1 million per year but could once again be able to do so in 2031, as shown in Figure 9.

Figure 9: Income, Expenses and Reserve Projections Post-Detachment (Adjusted for Higher, Long-Term Hospital Subsidies and Lower Community Health Program Expenses)

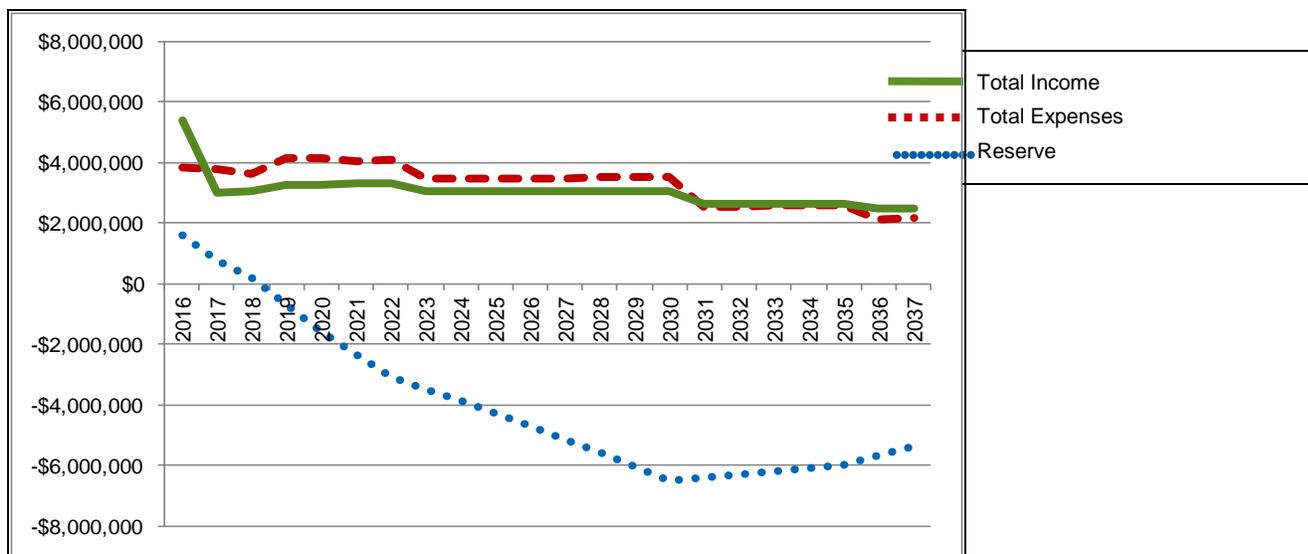
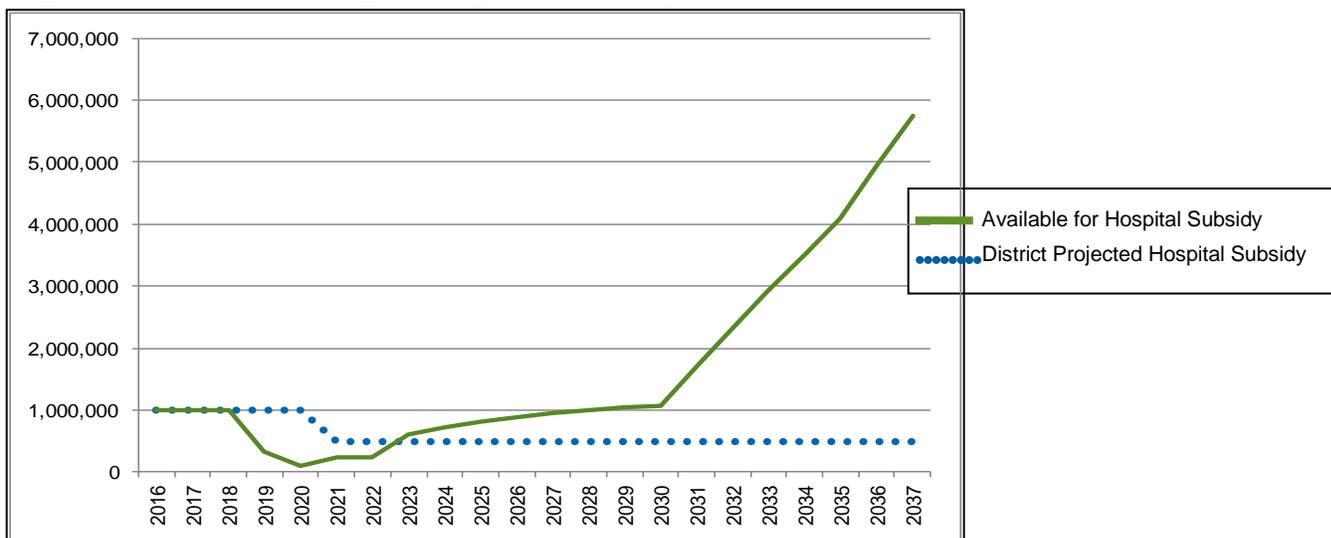


Figure 10 shows the availability of funding that could be devoted to hospital operation subsidies, compared to the District's projected funding levels, and perhaps better illustrate the preceding discussion.

The District would be substantially impacted by a detachment of the Russian River area communities, precluding it from providing subsidies to the hospital at the levels it projects in its bankruptcy settlement plan, beginning in 2018. The District would remain solvent and could also identify new revenues, debt financing, reductions in expenses, or some combination thereof, that would allow it to fund hospital subsidies at higher levels.

Figure 10: Available Funding for Hospital Subsidies, Post-Detachment



Is Subsidy of Hospital “Sufficient” to Ensure Sustainability?

The District, historically and as a matter of policy, believes that, to fulfill its mission, it must support a hospital that provides acute and emergency care in the West County.

Under its Management and Staffing Services Agreement (Agreement or MSA) with SWMC, the District has committed to augmenting hospital revenue with \$1 million per year from annual District tax revenues, for five years, subject to the availability of funds.

The subsidy funds, according to the MSA, are to be used for repair and maintenance of the hospital property, purchase and repair of medical equipment, and subsidies for charity care and programs that benefit the community.

A fundamental question related to the sustainability of the District is whether there is and will be availability of District tax revenue to fund the agreed-to subsidy. Additionally, if it is agreed that supporting a hospital that provides acute and emergency care is the primary mission of the District, will the subsidy result in the sustainable operation of the hospital?

Even with a comprehensive analysis of SWMC’s initial operational and financial circumstances (which can be gleaned from monthly financial reports that SWMC is obligated to provide to the District under the terms of the MSA), as well as a critique of SWMC’s Business Plan, it would be difficult to provide a definitive assessment of the sustainability of the hospital operation under SWMC (or other operator) management.

Suffice it to say that SWMC has relied on millions of dollars in donations and/or loans to underwrite the re-opening of the hospital and continues to experience significant difficulties with cash flow and outright financial losses that have been as high as \$800,000 per month or more.

Sonoma LAFCO has therefore chosen to focus primarily on the first question: Can the District provide the agreed-to subsidy to the hospital operator? Our financial analysis, based on District financial reports, provides a basis for answering this question under a variety of scenarios.

Nevertheless, LAFCO staff proposes two recommendations that would help the District evaluate the “sufficiency” of the subsidy payments: completing a facility capital and expense plan and developing a medical equipment acquisition and maintenance plan. Prudent assessments of both of these cost categories might yield a better understanding of whether the annual subsidy amount will be sufficient to cover these two (of three) cost categories.

Facilities and Equipment Plans, and Authority

A facilities plan is an assessment of the condition of the hospital facility, with projections for maintenance and replacement activities over a reasonable time horizon (generally at least ten years).

Assessments of this type would yield an annualized acquisition and maintenance budget, with a reserve account for anticipated major repairs. Simply stated, the budget would cover regular ongoing maintenance activities (i.e. utility service payments, maintenance of heating, ventilation, and air conditioning equipment, etc.) as well as anticipated costs for major repairs (i.e. roof replacement, mandated seismic upgrades, etc.).

The District undertook an initial assessment of the hospital facility in 2013, with preliminary results identifying investment requirements of \$15.3 million for the first five years and an additional \$5 million in the following three years. However, these estimates were both preliminary and included many options for selecting capital projects.

It should also be noted that the District (and SWMC) have made some investments in the hospital facility in order to reopen in late 2015. At present, the District relies on SWMC to propose capital improvement projects.

The District does not apparently have a medical equipment acquisition and maintenance plan over a similar timeframe, and also relies on SWMC to propose equipment purchases. Given that the hospital facility and medical equipment are the District’s sole assets and would conceivably be offered to another healthcare management operator in the event of failure of SWMC, it would be prudent for the District to retain sole responsibility for the maintenance and expenditures that support these assets.

LAFCO recommends that the District consider renegotiating the MSA with SWMC (or negotiate a different arrangement if a new hospital operator is engaged), reclaiming authority for property management and management of medical equipment, rather than ceding this authority per the current agreement (Article 2.2 f).

Subsidy Comparison to Other Sonoma HCDs

Contextually, LAFCO staff analyzed the other three health care districts in Sonoma County to determine how much tax revenue support is provided to Healdsburg District Hospital, Sonoma Valley Hospital, and Petaluma Valley Hospital and how those levels of support compare with the support Palm Drive Health Care District will nominally provide to SWMC or another hospital operator. Table 1 summarizes these findings.

Table 1: Comparative Subsidy Rates for Sonoma County Health Care Districts

| District | Hospital | Annual Net Revenue* of Hospital | Tax Subsidy | Percent | Notes |
|-----------------------------------------|------------------------------|---------------------------------|------------------------|--------------|---------------------------------------------------------------------------|
| Petaluma Health Care District | Petaluma Valley Hospital | Unknown | \$0 | 0 | District does not levy taxes and receives payments from hospital operator |
| North Sonoma County Healthcare District | Healdsburg District Hospital | \$40,210,165 | \$3,357,254 | 8.3% | Data from audited financial statements, 2015 |
| Sonoma Valley Healthcare District | Sonoma Valley Hospital | \$51,394,060 | \$6,034,710 | 11.7% | Data from audited financial statements, 2015 |
| Palm Drive Health Care District | Sonoma West Medical Center | \$27,488,000 | (up to) \$1,000,000 | (up to) 3.6% | Revenue from audited financial statement of Palm Drive Hospital, 2013 |

*"Net Revenue" is a measure of the actual revenue received from insurers, patients, and other sources, rather than the amount billed to patients and insurers. Net revenue is typically less than half of billed "revenue."

Petaluma Health Care District

Petaluma Healthcare District is anomalous, in that the District leases its hospital facilities and equipment to a healthcare operator and receives annual lease payments. The District does not assess tax levies of any kind and uses lease payments and other sources of revenue (e.g., grants) to fund community health initiatives.

The District may be in a position to maintain this fortuitous arrangement due to the underlying circumstances of location: residents of Petaluma may use services at Petaluma Valley Hospital at a somewhat higher rate than the other community hospitals in the County because other

options are located further away (Santa Rosa, Marin), although Kaiser Permanent offers non-emergency services at its Petaluma facility.

North Sonoma County Healthcare District

North Sonoma County Healthcare District operates Healdsburg District Hospital, and a parcel tax levied in the District provides over eight percent of the net revenues of the operation. According to the District’s CEO, Nancy Schmid, the subsidy is crucial to the viability of the hospital.

A small group of residents in Windsor filed a notice of intent to circulate a petition in Windsor to support a detachment application in 2015, but that effort has been abandoned.

Sonoma Valley Healthcare District

The District has been running consistent operational deficits in recent years on the order of \$4 million annually, and financial reports acknowledge that the District’s tax revenues are crucial for ongoing viability and sustainability.

Palm Drive Health Care District

The District has been able to provide operating subsidies to the hospital (when operated by the District) approaching \$2 million annually but has now committed to providing SWMC a subsidy of as much as \$1 million per year, subject to the ability of the District to fund that amount. For this contextual comparison, the net revenue for the hospital uses the audited financial results for the hospital in 2013, when it was operated by the District. If SWMC or another hospital operator has similar annual net revenue, the District’s subsidy is proportionally less than half that of North Sonoma County HCD’s and less than a third of Sonoma Valley HCD’s contributions.

FACTOR 5 – OPPORTUNITIES FOR SHARED SERVICES AND FACILITIES

| Status of, and opportunities for, shared facilities. | YES | MAYBE | NO |
|--------------------------------------------------------------------------------------------------------------------------------------------------------------------------|-----|-------|----|
| a. Is the agency currently sharing services or facilities with other organizations? If so, describe the status of such efforts. | | | X |
| b. Are there any opportunities for the organization to share services or facilities with neighboring or overlapping organizations that are not currently being utilized? | | | X |
| c. Are there any governance options that may produce economies of scale and/or improve buying power in order to reduce costs? | | | X |
| Status of, and opportunities for, shared facilities. | YES | MAYBE | NO |
| d. Are there governance options to allow appropriate facilities and/or | | | X |

| | | | |
|--------------------------------------------------------------------------------------------------------------------------------------------------------------------------|--|--|--|
| resources to be shared, or making excess capacity available to others, and avoid construction of extra or unnecessary infrastructure or eliminate duplicative resources? | | | |
|--------------------------------------------------------------------------------------------------------------------------------------------------------------------------|--|--|--|

Determinations

- PDHCD has no apparent opportunities for shared services for District operations.

Discussion

Because the District has opted to secure a contracted operator of the hospital, there are no apparent opportunities for the District proper to seek shared services arrangements.

(The hospital operator may benefit from partnerships with other regional hospitals for shared services, purchasing programs, or other arrangements to reduce costs, however, perhaps improving financial viability and thereby reducing the need for subsidies from the District. For example, when PDHCD operated the hospital directly, it initiated a shared services agreement with Sonoma Valley Hospital for information technology services.)

FACTOR 6 – ACCOUNTABILITY, STRUCTURE AND EFFICIENCIES

| Accountability for community service needs, including governmental structure and operational efficiencies. | YES | MAYBE | NO |
|-----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|-----|-------|----|
| a. Are there any issues with meetings being accessible and well publicized? Any failures to comply with disclosure laws and the Brown Act? | | | X |
| b. Are there any issues with filling board vacancies and maintaining board members? | | | X |
| c. Are there any issues with staff turnover or operational efficiencies? | | | X |
| d. Is there a lack of regular audits, adopted budgets and public access to these documents? | | | X |
| e. Are there any recommended changes to the organization’s governance structure that will increase accountability and efficiency? | X | | |
| f. Are there any governance restructure options to enhance services and/or eliminate deficiencies or redundancies? | | X | |
| g. Are there any opportunities to eliminate overlapping boundaries that confuse the public, cause service inefficiencies, unnecessarily increase the cost of infrastructure, exacerbate rate issues and/or undermine good planning practices? | | | X |

Determinations

- The District strives to follow requirements to hold publicly-noticed and publicly-accessible board meetings but has been criticized by constituents for perceived lapses.
- It is apparent that, for a portion of the District's constituents, there is a sense that the District does not operate transparently and is otherwise unresponsive to questions and concerns raised by citizens.
- Without prejudice, LAFCO recommends that the District endeavor to exceed the minimum regulatory standards of disclosure and re-commit to a sense of partnership with the community it serves; and that the constituents of the District, while fully exercising their rights to participate in District deliberations, continue to attempt to work cooperatively with the District board and staff.
- The District continues to attract candidates for board positions and conducts competitive elections. Historically, board members have largely come from Sebastopol (and occasionally from Bodega Bay), and it is only recently that members from the Russian River area have successfully been elected to Board of Directors. The Commission recommends that the District consider holding elections by district to ensure geographic representation on the Board.
- District board members are in compliance with legal requirements related to reporting of income and business interests (Fair Political Practices Commission), and have documented their completion of legally-required training (ethics and Brown Act).
- District finances are regularly independently audited. Recent audits have found deficiencies in financial management of the District, and it is unclear whether the District has responded effectively to the recommendations of their auditors.
- The governance model employed by the District in partnership with SWMC (or potentially another hospital operator) should be re-evaluated to address concerns regarding transparency of decision-making and potential responsibilities for liabilities of the hospital operator.

Discussion

Public Meetings

The District strives to appropriately notice and conduct public meetings and maintains a website to post relevant information in a timely fashion (including meeting agendas and minutes and other documents, such as financial reports).

The District directors have completed all legislatively-mandated training, (e.g., Ethics for Public Officials), are current on mandated disclosures (e.g., financial disclosures filed with the California Fair Political Practices Commission), and have undertaken other appropriate training (e.g., Brown Act compliance).

District directors have completed all legislatively-mandated training, (e.g., Ethics for Public Officials), are current on mandated disclosures (e.g., financial disclosures filed with the California Fair Political Practices Commission), and have undertaken other appropriate training (e.g., Brown Act compliance).

Critics have alleged that the District does not respond to information requests in a timely fashion, that board interactions with the public are not inclusive and welcoming, and that potential violations of the Brown Act have occurred. LAFCO has declined to take a role in reviewing these allegations in the absence of formal regulatory complaints and responses from regulatory agencies. (One formal complaint, made to the District Attorney in 2016, resulted in a finding that no violation of the Brown Act occurred.)

District Directors and staff are sensitive to allegations regarding transparency and compliance with regulatory requirements and note that District counsel provides advice on these matters and is present at almost every District meeting.

Without prejudice, LAFCO recommends that the elected directors of the District and staff redouble their efforts to adjudicate District business matters in an open and transparent fashion, seeking inclusion of community perspective in their decision-making process.

Similarly, LAFCO recommends that citizens continue to exercise their rights to participate in District business in a respectful manner, seeking to partner with their elected representatives to assist the District in meeting its mission.

Board Membership

PDHCD has a five-member board with members elected at large within the District, on staggered four-year terms. The District has not encountered difficulty in attracting board candidates, and there have always been more candidates than available seats in past elections, resulting in contested elections.

Some residents in the Russian River communities within the District believe that their voting power is not commensurate with their financial support of the District: while the communities provide over 40% of District parcel tax revenue, fewer than 20% of the registered voters within the District reside in the River area.

Because “landowner” districts (districts where landowners elect board members rather than registered voters) are forbidden by state law (there are “residual” landowner districts in the state, but new ones cannot be formed unless through legislation), the disparity between voter registration and financial contribution in the District cannot be addressed in this fashion.

If it is apparent that a particular region within a city or special district is regularly disenfranchised due to an inability to elect representative board members, a move to elections by district is generally considered a suitable solution.

In the case of PDHCD, a resident from the Russian River communities has only recently been elected to the board. (Proportionally, the District should typically have one representative who resides within the River area.) The District should therefore consider holding elections by district in order to ensure geographical representation on the board.

Staff Turnover

While PDHCD operated the hospital in Sebastopol directly, there were staff turnover issues during various periods of financial instability. Now that the District has chosen to contract for management and operation of the hospital going forward, it is not expected to face turnover issues for the two staff positions it directly funds.

Financial Transparency

The District has commissioned annual independent financial audits and provides access to the reports to the public. In addition, the MSA with SMWC requires that monthly hospital operation financial results are reported to the PDHCD board; these are also publicly available.

The FY 2015 audit identified that the District lacked an identified financial management team for a significant portion of the year and was therefore unable to record transactions and produce financial statements. There were transactions, such as disposal of hospital equipment that were not properly accounted for and recorded. The auditor recommended that the District form a financial management team and institute appropriate financial controls. The District has not indicated whether it has acted on this recommendation, and there is no indication that the District has adopted other fiscal control policies.

Governance Structure

For the first time since formation, the District has opted to select an independent operator for the hospital. After conducting a search for potential operators, the Sonoma West Medical Center was granted the “contract” to re-open and operate what was the Palm Drive Medical Center.

SWMC is comprised of local medical professionals and business representatives who do not operate any other medical facilities.

The District governs the contract with SWMC through a Management and Staffing Services Agreement that delineates PDHCD oversight of SWMC, and governs what services SWMC is to provide to the District.

Ostensibly to shield the District from any potential financial liabilities that might be incurred by SWMC, but at the same time allow for a level of control and oversight of SWMC's management, PDHCD has formed a "subcommittee" of the board named the Hospital Governance Board. The Governance Board consists of all five members of the PDHCD board, five members of the public, and two additional members selected by SWMC.

The responsibilities of the board include monitoring SWMC's performance. The Governing Board also has the authority to select SWMC's CEO.

The governance structure that PDHCD has instituted raises several concerns:

- Is PDHCD sufficiently "insulated" from any liabilities that are incurred by SWMC, particularly given that all five PDHCD board members serve on the Governing Board, and that the Governing Board has significant direct management oversight of SWMC?
- Can the actions taken by the Governing Board, which is a subcommittee of the PDHCD board, be sufficiently transparent that a member of the public could reasonably be expected to understand how decisions are being made?

PDHCD asserts that the governing structure is similar to ones in place for other health care districts and has been reviewed by its legal counsel and found sufficient with regard to the liability question.

District critics are concerned about the liability issue but also point to confusion regarding where decision-making authority lies and how to meaningfully participate in District governance.

It is also notable that the governance structure has proven cumbersome in at least one recent instance, where it was less than clear to SWMC, the Governing Board, and the PDHCD board what approval process was needed to select and approve a new CEO for SWMC.

Given the gravity of the question of whether liabilities incurred by SWMC might very well be transferable to PDHCD given the current governance structure and the concerns of District constituents about clear lines of authority, transparency, and opportunities for citizen participation in decision-making, the District might consider re-evaluating the governance structure, even if that results in a need for renegotiation of the MSA.

FACTOR 7 – COMMISSION POLICY CONSIDERATIONS

| Any other matter related to effective or efficient service delivery, as required by commission policy. | YES | MAYBE | NO |
|--------------------------------------------------------------------------------------------------------|-----|-------|----|
| Are there any other service delivery issues that can be resolved by the MSR/SOI process? | | | X |

Determinations

None

Discussion

There are no other issues that have been identified related to effective or efficient service delivery and therefore no MSR determinations in this category.

IV. SPHERE OF INFLUENCE

Sonoma LAFCO has several options for addressing the sphere of influence of the Palm Drive Health Care District, including:

1. Re-affirming the existing sphere of influence, indicating that the District is not expected to serve new territory or detach existing territory.
2. Expanding the sphere of influence to recognize additional territory that the District might annex.
3. Reducing the existing sphere to indicate territory that the District or the Commission may consider detaching.
4. Setting a “zero sphere;” an indication that the District should at some point be dissolved.

On the basis of this Municipal Service Review, LAFCO staff **does not recommend** an amendment to the Palm Drive Health Care District sphere of influence **at this time**. Please note that this recommendation **does not** pertain to Sonoma LAFCO's adjudication of an application for detachment from the District of communities in the Russian River area, which is pending.

Given that there is a pending citizen-led petition for detachment, LAFCO staff recommends that the Commission consider a sphere amendment should the detachment be approved, recognizing that the District would be very unlikely to secure approval from the detached communities to rejoin the District through annexation at a later date.

As mentioned in the Agency Profile section of this report, the Palm Drive Health Care District continues to experience changing circumstances, particularly with regard to the ability of the hospital to operate sustainably. If circumstances change for the hospital operation, that may call into question the appropriate role for PDHCD to take in order to fulfill its mission.

Therefore, again depending on circumstances that are impossible to predict accurately, Sonoma LAFCO should be prepared to update this report as needed and to reconsider a sphere amendment or a change of organization for the District at a later time.

ADDENDUM 1

Municipal Service Review And Sphere of Influence Study For the Palm Drive Health Care District

Sonoma Local Agency Formation Commission

September 26, 2016

Supplemental Discussion for Factor 3 – Capacity and Adequacy of Public Facilities and Services

Emergency Services Certification and Status Reporting

PDHCD has considered operation of the hospital in Sebastopol as the key activity to support its mission of providing “emergency, acute care and other medical services”. The current operators of the hospital, Sonoma West Medical Center, have obtained certification of emergency room services from the California Department of Public Health, but have not been reporting their day-to-day operational status to the Coastal Valleys EMS agency.

Certification

The California Department of Public Health operates a Licensing and Certification division that categorizes health care facilities and evaluates what types of services they provide.

Sonoma West Medical Center is classified as a “General Acute Care” hospital, with a “Standby Emergency Medical Services” approval. (The Dept. of Public Health relies on accreditation agencies to determine if a facility can be classified as a hospital.)

“Standby Emergency Medical Services” indicates the provision of emergency medical care in a specifically designated area of the hospital that is equipped and maintained at all times to receive patients with emergency medical problems and is capable of providing physician service within a reasonable time (per the Emergency Medical Service Authority).

Healdsburg Hospital, operated by the North Sonoma Health Care District, has the same emergency services classification as SWMC. The other five major hospitals (Kaiser, Sutter, Memorial, Petaluma, and Sonoma Valley) are classified as “Basic Emergency Medical Services” providers. “Basic Emergency Medical Services” indicates that these facilities provide emergency medical care in a specifically defined area of the hospital

that is equipped at all times to provide prompt care for any patient presenting urgent medical problems.

The District has indicated that SWMC has essentially been offering emergency care services at the “Basic” level, and that SWMC intends to apply for certification at that level with the California Department of Public Health.

Status Reporting

The Coastal Valleys EMS Agency (CVEMSA) operates under the statutory authority established in the California Health and Safety Code and acts as the regulator of emergency medical services in Sonoma County (and, under contract, Mendocino County). The primary mission of CVEMSA is to plan, implement, and evaluate the local EMS system, including licensing ambulance provider companies, coordination of air and ground ambulances, certification of EMTs and paramedics, and other activities.

CVEMSA gathers information from the seven hospitals in Sonoma County to identify the specific services and level of care offered; this information is used to review destination policies that guide the distribution of patients within the EMS system (i.e. directing ambulance providers to take patients to specified hospitals).

CVEMSA uses a notification system called ImageTrend to allow hospitals to report a general or specific lack of a defined capability in real time. For example, a hospital that cannot provide emergency care services to certain types of patients because of an imaging equipment failure would use ImageTrend to report that lack of capability, and patients needing those services would be directed to other facilities.

Since reopening, SWMC has not participated in the ImageTrend reporting system, so CVEMSA declines to state whether they have been made aware of all instances when SWMC may have had service, capability, or capacity deficiencies. However, as of September 9th, 2016, CVEMSA reports that SWMC has engaged with the Agency and is intent on reporting emergency care status in the future.

V. ATTACHMENTS

1. Sonoma LAFCO: Scope of MSR for Palm Drive Health Care District
2. Sonoma LAFCO: Formation Resolution for Palm Drive Health Care District
3. Palm Drive Health Care District, Financial Audit 2014/15,
4. Palm Drive Health Care District, Proposed Bankruptcy Settlement Plan
5. Coastal Valleys EMS Agency: Patient Destination/Point of Entry Policy 7007
6. Sonoma LAFCO: Financial Analysis of PDHCD (Annotated Excel Spreadsheet)
7. North Sonoma County Healthcare District: Letter Dated May 11, 2016, Regarding Financial Information
8. Sonoma LAFCO Request for Information to the District and District Response.
9. MSA between the District and Sonoma West Medical Center

SONOMA LOCAL AGENCY FORMATION COMMISSION

575 ADMINISTRATION DRIVE, ROOM 104A, SANTA ROSA, CA 95403

(707) 565-2577 FAX (707) 565-3778

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**Service Review Scope for
Palm Drive Health Care District****April 28, 2016**

The Sonoma Local Agency Formation Commission will be conducting a service review of the Palm Drive Health Care District (District or PDHCD).

The Commission is conducting the study to support several potential activities, including:

- Evaluation and adjudication of an application filed by community members to detach from the District.
- A Commission-initiated amendment to the Sphere of Influence of the District.
- A Commission or District-initiated dissolution of the District (although, at this time, this is not considered a likely outcome).

In order to provide the appropriate level of investigation and guidance to the Commission and to support adjudication of any of the actions noted above, LAFCO staff is recommending that a study meet the determinations required for Municipal Service Reviews in the Cortese-Knox-Hertzberg Local Government Reorganization Act of 2000, Government Code §56430 (Cortese-Knox-Hertzberg).

Cortese-Knox-Hertzberg mandates that a Municipal Service Review (which is required to prepare and update the Sphere of Influence of a District) prepare written **determinations** with regard to each of the following:

1. Growth and population projections for the affected area;
2. The location and characteristics of any disadvantaged unincorporated communities within or contiguous to the sphere of influence;
3. Present and planned capacity of public facilities, adequacy of public services, and infrastructure needs or deficiencies;
4. Financial ability of agencies to provide services;
5. Status of, and opportunities for, shared facilities;
6. Accountability for community service needs, including governmental structure and operational efficiencies;
7. Any other matter related to effective or efficient service delivery, as required by Commission policy.

For each of these study areas, staff has prepared discussion points, specific questions related to PDHCD, and general study factors with notes as appropriate.

Scope of Study

1. Population Projections

For this District, population growth projections might be marginally useful in understanding the projected need for health care services in the region, although an understanding of health care provision trends might be more useful (i.e., what proportion of District residents seek health care services from other providers, and is this proportion likely to change over time?)

With regard to the District's ability to fund health care services, population projections are not meaningful because the District relies on a parcel tax levy for revenue, which is wholly independent of population (or of property value).

Staff believes, then, that population growth projections would be marginally informative, and that a determination could simply indicate same.

2. Disadvantaged Unincorporated Communities (DUCs)

Under current definitions, the District serves two of seven Disadvantaged Unincorporated Communities in Sonoma County (Guerneville and Monte Rio) and borders one (Cazadero).

Discussion of the provision of services to DUCs, while potentially pertinent, might be better understood within a broader analysis of what services the District does or should be providing to meet the needs of District residents in the next section.

3. Adequacy of Public Services

Staff believes that this area warrants particular coverage in a study, including an evaluation of what types of services are needed by the communities and residents throughout the District and how best to provide them, given the health care landscape in the County now and into the future.

Specific Questions

What are the types of services that the District is authorized to provide, according to formation documents?

If the Sonoma West Medical Center (SWMC, the newly formed entity that the District has contracted with to operate the hospital) is unable to continue operations at some time in the future, what is the District's plan to continue providing medical services? What services might these include?

What, if any, medical services are the District planning to provide or financially support beyond the services provided by SWMC? Will any of these services be

directed to Russian River Corridor communities or other outlying communities that are within the District boundary (i.e., coastal areas)?

What have been the historical annual admission rates for Palm Drive Hospital by broad service category (emergency care, critical care, general admissions)? Can this information indicate what proportion of hospital users have come from Russian River Corridor communities?

The parcel tax assessments supporting the District have no expiration date, nor do they feature a mechanism for indexing them to increases in District operational costs. Does the District expect to have increasing costs in the future, and if so, how would it plan to address increasing costs for the provision and support of hospital and medical services?

4. Financial Ability to Provide Services

Staff believes that this portion of the study be narrowly defined with regards to an evaluation of the **District's** financial picture, rather than a critique of the business plan for the Sonoma West Medical Center: i.e., can the District afford to provide the agreed-to subsidy to the SWMC in order to secure sustainable emergency, acute care, and other medical services now and in the future?

Specific Questions

What authority does the District have to issue new bonds, pledging future tax revenue to pay for them? Does the District have to seek voter approval for issuing new bonds?

What is the status of the District's bankruptcy proceedings? What is the expected range of financial obligations that the District may face as a result of the current bankruptcy proceedings? Does the District plan to issue bonds to pay for the settlement?

Is there a mechanism for limiting the District's liability for the SWMC debt and potential litigation? Can there be a firewall established between the two entities?

If communities in the Russian River Corridor are detached from the District, what would be the implications for the District's "general fund" revenues?

If the District needed to make up for that reduction by raising parcel tax assessments in the remaining District area, what increase would be needed? (Note: the District would have to hold an election seeking approval of a parcel tax assessment increase.)

What is the District's ability to obtain financing? What is their bond rating?

Does the District have any plans to pay down existing debts early using existing revenue?

If the District were dissolved, how would debts be discharged?

Are services provided by PDHCD needed in the current health care service environment of Sonoma County, or should a different set of services be considered?

Is the District providing services to all constituents and communities within its service area?

Should Sonoma LAFCO consider amending the District's Sphere of Influence?

Describe the District's accounting practices, including an evaluation of contingency reserves, auditing practices, and written budget, debt servicing, accounting, and investment practices.

5. Shared Services

Staff believes that this subject area has little import for the evaluation of the District. The District itself likely has little opportunity for sharing services with other agencies; while SWMC may have opportunities to partner with other regional facilities (e.g., for purchasing supplies or renting equipment), these opportunities would have no discernible impact on the District itself.

6. Accountability for Community Service Needs

Study of this area typically focuses on the ability of a District to attract and retain candidates for board service and on the question of whether the board adequately represents the varied interests of the population and communities which the District serves.

Staff believes that the former question is relatively easy to address in an objective fashion but that the latter is very much a subjective one.

Specific Questions:

Is the District in compliance with the Brown Act and state disclosure laws?

Does the District seek and obtain public participation through publicly noticed and accessible meetings?

Have members of the District Board of Directors been elected from representative communities within the District's service area?

Describe the District's public outreach activities.

Are financial and operational documents accessible to constituents of the District?

7. Effective Service Delivery, Per District Policy

Specific Questions

The District has entered into an agreement with SWMC pledging to provide "up to \$1 million" in annual funding to support hospital operations. Are there clauses in the agreement that allow adjustments in this funding level?

What are some of the operational factors that face SWMC that might necessitate a request for additional financial support from the District?

Resolution No. 2345

575 Administration Drive
Santa Rosa, CA 95403

January 5, 2000

RESOLUTION OF LOCAL AGENCY FORMATION COMMISSION OF THE
COUNTY OF SONOMA RESCINDING RESOLUTION NO. 2341, MAKING
DETERMINATIONS, AND APPROVING THE PROPOSED DISTRICT
FORMATION, DESIGNATED AS: FORMATION OF PALM DRIVE HEALTH
CARE DISTRICT AND ESTABLISHMENT OF A SPHERE OF INFLUENCE
FOR THE DISTRICT

RESOLVED, by the Local Agency Formation Commission of the County of
Sonoma, State of California, that:

WHEREAS, a petition for formation of the Palm Drive Health Care District was
heretofore filed by 12% of the registered voters residing within the boundaries of the
proposed district and accepted for filing by the Executive Officer of this Commission
pursuant to the Cortese-Knox Local Government Reorganization Act of 1985,
commencing with Section 56000 et seq. of the Government Code, the Local Health
Care District Law, commencing with Section 32000 of the California Health and Safety
Code, and the District Organization Act, commencing with Section 58000 of the
California Government Code; and

WHEREAS, the Executive Officer, pursuant to Government Code Section 56828,
set November 3, 1999, as the hearing date on the proposal and gave the required
notice of hearing; and

WHEREAS, an initial study was conducted for the proposal pursuant to the
California Environmental Quality Act, and, based on the initial study's finding that the
proposal would not have a significant effect on the environment, a negative declaration
has been prepared; and

WHEREAS, the Executive Officer, pursuant to Government Code Section 56833,
has reviewed the proposal and prepared a report including her recommendations
thereon, and has furnished a copy of this report to each person entitled to a copy; and

WHEREAS, this Commission called the proposal and proposed negative
declaration for public hearing on November 3, 1999, heard from the interested parties,
considered the proposal and the report of the Executive Officer, and all pertinent
documents and considered the factors determined by the Commission to be relevant to
the proposal including, but not limited to, the factors specified in Government Code
Section 56841; and

WHEREAS, this Commission adopted Resolution No. 2341 on November 3, 1999, making determinations and approving formation of the proposed district and establishing a sphere of influence for the proposed district; and

WHEREAS, certain inadvertent mistakes have been discovered in Resolution No. 2341 and the Sonoma County Board of Supervisors, as conducting authority, has requested this Commission to correct those mistakes before it completes proceedings on formation of the proposed district; and

WHEREAS, this Commission desires to correct the mistakes in Resolution No. 2341 by rescinding Resolution No. 2341 and adopting this resolution making determinations and approving formation of the proposed district and establishing a sphere of influence for the proposed district;

NOW, THEREFORE, the Local Agency Formation Commission of the County of Sonoma does hereby resolve, determine, and order as follows:

- Section 1. The foregoing findings and determinations are true and correct, are supported by substantial evidence in the record, and are adopted as hereinabove set forth.
- Section 2. Resolution 2341 is hereby rescinded in its entirety.
- Section 3. Notice as required by law was given.
- Section 4. All persons desiring to be heard regarding the proposal have been given the opportunity to be heard and all persons requesting to be heard have been heard.
- Section 5. The Commission makes the following findings:
 - a. The formation of the proposed district is in direct response to petitions filed in support of the district formation.
 - b. The territory of the proposed district with 31,083 registered voters is inhabited as defined in Government Code Section 56046.
 - c. The purpose of the proposed district is to ensure local access to emergency, acute care and other medical services to residents and visitors of the district area.
 - d. The proposed district intends to purchase the real property, buildings, and building improvements known as Palm Drive Hospital and lease the hospital to a qualified operator.
 - e. According to the Financial Analysis prepared by proponents of the proposal initial financing of the district will be accomplished through the proceeds of a bond measure which requires two-

thirds voter approval. The general obligation bond is projected to be \$5.9 million dollars.

- f. The approval of the proposal will not have a significant adverse impact on the environment.

Section 6. The formation of the proposed district is approved, subject to the following terms and conditions:

- a. The name of the proposed district shall be the Palm Drive Health Care District.
- b. The proposed district's board of directors shall consist of five (5) members, each of whom shall be a registered voter residing within the proposed district and whose term shall be four years with the exception of the first board. The first board of directors shall be appointed, upon formation of the proposed district, by the Sonoma County Board of Supervisors. Upon appointment, the first board of directors shall, by lot, designate two members who shall leave office when their successors take office pursuant to Section 10554 of the Elections Code, and three members shall leave office two years thereafter. All subsequent boards of directors shall be elected at large from throughout the proposed district.
- c. Formation of the proposed district shall occur only if the question submitted in the election called with respect to such formation includes, with the matters set forth in Section 57133(k), Section 57134 and Section 57135(a) of the Government Code, a statement of the condition on the formation that the proposed district must be authorized to issue bonds to provide adequate funding for the proposed district's acquisition of the real property, buildings, and building improvements known as Palm Drive Hospital by two-thirds voter approval at the same election, it being understood that Section 57127 of the Government Code authorizes the conducting authority to call a special election as to such a bond issue in lieu of the board of directors of the proposed district, as contemplated under Section 32301 and Section 32302 of the Health and Safety Code.
- d. The effective date for formation of the proposed district shall be the date of execution of the certificate of completion by the Executive Officer.
- e. The appropriations limit for the proposed district shall be \$500,000.00.
- f. The conducting authority shall call a special election on the question of whether the proposed district be authorized to issue bonds to provide adequate initial funding for the purchase of real

property, buildings, and building improvements proposed (projected to be \$5.9 million), to be held simultaneously with the election on the formation of the proposed district.

Section 7. In accordance with Government Code section 56425, the Commission makes the following determinations relative to establishment of the proposed district's sphere of influence:

- a. Present and planned land uses in the area, including agriculture and open space lands: The proposed district has no authority over land use and its functions are not growth-inducing. Any change in land use of district property would require approval and environmental review by the appropriate land use agency.
- b. Present and probable need for public facilities and services in the area: Formation of the proposed district is for the purpose of funding the purchase of an existing hospital: Public facilities and services currently exist to serve the hospital. Retention of the hospital in the west county maintains levels of service for emergency services especially with respect to transport of patients.
- c. Present capacity of public facilities and adequacy of public services which the agency provides or is authorized to provide: Retention of the hospital by the proposed district would maintain public facilities and adequate delivery of public services. Hospital closing would negatively affect provision of service because this is the only such facility in the west county.
- d. The existence of any social or economic communities of interest in the area: The formation of the proposed district is in direct response to petitions from registered voters in the subject territory. A poll in the area indicated strong support for proposed district formation. In addition, the bond measure to fund the district requires voter approval.

Section 8. The Commission hereby determines that the proposed district's sphere of influence shall be coterminous with the proposed district's approved boundaries.

Section 9. The boundaries of the proposed district are hereby approved as described in Exhibit "A" attached hereto.

Section 10. The regular county assessment roll will be utilized.

Section 11. The distinctive short form for the proposal shall be: "Formation of Palm Drive Health Care District".

Section 12. Approval of the proposal will have no effect on maintaining the physical and economic integrity of any agricultural preserve that might be considered within the sphere of influence of the proposed district.

Section 13. The Commission hereby adopts a negative declaration with the finding that approval of the proposal will have no significant effect on the environment.

Section 14. The Sonoma County Board of Supervisors is designated as the conducting authority and is hereby directed to proceed with notice and hearing, and, pursuant to Section 57127 of the Government Code, to call any special elections required on behalf of the proposed district.

Section 15. The Commission hereby approves the impartial analysis pursuant to Section 56859 of the Government Code, as provided in Exhibit "B" attached hereto, and pursuant to Sections 56843 and 56844 of the Government Code, the Tax Rate Statement required by Section 9401 of the Elections Code, as provided in Exhibit "C" attached hereto.

Section 16. The Executive Officer is hereby authorized and directed to mail certified copies of this resolution in the manner provided by law.

The foregoing resolution was introduced at a regular meeting of this Local Agency Formation Commission on the fifth day of January, 2000 and ordered adopted by the following vote:

Commissioners: Harvey: Aye Cullinen: Aye Smith: Absent Massey: Aye
Brunton: Aye Boyett: Aye Cale: Aye

Ayes: 6 Noes: 0 Absent or not voting: 1

WHEREUPON, the Chair declared the foregoing resolution adopted and

SO ORDERED

ATTEST:

Steven J. Sharpe
Steven J. Sharpe, Assistant Executive Officer

The within instrument is a correct copy of the original on file in this office.

ATTEST: JAN 12 2000

BY: John Johnson
Clerk

Palm Drive Health Care District

District Boundaries

The area of The Palm Drive Health Care District includes the following elementary school districts within Sonoma County:

- Oak Grove Union School District, as formed by the Board of Education, December 7, 1951, with present boundaries as set March 6, 1969 by Resolution No. 121. Excepting therefrom five parcels annexed into the City of Santa Rosa. Annexation 9-84, parcels 9-12. Annexation 1-98, parcel 5.
- Sebastopol Union School District, as formed by the Board of Education, July 1, 1919, with present boundaries as set August 27, 1963. Excepting therefrom ten parcels annexed into the City of Santa Rosa. Annexation 9-84, parcels 1-7. Annexation 1-98, parcels 1-4.
- Gravenstein Union School District, as formed by the Board of Education, June 7, 1965, with present boundaries as set June 8, 1965, excepting therefrom all that portion of the Petaluma Health Care District which lies within this district. Excepting therefrom four parcels annexed into the City of Santa Rosa. Annexation 9-84, parcels 1 and 8. South Santa Rosa Annexation No. 7, parcels 1 and 2.
- Twin Hills Union School District, as formed by the Board of Education, July 1, 1955, with present boundaries as set August 27, 1963.
- Also, all that portion of the Shoreline Unified School District which lies within Sonoma County (Joint Sonoma County and Marin County School District).
- Harmony Union School District, as formed by the Board of Education, July 1, 1951, with present boundaries as set October 15, 1963.
- Monte Rio Union School District, as formed by the Board of Education, October 3, 1968, effective for all purposes July 1, 1969, with present boundaries as set October 3, 1968.
- Guerneville School District, as formed by the Board of Education, August 6, 1897, with present boundaries as set December 1, 1966.
- Forestville Union School District, as formed by the Board of Education, July 1, 1939, with present boundaries as set March 6, 1962 by Resolution No. 121.

The boundary of the Palm Drive Health Care District is conterminous with the exterior boundary of the above described area. The District is more particularly described on Attachment I below.

Final Draft 3/31/2016

Approved Apr. 4, 20

FINAL DRAFT

Report of Independent Auditors and
Financial Statements with
Supplementary Information

Palm Drive Health Care District

Year Ended June 30, 2015

FINAL DRAFT

MANAGEMENT'S DISCUSSION AND ANALYSIS

**PALM DRIVE HEALTH CARE DISTRICT
MANAGEMENT'S DISCUSSION AND ANALYSIS
June 30, 2015 and 2014**

Introduction – The management's discussion and analysis of the financial performance of Palm Drive Health Care District (the "District") provides an overview of the District's financial activities for the year ended June 30, 2015 and 2014, respectively. It should be read in conjunction with the accompanying financial statements and footnotes of the District.

During fiscal year 2014 the District was under significant economic stress. This was caused by a significant decline in patient volumes and specifically commercial patient volumes and the irregular postings of projected accounts receivable. The decision was made in March and April of 2014 to seek relief under Chapter 9 of the U.S. Bankruptcy code, and to close the hospital and the emergency room.

From April of 2014 through the 2015 fiscal year the hospital remained closed. The District remained in Chapter 9 Bankruptcy and through February of 2016 has not submitted a plan to the Bankruptcy court for approval. This means that there are no patient services revenues being generated during 2015, though there are changes in prior estimates which effect the period. There are also significantly less staffing costs as the District operated for most of fiscal year 2015 with eight or less employees. There were significant legal costs incurred in the bankruptcy process.

During the 2015 fiscal year the District solicited and considered plans from several organizations to help the District fulfill its mission of providing healthcare to its constituents. In May of 2015 it entered a Management Services Agreement with Sonoma West Medical Center Inc. (SWMC), whereby SWMC would re-open the hospital, retain and employ staff, and provide management services for the hospital. The hospital was renamed Sonoma West Medical Center and was re-opened on October 30, 2015.

In addition, the District did not know how to structure the bankruptcy plan until we were sure that SWMC had reopened or was going to open. The new entity was confident it would open by summer 2015 but this was delayed until October 31, 2015.

SWMC is a separate 501(c)(3) organization which has not been included in the reporting entity of the District for the fiscal year ended June 30, 2015, but will be included as of July 1, 2015, as a blended component unit of the District.

Financial Highlights

Year Ended June 30, 2015

- Total assets decreased by approximately \$3,205,000 from June 2014.
- Total cash and equivalents decreased by approximately \$390,000 from June 2014.
- Patient accounts receivable decreased by approximately \$770,000 from June 2014.
- Current assets decreased by approximately \$1,442,000 from June 2014, while current liabilities decreased by approximately \$1,252,000 during that same period.
- Long-term capital assets decreased by approximately \$1,767,000 from June 2014, while long-term debt increased by approximately \$1,535,000 during that same period.
- The increase in net deficit was approximately \$418,000 for the year ended June 30, 2014.

Year Ended June 30, 2014

- Total assets decreased by approximately \$5,910,000 from June 2013.
- Total cash and equivalents decreased by approximately \$319,000 from June 2013.
- Patient accounts receivable decreased by approximately \$3,150,000 from June 2013.
- Current assets decreased by approximately \$4,229,000 from June 2013, while current liabilities increased by approximately \$3,503,000 during that same period.
- Long-term capital assets increased by approximately \$675,000 from June 2013, while long-term debt decreased by approximately \$122,000 during that same period.
- The increase in net deficit was approximately \$8,305,000 for the year ended June 30, 2014.

Overview of Palm Drive Health Care District's Financial Statements

This annual report consists of the audited financial statements and the notes to the financial statements which reflect the District's financial position and operating results for the year ended June 30, 2015. The audited financial statements include the report of the independent auditors, statement of revenues, expenses and changes in net assets, and statement of cash flows. They also include notes to the financial statements.

- The statements of net position includes all of the District's assets and liabilities based on the accrual method of accounting for the year ended June 30, 2015 and 2014.
- The statements of revenues, expenses and changes in net position present the operating activities of the District during the year ended June 30, 2015.
- The statements of cash flows reports the net cash provided by operating activities as well as other sources and uses of cash from various District financial activities.

Cash and Cash Equivalents

For the fiscal year ended June 30, 2015, the District's cash and cash equivalents totaled approximately \$320,000 compared to approximately, \$710,000 at June 2014. At June 30, 2015, days of operating cash on hand were approximately 37.0 as compared to 7.9 at June 2014. The majority of the District's cash is deposited with a local bank in various forms of cash and cash equivalent funds.

Current Assets and Liabilities

During fiscal year ended June 30, 2015, current assets decreased by approximately \$3,205,000 with decreases in patient accounts receivable of approximately \$770,000 and a decrease in cash and cash equivalents of approximately \$390,000. Current liabilities decreased by approximately \$1,252,000 due mainly to a decrease of approximately \$776,000 in accounts payable and accrued expenses, and a decrease of approximately \$112,000 in accrued payroll and related liabilities.

During fiscal year ended June 30, 2014, current assets decreased by approximately \$4,229,000 with decreases in patient accounts receivable of approximately \$3,150,000 and a decrease in cash and cash equivalents of approximately \$319,000. Current liabilities increased by approximately \$3,503,000 due mainly to an increase of approximately \$2,505,000 in accounts payable and accrued expenses and a decrease of approximately \$77,000 in accrued payroll and related liabilities.

The current ratio at June 30, 2015, is 0.05 compared to 0.24 at June 2014.

Capital Assets

During the fiscal year ended June 30, 2015, the District divested assets of approximately \$715,000 through the return of leased equipment as compared to the years ending June 2014, where the District recorded impairment for Equipment of \$715,000. However, the divestment during fiscal year June 30, 2015, did not lower capital lease obligations due to bankruptcy court constraints contrasting fiscal year 2014.

Long-Term Debt and District Tax Revenues

During the fiscal year ending June 30, 2015, the District stopped making payments on most capital leases in effect at July 20, 2014, which resulted in one lessee physically removing some equipment. Again, the long-term debt during fiscal year ending June 30, 2015, was unchanged due to bankruptcy court constraints, which makes it significantly lower than the decrease in long-term debt during fiscal year 2014. During the year ended June 30, 2015, the total tax collections from the District totaled \$4,132,780 as compared to \$4,085,234 in 2014. These collections service the debt obligations for bond issues totaling \$21,550,000 and \$22,265,000 in principal as of June 30, 2015 and 2014, respectively.

Volumes

There were no patient days reported for the year ended June 30, 2015, as compared to 2,514 for the year ended June 30, 2014. There were no ER visits for the year ended June 30, 2015, as compared to 4,358 for the year ended June 30, 2014.

**PALM DRIVE HEALTH CARE DISTRICT
MANAGEMENT'S DISCUSSION AND ANALYSIS
June 30, 2015 and 2014**

Gross Patient Charges

The District charges all its patients equally based on its established pricing structure for the services rendered. However, the District did not provide services to patients during the fiscal year ended June 30, 2015. The reported revenues represent collections on accounts receivable of approximately \$221,000 that had been written off in previous years, payments by the Department of Health Care Services ("DHCS") of approximately \$66,500 and Partnership Health Plan of approximately \$315,000 for uncompensated care provided in fiscal year 2014 under the Assembly Bill 915 program, and payments by the DHCS of approximately \$182,000 for Medicaid safety net care provided in fiscal year 2014 under the Assembly Bill 113 Intergovernmental Transfer program.

These results contrast dramatically with inpatient gross service charges of approximately \$32,895,000 for the year ended June 30, 2014, as well as outpatient gross service charges of approximately \$45,117,000 for the year ended June 30, 2014.

Deductions from Revenue

Deductions from revenue are a combination of contractual allowances and provisions for bad debts. Contractual allowances are computed deductions based on the difference between gross charges and the contractually agreed upon rates of reimbursement with third party government-based programs such as Medicare and Medi-Cal, and other third party HMO-based payers such as Blue Shield and Aetna.

Since the District did not provide services to patients and reported no inpatient or outpatient revenues for the year ended 2015, there were also no deductions from revenue for the fiscal year. These results contrast dramatically with the deductions from revenue (in aggregate and as a percentage of gross patient services charges) of approximately \$56,868,000 and 69.0% for the fiscal year ending June 30, 2014.

Net Patient Revenues

Net patient service revenues are the resulting difference between gross patient charges and the deductions from revenue. Net patient service revenues were approximately \$803,000 for the year ended June 30, 2015, as compared to \$21,145,000 for fiscal year ending June 30, 2014.

Operating Expenses

Total operating expenses were approximately \$5,409,354 for the fiscal year ending June 30, 2015, as compared to \$32,598,000 for fiscal year ending June 30, 2014. The net decrease from fiscal year ended June 30, 2014, was approximately \$27,179,000. The significant changes were:

- Labor-related expenses (salaries and wages, employee benefits and contract labor) decreased from 2014 by approximately \$14,500,000 due primarily to the hospital closing and the laying off of staff.
- Supplies expense decreased by approximately \$4,194,000 due primarily to the hospital closing and the winding down of patient care activities in late 2014.
- Contract labor, physician fees and various other expenses decreased by approximately \$5,515,000 due primarily to the hospital closing and the winding down of patient care activities.

Economic Factors

The current fiscal year saw a surge in community support for reopening an acute health care facility for the community. Through significant voluntary donations of cash and services, a new hospital opened in October 2015 under the name of Sonoma West Medical Center. The District Board of Directors holds five (5) of eleven (11) seats on the hospital's Governing Board.

The District remains in Chapter 9 bankruptcy proceedings for the foreseeable future. However, it continues as a going concern through its ability to levy a parcel tax, allowing it to continue to meet all of its regulatory covenants.

REPORT OF INDEPENDENT AUDITORS

The Board of Directors
Palm Drive Health Care District

Report on Financial Statements

We have audited the accompanying financial statements of Palm Drive Health Care District (the "District"), which comprise the statement of net position as of June 30, 2015, and the related statement of revenues, expenses, and changes in net position, and cash flows for the year then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the District as of June 30, 2015, and the changes in its net position and its cash flows for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Emphasis of Matter Regarding Going Concern

The accompanying financial statements have been prepared assuming that the District will continue as a going concern. As discussed in Note 2 to the financial statements, the District has closed the hospital, filed for Chapter 9 bankruptcy, and has a net capital deficiency that raise substantial doubt about its ability to continue as a going concern. Management's plans in regard to these matters are also described in Note 2. The financial statements do not include any adjustments that might result from the outcome of this uncertainty. Our opinion is not modified with respect to this matter.

Other Matters

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis on pages 1 through 4 be presented to supplement the financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management regarding the methods of preparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

San Francisco, California
_____, 2016

FINAL DRAFT

FINANCIAL STATEMENTS

PALM DRIVE HEALTH CARE DISTRICT
STATEMENT OF NET POSITION
June 30, 2015

| | <u>2015</u> |
|-------------------------------------------------------------|-----------------------------|
| ASSETS | |
| CURRENT ASSETS | |
| Cash and cash equivalents | \$ 319,799 |
| Restricted trust funds available for current debt service | 1,118,321 |
| Property taxes receivable | 181,219 |
| Prepaid expenses and deposits | 50,100 |
| Total current assets | <u>1,669,439</u> |
| NONCURRENT INVESTMENTS | |
| Funds held by county for bond debt service | 359,802 |
| Funds held by trustee under bond requirements | 1,791,978 |
| Designated by the board or agreements for specific purposes | 2,551 |
| | <u>2,154,331</u> |
| Related party notes receivable | 1,538 |
| Capital assets, net of accumulated depreciation | 10,824,729 |
| Total assets | <u><u>\$ 14,650,037</u></u> |
| LIABILITIES AND NET POSITION | |
| CURRENT LIABILITIES | |
| Accounts payable and accrued expenses | \$ 7,095,319 |
| Accrued payroll and related liabilities | 1,309,993 |
| Accrued interest payable | 368,321 |
| Estimated third party payor settlements | 327,099 |
| Unearned property tax revenues | 635,037 |
| Current portion of capital lease obligations | 1,383,889 |
| Current portion of bonds payable | 750,000 |
| Total current liabilities | <u>11,869,658</u> |
| Capital lease obligations, net of current portion | 454,870 |
| Bonds payable, net of current portion | 20,800,000 |
| Total liabilities | <u>33,124,528</u> |
| NET POSITION | |
| Restricted, by bond indenture agreements and other | 3,270,101 |
| Unrestricted (deficit) | <u>(21,744,592)</u> |
| Total net deficit | <u>(18,474,491)</u> |
| Total liabilities and net position | <u><u>\$ 14,650,037</u></u> |

See accompanying notes.

PALM DRIVE HEALTH CARE DISTRICT
STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN NET POSITION
Year Ended June 30, 2015

| | 2015 |
|---------------------------------------------|------------------------|
| OPERATING REVENUES | |
| EHR incentive revenue | \$ 1,154,510 |
| Medi-Cal supplemental reimbursement | 381,992 |
| Inter-governmental transfer revenue | 181,921 |
| Other operating revenue | 116,278 |
| Total operating revenues | 1,834,701 |
| OPERATING EXPENSES | |
| Salaries and wages | 433,026 |
| Employee benefits | 51,960 |
| Professional fees | 724,775 |
| Supplies | 140,273 |
| Purchased services | 973,922 |
| Utilities and phone | 224,368 |
| Repairs and maintenance | 119,692 |
| Rents and leases | 48,662 |
| Insurance | 323,380 |
| Depreciation | 1,537,718 |
| Impairment of equipment | 714,925 |
| Other operating expenses | 116,653 |
| Total operating expenses | 5,409,354 |
| OPERATING LOSS | (3,574,653) |
| NONOPERATING REVENUES AND (EXPENSES) | |
| District tax revenues | 4,132,780 |
| Investment income(expense), net | (962) |
| Interest expense | (1,368,879) |
| Other income | 393,909 |
| Total nonoperating revenues | 3,156,848 |
| INCREASE IN DEFICIT | (417,805) |
| NET POSITION, beginning of the year | (18,056,686) |
| NET POSITION, end of the year | \$ (18,474,491) |

See accompanying notes.

PALM DRIVE HEALTH CARE DISTRICT
STATEMENT OF CASH FLOWS
Year Ended June 30, 2015

| | <u>2015</u> |
|----------------------------------------------------------------------|--------------------------|
| CASH FLOWS USED IN OPERATING ACTIVITIES | |
| Cash received from patients and third-parties on behalf of patients | \$ 864,888 |
| Cash received from operations, other than patient services | 2,106,327 |
| Cash payments to suppliers and contractors | (4,611,132) |
| Cash payments to employees and benefit programs | (596,714) |
| Net cash from operating activities | <u>(2,236,631)</u> |
| CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES | |
| District tax revenues | 2,059,420 |
| Grants, contributions and other | 393,909 |
| Net cash from noncapital financing activities | <u>2,453,329</u> |
| CASH FLOWS USED IN CAPITAL AND RELATED FINANCING ACTIVITIES | |
| District tax revenues | 2,073,360 |
| Purchase of capital assets | (485,319) |
| Principal payments on capital lease obligations | (83,268) |
| Principal payments on bonds payable | (715,000) |
| Interest payments on debt borrowings | (1,368,879) |
| Net cash from capital and related financing activities | <u>(579,106)</u> |
| CASH FLOWS USED IN INVESTING ACTIVITIES | |
| Purchases of (proceeds from) sale of investments | (26,802) |
| Interest and dividends received from investments | (962) |
| Net cash from investing activities | <u>(27,764)</u> |
| NET CHANGE IN CASH AND CASH EQUIVALENTS | <u>(390,172)</u> |
| CASH AND CASH EQUIVALENTS, beginning of the year, as restated | <u>709,971</u> |
| CASH AND CASH EQUIVALENTS, end of the year | <u><u>\$ 319,799</u></u> |

FINAL DRAFT

See accompanying notes.

PALM DRIVE HEALTH CARE DISTRICT
STATEMENT OF CASH FLOWS (CONTINUED)
Year Ended June 30, 2015

| | 2015 |
|----------------------------------------------------------|----------------|
| RECONCILIATION OF OPERATING LOSS TO NET CASH FROM | |
| OPERATING ACTIVITIES | |
| Operating loss | \$ (3,574,653) |
| Adjustments to reconcile operating loss | |
| to net cash used in operating activities: | |
| Depreciation | 1,537,718 |
| Impairment of imaging equipment | 714,925 |
| Changes in operating assets and liabilities: | |
| Patient accounts receivable | 770,415 |
| Property taxes receivable | (34,035) |
| Prepaid expenses and deposits | 15,940 |
| Related party notes receivable | 8,634 |
| Accounts payable and accrued expenses | (775,772) |
| Accrued payroll and related liabilities | (111,728) |
| Accrued interest | (20,813) |
| Estimated third party payor settlements | (795,008) |
| Unearned property taxes | 27,746 |
| Net cash from operating activities | \$ (2,236,631) |

FINAL DRAFT

PALM DRIVE HEALTH CARE DISTRICT NOTES TO FINANCIAL STATEMENTS

NOTE 1 – ORGANIZATION

Organization – Palm Drive Health Care District, (the “District”) is a public entity organized under Local District Law as set forth in the Health and Safety Code of the State of California. The District is a political subdivision of the State of California and is generally not subject to federal or state income taxes. The District is governed by a five-member Board of Directors, elected from within the district to specified terms of office. The District is located in Sebastopol, California and operated a 37-bed acute care hospital. The District’s mission is to provide health care services primarily to individuals who reside in the local geographic area.

The District has signed a Master Services Agreement (“MSA”) with Sonoma West Medical Center (“SWMC”) on March 18, 2015, and amended May 22, 2015. This agreement calls for SWMC to operate the hospital facility on behalf of the District, and for the District to provide \$1,000,000 to augment the operations of the hospital that SWMC will be operating. Specifically, the funding is to be used to maintain hospital property, purchase or repair equipment and to subsidize charity care and programs that benefit the community. The MSA creates a governing board which will oversee the operations of the hospital. This governing board is a subcommittee of the District, with representation from SWMC and participating physicians.

Management has determined that the District will include SWMC as a component unit of its reporting entity. The inclusion of SWMC will begin on July 1, 2015. Management does not believe that the omission of SWMC from the operations of 2015 and ending net assets of 2015 has a material effect on the District. See the subsequent events Note 13 for more information on what happened after year end with the hospital and SWMC.

NOTE 2 – SUBSEQUENT EVENTS

On July 1, 2015, the District began including SWMC in the results of its operations as a component unit. The hospital was reopened on October 30, 2015, under the MSA as operated by Sonoma West Medical Center. The name of the hospital was changed to Sonoma West Medical Center. On December 17, 2015, the hospital received its Medicare certification. The District has purchased approximately \$600,000 in equipment for the hospital.

The District also provided \$522,730 to SWMC to complete OSHPD projects that that were necessary for licensure and the reopening of the hospital.

SWMC has faced financial difficulties while operating a hospital without being able to bill and collect from Medicare and certain commercial payors. In January 2016, in accordance with the MSA Article 5.4, the District provided SWMC a \$600,000 tranche from the property taxes received in December. On February 5, 2016, the District then loaned \$400,000 to SWMC at 4% interest for 90 days and collateralized by SWMC’s patient accounts receivable. The hospital has also sought outside gifts and other borrowings to finance its operations during this time period.

NOTE 3 – BANKRUPTCY AND MANAGEMENT’S PLAN

Bankruptcy – By late March 2014, the District’s financial circumstances had reached the point that the District was unable to pay all of its debts as they came due. The Board of Directors accordingly adopted a resolution on April 1, 2014, declaring a fiscal emergency under California Government Code Section 53760.5 and authorizing the Chief Executive Officer to cause the District to seek relief under the U.S. Bankruptcy Code. On April 7, 2014, the District filed a petition under Chapter 9 of the Bankruptcy Code. After a mandatory notice period for potential objections, none were received and the Bankruptcy Court determined that the District is eligible for relief under Chapter 9 and confirmed the validity of the District’s bankruptcy petition.

On April 28, 2014, the District closed the hospital and its emergency room. Thereafter the District had issued Requests for Proposal (RFP) from interested parties who might participate with the District in either resuming operation of the hospital, or offering a different scope of medical services to the residents of the District. The District accepted a proposal from Sonoma West Medical Center to reopen and operate an acute care community hospital. A Managed Services Agreement was formulated and signed March 18, 2015.

With the approval of the Bankruptcy Court, in May-July 2014 the District rejected more than 200 contracts with suppliers and services providers. This step ended current payments on these contracts, and gave rise to claims in the bankruptcy case by the counterparties for contract rejection damages. These claims will be dealt with along with other creditor claims through the bankruptcy process.

**PALM DRIVE HEALTH CARE DISTRICT
NOTES TO FINANCIAL STATEMENTS**

The Bankruptcy Court set October 8, 2014, as the deadline for all creditors of the District to file claims for debts of the District. There have been 181 claims filed to date, asserting claims amounting to \$27,206,080. The validity and amounts of these claims are under review by the District. Through the bankruptcy process, invalid and/or overstated claims have been challenged by the District.

Committees representing general unsecured creditors, and former employees, have been appointed in the bankruptcy process.

To exit from bankruptcy, the District needs to present a plan for adjustment of its debts that meets criteria under the Bankruptcy Code, and seek its confirmation by the Bankruptcy Court. As of this date a plan of adjustment has not been presented to the Bankruptcy Court. It is anticipated that the bankruptcy plan will be completed and presented to the Bankruptcy Court in 2016.

Management's plan – Management, in conjunction with District Board direction, continues to focus upon the bankruptcy process and working with all creditors to develop a plan to submit to the Bankruptcy court. This process will continue into the 2015 and 2016 fiscal years. Management, by virtue of a District Board resolution, negotiated with SWMC to develop a comprehensive plan and model to reopen and manage the hospital. The MSA was signed March 18, 2015, that facilitated the re-opening of the hospital on October 30, 2015, as Sonoma West Medical Center.

NOTE 4 – SIGNIFICANT ACCOUNTING POLICIES

Accounting standards – Pursuant to Government Accounting Standard Board ("GASB") Statement No. 62, *Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 Financial Accounting Standards Board ("FASB") and AICPA Pronouncements*, the District's proprietary fund accounting and financial reporting practices are based on all applicable GASB pronouncements as well as codified pronouncements issued on or before November 30, 1989.

Proprietary fund accounting – The District utilizes the proprietary fund method of accounting whereby revenues and expenses are recognized on the accrual basis and financial statements are prepared using the economic resources measurement focus.

Use of estimates – The preparation of the financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenditures during the reporting period. Although management believes the estimates and assumptions are reasonable, they are based upon information available at the time the estimate or judgment is made and actual amounts could differ from those estimates.

Cash and cash equivalents – Cash and cash equivalents include deposits with financial institutions and investments in highly liquid debt instruments with an original maturity of three months or less. Cash and cash equivalents exclude amounts whose use is limited by board designation or by legal restriction.

Assets limited to use – Assets limited to use are recorded at fair value, securities are generally valued at the last sale price on the last business day of the fiscal year, as quoted on a recognized exchange or utilizing an industry standard pricing service, when available. Assets limited to use include contributor restricted funds, amounts designated by the Board of Directors for replacement or purchases of capital assets, and other specific purposes, and amounts held by trustees under specified agreements. Assets limited to use consist primarily of short term money market funds and cash held with local banking and investment institutions.

Capital assets – Capital assets consist of property and equipment and are reported on the basis of cost, or in the case of donated items, on the basis of fair market value at the date of donation. Routine maintenance and repairs are charged to expense as incurred. Expenditures which increase values, change capacities, or extend useful lives are capitalized. Depreciation of property and equipment and amortization of property under capital leases are computed by the straight-line method for both financial reporting and cost reimbursement purposes over the estimated useful lives of the assets, which range from 10 to 30 years for buildings and improvements, and 3 to 15 years for equipment and software.

The District evaluates prominent events or changes in circumstances affecting capital assets to determine whether impairment of a capital asset has occurred. Impairment losses on capital assets are measured using the method that best reflects the diminished service utility of the capital asset. As of June 30, 2014, the District has determined that an information technology project was impaired. Given that the pause in the construction of this software is significant in duration, and the departure of the team working on this project, management believes that the existing project in process has impaired utility.

**PALM DRIVE HEALTH CARE DISTRICT
NOTES TO FINANCIAL STATEMENTS**

Risk management – The District is exposed to various risks of loss from torts; theft of, damage to, and destruction of assets; business interruption; errors and omissions; employee injuries and illnesses; natural disasters; and medical malpractice. Commercial insurance coverage is purchased for claims arising from such matters.

Net position – Net position of the District are classified as invested in capital assets, net of related debt, restricted net assets, and unrestricted net assets.

Invested in capital assets, net of related debt – Invested in capital assets, net of related debt consists of capital assets, net of accumulated depreciation and reduced by the outstanding balances of any borrowings that are attributable to the acquisition, construction, or improvement of those assets.

Restricted net position – Restricted net position have limits on their use that are externally imposed by creditors (such as through debt covenants), grantors, contributors or by laws or regulations of other governments or constraints imposed by law through constitutional provisions or enabling legislation.

Unrestricted net position – Unrestricted net position are the remainder that do not meet the definition of invested in capital assets, net of related debt or restricted.

Statements of revenues, expenses, and changes in net assets – For purposes of display, transactions deemed by management to be ongoing, major, or central to the provisions of health care services are reported as revenues and expenses. Peripheral or incidental transactions are reported as gains and losses. These peripheral activities include district tax revenues, investment income, interest expense, and grants, contributions and other and are reported as nonoperating.

District tax revenues – The District receives the majority of its financial support from property taxes. These funds are used to support operations and meet required debt service agreements. They are classified as nonoperating revenue as the revenue is not directly linked to patient care. Property taxes are levied by the County on the District's behalf during the year, and are intended to help finance the District's activities during the same year. Amounts are levied on the basis of the most current property values on record with the County. The County has established certain dates to levy, lien, mail bills, and receive payments from property owners during the year. Property taxes are considered delinquent on the day following each payment due date. For the year ended June 30, 2015, district tax revenues included debt service on general obligation bonds of \$430,838, debt service on parcel tax revenue bonds of \$1,642,522, and an operating levy of \$2,057,491.

EHR incentive revenue – The District participates in electronic health record ("EHR") incentive programs. The District recognized an accrued liability of \$1,154,510 as of June 30, 2014, that was included as an EHR incentive expense in the year ended June 30, 2014, as a result of a demand letter received from Centers for Medicare and Medicaid Services ("CMS"). During the year ended June 30, 2015, CMS reversed its decision upon successful appeal from the District. The EHR incentive revenue of \$1,154,510 is recognized as a result of the cancelation of the accrued liability.

Grants and contributions – From time to time, the District receives grants from various governmental agencies and private organizations. The District also receives contributions from related foundation and auxiliary organizations, as well as from individuals and other private organizations. Revenues from grants and contributions are recognized when all eligibility requirements, including time requirements are met. Grants and contributions may be restricted for either specific operating purposes or capital acquisitions.

Compensated absences – District policies permit most employees to accumulate paid time-off benefits that may be realized as paid time-off or as a cash payment upon termination. Expense and the related liability are recognized as paid time-off benefits when earned. Compensated absence liabilities are computed using the regular pay and termination pay rates in effect at the balance sheet date plus an additional amount for compensation-related payments such as social security and Medicare taxes computed using rates in effect at the date of computation. The accrued vacation liability as of June 30, 2015, was \$590,382.

WARN Act – The Worker Adjustment and Retraining Notification Act (WARN) protects workers, their families, and communities by requiring notification of 60 calendar days in advance of mass layoffs. The District had such an event occur during 2014 and accordingly has recognized a liability for payments to be made under the WARN act. Expense and the related liability are recognized as salaries and wages using the regular pay rates in effect at the statement of net position date, plus an additional amount for compensation-related payments such as social security and Medicare taxes computed using rates in effect at the date of computation. The District accrued a WARN Act liability of \$708,894 as of June 30, 2015, and it is included in accrued payroll and related liabilities.

PALM DRIVE HEALTH CARE DISTRICT
NOTES TO FINANCIAL STATEMENTS

Income taxes – The District operates under the purview of the Internal Revenue Code, Section 115, and corresponding California Revenue and Taxation Code provisions. As such, it is not subject to state or federal taxes on income. However, income from the unrelated business activities of the District may be subject to income taxes.

New accounting pronouncements –

GASB Statement No. 72 – Fair Value Measurement and Application – The provisions of GASB Statement No. 72 are effective for financial statements beginning after June 15, 2015. The District has not made an assessment of any changes that will occur upon this statement's implementation.

GASB Statement No. 74 – Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans – The provisions of GASB Statement No. 74 are effective for financial statements beginning after June 15, 2016. The District has not made an assessment of any changes that will occur upon this statement's implementation.

GASB Statement No. 75 – Accounting and Financial Reporting for Postemployment Benefit Plans Other Than Pensions – The provisions of GASB Statement No. 75 are effective for financial statements beginning after June 15, 2016. The District has not made an assessment of any changes that will occur upon this statement's implementation.

GASB Statement No. 76 – The Hierarchy of Generally Accepted Accounting Principles for State and Local Governments – The provisions of GASB Statement No. 76 are effective for financial statements beginning after June 15, 2015. The District has not made an assessment of any changes that will occur upon this statement's implementation.

GASB Statement No. 77 – Tax Abatement Disclosures – The provisions of GASB Statement No. 77 are effective for financial statements beginning after December 15, 2015. The District has not made an assessment of any changes that will occur upon this statement's implementation.

GASB Statement No. 80 – Blending Requirements – The provisions of GASB Statement No. 80 are effective for financial statements beginning after June 30, 2015. The District has not made an assessment of any changes that will occur upon this statement's implementation.

NOTE 5 – CASH AND CASH EQUIVALENTS AND INVESTMENTS

As of June 30, 2015, the District had deposits in a financial institution of \$319,799. All of these funds are in the form of cash and cash equivalents, which were collateralized in accordance with the California Government Code ("CGC"), except for \$250,000 per account that is federally insured.

Under the provisions of the CGC, California banks and savings and loan associations are required to secure the District's deposits by pledging government securities as collateral. The market value of pledged securities must equal at least 110% of the District's deposits. California law also allows financial institutions to secure District deposits by pledging first trust deed mortgage notes having a value of 150% of the District's total deposits. The pledged securities are held by the pledging financial institution's trust department in the name of the District.

District investment policies allow investments in U.S. Government securities and state and local agency funds which invest in U.S. Government securities. These investments, when present, are stated at quoted market values. Changes in market value between years are reflected as a component of investment income in the accompanying statement of revenues, expenses, and changes in net position.

**PALM DRIVE HEALTH CARE DISTRICT
NOTES TO FINANCIAL STATEMENTS**

NOTE 6 – BOARD–DESIGNATED, RESTRICTED FUNDS AND OTHER LONG-TERM INVESTMENTS

As of June 30, 2015, District investment balances and average maturities were as follows:

| Type | Fair-Value | 2015 | |
|-------------------------------|--------------|-----------------------|--------|
| | | Maturities (in years) | |
| | | Less than 1 | 1 to 5 |
| Short-term money market funds | \$ 2,637,615 | \$ 2,637,615 | \$ - |
| Cash held by county | 635,037 | 635,037 | - |
| Total fair-value | \$ 3,272,652 | \$ 3,272,652 | \$ - |

Interest rate risk – Interest rate risk is the risk that changes in market interest rates will adversely affect the fair value of an investment. Generally, the longer the maturity of an investment the greater the sensitivity of its fair value to changes in market interest. The money market mutual funds are presented as an investment with a maturity of less than one year because they are redeemable in full immediately.

Credit risk – Credit risk is the risk that the issuer or other counterparty to an investment will not fulfill its obligations. Management believes that there is minimal exposure related to cash held by the County for bond debt service requirements.

NOTE 7 – CAPITAL ASSETS

At June 30, 2015, capital assets were comprised of the following:

| | Balance at June 30, 2014 | Increases | Decreases | Balance at June 30, 2015 |
|--------------------------------------|-----------------------------|----------------|--------------|-----------------------------|
| Nondepreciable capital assets | | | | |
| Land and land improvements | \$ 5,876,900 | \$ - | \$ - | \$ 5,876,900 |
| Construction work in progress | - | 485,319 | - | 485,319 |
| | 5,876,900 | 485,319 | - | 6,362,219 |
| Depreciable capital assets | | | | |
| Land improvements | 34,493 | - | - | 34,493 |
| Buildings and improvements | 4,565,376 | - | - | 4,565,376 |
| Property under capital leases | 3,201,901 | - | - | 3,201,901 |
| Equipment and software | 7,846,172 | - | (2,398,498) | 5,447,674 |
| | 15,647,942 | - | (2,398,498) | 13,249,444 |
| Less accumulated depreciation | (8,932,789) | (1,537,718) | 1,683,573 | (8,786,934) |
| Capital assets, net | \$ 12,592,053 | \$ (1,052,399) | \$ (714,925) | \$ 10,824,729 |

Total depreciation expense related to capital leases totaled \$808,900 for the year ended June 30, 2015. As of June 30, 2015, accumulated depreciation related to capital leases was \$6,020. Equipment and software, related to capital leases, with a cost basis of \$1,434,498 and no net book value, were taken back by the lessor as of June 30, 2015. A piece of imaging equipment with a net book value of \$714,925 was taken back by the lessor and as such this was recognized as impairment of equipment for the year ended June 30, 2015.

NOTE 8 – MEDICAL MALPRACTICE AND WORKERS’ COMPENSATION COVERAGE AND CLAIMS

The District has joined together with other providers of health care services to form Beta Healthcare Group (“Beta”), a public entity risk pool (the “Pool”) currently operating as a common risk management and insurance program for its members. The District has purchased an extended coverage period medical malpractice insurance policy from the Pool. It is a claims-occurred policy with limits of \$10 million per occurrence, \$20 million in aggregate, and with a self-insured retention level of \$0 per claim reporting period that extends into perpetuity. This does not cover claims occurring after June 30, 2015, but it does insure for claims made after that date, arising before that date, when the hospital was operating. The Pool’s governing agreements specify that the Pool will be self-sustaining through member premiums and will reinsure through commercial carriers for claims in excess of stop-loss amounts.

The District also purchases workers’ compensation insurance from Alpha Fund, a California self-insured workers’ compensation pool, dedicated to public and non-profit health care organizations. The District purchases workers’ compensation insurance under a claims-made policy with limits of \$1 million per occurrence and \$1 million in the annual aggregate. The District also purchases excess insurance coverage up to \$2 million per occurrence or statutory limits.

Based upon the District’s claims experiences, the District has estimated that no accrual is necessary as of June 30, 2015, for accrued malpractice and workers’ compensation costs.

NOTE 9 – BONDS PAYABLE

At June 30, 2015, bonds payable were as follows:

| | 2015 |
|--------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|---------------|
| Health Care District Insured General Obligation Bonds, Series 2000; interest rates ranging from 4.5% to 8.0%; principal due each August 1; interest due semi-annually each February 1 and August 1; final due in 2030; repayments through collection of County property taxes. | \$ 4,510,000 |
| Parcel Tax Revenue Bonds, Series 2005; interest ranging from 3.25% to 5.25%; principal due each April 1; interest due semi-annually each April 1, and October 1; final due in 2024; secured by parcel property taxes. | 7,005,000 |
| Parcel Tax Certificates of Participation (“COPs”), Series 2010; interest ranging from 7.0% to 7.5%; principal due each April 1; interest due semi-annually each April 1, and October 1; final due in 2035; secured by parcel property taxes. | 10,035,000 |
| | 21,550,000 |
| Less current maturities of bonds payable. | (750,000) |
| | \$ 20,800,000 |

**PALM DRIVE HEALTH CARE DISTRICT
NOTES TO FINANCIAL STATEMENTS**

Debt service requirements for bonds payable are as follows at June 30, 2015:

| <u>Year Ending June 30.</u> | <u>General Obligation Bonds</u> | | <u>Revenue Bonds and COPs</u> | |
|-----------------------------|---------------------------------|---------------------|-------------------------------|----------------------|
| | <u>Principal</u> | <u>Interest</u> | <u>Principal</u> | <u>Interest</u> |
| 2016 | \$ 175,000 | \$ 232,703 | \$ 575,000 | \$ 1,064,190 |
| 2017 | 185,000 | 223,510 | 610,000 | 1,032,003 |
| 2018 | 200,000 | 213,390 | 640,000 | 1,000,137 |
| 2019 | 210,000 | 202,530 | 675,000 | 964,817 |
| 2020 | 220,000 | 190,930 | 715,000 | 927,163 |
| 2021-2025 | 1,325,000 | 749,744 | 4,220,000 | 3,978,230 |
| 2026-2030 | 1,775,000 | 323,892 | 5,655,000 | 2,519,587 |
| 2031-2035 | 420,000 | 1,890 | 3,950,000 | 863,487 |
| | <u>\$ 4,510,000</u> | <u>\$ 2,138,589</u> | <u>\$ 17,040,000</u> | <u>\$ 12,349,614</u> |

The following tables summarize the District's bonds long-term debt transactions for the year ended June 30, 2015:

| | <u>Balance June 30, 2014</u> | <u>Increases During Year</u> | <u>2015</u> | | <u>Balance June 30, 2015</u> | <u>Current Portion</u> |
|--------------------------------------|----------------------------------|----------------------------------|----------------------------------|--|----------------------------------|----------------------------|
| | | | <u>Decreases During Year</u> | | | |
| Bonds payable | | | | | | |
| Series 2000 General Obligation Bonds | \$ 4,675,000 | \$ - | \$ (165,000) | | \$ 4,510,000 | \$ 175,000 |
| Series 2005 Parcel Tax Revenue Bonds | 7,330,000 | - | (325,000) | | 7,005,000 | 335,000 |
| Series 2010 Parcel Tax COPs | 10,260,000 | - | (225,000) | | 10,035,000 | 240,000 |
| Capital lease obligations | 1,922,027 | - | (83,268) | | 1,838,759 | 1,383,889 |
| | <u>\$ 24,187,027</u> | <u>\$ -</u> | <u>\$ (798,268)</u> | | <u>\$ 23,388,759</u> | <u>\$ 2,133,889</u> |

NOTE 10 – CAPITAL LEASE OBLIGATIONS

Capital lease obligations outstanding as of June 30, 2015, are as follows:

| <u>Description</u> | <u>Maturity</u> | <u>Interest Rates</u> | <u>Original Issue</u> | <u>June 30, 2015</u> |
|-----------------------------------------------|--------------------------|-----------------------|-----------------------|----------------------|
| Capital leases - equipment net of interest | July 2014 - July 2018 | 4.15% - 8.30% | \$ 3,314,670 | \$ 1,838,759 |
| Less current portion | | | | (1,383,889) |
| | | | | <u>\$ 454,870</u> |

| <u>Description</u> | <u>June 30, 2014</u> | <u>Increases</u> | <u>Decreases</u> | <u>Outstanding June 30, 2015</u> |
|---------------------------|----------------------|------------------|------------------|--------------------------------------|
| Capital lease - equipment | \$ 1,922,027 | \$ - | \$ (83,268) | \$ 1,838,759 |

**PALM DRIVE HEALTH CARE DISTRICT
NOTES TO FINANCIAL STATEMENTS**

Debt service requirements for capital lease obligations are as follows:

Year Ending June 30.

| | | | |
|----------------------|--|----|--------------------|
| 2016 | | \$ | 1,383,889 |
| 2017 | | | 280,310 |
| 2018 | | | 256,784 |
| Less interest | | | <u>(82,224)</u> |
| | | | 1,838,759 |
| Less current portion | | | <u>(1,383,889)</u> |
| | | \$ | <u>454,870</u> |

NOTE 11 – RELATED PARTY TRANSACTIONS

Palm Drive Health Care Foundation – The Palm Drive Health Care Foundation, formerly the West County Health Care Foundation (the “Foundation”), has been established as a nonprofit public benefit corporation under the Internal Revenue Code Section 501(c)(3) to focus on activities which contribute to the health status of residents in Sebastopol and western Sonoma County. The Foundation periodically accepts donations and raises funds to support the District and makes distributions to the District in amounts and for purposes determined by the Foundation’s Board of Trustees and in accordance with any specific donor restrictions. The Foundation is not considered a component unit of the District because management believes the resources of the Foundation are not significant to the District.

During 2015, the Foundation changed its name to Sonoma West Medical Foundation, which is the sole corporate member of Sonoma West Medical Center (SWMC). See Note 1 and Note 13 for more information on SWMC. SWMC is considered a related party in 2015. SWMC continued with similar activities to what the Foundation had done prior to the name change during 2015.

NOTE 12 – COMMITMENTS AND CONTINGENCIES

Litigation – The District may from time-to-time be involved in litigation and regulatory investigations which arise in the normal course of doing business. While the ultimate liabilities cannot now be determined due to uncertainties that exist, management believes the ultimate resolution of these lawsuits and claims will not have a material effect on the District’s financial position.

Operating leases – The District leases various equipment and facilities under operating leases expiring at various dates. Total building and equipment rent expense for the year ended June 30, 2015, was \$12,862. Future minimum lease payments for the succeeding years under operating leases at June 30, 2015, that have initial or remaining lease terms in excess of one year are not considered material.

Regulatory environment – The health care industry is subject to numerous laws and regulations of federal, state, and local governments. These laws and regulations include, but are not necessarily limited to, matters such as licensure, accreditation, government health care program participation requirements, reimbursement for patient services, and Medicare and Medi-Cal fraud and abuse. Recently, government activity has increased with respect to investigations and allegations concerning possible violations of fraud and abuse statutes and regulations by health care providers. The District is subject to routine surveys and reviews by federal, state, and local regulatory authorities. The District has also received inquiries from health care regulatory authorities regarding its compliance with laws and regulations. Although the District’s management is not aware of any violations of laws and regulations, it has received corrective action requests as a result of completed and on-going surveys from applicable regulatory authorities. Management continually works in a timely manner to implement operational changes and procedures to address all corrective action requests from regulatory authorities. Breaches of these laws and regulations and noncompliance with survey corrective action requests could result in expulsion from government health care programs together with the imposition of significant fines and penalties, as well as significant repayments for patient services previously billed. Compliance with such laws and regulations can be subject to future government review and interpretation, as well as regulatory actions unknown or unasserted at this time.

**PALM DRIVE HEALTH CARE DISTRICT
NOTES TO FINANCIAL STATEMENTS**

NOTE 13 – EMPLOYEE BENEFIT PLANS

The District maintains a 401(a) defined contribution retirement plan (the “401(a) Plan”) on a calendar year-end that covers all employees by a collective bargaining agreement and all non-benefited employees who are 21 years of age and have completed one year of credited service. The Plan provides for contributions up to \$40,000 or 100% of eligible participants’ annual compensation, if less. The District’s contribution is discretionary. Eligible employer contributions are 100% vested.

The District sponsored a 457(b) defined contribution retirement plan (the “457(b) Plan”) on a calendar year-end that covered all employees not participating in the 401(a) Plan who are 21 years of age and have completed three months of employment. In September 2014, the District terminated the 457(b) Plan.

There were no contributions to either retirement plan during the year ended June 30, 2015.

FINAL DRAFT

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 PALM DRIVE HEALTH CARE DISTRICT

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UNITED STATES BANKRUPTCY COURT
 NORTHERN DISTRICT OF CALIFORNIA
 SANTA ROSA DIVISION

In Re:

PALM DRIVE HEALTH CARE
 DISTRICT,

Debtor.

Bk. No. 14-10510-AJ

Chapter 9

Judge: Hon. Alan Jaroslovsky

PALM DRIVE PLAN FOR ADJUSTMENT OF DEBTS Dated May 3, 2016

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TABLE OF CONTENTS

I. DEFINITIONS..... 1
II. DESIGNATION OF CLASSES OF CLAIMS AND INTERESTS..... 6
III. TREATMENT OF UNCLASSIFIED CLAIMS..... 7
IV. TREATMENT OF CLASSIFIED CLAIMS AND INTERESTS..... 8
V. EXECUTORY CONTRACTS..... 10
VI. MEANS OF IMPLEMENTATION OF THE PLAN..... 10
VII. INJUNCTION AND CUSTODIA LEGIS..... 17
VIII. RETAINED JURISDICTION..... 18
IX. EFFECT OF CONFIRMATION OF THE PLAN..... 18
X. NON-SUBSTANTIVE MODIFICATION OF PLAN..... 19
XI. CRAMDOWN REQUESTED..... 20

1 Palm Drive Health Care District, a California local health care district (“Palm Drive” or
2 “Debtor”), debtor in this case (the “Bankruptcy Case”) under the United States Bankruptcy Code
3 proposes this Palm Drive Plan For Adjustment Of Debts Dated May 3, 2015 (the “Plan”), pursuant
4 to the provisions of Chapter 9 of the Bankruptcy Code. The Disclosure Statement that accompanies
5 this Plan contains a discussion of the financial condition of Palm Drive and a description of the Plan.
6 Palm Drive commenced this voluntary case under Chapter 9 of the Bankruptcy Code on April 7,
7 2014. Confirmation of the Plan is the culmination of the Chapter 9 process for the adjustment of
8 Palm Drive’s debts. Creditors should thoroughly review both the Plan and the accompanying
9 Disclosure Statement before deciding whether to accept or reject the Plan.

10 **Definitions** used in the Plan are provided in the following Article I.

11 **ARTICLE I**

12 **DEFINITIONS**

13 Unless the context requires otherwise, the following definitions apply in this Plan:

14 1.1 **“Administrative Claim”** means a claim for any cost or expense of administration of
15 a kind specified in Section 503(b) of the Bankruptcy Code that is entitled to priority over general
16 unsecured claims under Section 507(a)(2) of the Bankruptcy Code, as limited by Section 901(a) of
17 the Bankruptcy Code, including, without limitation, (a) any actual or necessary costs and expenses
18 of preserving the property of the Debtor incurred on or after the Petition Date and through and
19 including the Effective Date of the Plan, (b) any cure amounts that must be paid in connection with
20 the assumption of any executory contract or unexpired lease of Palm Drive under Section 365 of the
21 Bankruptcy Code, (c) timely-filed 503(b)(9) Claims, and (d) compensation for fees and reimbursable
22 expenses for legal and other services of professional persons, to the extent both (i) consented to by
23 the Debtor and (ii) approved as reasonable by the Bankruptcy Court under Section 943(b)(3) of the
24 Bankruptcy Code.

25 1.2 **“Administrative Claims Bar Date”** means Bankruptcy Court, the date established
26 by the Confirmation Order as the last day to file proof of an Administrative Claim, which date will
27 be forty-five (45) calendar days after the Effective Date, after which date any Administrative Claim
28 not timely filed will be forever barred, and Palm Drive will have no obligation with respect thereto;

1 *provided, however*, that no filing of proof of an Administrative Claim will be required if such
2 Administrative Claim was incurred (a) in accordance with an order of the Bankruptcy Court or (b)
3 with the written consent of Palm Drive.

4 1.3 **“Allowed Administrative Claim”** means all or any portion of an Administrative
5 Claim that has either been (a) allowed by a Final Order or (b) has not been objected to within the
6 time period established by the Plan or by an order of the Bankruptcy Court.

7 1.4 **“Allowed Claim”** means a claim against Palm Drive, other than an Administrative
8 Claim, as to which:

9 (a) A proof of claim was (i) timely filed not later than the Claims Bar Date
10 established by order of the Bankruptcy Court in the Bankruptcy Case, or any other applicable claim
11 filing deadline, or (ii) deemed filed and allowed under Sections 924 and 925 of the Bankruptcy
12 Code, or (iii) filed late with permission of the Bankruptcy Court after notice and an opportunity for
13 hearing appropriate in the circumstances; and

14 (b) Such claim is not a Disputed Claim, or, if a Disputed Claim, such claim has been
15 allowed in whole or in part by a Final Order, provided that any such claim shall be an Allowed
16 Claim only to the extent stated in any such Final Order. Unless otherwise provided in the Plan or
17 ordered by the Bankruptcy Court, no distributions shall be made under the Plan in respect of the
18 disputed portion of any Disputed Claim until there is a Final Order specifying the allowed amount of
19 such claim.

20 No disputed portion of any claim shall be considered as an Allowed Claim if an
21 objection to the allowance of such claim is made by Palm Drive or another party in interest within
22 the time set by the Plan or the Bankruptcy Court, and such objection to claim has not been denied by
23 a Final Order of the Bankruptcy Court.

24 1.5 **“Allowed Secured Claim”** means that amount of an Allowed Claim which is secured
25 by a lien or subject to offset within the provisions of Section 506(a) of the Bankruptcy Code.

26 1.6 **“Allowed Unsecured Claim”** means any Allowed Claim that is a general unsecured
27 claim, including a Rejection Claim or an Employee Claim, but does not include Allowed Secured
28 Claims, Allowed Administrative Claims, or Priority Claims.

1 1.7 **“Avoiding Actions”** means any rights, claims or causes of action (and any litigation
2 thereon) which may be brought by or on behalf of Palm Drive under any section contained within
3 Chapter 5 of the Bankruptcy Code, or under related state or federal statutes or common law,
4 applicable in a case under Chapter 9 of the Bankruptcy Code, expressly including preference claims,
5 regardless of whether such action has been commenced prior to the Effective Date.

6 1.8 **“Avoiding Actions Claim Bar Date”** means, with respect to any person asserting
7 claims arising from the avoidance of a transfer under chapter 5 of the Bankruptcy Code, the first
8 business day that is at least thirty (30) calendar days after entry of the order or judgment authorizing
9 avoidance of the transfer.

10 1.9 **“Ballot”** means the ballot forms distributed to each holder of an impaired claim that
11 is entitled to vote to accept or reject the Plan, on which form the holder may cast its vote in respect
12 of the Plan, and which must be actually received by Palm Drive on or before the Ballot Deadline in
13 order to be counted.

14 1.10 **“Ballot Deadline”** means the deadline established by the Bankruptcy Court for the
15 receipt by Palm Drive of executed Ballots.

16 1.11 **“Bankruptcy Code”** or **“Code”** means Title 11 of the United States Code, as it was
17 in effect on the date of filing of the Plan, as amended by any amendments applicable to this
18 Bankruptcy Case, and also includes Sections 157, 158, 1334, 1408-1412, and 1452 of Title 28 of the
19 United States Code.

20 1.12 **“Bankruptcy Court”** or **“Court”** means the United States Bankruptcy Court for the
21 Northern District of California, Santa Rosa Division, having jurisdiction over this Bankruptcy Case,
22 and any other courts or panels of courts having competent jurisdiction over the Bankruptcy Case or
23 appeals from orders entered in the Bankruptcy Case.

24 1.13 **“Bankruptcy Rules”** means the rules of practice and procedure in cases under Title
25 11 of the United States Code, as promulgated under 28 U.S.C. § 2075.

26 1.14 **“Chapter 9”** means Chapter 9 of the Bankruptcy Code.

27
28

1 1.15 **“Claims Bar Date”** means October 8, 2014, the deadline date for filing proofs of
2 claim, other than Administrative Claims, by creditors against Palm Drive, established in the
3 Bankruptcy Case by court order and notice to creditors.

4 1.16 **“Claims Objection Deadline”** means, unless extended by the Bankruptcy Court
5 upon an application filed by Palm Drive, the date that is the later of (a) the first business day that is
6 at least 120 calendar days after the Effective Date, and (b) the first business Day that is at least 120
7 calendar days after the date on which a proof of claim in respect of a claim has been filed. For the
8 avoidance of doubt, the Claims Objection Deadline may be extended one or more times by the
9 Bankruptcy Court.

10 1.17 **“Confirmation”** means the entry by the Bankruptcy Court of an order (the
11 **“Confirmation Order”**) confirming the Plan.

12 1.18 **“Creditors’ Committee”** means the Official Committee of Unsecured Creditors
13 appointed by the Office the United States Trustee in the Bankruptcy Case, with any subsequent
14 changes of membership prior to the Effective Date of the Plan.

15 1.19 **“Debtor”** means Palm Drive Health Care District, the debtor in the Bankruptcy Case.

16 1.20 **“Disputed Claim”** means any claim, proof of which has been filed or deemed filed
17 against the Debtor, as to which (a) such claim is listed as disputed, contingent, or unliquidated, or for
18 zero or no amount, on the List of Creditors filed by Palm Drive under Section 924 of the Bankruptcy
19 Code, or (b) an objection or adversary proceeding has been timely filed and has not been withdrawn
20 or disposed of by a Final Order of the Bankruptcy Court.

21 1.21 **“Disputed Claims Reserve Account”** means a non-segregated account, designated
22 on the books and records of Palm Drive and maintained and administered by Palm Drive, for the
23 purpose of holding cash payments attributable to Disputed Claims pending their resolution as
24 allowed or disallowed.

25 1.22 **“District”** means Palm Drive Health Care District.

26 1.23 **“Effective Date”** means the business day designated as such by Palm Drive that is
27 not later than fifteen (15) calendar days following the entry of the Confirmation Order, unless such
28 order is stayed by order of a court with original or appellate jurisdiction over this Bankruptcy Case,

1 in which event such date shall be the first business day on or after the eleventh calendar day after
2 such stay expires.

3 1.24 **“Employees Committee”** means the official committee of former employees of Palm
4 appointed in the Bankruptcy Case.

5 1.25 **“503(b)(9) Claim”** means a claim of a vendor to Palm Drive that provided *goods* to
6 Palm Drive that were *received* during the 20 days *before* the commencement of the Bankruptcy
7 Case, *i.e.*, from March 18 through April 6, 2014.

8 1.26 **“Final Order”** means an order of the Bankruptcy Court as to which the appeal period
9 has expired without an appeal having been timely taken or, if an appeal is timely taken, such order
10 has been affirmed on appeal and any time for further appeal or petition has expired without any such
11 further appeal or petition having been filed.

12 1.27 **“General Unsecured Claim”** means an Unsecured Claim, including any claim
13 arising from the rejection of an unexpired lease or other Executory Contract.

14 1.28 **“Hospital”** means the public hospital operated on Palm Drive’s behalf in Palm
15 Drive’s facilities by SWMC (or any successor to SWMC as the Board of Directors may designate,
16 within the provisions of California health care district law).

17 1.29 **“List of Creditors”** means the list of creditors filed by Palm Drive in the Bankruptcy
18 Case under Section 924 of the Bankruptcy Code as it has been amended in its entirety by Palm Drive
19 [Docket No. 159, filed August 21, 2014].

20 1.30 **“MSA”** means the Management and Staffing Services Agreement entered into
21 between Palm Drive and Sonoma West Medical Center as of March 18, 2015.

22 1.31 **“Petition Date”** means April 7, 2014, the date on which Palm Drive commenced the
23 Bankruptcy Case.

24 1.32 **“Plan”** means this Palm Drive Plan For Adjustment Of Debts Dated May 3, 2016,
25 and filed by Palm Drive with the Bankruptcy Court, including any modification(s) or amendment(s)
26 thereto.

27 1.33 **“Priority Claim”** means any Allowed Claim entitled to priority pursuant to Section
28 507(a)(2) of the Bankruptcy Code.

1 Any claim of the counsel for the Creditors' Committee shall be allowed at the amount
2 determined as reasonable by the Bankruptcy Court, after application and review, but in any event not
3 to exceed \$50,000.

4 No claim of counsel for the Employees Committee shall be allowed as administrative
5 expense or otherwise.

6 ARTICLE IV

7 TREATMENT OF CLASSIFIED CLAIMS AND INTERESTS

8 The classified claims designated in Article II of the Plan will receive the treatment specified
9 in this Article IV. Classes 2, 3, 4, 5A, 5B, and 6 are impaired under the Plan. Class 1 is not
10 impaired under the Plan.

11 4.1 Class 1 Claims — Secured Claims of Series 2000 GO Bonds: The holders of allowed
12 Secured Claims of the Series 2000 GO Bonds shall retain, unaltered, the legal, equitable, and
13 contractual rights to which such claim is entitled according to the existing terms thereof.

14 4.2 Class 2 Claims — Secured Claims of Series 2005 Revenue Bonds. The holders of
15 allowed Secured Claims of the Series 2005 Revenue Bonds shall retain, unaltered, the legal,
16 equitable, and contractual rights to which such claim is entitled according to the existing terms
17 thereof, except that payment of principal will be deferred for two years from the current repayment
18 schedule, and the terms shall be modified to provide for a reserve solely of the next one semi-annual
19 payment due. When principal payment is resumed, payments will be in the annual amounts called
20 for under the bond terms adjusted for the deferral period, and the maturity date of the Series 2005
21 Revenue Bonds will be two years later than the current maturity date. Interest will be kept current
22 on these Bonds throughout, including during the principal deferral period.

23 All reserves of any category or nature held by the indenture trustee under the terms of the
24 Series 2005 Revenue Bonds, other than the rolling one next-payment reserve, shall be released to the
25 District fifteen (15) business days after the Effective Date.

26 4.3 Class 3 Claims – Secured Claims of Series 2010 COPs. The holders of allowed
27 Secured Claims of the Series 2010 COPs shall retain, unaltered, the legal, equitable, and contractual
28 rights to which such claim is entitled according to the existing terms thereof, except:

1 (a) Payment of principal will be deferred for two years from the current repayment
2 schedule. When principal payment is resumed, payments will be in the annual amounts called for
3 under the bond terms adjusted for the deferral period, and the maturity date will be two years later
4 than the current maturity date. Interest will be kept current on these COPs throughout, including
5 during the principal deferral period.

6 (b) Interest rates payable on the Series 2010 COPs will be reduced by two percent
7 (2%) from the rates currently provided under the terms of these instruments.

8 (c) All reserves of any category or nature held by the indenture trustee under the
9 terms of the Series 2010 COPs, other than a rolling one next-payment reserve – including without
10 limitation funds held by the indenture trustee for the Series 2010 COPs in the Reserve Fund
11 established and maintained under Article VI of the Trust Agreement dated as of May 1, 2010 – shall
12 be released to the District fifteen (15) business days after the Effective Date.

13 4.4 Class 4 – Former Employees. Allowed claims of former employees (unless they fall
14 into, or choose to opt into, Class 6 below) will receive fifty percent (50%) distribution of the allowed
15 amount of their claims, payable in two equal installments. The first installment will be paid six
16 months from the Effective Date. The second, final installment will be paid 12 months from the
17 Effective Date

18 4.5 Class 5A – General Unsecured Claims \$100,000 or Less. Allowed General
19 Unsecured Claims of \$100,000 or less, including executory contract Rejection Claims other than
20 claims in Classes 4, 5B, and 6, will receive distribution of forty percent (40%) of the allowed amount
21 of their claims, paid in two equal installments, with the first installment 90 days from the Effective
22 Date and the second, final installment on the first anniversary date from the Effective Date.

23 4.6. Class 5B – General Unsecured Claims Greater Than \$100,000. Allowed General
24 Unsecured Claims, including executory contract Rejection Claims, other than claims in Classes 4,
25 5B, and 6, will receive distribution of sixty percent (60%) of the allowed amount of their claims,
26 paid in five equal installments, with the first installment paid on the second anniversary date from
27 the Effective Date and the subsequent four installments on the succeeding anniversary dates from the
28 Effective Date.

1 (a) As of and after the Effective Date, the duly elected Palm Drive Board of
2 Directors, as constituted from time to time, shall will continue to govern the Palm Drive Health Care
3 District. Palm Drive will administer, control, manage, and operate the property and revenues of the
4 District in accordance with the Plan, the District's governing documents, applicable California law,
5 and other applicable laws.

6 (b) Palm Drive will continue to receive those tax revenues collectible from
7 residents of the District for its benefit pursuant to laws and official measures in effect as of the
8 Petition Date, subject to the debt service obligations to which portions of such revenues are
9 dedicated except as modified by this Plan.

10 (c) Palm Drive will exercise control and oversight over the Hospital through the
11 MSA with SWMC (or any successor to SWMC as the Board of Directors may designate, within the
12 provisions of California health care district law). The Governing Body established under the MSA,
13 a subcommittee of Palm Drive's Board of Directors, is the mechanism through which Palm Drive
14 will exercise its oversight of Hospital operations.

15 (d) Palm Drive will provide financial support to SWMC for facilities maintenance
16 and other purposes as provided by the MSA, to the extent provided therein, provided, however, that
17 Palm Drive, consistent with the terms of the MSA, will not be responsible for any operating losses or
18 debts of SWMC, and Palm Drive's financial support to SWMC will not impair Palm Drive's ability
19 to meet all distributions to creditors required under the terms of this Plan.

20 (e) In addition to operating, through SWMC, the Hospital, Palm Drive will
21 continue to engage in community-based health services. Palm Drive may do so directly through
22 programs of its own, or indirectly through cooperation with and financial support for other agencies
23 and entities active in Palm Drive's territory.

24 6.2 Payment of Administrative and Priority Claims: From cash on hand, Palm Drive will
25 pay promptly all payments under this Plan required to be made in connection with the Effective
26 Date, including:

27 (a) All Administrative Claims required to be paid on or about the Effective Date,
28 unless the holder of any such claim agrees in writing to a later payment date. Palm Drive will pay

1 any subsequently allowed Administrative Claims in full promptly after a Final Order allowing such
2 claim, unless otherwise agreed in writing by the holder of any such claim.

3 (b) Allowed Priority Claims, including allowed 503(b)(9) Claims, required to be paid
4 on or about the Effective Date.

5 6.3 Payment of Distributions on Classified Claims: In its annual budget process, and any
6 supplemental budgeting decisions as may be necessary, Palm Drive shall provide for payment of the
7 distributions to the classes of claims provided under Article IV of this Plan, according to the
8 treatment of those classes as provided therein. In making such distributions, Palm Drive will make
9 appropriate calculations, and provide for appropriate reserves in the Disputed Claims Reserve
10 Account as provided in Section 6.11(d) below. Palm Drive will act as disbursing agent under the
11 Plan with regard to all payments and distributions to be made to creditors or other parties in interest
12 hereunder, without bond.

13 6.4 Objections to Claims: Palm Drive is authorized to review and object to claims.
14 Subject to making the payments required by Article IV of the Plan, and the funding of the reserve
15 required by Section 6.11(d), Palm Drive is authorized to enter into compromises to allow and satisfy
16 Disputed Claims, and to sell, liquidate, or abandon any claim or cause of action of Palm Drive
17 against any third party.

18 6.5 Post-Confirmation Powers of Palm Drive: Subject to the other express provisions of
19 the Plan, Palm Drive:

20 (a) is authorized to determine whether Palm Drive will pursue any claims or causes
21 of action available under applicable law (including Avoiding Actions); and

22 (b) if it determines that any such claim or cause of action should be pursued, to
23 commence, prosecute, or compromise such claim. Any recovery on such claim or cause of action
24 shall be considered property of Palm Drive, and treated as any other assets under the terms of the
25 Plan.

26 6.6 Post-Confirmation Reporting

27 (a) Annually, Palm Drive will file with the Bankruptcy Court a post-confirmation
28 status report ("Report"), the purpose of which is to explain the progress made toward full

1 administration of the confirmed plan of reorganization. The first Report will be filed for the portion
2 of the calendar year from the date of confirmation to the end of the period. Subsequent reports will
3 be filed at the expiration of each calendar year thereafter until entry of a final decree closing the
4 Chapter 9 Case. Reports will be filed with the Bankruptcy Court not later than forty-five (45) days
5 after the expiration of the reporting period.

6 (b) The Report will include a statement of receipts and disbursements, with the
7 ending cash balance, for the reporting period. The Report will also include information sufficiently
8 comprehensive to enable the Bankruptcy Court to determine: (1) whether the order confirming the
9 Plan has become final; (2) whether payments under the Plan have commenced; (3) whether
10 payments required under the Plan are current; and (4) whether all motions, contested matters, and
11 adversary proceedings have been finally resolved.

12 (c) A copy of each Report will be served promptly on such persons or entities as
13 have made a request for service of such Reports in writing with the Bankruptcy Court ("Post-
14 Confirmation Notice List"), with copy of such request served on Palm Drive and its counsel not later
15 than the day on which it is filed with the Bankruptcy Court.

16 (d) At such time as Palm Drive deems appropriate, consistent with applicable law
17 and rules, but only after payments required by Sections 4.4, 4.5, 4.6, and 4.7 of this Plan, and the
18 funding of the Disputed Claims Reserve Account required by Section 6.11(d), Palm Drive will file
19 an application for entry of a final decree in this Bankruptcy Case, and shall serve the application on
20 the Post-Confirmation Notice List, together with a proposed final decree. Palm Drive will prepare
21 and file any status report that may be required by the Bankruptcy Court in connection with the
22 issuance of a final decree. Parties on the Post-Confirmation Notice List will have twenty-one (21)
23 days within which to object or otherwise comment upon application to the Bankruptcy Court for
24 entry of the final decree.

25 6.7 Other Post-Confirmation Powers: Palm Drive is authorized to do or cause to be done
26 all things necessary and appropriate to administer and execute the Plan, consistent with the terms of
27 the Plan, the Confirmation Order, and the Bankruptcy Code and the Bankruptcy Rules to the extent
28

1 applicable. Palm Drive shall have full power and authority to execute and deliver any and all
2 documents necessary or appropriate to carry out the Plan.

3 6.8 Creditors' Committees: On the Effective Date, the Creditors' Committee and
4 the Employees Committee will be dissolved. Post-confirmation, the former members of these
5 committees will enjoy all defenses and immunities available under the Bankruptcy Code. Palm
6 Drive releases any and all claims, rights, and causes of action that it may hold against either
7 Committee or any Committee member arising as a result of any action taken or omitted to be taken
8 by either Committee or any of its members in connection with or related to the solicitation of votes
9 on the Plan, the confirmation of the Plan, or any action otherwise within the scope of the duties and
10 powers of the Committee or any Committee member, whether granted under the Bankruptcy Code,
11 under applicable court order, or otherwise, except to the extent that such claims or causes of action
12 arise as a result of willful misconduct by the Committee or any Committee member acting as such,
13 as the case may be. Notwithstanding the foregoing, the provisions of this Subsection 6.8 are not
14 intended to, and shall have no effect on, the allowability (or lack thereof) of any creditor claim held
15 by any member of a Committee, or the status or result of any objection to such creditor claim held by
16 any member of a Committee.

17 6.9 Avoiding Actions: All Avoiding Actions available to Palm Drive are preserved after
18 the Effective Date, and may be prosecuted post-confirmation by Palm Drive, subject to the following
19 provisions:

20 (a) Except as otherwise provided in paragraph (b) below, any action to recover on an
21 Avoiding Action must be commenced in a court of competent jurisdiction not later than six (6)
22 months after the Effective Date, or it will be barred.

23 (b) The deadline set forth in paragraph (a) above for commencing an action may be
24 extended by:

- 25 (1) Written agreement of the proposed defendant; or
26 (2) Order of the Bankruptcy Court, made on a showing of good cause after
27 motion served before the expiration of the deadline (including any previously extended deadline) on
28 the proposed defendant; provided, that in the event the Bankruptcy Court denies any timely brought

1 motion to extend the deadline, the deadline shall nevertheless be extended until fourteen (14)
2 calendar days after the date of entry of the order denying the requested extension.

3 6.10 Unclaimed Property: If a distribution to the holder of an Allowed Claim remains
4 unclaimed for forty-five (45) days following the attempted distribution, Palm Drive shall use
5 reasonable diligence to attempt to locate such claim holder. If after reasonable diligence, such claim
6 holder still cannot be located, such distribution shall be conclusively deemed waived by the holder of
7 the claim.

8 6.11 Disputed Claims:

9 (a) Except as otherwise provided in paragraph (b) immediately below, any objection
10 to claims must be filed no later than one-hundred twenty (120) days after the Effective Date.

11 (b) The deadline set forth in paragraph (a) above for objecting to any claim may be
12 extended by:

13 (1) Written agreement of the holder of the claim; or

14 (2) Order of the Bankruptcy Court, made on a showing of good cause after
15 motion served before the expiration of the deadline (including any previously extended deadline) on
16 the holder of the claim; provided, that in the event the Bankruptcy Court denies any timely brought
17 motion to extend the deadline, the deadline shall nevertheless be extended until fourteen (14)
18 calendar days after the date of entry of the order denying the requested extension.

19 (c) Notwithstanding any other provisions of this Plan, the disputed portion of a
20 Disputed Claim shall not receive any distribution, unless and until the status of an Allowed Claim is
21 attained for such disputed amount.

22 (d) Palm Drive will maintain and administer, by designation on its books and
23 records, a non-segregated Disputed Claims Reserve Account, subject to the following provisions:

24 (1) In the event that a claim is disputed and has not become an Allowed
25 Claim as of the date of any distribution to creditors, an amount of cash sufficient to pay the
26 applicable distribution to the Disputed Claim if allowed in the full amount for which it is asserted
27 shall be designated in the Disputed Claims Reserve Account.

28

1 (2) If and when a Disputed Claim becomes an Allowed Claim by entry of a
2 Final Order so ruling, the appropriate portion of the funds designated in the Disputed Claims
3 Reserve Account with respect to such claim shall be paid to the holder of the Disputed Claim as soon
4 as practicable thereafter.

5 (3) Funds attributable to the disallowed portion of Disputed Claims which are
6 disallowed in whole or in part by a Final Order shall be released from the Disputed Claims Reserve
7 Account.

8 (4) The Final Order which either allows or disallows a Disputed Claim shall
9 also specify and order the amounts that are to be disbursed from the Disputed Claims Reserve
10 Account.

11 6.12 Administrative Claims Bar Date: Except as otherwise provided in paragraphs (a) and
12 (b) immediately below, requests for payment of all Administrative Claims which are due on or about
13 the Effective Date (specifically including requests by professionals for compensation or expenses in
14 connection with services performed before the Effective Date) must be filed with the Bankruptcy
15 Court and served on Palm Drive not later than thirty (30) calendar days following the Effective Date,
16 or be forever barred and Palm Drive will then not have any further liability therefor.

17 (a) The bar date for filing a request for payment of an Administrative Claim may
18 be extended by written agreement between the claimant and Palm Drive, or by Bankruptcy Court
19 order by request for good cause, on notice to Palm Drive, filed and served prior to the bar date.

20 (b) The bar date established in this Section 6.12 does not apply to post-petition
21 ordinary trade payables or other obligations incurred in the ordinary course of Palm Drive's post-
22 petition activities, which claims will, pursuant to Section 3.1 of this Plan, be payable in the ordinary
23 course in accordance with the existing terms otherwise applicable to such obligations.

24 6.13 Preservation of Claims and Objections: Nothing in the Plan is intended to, nor will it,
25 limit in any way the ability of Palm Drive to:

26 (a) exercise the rights and powers conferred upon it by applicable bankruptcy law,
27 including but not limited to the pursuit of Avoiding Actions and the prosecution of objections to
28 claims (whether or not their holders have accepted the Plan),

1 (b) pursue recovery on any and all other causes of action held by Palm Drive prior to
2 Confirmation under otherwise applicable non-bankruptcy laws, or

3 (c) exercise the rights and powers of governance and take other official actions
4 through Palm Drive's Board of Directors and officers; provided that all such powers and actions are
5 exercised in all respects in compliance with the provisions of the Plan and the Confirmation Order,
6 and provided further that no claims, causes of action, rights, avoiding powers, other powers of Palm
7 Drive, or objections to any claims against Palm Drive whatsoever are released, waived, deemed
8 adjudicated, or allowed by confirmation of the Plan except as expressly provided in the Plan or the
9 Confirmation Order.

10 ARTICLE VII

11 INJUNCTION AND CUSTODIA LEGIS

12 7.1 Confirmation of this Plan constitutes an injunction prohibiting any person from taking
13 any act, commencing any suit, or enforcing any right, including the right to a judicial or non-judicial
14 foreclosure of any lien, which has the effect of asserting, liquidating, or enforcing any claim
15 provided for herein against any property or revenues of Palm Drive, and prohibiting any person from
16 taking any act, commencing any suit, or enforcing any right which has the effect of asserting,
17 liquidating, or enforcing any claim provided for herein against Palm Drive except as provided
18 hereunder.

19 7.2 All of the property of Palm Drive shall be retained by Palm Drive as of and from the
20 Effective Date, free and clear of all claims and interests of creditors, subject to the provisions of the
21 Plan, and shall be under the control and direction of, and shall be administered by, Palm Drive.

22 7.3 Entry of the Confirmation Order acts as a discharge of any debt of Palm Drive that
23 arose prior to Confirmation to the extent provided by Section 944(b) of the Bankruptcy Code,.
24 Neither Palm Drive nor its Board of Directors or officers shall have any liability to any creditors
25 other than to make the distributions expressly provided for under the Plan.

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ARTICLE VIII

RETAINED JURISDICTION

After Confirmation, the Bankruptcy Court shall retain jurisdiction pursuant to Section 945 of the Bankruptcy Code and this Plan to enforce the provisions, purposes, and intent of this Plan or any modification hereof, including without limitation, matters or proceedings relating to:

8.1 Allowance, disallowance, reconsideration, estimation, compromise, settlement, adjustment, treatment, or liquidation of claims and objections thereto;

8.2 Allowance of claims and requests for payment of administrative expenses of the Debtor;

8.3 Resolution of controversies and disputes, including disputes regarding interpretation of the Plan and the Confirmation Order, and the correction of any mistake, defect, or omission regarding interpretation or enforcement of the Plan and the Confirmation Order;

8.5 Modification(s) of the Plan pursuant to Section 1127(d) or Section 942 of the Bankruptcy Code;

8.6 Adjudication of any actions brought by post-confirmation by Palm Drive to enforce any right or recover any claim created, granted, or preserved under this Plan;

8.7 Entry of orders in aid of implementation of this Plan;

8.8 Such other matters for which jurisdiction is provided under the Bankruptcy Code, the Plan, or the Confirmation Order; and

8.9 Entry of a final decree closing the Bankruptcy Case.

ARTICLE IX

EFFECT OF CONFIRMATION OF THE PLAN

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Upon Confirmation, pursuant to Section 944(a) of the Bankruptcy Code, the provisions of the Plan shall be binding upon Palm Drive, any person or entity acquiring property under the Plan, and any creditor, whether or not the claim of such creditor is impaired under the Plan and whether or not such creditor or interest holder has accepted the Plan.

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ARTICLE X

NON-SUBSTANTIVE MODIFICATION OF PLAN

Palm Drive may, after such notice as the Bankruptcy Court determines to be appropriate, modify the Plan prior to the Effective Date, if the Bankruptcy Court determines that such modification does not materially and adversely affect or impair the interest of any holder of a claim who has not accepted such modification. Such modification shall be deemed accepted by all holders of claims or interests who have previously accepted the Plan.

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ARTICLE XI

CRAMDOWNS REQUESTED

Palm Drive requests that, if a class of impaired claims does not accept this Plan by the requisite majorities, confirmation nevertheless proceed under Section 1129(b) of the Bankruptcy Code.

DATED: May 3, 2016

PALM DRIVE HEALTH CARE DISTRICT
Debtor

By: /s/ Jim Maresca
Jim Maresca
President of the Board of Directors

FOX ROTHSCHILD LLP

By: /s/ Dale L. Bratton
Michael A. Sweet
Dale L. Bratton
Attorneys for Debtor
Palm Drive Health Care District

EXHIBIT D

ASSUMPTIONS IN CONNECTION WITH DISTRICT PLAN PROJECTIONS

1. Class 1 – Series 2000 GO Bonds : Unimpaired; paid according to existing pre-bankruptcy terms.
2. Class 2 – Series 2005 Revenue Bonds: Principal payments deferred for two years; interest kept current during deferral period; all reserves held by indenture trustee other than rolling next one-payment-due reserve released to District upon Plan confirmation.
3. Class 3 – Series 2010 COPs: Principal payments deferred for two years; interest kept current during deferral period; all reserves held by indenture trustee other than rolling next one-payment-due reserve released to District upon Plan confirmation; interest rates reduced by 2% from existing pre-bankruptcy rates.
4. Class 4 – Former employees: Receive 50% on allowed claims, paid in two equal installments; first installment six months after Plan effective date; second installment 12 months after Plan effective date.
5. Class 5A – General Unsecured Claims \$100,000 or less: Receive 40% on allowed claims, paid in two equal installments, first installment 90 days from the Plan effective date, second installment on the first anniversary date from Plan effective date.
6. Class 5B – General Unsecured Claims Greater than \$100,000: Receive 60% on allowed claims, paid in five equal installments, first installment on second anniversary from Plan effective date, subsequent four installments on the succeeding anniversary dates from Plan effective date.
7. Class 6 – Convenience Class (Unsecured Claims \$10,000 or less in amount): Receive 50% on allowed claims 90 days after Plan effective date; claims in Classes 4 and 5A may reduce their claims to this amount and “opt-down” to this class to receive this early payout; assumed that significant number of small trade creditors will choose to opt down.
8. ESTIMATES: The amounts in these Projections, including total amounts to be paid to each class over the life of the Plan are estimates only, and are subject to change depending on such factors as whether there are claims in any class that are subject to objection as to amount, classification, or priority. By way of example only, there are claims filed as secured that are plainly not secured, and claims filed as priority that are plainly not priority.

District Bankruptcy Plan Projections

| | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 | 2021 | 2022 | |
|---------------------------------------------------------------------|---------|------------------|------------------|------------------|------------------|------------------|------------------|------------------|-----------|
| Tax Revenue Analysis | | | | | | | | | |
| Gross Tax Receipts | | 3,874,849 | 3,689,849 | 3,689,849 | 3,689,849 | 3,689,849 | 3,689,849 | 3,689,849 | |
| Withholding for next debt service | | 422,913 | 422,913 | 1,009,030 | 1,023,037 | 1,048,884 | 1,048,884 | 1,048,884 | |
| Net Tax Receipts | | 3,451,936 | 3,266,936 | 2,680,819 | 2,666,812 | 2,640,965 | 2,640,965 | 2,640,965 | |
| Release of Reserves | | 2,300,000 | 0 | 0 | 0 | 0 | 0 | | |
| Receipts from pre-petition AR | | 0 | 0 | 0 | 0 | 0 | 0 | | |
| Other Income | | | | | | | | | |
| Gross Available Cash | | 5,751,936 | 3,266,936 | 2,680,819 | 2,666,812 | 2,640,965 | 2,640,965 | 2,640,965 | |
| Debt Service on 2000 | | 416,988 | 422,738 | 422,538 | 421,618 | 424,958 | 427,328 | 428,890 | |
| DebtService on 2005 | | 336,368 | 315,200 | 315,200 | 664,168 | 667,198 | 664,268 | 664,268 | |
| Debt Service on 2010 | | 434,925 | 516,775 | 516,775 | 661,094 | 678,736 | 797,524 | 797,524 | |
| Net Available Cash | | 4,563,655 | 2,435,136 | 1,849,219 | 1,928,962 | 1,893,110 | 1,800,729 | 1,799,167 | |
| District Expenses | | | | | | | | | |
| Post-petition ongoing | | 850,000 | 850,000 | 550,000 | 550,000 | 550,000 | 350,000 | 350,000 | |
| Post-petition bankruptcy | | 50,000 | 0 | 0 | 0 | 0 | 0 | 0 | |
| Deferred maintenance, ongoing maintenance, equipment & charity care | | 1,000,000 | 1,000,000 | 1,000,000 | 1,000,000 | 1,000,000 | 500,000 | 500,000 | |
| ACA Population Health services | | 100,000 | 100,000 | 150,000 | 150,000 | 150,000 | 150,000 | 150,000 | |
| Available for pre-petition claims | | 2,803,655 | 2,565,360 | 2,066,875 | 1,499,638 | 896,549 | 901,079 | 904,047 | |
| Unsecured Claims Distributions | | | | | | | | | |
| Trade Class >100k | | 0 | 0 | 796,199 | 796,199 | 796,199 | 796,199 | 796,119 | 3,980,915 |
| Trade Class <100k | | 238,126 | 238,126 | 0 | 0 | 0 | | 0 | 476,252 |
| Employee class | | 409,578 | 409,578 | 0 | 0 | 0 | | 0 | 819,156 |
| Convenience class | | 75,727 | 0 | 0 | 0 | 0 | | 0 | 75,727 |
| Total Unsecured Claims Distributions | | 723,431 | 647,704 | 796,199 | 796,199 | 796,199 | 796,199 | 796,119 | 5,352,050 |
| Ending cash balance | 240,000 | 2,080,224 | 1,917,656 | 1,270,676 | 703,439 | 100,350 | 104,880 | 107,928 | |



**HEALDSBURG
DISTRICT HOSPITAL**

Bridging Health

May 11, 2016

Mark Bramfitt, Executive Officer
Sonoma Local Agency Formation Commission
575 Administration Drive, Room 104A
Santa Rosa CA 95403

RE: Request for Financial Information

Dear Mr. Bramfitt:

In response to your letter dated April 28 requesting financial information, I am pleased to provide the data you have asked for to assist with your financial analysis.

- For the most recent fiscal year with complete and/or audited information, the North Sonoma County Healthcare District dba Healdsburg District Hospital received \$3,357,254 in parcel levy taxes. There are 22,677 parcels assessed within the District, and the amount paid per parcel is \$150.
- In response to your inquiry regarding revenue, the unaudited amount received during the time period beginning January 1, 2015 and ending December 31, 2015 is \$99,934,716 in gross revenue, and \$40,210,165 in net revenue for the same time period.

Should you have any questions about the information provided above or need any clarification, please do not hesitate to contact me.

Thank you.

Sincerely,

Nancy Schmid, CEO
North Sonoma County Healthcare District dba Healdsburg District Hospital

NSCHD

NORTH SONOMA COUNTY HEALTHCARE DISTRICT

SONOMA LOCAL AGENCY FORMATION COMMISSION

575 ADMINISTRATION DRIVE, ROOM 104A, SANTA ROSA, CA 95403
(707) 565-2577 FAX (707) 565-3778
www.sonomalafco.org

June 9, 2016

Ms. Alanna Brogan, Executive Director
Palm Drive Health Care District
612 Petaluma Avenue
Sebastopol, CA 95472

Re: Request for Information to Support Municipal Services Review

Dear Ms. Brogan:

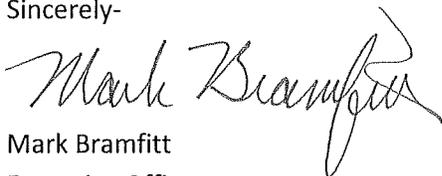
The Sonoma Local Agency Formation Commission will be drafting a Municipal Service Review of the Palm Drive Health Care District, and is seeking information from the District to support our analysis.

Attached is a list of our initial questions; although we will endeavor to limit impact on your limited staff resources, we may submit additional questions as we draft our report.

We would appreciate receiving your response as soon as possible. We intend to have a public review draft of the report, which will be made available for comment by affected agencies and interested parties, completed by July 8th.

If you have any questions, please feel free to contact me. We truly appreciate your support in this matter.

Sincerely-



Mark Bramfitt
Executive Officer

SONOMA LOCAL AGENCY FORMATION COMMISSION

575 ADMINISTRATION DRIVE, ROOM 104A, SANTA ROSA, CA 95403

(707) 565-2577 FAX (707) 565-3778

www.sonomalafco.org

Request for Information from Palm Drive Health Care District June 9, 2016

1. Has the District completed the capital management plan that projects future expenses for maintenance of the Districts real property that was underway in 2013? (Please provide a copy if so; if not, please explain.)
2. Does the District have a capital management plan for equipment purchases, leases, and maintenance?
3. Please provide a listing of board members and terms served since the District was formed, and the geographical location that each board member resided in at the time of service (City, town or street is sufficient).
4. Is the District currently performing an appraisal of District-owned real property? If so, what is the intended use or purpose of the appraisal?
5. Does the District plan to, or is it considering a plan to encumber the real property in any way in the next twelve months?
6. Do current District board members have current Form 700 disclosure forms on file with the California Fair Political Practices Commission?
7. Have District Board members completed Ethics Training meeting the requirements of AB 1234, Chapter 700, Stats. Of 2005, and are certificates of completion available at the District's offices? If not, please explain.
8. Have District Board members completed any training programs related to compliance with the Brown Act?
9. Please forward any public records, including meeting minutes, related to discussions regarding establishment of the governance structure described in Article 1 the Management and Staffing Services Agreement entered into by the District and Sonoma West Medical Center.
10. What plans, if any, does the District have to borrow funds against unencumbered tax revenues in the next twelve months?
11. What is the current asset value of property, plant, and equipment owned by the District?
12. Please provide documentation regarding the \$400,000 loan to SWMC made by the District this year.



RECEIVED

July 7, 2016
SONOMA LAFCO
LOCAL AGENCY
FORMATION COMMISSION

Response to LAFCO Questions Related

1. Has the District completed the capital management plan that projects future expenses for maintenance of the District's real property that was underway in 2013 (please provide a copy if so; if not please explain).

The capital management plan from 2013 was not completed. The current plant maintenance Director/Chief Engineer is working on one but it will not be ready in time for this review.

2. Does the District have a capital management plan for equipment purchases, leases and maintenance?

Capital Equipment - Under the Management and Staffing Services Agreement signed in 2015, SWMC is obligated to determine their capital equipment needs and present them to the District board. They have presented a list of desired capital equipment but it needs to be prioritized and that has not been done yet.

Building Maintenance - We do have plans for building maintenance. The roof needs to be replaced in the next 2 years.

We did have CASP survey and are working on a complete plan of correction related to this. The SWMC plant maintenance staff has begun to make some of the corrections as they work in the areas of need.

Lease -- There is no plan related to leases.

3. Please provide a list of board members and terms served since the District was formed, and the geographical location that each board member resided in at the time of service.

Please see the attached document

4. Is the District currently performing an appraisal of District owned property? If so, what is the intended use or purpose of the appraisal?

The District is not currently performing an appraisal. The last appraisal was obtained in 2000. The District may choose to update that appraisal in the next 6 months if the benefit justifies the cost, but right now, there is no immediate purpose or intended use for such an appraisal.

5. Does the District plan to, or is it considering a plan to encumber the real property in any way in the next 12 months?

There are absolutely no plans to do this.

6. Do current District board members have current Form 700 disclosure forms on file with the California Fair Political Practices Commission?

The County, not the FPPC, is the code reviewing body and filling officer for the District, and it maintains the Form 700's. As required, these forms were submitted to the County by the District on or before April 1, 2016.

7. Have District board members completed the Ethics Training meeting the requirements of AB 1234, Chapter 77, Stats. of 2005, and are certificates of completion available in the District's offices. If not, please explain.

Yes, the District Board members completed the training and certificates are available.

8. Have District board members completed any training programs related to compliance with the Brown Act?

Yes, once within 6 months of their election, and thereafter once every 2 years, in accordance with AB 1234.

9. Please forward any public records, including meeting minutes, related to discussions regarding the establishment of the governance structure described in Article 1 of the Management and Staffing Services Agreement entered into by the District and Sonoma West Medical Center.

Please see attached

10. What plans, if any, does the District have to borrow funds against the unencumbered tax revenues in the next 12 months?

The District does not plan to borrow funds against any tax revenues in the next 12 months.

11. What is the current asset value of the property, plant and equipment owned by the District?

As noted above, an appraisal has not been done since 2000. At that time the property value was \$6,300,000.

12. Please provide documentation regarding the \$400,000 loan to SWMC made by the District this year.

The loan documents are attached. You will note that the \$400,000 was due to be repaid on May 5, 2016. The District notified SWMC that they had defaulted on the note. The PDHCD

board members authorized the District Executive Director to renegotiate the terms of the loan with SWMC at the 6/6/2016 Board meeting. Those negotiations are in process and will be presented at the July 11, 2016 Board meeting.

Palm Drive Health Care District Board Members

| Year | Board member | Geographical Location | Terms Served | |
|------|----------------------|-----------------------|--------------|----------------|
| 2000 | Barbara Graves | Sebastopol | 2000-2004 | |
| | Dan Smith | Sebastopol | 2000-2004 | |
| | Dana Kueffner | Bodega Bay | 2000-2004 | |
| | Glenn Minervini-Zick | Sebastopol | 2000-2004 | |
| | Mary Szsecsey | Occidental | 2000-2004 | |
| 2001 | Barbara Graves | Sebastopol | 2000-2004 | |
| | Dan Smith | Sebastopol | 2000-2004 | Resigned 2001 |
| | Dana Kueffner | Bodega Bay | 2000-2004 | |
| | Glenn Minervini-Zick | Sebastopol | 2000-2004 | Resigned 2001 |
| | Mary Szsecsey | Occidental | 2000-2004 | |
| | Robert Gillen | Sebastopol | 2001-2004 | Appointed 2001 |
| 2002 | Barbara Graves | Sebastopol | 2000-2004 | |
| | Dana Kueffner | Bodega Bay | 2000-2004 | Resigned 2002 |
| | Mark Sell | Sebastopol | 2002-2006 | Appointed 2002 |
| | Mary Szsecsey | Occidental | 2000-2004 | |
| | Naomi Fuchs | Sebastopol | 2002-2006 | |
| | Robert Gillen | Sebastopol | 2001-2004 | |
| 2003 | Barbara Graves | Sebastopol | 2000-2004 | |
| | Mark Sell | Sebastopol | 2002-2006 | |
| | Mary Szsecsey | Occidental | 2000-2004 | |
| | Naomi Fuchs | Sebastopol | 2002-2006 | |
| | Robert Gillen | Sebastopol | 2002-2004 | |
| 2004 | Barbara Graves | Sebastopol | 2004-2008 | |
| | Mark Sell | Sebastopol | 2002-2006 | |
| | Mary Szecszy | Occidental | 2000-2004 | |
| | Naomi Fuchs | Sebastopol | 2002-2006 | |
| | Robert Gillen | Sebastopol | 2002-2004 | |
| 2005 | Ezbon Jen | Bodega Bay | 2004-2008 | |
| | Irma Cordova | Sebastopol | 2004-2008 | |
| | Mark Sell | Sebastopol | 2002-2006 | |
| | Naomi Fuchs | Sebastopol | 2002-2006 | |
| | Robert Gillen | Sebastopol | 2004-2008 | |

| | | | | |
|------|------------------|------------|-----------|----------------|
| 2006 | Ezbon Jen | Bodega Bay | 2004-2008 | |
| | Irma Cordova | Sebastopol | 2004-2008 | |
| | Mark Sell | Sebastopol | 2002-2006 | |
| | Naomi Fuchs | Sebastopol | 2002-2006 | |
| | Robert Gillen | Sebastopol | 2004-2008 | |
| 2007 | Ezbon Jen | Bodega Bay | 2004-2008 | Resigned 2007 |
| | Frank Mayhew | Sebastopol | 2004-2008 | Appointed 2007 |
| | Irma Cordova | Sebastopol | 2004-2008 | |
| | Linda Johnson | Sebastopol | 2004-2008 | |
| | Nancy Dobbs | Sebastopol | 2007-2008 | Appointed 2007 |
| | Naomi Fuchs | Sebastopol | 2006-2010 | Resigned 2007 |
| | Robert Gillen | Sebastopol | 2004-2008 | |
| 2008 | Frank Mayhew | Sebastopol | 2008-2012 | |
| | Irma Cordova | Sebastopol | 2004-2008 | Resigned 2008 |
| | Linda Johnson | Sebastopol | 2004-2010 | |
| | Nancy Dobbs | Sebastopol | 2008-2008 | |
| | Robert Gillen | Sebastopol | 2004-2008 | |
| | Stephen Murphy | Sebastopol | 2008-2008 | Appointed 2008 |
| | | | | |
| 2009 | Dan Smith | Sebastopol | 2008-2012 | |
| | Frank Mayhew | Sebastopol | 2008-2012 | |
| | Linda Johnson | Sebastopol | 2006-2010 | |
| | Nancy Dobbs | Sebastopol | 2007-2010 | |
| | Steven Murphy | Sebastopol | 2008-2012 | |
| 2010 | Chris Dawson | Sebastopol | 2010-2014 | Appointed 2010 |
| | Dan Smith | Sebastopol | 2008-2012 | |
| | Frank Mayhew | Sebastopol | 2008-2012 | |
| | Linda Johnson | Sebastopol | 2006-2010 | |
| | Nancy Dobbs | Sebastopol | 2010-2014 | |
| | Stephen Murphy | Sebastopol | 2008-2012 | Resigned 2010 |
| 2011 | Chris Dawson | Sebastopol | 2010-2014 | |
| | Dan Smith | Sebastopol | 2008-2012 | Resigned 2011 |
| | Frank Mayhew | Sebastopol | 2008-2012 | |
| | Jared Dreyfus | Sebastopol | 2010-2014 | Deceased 2011 |
| | John Canova M.D. | Sebastopol | 2011-2014 | Appointed 2011 |
| | Mark Innman | Sebastopol | 2011-2012 | Appointed 2011 |
| | Nancy Dobbs | Sebastopol | 2010-2014 | |
| 2012 | Chris Dawson | Sebastopol | 2010-2014 | |
| | Frank Mayhew | Sebastopol | 2008-2012 | |
| | John Canova M.D. | Sebastopol | 2011-2014 | |

| | | | | |
|------|--------------------|-------------|-----------|----------------|
| | Mark Innman | Sebastopol | 2011-2012 | |
| | Nancy Dobbs | Sebastopol | 2010-2014 | |
| 2013 | Chris Dawson | Sebastopol | 2010-2014 | |
| | Jim Maresca | Gureneville | 2012-2016 | |
| | Marsha Sue Lustig | Sebastopol | 2012-2016 | |
| | Nancy Dobbs | Sebastopol | 2010-2014 | |
| | Sandra Bodley | Sebastopol | 2012-2016 | |
| 2014 | Chris Dawson | Sebastopol | 2010-2014 | Resigned 2011 |
| | Jim Horn | Forestville | 2014-2014 | Appointed 2011 |
| | Jim Maresca | Gureneville | 2012-2016 | |
| | Marsha Sue Lustig | Sebastopol | 2012-2016 | |
| | Nancy Dobbs | Sebastopol | 2010-2014 | |
| | Sandra Bodley | Sebastopol | 2012-2016 | |
| 2015 | Dennis Colthurst | Sebastopol | 2014-2018 | |
| | Dr. Richard Powers | Sebastopol | 2014-2018 | |
| | Jim Maresca | Gureneville | 2012-2016 | |
| | Marsha Sue Lustig | Sebastopol | 2012-2016 | |
| | Sandra Bodley | Sebastopol | 2012-2016 | |
| 2016 | Dennis Colthurst | Sebastopol | 2014-2018 | |
| | Dr. Richard Powers | Sebastopol | 2014-2018 | |
| | Jim Maresca | Gureneville | 2012-2016 | |
| | Marsha Sue Lustig | Sebastopol | 2012-2016 | |
| | Sandra Bodley | Sebastopol | 2012-2016 | |

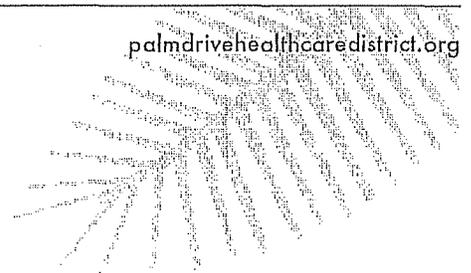


PALM DRIVE HEALTH CARE
DISTRICT

612 Petaluma Avenue, Sebastopol, CA 95472

P:707.823.3586
F:707.823.3728

palmdrivehealthcaredistrict.org



June 15, 2016

Mr. Raymond Hino, CEO, Sonoma West Medical Center
Mr. Dan Smith, President Sonoma West Medical Center Board of Directors
Sonoma West Medical Center
501 Petaluma Avenue
Sebastopol, CA. 95472

Dear Ray and Dan,

On February 5, 2016 the Palm Drive Health Care District (PDHCD) granted a loan to Sonoma West Medical Center (SWMC) for \$400,000 at a 4% annum interest rate from February 5, 2016 until the loan was paid back. The terms of the loan included that it would be paid back in 90 days. If the loan is not paid back on maturity the entire amount of money becomes due and payable. Also, the interest rate on the unpaid balance increases to the lesser of 10% or the maximum legal rate.

The date of maturity on the loan was May 4, 2016. No payment has been made on this loan. I am informing you that SWMC is in default of the loan agreement. The PDHCD stated this at their regular meeting on June 6, 2016. This letter is meant to confirm their determination on this.

The PDHCD also authorized me, Alanna Brogan, ED to renegotiate the terms of the loan.

I met with Stewart Goldberg Monday June 13, 2016 to initiate this discussion. I need to have the loan agreement renegotiated by June 24, 2016. I ask for your assistance in expediting this process.

Sincerely,

Alanna Brogan, MS, PHN, RN
Executive Director
Palm Drive Health Care District
612 Petaluma Avenue
Sebastopol, CA. 95472
work: 707.823.3596
Cell: 707.548.6675
E-mail: abrogan@pdhcd.com

CC: Stewart Goldberg, Treasurer Sonoma West Medical Center Board of Directors

BUSINESS LOAN AGREEMENT

This Business Loan Agreement ("Agreement") is entered into by and between Palm Drive Health Care District ("District") and Sonoma West Medical Center, Inc. ("Borrower") as of February 5, 2016 (the "Effective Date"), with regard to the following:

Recitals

- A. District is a California healthcare district formed in accordance with California's Local Health Care District Law (California Health & Safety Code sections 32000 et seq.). District owns an acute care hospital in Sebastopol, California ("Hospital").
- B. Borrower is a California Corporation that operates the Hospital pursuant to the terms of a Management and Staffing Services Agreement dated May 22, 2015 ("MSA"). Pursuant to the MSA, revenue received from accounts receivable generated from operation of the Hospital are paid into a bank account ("lock box") and then disbursed to Borrower to reimburse its direct and reasonable costs of operation.
- C. Due to unavoidable delays in obtaining necessary billing numbers and accreditations, payments on accumulated accounts receivable have been delayed, resulting in a need for short term bridge financing.
- D. District currently has cash in the amount of \$400,000.00 that is available to provide the needed bridge financing, and is willing to make a short term loan to Borrower on the terms and conditions set forth in this Agreement.

NOW, THEREFORE, in consideration of any financial accommodations given, or to be given or continued ("Credit") by District to Borrower pursuant to the Straight Note signed contemporaneously herewith, and any extensions, renewals or replacements thereof ("Document(s)"), Borrower hereby represents, warrants, and agrees as follows, unless District waives compliance in writing:

Agreement

1. **Recitals.**
The forgoing Recitals are true and correct.
2. **Purpose of Credit.**
Borrower shall continue to perform its obligations under the MSA and operate the Hospital in the manner it is presently operated ("Business") and shall utilize the Credit only for the purpose of paying operating expenses of the Business.
3. **Security for Credit.** As security for amounts owing in respect of the Credit, District and Borrower agree to modify the terms of the MSA to the extent required for District to control the lock box, and to allow District to withhold payments from the lock box that would otherwise be due to Borrower in order to satisfy Borrower's payment obligations under the terms of the Documents. Upon District's request, Borrower shall execute and deliver to District any documents deemed necessary or desirable by District to perfect the security interest granted hereby.

4. **Representations and Warranties; Additional Covenants.**

(a) Borrower is a corporation duly organized, validly existing and in good standing under the laws of the State of California, with its principal place of business at 6800 Palm Ave., Suite K, Sebastopol, California 95472. Borrower has the lawful power to own its properties and to engage in the business it conducts.

(b) Borrower has full power and authority (corporate and other) to borrow the sums provided for under the Credit, to execute, deliver, and perform this Agreement, the Document(s), and all other instruments and agreements made in connection herewith and with the Credit (the Document(s) and other instruments and agreements hereinafter called "Related Documents").

(c) All actions by Borrower, its directors, stockholders, members, or partners, as applicable that are necessary for the authorization execution, delivery, and performance of this Agreement, and of the Related Documents have been duly taken.

(d) The officers or representatives of Borrower executing the Agreement and the Related Documents are duly and properly in office or acting as representatives and are fully authorized to execute the same.

(e) The Agreement has been duly authorized, executed, and delivered by Borrower, and is a legal, valid, and binding agreement of Borrower, enforceable against it in accordance with its terms, and the Related Documents have been so authorized and, when executed and delivered, shall be similarly valid, binding and enforceable against the parties thereto.

(f) There is no charter, bylaw, or capital stock provision of Borrower, and no provision of any indenture instrument, or agreement, written or oral, to which Borrower is a party or which governs the actions of Borrower or which is otherwise binding upon Borrower or Borrower's property, nor is there any statute, rule or regulation, or any judgment, decree, or order of any court or agency binding on Borrower or Borrower's property which would be contravened by the execution, delivery or performance of this Agreement, or of the Related Documents.

(g) There is no action, suit, or proceeding at law or in equity or by or before any governmental instrumentality or other agency now pending, or, to the knowledge of Borrower, threatened against or affecting Borrower, or any properties or rights of Borrower, which, if adversely determined, would materially impair the right of Borrower to carry on the Business substantially as now conducted or would materially adversely affect the financial condition of Borrower.

(h) No event has occurred and is continuing or would result from the extension of any part of the Credit which constitutes an Event of Default as described in Paragraph 5, or which, on the lapse of time or notice or both, would become such Event of Default.

(i) Borrower shall not issue, purchase or retire any of its shares or interests, reorganize, merge or be the subject of a change of control, or otherwise alter or amend its capital, management or Business structure. In the event that Borrower receives or makes a proposal to engage in any of the transactions described in this sub-paragraph, Borrower shall immediately inform District thereof in writing.

(j) In the event that Borrower receives an offer to purchase its assets, or to merge or otherwise reorganize with another party, District shall have a right of first refusal to engage in the proposed

transaction before consideration is given to accepting the offer received. Similarly, if Borrower wishes to initiate a transaction involving a sale, merger or other reorganization, District shall have the right of first refusal to consider the transaction before deciding whether it will consent to Borrower initiating such discussions with others, which consent may be withheld in the District's sole discretion.

5. **Events of Default and Acceleration.**

On the occurrence of any of the following events or circumstances, District at its election may terminate any or all commitments and other obligations of District to Borrower and declare all amounts outstanding in respect of the Credit to be immediately due and payable without demand or notice to Borrower:

(a) Any failure on the part of Borrower to pay any amounts owing in respect of the Credit when due, or any breach or default by Borrower of or under any term, condition, provision, warranty; or representation made herein or in any of the Related Documents; or

(b) If Borrower becomes insolvent, is generally not paying its debts as such debts become due, suffers a material adverse change of financial condition, or defaults with respect to any order, judgment, injunction, decree, writ or demand of any court or other public authority; or

(c) If District in good faith believes that the prospect of payment or performance in respect of the Credit or the Related Documents is impaired.

All amounts outstanding in respect of the Credit shall be in default, and immediately due and payable in full, and all commitments and other obligations of District to Borrower shall be terminated, without declaration, demand or notice to Borrower if Borrower:

(a) Makes an assignment for the benefit of creditors; or

(b) Is the subject of any voluntary or involuntary case commenced under the federal Bankruptcy laws, as now constituted or hereafter amended, or any other proceeding under other applicable laws regarding bankruptcy, insolvency, reorganization, adjustment of debt or other forms of relief for debtors in any jurisdiction; or

(c) Consents to the appointment of a receiver, trustee, custodian or similar official for substantially all of its property or permits a decree ordering such appointment to remain in effect and unstayed for 60 days; or

(d) Is the subject of any dissolution or liquidation proceeding; or

(e) Has issued against it or its property any writ of attachment, execution, or other legal process involving an amount or risk deemed material by District; or

(f) Has filed or recorded against it or its property any notice of levy, notice to withhold, or other claim for taxes other than real property taxes not yet delinquent involving an amount deemed material by District.

The events described in this paragraph shall be defaults notwithstanding the terms of any of the Related Documents.

6. **Collection Costs.**

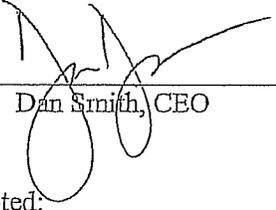
If District incurs any legal fees or other expense in protecting or enforcing its rights hereunder or under any of the Related Documents, in addition to any other sum which Borrower may be required to pay, Borrower shall pay to District the amount of such legal fees or other expense.

7. **Miscellaneous.**

This Agreement benefits District's successors and assigns and binds Borrower's heirs, legatees, personal representatives, and successors. Borrower may not delegate or assign any of its obligations hereunder and may not assert against any assignee of District any claim or defense it may have against District. The Agreement shall be governed by the laws of the State of California. Titles preceding any paragraph of the Agreement are for convenience only and are not a part of the Agreement. The Agreement shall continue as long as any amounts owing in respect of the Credit remain unpaid. No consent or waiver under, or modification of, this Agreement shall be effective unless in writing. No waiver of any breach or default shall be deemed a waiver of any breach or default thereafter occurring. Unless otherwise provided in this Agreement, all accounting terms shall be construed in accordance with generally accepted accounting principles consistently applied.

In WITNESS WHEREOF, Borrower has executed this Agreement on this 5 day of February, 2016.

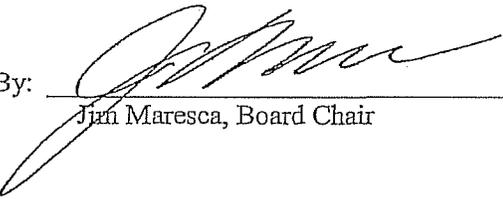
BORROWER

By: 

Dan Smith, CEO

Accepted:

DISTRICT

By: 

Jan Maresca, Board Chair

STRAIGHT NOTE

\$400,000.00

Sebastopol, California

For value received, Sonoma West Medical Center, Inc., a California corporation promises to pay to Palm Drive Health Care District, or order, at its business office located at 612 Petaluma Ave, Sebastopol, California, the sum of four hundred thousand dollars (\$400,000.00) on 2/5, 2016, with interest at the rate of 4% per annum from date written below until paid. All interest and principal shall be paid upon maturity in lawful money of the United States of America. Upon the occurrence of an Event of Default, as defined in the Business Loan Agreement signed contemporaneously herewith, the entire amount owed hereunder shall become immediately due and payable, and the interest rate on the unpaid balance shall increase to the lesser of 10% or the maximum legal rate. If payment is not made at maturity, the undersigned promises to pay all costs of collection and reasonable attorneys' fees. *maturity is 90 days, DS*

Sonoma West Medical Center, Inc.,
a California corporation
6800 Palm Ave., Suite K
Sebastopol, CA 95472

By



Dan Smith, CEO

Date:

2/5/2016

E-MAILED TO
DANA FORNEY
for GAIL MATTHEWS
6-9-15
JK

**PALM DRIVE HEALTHCARE DISTRICT
SONOMA WEST MEDICAL CENTER
AMENDMENT OF MANAGEMENT
AND STAFFING SERVICES AGREEMENT**

This Amendment to the Management and Staffing Services Agreement ("Agreement") is made and entered into and effective as of the 22nd day of May, 2015, by and between Sonoma West Medical Center, a California nonprofit public benefit corporation ("SWMC"), and Palm Drive Healthcare District, a California local health care district (the "District"), with reference to the following facts:

RECITALS

- A. The District and SWMC entered into the Agreement as of March 18, 2015, pursuant to which SWMC provides management and staffing services in connection with the reopening and operations of the District's Hospital.
- B. The District and SWMC wish to amend the Agreement to reflect that the parties do not anticipate that a future change in operator or owner of the Hospital would occur without applicable State licensing processes if SWMC becomes the licensed operator of the Hospital.
- C. Except as set forth in this Amendment, no other modifications are being made to the Agreement, and the Agreement shall remain in full force and effect.

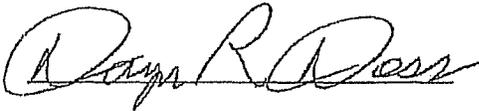
NOW, THEREFORE, the parties agree to amend the Agreement as set forth below.

Section 8.3 presently reads, "Termination Upon Transfer of License. In the event the Hospital License is transferred to SWMC, this Agreement shall terminate on the date on which SWMC becomes the licensed operator of the Hospital." This provision is hereby deleted and replaced with new Section 8.3, as follows:

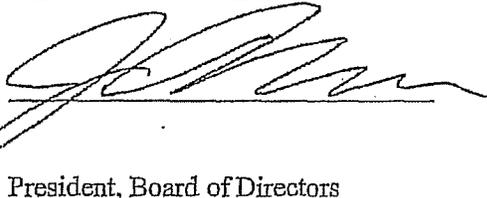
Section 8.3. Termination Upon Change of Operator. In the event SWMC becomes the licensed operator of the Hospital, this Agreement shall terminate.

IN WITNESS WHEREOF, the duly authorized officers of the parties have executed this Amendment as of the date first written above.

PALM DRIVE HEALTH CARE DISTRICT

By: 

Its: Chief Executive Officer

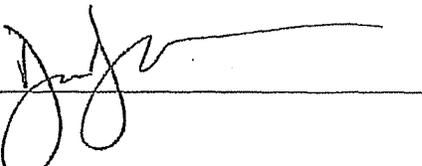
By: 

Its: President, Board of Directors

SONOMA WEST MEDICAL CENTER

By:  5/22/2015

Its: Chief Executive Officer

By: 

Its: President, Board of Directors

**MANAGEMENT AND STAFFING
SERVICES AGREEMENT**

This Management Services Agreement ("Agreement") is made and entered into as of the 18th day of March, 2015, by and between Sonoma West Medical Center, a California nonprofit public benefit corporation ("SWMC"), and Palm Drive Healthcare District, a California local health care district (the "District"), with reference to the following facts:

RECITALS

- A. The District owns that certain licensed thirty-seven (37) bed acute care hospital commonly known as Palm Drive Hospital (the "Hospital") located at 501 Petaluma Avenue, Sebastopol, California.
- B. The District ceased operations at the Hospital on April 27, 2014.
- C. SWMC is a California nonprofit corporation that has employed or contracted with individuals who have the experience and training necessary to recommence operations at the Hospital.
- D. The Parties intend that the Hospital be reopened to bring quality health care services to the community served by the District.
- E. Throughout the provisions of this Agreement the terms "Hospital" and "District" are used. Both terms are used to reference one entity. The term "Hospital" is used in relation to the facilities, and services provided at the facilities, owned and operated by the District, while the term "District" is used to refer specifically to the legal entity, a local governmental agency, that owns the Hospital.

AGREEMENTS

NOW, THEREFORE, in consideration of the recitals, covenants, conditions and promises herein contained, and for other good and valuable consideration, the receipt of which is hereby acknowledged, the parties hereto agree as follows:

A R T I C L E I

HOSPITAL GOVERNING BOARD

1.1 Appointment. A subcommittee of the Board of Directors of the District (the "District Board") shall be established with overall administrative and professional responsibility for the Hospital, to serve as the governing body of the Hospital, as that term is used in Sec. 70000 et seq. of Title 22 of the California Code of Regulations (respecting licensure and regulation of acute care hospitals). Such subcommittee is referred to herein as the "Hospital Governing Board."

1.2 Composition. The Hospital Governing Board shall be composed of thirteen (13) members appointed in accordance with the bylaws of the District and with the following:

- a) Five (5) District representatives, who shall be the current members of the

District Board serving ex officio;

- b) Five (5) members who reside within the geographic boundaries of the District nominated by SWMC and approved by a majority of the remaining members of the Hospital Governing Board, each of whom shall serve two year terms; and

- c) One (1) member who resides within the geographic boundaries of the District and is elected by a majority of the ten members described in (a) and (b) above. This “at large” member shall serve two year terms; and
- d) Two (2) representatives of the medical staff of the hospital nominated by the Medical Executive Committee and approved by a majority of the Governing Body other than the medical staff representatives. The medical staff representatives shall serve one year terms.

1.3 Authority Related to Hospital Operations. Notwithstanding the authority delegated to SWMC under Article 2 hereof, the Hospital Governing Board shall retain operational control of the Hospital through exercise of all power and responsibilities required to be reserved to the board of directors of a licensed general acute care hospital by the State of California and the JCAHO, or other recognized accreditation agency, which cannot, under law, JCAHO standards, or the standards of such other recognized accreditation agency, be properly delegated. The Hospital Governing Board specifically has the authority to approve the Hospital's medical staff bylaws, rules and regulations and fair hearing plan as required under the District Bylaws, and to make all decisions related to appointment or reappointment to medical staff membership or the granting of clinical privileges, or related to the denial, revocation, suspension or other adverse decision with respect to such membership or clinical privileges, as set forth in the District Bylaws and the medical staff bylaws of the Hospital. The Hospital Governing Board shall be ultimately responsible for the quality of medical care in the Hospital, as set forth in the District Bylaws and the medical staff bylaws of the Hospital.

1.4 Policies and Procedures. The Hospital Governing Board shall have the power and authority to establish or amend the policies and procedures referenced in Section 2.1 hereof, in accordance with the District Bylaws and subject to the limitations set forth in Section 1.6 hereof.

1.5 Power to Commit the Hospital and District. To the extent permitted by applicable law, the Hospital Governing Board from time to time shall establish policies that specify limitations on the authority of the Chief Executive Officer, Chief Financial Officer, or any other officer to commit the Hospital to the expenditure of sums in excess of a dollar amount established by the Hospital Governing Board, subject to any approval required to be made by the District Board pursuant to Section 1.6 hereof. In addition to having the final authority and responsibility for the conduct of the Hospital as specified in §§70000 et seq. of Title 22 of the California Code of Regulations, the Hospital Governing Board shall have the following specific authority:

- a) Development of capital and operating budgets for the Hospital;
- b) Approval of appointment of the Hospital CEO, the Chief Financial Officer of the Hospital, and the Chief Nursing Officer, subject to the approval of the District Board as required by the Health Care District Law;
- c) Amendment of the Hospital's quality improvement plan and oversight of the Hospital's quality improvement committee;
- d) Establishment of annual goals and objectives for implementing this Agreement; and
- e) Disposal of Hospital assets or the incurrence of debt outside the ordinary course of business.

1.6 Powers Delineated in the District Bylaws. Notwithstanding the foregoing, the District Board reserves to itself the power and authority delineated in the District Bylaws and such other powers as may be specified by the Health Care District Law as being reserved to the board of a California local health care district. Further, the District shall retain ultimate professional and administrative responsibility for the services rendered during the course of this Agreement, as required under Title 22 of the California Code of Regulations. In furtherance of such reserved power and authority, the following actions shall not be taken unless approved by the District Board:

- ✓ a) A change in the Hospital's mission statement;
- ✓ b) A change in the Hospital's charity care policy;
- ✓ c) A change in the Hospital's name (it is the intent of the District to change the facility's "d.b.a." name to "Sonoma West Medical Center");
- d) The establishment of any affiliates of the Hospital or the District;
- ✓ e) The incurrence of any new debt or encumbrance by the Hospital or the District in an amount in excess of \$100,000;
- f) The adoption and amendment of the Hospital's institutional master plan;
- g) The disposal or transfer of District Assets with a value in excess of \$50,000;
- h) The closure of the Hospital;
- i) Approval of any amendment of this Agreement;
- ✓ j) The appointment and removal of the Hospital CEO; and
- k) A change in the use of District tax revenues or alteration of the budget established at the commencement of this Agreement pertaining to the District Board's

administrative affairs, and subject to Section 5.4.

A R T I C L E I I

RESPONSIBILITIES OF SWMC

2.1 Appointment as Manager. The District hereby appoints SWMC and delegates to SWMC the responsibility and commensurate authority to provide the services necessary and appropriate to manage all aspects of the Hospital's operations ("Services") in accordance with terms and conditions of this Agreement and with the strategic plans, budgets and policies and procedures that the Hospital Governing Board (a) determines are appropriate for the governance of Hospital and its provision of care to the communities it serves and (b) adopts from time to time. The District shall, during the term of this Agreement, give SWMC full access to the Hospital, its records, offices and facilities, as reasonably required for SWMC to carry out its duties hereunder.

2.2 Description of Specific Services to be Provided. Without limiting the generality of the foregoing, during the term of this Agreement, including any extensions and renewals hereof, SWMC shall provide the services described in this Section 2.2 as required for the operation of the Hospital, and such other services as SWMC may determine would result in reduced costs and/or improved organizational effectiveness.

a) Implementation of Business Plan. Implementation of the Sonoma West Medical Center Business Plan, dated as of March 5, 2015 and, consistent therewith, items b) to o) below.

b) Budgets. SWMC shall develop an annual capital and operating budget for the Hospital prior to the commencement of SWMC's fiscal year, which budgets shall be subject to the approvals specified in Article 1 hereof, including budgeting adjustments in the allocation of District tax revenues not reserved for District Board administrative needs and set forth in the allocation for same established at the commencement of this Agreement.

c) Physician Strategy. SWMC shall develop and implement a physician integration strategy for the Hospital and shall be responsible for maintaining good physician relations with the Hospital's Medical staff.

d) Information Technology. SWMC shall implement information technology software and services to be owned or licensed and operated by the Hospital to assure the Hospital's information systems supporting patient care, medical management, finance, and operations are functioning properly as required for efficient management of the Hospital. Except as provided in Section 2.2 (e) below with regard to the HarmoniMD EHR Platform, upon the expiration or termination of this Agreement, for the benefit of continued Hospital operations,

SWMC shall assure that District shall be entitled to continued use of all licenses and other entitlements commensurate with ownership and operation of the information technology systems for a period of at least two years beyond termination or the expiration of this Agreement. SWMC shall assure that all maintenance and update services ordinarily available from Information Technology vendors will continue to be available to the District and the Hospital after expiration and termination of this Agreement.

e) HarmoniMD EHR Platform. The parties acknowledge that the HarmoniMD platform is a cloud based software system that is hosted by EHRI Inc. and as such no ownership rights to the software or software license are granted to SWMC or the District. The parties further acknowledge that the use of the software is being donated to SWMC by EHRI Inc. for use on behalf of the Hospital for a period of five (5) years and that this donation includes all hosting, implementation, product support, upgrades, and technical service as spelled out in the attached Software as Service agreement between EHRI Inc. and SWMC. As indicated the rights to the use of the HarmoniMD platform will transfer to the successors or heirs of the hospital operations. If this Agreement is terminated prior to the expiration of the five (5) year donation period, SWMC will assure that the donated usage will continue for a period of two (2) years following termination, but not exceeding the original five year period of donated utilization of the HarmoniMD platform. In the event of such termination, SWMC shall assign its interests in the Software as Service agreement to the Hospital.

f) Construction and Property Management. SWMC shall provide construction management and property management services to the Hospital, consistent with the Hospital's needs.

g) Financial Services.

1. SWMC shall prepare or cause to be prepared monthly financial statements for the Hospital, including balance sheet, income statements and statements of changes in net assets, cash flow projections and an accounting of SWMC's Management Costs. Monthly financial statements for the prior period shall be presented to the Hospital Governing Board at its regularly scheduled meetings and shall be made available to the District upon request.

2. SWMC shall provide direction and oversight for all financial, accounting and bookkeeping functions appropriate to the operations of general acute care hospitals, including but not limited to maintenance, custody and supervision of business records, papers, documents, ledgers, journals and reports relating to the business operations of the Hospital, the establishment, administration and implementation of accounting procedures, controls, forms and systems, the preparation of financial reports, the planning of the business operations of the Hospital, the payment of accounts payable and collection of accounts receivable, and the administration of the Hospital payroll. All financial reports to the Governing Body shall include specific references to the Hospital's accounts payable status and any changes in the coverage or scope of the Hospital's insurance coverage. In the event accounts payable status exceeds 60 days in payments, SWMC shall provide a plan for approval by the Governing Body for bringing accounts payable status under 60 days .

3. SWMC shall arrange and provide support for an annual audit of the Hospital's financial statements through auditors selected by the Hospital Governing Board. The annual audited financial statements shall be presented to the District Board for review and approval.

4. SWMC shall prepare or cause to be prepared on behalf of the Hospital all federal and California information and other returns and other forms and documents (collectively, "Returns") required to be filed with the Internal Revenue Service or the California Franchise Tax Board. Any taxes owed shall be a Hospital Expense, as that term is used in Section 5.3 of this Agreement.

h) Managed Care Contracting. The Hospital shall participate fully in payor contracts, including marketing, contract review and analysis, and negotiation with third party payors.

i) Materials Management. Consistent with the Hospital's operating needs, SWMC will manage Hospital materials and supplies and shall seek to participate in any beneficial group purchasing organizations in which the Hospital is eligible to take part.

j) Communications. SWMC shall provide marketing and public relations services to the Hospital. SWMC shall also assist the Hospital with internal communication involving staff and Medical staff.

k) Human Resources.

1) Non-Physician Personnel. SWMC shall provide, on behalf of Hospital, such non-physician personnel and staffing as may be reasonably necessary to enable operation of the Hospital and its facilities "Support Personnel." Such Support Personnel may be SWMC employees or independent contractors.

2) Recruiting. Except as otherwise provided in this Agreement, SWMC shall recruit, employ or otherwise retain, manage and, with respect to non-medical services, supervise the Support Personnel as necessary for the proper and efficient operation of the Hospital and its facilities.

3) Employee Policies and Procedures. SWMC's general employee practices and procedures, as well as the policies and procedures of the hospital that are not inconsistent therewith, shall be applicable to Support Personnel.

4) Employees and Independent Contractors. All Support Personnel shall be employees or independent contractors of SWMC. SWMC shall be responsible for the payment of all SWMC Employee Liabilities. Hospital shall have no liability whatsoever under this Agreement or otherwise for any SWMC Employee Liabilities. SWMC shall defend, indemnify and hold harmless the Hospital and District against any claim, cause of action, loss, cost and expense arising in connection with or resulting from SWMC Employee Liabilities. At Hospital's request, SWMC shall provide Hospital with certificates or other evidence satisfactory to Hospital that

SWMC has satisfied its obligations with respect to SWMC Employee Liabilities. "SWMC Employee Liabilities" shall mean SWMC's responsibility for payment to Support Personnel of all compensation, including base salary and benefits, including health, dental and life insurance. SWMC shall also be solely responsible for all compensation, federal and state withholding taxes, vacation pay, sick leave, benefits, social security, health insurance, worker's compensation insurance, disability or unemployment insurance, employee benefits of any kind and other applicable taxes and contributions to government mandated employment related insurance and similar programs for or related to Support Personnel and any other employee or agent of SWMC.

5) Management of Personnel. SWMC shall hire, terminate and take appropriate disciplinary action against all Support Personnel in compliance with SWMC's employment policies and in compliance with State & Federal laws. SWMC will periodically review Support Personnel performance with the Governing Body to receive the Governing Body's input as to its satisfaction with Support Personnel performance, but in all circumstances SWMC shall hire, terminate and take appropriate disciplinary action against all such Support Personnel.

6) Human Resources Department. SWMC shall manage the Hospital's human resources department, providing guidance and supervision in the areas of labor and compliance with federal and California laws affecting personnel. SWMC shall establish policies regarding staffing levels, work hours and shifts, wages, salaries and compensation, retention, promotion and demotion, the awarding of bonuses and salary adjustments, and other matters affecting the terms and conditions of the employment of personnel at the Hospital.

l) Risk Services. SWMC shall manage the Hospital's risk services department, providing direction and supervision over the management of risk and loss prevention at the Hospital, and the management of claims or potential claims. The Hospital shall participate in programs of insurance or self-insurance as deemed necessary and reasonable by SWMC, including general and professional liability, directors' and officers' liability, property, employment practices liability (EPL) and worker's compensation liability, with SWMC as a named or additional insured.

m) Support for District Operations. SWMC shall provide administrative support for the functioning of the District, including clerical and financial services, the cost of which to SWMC shall be paid from funds generated by District tax revenues allocated to the budget for District administration. SWMC shall further ensure that facilities at the Hospital reasonably required by the District for its meetings and storage of District property are available to the District at all times during the term of this Agreement.

n) SWMC Insurance. SWMC shall comply, at its expense, with applicable workers' compensation laws with respect to its own employees through maintenance of an insured program.

o) Maintenance of Property. SWMC shall manage and maintain the Hospital and the Hospital Facilities, in good condition. Where approval of the District Board is

necessary pursuant to Section 1.6(e), SWMC shall advise the District Board if and when equipment, furnishing and fixtures require replacement or upgrading in the ordinary course of the Hospital's business. For the purposes of this Section, Hospital Facilities shall include all exterior areas of the Hospital and the parcel on which it is located including, without limitation, all landscaping and trees, parking areas, appurtenant structures and the exterior of the Hospital itself.

A R T I C L E I I I

MANAGEMENT STRUCTURE

3.1 Chief Executive Officer. SWMC shall be responsible for employment of the Chief Executive Officer of the Hospital (the "Hospital CEO"). The Hospital CEO shall be responsible for overall, day-to-day management of the Hospital, and shall develop a management team for the Hospital. All directors and managers employed by the Hospital shall report, directly or indirectly, to the Hospital CEO. SWMC shall present a candidate for the position of Hospital CEO to the Hospital Governing Board, and appointment of the Hospital CEO shall be subject to the approvals specified in Article I hereof. The Hospital CEO shall be accountable to the Hospital Governing Board. The Hospital Governing Board shall participate in the annual performance review of the Hospital CEO. Pursuant to the Health Care District Law, the CEO's maximum contractual term shall be four (4) years, and may be periodically renewed for additional four year terms.

3.2 Chief Financial Officer. SWMC shall be responsible for employment of the Chief Financial Officer of the Hospital (the "Hospital CFO"). The Hospital CFO shall be accountable to the Hospital CEO and the Hospital Governing Body. The Hospital Governing Body shall participate in the annual performance review of the Hospital CFO.

3.3 Review of Senior Management. SWMC shall also be responsible for employment of qualified individuals to serve as Chief Nursing Officer and in other senior management positions. Where appropriate, individuals may serve in more than one such role. In conducting annual evaluations of the performance of the Chief Nursing Officer and other senior management at the Hospital, the Hospital CEO will receive input from the Hospital Governing Board.

A R T I C L E I V

COMPLIANCE WITH LAW AND BOARD POLICY

4.1 Compliance with Legal Requirements. SWMC shall prepare or cause to be prepared all materials and follow all procedures necessary to maintain: (a) certification of the Hospital as a provider of services under Titles XVIII (Medicare) and XIX (Medicaid) of the Social Security Act; (b) State licensure of the Hospital as a general acute care hospital under all applicable laws; (c) all other licenses and permits required to operate the Hospital and provide services therein; (d) accreditation of the Hospital by the appropriate accrediting organization; and (e) the Hospital's compliance with the California Local Health Care District Law, Health & Safety Code §§ 32000 *et seq.*, or any successor law thereto (the

“Health Care District Law”) and all other laws applicable to the operation of the Hospital. SWMC shall do nothing to jeopardize the Hospital's Medicare, Medi-Cal and other third-party reimbursement arrangements. In all respects, SWMC shall comply with all legal requirements in the performance of its obligations under this Agreement.

4.2 Confidentiality of Patient Records. SWMC shall maintain the confidentiality of all files and records of the Hospital in compliance with all applicable legal requirements, disclosing the same only as required or permitted by law. The Parties will execute appropriate Business Associate Agreements in compliance with the Health Insurance Portability and Accountability Act of 1996 and regulations promulgated thereunder by the Department of Health and Human Services (collectively, “HIPAA”).

A R T I C L E V

COMPENSATION FOR MANAGEMENT SERVICES

5.1 Management Fee. In consideration of the management services provided by SWMC, SWMC shall receive pass through reimbursement from Hospital Revenue of all of its direct and reasonable costs necessary to the provision of its management services to the Hospital under this Agreement (its “Management Costs”).

5.2 Hospital Revenues. “Hospital Revenue” shall mean and include: (a) all gross revenue from the provision of any and all hospital services provided on or after the Commencement and during the term the arrangement, determined on an accrual basis in accordance with GAAP consistently applied; (b) any and all disproportionate share payments or credits from Medicare or Medicaid; (c) any and all quality assurance and supplemental Medi-Cal payments made by the California Department of Health Care Services to District or SWMC after the Commencement Date pursuant to Section 14167 *et seq.* or Section 14169 *et seq.* of the California Welfare and Institutions Code, including supplemental payments or funds available to State “non-designated public hospitals;” (d) any and all HITECH or meaningful use payments; (e) any and all distressed hospital fund payments; (f) any AB 915 Outpatient Supplemental Funds; (g) any and all rent payments from any use of space in or at the Hospital; and (h) any all revenue of any other type or any other source related to the operation of the Hospital on and after the Commencement Date, and (i) any District tax revenues allocated to support general Hospital operations pursuant to Section 5.4 below.

5.3. Hospital Expenses. Pursuant to its management responsibilities SWMC will assure that all Hospital Expenses incurred in connection with the operation of the Hospital on or after the Commencement Date and during the term of the Agreement are paid, including without limitation its Management Costs, and any expenditures approved by the District Board pursuant to Section 1.6(e) (collectively, the “Hospital Expenses”) from Hospital Revenue to the extent it is available to cover Hospital Expenses, and if not available, from funds committed pursuant to Section 5.4 below. Hospital Expenses shall not include any cost or expenses resulting from or relating to any of the following: (a) any Retained Liabilities as defined herein; (b) any performance or non-performance by the District of any of its obligations; and (c) any fee, charge, assessment or Tax due or payable as a condition to or otherwise in connection with District operations other than the operations of the Hospital.

5.4. District Tax Revenue. For the initial term of this agreement the District will augment Hospital Revenue with One Million Dollars (\$1,000,000) per year from annual tax revenues, which will be paid in tranches at the time parcel taxes are received by the district in April, July and December of each year for five years and subject to the amount of such funds available. It is understood by the parties that these funds may be spent to repair and maintain the hospital property, purchase and repair medical equipment, and subsidize charity care and programs that benefit the community.

5.5. SWMC Funding of Losses. Notwithstanding 5.4 above, the District shall not be responsible for, and shall not be required to contribute funds to make up for, any shortfall in Hospital Expenses if Hospital Revenue is inadequate to pay Hospital Expenses, including SWMC Management Costs. SWMC shall bear all obligations and risks of loss, and shall cover and pay for, in a timely manner consistent with industry standards for accounts payable, payables and all actual losses, incurred as a result of the operation of the Hospital on and after the Commencement Date.

5.6. No Assumption of Liabilities. Nothing in this arrangement is intended or shall be construed to constitute SWMC's assumption of any liabilities of District a) existing prior to the Commencement Date including, without limitation, any claims asserted in District's bankruptcy proceedings and/or any secured debt of District, b) related to the operation of the Hospital prior to the Commencement Date, c) related to District's operations which do not arise out of the operation of the Hospital, and d) that are not specifically identified in this Agreement as being assumed by SWMC (collectively, the "Retained Liabilities").

A R T I C L E V I

REPRESENTATIONS AND WARRANTIES OF THE DISTRICT

The truth, accuracy and completeness of the District's representations, warranties and covenants contained in this Agreement shall be conditions precedent to the obligations of SWMC to enter into and perform its obligations under this Agreement. As an inducement to SWMC to enter into this Agreement and to consummate the transactions contemplated by this Agreement, the District hereby represents, warrants and covenants to SWMC as to the following matters, and, except as otherwise provided herein, shall be deemed to make all of the following representations, warranties and covenants again as of the Commencement Date:

6.1 Organization and Good Standing. The District is a local health care district of the State of California duly organized and existing under the Health Care District Law. The District has the full power and authority to carry on its businesses as they are now being conducted, and to enter into and perform its obligations under this Agreement.

6.2 The District's Authority. The District has the full right, power, legal capacity and authority to execute, deliver and carry out the terms of this Agreement and all documents and agreements necessary to give effect to the provisions of this Agreement and to

consummate the transactions contemplated hereby. The Hospital Governing Board, when appointed, shall be a duly constituted committee of the District Board, with full power and authority to carry out the duties of the District Board delegated to it. All actions required to be taken by the District to authorize the execution, delivery and performance of this Agreement, all documents executed by the District necessary to give effect to this Agreement, and all transactions contemplated hereby have been duly and properly taken or obtained or will be duly and properly taken or obtained by the District prior to the Commencement Date.

6.3 Validity and No Breach. This Agreement is, and all other agreements required to be delivered or performed in connection herewith will be, the lawful, valid and legally binding obligations of the District, enforceable in accordance with their terms, subject to bankruptcy, insolvency, moratorium or similar laws affecting the enforcement of creditors' rights generally or the implementation of any of the terms of this Agreement.

A R T I C L E V I I

REPRESENTATIONS AND WARRANTIES OF SWMC

The truth, accuracy and completeness of SWMC's representations, warranties and covenants contained in this Agreement shall be conditions precedent to the obligations of the District to enter into and perform its obligations under this Agreement. As an inducement to the District to enter into this Agreement and to consummate the transactions contemplated by this Agreement, SWMC hereby represents, warrants and covenants to the District as to the following matters, and, except as otherwise provided herein, shall be deemed to make all of the following representations, warranties and covenants again as of the Commencement Date:

7.1 Organization and Good Standing. SWMC is a nonprofit public benefit corporation, duly organized and in good standing under the laws of the State of California, and has applied for exemption from taxation as an organization described in Section 501(c)(3) of the Internal Revenue Code of the United States of America. SWMC has the full power and authority to carry on its businesses as they are now being conducted, and to enter into and perform its obligations under this Agreement.

7.2 SWMC's Authority. SWMC has the full right, power, legal capacity and authority to execute, deliver and carry out the terms of this Agreement and all documents and agreements necessary to give effect to the provisions of this Agreement and to consummate the transactions contemplated hereby. All actions required to be taken by SWMC to authorize the execution, delivery and performance of this Agreement, all documents executed by SWMC necessary to give effect to this Agreement, and all transactions contemplated hereby have been duly and properly taken or obtained or will be duly and properly taken or obtained by SWMC prior to the Commencement Date.

7.3 Validity and No Breach. This Agreement is, and all other agreements required to be delivered or performed in connection herewith will be, the lawful, valid and legally binding obligations of SWMC, enforceable in accordance with their terms, subject to bankruptcy, insolvency, moratorium or similar laws affecting the enforcement of creditors'

rights generally or the implementation of any terms of this Agreement.

ARTICLE VIII

TERM AND TERMINATION

8.1 Term. The term of this Agreement (the “Term”) shall commence on March 18, 2015 (the “Commencement Date,” and continue for a period of five (5) years, unless sooner terminated as provided herein. So long as SWMC is not in default of its obligations under this Agreement, SWMC shall have the right to extend the Term of this Agreement for two (2) additional terms of five (5) years each (each, a “Renewal Term”) by providing District with at least one hundred eighty (180) days prior written notice prior to the expiration of the Initial Term or Renewal Term then in effect of SWMC’s intent to exercise such option. Any such renewal will be subject to District approval, such approval not to be unreasonably withheld.

8.2 Termination for Cause. Notwithstanding the provisions of Section 12.15 of this Agreement, either party may terminate this Agreement at any time for “cause,” as defined in this Section 8.2, upon delivery of written notice as hereinafter provided.

8.2.1 Termination by District. District shall have “cause” to terminate:

a) If SWMC shall apply for or consent to the appointment of a receiver, trustee or liquidator of SWMC or of all or a substantial part of its assets, file a voluntary petition for bankruptcy or admit in writing its inability to pay its debts as they come due, make a general assignment for the benefit of creditors, file a petition or an answer seeking reorganization or arrangement with creditors or to take advantage of any insolvency law, or if a creditor of SWMC files an involuntary petition under any state or federal reorganization, insolvency, arrangement, bankruptcy or other debtor relief provision, and such petition is not dismissed within sixty (60) days; or

b) If SWMC shall default in the performance of any material covenant, agreement, term or provision of this Agreement, including without limitation Section 5.5 on the funding of loses, and such default shall continue for a period of sixty (60) days after written notice to SWMC from District stating the specific default; or

c) If SWMC shall intentionally engage in any fraudulent practices or repeated negligence, omissions or intentional acts that materially affect the business or reputation of the Hospital, including but not limited to conduct that evidences a willful disregard for patients treated at the Hospital; or

d) If SWMC fails to maintain the certifications, accreditations, and licenses for the Hospital as delineated in Section 4.1.

8.2.2 Termination by SWMC. SWMC shall have “cause” to terminate this Agreement:

a) If District shall default in the performance of any material covenant, agreement, term or provision and such default shall continue for a period of sixty (60) days after written notice to District from SWMC stating the specific default; or

b) If Hospital or any portion thereof shall be damaged or destroyed, or if any material assets of the Hospital shall be rendered incapable of normal operation, by fire or other casualty and if Hospital fails to commence repairing, restoring, rebuilding or replacing any such damage or destruction within ninety (90) days after such fire or other casualty, or fails to complete such work within a reasonable period of time; or

c) If District shall apply for or consent to the appointment of a receiver, trustee or liquidator of District or of all or a substantial part of its assets, file a new voluntary petition in bankruptcy or admit in writing its inability to pay its debts as they come due, make a general assignment for the benefit of creditors, file a petition or an answer seeking reorganization or arrangement with creditors or to take advantage of any insolvency law, or if a creditor of District files an involuntary petition under any state or federal reorganization, insolvency, arrangement, bankruptcy or other debtor relief provision, and such petition is not dismissed within sixty (60) days it being understood and agreed that District's current bankruptcy proceedings shall not constitute cause under this Section 8.2.2; or

d) If District shall fail to make any payments or keep any material covenants owing to SWMC within ten (10) calendar days of the date on which payment is due provided, however, that the failure to make a payment due to a subordination agreement with a third party shall not give rise to a right to terminate the Agreement; or

e) If District shall fail to make any payments owing to any third party that would cause District to lose possession of the Hospital's building, equipment or property.

8.3 Termination Upon Transfer of License. In the event the Hospital License is transferred to SWMC, this Agreement shall terminate on the date on which SWMC becomes the licensed operator of the Hospital.

8.4 Obligations Upon Termination of Agreement. In the event of any termination, SWMC shall:

a) Cooperate and assist in the orderly and efficient transfer of all phases of the administration of the Hospital to any new administrator or management firm; provided, however, that SWMC shall be entitled to reasonable and customary fees for SWMC's transition services; and

b) Surrender to District all documents and records in SWMC's possession relating to the operation of the Hospital.

c) Cooperate in the effective and efficient transition of any employees that will become employees of the District to support continued Hospital operations.

d) Assure that all Hospital and District assets remain in the possession of the District and that all donated assets utilized by the Hospital during the term of this agreement remain in the possession and ownership of the District.

e) To the extent applicable, fulfill its obligation under Section 2.2(e) to assign to the Hospital SWMC's interest in the Software as Service agreement.

8.5 Effect of Illegality. In the event that any federal, state or local law or regulation currently existing or hereinafter enacted, or any final and nonappealable construction or interpretation of such law or regulation by a court of competent jurisdiction, licensing or regulatory body, governmental agency, department, political subdivision, commission, tribunal or other instrumentality of any government, whether federal, state or local, or enforcement of such laws or regulations hereafter occurs, which makes substantial performance of this Agreement illegal, this Agreement shall be terminated on the effective date on which the new law, regulation or construction, interpretation or enforcement of an existing law or regulation makes illegal the substantial performance of this Agreement; provided, however, that the parties shall negotiate in good faith, exercising commercially reasonable best efforts, to enter into a written modification of this Agreement to make substantial performance of this Agreement legal in view of such event.

ARTICLE IX

INDEMNIFICATION

9.1. Indemnification of SWMC. To the extent not covered by insurance as provided above, District shall defend, indemnify and hold harmless SWMC and SWMC's officers, agents, subcontractors and employees from and against liability for any and all costs (including court costs), expenses, fees (including reasonable attorneys' fees) and payments by, and losses and damages that arise out of, or are in any way connected with, the negligent or intentional acts or omissions of District, its directors, employees, members, officers or agents (excepting SWMC), or any Retained Liabilities, unless such act or omission is caused by the negligence or willful misconduct of SWMC or one of its managers, members, officers, employees, subcontractors or agents.

9.2. Indemnification of District. To the extent not covered by insurance, SWMC shall defend, indemnify and hold harmless District, its managers, members, officers, agents, and employees from and against liability for any and all costs (including court costs), expenses, fees (including reasonable attorneys' fees) and payments by, and losses and damages that arise out of, or are in any way connected with, the negligent or intentional acts of SWMC or its officers, agents, employees or subcontractors in the performance of SWMC's duties under this Agreement unless such act or omission is caused by the negligence or willful misconduct of the District or its employees, managers, members, officers or agents.

9.3 Limitation on Applicability of This Article. The provisions of the preceding sections of this Article IX are intended to apply only to claims and liabilities that are not covered by or exceed the limits of insurance coverage and for which liability has not been otherwise allocated by agreement of the parties. Nothing contained in this Article IX is intended or should be

construed to create any liability to or rights of recovery or subrogation on the part of any insurance carrier or any other third party against either of the parties or to affect the allocation of responsibility among insurance carriers or other persons who may have responsibility for satisfaction of all or any part of any claim made against either party.

A R T I C L E X

R E C O R D S

10.1 District Ownership of Hospital Records. At all times during and after the term of this Agreement, all patient medical records, financial, corporate and personnel records and information relating to the business and activities of the Hospital shall be and remain the sole property of the District. Notwithstanding the foregoing, at all times during the term of this Agreement, SWMC shall have available to it all such records required for SWMC to provide services and otherwise carry out its responsibilities hereunder.

10.2 Confidentiality of Records. SWMC and the District shall adopt procedures to assure the confidentiality of SWMC's business records and the records relating to the operations of the Hospital, including, but not limited to, all statistical, financial and personnel data related to the operations of the Hospital, which information is not otherwise available to third parties publicly or by law, and each party hereto shall comply with all applicable federal and state statutes and regulations relating to such records. Patient medical records and other privileged patient information shall not be disclosed or utilized by the parties or their agents or employees except as required or permitted by applicable laws and regulations.

A R T I C L E X I

C O N D I T I O N S P R E C E D E N T

The obligation of the parties to commence the performance contemplated by this Agreement shall be subject to the satisfaction of each of the following conditions (which may be waived specifically in writing by the party for whose benefit said condition is stated, in whole or in part) on or after the Commencement Date:

11.1 Appointment of Hospital Governing Board. The District shall have appointed the initial ten (10) members (District / SWMC nominated) to the Hospital Governing Board and taken all necessary formal action to delegate to the Hospital Governing Board all of the District's power and authority necessary for the performance of this Agreement as contemplated and to the extent authorized by the Health Care District Law and any other applicable law. The Bylaws of the Hospital Governing Board shall provide that, so long as this Agreement remains in effect, the Bylaws may be amended only upon receipt of the prior written consent of SWMC.

11.2 District Board Bylaws. The District shall have adopted Amended and Restated District Board Bylaws that contain all provisions needed to reflect the District's

obligations under this Agreement, including but not limited to provision for the establishment of the Hospital Governing Board as provided in Section 11.1. Said Amended and Restated Bylaws shall provide that, so long as this Agreement remains in effect, no amendments to the Amended and Restated Bylaws that would remove, reduce or impair participation by the SWMC-nominated members of the Healthcare Governing Body without the prior written consent of SWMC.

11.3 Corporate and District Approvals. The respective Boards of the parties shall have approved the transactions contemplated by this Agreement, which approval may be withheld in the sole discretion of such Boards.

11.4 Bankruptcy Court. The U.S. Bankruptcy Court for the Northern District of California, Santa Rosa Division, in Case. No. 14-10510, shall have been informed of the District's intent to enter into this Agreement.

A R T I C L E X I I

MISCELLANEOUS

12.1 Notices. All notices required or permitted hereunder shall be given in writing and delivered by hand or sent by registered mail, postage prepaid, return receipt requested, or sent by express courier or telecopier and confirmed by mail as aforesaid. The date of receipt shall be deemed to be the date on which such notice has been received by the party to whom it is addressed. Notice shall be delivered or mailed to a party to the attention of the persons named below and at the following addresses or to such other persons or at such other places as a party shall designate in writing.

To SWMC: SONOMA WEST MEDICAL CENTER, INC
501 PETALUMA AVE.
SEBASTOPOL, CA 95472

ATTENTION: RAYMOND HINO, CEO

To the District: Palm Drive Health Care District
501 Petaluma Ave.
Sebastopol, California 95472
Phone:
Fax:
Attention: President, Board of
Directors

12.2 Independent Contractors. SWMC's appointment and actions hereunder are in the status of an independent contractor. SWMC and the District acknowledge and agree that one is neither the employee nor the employer of the other, and that they are not partners or joint venturers. For all purposes, this Agreement shall be construed as creating only a relationship pursuant to which SWMC may act as agent of the Hospital Governing Board.

12.3 Medicare Books and Records. SWMC agrees that, until the expiration of seven (7) years after the furnishing of services pursuant to this Agreement, it will, if requested by the Secretary of the Department of Health and Human Services or the U.S. Comptroller General or any of their designees, furnish to them copies of its books and records evidencing the nature of the services performed and, if any services are performed under a subcontract, SWMC shall require any such subcontractor to so agree as well.

12.4 Assignment; Successors and Assigns. Except as specifically provided herein, SWMC shall not assign its rights and duties under this Agreement without the prior written consent of the District. The terms, provisions, covenants, obligations and conditions of this Agreement shall be binding upon and shall inure to the benefit of successors in interest and assigns of the parties hereto; provided, however, that no assignment, transfer, pledge or mortgage by or through a party in violation of the provisions of this Agreement shall vest any rights in the assignee, transferee, pledgee or mortgagee.

12.5 Entire Agreement; Amendment. This Agreement constitutes the entire agreement between the parties with respect to the subject matter hereof and supersedes all prior and contemporaneous agreements, understandings, negotiations and discussions, whether written or oral, between the parties regarding said subject matter. No amendments, changes or additions to this Agreement shall be binding upon the parties unless made in writing and signed by the parties hereto.

12.6 Captions. The captions used herein are for convenience of reference only and shall not be construed in any manner to limit or modify any of the terms hereof.

12.7 Prevention of Performance. Neither party shall be liable to the other for any delay or damage or any failure to act (other than payment of money) as a result, occasioned or caused by reason of federal or State laws or the rules, regulations or orders of any public body or official purporting to exercise authority or control respecting the operations covered hereby, or as a result of, occasioned or caused by strikes, action of the elements, acts of God or other causes beyond the control of the parties, and delay as a result of the above causes shall not be deemed to be a breach of or failure to perform under this Agreement.

12.8 Waiver. The waiver of a performance of any the obligation of any term or condition of this Agreement shall not be effective unless in writing executed by the party to whom performance is owed, and shall under no circumstances be deemed to constitute a waiver of subsequent performance of the same, or a breach or subsequent breach of any term or condition hereof.

12.9 Severability. Subject to Section 9.1 hereof respecting disposition of the validation action; In the event any provision of this Agreement is held to be unenforceable for any reason, the unenforceability thereof shall not affect the remainder of this Agreement, which shall remain in full force and effect and enforceable in accordance with its terms.

12.10 Further Assurances. Both parties shall promptly and duly execute and deliver to the other such further documents and assurances and take such actions as such party may reasonably request in order more fully to carry out the intent and purposes of this Agreement.

12.11 Time of Essence. Time is of the essence of this Agreement and the observance of each and every covenant and obligation made and created hereby.

12.12 Counterparts. This Agreement may be executed in any number of counterparts, each of which shall be an original, and all such counterparts together shall constitute but one and the same instrument.

12.13 Choice of Laws. This Agreement shall be governed by and construed in accordance with the laws of the State of California applicable to contracts entered into and to be performed wholly within the State.

12.14 Attorneys' Fees; Costs of Legal Action. In the event a party to this Agreement resorts to legal action against the other to enforce the terms and provisions of this Agreement, the prevailing party shall be entitled to recover the expenses and costs of such action, including, without limitation, its reasonable attorneys' fees incurred in connection therewith.

12.15 Dispute Resolution. Except as otherwise provided in this Agreement, in the event any disagreement, dispute or claim arises between SWMC and the District with respect to the enforcement or interpretation of this Agreement or any specific terms and provisions set forth in this Agreement, other than the right to terminate pursuant to Section 8.2 (collectively referred to in this section as a "Dispute"), such Dispute shall be settled in accordance with the following procedures:

a) Meet and Confer. In the event of a Dispute between the District and SWMC, either party may give written notice to the other party setting forth the nature of such Dispute ("Dispute Notice"). The parties shall meet and confer to discuss the Dispute in good faith within fifteen (15) days of the other party's receipt of a Dispute Notice in an attempt to resolve the Dispute ("Meet and Confer Discussions"). Each party shall designate two (2) representatives to participate in the Meet and Confer Discussions, and these representatives shall meet at such date(s) and time(s) as are mutually convenient to the representatives of each participant within the Meet and Confer Period (as defined below).

b) Mediation. If the parties are unable to resolve the Dispute within forty five (45) days following the date of receipt of the Dispute Notice by the District or SWMC, as applicable ("Meet and Confer Period"), then the parties agree to try in good faith to settle the Dispute through nonbinding mediation under the Commercial Mediation Rules of the American Arbitration Association. A single disinterested third-party mediator shall be selected jointly by the District and SWMC within ten (10) days following the end of the Meet and Confer Period. If the District and SWMC are unable to agree upon a mediator within such ten

(10) day period, then a mediator shall be selected by the nearest chapter of the Commercial Panel of the American Arbitration Association in accordance with its then current rules. The District and SWMC shall share equally the expenses of the mediator and the other costs of mediation

c) Arbitration of Disputes. Any Dispute which cannot be resolved by the parties within sixty (60) days following the end of the Meet and Confer Period will be submitted to binding arbitration, which arbitration shall be conducted in accordance with the following provisions:

i) Venue. The arbitration shall be conducted in the County of Sonoma, California, at such site as is mutually agreed by the parties

ii) Law. The governing law shall be the law of the State of California.

iii) Selection. There shall be a single arbitrator, selected in accordance with the then current rules of the Commercial Panel of the American Arbitration Association. The decision in writing of the arbitrator shall be final and binding upon the parties.

iv) Administration. The arbitration shall be administered by the American Arbitration Association.

v) Rules. The rules of arbitration shall be the Commercial Arbitration Rules of the American Arbitration Association, as modified by any other written instruments that the parties hereto may agree upon at the time of the arbitration, except that the provisions of the California Code of Civil Procedure ("CCP") Section 1283.05 are incorporated into and made applicable to this agreement to arbitrate, unless the parties agree otherwise at such time. For good cause shown and on order of the arbitrator, depositions may be taken and discovery may be obtained in accordance with CCP Section 1283.05.

vi) Award. The award rendered by arbitration shall be final and binding upon the parties hereto, and judgment upon the award may be entered in any court of competent jurisdiction in the United States. The arbitrator(s) may decide the dispute in accordance with the applicable substantive law of California. An award shall be beyond the power of the arbitrator(s) if the findings of fact are not supported by substantial evidence or the award is based on an error of law. The award shall include written findings of fact, a summary of the evidence and reasons underlying the decision and conclusions of law. As part of the award, the arbitrator(s) may award reasonable and necessary costs actually incurred by the prevailing party, including that party's share of the arbitrator's fees, costs and expenses, as well as any administrator's fees. The arbitrator(s) may also include reasonable attorney's fees in an award of costs if the arbitrator(s) find that the party against whom the fees are assessed acted frivolously or in bad faith in its demand for, or participation in, the arbitration.

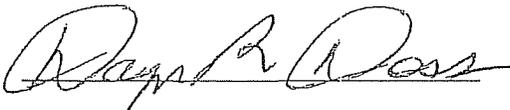
d) Right to Terminate Preserved. The provisions of this Section 12.15 shall not affect either party's right to terminate this Agreement in accordance with Section 8.2. The Parties shall nonetheless be bound by the terms of this Section 12.15 with respect to mediation and arbitration of any disputes asserting damages for breach by reason of

such termination.

12.16 Survival. In addition to any provisions which by their express terms survive termination of this Agreement, the provisions of Article IX hereof (Indemnification) shall survive the termination of this Agreement.

IN WITNESS WHEREOF, the parties have executed this Management Services Agreement, by their duly authorized representatives, as of the date and year first above written.

PALM DRIVE HEALTH CARE DISTRICT

By: 

Its: Chief Executive Officer

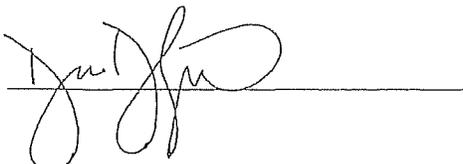
By: 

Its: President, Board of Directors

SONOMA WEST MEDICAL CENTER

By: 

Its: Chief Executive Officer

By: 

Its: President, Board of Directors