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2/28/2019

TO: Local Agency Formation Commission

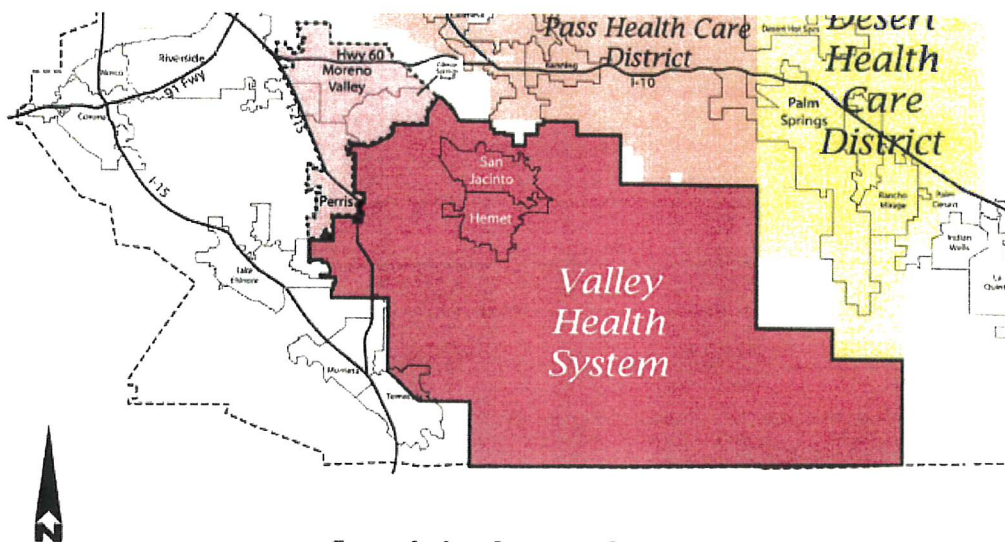
FROM: Joshua Altopp, Local Government Analyst III

SUBJECT: LAFCO 2018-14-3&5-SPHERE OF INFLUENCE REVIEW AND POTENTIAL AMENDMENT OF VALLEY HEALTH SYSTEM



EXECUTIVE SUMMARY:

This report reviews the sphere of influence (SOI) of Valley Health System (VHS), formerly Hemet Valley Hospital District, a health care district established pursuant to the Health and Safety Code §32000 et seq. After providing healthcare services for many decades, the District filed for Chapter 9 bankruptcy protection in 2007. The District completed sale of all its assets by the end of 2010 and terminated all its employees. Until recently, the District was involved in protracted litigation regarding its retirement plan, preventing final disbursement of funds to plan participants. The litigation has been dismissed and disbursement should soon be completed.

With all its obligations taken care of, the District is expected to file an application for dissolution within the next few months. Staff recommends the adoption of a "zero" SOI designation, to Valley Health System which, will streamline future dissolution proceedings.



Commission Approved on: 10/27/ 2005

-  Valley Health System
-  Valley Health SOI

RIVERSIDE LOCAL AGENCY FORMATION COMMISSION

6216 BROCKTON AVENUE, SUITE 111-B, RIVERSIDE, CA 92506 • PHONE (951) 369-0631 • www.lafco.org

provide increasing levels of charity care. Accordingly, uncompensated care costs rose dramatically, with no third-party reimbursement.

Faced with these conditions, in 2007, VHS sought voter approval of a parcel tax in order to undertake the mandated seismic retrofitting and replacement of its three hospitals. Unfortunately, although most voters approved the assessment, it failed to gain the requisite 2/3 majority. Faced with diminishing reimbursement, increasing annual losses, and the need for large capital expenditures, in December 2007, VHS filed for protection under Chapter 9 of the federal Bankruptcy Act.

BANKRUPTCY AND LITIGATION: In 2008, VHS sold its Moreno Valley hospital to Kaiser (current operator). In 2009, VHS entered into an agreement to sell its remaining hospitals and other facilities to Physicians for Healthy Hospitals, Inc. In April 2010 after signing Bankruptcy Court litigation by a losing suitor challenging the proposed sale. The sale of all of VHS's facilities was completed in October 2010. Substantially all the sale proceeds were utilized to pay VHS's secured and unsecured creditors. All VHS employees were terminated. VHA has had no employees since the completion of the sale. The only income which VHS had after the sale was a limited stipend from the buyer pursuant to sale agreement, which ended in 2015.

RECENT DISTRICT ACTIVITIES: VHS remained in existence after the sale of its assets, and the VHS Board continued to carry out its mandate of serving the community. However, without any remaining facilities and without the ability to obtain new tax revenues, its sole function was to expend remaining funds to assist local nonprofit entities serving the communities within VHS's District boundaries. These funds included some remaining District general funds, as well as unexpended funds from a 1977 bequest from a local resident Beatrice Brown (originally \$70,000), the balance of which had accrued to approximately \$800,000 (in 2016 dollars) and which was required to be used for health care related purposes for children. In addition, in 2013, when the nonprofit foundation at VHS's former Menifee hospital dissolved, pursuant to its charter documents and Probate Court order, approximately \$1,500,000 reverted to VHS.

The VHS board appointed a committee which included several Board members and several community representatives to develop standards for disbursement of these funds to various nonprofit organizations and school districts serving the community, and to make recommendations to the VHS Board for grants. Recommendations were made and some charities receiving funds included the Boys and Girls Club of Menifee Valley, VIP Tots, Voices for Children, Center Against Sexual Assault of Southwest Riverside County, Mt San Jacinto College

Foundation, Riverside County CASA Program and the 100 Mile Club all within VHS District territory. As of September 2018, all such designated funds have been disbursed for all intended purposes.

As of writing this report all lawsuits pending against VHS have either been resolved or dismissed. VHS is waiting for a response from the IRS regarding approval of the correct method of the disbursement of retirement funds. This may take several months to receive a response from the IRS, which means that the dissolution may not come back to the Commission for several months.

FINANCIAL STATEMENTS: The District does not receive a portion of the one percent base property tax levy, nor does it receive taxes or assessment. The VHS Board intends to designate the County of Riverside as the successor agency. VHS would then transfer any remaining funds to the County.

COMMENTS FROM AFFECTED AGENCIES/INTERESTED PARTIES: There have been no significant comments received from any affected agency concerning this proposal.

CONCLUSIONS:

At this point in time, VHS no longer owns or operates any facilities, the VHS Board has completed the distribution of all the charitable funds administered by the Board, and VHS has no tax revenue base or any other income to fund any new activities. Accordingly, the VHS Board believes that VHS has now fulfilled all its public health and charitable purposes, and that the District should be wound up and dissolved.

Per the requirements of Government Code Sec. 57077.1(c)(1) will allow the Commission to immediately order the dissolution without costly protest proceedings or election, which would otherwise be required for a healthcare district if VHS Board initiates the dissolution.

Staff recommends adoption of a "zero" SOI designation, which will streamline future dissolution proceedings.

SPECIFIC RECOMMENDATIONS:


Based on the factors outlined above, IT IS RECOMMENDED that the Commission adopt a resolution taking the following actions:

1. The LAFCO Commission, as lead agency under the California Environment Quality Act (CEQA), has found the sphere amendment to be statutorily exempt from CEQA pursuant to Public Resources Code Section 21080(b)(1) and CEQA Guidelines Section 15268, as

the filing of the proposal was required by statute and, therefore, it is a ministerial action. Furthermore, the concurrent amendment of the District sphere of influence is found to be exempt from CEQA pursuant to CEQA Guidelines Section 15061(b)(3), as it can be seen with certainty that there is no possibility that the activity will have a significant effect on the environment.

2. Adopt the attached Statement of Determinations for the proposed Valley Health System sphere of influence amendment ("zero" sphere of influence).
3. Approve **LAFCO 2018-14-3&5-SPHERE OF INFLUENCE REVIEW AND POTENTIAL AMENDMENT OF VALLEY HEALTH SYSTEM** from its current sphere and establishing a "zero" sphere of influence.
4. Approve **LAFCO 2018-14-3&5-SPHERE OF INFLUENCE REVIEW AND POTENTIAL AMENDMENT OF VALLEY HEALTH SYSTEM**, subject to the following terms and conditions:
 - a. The Valley Health System (VHS) shall defend, indemnify, and hold harmless the Riverside Local Agency Formation Commission ("LAFCO"), its agents, officers, and employees from any claim, action, or proceeding against LAFCO, its agents, officers, and employees to attack, set aside, void, or annul any approval of LAFCO concerning this proposal.

Respectfully submitted,



Joshua Altopp
Local Government Analysis III

**STATEMENT OF DETERMINATIONS FOR
LAFCO 2018-14-3&5-SPHERE OF INFLUENCE REVIEW AND POTENTIAL
AMENDMENT OF VALLEY HEALTH SYSTEM**

1. THE PRESENT AND PLANNED LAND USES IN THE AREA, INCLUDING AGRICULTURAL AND OPEN SPACE USES:

The affected area includes both incorporated and unincorporated urbanized areas of the cities of Hemet, San Jacinto, Menifee, Moreno Valley, Perris and the unincorporated communities of French Valley, Homeland, Romoland, Nuevo, Winchester, Aguanga, Anza and Idyllwild. The area within VHS District encompasses the full range of land uses, as well as suburban and rural unincorporated communities, agricultural lands and natural undeveloped lands. Similarly, land uses planned by the County and the cities included in the affected area include a wide range of residential, commercial, industrial, agricultural and open space designations.

2. THE PRESENT AND PROBABLE NEED FOR PUBLIC FACILITIES AND SERVICES IN THE AREA:

The current territory Valley Health System provides coverage to has been replaced in time, by additional medical services from both the private the public sectors, more so within the last 20 years as the cities and unincorporated communities continue to develop, areas once rural are becoming more urbanized and as such more medical resources are being provided to the growing population, as needed. This in turn makes Valley Health System obsolete.

3. THE PRESENT CAPACITY OF PUBLIC FACILITIES AND ADEQUACY OF PUBLIC SERVICES WHICH THE AGENCY PROVIDES OR IS AUTHORIZED TO PROVIDE:

Although there are some measures used in the healthcare industry, such as the ratio of providers to population, the capacity of health services is not as easily quantifiable as wastewater or transportation facilities. The District's service area, as it currently exists needs are met with through the growth of private/public medical facilities, which provide a wide range of services to the public at large. This increase in other providers eliminates the need for the existence of Valley Health System.

4. THE EXISTENCE OF ANY SOCIAL OR ECONOMIC COMMUNITIES OF INTEREST IN THE AREA:

The affected area is incredibly diverse. It contains some of the highest and lowest income communities in the County. The

amendment of the sphere of influence to "zero" will not have any affect on any social or economic community of interest because Valley Health System does not currently provide any services to the public.

CORRESPONDENCE
Letter from attorney's representing VHS
(summary of VHS activities)

Law Offices

LEWITT, HACKMAN, SHAPIRO,
MARSHALL & HARLAN
A LAW CORPORATION

JOHN B. MARSHALL, ESQ.
JMARSHALL@LEWITTHACKMAN.COM
(818) 907-3228

16633 VENTURA BOULEVARD
ELEVENTH FLOOR
ENCINO, CALIFORNIA 91436-1865

(818) 990-2120
TELECOPIER (818) 981-4764
WWW.LEWITTHACKMAN.COM

REFER TO FILE NUMBER
5387-170

October 30, 2018

Riverside County Local
Agency Formation Commission
6216 Brockton Avenue
Suite 111-B
Riverside, CA 92506

Attn: George J. Spiliotis,
Executive Officer

Re: Valley Health System

Dear Mr. Spiloitis:

I am General Counsel to Valley Health System, a California Local Health Care District ("VHS" or the "District"), and have acted in that capacity since 1991. At the request of Vinay Rao, Chairperson of the VHS Board of Directors, I have been asked to summarize the status of VHS's activities as a Local Health Care District and the reasons that it should now be dissolved.

VHS was originally formed as a special district in 1946 under the Local Hospital District Law (*Health & Safety Code* Section 32000, et seq.). It was originally formed as Hemet Valley Hospital District to acquire and operate a 20-bed hospital owned by the City of Hemet. The hospital later became known as Hemet Valley Medical Center. Over the years, VHS expanded this hospital facility, building several towers, and ultimately increasing capacity to over 300 beds. In 1989, it open two additional hospitals in what is now the City of Menifee and in Moreno Valley, as well as a skilled nursing facility in Hemet. In the 1990's, "Hospital Districts" became "Health Care Districts" and the District's name was changed to Valley Health System. The geographical size of VHS's District was also expanded to include the areas in and around its Menifee hospital, and the VHS Board was expanded to seven and divided into zones.

In the late 1980s, VHS incurred significant tax-exempt bond indebtedness to build and expand its facilities. However, during the 1990s, reimbursement to hospitals through Medicare, Medi-Cal and other governmental programs, as well as through preferred provider insurance plans and health maintenance organizations (HMOs), changed and decreased dramatically. Hospitals also became obligated under the federal Emergency Medical Treatment and Active Labor Act (EMTALA) to provide significantly greater levels of emergency and related services to patients without regard to ability to pay, and under State law to provide increasing levels of charity care. Accordingly, uncompensated care costs rose dramatically, with no third-party reimbursement. In

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addition, California legislation required hospitals to undertake expensive seismic retrofit and ultimately replacement programs. To complicate matters, during the 1970s, VHS had voluntarily given up imposing taxes and assessments. With the passage of Proposition 13 in 1978, new taxes and assessments required approval by two-thirds vote of the electorate. Accordingly, VHS could not make up lost revenues without voter approval of new taxes and assessments.

Faced with these conditions, in 2007, VHS sought voter approval of a parcel tax in order to undertake the mandated seismic retrofitting and replacement of its three hospitals. Unfortunately, although a majority of voters approved the assessment, it failed to gain the requisite 2/3 majority. Faced with diminishing reimbursement, increasing annual losses, and the need for large capital expenditures, in December, 2007, VHS filed for protection under Chapter 9 of the federal Bankruptcy Act.

In 2008, VHS sold its Moreno Valley hospital to Kaiser. In 2009, VHS entered into an agreement to sell its remaining hospitals and other facilities to Physicians for Healthy Hospitals, Inc. ("PHH"). Voter approval required under the Health Care District Law was obtained in December, 2009. In April, 2010, after significant Bankruptcy Court litigation by a losing suitor challenging the proposed sale, the Bankruptcy Court approved VHS's Plan of Adjustment, including the sale to PHH. The sale of all of VHS's facilities was completed in October, 2010. Substantially all of the sale proceeds were utilized to pay VHS's secured and unsecured creditors under the Plan of Adjustment. All VHS employees were terminated, with most being offered positions with PHH. VHS has had no employees since completion of the sale, other than a contracted part-time Clerk of the VHS Board. The only income which VHS had after the sale was a limited stipend from PHH pursuant to the sale agreement to cover various organizational and election expenses, which ended in 2015.

VHS remained in existence after the sale, and the VHS Board continued to carry out its mandate of serving the community. However, without any remaining facilities and without the ability to obtain new tax revenues, its sole function was to expend remaining funds to assist local nonprofit entities serving the communities within VHS's District boundaries. These funds included some remaining District general funds, as well as unexpended funds from a 1977 bequest, the balance of which was approximately \$800,000 and which was required to be used for health care related purposes for children. In addition, in 2013, when the nonprofit foundation at VHS's former Menifee hospital dissolved, pursuant to its charter documents and a Probate Court order, approximately \$1,500,000 reverted to VHS. Pursuant to the Court order, these funds were required to be expended for various health-related purposes in specific geographical areas formerly served by the Menifee hospital's nonprofit foundation.

The VHS Board appointed a committee which included several Board members and several community representatives to develop standards for disbursement of these funds to various nonprofit organizations and school districts serving the community, and to make recommendations to the VHS Board for grants. The committee made a number of recommendations, the recommended nonprofit entities and school districts made presentations at public Board meetings,

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and the VHS Board made various grants from these funds. As of September, 2018, all of such designated funds had been disbursed for the intended purposes.

VHS was involved in several lawsuits with respect to its defined benefit Retirement Plan, but all of such litigation has now been dismissed. Such litigation prevented final disbursement of remaining Retirement Plan funds, which the VHS Board holds in trust. It is the current intent of the VHS Board to disburse these funds and most of its remaining District funds to the participants in its former Employee Retirement Plan, and the Board is currently working with its independent actuaries to determine how to disburse these funds.

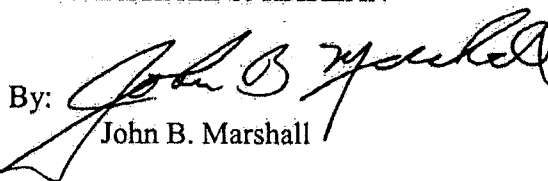
The VHS Board intends to designate the County of Riverside as the successor agency. VHS would transfer its small remaining funds to the County. There is currently no further litigation pending, the VHS Board does not believe that there are any other cognizable claims. VHS remains insured for any future malpractice claims through Beta Healthcare, the collective insurer for California's Health Care Districts (any applicable statute of limitations has long since passed, with the possible exception of babies and minors who have not yet reached age 21, and all cases arising from actions prior to VHS's sale of its hospitals in October, 2010, have long since been resolved by VHS's insurer).

Therefore, as of this point in time, VHS no longer owns or operates any facilities, the VHS Board has completed the distribution of all of the charitable funds administered by the Board, and VHS has no tax revenue base or other income to fund any new activities. Accordingly, with the exception of final distribution of Retirement Plan funds, the VHS Board believes that VHS has now fulfilled all of its public health and charitable purposes, and that the District should be wound up and dissolved.

If you have any questions concerning the foregoing, please do not hesitate to contact me or VHS Board Chairman Vinay Rao.

Very truly yours,

LEWITT, HACKMAN, SHAPIRO,
MARSHALL & HARLAN

By: 
John B. Marshall

cc: VHS Board