Service Review and Audit of the El Camino Hospital District

Presented to CALAFCO by:
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Background and History
Background and History

• 1956: El Camino Hospital District established before suburbanization, evolving to become a major healthcare service provider in the County.

• 1992: El Camino Hospital Corporation was created and major assets of the District were transferred, leased or sold to the Corporation.

• 1992: District designates the Corporation as the entity responsible for providing direct services to District residents.

• 1997: District assumes control of the Corporation as its “sole member”.
Background and History

• 2009: Corporation expands operations by purchasing the Los Gatos Hospital campus, which is located outside of the District and Sphere of Influence

• 2011: Santa Clara County Civil Grand Jury criticizes the District and Corporation for:
  
  unclear accountability
  
  lack of financial and organizational transparency
  
  Actions independently undertaken to acquire the Los Gatos Hospital campus without first seeking approval from Santa Clara County LAFCo.

• 2011: Santa Clara County LAFCo initiates service review and audit to examine specific questions
Scope of Service Review
And Audit
Two main project components:

• **Service Review**: State law, LAFCo Policies and Service Review Guidelines

• **Limited Scope Audit**: USGAO *Government Auditing Standards*

Primary objectives of the project: to determine whether -

• El Camino Hospital District is providing services outside of its boundaries using tax payer funds

• The District should continue to exist and/or continue to receive public funds.

• Another entity could provide the District’s services more efficiently?
Service Review & Audit Scope

Respond to specific questions posed by LAFCo to:

• Analyze the El Camino Hospital District’s governance structure;

• Determine the District’s financial relationship to the El Camino Hospital Corporation and affiliated non-profit organizations;

• Assess the financial condition of the District and Corporation;

• Report on the availability of reserves;

• Determine the source and use of taxpayer funds related to:
  
  hospital operations;
  
  capital improvements; and,
  
  the acquisition of the Los Gatos Hospital campus.
El Camino Hospital District

Service Review
ECHD Mountain View Service Profile

- El Camino Hospital utilization averages 62.2% for all major service categories, although percentage utilization varies by individual service.

<table>
<thead>
<tr>
<th>Unit</th>
<th>Licensed Beds</th>
<th>Patient Days</th>
<th>Average Daily Census</th>
<th>Percent Utilization</th>
</tr>
</thead>
<tbody>
<tr>
<td>Medical/Surgical</td>
<td>180</td>
<td>41,490</td>
<td>113.7</td>
<td>63.2</td>
</tr>
<tr>
<td>Perinatal (Obstetric)</td>
<td>44</td>
<td>10,458</td>
<td>28.7</td>
<td>65.2</td>
</tr>
<tr>
<td>Intensive Care</td>
<td>24</td>
<td>6,836</td>
<td>18.7</td>
<td>77.9</td>
</tr>
<tr>
<td>Neonatal ICU</td>
<td>30</td>
<td>4,297</td>
<td>11.8</td>
<td>39.3</td>
</tr>
<tr>
<td>General Acute Care</td>
<td>278</td>
<td>63,081</td>
<td>172.9</td>
<td>62.2</td>
</tr>
</tbody>
</table>

Note: The table reflects a 99 licensed medical/surgical beds reduction, scheduled to take effect in 2012.
Source: OSHPD ALIRTS Facility Utilization Statistics, 2010
El Camino Hospital provides 9.4% of acute care services in the County, with 8.9% of licensed beds and 8.9% of excess capacity.

Overall, El Camino Hospital utilization is near to the County’s as a whole, at 62.2% versus 60.9%.

### Countywide Comparison of Capacity and Service Utilization

<table>
<thead>
<tr>
<th>Unit</th>
<th>Countywide ADC</th>
<th>ECH ADC</th>
<th>Percent County</th>
</tr>
</thead>
<tbody>
<tr>
<td>Medical-Surgical</td>
<td>1,262.2</td>
<td>113.7</td>
<td>9.0%</td>
</tr>
<tr>
<td>ICU/CCU</td>
<td>242.3</td>
<td>18.7</td>
<td>7.7%</td>
</tr>
<tr>
<td>Perinatal (Obstetric)</td>
<td>185.9</td>
<td>28.7</td>
<td>15.4%</td>
</tr>
<tr>
<td>NICU</td>
<td>146.1</td>
<td>11.8</td>
<td>8.1%</td>
</tr>
<tr>
<td>Total Acute ADC</td>
<td>1,836.8</td>
<td>172.9</td>
<td>9.4%</td>
</tr>
<tr>
<td>Licensed Beds</td>
<td>3,017.0</td>
<td>278.0</td>
<td>8.9%</td>
</tr>
<tr>
<td>Excess/Deficiency</td>
<td>1,180.5</td>
<td>105.1</td>
<td>8.9%</td>
</tr>
<tr>
<td>Percent Utilization</td>
<td>60.9%</td>
<td>62.2%</td>
<td></td>
</tr>
</tbody>
</table>

Source: OSHPD ALIRTS Facility Utilization Statistics, 2010
## Inpatient Geographic Distribution

<table>
<thead>
<tr>
<th>Inpatient Address at Discharge</th>
<th>Cases</th>
<th>Percent</th>
<th>Cum Percent</th>
</tr>
</thead>
<tbody>
<tr>
<td>Within the District</td>
<td>7,331</td>
<td>43%</td>
<td>41%</td>
</tr>
<tr>
<td>Within the SOI</td>
<td>1,199</td>
<td>7%</td>
<td>50%</td>
</tr>
<tr>
<td>Other County/State/Outside State</td>
<td>8,418</td>
<td>50%</td>
<td>100%</td>
</tr>
<tr>
<td>Total</td>
<td>16,948</td>
<td>100.0%</td>
<td></td>
</tr>
</tbody>
</table>

Source: El Camino Hospital District

- Approximately 43% of inpatients are located within the District.
- Approximately 50% of inpatients are located within the District or its Sphere of Influence.
- Generally, hospitals consider 60% to 75% of their patients to originate from within their “primary service area.”
- State data suggests that ECHD has consistently captured about 40% of market share in the areas that it serves.
Inpatient Discharges

El Camino Hospital Inpatient Discharges by Zip Code (CY2010)

Source: El Camino Hospital District data compared against OSHPD data for prior fiscal year.
## Emergency Room Geographic Distribution

<table>
<thead>
<tr>
<th>Emergency Room Patient Address</th>
<th>Visits</th>
<th>Percent</th>
<th>Cum Percent</th>
</tr>
</thead>
<tbody>
<tr>
<td>Within the District</td>
<td>22,586</td>
<td>53%</td>
<td>53%</td>
</tr>
<tr>
<td>Within the SOI</td>
<td>2,960</td>
<td>7%</td>
<td>60%</td>
</tr>
<tr>
<td>Other County/State/Outside State</td>
<td>16,660</td>
<td>40%</td>
<td>100.0%</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td>42,176</td>
<td>100.0%</td>
<td></td>
</tr>
</tbody>
</table>

Source: El Camino Hospital District

- 53% of emergency room patients originate from within the District.
- 60% of emergency room patients originate from within the District or its SOI.
- Because of the emergent nature of services, expectation is that visit data would draw from a tighter geographic area.
Service Review Conclusions

**Excess Capacity Even with Projected Population Growth**

- County of Santa Clara has excess capacity for many services

- ECH general acute care inpatient utilization rate = 62.2%

- ECH has 8.9% of excess capacity for all licensed beds in County

- Projected increase in inpatient demand over the next 5-7 years:
  - Countywide: 9.0%-13.0%
  - El Camino Hospital: 5.8%-8.3%

- Excess capacity is likely to remain in most services, except ICU
Service Review Conclusions

Large Proportion of Services Provided Outside of the SOI

• Except the Los Gatos Hospital and 2 dialysis centers in San Jose, all ECHD facilities are located within jurisdictional boundaries.

• ECH Inpatient Services:
  • 43% = residents of the District
  • 7% = resident of the SOI
  • 38% = residents outside SOI, inside County
  • 12% = residents outside of the County

• ECH Emergency Dept Services:
  • 54% = residents of the District
  • 6% = residents of the SOI
  • 29% = residents outside SOI, inside County
  • 11% = residents outside of the County
Service Review Conclusions

**Market Share Consistent Across District Boundaries and SOI**

- ECH Mountain View captures 40% of market share in District & SOI

- Patients in these catchment areas seek 90% of their inpatient care from within the County

- ECH Mountain View receives some “in-migration” of inpatient volume from the Los Gatos area (in FY 2010, about 5.6% of area’s total cases.)
El Camino Hospital District

Audit
ECHD & Corporation Relationship

For financial reporting purposes, the District is shown as a single entity comprised of component units that include the Corporation and all other affiliated organizations.

“GAAP directs those who prepare financial statements to look beyond the legal barriers that separate these various units to define each government’s financial reporting entity in a way that fully reflects the financial accountability of the government’s elected officials.”

Criteria:

• Appointment of the entity’s governing board by the primary government
• Fiscal dependency on the primary government
• When exclusion would lead to misleading financial reporting

The governing boards were essentially the same since a 1996 restructuring that defined the District as the “sole member” of the Corporation

Corporation has benefited from asset transfer, tax contributions and the availability of public debt instruments used to finance various Mountain View campus improvements

Budget presentation to the Board(s) was exactly the same for the District and Corporation with little regard to 1) differentiation between the various units, 2)
ECHD & Corporation Relationship

Other Evidence of Organizational Integration:

Moody’s made no differentiation when it downgraded the Corporation’s revenue bonds in May 2011 and it noted the Los Gatos Hospital purchase was a “fundamental modification” of the District’s core operating strategy.

Corporation meets all tests requiring Brown Act public disclosure.

Created by a legislative body to exercise authority that may be delegated to the private corporation or entity - GC Section 54952(c)(1)(A)

Provides some funding to the private corporation or entity and appoints one of its members to serve as a voting member of the entity’s board of directors – GC Section 54952 (c)(1)(B)
District Financial Assessment

- The Corporation received a net asset transfer of $175.5 million in 1992

- The Corporation continues to receive access to discounted municipal debt financing, which it can access due to its affiliation with the District and status as a non-profit public benefit corporation

- Financial indicators show that the District, the Corporation and its affiliated entities were performing well and was in a relatively strong financial position, as of June 30, 2011 with the consolidated entity holding $440 million in unrestricted net assets, of which $409 million was in cash

- Outlook for FY 2011-12: District continues to strengthen based on financial status update presented February 8, 2012.

- The Corporation continues to receive significant property tax contributions from the District.
Financial Benefits Related to Public Agency Standing

Property Tax Share

Portion of 1% Ad Valorem

Debt Service on 2003 General Obligation Bonds ($148 million) to construct new Mountain View Hospital

Combined receipts of between $15 million and $16 million per year.

<table>
<thead>
<tr>
<th></th>
<th>2010-11</th>
<th>2009-10</th>
<th>2008-09</th>
<th>2007-08</th>
<th>2006-07</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>One Percent Ad Valorem</td>
<td>$3,368</td>
<td>$2,830</td>
<td>$3,510</td>
<td>$3,207</td>
<td>$3,046</td>
<td>$15,961</td>
</tr>
<tr>
<td>Restricted for Capital Use</td>
<td>$6,643</td>
<td>$6,920</td>
<td>$6,658</td>
<td>$5,692</td>
<td>$5,041</td>
<td>$30,954</td>
</tr>
<tr>
<td>Unrestricted</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>28,200</td>
</tr>
<tr>
<td>Totals</td>
<td>$15,793</td>
<td>$15,608</td>
<td>$15,900</td>
<td>$14,792</td>
<td>$13,022</td>
<td>$75,115</td>
</tr>
</tbody>
</table>
ECHD & Corporation Relationship

Financial Benefits Related to Public Agency Standing

• The District has transferred over $105 million to the Corporation over the past five years, including:
  - $17.7 million for debt service
  - $13.7 million for community benefit
  - $21.2 million for specified capital improvements
  - $52.5 million in surplus cash transfers, designated for capital improvements and made to avoid being in violation of the Gann Appropriation Limit

<table>
<thead>
<tr>
<th></th>
<th>Fiscal Year</th>
<th>Five Year</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>2010-11</td>
<td>2009-10</td>
</tr>
<tr>
<td>Debt Service</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Interest Payments</td>
<td>$4,897</td>
<td>$4,859</td>
</tr>
<tr>
<td>Principal Reduction</td>
<td>1,384</td>
<td>1,223</td>
</tr>
<tr>
<td>Community Benefits Transfer</td>
<td>2,025</td>
<td>5,731</td>
</tr>
<tr>
<td>Capital Expense Transfer</td>
<td>-</td>
<td>12,458</td>
</tr>
<tr>
<td>Surplus Cash Transfer</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Totals</td>
<td>$8,306</td>
<td>$24,271</td>
</tr>
</tbody>
</table>
The District and the Corporation are effectively one consolidated entity from a governance and financial perspective.

As a result of the $175.5 million net asset transfer the Hospital Corporation received from the District in 1992, the Corporation’s strong financial health is better than it would otherwise be.

The Corporation continues to be well served by receiving benefits typically reserved for public agencies, including the receipt and use of property tax, and access to discounted municipal financing.

The Corporation continues to receive surplus cash infusions from the District, amounting to at least $52.5 million in the past five years -- roughly equivalent to the $53.7 million purchase price of the Los Gatos hospital.

The Corporation is in a strong and strengthening financial position, with the consolidated entity holding $440 million in unrestricted net assets as of 6/30/2011, of which $409 million was in cash (cash reserves of more than 70% of annual operating expenses).
Community Benefits
Community Benefit

Hospital District Requirements – CA Law

SB 697 (1994) defines Community Benefit as “a hospital’s activities that are intended to address community needs and priorities primarily through disease prevention and improvement of health status, including, but not limited to, any of the following:

a) Health care services rendered to vulnerable populations
b) The unreimbursed cost of services
c) Financial or in-kind support of public health programs
d) Donation of funds, property, or other resources
e) Health care cost containment.
f) Enhancement of access to health
g) Services offered without regard to financial return
h) Food, shelter, clothing, education, transportation, and other goods or services that help maintain a person's health.
Charitable Hospital Requirements – IRS Law

IRS Revenue Rulings 69-545 & 83-157 define “Community Benefit Standard” to determine charitable status of hospitals:

a) Governing body of the hospital is composed of independent members of the community

b) Medical staff privileges in the hospital are available to all qualified physicians in the area

c) Hospital operates a full-time emergency room open to all regardless of ability to pay

d) Hospital otherwise admits as patients those able to pay for care, either themselves or through-third party payers such as private health insurance or government programs such as Medicare

e) Hospital’s excess funds are generally applied to expansion and replacement of existing facilities and equipment, amortization of indebtedness, improvement in patient care, and medical training, education and research
### Total Community Benefit Provided by El Camino Hospital FY 2011

<table>
<thead>
<tr>
<th>Category</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Government-sponsored health care (unreimbursed Medicaid)</td>
<td>$23,639,790</td>
</tr>
<tr>
<td>Subsidized health services funded through hospital operations</td>
<td>$20,616,112</td>
</tr>
<tr>
<td>Financial and in-kind contributions</td>
<td>$4,002,154</td>
</tr>
<tr>
<td><strong>Traditional charity care funded through hospital operations</strong></td>
<td>$2,772,576</td>
</tr>
<tr>
<td>Community Health Improvement Services</td>
<td>$1,857,998</td>
</tr>
<tr>
<td>Health professions education funded through hospital operations</td>
<td>$1,171,764</td>
</tr>
<tr>
<td>Clinical research funded through hospital operations</td>
<td>$402,216</td>
</tr>
<tr>
<td>Community benefit operations funded through hospital operations</td>
<td>$185,830</td>
</tr>
<tr>
<td>Government-sponsored health care (means-tested programs)</td>
<td>$150,000</td>
</tr>
<tr>
<td><strong>Total Community Benefit, FY 2011</strong></td>
<td><strong>$54,798,440</strong></td>
</tr>
</tbody>
</table>

In total, $47.2 million of $54.8 million, or 86.1% of all reported ECH-MV Community Benefit, is for uncompensated care, including both District and Hospital Contributions.
## Community Benefit

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Community health improvement services (community health education, community-based clinical services, health care support services) provided at Mountain view location – includes Partners for Community Health (PCH) programs</td>
<td>$1,603,074</td>
</tr>
<tr>
<td>Financial and in-kind contributions (cash donations, grants, sponsorships) provided at Mountain View location – includes PCH programs</td>
<td>$3,361,624</td>
</tr>
<tr>
<td>Government-sponsored health care (means-tested programs) provided at Mountain View location – includes Healthy Kids, a PCH program</td>
<td>$75,000</td>
</tr>
<tr>
<td><strong>Total District-funded Community Benefit, FY 2011</strong></td>
<td><strong>$5,039,698</strong></td>
</tr>
</tbody>
</table>

Of the total $54.8 million in total community benefits, the District directly funds approximately $5.0 million.
The ECHD budget presentation lists a significant disruption to area safety net hospitals as among the top 5 financial risks facing the institution, since such reductions could result in more Medi-Cal or uninsured patients receiving care at El Camino Hospital.

<table>
<thead>
<tr>
<th>Facility</th>
<th>Medi-Cal Days</th>
<th>Total Days</th>
<th>% Medi-Cal Days</th>
</tr>
</thead>
<tbody>
<tr>
<td>KAISER FOUNDATION HOSPITAL - SANTA CLARA</td>
<td>1,778</td>
<td>88,874</td>
<td>2%</td>
</tr>
<tr>
<td>KAISER FOUNDATION HOSPITAL - SAN JOSE</td>
<td>1,446</td>
<td>50,285</td>
<td>3%</td>
</tr>
<tr>
<td>EL CAMINO HOSPITAL</td>
<td>4,832</td>
<td>79,939</td>
<td>6%</td>
</tr>
<tr>
<td>GOOD SAMARITAN HOSPITAL - SAN JOSE</td>
<td>6,783</td>
<td>82,942</td>
<td>8%</td>
</tr>
<tr>
<td>STANFORD UNIVERSITY HOSPITAL</td>
<td>18,200</td>
<td>134,394</td>
<td>14%</td>
</tr>
<tr>
<td>O'CONNOR HOSPITAL</td>
<td>11,463</td>
<td>59,098</td>
<td>19%</td>
</tr>
<tr>
<td>REGIONAL MEDICAL CENTER OF SAN JOSE</td>
<td>11,608</td>
<td>56,433</td>
<td>21%</td>
</tr>
<tr>
<td>ST. LOUISE REGIONAL HOSPITAL</td>
<td>2,617</td>
<td>12,496</td>
<td>21%</td>
</tr>
<tr>
<td>SANTA CLARA VALLEY MEDICAL CENTER</td>
<td>62,801</td>
<td>123,551</td>
<td>51%</td>
</tr>
<tr>
<td>Grand Total</td>
<td>121,528</td>
<td>688,712</td>
<td>18%</td>
</tr>
</tbody>
</table>
ECHD receives more property tax revenue than all but 1 district;
2/3 spent on debt service/capital improvements
1/3 spent on CB’s
11 of the 73 healthcare districts operating in CA as of February 2012 (including ECHD) had sold or leased their hospitals to a non-profit or for-profit corporation.

ECHD is unlike most other districts – each of the other 10 districts sold or leased their hospitals to multi-hospital systems (i.e. Sutter, CHW).

El Camino Hospital’s computed community benefit*, as a percentage of operating expenses, fell within the range of the five hospitals for which comparison information was available (four of the five hospitals contributed between 8.9% and 9.5% of annual expenditures spent on Community Benefits, with El Camino at 9.5%).

For the most part, El Camino Hospital District Community Benefit programs are provided to all patients and are not targeted toward District residents, even though such programs are paid for with District tax dollars.

*For comparison purposes, includes charity care, unreimbursed Medi-Cal, and other unreimbursed health care services to the poor and indigent.
El Camino Hospital District

Recommendations
Recap of Major Report Conclusions

• The El Camino Hospital District, the Corporation and four affiliated organizations, while legally separate, **effectively operate as a single entity** from governance, administrative, financial and public accountability perspectives.

• District **taxpayers have provided property taxes** for the acquisition, construction, maintenance and debt service for the El Camino Hospital Mountain View campus.

• Although permitted by State law, the **majority of inpatient services are provided to non-District residents**, who do not pay property taxes to the District. This condition will likely be exacerbated by the purchase and operation of the Los Gatos campus.

• Generally, **community benefits are not targeted toward District residents** and are instead used to support the broader healthcare mission of the Corporation.

• The **District and Corporation do not distinguish themselves** by the amount expended on community benefits, when compared to other hospital and healthcare districts in the State or other hospitals in the County.

• El Camino Hospital District, the Corporation and affiliated entities have been able to **accumulate significant unrestricted net assets** over the last five years, which provided the Corporation with the financial **capacity to purchase Los Gatos Hospital**.
Recommendation 1

1. **Request the District to implement improvements in governance, transparency and public accountability:**
   
a. Limit automatic contributions to El Camino Hospital Corporation for expenses other than debt service and capital improvements;

b. Seek a legal interpretation of the Gann Appropriation Limit and its applicability to ECHD, and modify budgeting practices accordingly;

c. Establish a competitive process for appropriating community benefit dollars, to ensure that funds are used to more directly benefit District residents;

d. Implement changes to the budget process: clear articulation of financial, budget and reserve policies; budgeted and actual revenues/expenditures by purpose, program and line item; staffing and compensation; community benefit program expenditures; etc.

e. Evaluate and report on professional services agreements;

f. Review and revise code of ethics and conflict of interest policies, to ensure the District avoids perceived or actual conflicts of interest.

**If not implemented within 12 to 18 months, request the District to initiate actions to separate the District and Corporation boards to ensure that the District’s mission is not compromised by competing corporate interests.**
Recommendation 2

2. If the prior recommendations are not initiated within six months of the request for governance change or if the Corporation further expands services beyond the District boundaries, consider whether to begin actions toward dissolution of the El Camino Hospital District.
Rationale for Recommendations:

- Maintaining the status quo without improvements in governance, transparency and public accountability would result in continued concerns regarding the need for District revenue contributions to go toward a non-profit corporation that no longer appears to be in need of taxpayer support.

- Neither the District nor the Corporation provide remarkable levels of community benefits to District residents, when compared with other healthcare districts in the State and with other hospitals within Santa Clara County.

- Continuation of taxpayer support, without broadening community benefit contributions beyond the Corporation and its affiliates, does not provide assurance that District residents receive an appropriate return on investment. In addition, it creates equity concerns, since approximately 57 percent of all inpatient services and 46 percent of all emergency services are provided to non-District residents, who are not taxed.

- Because the District serves as the “sole member” of the Corporation, the acquisition of the Los Gatos Hospital complicates the purpose of the District and, by extension, the Corporation. Further, the District made indirect monetary contributions to the Corporation that allowed it to use unrestricted net assets for the Los Gatos campus acquisition. A more distinct separation of the two entities would ensure greater public accountability.

- The separation of the entities and disposition of assets and liabilities would be complex. Therefore, before embarking on a path toward dissolution, Santa Clara County LAFCo should make an effort to encourage the District to implement suggested reforms.