Petaluma HEALTH CARE DISTRICT

Board of Directors Discussion

July 22, 2020

Marine Street Consulting, LLC

Historical Context

Petaluma HEALTH CARE DISTRICT

- In 1997, District engaged with SRM Alliance Hospital Services (SRM) to operate Petaluma Valley Hospital (Hospital) under a 20-year lease
- District issued RFP which included lease or sale option March 2015
- District chose SRM to lease Hospital, negotiations ended September 2017
- District selected Paladin Healthcare to lease Hospital, transaction terminated 2018

Historical Context

- Dec 2018 | District entered into LOI to lease Hospital to proposed joint operating company (JOC) between Providence St. Joseph Health (PSJH) and Adventist Health
- Oct 2019 | California Attorney General denied JOC, LOI expired
- District has continued to work with SRM over this time period to ensure continued access to Hospital services

Negotiations Update

Petaluma HEALTH CARE DISTRICT

- Over the past several months, conversations and negotiations held with several parties interested in leasing Hospital, including NorCal HealthConnect, LLC (NorCal HealthConnect) who now is the Purchaser
  - All conversations subject to mutual Nondisclosure Agreements requiring confidentiality
- Draft terms sheets with respect to a lease transaction were shared with each interested party
- Concurrently, the District engaged VMG Health to complete Fair Market Value analysis of Hospital's business and assets

Negotiations Update

Petaluma HEALTH CARE DISTRICT

- Late in the negotiations, NorCal HealthConnect stated its desire to purchase, rather than lease, the Hospital
- Key factors influencing its decision
  - Capital expenditures
  - Future purchase option

Key Terms of Proposed Sale

Petaluma HEALTH CARE DISTRICT

- Purchaser is a newly created not-for-profit, NorCal HealthConnect, whose sole member is Western HealthConnect
- Sale price of $52.6 million
- NorCal HealthConnect will commit to continue to operate Hospital as an acute care hospital with Emergency Department for **minimum 20 years** following Closing of the transaction
  - Commitment to continue OB services for 5 years following the Closing
  - Hospital does not provide now and will not provide:
    - Physician-assisted suicide
    - Elective abortions
    - Destruction of human embryos (fertility)

Key Terms of Proposed Sale

Petaluma HEALTH CARE DISTRICT

- Governance
  - District retains right to nominate one Hospital Board member for 10 years as long as community board exists
  - District will appoint one member to attend Quality Committee and Community Benefit Committee meetings for 10 years
- District will not compete in Hospital's Service Area for 5 years following the Closing
- NorCal HealthConnect will maintain Community Benefit expenditures in the Hospital service area consistent with current amounts for at least 10 years following Closing

Key Terms of Proposed Sale

Petaluma HEALTH CARE DISTRICT

- Employee Commitments:
  - NorCal will hire all eligible Hospital employees as of Closing with no diminution of salaries and benefits
  - All employees will be retained for at least 6 months following Closing
  - NorCal HealthConnect will assume all contract bargaining agreements
- All NorCal HealthConnect obligations guaranteed by Western HealthConnect

- **Closing of the transaction expected after voter approval** on or before December 31, 2020

Western HealthConnect

- Western HealthConnect (WHC) is a nonprofit corporation and is a “sister company” to Providence Health & Services (a subsidiary of PSJH)
- Created as part of the Swedish Health Services and Providence Health & Services affiliation in 2012
- WHC is the parent/sole member of other-than Catholic organizations affiliated with PSJH, such as Kadlec and Swedish Health Services

Advantages of Sale vs. Lease

Petaluma HEALTH CARE DISTRICT

- Locks in value of District’s largest asset
- Creates substantial corpus available to fund operations and community benefit for District population
- Eliminates reliance on operator’s acute care hospital profitability (ability to pay rent) to fund future District operations
- Covenant to maintain acute care hospital with emergency services for a minimum of 20 years
- Significantly less complicated transaction reduces District’s risk
- Eliminates risk that SB977 negatively impacts interest from other operators, now and in the future upon lease purchase option exercise and lease termination

Disadvantages of Sale vs. Lease

Petaluma HEALTH CARE DISTRICT

- Hospital ceases to be a District owned and controlled hospital
- Transparency of hospital operations will likely decrease (hospital Board/committee participation, hospital financial statements, quality reporting)
- District asset value locked in at current FMV (long term lease with purchase option could potentially generate higher overall proceeds to District but at greater risk)
- No possibility to change operators if dissatisfied with NorCal HealthConnect
  - Except in the case where post-Closing covenants are breached but at risk of finding a new operator

Rent & Tolling Agreement Letter

Petaluma HEALTH CARE DISTRICT

- District and SRM entered into an agreement to toll any dispute between them regarding the 1997 lease
- District and SRM are coming to an agreement to ensure SRM pays rent on the lease of the Hospital
- Rent currently at $800,000 per year unless and until voter approval and then increases to $2.5 million per year unless the sale does not go forward due to breach of the transaction agreements by the District
- If the sale does not go forward, SRM will return the Hospital and the underlying business and related assets to the District after 30 months
- District afforded time to find a new operator
- Risk of Hospital closure if new operator is not identified