



CITY OF HAYWARD

Hayward City Hall
777 B Street
Hayward, CA 94541
www.Hayward-CA.gov

Cover Memo

File #: LB 16-070, **Version:** 1

DATE: June 14, 2016
TO: Mayor and Council
FROM: City Manager

SUBJECT

Request for Approval to Petition LAFCo for the Dissolution of the Eden Township Healthcare District

RECOMMENDATION

That Council approves the attached Resolution authorizing the City Manager to make application to the Local Agency Formation Commission (LAFCo) asking the Commission to consider the question of the possible dissolution of the Eden Township Healthcare District

SUMMARY

The Eden Township Healthcare District (ETHD) was formed by the voters in 1948 under the State's Local Healthcare District Act. Their purpose was to build and operate Eden Hospital in Castro Valley: the hospital opened its doors for the first time in 1954. The District owned and operated the hospital until 1986, when it acquired Laurel Grove Hospital and the two hospitals were integrated to create Eden Medical Center (EMC). ETHD no longer operates any hospital or other direct-service facility. It has not levied taxes since 1977. Their only source of revenue is from lease/rental income from owned office buildings. Their offices are located at 20400 Lake Chabot Road, Suite 104 in Castro Valley.

In 1998, ETHD transferred substantially all of the net operating assets and operations of Eden Hospital to Sutter Health, a California nonprofit corporation. The relationship did not progress well and resulted in a lawsuit by EMC against Sutter, which they eventually lost resulting in a \$19,673,353 judgement against EMC, including damages claim, court costs, fees, and pre-judgement interest.

In recent years, ETHD has made some annual grants to non-profit agencies in the District involved in or supporting healthcare, including hospitals. The grants were funded by revenue from lease/rent income from office buildings owned by the District. A question has arisen by jurisdictions within the ETHD as to whether or not the District continued to have a viable purpose as a Special District, with a separate administration and an elected Board of Directors; and there is disagreement. This report presents a transparent and inclusive way to have a conversation to discuss and resolve the question in a formal setting.

BACKGROUND (Taken in large part from the [December 9, 2013 LAFO Service Review Report <http://www.acgov.org/lafco/documents/finalmsr2013/eden-final.pdf>](http://www.acgov.org/lafco/documents/finalmsr2013/eden-final.pdf).)

District History and Characteristics

The Eden Township Healthcare District (ETHD) was formed by the voters in 1948 to build and operate Eden Hospital in Castro Valley: the hospital opened its doors for the first time in 1954. Their offices are located at 20400 Lake Chabot Road, Suite 104 in Castro Valley. ETHD was formed as an independent special district under the State's Local Healthcare District Act. The principal act empowers healthcare districts to levy taxes and provide an array of services relating to the protection of residents' health and lives.

The District was formed pre-LAFCo in 1948. There have been several actions taken by LAFCo including the detachment of a few parcels from the District in the early 1970s. ETHD boundary area encompasses 130.6 square miles and includes the City of San Leandro, most of the City of Hayward, and a large portion of Unincorporated Alameda County. (See Attachment I for a boundary map.) The District is governed by a five-member board of directors elected to four-year terms. The Board meets monthly on the third Wednesday of each month at 5:30 in the afternoon in the District conference room located at the Eden Medical Building.

As noted above, ETHD was originally formed to finance, construct, and operate Eden Hospital. The District owned and operated the hospital until 1986, when it acquired Laurel Grove Hospital and the two hospitals were integrated to create Eden Medical Center (EMC).

In 1994, in response to the damage caused by the Northridge earthquake, the legislature passed SB 1953, a seismic safety law that required hospitals to meet stricter seismic safety standards. An estimated retrofit cost of \$200-300 million resulted in ETHD's decision to affiliate with a larger partner to finance the replacement facility, and in 1998, ETHD transferred substantially all of the net operating assets and operations of the hospital to Sutter Health, a California nonprofit corporation. The eleven-member board overseeing EMC consisted of the District's five elected board members, five community members appointed by Sutter Health, and the Hospital's Chief Executive Officer.

In 2004, ETHD purchased San Leandro Hospital and leased it to Sutter Health. The lease agreement required Sutter Health to replace Eden Medical Center or pay ETHD \$260 million to replace it. In 2006, Sutter Health informed ETHD that the cost of the replacement hospital had exceeded \$400 million and it was no longer justifiable. ETHD and Sutter Health entered lengthy negotiations. Part of the negotiated agreement was the District's agreement to relinquish its place on the EMC board six months after the replacement hospital construction commenced. The replacement hospital would be constructed entirely at Sutter Health's expense, not to exceed \$300 million. Another part of the agreement was that Sutter Health obtained an option to buy San Leandro Hospital.

The construction of the replacement hospital began in July 2009 and the District's board members resigned from the EMC's board in January 2010. In the fall of 2009, Sutter Health exercised its option to purchase San Leandro Hospital. ETHD, fearing that Sutter Health intended to close San Leandro Hospital, did not consent to the transfer of ownership. Sutter Health sued in court, which resulted in trial judgment

against ETHD. ETHD appealed and lost in the California Court of Appeals. The District's final attempt to stop the sale of San Leandro Hospital to Sutter Health was its appeal to the Supreme Court of California. The Supreme Court refused to hear the case.

Currently, ETHD does not operate any hospital nor is it affiliated with EMC. The District administers a community grant fund. Grant funds are distributed to nonprofits and government agencies providing healthcare, food, legal service, and other support services to low-income people in the District's service area. Members of the Board carefully evaluate every application and make their grant selections twice annually in open session during their scheduled Board meeting. It has been claimed by ETHD Board Members that the San Leandro Hospital/Sutter action cost the District \$50 million -- \$30 million to San Leandro Hospital and Legal Fees and \$20 million to Sutter as an outcome of the lawsuit filed by the District.

In its current format, the District does not operate any medical/hospital facilities. Rather, it distributes grant funds to community organizations for activities related to the health and wellbeing of residents within the District's boundaries. ETHD has given grants to over sixty organizations over the last fourteen years (as of 2013) for a total of more than \$8.6 million to promote the health of the community. (NOTE: Due to legal fees, ETHD suspended grant giving in FY 10-11. It did not have enough financial capacity to provide grants to community organizations. Grant making resumed in FY 11-12.)

ETHD owns a medical office building, the Dublin Gateway Center, located outside of its boundaries in the City of Dublin in which ETHD leases space to doctors and medical clinics. The District also owns two other medical office buildings within its bounds, San Leandro Medical Arts Building and Eden Medical Building, which are rented out to healthcare providers who serve district residents and non-residents alike. Eden medical Building also houses the Districts administrative headquarters.

ETHD's Sphere of Influence (SOI) was established in 1984 as coterminous with its boundaries. Districts must apply and obtain LAFCo approval to exercise services authorized by the principal act but not already provided (i.e., latent powers) by the district at the end of 2000. During the 2004 SOI updates, LAFCO reaffirmed the coterminous SOI, since no reorganizations or changes in service area were proposed by the District at that time.

As of 2010, the population of the area in ETHD was 360,113. Its population density-2,757 residents per square mile-is significantly higher than the countywide density of 1,840 people per square mile. Based on Association of Bay Area Governments (ABAG) growth projections and ETHD's estimated 2010 Census population, the population of the area within the District is anticipated to reach 437,897 by 2035.

Overall View of District Finances

In FY 10-11, ETHD's revenues totaled \$4.4 million, which consisted of operating (83%) and non-operating (17%) revenue sources. A majority of the operating revenue came from rental income. Non-operating revenue included interest income and change in fair value of investments. ETHD no longer receives any property taxes, special taxes, or benefit assessments. The last year they levied any taxes was FY 1977.

At the end of FY 10-11, the rental properties generating income included San Leandro Medical Arts Building (acquired in July 2004), Lake Chabot Road Building (acquired in October 2004, but subsequently replaced by a newly constructed Eden Medical Building in 2012), and Dublin Gateway Center (acquired in

June 2007). Revenues for FY 11-12 and FY 12-13 were \$4.1 million and \$5 million respectively. The District's revenues in FY 12-13 increased due to increase in rental income.

In FY 10-11, ETHD investment in capital assets totaled \$94,774,617. At the end of FY 12-13, ETHD's total unrestricted net assets amounted to \$10 million, which constituted about eighteen months of operating expenditures. As of November 2nd, 2013, occupancy rates in the rental properties were: Dublin Gateway Center-72%, San Leandro Medical Arts Center-89%, and Eden Medical Building-60%. Eden Medical Building's occupancy rate has increased as two new leases went into effect on the third floor nearly filling that floor.

In FY 10-11, ETHD's expenses exceeded revenues by over \$5 million. The operating loss was \$4.4 million. In FY 12-13, the operating loss was \$2.3 million, while overall expenses exceeded revenues by \$3.5 million. At the end of FY 14-15, ETHD's total unrestricted net assets amounted to \$10.5 million; and revenue of \$6.7 million including \$637,964 one-time revenue from the sale of a partnership interest. The District's total liabilities at year-end as reflected in the recent audit are \$63.2 million dollars. Their balance sheet reflects a continued annual loss of around \$1 million dollars, not including accounting measures to reclassify assets from "Non-current" to "Current" based on due dates of applicable loans.

As a result of the law suit with Sutter, the District owes Sutter \$19,673,353 on the damages claim, court costs, fees, and pre-judgment interest. This is to be paid to Sutter along with annual interest payments on January 1, of each year, with the first installment having been paid on June 30, 2015. This payment was one tenth of the amount owed (\$1,967,335) plus interest from January 8, 2014 to December 31, 2014. The remaining balance is due as of June 30, 2015 is \$17,706,018, which is expected to be paid off over the course of ten years.

DISCUSSION

So, what is the current issue? There is a question in the communities served by the District, particularly Unincorporated Alameda County, San Leandro, and Hayward, about the continued existence of the District since they no longer have a hospital and no longer collect taxes. Their primary function appears to be as property owners/landlords and irregular grantors to hospitals and non-profit entities throughout the District. (See Attachment II for a historical representative sample of grantees.) The question has been posed as to the future of the District: Should it continue? If it should, what is the role of the District into the future? Should it be dissolved and its assets managed by a Successor Agency or sold with any remaining cash after resolution of liabilities distributed to others? And, if it should be dissolved, what is the proper mechanism for deciding and accomplishing that?

The following alternatives may exist as avenues to further explore options and/or to take steps in one direction or the other. Certainly, they are alternatives being discussed within ETHD and by others outside of the District.

- A. Self-Decision: There is controversy as to whether or not the District could or should decide its future on its own. What is clear is that the District has expressed a desire to continue in existence and is not planning on dissolving. There are other Healthcare Districts in California that also do not have a hospital in their purview but which continue to exist, and which may or may not continue collecting taxes. ETHD states that they serve a role in maintaining the community healthcare safety net through grants to hospitals (Alameda Healthcare System including San

Leandro Hospital and St. Rose); and to non-profit agencies. (See Attachment II for a historical representative sample of grantees.)

- B. State Legislation: Two pieces of legislation have recently been introduced to move the dissolution of the District along - [AB 72 <http://leginfo.legislature.ca.gov/faces/billNavClient.xhtml?bill_id=201520160AB72>](http://leginfo.legislature.ca.gov/faces/billNavClient.xhtml?bill_id=201520160AB72) (Bonta) and [AB 2471 <http://leginfo.legislature.ca.gov/faces/billNavClient.xhtml?bill_id=201520160AB2471>](http://leginfo.legislature.ca.gov/faces/billNavClient.xhtml?bill_id=201520160AB2471) (Quirk). The later appears to be in a better position to move forward. The disadvantage of approaching the problem legislatively is that this method lacks community conversation and by-passes the very agency charged with reviewing these exact situations - the Local Area Formation Commission (LAFCo). Legislation may have a role in the process should the community decision be made to dissolve the District, but it appears premature at this point.
- C. LAFCo: LAFCo is a state mandated local agency that oversees boundary changes to cities and special districts, the formation of new agencies including incorporation of new cities, and the consolidation of existing agencies. The broad goals of the agency are to ensure the orderly formation of local government agencies, to preserve agricultural and open space lands, and to discourage urban sprawl. More extensive information on the role of LAFCos in California can be found [here <https://www.acgov.org/lafco/documents/50_Years_of_LAFCos.pdf>](https://www.acgov.org/lafco/documents/50_Years_of_LAFCos.pdf).

LAFCos regulate, through approval or denial, the boundary changes proposed by other public agencies or individuals. LAFCos do not have the power to initiate boundary changes on their own, except for proposals involving the dissolution, merging, or consolidation of special districts.

One of the most important charges given to LAFCos was the adoption of "Spheres of Influence" for local governments (1972). A "Sphere of Influence" (SoI) is the physical boundary and service area that a local governmental agency is expected to serve in the future. Establishment of this boundary is necessary to determine which governmental agencies can provide services in the most efficient way to the people and property in any given area. The Sphere of Influence requirement also works to discourage urban sprawl by preventing overlapping jurisdictions and duplication of services. Commissions cannot tell counties or cities what their planning goals should be. Rather, LAFCos coordinate the orderly development of a community through reconciling differences between city and county plans so the most efficient urban service arrangements are created for the benefit of area residents and property owners.

Through special studies, LAFCos encourage governments to evaluate their current operations and options for reorganization. Local agencies often overlap and have the potential of duplicating services. LAFCos conduct service studies and consolidation feasibility studies. These studies provide general information about local governments and present alternatives for improving services and reducing operational cost.

As of July 1, 1994, LAFCos have the authority to initiate proposals that include the dissolution or consolidation of special districts, the merging of an existing district or establishment of subsidiary

districts. Prior to initiating such an action, LAFCo must determine that the district's customers would benefit from the proposal through adoption of a Sphere of Influence or other special study. Cities and districts are required to obtain LAFCo's approval prior to entering into contracts with private individuals or organizations to provide services outside of the agencies boundaries.

Alameda County LAFCo <<https://www.acgov.org/lafco/>> has taken up the issues around ETHD several times in the past, the most recent being a complete [Municipal Services Review](https://www.acgov.org/lafco/documents/finalmsr2013/eden-final.pdf) <<https://www.acgov.org/lafco/documents/finalmsr2013/eden-final.pdf>> (MSR) and [Sol Resolution](https://www.acgov.org/lafco/documents/ETHD.11.13.14update.pdf) <<https://www.acgov.org/lafco/documents/ETHD.11.13.14update.pdf>> in 2013, an update of it in 2014, and informal conversations over the last few months, with the last being on [May 6, 2016](http://www.acgov.org/lafco/documents/supporting_docs/supporting_docs/Item_6_AB_2471.pdf) <[http://www.acgov.org/lafco/documents/supporting_docs/supporting_docs/Item 6 AB 2471.pdf](http://www.acgov.org/lafco/documents/supporting_docs/supporting_docs/Item_6_AB_2471.pdf)> . Although each time, LAFCo has reaffirmed the District's existence, the Commission members are prepared to take up the issues again more formally if such an application to do so is presented to them.

- D. Voter Action: Obviously, the District was originally formed by the voters. The current ETHD [Board](http://ethd.org/about/board-members/) <<http://ethd.org/about/board-members/>>, as represented by Mr. Dev Mahadevan, Chief Executive Officer, holds the position that because the District was created by the voters, only the voters can dissolve the District. Even if a majority of the interested parties concurred in this perspective, it is unlikely that the District itself would initiate such an action; as this involves a full electoral process and the District does not concur that they should be dissolved.

The “interested parties” of Alameda County and the cities of San Leandro and Hayward may not totally agree on the future of ETHD, its current purpose, or the eventual dispersal of any assets, but they do share the perspective that the matter should receive a full public discussion. Of the alternatives identified above, having the matter formally heard before LAFCo appears to be the best and most transparent alternative. In order to activate that process, a formal application needs to be made to the Commission. As one of the largest member jurisdictions of the District, Hayward is being looked to as a leader in submitting that application. As such, Council is being asked to authorize the City Manager to initiate the application process.

It is important to note that the intention in initiating the LAFCo process is to assure that the future of EHTD gets a full and complete public airing and that there is an opportunity for all stakeholders to voice an opinion or perspective. It is not the intent of this application for Hayward to take a position at this time on the continuation/dissolution of the District or on the management of their assets should dissolution occur. In addition, partnering with other jurisdictions in staff effort and associated costs may be possible, including co-applying to LAFCo. However, that will have to be more fully explored as staff prepares and files the LAFCo application.

FISCAL IMPACT

There is a potential fiscal impact to this process, which although potentially shared among the above three named jurisdictions, will likely be “fronted” by the City of Hayward. The fee to LAFCo simply to submit the application is \$5,000. The process for the full public hearing process is much like that of a

Proposition 218 hearing:

1. Application is received
2. Notice is given to interested parties. (Per the 2010 census, there are approximately 175,000 voters in the District and 153,000 households. These are estimates and need to be verified.)
3. An opportunity exists in the process for a majority protest to terminate the action.
4. If the threshold is met for a majority protest (25% of the voters or 25% of landowners who own at least 25% of the assessed land value in the District), an election must be held. (Based on the above numbers, 25% of voters equals approximately 43,750 voters.)
5. If an election is to be held, notice and ballots will need to be made and distributed.
6. Votes will have to be counted.

Clearly, there is a cost to the LAFCo review and to the response to a possible successful protest. The exact cost is dependent on the actual number of households and voters and on the type of election/ballot process used.

NEXT STEPS

If Council authorizes the City Manager to make the LAFCo application, the application will be completed and filed by the end of June. LAFCo requires a thirty-day review period before setting the matter for hearing. Once it is scheduled for an agenda, there is a twenty-one day "Notice of Hearing" period; and then hearings are held as needed for the Commission members to fully hear all parties on an issue and to reach a conclusion. After adopting a resolution that takes a specific action, there is a thirty-day "reconsideration" period before the protest hearing can be held. Depending on the results of the protest hearing, LAFCo will order the dissolution, order the dissolution subject to election, or terminate the proceedings.

LAFCo meets the second Thursday on odd months, with their next regularly scheduled meeting being July 14, 2016. However, as mentioned above, LAFCo has readily agreed to meet more frequently in order to expedite the hearing of this topic.

Of note related specifically to the dissolution of a healthcare district: LAFCo is required to send notice of receipt of an application to dissolve a healthcare district to the various state agencies that have oversight or regulatory responsibility over healthcare districts including the State Department of Health Care Services, including the Medi-Cal division, the Office of Statewide Health Planning and Development, including the Cal-Mortgage Loan Insurance Division, the California Health Facilities Financing Authority, and the State Department of Public Health, including the Licensing and Certification Division. The state agencies have sixty days to comment on the proposal, which may add time to the above timeline. (See [government code section 56131.5 <http://leginfo.legislature.ca.gov/faces/codes_displaySection.xhtml?lawCode=GOV§ionNum=56131.5>](http://leginfo.legislature.ca.gov/faces/codes_displaySection.xhtml?lawCode=GOV§ionNum=56131.5).)

Approved by:



Fran David, City Manager

Attachments:

Attachment I	ETHD Map
Attachment II	ETHD Service Review

Cc: Dev Mahadevan, Chief Executive Officer, ETHD/EMC
Mona Palacios, Executive Officer, LAFCo
Wilma Chan, Supervisor, Alameda County
Pauline Cutter, Mayor, San Leandro