

Date of Hearing: January 19, 2022

ASSEMBLY COMMITTEE ON LOCAL GOVERNMENT

Cecilia Aguiar-Curry, Chair

SB 418 (Laird) – As Amended January 14, 2022

SENATE VOTE: 39-0

SUBJECT: Pajaro Valley Health Care District.

SUMMARY: Creates the Pajaro Valley Health Care District. Specifically, **this bill:**

- 1) Specifies that a local hospital district designated as the Pajaro Valley Health Care District (PVHCD) is hereby formed within the counties of Santa Cruz and Monterey. The District may be organized, incorporated, and managed as provided pursuant to existing health care district law, and may exercise the powers granted or necessary, only if the relevant county board of supervisors chooses to appoint an initial Board of Directors, as specified.
- 2) Defines the territory of the PVHCD.
- 3) Specifies that following the formation of the PVHCD, Local Agency Formation Commission (LAFCO) Law governs any change of organization.
- 4) Requires that within five years of the date of the first meeting of the Board of Directors of the PVHCD, the Board of Directors shall adopt a resolution to divide the PVHCD into zones and number the zones consecutively.
- 5) Specifies that in establishing these zones, the Board of Directors shall provide for representation in accordance with demographic and geographic factors of the entire area of the PVHCD, including population factors.
- 6) Provides that the Board of Directors shall fix the time and place for a hearing on the proposed establishment of zones, and at this hearing, any elector of the PVHCD may present their views and plans in relation to the proposed zoning, but the Board of Directors shall not be bound thereby and their decision, in the resolution, shall be final.
- 7) Requires the zones to be effective for the next PVHCD election after the resolution of the Board of Directors for which there is time to implement the zones and elections within the zones.
- 8) Contains an urgency clause.
- 9) Contains numerous findings and declarations to support its purposes.

EXISTING LAW:

- 1) Provides for local healthcare districts, which govern certain health care facilities and services. Each healthcare district has specific duties and powers respecting the creation, administration, and maintenance of the healthcare district, including the authority to purchase, receive, take, hold, lease, use, and enjoy property of every kind and description within and without the boundaries of the healthcare district.

- 2) Requires the board of directors of healthcare districts to do all of the following:
 - a) Adopt an annual budget in a public meeting, on or before September 1 of each year, that conforms to generally accepted accounting and budgeting procedures for special districts;
 - b) Establish and maintain an Internet Web site that lists contact information for the district. The Internet Web site may also list any of the following:
 - i) The district's adopted budget;
 - ii) A list of the district's current board members;
 - iii) Information regarding public meetings required pursuant to the Local Health Care District Law or the Ralph M. Brown Act (Brown Act);
 - iv) A municipal service review (MSR) or special study conducted by a LAFCO pursuant to the Cortese-Knox-Hertzberg Local Government Reorganization Act of 2000 (CKH Act), if any;
 - v) Recipients of grant funding or assistance provided by the district, if any;
 - vi) Audits of the district's accounts and records prepared pursuant to existing law;
 - vii) Annual financial reports to the Controller, submitted pursuant to existing law; and,
 - viii) Any other information the board deems relevant.
- 3) Requires healthcare districts to adopt annual policies for providing assistance or grant funding, if the district provides assistance or grants, which must include the following:
 - a) A nexus between the allocation of assistance and grant funding with health care and the mission of the district; and,
 - b) A process for the district to ensure allocated grant funding is spent consistently with the grant application and the mission and purpose of the district;
 - a) Requirements that a grant recipient must meet, such as contract terms and conditions, fiscal and programmatic monitoring by the district, and reporting to the district;
 - b) The district's plan for distributing grant funds for each fiscal year;
 - c) A process for providing, accepting, and reviewing grant applications;
 - d) A prohibition against individual meetings regarding grant applications between grant applicants and board members, officers or staff outside the district's grant award process, although this process may include the provision of technical assistance to grant applicants, upon request, by district program staff; and,

- e) Beginning January 1, 2020, guidelines for additional elements, such as awarding grants to underserved individuals and communities, evaluating the financial need of applicants, considering eligibility for the types of programs eligible for funding, and other grant policy guidelines.

FISCAL EFFECT: None.

COMMENTS:

- 1) **Bills Summary and Author's Statement.** This bill creates the PVHCD to provide services within Santa Cruz and Monterey Counties. This bill also establishes the territory of the PVHCD, specifies the powers and duties of the PVHCD, and requires that any future changes of organization to the PVHCD are subject to LAFCO Law. Lastly, this bill requires the PVHCD be divided into zones for the purposes of electing the Board of Directors. This bill is sponsored by the Pajaro Valley Healthcare District Project.

According to the author, "The Watsonville Community Hospital located in Santa Cruz County is an essential health care provider in the region, serving primarily low-income, under- and uninsured populations of color, and has proved crucial in helping those impacted by COVID-19 throughout the pandemic. Last year, the current owner/operator of the Watsonville Community Hospital announced its intention to file for Chapter 11 bankruptcy protection in early December and close the hospital in January. While the creditor has deferred closure through March 2022, immediate action is required to ensure the vital services and jobs that support the health care safety net remain in Watsonville.

"In response to the potential closure, a new not-for-profit organization, Pajaro Valley Healthcare District Project (PVHDP), was created by the County of Santa Cruz, the City of Watsonville, Salud Para La Gente, and the Community Health Trust of the Pajaro Valley, to form a new California healthcare district. The goal of Senate Bill 418 is to create the urgently needed hospital district to ensure the Watsonville Community Hospital remains open. The PVHDP has the first opportunity to acquire the hospital, and this bill will help local partners raise the necessary funds. Without SB 418, local partners face an uphill battle to save the hospital from closure."

- 2) **Background.** Near the end of World War II, California faced a severe shortage of hospital beds. To respond to the inadequacy of acute care services in rural areas, the Legislature enacted the Local Hospital District Law, to provide medically underserved areas without access to hospital facilities a source of tax dollars that could be used to construct and operate community hospitals. SB 1169 (Maddy, 1994) changed the name of the principal act to "The Local Healthcare District Law" to better reflect the shift in the provision of healthcare services outside hospital settings.

The powers and duties granted to healthcare districts under existing law have remained largely unchanged while the demographics of areas being served by the districts, access and provision of healthcare services, and the districts themselves have vastly changed. For example, following the change in law in 1994, 14 healthcare districts have filed for bankruptcy, and over one-third of the healthcare districts in California have either closed or sold their hospital.

State law allows healthcare districts to exercise various powers, including to lease or own property; build and operate healthcare facilities and services, including emergency services, free clinics, diagnostic and testing centers, health education programs, wellness and prevention programs, rehabilitation, and aftercare; to provide assistance to other entities to carry out those services; and to sell their assets.

Healthcare districts, like other special districts, are subject to review in a municipal service review or special study by a LAFCO to examine the efficiency and effectiveness of the services they provide. Similarly, healthcare districts must also receive approval from LAFCO to exercise its powers or change its boundaries.

Most healthcare districts receive a share of local property taxes; some levy special parcel taxes, and some charge for services. Some healthcare districts generate revenues from district resources, such as property lease income; and some districts receive grants from public and private sources.

- 3) **Watsonville Community Hospital (WCH).** This bill contains a number of findings and declarations detailing the hospital and the surrounding community, including:
“WCH is a 106-bed hospital located in the Pajaro Valley, which straddles southern County of Santa Cruz and northern County of Monterey on California’s central coast. The hospital provides important acute care and emergency services in a culturally diverse community where the nearest alternative hospital can be up to an hour away during regularly congested commutes.

“WCH employs 620 people and has a medical staff of over 200 physicians. It provides a range of quality medical services, including pediatrics, obstetrics and gynecology, internal medicine, family medicine, anesthesiology, wound care, gastroenterology, orthopedics, cardiovascular disease, dermatology, and more. In 2020, the hospital delivered more babies than any other hospital in the County of Santa Cruz. Serving a significant immigrant population, the hospital provides care to those without English language proficiency in their preferred language.

“The community of Watsonville has historically faced many health and economic disparities. The pandemic has resulted in the loss of employment and school closures, and has caused nonessential workers and at-risk populations to stay home. Overcrowded and substandard housing conditions, food insecurity, lack of transportation, and the high cost of housing have intensified disparities overnight. The Pajaro Valley saw dramatic and disproportionate rates of COVID-19 infections, hospitalizations, and death as compared to the rest of the County of Santa Cruz.

“Over the last 21 years of for-profit ownership, WCH administration has changed 20 times. Due to this history, partners of the Pajaro Valley Healthcare District Project all believe community ownership will provide more consistent management, oversight, and stability for the patients, staff, and community. Public ownership through a local hospital district also creates financing and funding opportunities not otherwise available to a for-profit or nonprofit entity.”

- 4) **Ongoing Bankruptcy.** WCH filed voluntary petitions under Chapter 11 of the U.S. Bankruptcy Code on December 5, 2021, as part of a plan to sell the hospital. According to WCH, “WCH has reached a preliminary agreement to sell its operations to a new healthcare district sponsored by the Pajaro Valley Healthcare District Project (PVHDP) to secure the hospital’s future and continue its role as a critical healthcare provider. The PVHDP is a not-for-profit organization created by the County of Santa Cruz, the City of Watsonville, the Community Health Trust of Pajaro Valley and Salud Para La Gente.

“The sale will likely be completed through a Chapter 11 reorganization, which will give the hospital the financial breathing room needed to focus on patient care and operations while the sale is conducted. As part of the Chapter 11 process, the hospital intends to file a motion asking the bankruptcy court to approve the PVHDP as the lead buyer or stalking horse bidder and approve the sale of its operations through a court-supervised auction. The hospital plans to ask the court to schedule a hearing to consider the sale in February 2022. The hospital has received sufficient funding to fund its operations and the sale process through the end of March 2022.”

The bankruptcy proceedings continue to move forward. According to court documents, all bids for the hospital must be received no later than February 14. The auction will take place on February 17, and the hearing to approve the sale to the winning bidder will take place before the Court on February 23. As the stalking horse bidder, PVHDP must meet certain benchmarks to be identified as a qualified bidder and to participate in the auction.

- 5) **LAFCO.** The CKH Act creates a LAFCO in each county to control the boundaries of cities, county service areas, and most special districts. The courts repeatedly refer to LAFCOs as the Legislature’s watchdog over boundary changes. To plan for the future boundaries and service areas of the cities and special districts, a LAFCO must adopt a policy document for each city and district called a sphere of influence. The LAFCOs’ boundary decisions must be consistent with the spheres of influence of the affected cities or districts.

Local governments, in almost all cases, can only exercise their powers and provide services where LAFCO allows them to: within their boundaries (which are set by LAFCO), within their spheres of influence but outside their boundaries (with authorization by LAFCO), and outside their spheres to address a major threat to public health if the extension is consistent with LAFCO’s policies. LAFCOs, along with the planning agencies of cities and counties, are supposed to ensure that services are effectively and efficiently delivered to all communities throughout the state.

Controlling boundaries means LAFCOs influence the timing and location of development, because they determine the type of services that are available to support development—and those that are not. The Legislature created LAFCOs to discourage urban sprawl, preserve open space and prime agricultural lands, encourage the orderly formation and development of local agencies, and to ensure the efficient provision of government services. LAFCOs must adopt written policies to further these goals.

- 6) **Policy Considerations.** The Committee may wish to consider the following:
- a) **LAFCO Law.** The dissolution and formation of a special district is often a complex, technical, and political matter. State law makes LAFCOs responsible for encouraging

orderly formation and development of local agencies based on local conditions and circumstances. The local officials who sit on the local LAFCO are typically in the best position to evaluate the local conditions and circumstances that should determine the services provided by a new healthcare district.

Additionally, the LAFCO process generally requires an analysis of the cost of initiating and maintaining the services to be provided by a newly formed special district. This analysis, known as a feasibility analysis or feasibility study, includes an estimate of the operations and administrative costs as well as the identification of proposed funding mechanisms for meeting those costs. Typically, the feasibility analysis would need to review the nature, location, and extent of any functions or classes of services to be provided. That could include a review of available and needed facilities and the capacity of existing facilities. The analysis also reviews revenue sources and expected costs to provide services.

Lastly, the local formation process allows for robust public engagement, sometimes including an election, generally allowing the residents that will be effected by the formation of a new special district to weigh-in multiple times within the particular community. Circumventing the existing requirements limits local public participation. Given these factors, the Committee may wish to consider if bypassing the local process is prudent or if the exigent circumstances that the community is facing warrant this measure.

- b) **Funding and Long-Term Sustainability.** One of the major factors LAFCOs consider during the formation of a special district is its potential long-term fiscal sustainability. This is in order avoid situations where a special district is created without the necessary revenue generation to successfully provide services. If formed, it is unclear how the PVHCD will be funded to achieve long-term sustainability. AB 4227 (Hauser), Chapter 375, Statutes of 1986, created the Coast Life Support District to provide emergency medical services, including emergency ambulance and life support services, to areas within Sonoma and Mendocino Counties. AB 4227 required the Sonoma and Mendocino County Boards of Supervisors to, on behalf of the Coast Life Support district, present to the voters of the district a measure imposing a special tax to be used by the district to provide services. However, this bill does not contain a similar provision that would ensure PVHCD has a consistent, long-term revenue source. Due to the uncertainty of the funding, it is unclear if the PVHCD will be able to successfully provide hospital services. The Committee may wish to consider the cost of providing such services and if the revenue needed to providing them long-term is sufficient.
- c) **Best Option?** Another determination LAFCOs must make is whether existing agencies can feasibly provide the needed services in a more efficient and accountable manner. LAFCOs must also consider a reorganization with other single-purpose agencies that provide related services. Creating a new health care district is not the only option for a public agency to acquire WCH and provide hospital services. Santa Cruz County and the adjacent Salinas Valley Memorial Healthcare System, a public healthcare district, are agencies also able to acquire WCH and provide hospital services. Without the typical LAFCO review, it is unclear if PVHCD is best suited to provide these services. The Committee may wish to consider if creating PVHCD is necessary or if a more suitable public agency already exists.

- d) **Recent Scrutiny and Precedent.** Healthcare districts as a class have been subject to significant scrutiny over the years, in part because so many no longer perform the responsibilities for which they were originally formed. A review by the Assembly Local Government Committee in 2017 found that of the 79 healthcare districts in existence at the time, many of them provide no direct healthcare services at all and instead only provide grants to other organizations. These districts are sometimes accused of being highly-compensated middlemen that incur unnecessary administrative costs.

Also in 2017, the state's Little Hoover Commission issued a report examining whether California taxpayers are well-served by special districts generally, and whether consolidation or dissolution of some special districts would improve local government operations and efficiency. The Commission also specifically examined healthcare districts because of the Legislature's recent interest in the subject. The Commission found that many rural healthcare districts continue to fulfill their intended mission of providing medical services to underserved areas. The Commission also found that in areas that have urbanized, healthcare districts often have changed roles. In some cases, these districts provide preventative care services that meet local needs, but in others, the Commission argued that LAFCOs could do more to assess whether every healthcare district should continue to operate.

This bill provides no guarantee that, if created, the PVHCD will be the ultimate purchaser of the WCH or that the PVHCD will not sell the hospital in the future. In light of this, and because this bill bypasses LAFCO law and foregoes LAFCO review, should the PVHCD continue to exist without providing direct hospital services? The Committee may wish to consider what happens to the District if it no longer provides direct hospital services.

- 7) **Committee Amendments.** In response to the policy considerations, the Committee may wish to consider the following amendments:

32498.7. (a) The district shall notify the Santa Cruz County local agency formation commission when the district, or any other entity, acquires the Watsonville Community Hospital.

(b) If the district does not acquire the Watsonville Community Hospital through the bankruptcy proceeding pursuant to Chapter 11 of Title 11 of the United States Code by January 1, 2024, the commission shall order the dissolution of the district.

32498.8. (a) The district shall notify the Santa Cruz County local agency formation commission if the district sells the Watsonville Community Hospital to another entity or stops providing health care services at the facility.

(b) If the commission receives notification subject to subdivision (a), it shall order the dissolution of the district.

(c) The dissolution of the district pursuant to this section shall not be subject to any of the following:

(1) Chapter 1 (commencing with Section 57000) to Chapter 7 (commencing with Section 57176), inclusive, of Part 4.

(2) Determinations pursuant to subdivision (b) of Section 56881.

(3) Requirements for commission-initiated changes of organization described in paragraph (3) of subdivision (a) of Section 56375.

(4) Sections 99 and 99.01 of the Revenue and Taxation Code.

- 8) **Related Legislation.** AB 912 (Gordon), Chapter 109, Statutes of 2011, created an expedited process for the dissolution of special districts in certain circumstances.

AB 2471 (Quirk) of 2016 would have required the Alameda County LAFCO to order the Eden Township Healthcare District's dissolution if the District met specified criteria. This bill died on the Senate Inactive File.

AB 1728 (Committee on Local Government), Chapter 265, Statutes of 2017, required healthcare districts to adopt an annual budget, adopt a grant funding policy, and establish an Internet Web site.

AB 2019 (Aguiar-Curry), Chapter 257, Statutes of 2018, required set-asides for affordable units when a healthcare district uses design-build to construct housing, required healthcare districts to post additional information online, expanded what healthcare districts must include in their grant policies, and required healthcare districts to notify their LAFCO when a district files for bankruptcy.

SB 522 (Glazer), Chapter 133, Statutes of 2018, dissolved the existing Board of Directors of the West Contra Costa Healthcare District and required the Board of Supervisors of Contra Costa County to either serve as or appoint the district board.

AB 903 (Frazier) of 2021 would have dissolved the Los Medanos Community Healthcare District and designated the County of Contra Costa as the successor agency to the district. This bill failed passage in the Senate Governance and Finance Committee.

- 9) **Arguments in Support.** According to the sponsors, "The hospital has a history of financial challenges under costly private equity ownership and while the community has discussed public ownership for a number of years, late last year the current owner/operator unexpectedly and abruptly announced its intention to (1) file for Chapter 11 bankruptcy protection in early December and (2) close the hospital in January. Required notices were sent to all employees. The Pajaro Valley Healthcare District Project (Project), a local non-profit organization created by the City of Watsonville, the County of Santa Cruz, Salud Para La Gente (a federally qualified health clinic in Watsonville), and the Community Health Trust of Pajaro Valley, immediately began negotiating with the current owner/operator to purchase the hospital in the bankruptcy proceeding. Those negotiations resulted in an asset purchase agreement with the owner/operator, establishing the Project as priority bidder and initiating a process for a yet-to-be -formed California Healthcare District to take over hospital operations. Additionally, the current owner/operator and its largest creditor agreed to defer closure of the hospital through March. The formation of a new healthcare district through legislation is required as a key milestone of the Project's asset purchase agreement filed as part of federal Chapter 11 bankruptcy court process, and must be accomplished prior to bid and auction dates scheduled for February, 2022.

"SB 418 lays out the boundaries of the district, makes clear that the new district will be subject to the oversight of the Santa Cruz and Monterey County Local Agency Formation Commissions (LAFCOs), and directs the initial District Board of Directors to establish zones for the eventual election of future Directors. Additionally, the new Pajaro Valley Healthcare District would be subject to all of the requirements and authorities of other California healthcare districts, as contained in Health and Safety Code Section 32000.

“The urgent formation of the Healthcare District, as outlined in SB 418, is necessary to ensure that the asset purchase agreement negotiated between the Project and the current owner/operator is achieved, thereby ensuring that the hospital remains open and is under the stewardship of a public entity.”

10) **Arguments in Opposition.** None on file.

REGISTERED SUPPORT / OPPOSITION:

Support

Pajaro Valley Healthcare District Project [SPONSOR]
Association of California Healthcare Districts
California Hospital Association
California Medical Association
California Special Districts Association
Casa of Santa Cruz
Catholic Charities Dioceses of Monterey
Central California Alliance for Health
Community Action Board of Santa Cruz County
Community Bridges
City of Watsonville
County of Monterey
County of Santa Cruz
Dientes Community Dental
Digital Nest
District Hospital Leadership Forum
Encompass Community Services
Granite Rock Company
Health Improvement Partnership of Santa Cruz
Hospice of Santa Cruz County
Monarch Services
Pajaro Valley Prevention and Student Assistance, Inc.
Pajaro Valley Unified School District
Salud Para La Gente
Santa Cruz Community Health Centers
Santa Cruz Community Ventures
Santa Cruz County Office of Education
Second Harvest Food Bank Santa Cruz County
Sutter Health
Watsonville Law Center

Opposition

None on file

Analysis Prepared by: Jimmy MacDonald / L. GOV. / (916) 319-3958