

Holland & Knight

560 Mission Street, Suite 1900 | San Francisco, CA 94105 | T 415.743.6900 | F 415.743.6910
Holland & Knight LLP | www.hklaw.com

John Kern
+1 415-743-6918
John.Kern@hklaw.com

May 31, 2024

Via First Class Mail

Georgine Tomasi
President
Escondido Democratic Club
PO Box 301105
Escondido, CA 92030

Re: Palomar Health's Clarifications to Letter Disseminated by the Escondido
Democratic Club

Dear Ms. Tomasi:

Recently the Escondido Democratic Club (“EDC”) made several statements regarding Palomar Health’s decision to enter into a contract with Mesa Rock. EDC’s statements suggest that it is working off of bad information. In the spirit of transparency and clarification, Palomar Health would like to share some important facts with you and set the record straight. As you will read below, this letter includes our specific, point-by-point response and refutation to the incorrect information the EDC has published. ***We also write to ask that you agree to sit down and meet with us to discuss the issues.*** I am available to travel to meet with you and any other members of the EDC at your earliest convenience. I would like to have an open discussion about the issues and answer any questions you have. This is Democrat-on-Democrat fighting that hurts all of us. We would like to speak with you and other members of your Executive Team urgently, if possible, before the EDC’s misinformation becomes good peoples’ mistaken “reality.”

Background Facts

First, although it is not really the central point here, it should be noted the vast majority of Palomar’s publicly-elected Board of Directors, its Executive Team, and its outside legal counsel, ***are registered members of the Democratic Party.*** We raise this point to emphasize this letter is not intended as an attack on the Democratic Party. More importantly, we raise this point to underscore that the decision of the Palomar Health Board to enter into a contract for services with Mesa Rock was not political at all—it was a decision born of necessity and designed to

strengthen Palomar Health financially, so that it can remain a public hospital and primary care provider open for *all* in the community.

Before we address each point raised in the EDC's letter, here are some important background facts about the transaction at issue:

1. What is the MSA with Mesa Rock Healthcare Management?

On February 29, 2024, the Palomar Health Board of Directors voted 5-2 to approve a Management Services Agreement (MSA) between Mesa Rock Healthcare Management and Palomar Health. Mesa Rock, a non-profit organization, will be empowered to conduct business for the benefit of Palomar Health, including by entering into new joint affiliation and investment relationships with, among others, regional health systems, which affiliations will strengthen and stabilize the finances of Palomar Health, expand its capabilities and services, and ensure that Palomar Health can remain a public and independent provider open to all.

2. Why did Palomar seek this MSA type arrangement?

Hospitals across the country, and especially in California, face significant economic pressures. This is even more true for public Health Care Districts like Palomar, which have all the regular concerns of hospitals plus the additional restrictions that come from their status as public bodies. Palomar Health is looking to contract with Mesa Rock Healthcare Management to help operate the District and overcome some of these regulatory hurdles. The proposed Management Services Agreement will provide Palomar the flexibility it needs to continue its public mission into the future.

3. What does the contract for services with Mesa Rock entail?

Mesa Rock will hire Palomar's executive team, ensuring continuity of leadership. The same team will then manage the operations of the District—but without owning any of the assets. Unlike similar transactions in Grossmont or Tri-City, Palomar will not be transferring any of its hospitals or equipment to outside ownership. Palomar's elected Board will retain oversight responsibility over Mesa Rock through, among other things, approving the CEO and controlling the annual budget.

4. Does this mean Palomar is privatizing?

NO, absolutely not. Only the executive team is moving over to operate under the non-profit (Mesa). All other employees, staff, physicians, nurses, etc., will remain employees of the Palomar Health Care District. And, more importantly, Mesa Rock will operate for the benefit of Palomar Health, and under the terms of the MSA will be accountable to and overseen by Palomar Health's publicly-elected Board. This structural change was designed as an alternative

to either privatization or closure—it is designed to save and strengthen Palomar Health as a public institution—NOT to sell it or privatize it or let it decline.

5. Will the MSA and the structural changes impact day-to-day employees, staff, nurses, physicians, or affect union contracts?

No. It will have no impact on these things. 99.99% of Palomar’s staff, employees—including medical and nursing staffs—will not notice any change. The MSA will have no impact on existing union or non-union contracts or employment arrangements.

6. Will the MSA impact medical decisions, credentialing, hospital policies?

No. It will have no impact on these things. All medical decisions, practices, policies, credentialing, etc., remain firmly and squarely within the control of the hospital, respective medical and nursing staffs, and the publicly-elected Board of Palomar Health.

7. When was this idea or agreement proposed?

For 18 months the executive team has been exploring specific, creative options to strengthen Palomar’s finances and compete better against for-profit regional health systems. In November of 2023, the elected Board of Directors at Palomar passed a resolution at an open, noticed session authorizing the Executive Team (including the CEO, COO, Chief Medical Officer, and General Counsel) to explore opportunities for new strategic relationships and/or organizational structures. Specifically, the Board tasked the Executive Team to identify and negotiate possible deals with outside, independent management service organizations (“MSOs,” organized as non-profits). Between November 2023 and February 21, 2024, the Executive Team—in consultation with the Board and the Board’s Strategic and Facilities Planning Committee—evaluated many options. On February 21, 2024, the Executive Team presented to the Board of Directors at another open, public meeting, a proposed service agreement with an MSO called Mesa Rock Healthcare Management. On February 29, 2024, the Palomar Health Board of Directors voted 5-2 at a third open, noticed public meeting to approve a Management Services Agreement (MSA) between Mesa Rock Healthcare Management and Palomar Health.

8. What is the reasoning behind this structural change in leadership?

Changes to the healthcare economy post-pandemic caused financial hardship, privatization, sale, reduction in services, bankruptcy, decline, and mass closures in hospitals across the state—especially for public hospitals like Palomar Health, which are essential providers (open to all) and have large subsidized patient populations (patients on Medi-Cal or otherwise). Palomar’s Board and Executive Team have continuously met and overcome these financial challenges, and have refused to consider privatization or closure like so many other public/community hospitals. But the reality is Palomar Health cannot survive as public institution without new investment and new partnerships and affiliations with other health systems.

The most significant of these prospective investment and affiliation partners simply will not do deals with Palomar, where they fear doing so will subject them to the politics of an ever-changing Board, and the disadvantages that come with having to conduct all hospital business in noticed, open public meetings—with all business records subject to public records act requests (including by competitors, possible litigants). The laws passed after World War 2 which created public health care districts like Palomar—and also created the rules that restrict them—simply did not envision the health care economics of today. Palomar cannot compete with the large for-profit health systems unless it finds new, creative pathways. Through its management agreement with Mesa Rock, Palomar will be able to affiliate with regional healthcare partners and hospitals systems to:

- Drive primary medical care growth and integration;
- Expand medical and surgical oncology care;
- Bring top-quality pediatric care to North San Diego County;
- Stabilize relationships with hospital-based physician groups;
- Expand access to laboratory medicine; and
- Improve Palomar Health’s ability to negotiate rates with health plans.

Palomar Health's Specific Clarifications to Escondido Democratic Club Letter

Now, Palomar Health wishes to respond specifically to each statement in the EDC letter:

Quote from the EDC Letter: *What will this agreement mean for our community?*

• *It finalizes an agreement with a newly created private entity, Mesa Rock Management, for a term of 15 years. It remains unclear who "exactly runs" Mesa Rock, as bylaws have not yet been created. The Attorney for Mesa, William Kushner, claims he works for Eric Friedlander who is connected to Starpoint Health, an ambulatory surgery center in Los Angeles. He resides in Sonoma County and to date no summary of his qualifications has ever been made available to board members or the public.*

Palomar Health's Clarification: Mesa Rock is a non-profit corporation, whose stated mission is solely to increase the public's access to essential healthcare services. Contrary to the statement above, it is exactly clear who runs Mesa Rock, because the agreement between Mesa Rock and Palomar Health requires that the CEO of Mesa Rock be the current CEO of Palomar Health. Accordingly, Diane Hansen, the CEO already selected by the elected Board of Palomar Health, will run Mesa Rock. The Board of Directors of Mesa Rock are charged with ensuring Mesa Rock is meeting the obligations of its contract for services with Palomar Health, and that it is performing its mission of strengthening public access to essential healthcare services. They are not involved in the running of Palomar Health.

Quote from the EDC Letter:

• *It authorizes Mesa Rock Management to appoint its own board of directors (not elected by voters) who will have sole discretion to supervise, hire, and fire top Palomar Health executives (including the CEO) and oversee the day-to-day operations of both hospitals.*

Palomar Health's Clarification: Under California law, as a non-profit corporation, Mesa Rock has the right to appoint its own board members. The Palomar Board retains its oversight of Mesa Rock (a) through control of the budget, (b) through its right to evaluate, consider, and vote on all un-budgeted material transactions Mesa Rock seeks to undertake pursuant to its contract for services with Palomar Health, (c) through its ability to notice breaches of Mesa Rock's duty to act in the best interests of Palomar Health, and, if necessary, (d) through its right to terminate the contract with Mesa Rock (*i.e.*, in the event Mesa Rock does not deliver results to the District) and revert to the historical management structure.

Quote from the EDC Letter:

Why does this matter and why should we care?

- *Palomar Health was created as a public institution using taxpayer money, not as a private corporation.*
- *Palomar Health's 7-member board were voted for by the community through a public election process*
- *Palomar Health 's 7-member board are responsible to the public to be transparent*

Palomar Health's Clarification: Palomar Health is still a public institution. In fact, the driving purpose of the MSA (the contract for services between Mesa Rock and Palomar Health) was the search for a structure to ensure that Palomar could remain public. Palomar Health retains all ownership of all public assets, including all the hospitals, still employs 99.9% of all staff, and still operates for the good of the community. Mesa Rock is contractually and legally charged with assisting Palomar Health in all those things, and Mesa Rock is at all times responsible to Palomar's publicly elected Board to make certain that happens.

Quote from the EDC Letter:

What actions did Griffith, Corrales, Barry, and Greer take to inform public stakeholders of the dire financial situation occurring at Palomar Health District?

- *They elected not to conduct any outreach to educate or receive any feedback from the public*
- *Several of these members of the board actively worked to dispel negative press shared on social media or in person as "rumors."*

Palomar Health's Clarification: Palomar's financial documents were and are open to the public. That has not changed. The rumors Palomar properly combatted were claims that the District was failing, would need to close, or go into bankruptcy. In reality, while hospitals (especially community and public providers) across California, and the country, are facing historic struggles, Palomar Health actually is doing better than most other health care districts in California. This is why Palomar was rejected for financial aid from the State of California, recently, in favor of other district hospitals. This is not to say that Palomar does not face financial challenges. Of course it does. Palomar was open about these challenges and its specific plans to address them. The contract with Mesa Rock is an important component in Palomar Health's plans to meet its financial challenges, because it will open the door for Palomar Health to pursue affiliations and strategic partnerships with other health systems, which partnerships otherwise might be unavailable to a health care district. It is also not correct that Palomar made no attempt to educate. Palomar held two open and noticed sessions in which it went through, paragraph by paragraph, the entire MSA, so it could be completely transparent.

Quote from the EDC Letter:

- They ended the recording of public meetings
- They held the minimum number of required meetings open to the public

- They scheduled the second and final public meeting to consider the agreement with only 24 hours ' notice.

Palomar Health's Clarification: Palomar Health ended its temporary recordings of public meetings (which it had done for the first time during the pandemic because of its switch to zoom meetings) when it again resumed meeting in person in 2023. The decision to cease recording meetings (which, again, was a temporary pandemic practice) had nothing to do with the MSA. ***But anyone who wants to has the right to record a public meeting, so long as they do not disrupt the meeting in doing so.***

Further, there was no required number of public meetings for the MSA. Because the MSA does not involve the transfer any of the assets of Palomar Health, in fact there was no public meeting requirement at all. ***But Palomar Health chose a path of increased transparency and held multiple public meetings anyway.*** It held a public meeting in November 2023, at which the Board authorized the executive team to search for MSA partners. It held a further public meeting to discuss in depth the terms of the MSA. Then, it held a third public meeting discussing those terms again. All of the meetings were open to the public and invited public comment. Palomar Health in each case complied with the 24-hour notice requirements of the Ralph M. Brown Act in setting those meetings.

Quote from the EDC Letter:

- *In June 2023 they voted against a motion to receive more frequent financial reporting (per Voice of San Diego)*

Palomar Health's Response: Palomar's financial documents were and are open to the public. Palomar Health maintains a Finance Committee that meets regularly to review and provide oversight of District finances. ***Quarterly reporting is standard throughout the healthcare industry and the business world*** and balances the need for oversight with the need for the personnel of Palomar to work on District business, not preparing reports. Palomar's Board does not need to do more regularly what its Finance Committee already does.

Quote from the EDC Letter:

- *In February 2024 they voted against a motion to have a second legal opinion (per Union Tribune)*

Palomar Health's Clarification: Palomar Health did not need to spend public funds on yet another legal review because, in reality, the MSA received review, input, and analysis ***by no fewer than four separate and independent legal teams***, and also by Palomar Health's own internal legal team.

Quote from the EDC Letter:

• In March 2024 they voted against a motion to delay the finalization of the agreement to obtain additional public and legal input.

Palomar Health's Clarification: The public had ample opportunity to speak—and did speak—at any of the three noticed and open Board meetings and in response to any of the several news articles discussing the MSA. Palomar heard all public comments, even extending its usual public comment time to make certain everyone who wanted to be heard could be heard. Again, Palomar did not need further delay in a time of financial hardship to obtain an unnecessary sixth legal opinion.

Quote from the EDC Letter:

What are the repercussions of the Griffith, Corrales, Barry, and Greer's votes for our community?

*Mesa Rock will **not** be required to:*

- Hold public meetings*
- Provide regular financial reports to the public*
- Terminate executive management for poor performance*
- Be subject to public records requests including but not limited to
 - o Report to the public on the day-to-day operations of the hospitals*
 - o Provide public access to the reports and documents they create*
 - o Report how the contracted 1 % management fee (potentially \$8 million annually or \$120 million over term of agreement), they will siphon from Palomar Health District for the next 15 years, regardless of whether the district remains financially solvent.*
 - o Account for the millions of dollars in property tax revenue they will receive each year**

Palomar Health's Clarification: In reality, Mesa Rock will not receive any property tax revenues. ***Its 1% management fee may be spent exclusively for either budgeted items approved by Palomar's public-elected Board or put back into the District.*** Mesa Rock will provide quarterly reports to the Palomar Board, which will still hold regular public meetings on District business. In addition Palomar may conduct annual audits of Mesa Rock to ensure proper oversight. Palomar, not Mesa Rock, will own the hospitals and employ the staff, and Palomar will still be subject to the same public records laws to which it has always been subject.

Quote from the EDC Letter:

What reasons did Griffith, Corrales, Barry, and Greer have for voting against Democratic values and exposing Palomar Health to more privatization moves in the future?

(Note: two (2) of the Republican board members, John Clark and Laurie Edwards-Tate, voted against the Mesa Rock Management Agreement)

Reasons:

Money, unfortunately, appears to be a motive and driving force for two of the four Democratic officials to align with management and vote for the Mesa Rock Agreement.

- *Greer received more than \$8 thousand dollars (26% of contributions) for her 2022 reelection campaign from Palomar Health executive management and Palomar Hospital Partners (per Voice of San Diego).*
- *Griffith received nearly \$4 thousand dollars for his 2022 Escondido City Council campaign from various members of Palomar Health executive management, including CEO Diane Hansen, (35% of total contributions - per campaign financial disclosures).*

Palomar Health’s Clarification: The MSA in no way “exposes Palomar to privatization.” The only conditions that could “expose” Palomar to privatization would be (a) a ballot referendum seeking privatization (*i.e.*, a public vote) first authorized and put on the ballot by the Palomar Board (and this Board is unified 7-0 against a privatization referendum), or (b) Palomar Health’s financial collapse or bankruptcy. In fact, the decision to enter into a contract with Mesa Rock is specifically designed to reduce the risk of privatization, because it helps remove some of privatization’s driving forces: limits on public entity investment, rigid and cumbersome meeting restrictions, and inability to guarantee the confidentiality of the trade secrets of strategic partners. Palomar’s MSA aims to be the best of both worlds, ensuring a public hospital remains open to everyone without regard for ability to pay, while still remaining fiscally solvent and competitive in today’s healthcare market.

Quote from the EDC Letter:

How did the Mesa Rock Agreement benefit Diane Hansen and her management staff?

- *CEO Diane Hansen pitched Mesa Rock Management as a way for Palomar Health District to resolve its financial troubles.*
- *Diane Hansen supported board members who she knew would align with the Mesa Rock proposal. She stated, in the Times Advocate, five of the seven board members have been very supportive in helping her make difficult financial decisions. Four of her five supporters are democrats.*
- *Diane Hansen told board members that having a top layer of management, employed by a private company, would allow her to broker deals (without discussion, accountability, or transparency) that she claimed get derailed by medical providers underpinnings in local government*
- *Diane Hansen devised this power grab before bond holders could force her and her management team out of Palomar Health and begin their search for a new CEO and management.*

Palomar Health’s Clarification: It is telling that when trying to describe the benefits to Ms. Hansen, all the EDC can do is point to benefits to Palomar Health. Through Mesa Rock Palomar will be able to broker deals for the benefit of Palomar—which will then become public and subject to Board oversight. No one from Palomar’s management team is receiving any additional compensation from the move, and Palomar’s Board will retain budget oversight over any raises. Just like it does now.

Quote from the EDC Letter:

CEO Diane Hansen's less than stellar record at Palomar Health includes the following:

- *A vote of no-confidence by the physician group and the entire medical and nursing staff*
- *An executive decision that resulted in 50% of emergency room physicians and 50% of internal medicine physicians quitting immediately to work elsewhere*

Palomar Health's Clarification: Vituity, a privately held medical corporation that previously held the Palomar contract, lost a public competitive bidding process to manage Palomar's emergency department, in favor of Emergent Medical Associates. Since winning the bid, EMA has dramatically improved patient outcomes and reduced patient wait times. All Vituity staff were given the choice to join EMA and step up to the increased challenge of providing better patient care. The vast majority did and currently are employed by EMA and working for the District.

Quote from the EDC Letter:

- *An executive decision that effectively caused Kaiser to exit Palomar Health and construct a new hospital, thereby destabilizing the district's finances*

Palomar Health's Clarification: The Kaiser-Palomar Health Services Agreement expired on its own terms, not as a result of any particular decision by either Kaiser or Palomar. More importantly, Kaiser began construction of its San Marcos facility many years prior to termination of the Kaiser/Palomar agreement and began its decision-making process in the early 2000s. Palomar made its own plans to handle the termination, knowing that Kaiser had been planning for years to build its San Marcos facility and direct its patients away from Palomar.

Quote from the EDC Letter:

- *Repeated false narratives about inflated financial gains*
- *Retaliation against board members for seeking truth about hospital finances*
- *Managing to help the district descend into near bankruptcy and looming default on obligation bonds*

Palomar Health's Clarification: Hospital districts in California face pressures unlike any of the private hospitals with whom they are required to compete. While people are generally in favor of community hospitals, few would be willing to increase their property tax obligations by the orders of magnitude required to properly fund a health care district. Health care districts are therefore expected to compete with one hand tied behind their backs. No surprise that more than half of all health care districts have closed or privatized in the past ten years. Too many people are willing only to pay lip service to the idea of community institutions instead of proving the work required to keep them alive. Palomar's Board, thankfully, is made up of people who are willing to make the hard choices that will preserve the District while opening it up to creative avenues for facing its private competitors.

Georgine Tomasi
May 31, 2024
Page 11

Thank you for taking the time to read this letter. We look forward to sitting down and discussing the above issues with you and other members of the Board of Directors at your earliest convenience.

Warm Regards,

HOLLAND & KNIGHT LLP

A handwritten signature in blue ink, appearing to read "John Kern", written over the printed name.

John Kern

JK