Effect of Affiliation of St. Luke's Hospital with Sutter Health on the Availability and Accessibility of Health Care Services

Prepared for:
California Attorney General's Office

Prepared By:
The Lewin Group, Inc.

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Introduction and Project Scope

This report, prepared for the California Office of the Attorney General, assesses the potential effects of the proposed transfer of control of St. Luke's Hospital (St. Luke's or the hospital) to Sutter Health on the availability and the accessibility of health care services.

The Lewin Group analyzed the health impacts of the proposed transfer of ownership by performing the following tasks:

- Review of documents, including the Application for Approval of the transaction submitted by St. Luke's Hospital to the California Attorney General on March 13, 2001, the redacted settlement agreement between Sutter Health and St. Luke's, community health care assessments, and other materials.
- Analysis of data regarding St. Luke's Hospital services and finances and the utilization of other health care providers in San Francisco.
- Interviews with representatives of the communities and parties potentially affected by the transaction: employees, administrators, and Board Members of St. Luke's Hospital and Sutter Health; employee labor union representatives; members of the City and County of San Francisco Health Commission and Department of Public Health staff; and representatives of community organizations concerned with access to health and human services in the area served by St. Luke's.
- Development of proposed mitigation measures to reduce or eliminate the potential for adverse health effects from the transaction.
- Attendance at the Attorney General's public meeting concerning the transfer of control.

The report is organized into the following sections:

- History and Description of the Transaction;
- Summary of Public Concerns Regarding the Affiliation;
- Interview Findings;
- St. Luke's Hospital and Its Services;
- St. Luke's Charity Care and Community Benefit Services;
- Summary and Conclusions; and
- Proposed Conditions.

Time constraints imposed certain limitations on this study and report.

- There are several alternative sources of data that measure hospital performance. In some cases data purporting to measure the same activity did not match. The Lewin Group did not independently audit data to verify accuracy.

- Interviews were conducted with 44 individuals selected to provide broad input into the study. The sample may not represent the full breadth and depth of opinions regarding the proposed affiliation.
- The analysis did not include examining the capacity of other area hospitals to accept inpatient and outpatient care that historically has been provided by St. Luke's should St. Luke's ever close.

The Lewin Group wishes to express its appreciation to those who provided input and data for the study.

History and Description of Transaction

St. Luke's Hospital, a nonprofit public benefit corporation, was founded as an Episcopalian charitable hospital in 1871. The hospital's service area includes the Mission District, Visitacion Valley, Bayview Hunters Point, and other areas of San Francisco. St. Luke's Hospital is one of two disproportionate share Medi-Cal hospitals in San Francisco, the other being San Francisco General Hospital. In addition to operating the hospital, St. Luke's sponsors and supports free-standing community clinics in its service area that provide health care services to medically under-served patients.

St. Luke's has had significant financial difficulty in recent years. In 1999, St. Luke's received court approval, with the Attorney General's consent, to withdraw $4.5 million from the corpus of its restricted endowment and to use these funds for operations. In September 2000, the court approved, also with the Attorney General's consent, a further withdrawal of $3.4 million from the endowment. By November 2000, St. Luke's had $9 million in overdue accounts payable, had a negative balance of $2.8 million in its checking account, and had to seek an emergency loan from the Episcopal Diocese to meet payroll. Since December 1, 2000, Sutter Health has been paying $1 million per month to St. Luke's to keep the hospital in operation.

Because of its financial condition, St. Luke's has in the past several years considered alternatives to retaining its current independent status. In 1996, St. Luke's issued a request for proposals (RFP) for a strategic alliance with a hospital system. Sutter Health responded to that RFP and proposed a merger with its affiliate, California Pacific Medical Center (CPMC). San Francisco General Hospital's response would not guarantee that St. Luke's would stay open as an independent, acute care hospital. St. Luke's rejected both proposals.

The proposed affiliation arises from the settlement of litigation between St. Luke's and Sutter Health. In 1999, St. Luke's sued CPMC and Sutter Health challenging, on state anti-trust grounds, a contract between CPMC and the Brown and Toland Medical Group, the largest physician group in San Francisco. In October 2000, the parties settled that lawsuit. A binding affiliation letter, which later became a formal Affiliation Agreement between St. Luke's and Sutter Health, was part of the Settlement Agreement.

Under the Affiliation Agreement, St. Luke's Hospital will become an affiliate of Sutter Health, which will become the sole corporate member of the hospital corporation. As an affiliate, St. Luke's will retain its status as a separate corporation and will continue to operate the hospital. The current St. Luke's board will remain, with the addition of two representatives of Sutter Health and a reciprocal representative of CPMC. Sutter Health will appoint future board members from nominees by the incumbent board. Sutter Health will also have significant fiscal

authority over St. Luke's and the hospital's assets and liabilities will be consolidated under Sutter Health's Obligated Group.

Sutter Health has made a number of financial commitments as part of the affiliation transaction. As previously mentioned, Sutter Health is providing $1 million per month, up to $12 million, for immediate financial relief. Sutter also will assume existing debt and will pay at least $4 million per year for ten years for facility and equipment upgrades.

Sutter will pay up to $10 million into a new nonprofit corporation, the Brotherton Fund. Additional funds will come from the remaining St. Luke's endowment. A board appointed by the St. Luke's board will administer this Fund.

The Affiliation Agreement also contains commitments regarding health care services at St. Luke's Hospital. Section 1.02A of the Agreement provides that Sutter will support the provision of charity care at the hospital at "historic levels." Existing health care services will be maintained at the hospital at the discretion of the St. Luke's Hospital board.

St. Luke's Hospital also states that the affected community will enjoy a number of benefits pursuant to its affiliation with Sutter Health. These include:

- An infusion to St. Luke's of $65 million in capital investments by Sutter Health. According to the application, these investments will enable St. Luke's "to significantly increase the programs and services that it provides to the South of Market community.[1]"
- The ability to maintain, upgrade, and expand its equipment and facilities. These upgrades will allow St. Luke's to adapt to advances in medical technology and continue to attract physicians and other professional staff necessary to provide a high level of health care to the community.
- Stability, enabling St. Luke's to expand services during periods of growing volume and allowing it to avoid significantly reducing services during economic downturns.
- Capital necessary to bring St. Luke's facility into compliance with seismic safety requirements mandated by SB 1953. Seismic upgrades will require at least $15,000,000 for construction at St. Luke's and over $5,000,000 to cover losses during construction.
- Funding necessary to expand its emergency services by keeping its "critical Emergency Room open to receive ambulances[2]" while other hospitals, particularly San Francisco General Hospital (SFGH), are on diversion.

St. Luke's also states that it provides annually 55,000 days of care, 28,000 emergency room visits, 100,000 outpatient visits and many additional services to the community. The Application states that St. Luke's provides more charity care than all other private hospitals in San Francisco combined, and "this charity care will be preserved if the Affiliation is approved because Sutter Health has agreed in the Affiliation Agreement to provide financial and other support for the historic level of charity care provided by the Applicant."[3]

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[1] Written Notice to the California Attorney General and Application for Approval of a Transaction in Accordance with Title 11 of the California Code of Regulations (Section 999.5), March 13, 2001.

[2] *Ibid.*

[3] *Ibid.*

The conditions proposed at the end of this report incorporate these representations and commitments.

Summary of Public Concerns Regarding the Affiliation

Public testimony presented to the Attorney General at a public meeting conducted on April 16, 2001 and to the San Francisco Health Commission, as well as The Lewin Group's subsequent interviews to assess potential health impacts associated with the transaction, revealed a number of concerns about the proposed affiliation. These included: Sutter Health's motivation for the affiliation, its track record in previous affiliations, and the perceived risks and benefits of proceeding with the Agreement, including what would happen if the affiliation did not occur. Interested parties identified both alternatives to the transfer of control of St. Luke's and conditions that might be attached to the affiliation.

Distrust of Sutter Health's intentions was expressed in testimony and in many of our interviews. Some of the motivations ascribed to Sutter for assuming responsibility for St. Luke's included: settlement of potentially damaging litigation; increasing Bay Area market share; acquiring a hospital and/or its real estate in anticipation of continued economic development in the area; the belief that St. Luke's could become economically viable; expanding the referral base for Sutter Health's other Bay Area institutions; consolidating charity and Medi-Cal funded care at a single, low-cost institution; or improving the system's public image.

There was concern that affiliation might result in decreased charity care, loss of local governance and community and employee input, and eventual reduction or closure of services. For these reasons, some alternatives were proposed: carrying the lawsuit to conclusion in hopes of a monetary judgement that would secure St. Luke's survival as an independent community hospital; affiliation with the City and County of San Francisco; or State intervention in the form of higher Medi-Cal rates.

Conditions suggested to be attached to the Attorney General's approval of the transfer of control, included: a commitment to maintain the institution as an acute hospital; specific service guarantees; maintenance of contracts for Medi-Cal, City and County of San Francisco mental health, and reproductive health services; maintenance of charity care expenditures; designating funding for increased staffing; creating a community health fund particularly if the hospital closes in the next few years; restricting the flow of funds out of the institution to other Sutter Health affiliates; assuring local governance and oversight; assuring that pension plan assets in excess of liabilities should be retained by current or former St. Luke's employees; providing legal standing for patients to sue to enforce any conditions; assuring full disclosure of the hospital's seismic compliance plans in time for area hospitals to adjust if necessary; assuring full funding of seismic facilities upgrades as required by SB 1953; requiring participation in an area-wide planning process before major service changes are implemented; reporting of charity care to the San Francisco Health Commission; and other suggestions.

There also was widespread concern that St. Luke's would soon close if the funding associated with the Sutter Health affiliation did not materialize. Both proponents of the affiliation and supporters of conditional approval identified potential benefits of the affiliation: injection of needed operating and capital funds; retention of a longstanding mission-driven community hospital; improvements in staffing and morale; ability for members of the St. Luke's medical staff to continue practicing in the community; and enhanced quality and range of hospital and

clinic services. Proponents argued that all possible alternatives had been explored and exhausted, that affiliation with Sutter was the only option left to secure the hospital's survival, and that onerous conditions could doom the planned affiliation with Sutter Health.

Interview Findings

This section summarizes additional topics that emerged during interviews conducted by The Lewin Group for this project. The purpose of the interviews was to identify elements of the affiliation that stakeholders considered likely to impact the health of the St. Luke's community.

The Lewin Group conducted interviews with 44 individuals, both in person and over the phone. Respondents represented San Francisco-area or Northern California hospitals, physicians, health plans, government agencies and other organizations, including Sutter Health, St. Luke's Hospital, St. Luke's Health Care Center, Local 250-SEIU, several clinics serving South of Market residents, and the City of San Francisco Department of Public Health. Respondents were selected to provide varied perspectives on health and health care in San Francisco, St. Luke's Hospital, Sutter Health, and the proposed affiliation between the two entities.

St. Luke's Financial Condition

Most respondents indicated that St. Luke's Hospital experienced extreme financial difficulties prior to the interim agreement with Sutter Health. The hospital was portrayed as being near bankruptcy. Paychecks reportedly bounced, and the hospital has been subjected to a credit freeze by suppliers. While the hospital has struggled financially for some years, recent troubles reportedly have been particularly difficult, evidenced by the hospital's use of restricted endowment funds for operations, a growing accounts payable balance, a relatively high staff vacancy rate, employee attrition, and other challenges.

Regardless of their support or opposition, most interviewees saw the affiliation as one means to end St. Luke's financial struggles. A few were skeptical regarding the depth of the financial difficulties at St. Luke's and believed the hospital could continue to survive as an independent organization.

St. Luke's reportedly needs at least $20 million to retrofit its buildings to meet SB 1953 seismic standards. Several interviewees noted that no written guarantee exists in the Affiliation Agreement that Sutter Health will provide all funding needed to achieve SB 1953 compliance.

Sutter Health Financial Policies

Sutter's Equity Cash Transfer policy received considerable discussion from those interviewed. The policy requires that each affiliate keep 14 days of expenses in cash on hand at all times and send all excess to the Sutter Health system. These funds are pooled, distributed among the hospitals as needed, and committed to bond holders so that the system has access to comparatively low-cost capital.

Some respondents stated that Sutter has helped financially distressed hospitals become stable. For example, they reported that Sutter Health has continued to support Santa Rosa Hospital financially in spite of this affiliate's operating losses. A few interviewees acknowledged that at least for the first few years of the affiliation, St. Luke's would be a net beneficiary of the

system's equity transfer policy as Sutter provides funding as committed through the proposed Affiliation Agreement.

Local Governance and Community Input into Governance

Virtually all those interviewed strongly favored maintaining local authority for St. Luke's under an affiliation. They disagreed about Sutter's commitment to maintaining local authority at St. Luke's. Some contended that Sutter would not leave decision-making power to St. Luke's. Others were optimistic that it would.

Sutter Health approves decisions made by local boards through its "reserve powers," which pertain to capital expenditures by affiliates of more than $1 million, budgets, strategic plans, bylaws, and nomination of board members. Senior hospital managers also are Sutter Health employees.

Several interviewees expressed concern that the agreement provides at least the mechanism for reorganizing a local board, although the process would be lengthy and laborious. Views were mixed on the probability of such a board change because a majority of the Sutter Health board is comprised of affiliate hospital board members. Sutter Health also reportedly never has rejected a local board choice.

Maintenance of St. Luke's Current Services

A number of respondents expressed concern that Sutter Health would reduce services at St. Luke's, negatively affecting the health or access to care of the hospital's current patient population. They reported examples of service reductions at other affiliates, including obstetrics at Novato General Hospital and skilled nursing facility (SNF) beds at Davies Hospital. Interviewees disagreed about the source of the cuts (whether Sutter or the local boards decided that service reductions were necessary) and whether they were warranted.

Some interviewees insisted that St. Luke's remain a full-service, acute care hospital. They reported that St. Luke's turned down an opportunity to partner with the San Francisco Department of Public Health some years ago, because the City planned to convert St. Luke's to a long term care facility.

Others indicated that it did not make good sense in the long run to support two acute hospitals as close together as St. Luke's and SFGH. They acknowledged a short-term need for St. Luke's as presently constituted, but felt a broader long-range planning effort should be undertaken for the area.

Several services currently provided at St. Luke's hospital were considered to be critical to its mission. Respondents identified pediatrics, obstetrics, emergency room services, urgent care services, community clinics, and mental health services as "mission critical" services to be maintained under all scenarios.

Although obstetrics services are available at other San Francisco facilities, interviewees noted that many South of Market women tend not to leave the community for their care and that St. Luke's is their obstetrics provider of choice. Obstetrics services also help qualify the hospital for disproportionate share funding and are thereby critical to the hospital's financial stability.

Some noted that while obstetrics volumes at St. Luke's might appear lower than desirable, the St. Luke's obstetricians are highly regarded and achieve good outcomes for patients. Several

mentioned plans to add services at St. Luke's, including cardiac catheterization once the affiliation with Sutter is consummated. No interviewees mentioned knowledge of specific plans by Sutter Health or St. Luke's to curtail services once the transfer of control is consummated.

Numerous interviewees argued that allowing health care providers like St. Luke's to maintain flexibility in the services they provide is critical because of the fluidity of the health care market and changing health care needs in the area.

Maintenance of Charity Care

Interviewees indicated that St. Luke's Hospital has a tradition of charity care, dictated both by mission and location. The level of charity care provided at St. Luke's averages $6 million annually but varies substantially from year to year. Most indigent patients enter the hospital through the emergency room, and keeping the emergency room open is seen as one way to maintain high levels of charity care.

Although different institutions quantify charity care differently, St. Luke's is almost universally perceived as a charitable institution and an integral part of the San Francisco safety net. According to interviews, St. Luke's charity care derives from a combination of patients who are unable to pay for their medical care and from inadequate Medi-Cal payments.

SFGH and St. Luke's are the two disproportionate share hospitals in the city. St. Luke's continued emergency room and charity care presence is viewed as critical in the context of staffing shortages, frequent emergency room diversions at SFGH, and a high proportion of Hispanic patients who rely greatly on St. Luke's and are unwilling or unable to seek care outside of the South of Market area of San Francisco.

In contrast, some interviewees see Sutter Health's charity care track record as poor, alleging for example that charity care was halved at one Sutter affiliate following its joining the system. Despite Sutter's stated intent to preserve the local authority of its affiliates to choose the amount of charity care they provide, many interviewees expressed skepticism regarding Sutter's plans for continuing charity care at St. Luke's. Respondents' predictions fell into two categories: (1) that levels of charity care at St. Luke's would sharply decrease following affiliation, and (2) that Sutter Health would divert charity care from its other Bay area hospitals to St. Luke's.

Specifying a strict dollar amount or percentage of revenues for charity care at St. Luke's was often mentioned as a potential condition to affiliation, though some expressed concern that this could render St. Luke's vulnerable to "dumping" by other hospitals.

Physicians

The Mission and Bayview Hunters Point communities served by St. Luke's suffer from a lack of health care providers. Doctors in the Independent Medical Group (IMG), St. Luke's physicians group, are closely aligned with the hospital. Some questioned whether the transfer of control to Sutter Health will change the level of access community physicians have to St. Luke's and whether community doctors will be able to have privileges at CPMC. Others indicated that these physicians might not be able to continue practicing in the area if St. Luke's closed. Most physicians, fatigued by the day to day uncertainty of St. Luke's future, appear in favor of the affiliation.

There is some indication that community physicians would be affected by the hospital's closure, as several admit patients only to St. Luke's. If St. Luke's closes, some may leave the neighborhood as well, potentially reducing access to primary care physicians for community members.

Staffing and Employee Issues

St. Luke's current staffing was described variously as "lean," "efficient," or "nearly dangerous." Many parties expected that affiliation would expand St. Luke's ability to recruit and maintain staff; others suggested that staff expansions would occur only as services grow. St. Luke's staff vacancy rates reportedly have declined since Sutter began supporting the hospital financially.

Several interviewees raised concerns regarding St. Luke's pension plan, which was created in the 1960s and now reportedly is over-funded. Sutter Health requires that affiliates create pension funds equal to those of all other affiliates and has committed in the proposed Affiliation Agreement that any "excess" pension plan funds would be used for the benefit of St. Luke's.

Labor representatives also are interested in greater input into patient care staffing and related issues, and in the local St. Luke's board continuing to hold significant authority over the hospital.

Consequences of Closure of St. Luke's

According to many interview participants, closure of St. Luke's would be a likely consequence of failing to achieve the planned affiliation with Sutter Health. Closure was unanimously expected to have a significant negative impact on the health of the community. As mentioned before, St. Luke's and SFGH are the only two South of Market hospitals and the only two disproportionate share hospitals in the City. SFGH is already considered overcrowded. Because SFGH's emergency department is frequently on diversion, closure of St. Luke's could be expected to pose a substantial problem for emergency services across the city. Psychiatric services and indigent care were also specifically mentioned as potential problem areas.

Many of the issues and concerns raised by interviewees were confirmed through market and data analysis. These analyses are discussed in the following section.

St. Luke's Hospital and Its Services

This section first describes St. Luke's Hospital services, then presents trends in service volumes at the hospital, discusses programs at St. Luke's and other hospitals in San Francisco, identifies the geographic areas served by St. Luke's, analyzes the hospital's market shares, and finally documents patient migration patterns in the city.

St. Luke's Hospital, a not-for-profit hospital under the auspices of the Episcopal Diocese of San Francisco, is located in the southeastern area of San Francisco, known locally as "South of Market" and encompassing the Mission District, Bayview Hunters Point, and other neighborhoods in San Francisco's southeast quadrant. According to the hospital's Annual Office of Statewide Health Planning and Development (OSHPD) Utilization Report of Hospitals, St. Luke's provided the following array of inpatient services in the fiscal year ended June 30, 1999.

TABLE 1
St. Luke's Hospital Inpatient Services: Beds and Utilization,
Fiscal Year Ended June 30, 1999

Bed Classification	Licensed Beds	Patient Days	Discharges	Average Census	Occupancy Rate
Medical Surgical Acute	100	10,711	3,175	29.3	29%
Perinatal (Obstetrics)	20	2,498	1,030	6.8	34%
Pediatric Acute	7	881	322	2.4	34%
Intensive Acute	10	2,647	771	7.3	73%
Coronary Acute	5				
Intensive Care Nursery (NICU)	5	960	116	2.6	53%
Subtotal	**147**	**17,697**	**5,414**	**48.5**	**33%**
Acute Psychiatric	31	9,189	1,057	25.2	81%
Skilled Nursing	79	21,401	931	58.6	74%
Total	**257**	**48,287**	**7,402**	**132.3**	**51%**

Source: OSHPD Annual Utilization Report of Hospitals, 1999.

The hospital is licensed for 257 beds. In fiscal year 1999 there was an average of 48.5 inpatients occupying medical-surgical, obstetrics, pediatric, and/or intensive care beds at the hospital. There also was an average of 25.2 acute psychiatric and 58.6 skilled nursing (including subacute) patients at the hospital. According to OSHPD, the hospital reported 929 live births in 1999.

Inpatient Psychiatric Services

In fiscal year 2000, slightly more than 75 percent of the acute psychiatric patient days at St. Luke's Hospital were provided under a contract with the City and County of San Francisco Department of Public Health (DPH). In California, counties have been delegated responsibility for managing and authorizing inpatient and ambulatory mental health services for indigent and Medi-Cal sponsored patients. In San Francisco, DPH relies on SFGH, St. Luke's, and other area hospitals to provide this care for mental health consumers with Medi-Cal coverage. The contracts also cover low-income Medicare patients who qualify for Medi-Cal for purposes of reimbursing Medicare co-payments and deductibles (the "Medi-Medi" patients).

According to data from the DPH Division of Community Mental Health Services, 7,129 acute patient days were authorized in fiscal year 2000 under the contract for Medi-Cal and Medi-Medi psychiatric patients at St. Luke's Hospital, or an average daily census of approximately 20 patients. St. Luke's has been the largest private hospital provider of inpatient mental health services for DPH patients. St. Mary's Hospital recently announced its intention to close adult inpatient psychiatric services. St. Mary's served an average daily census of about 10 Medi-Cal and Medi-Medi psychiatric inpatients. This development increases the importance of maintaining access to the St. Luke's mental health beds for low-income San Francisco residents.

Skilled Nursing and Subacute Services

The skilled nursing and subacute services include 79 "long term care" beds comprising 60 subacute and 19 skilled nursing facility (SNF) beds. All patients in the subacute beds are Medi-Cal beneficiaries ("subacute" being a Medi-Cal payment category, not a type of licensed bed).

Subacute patients are those requiring chronic ventilator care, primarily due to head trauma but also occasionally due to advanced multiple sclerosis and ALS. Patients are referred from all over northern California. The average length of stay in the unit is approximately one year. Thirty percent of the patients are discharged to their homes, a high proportion for such a unit. When the subacute beds opened, they were the only ones in the region. Seton Medical Center (Daly City) and Vencor-San Leandro now offer this service, although the latter does not have a Medi-Cal contract. Laguna Honda also has subacute beds but these are accessible only to referrals from San Francisco General Hospital.

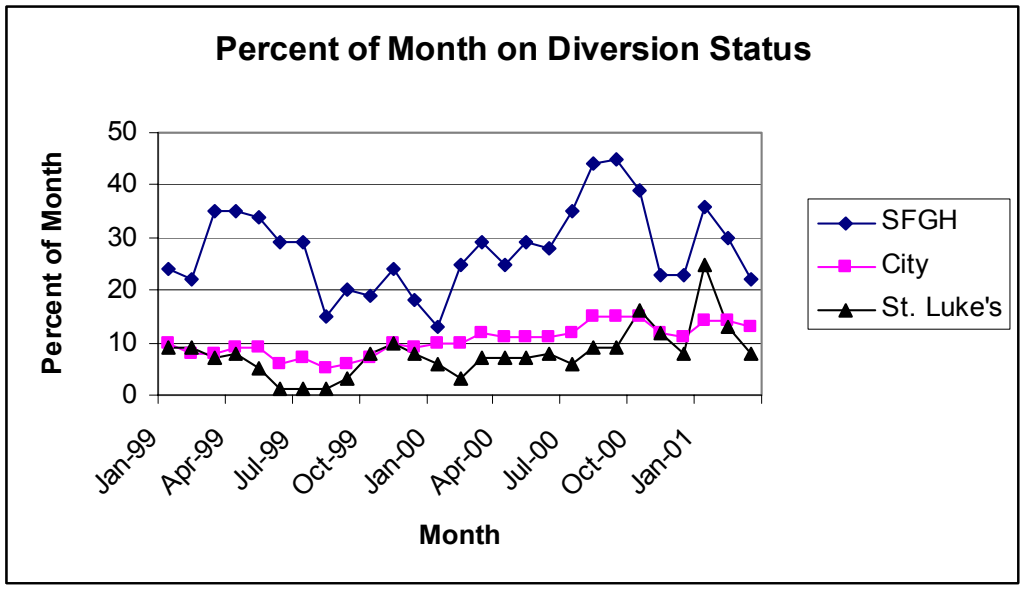
The 19 SNF beds at St. Luke's Hospital take only internal referrals from medical-surgical and ICU beds, and reportedly are always full, with an average length of stay of about 12 days.

Emergency Room Services

In calendar year 1999, the hospital reported 28,232 emergency room visits. 14,963 (or 53 percent) were classified as "non-urgent" and 47 percent were "urgent" or "critical" visits. Approximately one-half, or 3,190 of the hospital's medical-surgical and acute psychiatric admissions were admitted after patients first received services in the hospital's emergency room.

According to data provided by the City and County of San Francisco's Emergency Medical Services Section, St. Luke's Hospital received approximately 10 percent of the 50,557 ambulance patient transports that resulted from EMS incidents during the fiscal year ended June 30, 2000. One reason why emergency room (and as a result inpatient medical surgical) volume has increased in recent months is the increase in diversion hours (the periods of time that a hospital cannot accept ambulances and other patients in the emergency room due to capacity constraints) at nearby San Francisco General Hospital. As shown below, the percentage of time that SFGH was on diversion has increased in the last two years, and in the Fall of 2000 exceeded 40 percent. There is a general correlation between SFGH diversion and the need for St. Luke's also to be on this status.

FIGURE 2



Source: San Francisco Department of Public Health.

St. Luke's Health Care Center

In 1995, St. Luke's Hospital formed St. Luke's Health Care Center (SLHCC), a separate 501(c)3 (not-for-profit) corporation of which St. Luke's Hospital is the sole corporate member. SHLCC is a licensed community clinic. It runs several licensed clinics, the oldest of which was founded in 1920. According to St. Luke's Hospital representatives, SLHCC would become part of the Sutter Health Obligated Group under the proposed transaction. According to the hospital's fiscal year 1999 Community Benefit Report, "SLHCC is instrumental in spearheading St. Luke's expansion of services to medically underserved residents." Physicians practicing at the SLHCC clinics are employees of the SLHCC corporation.

The SLHCC clinics delivered about 44,350 visits during the fiscal year ended June 30, 2000 through physicians who are employees of the SLHCC. Patients are seen at several sites, including:

- The St. Luke's Neighborhood Clinic and an internal medicine office located adjacent to the hospital;
- St. Luke's Pediatric Center, located across Valencia Street;
- One Family Health Center at 24th Street in the Mission District;
- St. Luke's Women's Center, located across Valencia Street; and
- Specialty clinics at or adjacent to the hospital for neonatology, outpatient mental health, orthopedics, and occupational services.

Obstetrics and Gynecology visits comprised over 26,500 of the SLHCC visits during fiscal year 2000, followed by internal medicine at 8,400 visits.

The fiscal year 1999 Community Benefits Report indicates that St. Luke's Hospital underwrites SLHCC's deficits. The amount of deficit funding provided in 1999 was $1.6 million. The fiscal

year 2000 audited financial statements for St. Luke's Hospital and Subordinate Corporations indicates that the SLHCC deficit in that year was $2.3 million.

Trends in St. Luke's Hospital Patient Care Volumes

St. Luke's Hospital provided the following patient statistics for fiscal years 1994 through 2000.

TABLE 2
St. Luke's Hospital Patient Statistics, Fiscal Years Ended June 30, 1994 - 2000

	1994	1995	1996	1997	1998	1999	2000
INPATIENT DAYS							
Medicare	20,963	18,949	16,537	15,658	14,777	17,141	15,516
Medi-Cal	21,438	23,551	21,026	23,141	25,599	24,376	27,567
HMO's	8,690	8,790	9,477	11,625	9,833	9,454	9,743
Other	1,766	1,754	676	869	1,245	1,583	2,289
Total	**52,857**	**53,044**	**47,716**	**51,293**	**51,463**	**52,554**	**55,115**
DISCHARGES							
Medicare	2,326	2,257	2,126	1,964	2,168	2,325	2,224
Medi-Cal	3,243	3,335	2,851	2,782	2,913	2,588	2,697
HMO's	1,902	1,698	1,798	2,060	2,001	1,903	1,802
Other	442	478	254	245	289	405	354
Total	**7,913**	**7,768**	**7,029**	**7,051**	**7,371**	**7,221**	**7,077**
AVERAGE INPATIENT CENSUS							
Med/Surgical	63	59	48	49	46	43	47
Obstetric	9	7	6	6	6	7	6
Psychiatric	21	25	21	25	25	24	27
Subacute	17	22	23	30	33	37	39
SNF	35	34	32	31	31	33	32
All Inpatients	**145**	**145**	**131**	**141**	**141**	**144**	**151**
ADMISSIONS							
Med/Surgical	4,790	4,632	4,108	4,040	4,265	4,144	3,923
Obstetric	1,735	1,525	1,309	1,312	1,081	1,041	998
Psychiatric	711	746	694	749	953	938	1,085
Subacute	47	106	80	62	49	51	46
SNF	627	770	822	861	973	988	839
Total Admissions	**7,910**	**7,779**	**7,013**	**7,024**	**7,321**	**7,162**	**6,891**
OTHER STATISTICS							
Births	1,591	1,390	1,250	1,145	899	844	792
Emergency Room Visits	36,409	35,392	32,978	30,188	28,609	27,786	28,591
I/P Surgeries	1,645	1,505	1,345	1,307	1,292	1,229	1,142
O/P Surgeries	3,261	2,948	3,104	3,201	2,978	2,692	2,279
O/P Visits	73,037	88,802	105,521	111,728	113,210	122,188	113,590
O/P Psych Program	48,757	18,419	23,960	24,276	31,322	31,738	10,009
Case Mix Index	1.415	1.349	1.401	1.392	1.331	1.359	1.367

Source: St. Luke's Hospital.

These data show a hospital in transition. Some acute care services have declined steadily (obstetrics, medical-surgical, inpatient and outpatient surgeries), some non-acute services have been rising steadily (subacute and SNF services), and a few have been stable (inpatient psychiatric). These trends imply a dynamic environment and a need for flexibility in planning and operations.

The hospital provided projected statistics for fiscal year 2001. The data show increases in medical-surgical and subacute census, and decreases in skilled nursing patient days. Emergency room visits are projected to approach 30,000 in 2001, and other outpatient statistics have increased in recent months with the exception of the hospital's closure of its partial hospitalization psychiatric program during fiscal year 2000.

Services at St. Luke's and Other Hospitals in San Francisco

In 1999, St. Luke's Hospital represented approximately 4.5 percent of the total hospital beds in San Francisco, but comprised a higher proportion of a few services available to City residents. According to OSHPD, in 1999 there were 10 licensed, general acute care hospitals in San Francisco with sites in 14 locations. Table 3 portrays statistics for St. Luke's, SFGH, and other hospitals in the City.

TABLE 3
St. Luke's Proportion of San Francisco Hospital Services, Fiscal Year 1999

Service	St. Luke's	SFGH	Other Hospitals	Total	St. Luke's Proportion
Licensed Beds					
Medical-Surgical Acute	100	323	2,822	2,922	3.4%
Perinatal	20	23	194	214	9.3%
Pediatric	7	23	154	161	4.3%
Intensive Care	10	22	207	217	4.6%
Coronary Care	5	8	58	63	7.9%
Intensive Care Nursery	5	12	86	91	5.5%
Acute Psychiatric	31	106	273	304	10.2%
Skilled Nursing	79	215	1,788	1,867	4.2%
Other			166	166	0.0%
Total	**257**	**732**	**5,748**	**6,005**	**4.5%**
Patient Days					
Medical-Surgical Acute	10,711	52,879	294,618	305,329	3.5%
Perinatal	2,498	3,790	30,020	32,518	7.7%
Pediatric	881	1,911	29,301	30,182	2.9%
Intensive Care	2,647	12,835	54,076	56,723	4.7%
Coronary Care		652	15,742	15,742	0.0%
Intensive Care Nursery	960	3,493	30,493	31,453	3.1%
Acute Psychiatric	9,189	34,744	62,244	71,433	12.9%
Skilled Nursing	21,401	54,921	529,304	550,705	3.9%
Other			17,157	17,157	0.0%
Total	**48,287**	**165,225**	**1,062,955**	**1,111,242**	**4.3%**
Live Births					
Live Births	929	1,346	10,587	11,516	8.1%
Emergency Medical Services					
Non-Urgent	14,963	20,125	45,441	60,404	24.8%
Urgent	12,422	29,647	116,713	129,135	9.6%
Critical	847	14,876	51,037	51,884	1.6%
Total	**28,232**	**64,648**	**213,191**	**241,423**	**11.7%**

Source: OSHPD Annual Utilization Report of Hospitals, 1999.

The table indicates that:

- St. Luke's represented 4.5 percent of the hospital beds in San Francisco and over 10 percent of inpatient psychiatric capacity and patient days in the City.
- The St. Luke's emergency room provided approximately 12 percent of the City's emergency room visits and almost 25 percent of the emergency room based non-urgent care in the City. St. Luke's emergency room had the highest ratio of non-

urgent to total emergency room visits in San Francisco. This may indicate a lack of primary care services in the service area, a lack of affordable services, and/or a lack of culturally competent services.

The following table provides a similar analysis of volume by payer source.

TABLE 4
St. Luke's Proportion of San Francisco Hospital Utilization by Payer, 1999

Service	St. Luke's	SFGH	Other Hospitals	Total	St. Luke's Proportion
DISCHARGES					
Medicare	2,305	2,954	22,546	27,805	8.3%
Medi-Cal	1,621	10,485	8,379	20,485	7.9%
Other Third Parties	3,227	1,164	38,987	43,378	7.4%
Indigent and Other	257	4,497	3,602	8,356	3.1%
Total	**7,410**	**19,100**	**73,514**	**100,024**	**7.4%**
PAYER MIX OF DISCHARGES					
Medicare	31%	15%	31%	28%	
Medi-Cal	22%	55%	11%	20%	
Other Third Parties	44%	6%	53%	43%	
Indigent and Other	3%	24%	5%	8%	
PATIENT DAYS					
Medicare	16,037	23,360	164,157	203,554	7.9%
Medi-Cal	22,881	60,939	66,863	150,683	15.2%
Other Third Parties	12,634	29,769	196,809	239,212	5.3%
Indigent and Other	1,193	5,908	89,521	96,622	1.2%
Total	**52,745**	**119,976**	**517,350**	**1,111,242**	**4.7%**
PAYER MIX OF PATIENT DAYS					
Medicare	30%	19%	32%	18%	
Medi-Cal	43%	51%	13%	14%	
Other Third Parties	24%	25%	38%	22%	
Indigent and Other	2%	5%	17%	9%	

Source: OSHPD, 1999.

Approximately 22 percent of St. Luke's discharges were provided to Medi-Cal patients, compared to 55 percent for San Francisco General Hospital and 11 percent for all other hospitals in San Francisco.

The St. Luke's Hospital Service Area

While city-wide analyses are helpful in understanding the role of St. Luke's Hospital, assessing the health impacts of the proposed transaction requires examining more closely the specific communities served by the hospital. This requires defining the relevant

community and specifying the hospital's "service area." First, we examine which geographic areas contribute most to the hospital's total service utilization. Second, we assess the hospital's market share. The following table demonstrates these two perspectives.

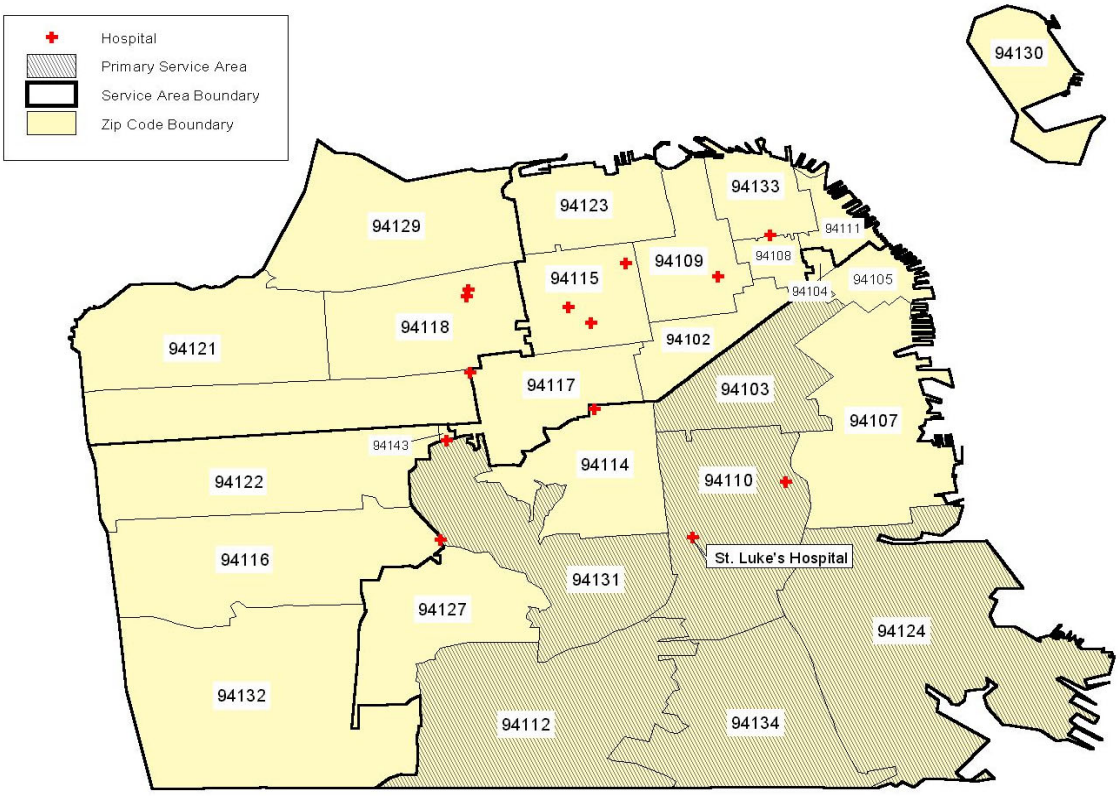
TABLE 5
Inpatient Discharges by Zip Code and Service Area, Calendar Year 1999

	St. Luke's	% of Total St. Luke's	All Hospitals	St. Luke's Market Share
SOUTH OF MARKET PRIMARY SERVICE AREA				
94110	2,116	26%	8,765	24.7%
94112	1,305	16%	8,667	15.1%
94124	799	10%	5,145	15.5%
94134	736	9%	4,813	15.3%
94103	314	4%	3,489	9.0%
94131	217	3%	2,633	8.2%
Total	**5,537**	**67%**	**33,512**	**16.5%**
SOUTH OF MARKET SECONDARY SERVICE AREA				
94114	149	2%	2,668	5.6%
94107	126	2%	1,799	7.0%
94127	57	1%	2,098	2.7%
94104	13	0%	179	7.3%
94105	7	0%	315	2.2%
Total	352	4%	7,059	5.0%
North of Market	539	7%	25,297	2.1%
Southwest San Francisco	207	3%	12,790	1.6%
Northwest San Francisco	74	1%	7,940	0.9%
San Francisco	**6,709**	**82%**	**86,598**	**7.7%**
All Other Areas	1,498	18%	44,586	3.4%
Total	**8,207**	**100%**	**131,184**	**6.3%**

Source: Lewin Group Analysis of OSHPD Discharge Database, 1999.

In calendar year 1999, two-thirds of St. Luke's Hospital's discharges originated from residents of six zip codes in the South of Market area. We have designated these zip codes the "primary service area." Another four percent were from residents of the remainder of the South of Market, or the "secondary service area." The hospital reported a market share of 16.5 percent in the primary service area and 7.7 percent for the City as a whole. The primary service area and the regions specified in Table 5 are portrayed in the map below.

FIGURE 3
St. Luke's Hospital Service Area Map



As presented above, the community most affected by the transaction is a portion of the area in the South of Market, including the Mission District, Visitacion Valley, and Hunters Point areas.

St. Luke's Hospital reports the following patient origin statistics for emergency room patients.

TABLE 6
Patient Origin for the St. Luke's Hospital Emergency Room by Fiscal Year

Area	1998	1999	2000
South of Market Primary Service Area	16,353	16,895	17,673
South of Market Secondary Service Area	1,185	1,236	1,293
North of Market	1,591	1,533	1,672
North West San Francisco	139	142	131
South West San Francisco	575	525	514
Other Areas	4,789	4,514	4,867
Unknown	732	716	852
Total	25,364	25,561	27,002
South of Market Primary Service Area % of Total	64%	66%	65%

Source: St. Luke's Hospital.

Table 6 shows that two-thirds of emergency room patients resided in the six-zip code South of Market Primary Service Area, a similar proportion to the inpatient statistics.

As shown in Table 7, the primary service area has a high concentration of residents of Hispanic origin and of young persons below the age of 20 years. The area is less affluent than San Francisco as a whole, but does not have the highest proportion of low-income persons in the City. The zip codes just north of Market Street (94102 and 94108) have high proportions of low income persons.

TABLE 7
Selected San Francisco Population Statistics

Area	Total Population, 2000	Percent Hispanic	Percent Aged 0-19 Years	Percent Aged 65 Years and Older	Percent with Income below $15,000
South of Market Primary Service Area	251,778	31.2%	23.3%	11.9%	11.4%
South of Market Secondary Service Area	68,952	15.0%	13.1%	13.0%	8.5%
North of Market	223,349	8.0%	13.3%	16.3%	17.5%
South West San Francisco	119,439	7.8%	19.4%	18.8%	8.1%
North West San Francisco	86,520	6.3%	18.8%	15.2%	8.5%
Total	750,038	16.2%	18.2%	14.8%	12.1%

Source: The Sourcebook: Zip Code Demographics 2000 (Estimates).

St. Luke's Services Utilized by South of Market Residents

As previously shown, St. Luke's Hospital admitted approximately 16.5 percent of the inpatients from the six zip-code South of Market primary service area and 7.7 percent for the City as a whole in calendar year 1999. However, these market share statistics varied by hospital service and by patient payer category. Table 8 highlights services and payer categories for which St. Luke's reported market shares exceeding 20 percent in the South of Market primary service area.

TABLE 8
St. Luke's Primary Service Area Market Share Analysis, 1999

Service	Payer Source					St. Luke's Discharges
	Medi-Cal	Medicare	Private	Other	Total	
Ventilator Support	**33%**	**21%**	**27%**	**33%**	**26%**	81
Rheumatology	**32%**	19%	**20%**	**22%**	**23%**	51
Psychiatry	**35%**	**32%**	7%	2%	**21%**	467
Neonatology	**34%**	-	12%	2%	**21%**	282
Neurology	**20%**	**20%**	**24%**	15%	**21%**	273
Gastroenterology	**25%**	**20%**	19%	15%	**20%**	389
Cardiology	**20%**	17%	**25%**	13%	**20%**	504
Vascular Surgery	**24%**	17%	**22%**	12%	19%	113
General Medicine	**27%**	19%	17%	7%	19%	1,279
Pediatrics	**26%**	-	12%	7%	18%	169
Gynecology	**33%**	19%	11%	12%	18%	153
Obstetrics	**28%**	**20%**	7%	16%	16%	650
Medical Oncology	17%	19%	14%	13%	16%	117
Dental/Oral Surgery	**36%**	-	**20%**	-	16%	7
Normal Newborn	**27%**	-	7%	4%	15%	368
Plastic Surgery	14%	17%	23%	8%	15%	37
Urology	13%	15%	14%	8%	14%	65
Dermatology	14%	7%	**23%**	-	13%	14
General Surgery	18%	12%	11%	8%	13%	213
Surgical Oncology	4%	16%	11%	13%	11%	15
Orthopedics	19%	12%	8%	3%	10%	167
Burns	17%	13%	10%	0%	9%	3
Neurosurgery	7%	7%	8%	4%	7%	21
Ophthalmology	16%	-	-	6%	6%	4
Otolaryngology	4%	8%	17%	0%	6%	15
Substance Abuse	11%	10%	1%	5%	6%	17
HIV Services	4%	8%	1%	6%	5%	21
Cardiothoracic Surgery	5%	5%	3%	-	4%	32
Trauma	6%	3%	9%	-	4%	6
Rehabilitation	1%	1%	1%	-	1%	4
Transplant services	-	-	-	-	-	-
Total	25%	17%	12%	7%	17%	5,537

Source: Lewin Group analysis of OSHPD Discharge Data, 1999.

Relatively high market shares (and a large number of discharges) for specific St. Luke's services or patient populations indicate the potential for the greatest health impacts if services are reduced or eliminated.

- In the South of Market primary service area, the hospital's market shares were relatively higher in the following services: ventilator support, rheumatology, neonatology, neurology, gastroenterology, psychiatry, cardiology, pediatrics, and general medicine.
- The hospital has comparatively low shares of the general surgery, orthopedics, rehabilitation, and surgical subspecialty markets.

There are three services for which the hospital's market shares varied significantly by payer source.

- St. Luke's market share of Medi-Cal obstetrics cases is 28 percent, while its share for patients with private coverage is 7 percent.
- The hospital admits one-third of the area's Medi-Cal and Medicare-funded psychiatric cases, but only seven percent of the privately-insured patients.
- The hospital's market share of Medi-Cal pediatrics cases is 26 percent versus 12 percent for privately insured inpatient children.

Outmigration from the South of Market

Market share data also allow identifying "outmigration" patterns from the South of Market Primary Service Area to other area hospitals. Table 9 portrays the number inpatient discharges for residents of the South of Market Primary Service reported by St. Luke's and SFGH as well as other hospitals in San Francisco and in the Bay Area.

TABLE 9
Outmigration from the South of Market Primary Service Area by Payer Source, 1999

Payer Source	Discharged from St. Luke's or SFGH	Discharged from Other Hospitals	All Discharges	Outmigration Percent
Medi-Cal	6,689	2,429	9,118	27%
Medicare	3,095	6,316	9,411	67%
Private Coverage	1,589	9,850	11,439	86%
All Other	2,557	987	3,544	28%
Total	13,930	19,582	33,512	58%

Source: Lewin Group analysis of OSHPD discharge data, 1999.

According to OSHPD data, in 1999 approximately 58 percent of the discharges for residents of the St. Luke's Hospital South of Market Primary Service Area received hospital care outside of this area, at hospitals other than St. Luke's or San Francisco General. While a majority of inpatients left the South of Market area for inpatient hospital care, these statistics are very different by payer source. Only 27 percent of Medi-Cal patients were hospitalized at other facilities, while 86 percent of patients with private insurance coverage and 67 percent of Medicare patients left the South of Market

for inpatient care. Additional analysis of these data by patient ethnicity and by hospital service indicates the following:

- While 27 percent of all Medi-Cal-funded patients residing in the South of Market Primary Service Area were hospitalized at hospitals besides St. Luke's and SFGH, only 11 percent of Hispanic Medi-Cal patients left the area (or 373 of 3,336 discharges).
- Overall, 64 percent of Hispanic residents and 50 percent of African-American residents of the South of Market Primary Service Area received their inpatient care from SFGH or St. Luke's in 1999.
- Eighty-two percent of the Medi-Cal funded obstetrics cases from this area of San Francisco were discharged from either San Francisco General Hospital or St. Luke's hospital.
- Comparatively low levels of outmigration also were observed for psychiatry, trauma, neonatology, otolaryngology (at SFGH), plastic surgery (at SFGH), and ophthalmology (at SFGH).
- Comparatively high levels of outmigration were observed for the following services: organ transplants, inpatient rehabilitation, cardiothoracic surgery, medical oncology, orthopedics, urology, neurology, and substance abuse care.

These disparities may indicate that some patients prefer St. Luke's or SFGH due to their linguistic and cultural competence, that there may be a lack of specialty and tertiary services in the South of Market area, or that some patients would leave the area for health care services if they could afford other alternatives.

These findings and the demographics of the local community also are reflected in the ethnicity of inpatients at St. Luke's Hospital, SFGH, and other area hospitals.

TABLE 10
St. Luke's and Other Hospital Discharges by Ethnicity, 1999

Ethnicity	St. Luke's	SFGH	Other San Francisco Hospitals
Hispanic	33%	23%	8%
Caucasian	27%	33%	58%
African American	19%	28%	10%
Asian / Pacific Islander	15%	14%	20%
Other / Unknown	6%	2%	4%
Total	100%	100%	100%

Source: Lewin Group Analysis of OSHPD Discharge Data.

St. Luke's Charity Care and Community Benefit Services

The St. Luke's Hospital fiscal year 1999 Community Benefit Inventory itemizes a number of services and benefits provided by the hospital for the community. These include:

- traditional charity care,

- unreimbursed cost of the Medi-Cal program,
- subsidies for the SLHCC clinics, and
- a variety of other programs including chaplaincy services and diagnostic community screenings.

The dollar value assigned to these services is $11.5 million for the first three categories and $11.9 million in total. The Community Benefit Report indicates that these services are designed to meet specific community needs, including a relatively high level of preventable hospitalizations in the area, an undersupply of primary care physicians, and a large number of uninsured consumers.

St. Luke's Hospital Charity Care Services

St. Luke's Hospital provides care through inpatient hospitalization, emergency services, outpatient care, and primary care services (through SLHCC). Historically, the hospital has been an important provider of charity care in San Francisco. Its status as the only disproportionate share hospital other than SFGH reflects the high proportion of its patients who are indigent or Medi-Cal patients.

The Office of Statewide Health Planning and Development (OSHPD) defines *charity care* by contrasting charity care and bad debt. According to OSHPD, "the determination of what is classified as ... charity care can be made by establishing whether or not the patient has the ability to pay. The patient's accounts receivable must be written off as bad debt if the patient has the ability but is unwilling to pay off the account." All hospitals are required to maintain written documentation regarding their charity care criteria and to maintain written documentation regarding all charity care determinations.

St. Luke's Hospital has established and implemented specific charity care policies and procedures that have governed the provision and reporting of its charity care services for the last several years. The policy, as stated on the hospital's "Request for Uncompensated Services" is as follows: "As its resources allow, St. Luke's Hospital makes uncompensated services available to its patients who could otherwise not afford it." The hospital's procedures include obtaining information regarding the patient's income and the number of household dependents.

Based on these polices and procedures and OSHPD's charity care reporting standards, the hospital stated that it reported the following amounts of total charity in its OSHPD Annual Financial Disclosure Reports.

TABLE 11
Charity Care Reported by St. Luke's Hospital,
Fiscal Years 1995 through 1999

Fiscal Year	Reported Charity Care
1995	$3,872,689
1996	$9,318,185
1997	$8,393,646
1998	$5,561,840
1999	$4,942,744
Average	$6,417,821

Source: St. Luke's Hospital.

According to the St. Luke's Hospital Finance Department, the charity care reported to OSHPD included the following categories of hospital services.

- Medically indigent adults who arrive at St. Luke's Hospital's emergency room by ambulance or through walk-in, in some cases because SFGH is on diversion;
- Medically indigent adults who seek care at St. Luke's Hospital's emergency room to avoid long waits at the SFGH emergency room;
- St. Luke's Neighborhood Clinic (and other SLHCC clinic) patients who require hospital services;
- Medi-Cal beneficiaries for whom Medi-Cal denies payment due to lack of proper authorizations, missing data in submitted bills, or other issues; and
- A portion of the co-payments and deductibles for Medicare patients who also are Medi-Cal beneficiaries (Medi-Medi crossover patients).

St. Luke's provided The Lewin Group with the following analysis of fiscal year 2000 charity care as tabulated by the hospital's accounting system.

TABLE 12
Analysis of Fiscal Year Ended June 30, 2000 Charity Care

Charity Care Category	Number of Patient Accounts	Inpatient Days	Amount Written-Off
Inpatients admitted through the Emergency Room			
• Medi-Cal denials	29	62	$218,852
• Other inpatients	196	547	2,654,538
• Total	225	609	2,873,391
Other Emergency Room patients			
• Medi-Cal denials	42		12,784
• Other patients	866	NA	514,234
• Total	908		527,018
Other Inpatients			
• Medi-Cal denials	54	220	336,341
• Other patients	95	497	1,063,463
• Total	149	717	1,399,805
Other Outpatients			
• Medi-Cal denials	80		50,696
• Other patients	747	NA	245,845
• Total	149		296,542
Totals:			
• Via Emergency Room	1,133	609	3,400,409
• Other Patients	976	717	1,696,346
• Total	2,109	1,326	$5,096,755

Source: St. Luke's Hospital.

In fiscal year 2000, patients arriving at the hospital's emergency room generated $3.4 million of the $5.1 million in charity care, or 67 percent. Other data provided by the hospital indicate that this proportion has been stable from fiscal years 1997 through 2000. The Emergency Room is a major point of access for indigent patients and the major source of charity care for St. Luke's. The data also indicate that Medi-Cal denials comprised about 13 percent of the fiscal year 2000 charity care write-off.

It is important to recognize that the dollar values for charity care reported above represent "gross patient care charges" that have been assigned (or "written off") to this category rather than the actual cost of services provided to the hospital's charity patients. While most hospitals (and OSHPD) generally account for charity care based on gross charges, this accounting convention creates measurement problems both when comparing hospitals and when evaluating trends and changes in the actual level of charity care provided. The following discussion illustrates these issues.

Although uncollected charges are an appropriate measure for many purposes, they overstate the actual cost of providing the care. More importantly, this deduction can distort comparisons between healthcare facilities because of differences in the "markup" of charges over costs. Thus, one hospital may appear to provide more charity care than another only because the hospital has higher charges. In addition, a substantial increase

in gross charge rates would lead to a higher reported level of charity care without more charity care services being provided. Healthcare facilities differ widely in how they determine charity care, ranging from those that offer no charity care category (classifying all uncompensated care as bad debt) to those that use a variety of income thresholds, asset tests, and sliding fee scales. Thus, two hospitals may provide the same amount of unreimbursed care to poor patients, but show very different charity amounts.

Calculation of the cost of charity care patients at St. Luke's and other San Francisco area hospitals can be accomplished by deriving a "cost to charge ratio," a standard, Medicare-approved practice. Results of this approach are shown in Table 13. St. Luke's charity care statistic is reduced to charity care costs of $2,086,547 for fiscal year 1999. Nevertheless, Table 13 shows that St. Luke's provides the highest "charity percent of expenses" of all private hospitals in the city. This finding is particularly notable given the high proportion of Medi-Cal funded skilled nursing and subacute care provided by St. Luke's.

TABLE 13
Charity Care in San Francisco Hospitals, FY 1999

Hospital	Total Expenses	Total Charges	Charity Care Write-Off	Cost to Charge Ratio	Charity Care Costs	Charity Percent of Expenses
CPMC	301,012,904	914,578,937	3,767,146	0.33	1,239,871	0.4%
Chinese	28,493,393	56,204,413	582,186	0.51	295,145	1.0%
Davies	38,327,886	78,628,478	813,912	0.49	396,746	1.0%
SFGH	307,150,264	418,095,448	61,043,263	0.73	44,844,914	14.6%
St. Francis	72,354,848	221,395,322	3,287,043	0.33	1,073,268	1.5%
St. Luke's	82,444,390	195,299,452	4,942,744	0.42	2,086,547	2.5%
St. Mary's	133,732,461	394,984,258	6,167,913	0.34	2,088,312	1.6%
UCSF	473,798,542	986,845,955	5,660,375	0.48	2,717,625	0.6%
UCSF/MT. ZION	125,133,795	262,970,636	724,911	0.48	344,947	0.3%
Total	1,562,508,483	3,529,002,899	81,265,164	0.44	35,981,129	2.3%

Source: Adapted from San Francisco Department of Public Health, Analysis of Charity Care Provided by San Francisco's Non-Profit and Public Hospitals, August 2000.

We note that charity care for any one hospital can vary significantly from year to year due to changes in Medi-Cal eligibility rules, health insurance expansion initiatives, economic growth, hospital service changes and closures, and other variables. St. Luke's has been a consistent provider of charity care services for the South of Market community.

Summary and Conclusions

Our assessment of the health effects of the proposed transaction between St. Luke's and Sutter Health substantiates St. Luke's claim to being a unique San Francisco institution. The following summary of findings provides the basis for study conclusions.

History and Description of the Transaction

- St. Luke's Hospital has experienced significant financial difficulty in recent years and, with court approval, has withdrawn funds from the corpus of its restricted endowment to fund the hospital's operations. St. Luke's for several years has considered alternatives to retaining its current independent status.
- The proposed affiliation arises from the settlement of litigation between St. Luke's and Sutter Health. Under the Affiliation Agreement, St. Luke's Hospital will become an affiliate of Sutter Health, which will become the sole corporate member of the hospital corporation. The current St. Luke's Hospital board will remain in place. Sutter Health will appoint future board members from nominees offered by the St. Luke's board and will retain significant fiscal authority over St. Luke's. St. Luke's assets and liabilities will be consolidated under Sutter Health's Obligated Group.
- Sutter Health's Board of Directors contains a majority who also serve on local affiliate Boards, implying but not guaranteeing commitment to local affiliate decision-making.
- Sutter Health has assisted financially distressed hospitals and affirms its intention to provide resources to St. Luke's.
- The Affiliation Agreement and the Written Notice to the California Attorney General for approval of the transaction contain commitments and representations that Sutter Health and St. Luke's will support the provision of charity care at the hospital at "historic levels"; and that the Sutter Health financial commitments will enable St. Luke's to significantly increase programs and services and maintain, upgrade, and expand equipment and facilities.
- The Written Notice indicates that if approval is not granted, the impact on health care services would be negative because the proposed Affiliation would support the contributions made by St. Luke's to the health care services in the community.

Public Concerns Regarding the Affiliation

- Public testimony presented to the Attorney General and the San Francisco Health Commission and The Lewin Group's subsequent interviews revealed a number of concerns about the proposed affiliation and distrust of Sutter Health's intentions and motivations for assuming responsibility for St. Luke's. Concern also was expressed that the affiliation might result in decreased charity care, loss of local governance and community and employee input, and service closures.
- Several interviewees raised concerns regarding the reportedly over-funded St. Luke's pension plan, and stressed the importance of labor input into patient care staffing and of the St. Luke's board continuing to hold significant authority over the hospital.
- Proponents of the affiliation identified potential benefits of the transaction, including: injection of needed funds, retention of a mission-driven community hospital, improved staffing and morale, and enhanced quality and range of services. Proponents argued that all other possible alternatives had been explored and exhausted and that onerous conditions could doom the affiliation with Sutter Health.

St. Luke's Services

- St. Luke's is licensed for 257 beds. In fiscal year 1999 there was an average of 48.5 inpatients occupying medical-surgical, obstetrics, pediatric, and/or intensive care beds at the hospital. There also was an average of 25.2 acute psychiatric and 58.6 skilled nursing (including subacute) patients at the hospital. The hospital reported 929 live births and approximately 28,000 emergency room visits in 1999.
- In 1999, St. Luke's represented 4.5 percent of licensed beds in San Francisco, over 10 percent of the city's inpatient psychiatric capacity, 12 percent of emergency room visits in the city, and 25 percent of the emergency-room based urgent care.
- Under a contract with the San Francisco Department of Public Health, St. Luke's has been the largest private hospital provider of inpatient psychiatric care for Medi-Cal and indigent patients. St. Mary's Hospital recently announced its intention to close adult inpatient psychiatric services. This development increases the importance of maintaining access to the St. Luke's mental health beds for low-income San Francisco residents.
- The hospital operates 79 long-term care beds, including 60 for subacute and 19 for skilled nursing services. The skilled nursing beds admit patients through internal referrals from other St. Luke's inpatient services, while the subacute program receives patients who need ventilator care from all over northern California. Few other alternatives in the region currently exist for the subacute patients.
- St. Luke's Hospital received 10 percent of the ambulance patient transports provided by the city's Emergency Medical Services (EMS) in fiscal year 2000. Of the 28,000 St. Luke's emergency room visits, 53 percent were classified as urgent care (the highest proportion in the city). The emergency room's visit (and inpatient) volume has increased in recent months due to an increase in diversion status for the SFGH emergency room. Emergency room patients (including inpatients first seen in the ER) have generated two-thirds of St. Luke's reported charity care for the last several years.
- The St. Luke's Health Care Center clinics, operated by St. Luke's in a separate corporation that would become part of the Sutter Health Obligated Group, provided over 44,000 visits and employ physicians at several sites in the South of Market. St. Luke's Hospital underwrites approximately $2 million in annual clinic losses; this commitment represents one of the hospital's major community benefit services.
- Interviewees identified obstetrics, emergency room services, urgent care services, community clinics, and mental health services as "mission critical" services to be maintained under all scenarios. Numerous interviewees argued that allowing health care providers like St. Luke's to maintain flexibility in the services they provide was critical because of the fluidity of the health care market and changing health care needs in the area.
- The hospital's primary service area is comprised of six zip-codes in the South of Market area of San Francisco. Approximately two-thirds of St. Luke's inpatients and emergency room patients resided in this area in 1999. The South of Market area would be most affected by health impacts from the proposed affiliation.

- The South of Market primary service area has a high concentration of residents of Hispanic origin and of young persons below 20 years of age. This area is less affluent than San Francisco as a whole.
- In the South of Market primary service area, the hospital admitted a relatively high share of patients needing the following services: ventilator support, rheumatology, neonatology, neurology, gastroenterology, psychiatry, cardiology, pediatrics, and general medicine. The hospital provided a relatively low share of the area's inpatient surgical services.
- In 1999, the hospital's share of the primary service area's Medi-Cal services was significantly higher than its share of services provided to Medicare or privately insured patients. A comparatively low number of Medi-Cal patients left the South of Market area for inpatient care, and only 11 percent of Hispanic Medi-Cal funded residents of the South of Market were discharged from hospitals other than St. Luke's or SFGH. "Outmigration" from the area was particularly low for obstetrics, psychiatric, neonatology, and trauma services.
- There is some indication that community physicians would be affected by the hospital's closure, as several admit patients only to St. Luke's. If St. Luke's closes, some may leave the neighborhood as well, potentially reducing access to primary care physicians for community members.
- Closure of St. Luke's Hospital was unanimously expected to have a significant negative impact on the health of the community. Closure was expected to pose a substantial problem for emergency, psychiatric, and indigent care services in San Francisco.

St. Luke's Charity Care and Community Benefits

- St. Luke's Hospital's principal community benefits services include traditional charity care, unreimbursed cost from serving Medi-Cal patients, and subsidies provided to the SLHCC clinics.
- St. Luke's is almost universally perceived as a charitable institution, a major provider of charity care services, and an integral part of the San Francisco safety net. St. Luke's continued emergency room and charity care presence is viewed as critical in the context of staffing shortages, frequent emergency room diversions at SFGH, and a high proportion of Hispanic patients who rely greatly on St. Luke's and are unlikely to seek care outside of the South of Market area of San Francisco. Concern was expressed that Sutter Health would reduce these commitments or divert charity care from its other Bay area hospitals to St. Luke's.
- Specifying a strict dollar amount or percentage of revenues for charity care at St. Luke's was often mentioned as a potential condition to affiliation, through some expressed concern that this could render St. Luke's vulnerable to "dumping" by other hospitals.
- The Emergency Room is a major point of access for indigent patients and the major source of charity care for St. Luke's. In fiscal year 2000, patients arriving at the

hospital's emergency room generated $3.4 million of the $5.1 million in charity care, or 67 percent. This proportion has been stable from fiscal years 1997 through 2000.

- These dollar values are measured in gross patient charges rather than the actual hospital cost of providing care to charity patients. While generally accepted, this accounting methodology creates measurement problems when comparing hospitals and evaluating trends in the amount of charity care provided. Several states and associations measure charity care on the basis of cost and/or charity care patient volume statistics.

Based on these findings, we conclude that:

- St. Luke's is the only private hospital in an area of San Francisco characterized by a marked multi-racial/multi-ethnic population, many of whom are poor and unlikely to travel outside the area for health care.
- St. Luke's provides substantial charity care and Medi-Cal services.
- The hospital has a longstanding history of providing outpatient care in community clinic settings.
- The hospital is a principal private provider of inpatient psychiatric services under contract to the San Francisco Health Department and the only provider of "subacute care" services in the city.
- The St. Luke's emergency room is an important resource for indigent patients and is the closest alternative when the SFGH General is on diversion.
- St. Luke's has been operating under deficit financing for several years, yet has maintained a substantial load of Medi-Cal and charity patients.
- The Board has solicited and considered offers of assistance to St. Luke's but not accepted alternatives that appear to compromise the hospital's ability to remain a mission-oriented, acute care facility.
- St. Luke's and Sutter Health have represented their intention to increase services and maintain charity care at historic levels.

Finally, The Lewin Group concludes that meaningful alternatives to the proposed transaction have not appeared to this point in time, thus:

- Continuation as an independent hospital is not financially feasible, especially in light of seismic safety requirements on all California hospitals;
- Hospital closure, despite St. Luke's proximity to SFGH and a history of excess bed capacity in San Francisco, is not desirable in terms of the tradeoffs implied for the population currently served;
- Proposed affiliations with other parties have not yielded terms that St. Luke's Board of Directors found acceptable;
- The proposed affiliation continues the involvement of the St. Luke's local board;

- St. Luke's presence and operation as both an acute care hospital and as the sponsor of well-utilized ambulatory services affect the health and the access to health care of tens of thousands of San Franciscans; and
- St. Luke's fate and future are of intense interest to many parties and there is concern about whether the affiliation with Sutter Health would adversely affect the provision of charity care and of needed health care services by St. Luke's Hospital.

These conclusions imply that approval by the California Attorney General of the proposed transaction is warranted but that conditions responsive to the concerns of the many parties potentially affected and consistent with representations and commitments made by Sutter Health and St. Luke's are also justified.

Proposed Conditions

In order to reflect the representations and commitments of the parties to the transaction, the following are minimum conditions for the transfer of control of St. Luke's Hospital to Sutter Health.

1. Existing services shall be maintained at St. Luke's Hospital as follows.
    - Sutter Health and St. Luke's Hospital shall maintain an acute care hospital at the current St. Luke's Hospital site licensed by the California Department of Health Services for five years from the date control of St. Luke's Hospital is transferred to Sutter Health (the transfer date).
    - St. Luke's Hospital shall maintain an emergency room service and an ICU on the current hospital site at current or greater licensure levels for five years from the transfer date.
    - St. Luke's Hospital shall maintain the clinics operated by SLHCC at current or greater service levels for five years from the transfer date. St. Luke's Hospital shall maintain access to care provided by the SLHCC clinics consistent with policies and procedures in place on January 1, 2001.
    - St. Luke's Hospital shall continue to maintain linguistically and culturally appropriate staff.
    - St. Luke's Hospital shall negotiate in good faith a continuation of its existing contract with the City and County of San Francisco for Medi-Cal and indigent mental health services provided to patients who are the responsibility of the Department of Public Health so that such services can be provided for at least five years from the transfer date.
    - For five years from the transfer date, St. Luke's Hospital shall maintain services for skilled nursing patients for whom alternatives are not available in San Francisco County.
    - For five years from the transfer date, St. Luke's Hospital and Sutter Health shall maintain accreditation for St. Luke's Hospital with the Joint Commission on Accreditation of Healthcare Organizations (JCAHO).

2. Sutter Health and St. Luke's Hospital shall maintain the following commitments to providing charity care.

   - For five years from the transfer date, St. Luke's Hospital shall maintain its historic level of charity care as set forth in its reports to OSHPD for 1995-1999 and shall continue its charity care policies and procedures that were in place on January 1, 2001.
   - There shall be no reduction in the charity care commitment at California Pacific Medical Center or Davies Medical Center for five years from the transfer date.