The Regents of the University of California

COMMITTEE ON HEALTH SERVICES
February 19, 1998

The Committee on Health Services met on the above date at UCSF - Laurel Heights, San Francisco.

Present: Regents Atkinson, Bagley, Brophy, Davies, Gonzales, Khachigian, Leach, and Preuss

In attendance: Regents Bustamante, Chandler, Connerly, Hotchkis, Johnson, Lee, Levin, McClymond, Nakashima, Parsky, and Soderquist, Regents-designate Miura and Willmon, Faculty Representative Weiss, Secretary Trivette, General Counsel Holst, Treasurer Small, Provost King, Senior Vice President Kennedy, Vice Presidents Gomes, Gurtner, and Hopper, Chancellors Dynes and Vanderhoef, Vice Chancellor Bainton representing Chancellor Debas, and Recording Secretary Bryan

The meeting convened at 3:50 p.m. with Committee Chair Davies presiding.

1. **APPROVAL OF FINANCING FOR UCSF STANFORD HEALTH CARE CONSTRUCTION PROJECTS AND RESTRUCTURING OF EXISTING DEBT**

The President recommended the approval of financing contemplated by UCSF Stanford Health Care in the amount of approximately $338.4 million, of which approximately $103.8 million relates to facilities at UCSF-Mt. Zion and approximately $234.6 million relates to facilities at Stanford Medical Center and Lucile Salter Packard Children's Hospital.

It was recalled that at the September 1997 meeting, The Regents authorized the execution of agreements related to the operation of UCSHC, a California non-profit public benefit corporation created in January 1997, to merge the clinical activities of UCSF Medical Center (UCSFMC), including Mt. Zion (UCSF-Mt. Zion) and the faculty practice plan of the UCSF School of Medicine with the clinical activities of Stanford Health Services (SHS) and Lucile Salter Packard Children's Hospital (LSPCH) and the faculty practice plan of the School of Medicine at Stanford University. The merger was operational on November 1, 1997, with the initiation of clinical activities of UCSHC in facilities leased from SHS/LSPCH and UCSF-Mt. Zion. The bylaws of UCSHC reserve certain matters to The Regents and the Trustees of Stanford (the "Members"), including "the power to approve any borrowing of the corporation in excess of $100 million in any single transaction . . . " (Art. III, §10(b) of the Bylaws of UCSHC.)

During discussions preceding the merger, it was anticipated that debt relating to UCSF-Mt. Zion facilities leased to UCSHC would be repaid or defeased. Accordingly, on October 31, 1997, approximately $45 million of debt related to UCSF-Mt. Zion facilities was repaid or defeased using reserves of UCSF Medical Center. On November 1, UCSHC assumed approximately $117 million of SHS debt and guaranteed $44 million of debt of LSPCH.

Proposed Financing Transaction

In March 1998, UCSHC proposes to issue approximately $294.4 million in bonds and to restructure $44 million in LSPCH debt. The bonds will be issued in two series: Series A bonds ($103.8 million) will be associated with assets and previously existing debt at the UCSF-Mt. Zion site; Series B bonds ($190.6 million) will be associated with the assets and previously existing debt at the Stanford site. Consistent with the dissolution provisions of the Consolidation Agreement of UCSHC, this separate series permits each university to assume or defease the series debt associated with the assets of its site, subject to compliance with financial tests under the master indenture.

The proposed transaction accomplishes several important objectives (financing amounts in parenthesis):

- Finance two facilities projects: the ambulatory care center at Stanford ($47 million) and the cancer center at UCSF-Mt. Zion ($33 million).

- Finance already-approved projects from the annual capital budgets ($25 million at each site, total $50 million).

- Achieve approximately $4 million present value savings from lower long-term interest rates by refinancing existing SHS debt ($117 million).

- Recapitalize the acquisition cost related to UCSFMC debt repayment ($45 million).

- Simplify the legal structure of its debt by restructuring LSPCH debt ($44 million) into the master indenture.

The total size of the transaction (including both the bond issue and the restructuring of existing debt) is approximately $338.4 million (including approximately $2.4 million for issuance costs), which is essentially all of UCSHC's long-term debt. Of this amount, $130 million represents new money borrowed for construction; the remaining $206 million refinances and restructures debt that existed on SHS's and UCSFMC's balance sheets prior to the merger.

There is no new or incremental capital spending included in the bond issue that was not previously approved by either The Regents or the Trustees. The two facilities--the ambulatory care center at Stanford and the cancer center at UCSF-Mt. Zion--and other capital projects to be financed had already been approved at the two medical centers through their respective budgeting and governance processes before November 1, 1997. The two facilities and other capital spending were also included in the financial analyses conducted as part of the merger discussions.

Cancer and Ambulatory Care Centers

The most important part of the bond issue is financing for the ambulatory care center at Stanford and the cancer center at UCSF-Mt. Zion. The ambulatory care center, half of which is a cancer center and the other half an ambulatory surgery and treatment center, was approved by the SHS Board in 1997. The Mt. Zion cancer center was approved by The Regents in 1992.

As noted earlier, both projects were included in business case analyses prepared during consideration of the merger. Extensive programmatic, market, and financial feasibility studies have been prepared for the two buildings. The UCSHC Board has reviewed these plans and voted at its January 1998 meeting to proceed with the projects, subject to Member approval for the financing.

It is anticipated that in the next several months the Office of the President will bring to The Regents additional items for action that are necessary to finalize the capital improvements project at the UCSF-Mt. Zion cancer center. These items would include a groundlease with UCSHC for the UCSF-Mt. Zion site and an updated design review for the project.

The ambulatory care center has a total project cost of $117 million, which includes bond financing of $47 million, fundraising of $50 million, and funding from annual capital budgets of $20 million. The cancer center at UCSF-Mt. Zion has a total project cost of $43 million, with bond financing of $33 million and targeted fundraising of $10 million. Under the Consolidation Agreement, fundraising activities remain within the two parent universities.

The two cancer centers are not duplicative but rather complement each other and represent a critical step toward developing an integrated cancer program. The goal is to become the National Cancer Institute (NCI)-designated "Cancer Center of Northern California at UCSF and Stanford." The benefits of becoming an NCI-designated comprehensive cancer center include the most advanced care for patients; a significant increment to NCI research funds for each school of medicine; and added prestige and recognition which will increase clinical trials, attract patients, and enhance fundraising. To achieve NCI cancer center designation, the schools of medicine at Stanford and UCSF must build collaborative, multidisciplinary clinical programs; collaborative clinical trials, translational, population, and fundamental science programs; and a common database and information system. The path to this goal begins with UCSF's 1998 application to become an NCI cancer center and the identification of a clinical program director who will lead the development of interschool collaborative clinical programs. At the same time, the two schools will seek an individual to build collaborative clinical science programs. As soon as a successful track record of joint programs is demonstrable, the UCSF NCI cancer center will apply for renewal as the Cancer Center of Northern California at UCSF and Stanford.

The two proposed buildings are needed to accommodate growth in cancer care as well as to consolidate clinical services in adjacent space. They will also support recruitment of faculty for new cancer research facilities at both UCSF and Stanford. Most importantly, the cancer centers will provide an environment and service levels appropriate for the most advanced care. Patients undergoing chemotherapy and radiation therapy make frequent visits and require readily accessible sites. UCSF's and Stanford's current market shares in cancer reflect geographic proximity and major transportation routes. There is relatively little overlap in markets for the two medical centers on a stand-alone basis, while on a combined basis UCSHC's cancer market area spans the 11-county Bay Area (from which over 70 percent of the organization's cancer patients come) and beyond. The size of the combined market, the nature of cancer treatment, and the 40-mile distance between the two locations make two cancer center sites the most appropriate response to the needs of cancer patients.

Other Capital Projects

As indicated, $50 million of the debt is for other capital projects at UCSF and Stanford ($25 million each), which is less than the total expenditures already approved for capital projects at each site. Projects for San Francisco include clinical equipment, including a gamma knife replacement, a biplane neuro-angiographic room, replacement of radiology equipment, and nuclear medicine gamma cameras for the Radiology Department. Equipment projects for Stanford include a linear accelerator replacement, replacement of equipment in a catheterization laboratory, replacement equipment for a computerized axial tomographer for tumor localization, a cardiac magnetic resonance imager, hospital beds, and wireless communication. Among the infrastructure capital projects approved for San Francisco are the addition of eight critical care beds, an upgrade of the Long Hospital elevators, Mt. Zion radiology expansion and renovation, and elevator upgrade for the ambulatory care center. At Stanford, the approved infrastructure capital projects include remodeling of the ultrasound suite, medical records renovation, renovation of the outpatient physical therapy space, and certain capital improvements in order to comply with accreditation requirements. Finally, there are certain capital improvements which have been approved for information systems.

Debt Structure

The $294 million of bonds proposed as part of this transaction will be fixed-rate tax-exempt bonds issued through the California Health Facilities Financing Authority, with an anticipated final maturity of 2031. Security for the debt is a revenue pledge of the Obligated Group; that is, the debt is secured by the revenues of UCSHC. Both bond series are issued under supplemental trust indentures of the Master Trust Indenture originally issued for SHS debt in 1990 and assumed by UCSHC in November 1997.

The $44 million of debt from LSPCH that makes up the remainder of the transaction was originally issued as variable rate tax-exempt debt that was converted into a 6.22 percent fixed-rate position through an interest rate swap. The terms of this swap make it very expensive to undo and uneconomical to refinance into fixed-rate debt, despite the lower interest rates now in the bond market. Thus the proposed transaction will convert the underlying variable rate debt into an obligation of master indenture, leaving the interest rate swap in place. Because UCSHC is the sole member of the LSPCH, this debt is already on its balance sheet. In connection with the issuance of the bonds, the documents governing this debt will be amended to simplify the legal structure of the debt without changing the accounting or economic substance.

Financial Impact

As a result of this bond issue, UCSHC will have a debt to capitalization ratio of approximately 28 percent, which remains very conservative. Pro forma debt service coverage (estimated at approximately 6 times debt service) and liquidity (measured by days cash on hand) are very strong. By taking advantage of the acquisition financing tax treatment available if the transaction is completed within six months of the merger date, UCSHC will secure present value savings of approximately $4 million from lower interest rates now in the bond market by refinancing the SHS debt, while gaining the option to advance the refunding of this debt sometime in the future should that be advantageous.

Withdrawal Provisions

The Consolidation Agreement creating UCSHC provides for dissolution of that corporation under certain circumstances. If UCSHC were to be dissolved, this structure of separate series permits either university to assume the series debt associated with its site's assets, subject to compliance with financial tests in the master indenture, or to defease its series debt. In a defeasance, an irrevocable escrow is established to pay the principal and interest on the defeased debt as the payments become due. The escrow can be funded using cash reserves of the medical center whose debt is being defeased or by issuing new taxable or tax-exempt debt, depending on federal tax regulations at that time. Under either an assumption or a defeasance option, the assets of the medical center are removed from the control of the master indenture. If, upon dissolution, UCSF were unable to meet the financial tests and did not defease or pay off the debt, The Regents would remain subject to the master indenture and the debt obligations thereunder.

Upon motion duly made and seconded, the Committee approved the President’s recommendation and voted to present it to the Board.

2. **APPROVAL OF AMENDMENTS TO THE UCSF STANFORD HEALTH CARE BYLAWS CONCERNING BOARD MEETINGS, COMMITTEES, AND APPOINTMENT OF EX OFFICIO UC DIRECTOR**

The President recommended approval of the following changes to the bylaws of UCSF Stanford Health Care:

deletions shown by strikeout, additions by shading

BYLAWS
OF
UCSF-STANFORD HEALTH CARE

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ARTICLE III
MEMBERSHIP

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Section 12. Powers of the Members.

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(c) The incurrence of indebtedness containing any conditions, covenants or other terms or provisions that may restrict the operation of Section 9.2 of the Consolidation Agreement entered into by the University of California and Stanford University as of November 1, 1997 in any manner, whether by third-party consent requirements or otherwise, shall require the written approval of the Members.

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ARTICLE IV
BOARD OF DIRECTORS

Section 1. Board of Directors.

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(b) Composition.

(1) Initial Board. The initial directors shall consist of the ten persons elected by the incorporator (the "Initial Elected Directors") and the persons holding the following positions, who shall serve ex officio with vote ("Initial Ex Officio Directors"): the Dean of the UCSF School of Medicine; the

Dean of the Stanford University School of Medicine; the President of Stanford University; the President of the University of California; the Chancellor of UCSF; the President of the corporation and the Chief Medical Officer of the corporation (collectively, the "Initial Directors"). Notwithstanding any provision of these Bylaws to the contrary, for so long as the Dean of the UCSF School of Medicine is also the acting Chancellor of UCSF or such offices are otherwise held by one and the same person, whether in an acting or permanent capacity, there shall exist a vacancy in the number of Initial Ex Officio Directors, which may be filled as follows: The University of California, acting as the UC Class Member, may appoint any individual otherwise qualified under these Bylaws to serve as a Director to fill such vacancy in the Initial Ex Officio Directors temporarily, such appointment to expire automatically when the offices of Dean of the UCSF School of Medicine and of Chancellor of UCSF shall be held by different individuals. Such temporary appointee shall be treated as an Initial Ex Officio Director for all purposes of these Bylaws. In addition, the President of the University of California may be replaced as an initial Ex Officio Director by action of the Regents Class appointing, to serve in the President's stead, a vice president of the University of California selected by the Regents Class to serve for a term coincident with his term as vice president or for such term as determined by the Regents Class; provided, however, that if the term of that vice president ends by reason of expiration of this term as vice president, resignation or otherwise, the then President of the University of California shall automatically be restored to the board unless the Regents Class designates another vice president to serve in his stead.

(2) Subsequent Boards. Upon expiration of the terms of the Initial Elected Directors, as specified in Article IV, Section 3, and thereafter, the board of directors shall consist of 17 directors, seven of whom shall serve ex officio with vote ("Ex Officio Directors") and ten of whom shall be elected by the Members ("Elected Directors"). The Ex Officio Directors shall consist of the persons occupying the following offices from time to time: the Dean of the UCSF School of Medicine; the Dean of Stanford University School of Medicine; the Chancellor of UCSF; the President of Stanford University; the President of the University of California; or a vice president of the University of California selected by the Regents Class to serve in lieu of the said President for a term coincident with his term as vice president, or for such term as determined by the Regents Class; provided, however, that if the term of the vice president ends by reason of expiration of his term as vice president, resignation or otherwise, the then President of the University of California shall automatically be restored to the board unless the Regents Class designates another vice president to serve in his stead; the President of the corporation; and the Chief Medical Officer of the corporation. The ten Elected Directors shall consist of: three individuals elected by the UC Class (the "UC Directors"), two of whom at the time of their election are Regents, and one of whom shall be a member of the faculty of UCSF School of Medicine; four

individuals elected by the Stanford Class (the "Stanford Directors"), at least two of whom at the time of their election are Trustees, a third person who may but need not be a Trustee and a fourth person who is a member of the faculty of the Stanford University School of Medicine; and three other persons who are not employees of either University or of the corporation, Regents, Trustees or "interested persons" within the meaning of this Article IV, Section 1(c). Directors shall serve without compensation for service in their capacity as directors.

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ARTICLE V
MEETINGS AND COMMITTEES OF THE BOARD OF DIRECTORS

Section 1. Place of Meetings.

Meetings (whether regular, special or adjourned) of the board of directors shall be held at the principal office for the transaction of business of the corporation or at such other place which is freely accessible to the public as may be designated from time to time by the board of directors.

Section 2. Regular Meetings.

Regular meetings of the board of directors~~, of which no notice need be given,~~ may be held at such time and place as shall be designated by the board of directors. A schedule of regular meetings will be established by the directors and distributed to the directors within 30 days after the annual meeting. Agendas for such meetings shall be posted in advance of the meeting as required by law.

Section 3. Special Meetings.

Special meetings of the board of directors may be called at any time by the Chair or by any two or more directors. Due notice of any special meeting shall be given to the directors by mail at least four days before the meeting or, if by personal delivery, facsimile or telephone, at least ~~48~~ 72 hours before the meeting. The recital by the Secretary in the minutes that due notice was given to the directors shall be sufficient evidence of the fact. In addition, the agenda for such a meeting shall be posted as required by law.

Section 4. Quorum: Action by Vote.

At any meeting of the directors, ~~13~~ a majority of the directors then in office shall constitute a quorum. The affirmative vote of nine directors present and voting at a meeting at which a quorum exists shall decide any question, including the election of officers, unless otherwise provided by law, the Articles of Incorporation or these Bylaws. The directors present and voting at a duly called or held meeting at which a quorum initially exists may continue to transact business notwithstanding the withdrawal of enough directors to leave less than a quorum if any action thereafter taken is approved by at least the number of directors necessary to carry a matter.

Section 5. Adjournment.

Whether or not a quorum exists, a majority of the directors present and voting at a meeting may adjourn the meeting to another time and place. If the meeting is adjourned for more than 24 hours, notice of such adjournment shall be given prior to the time of the adjourned meeting to the directors who were not present at the time of the adjournment. In addition, a notice of adjournment shall be posted in the same manner as the agenda (if any) for the meeting was posted.

Section 6. Committees.

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(e) Proceedings of Committee Meetings. Determinations concerning the procedures for the conduct of meetings of the committees shall be made by the Chair of the committee, consistent with the Charge of the Committee, the provisions of these Bylaws and applicable law.

Section 7. Telephone Meetings.

Members of the board of directors may participate in a meeting of the board of directors or a committee by means of a conference telephone or by any other means of communication by which all persons participating in the meeting and the public if required by statute are able to hear one another at the same time. Participation in a meeting by such means shall constitute presence in person at the meeting. At least one location, specified in the posted agenda (if any) for such a meeting shall be a principal place of business of the corporation. Actions at such meetings shall be by roll-call vote.

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ARTICLE VI
OFFICERS OF THE CORPORATION

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Section 4. Secretary.

The Secretary shall keep, or cause to be kept, the minutes of all meetings of the board of directors and of the Members and shall perform such other duties as the board of directors may prescribe. Separate minutes shall be kept of any closed sessions. The Secretary shall report to the President. The Assistant Secretary, if any, shall act in the absence of the Secretary and perform such other duties as the Secretary or the President of the corporation may prescribe. The Secretary and Assistant Secretary, if any, shall be subject to removal by the President of the corporation.

It was recalled that Senate Bill 1350, which became applicable to UCSF Stanford Health Care on January 1, 1998, sets forth requirements for open meetings, written and posted agendas, and accessibility and copying of corporate records which constitute public records. It is necessary to conform the bylaws to these statutory requirements.

Article V, §1 above addresses an addition to the Health and Safety Code of the State of California that requires that meetings of the board of directors be conducted in a place that is freely accessible to the public. Article V, §4 will reduce from 13 to 9 the number of directors necessary for a quorum of the board of directors. The number 13 was selected for the original bylaws so that it was clear that representatives of both The Regents and the Stanford Trustees would be at a board meeting where a quorum was present to take action; however, it has been difficult to have 13 of the 17 directors present at each board meeting. The bylaws will still require that 9 directors be present and voting at a meeting to decide any question within the jurisdiction of the board. Article IV, §1 will permit a vice president to act in the place of the President if The Regents, as a member of the corporation, so determine. The term will be no longer than the term of office of the vice president or for a term as determined by The Regents Class. The Vice President--Clinical Services Development has been attending meetings of the board of directors, but does so without a vote. In order to provide for a greater presence of the University, the bylaws will be amended to permit a vice president both to vote and to attend in place of the President. Article III, §12 requires The Regents and Stanford Trustees to approve indebtedness if the debt contains any conditions, covenants, or other terms or provisions which affect the plan of dissolution. The plan of dissolution provides for an orderly process whereby the assets of The Regents are returned to The Regents, the Trustees' assets are returned to the Trustees, and available liquid assets are used to pay liabilities not transferred to one of the members. In addition, assets acquired or constructed by UCSF Stanford Health Care, including projects financed by the bonds, that are located on the real property leased from each university will be returned to that university.

Upon motion duly made and seconded, the Committee approved the President’s recommendation and voted to present it to the Board.

The Committee went into Closed Session at 3:55 p.m.

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The meeting adjourned at 4:00 p.m.

Attest:

Secretary