

The Regents of the University of California

COMMITTEE ON HEALTH SERVICES

September 17, 1997

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

Members present: Regents Atkinson, Brophy, Clark, Davies, del Junco, Gonzales, Khachigian, Leach, Preuss, and Sayles

In attendance: Regents Connerly, Johnson, Lee, Levin, McClymond, Montoya, Nakashima, Parsky, and Soderquist, Regents-designate Miura and Willmon, Faculty Representatives Dorr and Weiss, Secretary Trivette, General Counsel Holst, Treasurer Small, Provost King, Senior Vice President Kennedy, Vice Presidents Darling, Gurtner, and Hopper, Chancellors Carnesale, Debas, Dynes, Orbach, and Wilkening, and Recording Secretary Bryan

The meeting convened at 10:05 a.m. with Committee Chair Davies presiding.

1. **UCSF-STANFORD MERGER: SUMMARY OF RATIONALE FOR MERGER OF UCSF-STANFORD HEALTH SERVICES CLINICAL ACTIVITIES**

It was recalled that at the November 1995 meeting of The Regents, UCSF leadership first informed The Regents that UCSF had initiated preliminary discussions with Stanford regarding the feasibility of collaboration in patient care and some areas of academic programming. Since that meeting, there have been a total of ten items brought to The Regents that address merger issues and activities.

Both the Committee on Health Services and the full Board of Regents have discussed the rationale, costs, and benefits of the merger for the UCSF campus. Most recently, at both the regular and a special meeting of The Regents in November 1996, the Third Party Review Team provided the Board with an in-depth analysis of the financial viability of the merger.

Two central principles have been the driving force for discussions and actions related to the merger:

- Preservation of the viability of UCSF's clinical enterprise that provides a significant source of financial and strategic support for the academic and research missions.

- Protection of and support for the academic mission of the UCSF School of Medicine, as well as those of the Schools of Nursing, Pharmacy, and Dentistry

Principle One: Preservation of the Clinical Enterprise

In November 1995, Chancellor Martin recognized the academic and research strength of both UCSF and Stanford, but pointed out that:

“The clinical enterprises of the two universities, however, are imperiled. Clinical cost savings and economies of scale would provide increased support for education and research as well as provide better access to care at the cutting edge of health services innovation. ..while the impetus (for the merger) had been an economic one, there are public interest aspects to consider as well. ”

At the March 1996 meeting of the Committee on Health Services, Chancellor Martin recalled that:

“The collaboration idea came about because the growth of managed care has caused a decline in the use of hospital and physician services, and insurers of managed care plans are consolidating in the face of demands from employers concerning health care insurance.. .cross subsidies that were once used to generate revenues from clinical activities for educational and clinical research are falling. In seeking to examine whether more can be accomplished together than apart, they (UCSF) have engaged in testing the following hypotheses:

- A. That their combined strengths will guarantee a critical mass of faculty and patients for teaching in both small specialty programs and diverse larger clinical training opportunities.
- B. That they can develop and maintain a viable market position as the system of choice for complex care and specialized expertise; that they will facilitate application of basic and health services research to more cost-effective clinical care of the highest quality.
- C. That they can create a special focus on the health needs of children.
- D. That they can achieve operating economies of scale through cost reductions in corporate administration and in clinical and academic programs.
- E. That they will improve their ability to compete for volume for managed care plan, integrated delivery systems, and capitated groups.

- F. That they can reduce duplication in investment for capital needs, high-priced faculty, and high-tech equipment.
- G. That clinical consolidation will facilitate significantly greater collaboration in education and research.”

In May 1996, the UCSF campus provided The Regents with the Newco Business Analysis that included a five-year historic combined financial statement for UC San Francisco, Stanford Health System, and Lucile Salter Packard Children’s Hospital.

The discussion in this item pointed out the role that a strong clinical enterprise plays in supporting the academic mission. The item stated:

“The combination of administrative and clinical cost reductions and increased clinical volume, when offset by merger costs, -creates the potential for overall improvement in the bottom line of the consolidated enterprise of \$256.6 million between 1997 and 2000. Such improved results would not be possible for either the UCSF or Stanford clinical enterprise to achieve on its own....”

“The most compelling reason for the merger is the long term benefit to the community that will result from combining highly specialized clinical resources to improve the health of adults and children, improve teaching and research, and assure the economic viability of academic medicine in Northern California. By merging their hospitals and the related services of the faculty clinical practices into a single, more cost-effective clinical enterprise, the parties believe that they will be better able to produce superior outcomes and be in a stronger advocacy position for graduate medical education. ”

Chancellor Martin stated in June 1996 that:

“ . . .the Board of Regents has witnessed increasing evidence of pending economic disarray in its medical centers. Changes in the marketplace threaten the future of academic medicine. It is a challenge to find viable solutions for the tightening grip of a chaotic managed care system that considers cost first.. . the long-term benefits of the merger will be to improve the health of children and adults and assure the economic viability of academic medicine in this region.”

At the same meeting, UCSF Medical Director Bill Kerr noted that:

“UCSF must engage with others to assure its continuing competitiveness. If an agreement is not reached on the proposed Stanford merger, it is improbable

that a merger will be possible with another organization. From the vantage point of assuring continued support of the academic mission, it is clear that no potential partner offers the shared values that Stanford offers. If the merger does not occur, UCSF and Stanford will continue to be vigorous competitors in the regional marketplace. .Not only is UCSF buffeted by the highly competitive California marketplace, it suffers from the absence of public policy to support indigent health care delivery and medical education. He (Kerr) was certain, however, that the risks UCSF faces in the future are real. Best-case projections in a stand-alone scenario yield an operating margin of between one and two percent. Its clinical and academic excellence cannot be maintained in the long run with such a modest operating gain. The improved financial performance achievable by the merged entity would allow UCSF to face its uncertain future with a much higher degree of confidence.”

At the July 1996 meeting of The Regents, President Richard Atkinson stated:

“This is a rare and exciting opportunity that deserves to be evaluated fully. The proposal (i.e., the merger) is tailored to address the fierce market forces confronting these two premier health sciences institutions.”

The focus of the November 8, 1996 special meeting of The Regents was a discussion of the Third Party Review report. The overall goal of the third party review process was to render an objective and independent opinion on the following three questions:

- Is this a sound business decision for the University of California?
- Has the analysis to date been sufficient to determine the business viability of the merger?
- What, if any, further analysis should be conducted?

The conclusion of that review was that “the proposed merger of clinical services is a sound business decision for the University of California.”

Principle Two: Protection of and Support for the Academic Mission.

In November 1995, Chancellor Martin observed that:

“The emerging reorganization of health care delivery systems in the nation, the state, and especially in the Bay Area, as well as the entry of the for-profit sector in the market place, present challenges to UCSF’s academic mission that would not have been anticipated six months ago.”

At the May 1996 meeting of the Committee on Health Services, Dean Haile Debas summarized the academic advantages of a UCSF and Stanford merger of clinical services:

“Truly outstanding medical schools cannot exist without comparably outstanding medical centers. . .The fundamental mission of medical schools and academic medical centers is being threatened. . .The proposed merger of the clinical enterprises of UCSF and Stanford University offers the best hope to ensure the future success of these two schools of medicine, and the preservation of their core functions of education, research, and clinical care. This merger will stabilize training programs at both universities by maintaining the critical mass of students and faculty necessary for excellence.

The proposed merger will enable the two universities to: (1) maintain financial support for their academic missions, including recruitment and retention of the best faculty, students, and residents; (2) sustain an adequate patient base for education; (3) significantly improve graduate education, continuing medical education, and also public education; and (4) create opportunities that will ensure vibrant clinical research and winning collaborations among basic scientists and between universities and the private sector, especially the pharmaceutical industries. ”

At the June 1996 meeting of the Committee on Health Services, the UCSF campus provided The Regents and the public with detailed answers to a number of questions regarding the merger. As related to undergraduate and graduate medical education, Dean Debas described the benefits of the merger including:

“ . . .expanded opportunity for housestaff rotations . . .opportunity to create new training programs. . .and the new merged clinical entity will have the capacity to be a strong partner to health maintenance organizations with an expanded opportunity to secure appropriate primary care teaching sites for students.”

Item 402 of the July 1996 meeting of the Committee on Health Services listed the potential benefits and risks to UCSF and the UC System of the Proposed Merger. The discussion of both benefits and risks addressed the two principles guiding the merger and demonstrated the complex financial and strategic relationship that exists between an academic health center’s clinical enterprise and academic mission. More specifically, approval of this action item established the specific and primary purpose of Newco:

“ . . .to provide competitive health care services in an environment suitable for the highest quality medical education and research.”

In a letter to The Regents dated August 1997, UCSF Chancellor Debas stated:

“The merger is a long-term strategy to ensure the survival of our two academic health centers. Much is at stake and much has been shared between the two institutions. Joint meetings have been characterized by remarkable candor, trust and enthusiasms...If we do not go forward with this plan, we not only stand to lose our current position as a world leader in academic medicine but our future survival will be at greater risk than when we first began these discussions.”

Conclusion

In conclusion, in all meetings of The Regents regarding the merger, there have been two principles that have supported the rationale for the merger, as well as a recognition that these principles are not mutually exclusive because of the interdependence of the clinical enterprise and the academic and research missions of the University. The Third Party Review report of November 8, 1996 stated the rationale for the proposed merger as follows:

“To continue to thrive as a premier academic medical center in the highly competitive Bay Area marketplace, UCSF Medical Center is pursuing a merger with Stanford’s clinical enterprises to become increasingly cost competitive, to share in expensive investments required to maintain each institution’s leading edge clinical care, and to improve its ability to assume risk for defined patient populations in order to attract and retain managed care contracts and access to the specialty referral market. ”

At the November 13, 1996 meeting of the Committee on Health Services The Regents authorized the formation and capitalization of Newco. At that time, President Atkinson stated that he:

“...believed that the union of UCSF and Stanford clinical activities has the potential to enrich the teaching and research programs of the two universities, to create extraordinary opportunities to move research discoveries to the bedside, and to provide a stronger financial underpinning for the clinical enterprise.”

In his remarks to the Board of Regents at the June 1997 meeting, President Atkinson concluded:

“I have said on more than one occasion that UCSF, strong as it is, must join with another regional partner to compete successfully in the marketplace of the future. Equally important, the merger will not just improve UCSF’s competitive position but will generate opportunities to offer new and innovative teaching, research, and patient care programs.”

Discussion of this item was undertaken after presentation of the next item.

2. **UCSF-STANFORD MERGER: AUTHORIZATION TO EXECUTE AGREEMENTS**

The President recommended that he, in consultation with the General Counsel and the Vice President for Clinical Services Development, be authorized to execute agreements necessary to effectuate the merger between the clinical enterprises of the University of California, San Francisco (UCSF) and Stanford Health Services (SHS).

It was recalled that at the November 1996 meeting of the Board of Regents, The Regents were told that the University of California (UC) and Stanford University (SU) would negotiate the final key agreements with the management of UCSF Stanford Health Care (USHC). These negotiated agreements would then be brought to The Regents for approval.

At the June 1997 meeting of the Committee on Health Services, The Regents were provided with information regarding the status of the transaction to date.

Summary of Key Principles Negotiated Between USHC and Its Members

The following is a summary of the key principles that have been negotiated for each of the merger agreements:

- Consolidation Agreement between UC and SU
- Assignment and Assumption Agreement between UC and USHC
- Professional Services Agreement and Affiliation Agreement--UCSF School of Medicine
- Affiliation Agreement--UCSF Schools of Dentistry, Pharmacy, Nursing
- Lease Agreements for facilities
- Workforce Agreements

Consolidation Agreement Between UC and SU

In the Consolidation Agreement (the underlying merger document) UC, SU, and SHS agree that:

- A. Mofitt Long Hospitals, UCSF Mount Zion Hospital, the clinical practices of UCSF School of Medicine and related multi-specialty clinics, Stanford University Hospital, Lucile Salter Packard Children's Hospital (LSPCH), and the clinical practices of Stanford University School of Medicine be transferred to USHC.
- B. Langley Porter Psychiatric Hospital remains with the UCSF campus.

- C. Audited financial statements will be prepared as of October 31, 1997. In addition, the due diligence performed by KPMG and Arthur Andersen will be updated to October 31, 1997. For purposes of the equity ratio calculation only, the fund balances will be adjusted for specific items including forgiveness of SU indebtedness to SHS/LSPCH (approximately \$9.4 million), removal of Langley Porter Psychiatric Hospital (approximately \$10.5 million), inclusion of UCSF Faculty Practice Plan (approximately \$14 million), contribution by SU of the Boswell Building (approximately \$8 million), and an increase in UCSF's net assets for bad debt reserves (approximately \$8.5 million) and general reimbursement reserves (approximately \$50 million). In addition, other accounting adjustments will need to be made on the closing of SHS and UCSF's books and the opening balance for USHC. Recognizing that the parties may disagree regarding adjustments, they have agreed to appoint an independent third party who will function as a referee for the other adjustments. The decision of the referee would be final. The goal is to provide for contributions to equity of 55 percent on the part of SU and SHS and 45 percent on the part of UCSF. To the extent that the difference in the "other accounting adjustments" between UCSF and SU exceed \$30 million, the adjustments to UCSF's net assets will be reduced so that the difference is no more than \$30 million. UCSF's contribution shall be set at 45 percent and a calculation for SU's contribution at 55 percent will be made. If SU's contribution is in excess of 55 percent, SU will be permitted to withdraw an amount not to exceed \$25 million in order to bring the contribution to equity back to a 45 percent to 55 percent contribution on the part of UCSF and SU/SHS respectively.
- D. LSPCH is separately incorporated as a California nonprofit public benefit corporation. USHC shall become the sole corporate member of LSPCH with full control over LSPCH's assets and operations. USHC's Board of Directors will become LSPCH's Board.
- E. The proposed effective date of the merger is November 1, 1997 (Effective Date). If consolidation has not occurred by December 31, 1997, either party may terminate the Consolidation Agreement on 30 days' notice.
- F. USHC shall be solely responsible for hiring, supervising, setting terms and conditions of employment, disciplining and terminating all USHC employees subject to terms and conditions imposed by The Regents and Stanford Trustees on USHC. (See Workforce Agreements in this item.)
- G. USHC shall maintain programs of insurance or self-insurance for professional liability (medical malpractice), general liability and workers' compensation. The programs will cover all USHC employees, fellows, residents, and students. In addition, all leased employees will be covered by USHC for

malpractice and general liability and by UCSF for workers compensation. UCSF will charge USHC the cost of such workers' compensation coverage.

- H. All fundraising for the benefit of USHC shall be conducted solely by the respective universities. Existing endowments shall remain with the respective universities, with income supporting the activities at USHC in a manner consistent with any donor instructions.
- I. Reciprocal representations and warranties include the authority to enter into the transaction, title to assets, environmental status of the underlying property and current financial conditions of the respective medical centers.
- J. Each university will maintain its professional liability, general liability, and workers' compensation programs for claims and liabilities arising for incidents prior to the Effective Date of the transaction.
- K. Both UCSF and SU will provide indemnification to the other and to their respective Regents or Trustees, officers and employees regarding all liabilities, liens, orders, judgments, taxes, fees, costs, amounts paid in settlement, reasonable attorney's fees, expert witness fees, and disbursements in connection with investigating, defending, or settling any action arising from or relating to the operations prior to the Effective Date of the merger.
- L. SU and UC's obligation to close the transaction is subject to the satisfaction of certain conditions including execution of all necessary agreements; obtaining all regulatory approvals, consents, licenses, permits; obtaining tax exempt status for USHC; and satisfactory completion of due diligence. In addition, SU has made a condition of closing that USHC is a private institution subject however, to the application of open meeting and public record requirements.
- M. USHC will report to each of the members (The Regents of the University of California through the Office of the President and the Trustees of Stanford University through the President's Office at Stanford) the following:
 - (1) Monthly financial statements and annual audited financial statements.
 - (2) The opening or closure of and any significant changes in medical programs and mitigation measures when particular programs are located on one campus rather than another.
 - (3) Reports of the disparity, if any, in the capital improvements at one campus or another as a result of improvements or degradation of seismic and structural condition and code compliance.

- (4) Statements of borrowings and debt services to cover such borrowings
 - (5) Federal and state corporate tax returns.
 - (6) Annual operating and capital budgets.
 - (7) Compensation of the five most highly compensated employees of USHC.
 - (8) Such other matters as may be requested by each of the members.
- N. Any proposed USHC capital expenditure for repair or replacement of physical facilities as a result of environmental or seismic deficiencies in excess of \$25 million will require approval of the Members.
- O. Upon dissolution all tangible assets attributable to a Member will revert to that Member. The tangible assets would be in proportion to each Member's contribution. Tangible assets acquired after the close will be attributed to the Member who owns the property upon which it is located, who has paid for the property, or, where there is an equitable payment on the part of one Member when such assets cannot be traced in origin, to one Member or the other. The plan of dissolution shall establish agreed-upon values for tangible and intangible assets. The valuation shall take into account all indebtedness then outstanding, allocating such indebtedness to the assets to be distributed, or proposing a plan of discharging such indebtedness structured in such a way as not to cause a default in the terms, covenants, or conditions of any indebtedness.
- P. Disputes will be referred to the President of Stanford and the Chancellor of UCSF. If they are unable to resolve the dispute, each university may appoint three representatives to attempt to resolve the dispute. A vote of five of the six representatives will carry the matter. It is assumed that all disputes will be resolved in this manner, except when the corporation is failing to support the two schools of medicine or USHC's financial performance is unsatisfactory as determined by either Member and measured by key financial measures, and significant ratings decline. In either event, after attempting to resolve the problems, either member may petition for involuntary dissolution of the corporation.

Assignment and Assumption of Agreement Between UC and USHC

- A. The Assignment and Assumption Agreement provides for transfer of assets including leases of real property, transfers of equipment, leasehold rights, cash, medical center and faculty practice plan accounts receivable, investments,

rights under contracts, and books and records. In addition, liabilities and adjustments to assets reflected on audited financial statements for UCSF and SHS/LSPCHS on October 31, 1997, will be assumed by USHC. The Consolidation Agreement sets forth the financial closing process (see Consolidation Agreement, paragraph C. above).

- B. Environmental, seismic, and structural liabilities, including those that arise prior to the Effective Date and those after the Effective Date, will be assumed by USHC, subject to approval of both Members for any environmental or seismic capital improvement costing in excess of \$25 million.
- C. USHC will be responsible for the first \$40 million each of contingent liabilities of UCSF and SHS. For purposes of this agreement contingent liabilities are unknown, unasserted, and/or unrecorded obligations. In the event that USHC makes a payment on behalf of either UCSF or SHS under this agreement, then the other university will receive the same amount as a special payment. In order to ensure appropriate funding for these contingent liabilities, USHC will maintain its investments at \$80 million (the floor) which will be adjusted for payments made in accordance with this provision. If the investment level falls below the floor, then USHC will obtain a letter of credit for the difference between the current investment balance and the adjusted floor level. After ten years the requirement to maintain investments at \$80 million will lapse and be of no further force and effect. If the contingent liability for either UCSF or SHS is in excess of \$40 million, the parent institution is financially responsible for the excess.
- D. Each university will be responsible for preexisting funded or recorded liabilities including professional (medical malpractice), general and workers' compensation liability.
- E. The obligation to perform under certain existing debt instruments will be assumed by USHC. UCSF's debt obligation will be paid off at the Effective Date.
- F. UC and SU would indemnify USHC for claims which arise from operations or assets of UCSF or SU's clinical enterprise, as the case may be, before the Effective Date, subject to USHC's indemnity for contingent liabilities as well as liabilities associated with environmental and seismic defects arising prior to the Effective Date, and USHC will indemnify UC and SU from any claims which arise, or any assumed liabilities, after the Effective Date.

Professional Services Agreement

- A. Stanford and UCSF will each enter into a professional services agreement with USHC on similar terms and conditions. The professional services agreement is the document which leases covered practitioners, including faculty, staff physicians, and residents, for the performance of professional medical services for patients.
- B. Collection of professional fee income is assigned to USHC.
- C. USHC is the exclusive contractor for physician services provided at the four USHC hospitals and clinics. USHC will negotiate contracts with third party public and private payors of medical services.
- D. USHC shall provide facilities and services appropriate to permit physicians and residents to provide services to patients, including space, equipment, supplies, utilities, and non-physician personnel services and marketing.
- E. USHC has an obligation to pay each school of medicine, specifically the practice plan, funds collected for professional fees. In year one, the professional fee collections associated with UCSF faculty less the expense of collection, will flow through USHC to the UCSF School of Medicine. For Stanford faculty-generated revenues in year one, a base payment for specialty and primary services will be paid to SU. The base payment is based on projections of revenue and adjusted at the end of the year and may be increased or decreased based upon quality and cost, but may not be increased or decreased more than a capped amount. In years two and three, it is anticipated that the amount paid to each school of medicine will be based on departmental budgets for unit-based services which measure fee-for-service volume, revenue and expenses in terms of relative value units (RVU), and risk-based business revenue and expenses in terms of either capitated lives or cases. Within three years, it is anticipated the faculties of the two schools of medicine will be fully integrated regarding clinical activities at all USHC sites providing for common RVUs based upon agreed-upon, departmentally-based budgets.
- F. All agreements will be terminated automatically in the event of the dissolution of USHC or if other related agreements are terminated in accordance with their terms. The Regents or the Board of Directors of USHC may terminate each agreement if the other party is in material breach and such breach remains uncured beyond a reasonable period of time necessary to cure such breach. In addition, the agreements may be terminated at Stanford University's request if USHC is ever adjudicated by a court of competent jurisdiction to be other than a private entity and subject to laws applicable to public bodies by virtue of their being public or the alter ego of a public body.

Affiliation Agreements

The affiliation agreements ensure that USHC will provide an environment conducive to the training of the students, residents, and fellows of the respective schools and to the development, assessment, and application of the latest advances in the disciplines of the respective schools. In addition, the affiliation agreements ensure that USHC supports the teaching and research needs of the respective schools and protects the program viability of the schools.

UCSF School of Medicine Affiliation Agreement

- A. The affiliation agreement between The Regents and USHC provides for continuation of teaching, research, and clinical programs of the School of Medicine in USHC facilities.
- B. Significant, proposed programmatic changes or new programs will be considered by USHC's service chief(s), chairs from Stanford and UCSF, and if appropriate, by relevant program directors. In addition to referral to the above groups, consideration may be provided by the USHC physicians group, the USHC CEO, and the Board, as appropriate. In the event there is no consensus from the foregoing, the two Deans and the USHC CEO shall have the authority regarding new programs and program changes.
- C. In the event of significant program additions, terminations, or significant changes, a report will be provided to the Members (Regents and Trustees), including mitigation measures, in order to deal with the impact on the physical location affected. The following factors shall be taken into account with respect to program changes or proposed new programs:
 - the financial viability of the program
 - the impact on medical student education
 - the impact on postgraduate education
 - the impact on research
 - the availability of existing facilities versus the need for new facilities or other capital expenditures
 - the compatibility with other programs
 - the availability of personnel
 - other costs
 - the availability of external funding, where relevant
 - such other factors as are from time to time identified by the two deans of the medical schools and USHC
- D. Traditional areas of support for the School of Medicine are provided by USHC to the School of Medicine, including medical direction which includes unit

leadership, administrative support for department chairperson, utilization review and quality assurance, and funds to purchase physician services for program support and for resident stipends. The amount of support to be provided by USHC in the first year of the Agreement is approximately \$34.7 million to the Stanford School of Medicine and approximately \$32.4 million to the UCSF School of Medicine. Any decreases in funding to either school will be made only after a full exploration of the alternatives taking into account the needs of the medical schools and the realities of the medical marketplace. (The Bylaws permit either member to dissolve the corporation in the event USHC fails adequately to support the two schools of medicine.)

- E. Research conducted in USHC facilities will follow applicable policies and rules of the respective universities. Research will be under the auspices of the Schools of Medicine. Clinical trials can be performed by USHC if approved by the Chancellor of the San Francisco campus and the President of Stanford University.
- F. The agreement provides for teaching of medical students, supervision of residents and post-doctoral fellows, and provides for USHC's financial support of the Dean's Office. In the first year financial support for the Dean of UCSF is based upon a graduated formula, but has traditionally been approximately \$6 million. The Dean's assessment for Stanford is approximately \$6.5 million.
- G. The terms of the affiliation agreements with the two universities' schools of medicine and USHC will be virtually identical.

UCSF Schools of Dentistry, Pharmacy, and Nursing Affiliation Agreements

The affiliation agreements for the Schools of Dentistry, Pharmacy, and Nursing are modeled closely on the terms of the affiliation agreement between USHC and the UCSF School of Medicine, as described previously. Each agreement is subject to the approval of Stanford University's President with respect to the use of south campus facilities and taking into account Stanford land use planning, programmatic needs, and other educational and research uses. The provisions which are common to all three affiliation agreements are as follows:

Clinical Program Changes and New Clinical Programs

- A. Any proposal to make significant changes in existing clinical programs or establish new clinical programs, whether initiated by the respective schools or USHC, will be considered by the relevant USHC service chief and the relevant chair from UCSF, with appropriate interaction and support from USHC management. The Academic Council (made up of the four UCSF deans, one

UCSF faculty member, the dean of the Stanford School of Medicine, and four Stanford faculty) will make recommendations for action by the USHC CEO and/or Board, as appropriate. In developing new programs, USHC shall look in the first instance to the UCSF schools.

- B. Factors to be considered in clinical program decisions include: the potential for improving patient care, the program's financial viability, the impact on medical student and postgraduate education, the impact on research, the availability of facilities, the compatibility with other programs, the availability of personnel, other costs, the availability of external funding, and such other factors as are identified from time to time by the dean of the respective school or the USHC CEO.
- C. At least annually the USHC Board of Directors will report to the Members of USHC on the effects of any program decisions that have had, or are likely to have, a material impact on the respective schools. The report may include actions that may be taken to mitigate negative impacts. In addition, the annual report will address the following:
- reduction of costs
 - avoiding costs
 - increasing patient satisfaction
 - increasing efficiencies in the process of care
 - improving the clinical patient outcomes, especially patients maintained on medications
 - reducing financial risks for physicians at risk
 - increasing net revenue
 - maintaining the regional and national reputation of USHC and the respective UCSF school
- D. In developing new clinical programs, USHC will look first to the faculty of the respective schools for the provision of professional services, and the respective schools will look first to USHC for the provision of facilities, equipment, and support personnel. The parties agree to exhaust the program review process before seeking professional services or before proceeding to locate a program at a non-USHC facility, except as to those sites where the UCSF School has programs in place.

Research

- E. All grant applications for research by UCSF faculty at a USHC facility will be administered through UCSF.

- F. All research will be conducted in accordance with applicable USHC patient care and billing policies and procedures and with the policies and procedures of the host university and applicable institutional review board requirements

Teaching

- G. The respective schools will be responsible for the direction, quality, and content of their teaching programs conducted in USHC facilities.
- H. All patients in USHC facilities will be considered, consistent with patient wishes, teaching patients participating in the relevant academic clinical programs.
- I. SU will not maintain any teaching program at its facilities which is substantially similar to any teaching program maintained by the respective schools without prior written notice. USHC will use housestaff and post-doctoral fellows under programs supervised exclusively by or through the respective schools.
- J. USHC will defend, protect, indemnify, and hold harmless The Regents from and against all claims, liabilities, or judgments arising from the acts or omissions of faculty, house staff, post-doctoral fellows, and students of the respective schools while providing services at USHC facilities and will provide a reasonable amount of general and professional liability insurance coverage or actuarially sound self-insurance for the faculty, house staff, fellows, and students while providing services at USHC facilities.

Dispute Resolution

- K. Disputes will be subject to resolution by the USHC CEO and the respective deans. If they are unable to resolve the dispute within an agreed-upon period, the matter will be referred to the Chancellor of UCSF and the President of Stanford. If they are unable to resolve the matter within a reasonable period of time, the matter will be referred to the Members of USHC for resolution in accordance with the bylaws.

Term and Termination

- L. Subject to the termination events described below, the term of the affiliation agreements will be of unlimited duration.
- M. The affiliation agreements will be terminated automatically in the event of the dissolution of USHC or if other related agreements are terminated in accordance with their terms. The Regents or the Board of Directors of USHC

may terminate the agreement if the other party is in material breach and such breach remains uncured beyond a reasonable period of time necessary to cure such breach. In addition, the affiliation agreements may be terminated at Stanford University's request if USHC is ever adjudicated by a court of competent jurisdiction to be other than a private entity and subject to laws applicable to public bodies by virtue of their being public or the alter ego of a public body.

Academic Contribution

- N. USHC will determine the amount of academic contribution in the context of its annual budget setting process and overall financial plan. USHC will agree that any reduction in its academic contribution to the School of Nursing, School of Dentistry, or the School of Pharmacy will be made only after a full exploration of alternatives after extensive consultation with the respective deans and after consultation with the affected academic departments to understand the impact on their programs.

Establishment of other Programs

The following paragraphs of this section of the item describe provisions of the agreements between USHC and the respective schools which apply only to the school described.

- O. USHC and the School of Dentistry intend to establish a strong dental presence at the USHC facilities and work toward establishing the south campus as an important referral center, primary care facility, and tertiary care facility for dental services in the surrounding community. In the affiliation agreement USHC will designate the UCSF School of Dentistry as its exclusive School of Dentistry affiliate for the north campus and its primary affiliate for the south campus.
- P. In the School of Pharmacy affiliation agreement USHC will designate the UCSF School of Pharmacy as its exclusive School of Pharmacy for the north campus of USHC and its primary School of Pharmacy affiliate for the south campus of USHC. USHC will make a fixed payment to the School of Pharmacy in the first year of its operation. This payment includes reasonable compensation for the anticipated level of professional services provided to USHC by the School of Pharmacy faculty and products provided by the Drug Products Services Laboratory. In addition, the parties will negotiate with respect to a second payment for innovative programs that contribute to the positive adjusted operating income of USHC, and USHC will make a payment to the UCSF School of Pharmacy equal to the salary of five residents.

- Q. USHC, in consultation with the Dean of the UCSF School of Pharmacy, shall appoint a Director of Pharmaceutical Services who will be an employee of USHC, but who will consult with and report to the Dean with respect to professional training and education. UCSF will pay to USHC a fee for such consulting and reporting functions equal to one-half of the cost of salary and benefits of the Director.
- R. In the School of Nursing affiliation agreement USHC will designate the UCSF School of Nursing as its primary School of Nursing affiliate. With respect to the School of Nursing, USHC will make a fixed payment during its first year of operation, in support of educational obligations of the School of Nursing and as reasonable compensation for services provided by the school.

Lease Agreements for Facilities

The Regents will enter into lease agreements between The Regents, as landlord, and USHC, as tenant, for space located on the UCSF campus. The lease agreements are of two types: long-term leases in which USHC is the primary tenant and short-term leases in which USHC will occupy a portion of the premises.

- A. Term of the long-term leases is 40 years; term of the short-term leases is 10 years with one IO-year option to renew.
- B. Rent will be \$1/year, and USHC will pay for all utilities, services, maintenance and repair, including capital repair and replacement. For the long-term leases, USHC will be required to provide repair, maintenance and other services; such services will be required to conform to the maintenance protocol standards developed by UCSF for each facility and included in the leases. USHC will also defease any Medical Center debt on the long-term leases by making a lump sum payment at lease commencement. For the short-term leases such utilities, services, maintenance and repair, as well as non-medical center debt payments, will be passed through to USHC on a full-cost recovery, pro-rata basis.
- C. Parking accommodations currently in the UCSF parking system will be contracted separately under the same terms as for other tenants.
- D. USHC will adhere to the Parnassus Heights space and population ceiling as articulated in the 1996 Long Range Development Plan (LRDP) and the supporting Environmental Information Report (EIR) and will adhere to environmental commitments in the 1996 LRDP EIR and other UCSF EIR mitigation measures. All monitoring of USHC compliance with 1996 LRDP EIR and other UCSF EIR mitigation will be done by UCSF. UC will retain

lead agency status and land use authority for USHC planning and construction activities on the leased premises.

- E. USHC will accept the leased premises in an “as-is” condition and surrender the premises at lease termination in good condition, reasonable wear and tear excepted.
- F. USHC will be responsible for tenant improvement costs for all leases and will be responsible for construction for the long-term leases.
- G. USHC will be responsible for complying with the requirements of the Office of Statewide Health Planning and Development, including SB1953, and other hospital facilities regulatory and licensing agencies, and will be required to forward copies to UC of any facilities violations, warnings, or notices received from all regulatory and licensing agencies.
- H. Basic terms and conditions of these leases will be substantially the same as those incorporated into the leases between Stanford University and USHC.

UC will also assign, or sublet as appropriate, to USHC its leasehold interests in approximately forty leases of medical clinic, office, and laboratory space. The leases will be assigned or sublet to USHC at its sole cost for the remaining terms subject to current rent terms and conditions.

Workforce Agreements

- A. USHC will commit to offer employment to at least 95 percent of the employees affected by the transaction and to agree that for each affected employee who accepts such offer it will:
 - pay a base wage or salary up to two years which is at least equal to the base wage or salary that the employee earned when last employed by the University
 - recognize UCSF length of service for those terms and conditions of employment for which USHC considers length of service
 - allow affected employees to transfer accrued compensatory time, vacation, and sick leave balances for use at USHC, with the understanding that USHC will be free to establish new vacation and sick leave policies of its own

- excuse affected employees who have successfully completed their probationary period at UCSF from serving a new probationary period at USHC. and
 - provide health, dental, vision, disability, life insurance, and retirement plans for former UCSF career employees
- B. USHC intends to condition its offer of employment to the affected employees who will receive the assurances of these minimum conditions upon each employee's separation from UC employment.
- C. UC will include within the contractual commitments required of USHC the provision for an election period which will be coterminous with the period of time within which the employee is to accept the employment offer to secure the position offered at USHC and the minimum benefit conditions included with the offer.
- D. Employees whose job functions have transferred to USHC will be eligible to remain UC employees and be leased to USHC if:
- they do not have managerial or significant supervisory responsibilities at USHC
 - they do not have significant responsibilities in the area of employee or labor relations at USHC, and
 - they have attained age 50 with 5 or more years of service credit under the University of California Retirement System (UCRS) or they have attained age 40 with 10 or more years of service credit under the UCRS or they have 15 years of service credit under the UCRS irrespective of age
- E. Each employee qualifying in D. above will have the option of employment by USHC or continuing in University employment as an employee leased to USHC. UC will retain the right and responsibility to direct and supervise these employees. These employees will be subject to UC terms and conditions of employment and will receive UC benefits including UCRS benefits on the same basis as other UC employees.
- F. It is anticipated that the lease arrangement will continue in effect for thirty years or so long as the Consolidation Agreement is in effect and the University employees covered by the lease remain in continuous University service.

- G. USHC will pay to UC a fee for the services provided which would cover all of the UC costs associated with the leased employees.
- H. USHC has informed the University that its employment needs are such that it anticipates being able to make offers of employment to all but 28 employees employed by UCSF and SU, 10 of whom are anticipated to be from UCSF. These employees could be laid off if they are not otherwise placed.

President Atkinson observed that the San Francisco campus must have a long-term strategy that addresses the changes taking place in American healthcare and UCSF's fiercely competitive market situation. He believed that the merger is a realistic and innovative response to the new world in which academic medical centers now find themselves, and he expressed confidence in the leadership and management skills of the people leading the venture. He supported the merger of the clinical enterprises as a long-term strategic decision that will enable both universities to continue as world-class centers of education, research, and clinical care.

Vice President Gurtner reported that there are no unresolved key issues. Stanford University Trustees have delegated the merger decision to a committee of their board, which will vote on the merger in the near future. General Counsel Holst noted that he had distributed to the Regents a letter summarizing his view and the opinion of the Howard Rice law firm, both of which are that the proposed merger of UCSF and Stanford clinical activities is within the Regents' power to authorize under the constitutional authority vested in The Regents. He stressed that the Regents' decision should be based on a judgment of the merits of the issues, taking into account the data, the analyses, and the commentary that have been provided from all sources. He believed that the volume and character of the material that the Regents have received and the presentations they have heard place them in a position fully to discharge their fiduciary responsibilities with respect to the transaction. He noted that, at the request of Regents Davies and Preuss, his office reviewed the circumstances of certain of Stanford's equity holdings in relation to the Political Reform Act and the provisions of it related to participation in Regents' discussion and voting. He believed that there is no conflict which would require disqualification unless the merger transaction would have a material financial affect on any of those companies in which Regents have investments. His office has inquired into the circumstances of these companies and the nature of their business relationships with UCSF and concluded that there is no basis upon which such a finding could be sustained.

Chancellor Debas stated that UCSF is preparing to secure a leadership position in the next millenium, both in its academic and clinical missions. To accomplish this, it has embarked on two bold missions: first to build a new campus in Mission Bay to ensure continued success and growth of its biomedical research; second, to merge clinical services with Stanford to secure a vibrant clinical enterprise to support the academic missions of teaching, research, and public service. He stressed that the merger is one

only of hospitals and faculty clinical practices. Neither the medical schools nor their activities in undergraduate medical education, biomedical research, or fundraising will be merged. All faculty and residents will remain the faculty and residents of their respective schools. He noted that three separate reports attest to the business wisdom of the merger: the Ernst and Young analysis, the third-party review by Warren Hellman, and the State Auditor's report. He introduced key faculty leaders at UCSF to comment further about the merger.

Dr. Nancy Ascher, Professor of Surgery, Director of the UCSF Transplantation Program, and Director of Tertiary Care Services for the clinical practice organization, noted that the transplant service at UCSF is one of the largest in the country. She reported that in her job as tertiary care director, she meets with the medical directors of all the major health plans, groups, and payors in Northern California and hears complaints about UCSF physicians. She views herself as a conduit of change in the clinical behavior of faculty. She reported that over the past year she has visited with fifty health plan directors and has been exposed to many points of view. The practice of medicine has changed remarkably for physicians practicing at UCSF, just as it has for physicians practicing in the community. The cornerstones of a successful treatment and retention of patients are stellar results, patient service, and timely communications. Many of the hospital's referrals are dictated by contracts rather than patient or referring physician choice. Consequently, its strength and success depend on the strength and success of its marketing and contracting. She believed that a merged health center will provide strength in the marketplace in terms of the wide array of services that can be offered and in the breadth of experience of a collective faculty. Referring groups and payors look forward to a combined all-service tertiary and quaternary organization to which they can send challenging cases, assuming that it continues to provide the same quality of service as in the past. From the vantage point of daily practice, clinicians want an organization that can meet the needs of the marketplace and continue to ensure access to additional patients and that allows for rapid response to marketplace trends. As a busy clinical faculty member, as chief of the transplant service, and from the point of view of the medical center's customers, she supported the merger.

Dr. Larry Shapiro, Professor and Chair of Pediatrics, has provided leadership for the planning of children's services for the merger. He recalled that during the past ten months there has been an effort to create mechanisms to bring together all of the faculty at both institutions who are interested in child health. This includes participants from the departments of pediatrics, surgery, radiology, anesthesia, urology, otolaryngology, ophthalmology, neurology, neurosurgery, pathology, and orthopedics. Several programs have already been integrated. The first is a program created by the National Institutes of Health to foster and advance research in diseases of children. Funded by competitive grants, the departments of pediatrics at UCSF and at Stanford are among approximately fifteen nationwide which host such activities. The two centers have begun to collaborate and recently jointly hosted the annual retreat

for these fifteen centers. A second example can be seen in the rapidly moving field of medical genetics, where approval has been obtained from the Genetics Residency Review Committee to operate a joint UCSF/Stanford American Board of Medical Specialities certified residency in this discipline. Dr. Shapiro believed that this joint residency program is a model of what could develop in other areas. In addition, the directors of the two genetics program have submitted a joint grant application to NIH to fund research training which replaces an existing training grant held by UCSF. This new grant has already been awarded in a very competitive environment. The third example of integration is in academic general pediatrics, where both Stanford and UCSF have for some time wanted to create an advanced fellowship program to train primary care oriented physicians in the skills required to become academic leaders in this discipline. These two groups of faculty have designed a cooperative training program, applied successfully to the Robert Wood Johnson Foundation for support, and enrolled the first trainees. While such integrated programs, both within the campus community and in collaboration with colleagues at Stanford, could have been created in the past, they were not. Dr. Shapiro believed that the merger will act as an enabling force to allow novel academic and clinical programs to be born and to thrive. The merger provides a structural framework for bringing together the faculty and for accruing enough patients in some of the relatively rare types of pediatric illness to make advances more achievable. In addition to the academic benefits, the merger provides unprecedented opportunities to reshape the highly specialized medical care for children throughout northern California.

Dr. Bill Wara, Professor of Radiation Oncology and immediate past chair of the UCSF Academic Senate, who is involved daily in clinical research and the clinical care of cancer patients, reported that he has participated in many hours of merger discussions which have convinced him that the majority of the faculty are in favor of the merger. He believed that, although communication to the faculty has not been as complete as it could have been, the merger leadership has attempted to be as inclusive as possible. As part of the merger discussions, sixty faculty from each institution worked throughout the summer to resolve specific issues. This joint cooperation and volunteered hours by faculty is unprecedented. Dr. Wara co-chaired the Academic Mission Review Committee, which has recommended to the new merged entity that an Intercampus Academic Group be composed of elected faculty and administrators whose charge will be to evaluate new programs, have influence on the distribution of funds for academic programs, develop academic benchmarks, serve as a grievance committee for faculty who disagree with programmatic directions, promote joint collaboration between the two institutions, review student, house staff, and postdoctoral fellow educational evaluations, and make this collected information available openly to the public, faculty, the deans, Regents, Office of the President, Trustees, and the merged leadership of the new entity. The Academic Mission Review Committee has proposed that not just Academic Senate members but all faculty be included, so that salaried clinical faculty, which number approximately 400 at UCSF, will have a voice in the new entity.

Dr. Larry Pitts, Professor of Neurosurgery and Vice Chair of the UCSF Academic Senate, reported that UCSF faculty represent varying views, from clinicians eager to enhance their clinical practice for teaching and research to basic and clinical scientists who fear erosion of the research and educational mission of the University as dominantly clinical emphases control resources and funds flow. Optimists feel that the merger will increase revenues and the number of patients for clinical research; pessimists feel that the institution's emphasis will shift from academic pursuits to decisions driven by bottom-line clinical considerations, leaving few resources for research and education. These opponents note UCSF's recent increase in the numbers of patients and the medical center's revenues and question the motivation of joining an institution that is not performing well financially. The merger's proponents worry that the recent financial improvement will be transient. They believe that the real path to solid and lasting support for UCSF's academic mission is the higher clinical profile for primary and tertiary care in California that they feel the merger will bring.

Dr. Pitts reported that faculty were involved extensively in planning for the merger. Nine task forces comprised mainly of UCSF and Stanford faculty addressed critical academic and financial issues, and the faculty are hopeful that the administration will adopt most of their recommendations. He noted that the Academic Mission Review Committee produced a plan for faculty oversight of the quality of the institution's ongoing research and teaching missions, and he reported that UCSF's Academic Senate met recently to consider how to elect its faculty representative to the USHC Board of Directors. The group excluded administrators and department chairs from this position, feeling that those interests will be represented by other Board members. Recognizing the importance of non-Senate clinicians, however, voting rights have been extended to clinical faculty with at least an 80 percent commitment to UCSF and including the Schools of Medicine, Nursing, Dentistry, and Pharmacy.

In response to a question from Regent Brophy, Dr. Pitts noted that the Academic Senate has not taken a vote on the issue of the merger. He believed that administrators and faculty view the merger as an evolving process which could not be represented fairly by a limited proposal. Faculty Representative Weiss added that, although the planning process has been going on for the past two years, many faculty have only recently entered the discussions and are just beginning to understand some of the implications of the proposed merger. Regent Clark asked whether the Academic Senate has reviewed Stanford's operating figures. Dr. Wara responded that they have been presented at town hall meetings. Regent Clark was skeptical that the faculty could make an informed decision about the merger without analyzing the financial reports in depth. Chancellor Debas noted that responsibility for the hospital's financial viability and the protection of the academic mission rest with the Chancellor. He believed it would be inappropriate to ask the faculty to delve into financial analysis. He believed it was a positive note that the merger has made the Academic Senate more interested in the clinical enterprise.

President Atkinson commented that during extended discussions on the merger he checked with the leadership of the Academic Senate, both systemwide and on the campus, as to whether there was adequate consultation with the faculty. He was assured that they were satisfied with the consultative process. Although some Senate members might want to call for a vote, the leadership did not believe a vote should be taken.

Regent Brophy asked for a further explanation of why the Academic Senate had not taken a position on the merger, noting that to do so is within its purview. Dr. Wara reported that six months earlier he had appointed an ad hoc Academic Senate committee called the Merger Committee to review specific issues. The committee decided not to review economic issues because its members did not feel they were well qualified to do so. They did examine the academic mission, but they recommended not to have a vote because many issues needed to be resolved and the entity had to evolve further. Regent Leach asked whether he had a sense of the feeling of the faculty. Dr. Wara believed that the majority, at least 80 percent, supported the merger.

Professor Jane Norbeck, Dean of the UCSF School of Nursing, spoke on behalf of the Schools of Dentistry, Nursing, and Pharmacy. She reported that the three schools have been very positive about the potential benefits of the merger from the beginning; at the same time, their support for the merger was contingent upon confirmation that the long-term relationships between the new corporate entity and each school would be assured. To that end, suggestions were made for specific language changes in the campus Consolidation and Affiliation Agreements that were circulated in June. Five changes in the wording, which were immediately approved by UCSF and USHC, have also been approved by Stanford and incorporated into the documents.

Ms. Norbeck reported that the Dean of the School of Dentistry is enthusiastic about the opportunities that will arise from the merger. The school will be able to sustain and build upon its patient care base for educating students and for increasing patient-oriented research. She noted that the School of Nursing has worked with the Directors of Nursing at UCSF/Mt. Zion and at Stanford and Packard Children's Hospitals to develop the Center for Research and Innovation in Patient Care. The merger brings together into this center most of the best-educated nurses in northern California. The affiliation will provide support for a center director and seed funding to develop projects to improve patient care and to evaluate innovations designed to enhance the quality of care while controlling costs. The School of Pharmacy endorses the proposed merger for similar reasons. Not only will the merger enhance the economic viability of each entity, but the school also foresees economies of scale in the purchase and distribution of pharmaceutical supplies. Moreover, the Dean foresees even greater cooperation than already exists in providing training opportunities for pharmacy students and residents at the Stanford Medical Center and the Packard Children's Hospital .

Chancellor Debas stated that there are two compelling aspects of the merger. The first is that it will create the nation's foremost academic health center. The second is that the merger sets the stage to create a revolution in the way academic healthcare is organized and delivered. The architects of the revolution are the faculty themselves, who have spent hundreds of hours in defining the governance, the organization, the service lines, the fund flow mechanisms, and the clinical services. He was convinced that their efforts will produce a national model and standard for the provision of healthcare for academic health centers. He thanked the leadership and faculty of both campuses, staff within the Office of the President, and State legislators Burton and Shelley for their support and dedication.

Regent Johnson asked whether the proposed Intercampus Academic Group (IAG) would be ongoing. Dr. Wara responded that it will be the key academic group to review existing and new programs. The group is to have as its members six elected faculty from each institution and to have six administrators who are associate deans for research or education as appropriate to interact with the group. Dr. Debas added that there is the Academic Council made up of deans and academic senates from both campuses which is expected to provide an annual report to the two Members on any disparate or unusual impacts on the academic mission. It has been proposed that IAG members have staggered terms initially. Academic faculty and salaried clinical faculty will participate.

Regent Connerly observed that there is some cloudiness as to the rationale for the merger with respect to financing. Initially, it seemed to be driven by financial considerations. Later, the clinical and research aspects were brought up. He was troubled by what he perceived as a lingering conflict between the financial rationale and the research rationale. He wondered whether the difference in the annual financial performance of the two institutions was sufficiently outweighed by the projected benefits to the clinical and research aspects. Dr. Debas stated that, in preparing for today's discussion, he had reviewed all of his statements to the Board and that every time he spoke he extolled the academic advantages of the merger.

Regent Montoya was concerned about the impact of the proposed merger on academic programs. She asked whether the new programs that have been sparked by the merger could have been created in the past. Dr. Shapiro acknowledged that the programs that have been created to date could have been developed in the past, but he pointed out that in over eighty years of coexistence they were not, because the two institutions were competitors for clinical business, in research, and for trainees.

Chairman delJunco asked how intellectual property will be shared and whether The Regents will establish that policy. Dr. Debas responded that research and the products of research, including intellectual property, are within the purview of the individual schools. It is hoped that the merged entity will enable greater clinical research by providing more resources and the necessary patient population. He noted that it is

stated clearly in the affiliation agreement that the University's research and intellectual property remain with the University. Dr. Debas reiterated that this is not a merger of UCSF and Stanford but of the clinical enterprises of the two entities. As such, faculty research, undergraduate education, and postgraduate education remain with the schools. Deputy General Counsel Lundberg noted that the agreements provide for the leasing of faculty, who remain employees of their respective universities. The University of California patent policy will remain in effect with respect to those faculty members in their research endeavors. Regent Clark was concerned that about half of patentable research is conducted in the hospitals as distinguished from the medical schools. It is unclear as to how research conducted in a hospital that is owned jointly can be handled from a patent standpoint. General Counsel Holst believed that the critical issue is not where the research is performed but by whom. To the extent it is performed by UC faculty, who in the merger will remain employees of UC, it will be subject to the University's existing patent policy. If it is carried out in a joint project, there will be a joint ownership arrangement. President Atkinson confirmed that there are no new principles involved; procedures for handling intellectual property rights that have been established in the past will continue to be followed.

Vice President Gurtner referred to Regent Connerly's question concerning the economic viability of the two institutions. He observed that three independent reviews have produced similar conclusions about the economic viability of each. He noted that there has been a philosophical difference between the way in which UC and Stanford viewed their operational activities. In analyzing the advisability of the merger, an attempt was made to create a fair comparison between the two organizations. In the case of UC, there are issues relative to several kinds of State support, including Clinical Teaching Support and SB855 funding, that engender legitimate questions as to whether those funds are operational in nature or are subsidies. Stanford, on the other hand, made a clear decision to underwrite its missions of education and research using contributions from its investment portfolio. Mr. Gurtner explained that the first challenge in trying to negotiate the merger process was to make sure that the new entity has the resources available to meet its potential; second, that it is sufficiently independent of the parents to make good business decisions going forward; and third, that it has a management structure that can produce a solid, efficient organization. He was confident that those challenges have been met successfully. Mr. Gurtner believed that the other greatest concern that has been expressed is why the merger is necessary in light of the current financial strength of UCSFMC. He believed that there is nothing to suggest that the economic future of healthcare organizations is bright. All indicators point toward a future of more restrictive revenues. Under such circumstances, there is a need to be as protective of the University's mission as possible. He believed that there is a significantly higher chance that the combined entity will be more productive in the current environment than either entity could be alone. He emphasized that there are many issues that can be dealt with after the merger gets under way. He expected full implementation will take two years. He was confident that the merger is the best way to attack the future. He stressed that the real

mission of the clinical service is to **support** the academic mission. The merger is a step to create a structure that is positioned to protect that academic mission.

Regent Connerly asked Mr. Gurtner what would happen if Stanford's historically negative financial performance turned out to be the result of mismanagement. Mr. Gurtner reiterated that he believed that the management structure and the board of the merged entity have been constructed in such a way as to be responsive to any problems that may arise. The Regents will be provided with sufficient data to allow them to act quickly and aggressively in response to any failure of the merged entity to meet its goals. The governing board was designed so that all three factions are minority members. Deputy General Counsel Lundberg pointed out that, although there are two members of this non-profit public benefit corporation, the Trustees of Stanford University and The Regents of the University of California, the bylaws provide the authority for The Regents to act alone to bring an action for involuntary dissolution in the event that there are financial losses which the Regents believe, in their judgment and measured by market data, put the institution in jeopardy.

Regent Clark delivered a statement concerning his position on the issue of the merger, which he believed was the most serious matter the Board has ever considered. He stated that as trustees of a constitutional public trust, the Regents must examine all of the facts impartially. He was disturbed that specific information about the continuing financial strength of UCSF Medical Center had not been shared with the Regents or with medical center medical and support staff. He believed that key indicators show that the medical center's financial strength is actually increasing, which is opposite from what the Hellman Report predicted. He was concerned also that the predicted effects on Stanford of anticipated changes in Medicare and Medi-Cal have not been included in the analysis. His conclusion was that predictions of financial disaster for UCSF Medical Center in the absence of the merger are fabricated. A further concern was the legality of the merger. He noted that General Counsel Holst has stated that there is no legal precedent for the specific proposed transaction. Regent Clark believed that the merger would be an outright violation of the Constitution of the State of California, based on the Attorney General's ruling that, "The University of California is a State institution. It is a constitutional corporation or department and constitutes a branch of the State government equal and coordinate with the Legislature, the Judiciary, and the Executive." "It was Regent Clark's opinion that the merger, therefore, comprises a privatization of one of the four branches of the State government. Beyond that, he believed that because there is litigation pending in court as to the legality of the merger, any Regent who voted in favor of it would be held personally liable should the court rule that the merger is not legal. He stressed that it would be a critical legal fiduciary mistake for The Regents to approve the proposed merger under these conditions.

Regent Leach observed that the Board has relied for its legal advice on its General Counsel, who sought outside help from a well-regarded San Francisco firm to provide

the Board with information on the subjects which Regent Clark had addressed. He believed that the Board should continue to rely on General Counsel Holst's advice. Regent Clark noted that the outside counsel did not address the issue of constitutionality.

Chancellor Debas reiterated that the medical schools are organized into departments. Each department has a faculty and each has primary functions of education for undergraduates and graduates, basic and clinical research, and clinical care. He stressed that the departments are not merging; the clinical practices of the faculty are merging. The faculty members are UC employees, but they will provide clinical services under an agreement.

Vice President Gurtner noted that the State audit, which was requested originally by Senator Quentin Kopp, and a third-party review update to reexamine the business rationale for consistency had been mailed to all Regents. He reported that the Governor is expected to sign legislation that will exempt UCSF-Stanford Health Care from the Fair Political Practices Act. He noted that also mailed to the Regents was a consultant's report on seismic problems for which the merged entity will be responsible.

Deputy Counsel Lundberg discussed significant features of the terms and conditions of the negotiated agreements. He reported that the merger transaction will be completed through the execution and implementation of various agreements by and between the University of California, Stanford University, including its subsidiary, Stanford Health Services, and the University of California Stanford Health Care (USHC). As of November 1, 1997, the existing clinical enterprises of UCSF and SHS will be transferred to USHC. He noted that while it has been recognized that Stanford's contributions to equity would be somewhat more than those of UCSF, this is an equal transaction. As members of the nonprofit corporation, Stanford and The Regents each has an equal number of directors and the same powers under the articles and bylaws.

Mr. Lundberg then reviewed in detail the provisions governing the dissolution of USHC, the professional services agreements, and the affiliation agreements with the Schools of Medicine, Dentistry, Pharmacy, and Nursing. He noted that any significant changes in the clinical programs of the UCSF Schools of Dentistry, Pharmacy, and Nursing or the establishment of new programs will involve not only the USHC service chief but the relevant chair from the UCSF department, with appropriate interaction and support from USHC management. In developing new programs, USHC is bound to look in the first instance to each of the three UCSF schools. An annual report will be made to the Regents and Trustees on the effect of any program decisions regarding these schools. The affiliation agreements with the Schools of Nursing and Pharmacy have additional features. During the first year, the School of Pharmacy will receive compensation for professional services provided by

the School's faculty and products provided by the School's drug products service laboratory. In addition, USHC will pay UCSF for five pharmacy residents, and USHC will pay one-half the salary of an individual who is to be appointed Director of Pharmaceutical Services of USHC. The School of Nursing will receive a payment from USHC during its first year of operation and support of its clinical activities traditionally provided by the School of Nursing. Although it is not contemplated that a payment will be made to the School of Dentistry, the School intends to establish a strong presence at USHC's northern facilities and anticipates establishing a presence at Stanford as well.

Mr. Lundberg stated that leases will be executed between The Regents and USHC for physical space located on the UCSF campus. Long-term leases will be for forty years, and short-term leases will be for ten years with a ten-year option to renew. The long-term leases include those in which USHC is the primary tenant, such as for the hospitals, whereas the short-term leases include those in which USHC occupies only a portion of the premises. USHC will commit to offering employment to at least 95 percent of the employees affected by the transaction. Because the transaction has taken longer to consummate and there has been a certain level of attrition and transfer of employment at both institutions, USHC anticipates being able to make offers of employment to all but 28 employees, ten of whom are presently employed by UCSF.

The Committee adjourned for lunch at 12: 10 p.m.

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The Committee went into Closed Session at 1:25 p.m.

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The Committee reconvened in Open Session at 2:00 p.m.

(For speakers' comments, refer to the minutes of the September 17, 1997 afternoon session of the Committee of the Whole.)

Secretary Trivette reported that five letters were received concerning the UCSF-Stanford merger. Three letters expressing support for the merger were from the Chairs of the Departments of Radiation Oncology, Surgery, and Laboratory Medicine at UCSF, and two letters expressing opposition were from an Associate Professor of Pediatrics at Stanford Medical Center and a resident of San Francisco.

Upon motion duly made and seconded, the Committee approved the President's recommendation, Regents Atkinson, Brophy, Davies, Gonzales, Khachigian, Leach, and Preuss (7) voting "aye," and Regent Clark (1) voting "no." Committee members del Junco and Sayles were not present during the vote.

Regent Brophy believed that Stanford needs the merger more than the University does. He explained that he decided to support the proposal based on his faith in the strong leadership of Chancellor Debas. He hoped that Dr. Debas would choose to remain as Chancellor of UCSF and that the Regents would support him in that choice.

3. UCSF-STANFORD MERGER: APPOINTMENT OF UNIVERSITY OF CALIFORNIA DIRECTOR TO UCSF-STANFORD HEALTH CARE BOARD

The President recommended that subsection l(b)(l) of Article IV of the Bylaws of UCSF-Stanford Health Care be amended to provide for the following: (1) another University Director of UCSF-Stanford Health Care during the period that Haile T. Debas, M.D. is Chancellor and Dean of the School of Medicine of UCSF; and (2) designate Charles Wilson, M.D. to serve as a Director of USHC during the period that Dr. Debas is both Chancellor and Dean of the School of Medicine.

The Committee was informed that Article IV of the Bylaws of UCSF-Stanford Health Care provides for the membership of the Board of Directors. Section 1 (b)(1) sets forth the initial Board of Directors including the Dean of the UCSF School of Medicine and the Chancellor of the University of California, San Francisco campus. As Haile T. Debas, M.D. is now both the Chancellor and the Dean of the UCSF School of Medicine, for the period in which Dr. Debas fulfills both functions, another University of California Director needs to be appointed to the UCSF-Stanford Health Care Board of Directors. Thus, the language related to the Board composition is to be amended as follows:

“(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 provisions of these Bylaws to the contrary, for so long as the Dean of the UCSF School of Medicine is also the Interim 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 Chancellor UCSF shall be held by different individuals. Such temporary appointees shall be treated as an Initial Ex-Officio Director for all purposes of these Bylaws.”

Selection of Charles Wilson, M.D. as a Director for the period Haile T. Debas, M.D. holds dual appointments is recommended by both President Atkinson and Dr. Debas. Dr. Wilson is Professor of Neurosurgery, University of California at San Francisco, and has served for the past year as Senior Associate to the President, University of California.

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

4. **UCSF-STANFORD MERGER: AUTHORIZATION TO APPOINT REGENTS TO ACT FOR THE UNIVERSITY AS MEMBER OF UCSF-STANFORD HEALTH CARE**

The President recommended that the Chairman of the Board of Regents, the Chairman of the Committee on Finance, the Chairman of the Conimittee on Health Services, the President, or any one of them as designated by both the President and the Chairman of the Board, is authorized to act as the representative of The Regents of the University of California, as a statutory member of UCSF-Stanford Health Care, in voting on any matter requiring a vote of the members of UCSF-Stanford Health Care.

The Committee was informed that Article III of the Bylaws of UCSF-Stanford Health Care provides for two classes of members: the UC Class consisting of the entity known as The Regents of the University of California and the Stanford Class consisting of the entity known as the Board of Trustees of Leland Stanford, Jr. University. Section 2 of Article III provides that the University of California may in writing authorize one or more of its Regents to vote on its behalf on any matter or matters that may require a vote of the members. The members have powers as conferred upon them by the Articles of Incorporation and the Bylaws as well as by the Nonprofit Public Benefit Corporation Law of California. The powers include voting for the election of directors; bringing an action in the name of the corporation to remedy a breach of the charitable trust; approving the adoption, amendment, or repeal of bylaws; removing directors without cause; petitioning the superior court for the appointment of a provisional director; approving amendments to the articles of incorporation; approving the sale, lease, conveyance, exchange, transfer, or disposition of all or substantially all of the corporation's assets; approving the principal terms of a merger; petitioning for involuntary dissolution of the corporation; and voting to voluntarily windup and dissolve the corporation.

In addition, the Bylaws call for an annual meeting of the members. The meeting is to be held the second Tuesday of June of each year. Although there has not been a meeting of the members to date, given the fact that the transaction is still under negotiation, an annual or special meeting will be called, and individuals must be designated by the Board to take action for The Regents.

This authorization permits one, two, three, or all four of the referenced Chairmen or the President to act as The Regents' member of UCSF-Stanford Health Care. The Chairman of the Board and the President shall concur on the number to act as member.

It was moved and duly seconded that, upon the advice of Deputy General Counsel Lundberg, the President's recommendation be amended by adding the following as a last sentence:

Exercise of any power under Article III, Section 9(b) or Section 12 of the Bylaws relating to involuntary dissolution and reserved powers shall be taken only after a vote of the full Board of Regents.

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

5. **APPROVAL OF UCSD MEDICAL GROUP PARTICIPATION IN ALLIANCE RENAL CARE, INC., SAN DIEGO CAMPUS**

The President recommended that he, in consultation with the General Counsel and the Vice President for Clinical Services Development, be authorized to execute documents necessary to enter into service agreements with Alliance Renal Care Medical Group, Inc. The service agreements will allow individual faculty members to participate in, and to hold Board of Director positions with, the Alliance Renal Care Medical Group, Inc. (Alliance) a specialty independent practice association (IPA).

It was recalled that the UCSD Medical Center, like other academic medical centers across the country, must be able to compete effectively in highly competitive managed care markets. This is necessary both for continued access to patients to support educational and clinical research programs and to provide financial support for the School of Medicine. As demonstrated by the considerable success enjoyed by the San Francisco campus through its partnership with a major community medical group (Brown and Toland), such alliances increase the competitiveness of University faculty practice plans and allow the faculty, under certain conditions, to participate as individuals in the conduct of these organizations. As a result, the faculty can gain access to capitated lives which are managed by these groups, as well as have the opportunity to influence health care delivery in the community.

The proposed service agreement includes the following terms:

- A. Capitation will be paid to the UCSD Medical Group for each enrollee assigned to a UCSD participating physician under a managed care contract. In addition to such capitation payments, UCSD may also receive fee-for-service payments for enrollees not covered by capitation arrangements but who are eligible to receive professional medical services under non-capitation agreements into

which Alliance may enter. Rates for UCSD services will be consistent with rates for other IPA participants, but will be dependent upon contracts the IPA negotiates.

- B. Individual faculty members, who are members of the UCSD Medical Group, will participate in the IPA Board of Directors, committees, and operational activities, including utilization management, quality control, physician credentials, payor contracting, physician contracting, physician payment policies, procedures, and rules. UCSD physicians may serve as officers of the organization.
- C. The initial term of the agreement will be through December 31, 1998 with automatic renewal for successive year terms. UCSD may stop the automatic renewal by giving notice of termination prior to August 31 of the preceding year. Standard provisions have been included in the contract allowing for early termination "with cause." Either party may elect to terminate the agreement immediately upon the dissolution or sale of the IPA. Upon termination, both UCSD and Alliance will each be free to compete for payor contracts and enrollees.
- D. UCSD IPA representatives will participate as a part of Alliance in the selection of a management services organization to operate the IPA. UCSD will be charged for such management services in proportion to UCSD physician participation in the IPA.
- E. Alliance will not use the University of California or UCSD's name without the prior written consent of UCSD.
- F. All revenue generated by the faculty participating in Alliance, whether fee-for-service or capitated business, will be part of the Faculty Practice Plan. Though Alliance will bill on behalf of the physicians, all revenue will be paid to the Medical Group and not to individual faculty members. Individual faculty members will not be shareholders in the IPA.

The Committee was informed that the proposed relationship will provide access to certain nephrology patient populations that in the future UCSD may not have access to on its own.

The management of care for end-stage renal disease (ESRD) patients appears likely to change significantly in the United States during the next several years. The Rand Corporation released a 1995 study on potential options for the Health Care Financing Administration (HCFA) to use in dealing with such patients. The study led to ESRD demonstration projects in Florida, Tennessee, and California. The Florida project involves Blue Cross/Blue Shield; the one in Tennessee, Phoenix Health Care; and the

one in California, Kaiser Permanente. These projects will give HCFA experience with dialysis disease management full risk contracts, which is important to HCFA because it has a major role in the management of such patients in the United States. Of the estimated 1,400 dialysis patients in San Diego at this time, approximately 80 percent are covered through HCFA.

Because of the Rand study and current demonstration project activity, it seems likely that HCFA will migrate ESRD patient care services toward fully capitated contracts over the next five years. The proposed agreement with Alliance will allow UCSD nephrologists to be a major participant in the IPA, which serves a significant portion (50 percent) of the ESRD patients in San Diego. The Sharp system currently has responsibility for approximately 600 of the other 700 patients in San Diego.

Current demonstration project reimbursement rates range from approximately \$45,000 per dialysis patient per year to approximately \$65,000, depending on age and whether the patient also has diabetes. Patients with diabetes who are more than 65 years of age have the highest rates, while patients without diabetes who are less than 65 years of age have the lowest rates. It is estimated that the average capitation rate for demonstration project patients is approximately \$55,000 per annum per dialysis patient. Stop loss insurance is routinely a part of capitation arrangements. The major expense associated with the care of these patients is an allocation of current physician salary amounts.

Faculty participation in the Alliance IPA will provide several important benefits. First, HCFA will likely enter into only a small number of capitated contracts, each with large numbers of patients. Therefore, it is important and necessary for the UCSD nephrology faculty to participate in some organized group, such as Alliance, in order to have access to such contracts in the future. Second, the Alliance will negotiate with health plans for the thirty-month initial period during which plans will have responsibility for ESRD patients prior to HCFA coverage. Alliance represents a good geographical distribution throughout San Diego County and specializes in renal care, which will provide an advantage in contracting with health plans for coverage of dialysis patients. Third, Alliance will contract for pre-dialysis renal care providing UCSD access to a full scope of patients with renal disorders.

Some risks are associated with authorizing individual UCSD faculty to participate in activities of a private, for-profit IPA. The representatives of UCSD Medical Group serving on the IPA Board of Directors will be subject to the conflict of interest provisions of the Political Reform Act of 1974 covering all University of California employees and officials. This may require an individual to disqualify himself from certain University decisions, as defined by the Political Reform Act, while acting as a Director for the TPA.

Although UCSD anticipates a financial benefit to the UCSD Medical Group through this arrangement, there is some risk regarding the Medical Center component of reimbursement. To receive the maximum benefit of the relationship with community IPAs, UCSD must also be able to successfully negotiate corresponding Medical Center agreements. As with all managed care agreements, the UCSD Medical Center must be competitive in its rates in order to participate.

UCSD has concluded that the proposed agreement offers strategic affiliations that are likely to have far greater benefit to the UCSD Medical Group than non-participation. These relationships will provide UCSD and its faculty access to capitated lives that might otherwise be lost. In joining forces with community IPAs, UCSD can ensure continued access to the pool of patients that are currently served by these groups.

Vice Chancellor Alksne noted that the proposal will make it possible for full-time faculty who are involved in kidney dialysis and the management of patients with end-stage renal disease to join with private practice physicians in the community to create a group with county-wide coverage for contracting with major payors such as the federal government. All income generated by the faculty will be handled by the practice plan in conformance with University guidelines.

Mr. Kent Sherwood, CEO of UCSD Healthcare, provided some details of the proposal, noting that it is a specialty IPA that was started in December 1996. It is an avenue for full-time clinically active faculty to gain access to contracts. Nearly 50 percent of the physicians in the community have been organized into a competing IPA, making it necessary for UCSD to move forward without delay.

Regent Clark asked about the University's liability in an IPA arrangement. General Counsel Holst responded that indemnification provisions will protect the University from liability that extends beyond the University's own faculty. University Counsel Resnick explained that both an insurance provision in the contract and an indemnification clause use standard UC language to protect against liability.

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

6. UPDATE ON BUSINESS AFFILIATION ACTIVITIES, IRVINE CAMPUS

Chancellor Wilkening announced that the University of California, Irvine has ended its discussions with Tenet Healthcare about the possibility of leasing the UCI Medical Center. She recalled that similar discussions with Columbia HCA ceased in August. She reviewed briefly why a strategic review of the medical center's options for the future was undertaken and the changing context that resulted in her announcement.

In November 1993 the Regents spent a day discussing the healthcare marketplace in California. Ms. Wilkening recalled that at that time each of the UC medical centers was left to determine its own direction. During the following years, UCI undertook a review of its options. The healthcare environment nationally has continued to undergo profound changes. The growth of managed care in particular has reduced hospital and physician reimbursements tremendously, and hospital censuses across the country have fallen, as more and more care is delivered in outpatient settings. These changes have had a profound effect on teaching hospitals. For years they covered many of the costs of medical education and to some extent their clinical research activities with monies that were earned by providing medical care. In the managed care era those academic costs are no longer adequately covered by clinical income. The University's hospitals have changed from being profit centers to being potential risks for the University. Also, having fewer patients in the University's teaching hospitals has resulted in other consequences. The University's physicians are having to be trained in new and unfamiliar ways in outpatient clinics and managed care settings. There are great pressures to reduce specialty training, and there are fewer patients for specialty training. The payment rate for performing exactly the same procedure on two patients, one a Medi-Cal patient and one a Medicare patient, can differ by as much as a factor of four. Those hospitals that provide excellent care to patients who happen to be poor have a vastly more difficult time making ends meet. Ms. Wilkening observed that, although the options that were explored to address the medical center's problems were not chosen, a great deal was gained from the process.

Dean Cesario described plans and activities in the College of Medicine. He noted that the medical school has long emphasized primary care as the cornerstone of its training programs. Recently it has hired an outstanding Chair of Family Medicine and additional faculty of various backgrounds to build a program that emphasizes the cultural sensitivities required to deliver high-quality healthcare.

Dean Cesario reported that UCI will continue to develop an approach to primary care that nurtures a united teaching program of the four primary care fields: internal medicine, pediatrics, obstetrics, and family practice. Leaders from these departments meet regularly to plan programs. This effort has resulted in the procurement of a \$750,000 grant from Pacificare to introduce managed care into the primary care curriculum. Furthermore, the strength of these programs has attracted more medical school applicants to UCI as a first choice.

Dr. Cesario noted that faculty in basic science programs also have obtained competitive funding at a very high rate. Several excellent recruitments have been made in these areas. Efforts are under way to facilitate interactions between these scientists and the local biotechnical and biomedical device community. The first building of the five-building Irvine Biomedical Research Center, which is immediately adjacent to the Irvine Company's new technology center, has been dedicated.

Dr. Cesario reported that an examination is under way of the 42 accredited graduate medical training programs with the thought of consolidating programs in those areas where managed care has reduced patient volumes significantly. Discussions have begun with other medical schools about the possibility of combining two or three of these programs.

Dr. Cesario concluded by reporting that during the last several years, as faculty have participated in the discussions about the medical center's future, they have gained confidence about the prospect of being able to stand alone and attack some of the problems that confront them. Also, it has become apparent how strongly the community desires to maintain UCIMC and to support its School of Medicine.

Director Laret noted that the decision to terminate negotiations with Tenet Health Systems was a difficult one. UCI had three goals for that business affiliation: first, as the number of patients has declined, action was needed to assure access to a sufficient number of patients to support the medical education programs; second, as hospital reimbursement has fallen, a need developed to find a stable alternative source of financial support for UCI's College of Medicine; and third, as Orange County hospitals and medical groups have merged at a frenzied pace, it became apparent that UCI Medical Center should link to a local provider network. Intensive analysis indicated that by leasing UCIMC to a local hospital network, UCI faculty and residents would have had greater access to patients, there would be rental income that could be used by the College of Medicine, and overhead expenses could be reduced as negotiating strength with HMOs increased. All of this was dependent on UCI's ability to find the right network of hospitals and to negotiate satisfactory terms.

Mr. Laret reported that since May, two major positive changes have occurred to UCIMC's financial projections. First, as a result of a complex agreement by the California Health Care Association, the public hospitals, the children's hospitals, the private essential access community hospitals, and UC, UCI's projected disproportionate share payments will be \$22.5 million greater over the next three years than expected. Second, following the administration's efforts to secure a medical education supplement to Medi-Cal along the lines of the Medicare program, UCI expects to receive over \$29 million of additional funds over the next three years. Receipt of these funds is largely dependent on UCIMC's remaining a UC medical center. As such, these new funds have made the economics of keeping the hospital under University ownership superior to those involved in leasing the hospital to Tenet. While leasing the medical center to Tenet would have increased access to patients and would eliminate the University's operational risks, it would not provide the resources for the College of Medicine that are required to complete a transaction. For this reason, the negotiations were terminated.

Mr. Laret noted that, notwithstanding receipt of new funds, underlying issues have not been addressed. It may be necessary to reevaluate a lease arrangement in the future.

UCI has been developing a contingency plan that has three major thrusts: first, to gain greater security of payment from federal, county, and particularly State sources related to the care of Medi-Cal and indigent patients; second, to pursue new types of business affiliations with other providers in Orange County in such a way as to achieve the full benefits of a business affiliation without having to change the ownership of the hospital; and third, the continuation of the aggressive changes that have been taking place at UCI. UCIMC has three goals: improving the quality of care provided, improving service to customers, and improving its financial performance. Great strides have been made in these areas in the past two years.

Mr. Laret believed that the process UCIMC has gone through during the last two years has been valuable. Its administrators have developed relationships with providers that the medical center has never had before, they are closer to Orange County physicians, and they have become familiar with the Columbia and Tenet systems. The medical center has received increased attention from the State and county. Two weeks ago the Orange County Board of Supervisors appointed Mr. Laret to the board of CalOPTIMA, which he believed happened as a result of the initiatives Medical Center administrators have taken.

Mr. Laret expressed his appreciation to the many University administrators and the Regents who provided support and helped with those initiatives and to Chancellor Wilkening for putting in place a process that will ensure the long-term success of the UCI College of Medicine and Medical Center. Chancellor Wilkening thanked the Orange County legislative delegation for its support. She hoped that the UC system as a whole will press for the kinds of changes in policy that are needed at the State and federal levels for the support of teaching hospitals.

Regent Lee advocated the continued examination of affiliation and collaboration options at the Irvine, Los Angeles, and San Diego campuses. President Atkinson acknowledged the importance of setting up a special committee to examine opportunities at Irvine and how they might tie into other parts of the institution. A small committee, which would include at least one Regent, appropriate representatives from UC Irvine, and representatives from other UC campuses, will review the situation.

Regent Clark noted that Dean Cesario had referred consistently to primary care. He wondered whether the School of Medicine was cutting back on tertiary care instruction. Dr. Cesario explained that although primary care is emphasized, the curriculum will not change. Regent Clark believed that cooperation between the University's hospitals is important, and he supported the President's appointment of a committee to review institution-wide opportunities. Regent Brophy was concerned about the lack of recognition on the part of the Orange County Board of Supervisors of the value of the University's hospital at UC Irvine to the County. He pointed out that the Chancellor and numerous high-level administrators spend a disproportionate

amount of their time trying to resolve the problems there. He and Regent Khachigian agreed that the Regents should find ways as individuals and as a board to support and promote the medical center.

7. ANNUAL REPORT OF CLINICAL POLICY REVIEW TEAM

It was recalled that in March 1996, President Atkinson requested the Office of General Counsel (OGC), in coordination with Vice President Gurtner, to establish the Clinical Policy Review **Team** (Team). The Team is responsible for providing the Office of the President and the Board of Regents with an ongoing legal analysis and review of medical staff policy and procedures. The Team was assembled by the OGC and consists of the following members: Joe Tupin, M.D., retired medical director at UC Davis Medical Center; Cathryn Nation, M.D., Office of Health Affairs; Joanna Beam, Esq., Office of General Counsel; Roseanne Packard, J.D., R.N., coordinator; and Barbara Peck, analyst. Two phases of the clinical policy review (CPR) to date, the team's status report, and recommendations were summarized as follows:

Phase I Activities 1996-97: The Team developed a CPR report for each campus except UCSF. The focus was on clinical quality monitoring, which includes the areas of medical staff self-governance, granting of privileges and credentialing, peer review, discipline and reporting, human subjects research, quality improvement, and risk management. The Team also reviewed medical staff governance and contracting. The analysis considered whether there are appropriate and effective policies and structures to carry out the required procedures and whether the administration and medical staff have met their responsibilities for compliance and oversight.

The review and assessment methodology consisted of site visits to the schools of medicine and medical centers, review of documents, and interviews with key administrators. Each campus report included both findings and recommendations for each area of review, and the campus had an opportunity to provide feedback and comments. Campus leadership, including the chancellor, the school of medicine dean, and the medical center director met with President Atkinson, Vice President Gurtner, General Counsel Holst, and Dr. Tupin. Following review of each report, campus leadership worked with the Team and UCOP to develop a work plan to address key recommendations. The Team provided ongoing site visits for follow-up on work plan implementation. Phase I activities continue parallel to Phase II as the Team reviews and evaluates the implementation of the CPR recommendations.

Phase II Activities 1997-98: Phase II activities include ongoing monitoring of the campuses and comparable reviews in areas identified in Phase I. New areas incorporated into Phase II include resident assignment and supervision, malpractice data use by medical staff, and coordination of clinical quality monitoring.

Phase I: Status Report -- Medical Centers and Schools of Medicine:

- UC Davis The Team issued its draft report in July 1997. The campus prepared a work plan for review by the OGC, the President, and Vice President Gurtner in August 1997. The report recommended a focus on medical staff reappointment and affiliation agreements. Although existing self-governance and risk management programs are effective, the campus will continue to work toward extending risk management and quality improvement concepts to the area of primary care and newly acquired, but geographically distanced, clinical sites. The Team has scheduled further site visits for October 1997 to monitor implementation of the work plan.
- UC Irvine Campus leadership received a final report in October 1996. The campus prepared a work plan for quality improvement and medical staff governance for review by the OGC, the President, and Vice President Gurtner. The medical center had already begun consultation and review of the medical staff organization before the arrival of the Team. The review of the medical staff organizations is an ongoing process. Since the report was issued, changes have been made to the governance structure and a new medical director position has been created at the medical center. Representing the Team, Dr. Tupin met with the new director and discussed the oversight of contracts, human subjects, and resident supervision.
- UC Los Angeles The Team completed its final report in April 1997. Campus leadership presented a work-plan to President Atkinson, Vice President Gurtner, Vice President Hopper, General Counsel Holst, and Dr. Tupin that included programs for risk management and malpractice, and medical staff credentialing. Medical center leadership is reorganizing the quality improvement program and strengthening the medical staff reappointment process. The Team conducted a review of the human subjects area and issued recommendations. A review of human subjects was also conducted by a blue ribbon committee which issued its own report. The Human Subjects Review Program has been restructured, consistent with the recommendations of the committee and the Team, with additional qualified personnel, space, and computer support. The campus continues to work with the Team on issues involving resident supervision and affiliation agreements.
- UC San Diego The Team will send its draft report in September 1997. Strong self-governance and risk management programs are in place. The clinical enterprise and clinical department structures are in evolution, and the Team will continue to monitor them. The campus will develop a work plan for review by the Team and the President, Vice President Gurtner, General Counsel Holst, and Vice President Hopper. Thereafter, the Team will make

site visits, monitor contracts, including affiliation agreements, and review clinical program organization.

- UC San Francisco Due to the anticipated UCSF - Stanford merger and the resultant changes in governance and organization, the Team did not review the UCSF campus this year. At UCSF - Fresno, the OGC developed a new affiliation document and then successfully negotiated its acceptance by Community Hospitals of Central California. In addition, there will be a new faculty contract. A report prepared at the direction of UCSF Dean and Chancellor Debas will be the basis for further program development. The campus is bringing the residency program into compliance with national accreditation standards. Appropriate risk management structures are now in place.
- Phase II At the direction of the President and Vice President Gurtner, the Team established the following objectives for Phase II based on results from the CPR reports and discussions at the campuses:
 - Establish an ongoing, expedited review of each of the five campuses which includes topics such as malpractice data management, quality improvement, resident supervision, and other issues that may be raised by UCOP and/or the campuses.
 - Work with UCOP and campus administration to formalize changes in organizational structure that may be necessary to implement the Team's recommendations.
 - Develop systemwide policies and guidelines for medical malpractice, medical staff self-governance, and human subjects research.

Systemwide Trends

Over the past several years, the University of California's Medical Centers and Schools of Medicine have been undergoing dramatic organizational and structural change in response to the equally dynamic health care market. After completing the clinical policy review at UCD, UCI, UCLA, and UCSD, it is clear that campus leadership has effectively begun to redefine the organizational form of the academic clinical enterprise (enterprise) to consolidate many of the historically distinct functions of the schools of medicine and medical centers into a single system to enhance financial and strategic effectiveness and efficiency. However, reduced resources and limited attention to key areas such as medical staff governance and discipline, risk management, quality improvement, human subjects research, and contracting, which are necessary for the successful implementation of the University's mission, have led to certain systemwide deficiencies.

Both at the campuses and the Office of the President, these functions have historically been fragmented into a number of divisions or departments with little to no central monitoring or oversight authority. Given the fact that these functions are by definition interactive and substantially interdependent, failures in one area diminish the ability of the others to function effectively. For example, if there is limited attention to quality improvement, professional oversight and risk management structures may be negatively affected as well.

In spite of the considerable talent and effort of campus and UCOP leadership to develop entrepreneurial responses to the market, the organizational isolation and minimal oversight in these key areas have compromised the capacity of the campuses to respond efficiently.

Recommendations

- A. Continue Phase I and Phase II activities.
- B. Identify and develop campus and UCOP policies and procedures necessary to support and implement the issues and recommendations identified in Phase I and Phase II.
- C. Facilitate program coordination at the campuses and UCOP that will improve the ability of the key functional areas listed above to work together in an effective, cost-efficient manner.
- D. Support interaction between UCOP and the campuses to enhance oversight and monitoring activities that will provide support to the academic clinical enterprise.

Dr. Tupin presented the Team's annual review, noting that President Atkinson's original charge to the team was to examine medical staff self-governance; compliance with University, regional, and national policies; physician discipline and reporting; and to make recommendations about policies and procedures and other structures that might enhance the operation of the University's medical staffs. Dr. Tupin reported that the Team expanded that charge by examining clinical risk management and professional liability, contracts, and education affiliation agreements. He reported that cooperation with the Team was outstanding. Action plans have been put in place, and follow-up visits have begun to assess the effectiveness of those action plans. During a next phase the Team will develop new initiatives that are derivatives and outgrowths of the first phase.

Dr. Tupin made several general observations about the team's work. He reported that the team was impressed by the capacity of the campuses to react to the existing financial and medical managed care situations in the state. He noted that the team

examined the issues related to the cause of the decentralization of the University's governance structure through the years. In some cases, quality assurance activities have become fragmented as a result and need to be coordinated. Also, there have not been fully developed feedback loops among the system's components and the Office of the President. The team observed that clinical risk management and professional liability systems are working quite well. Some improvements could be made, but the team noted that the claims rate is lower for the University than for regional and national comparable parts of the private insurance market. Expenses are lower, and losses are lower case by case. Some areas of reporting and correcting past problems need improvement. Overall, however, the team has been pleased with improvements in all areas to date.

Faculty Representative Weiss noted that the team identified a systemwide deficiency in medical self-governance. She asked what problems were seen there. Dr. Tupin responded that systemwide there is a range of medical-staff self-governance elements. The team observed that the databases being used for semi-annual reviews and reappointments are not as good as they should be. In a private hospital that does not carry out a teaching mission, single providers may be isolated more easily, and their contributions to a particular patient's care are more evident. The University's medical centers function in a team structure where the faculty is the senior member of that team and the actions of the team, rather than individuals, affect patient care. Systems need to be improved for tracking the contributions of faculty and residents to individual care. The resulting database could then be used in the reappointment and review summaries that occur every two years. Professor Weiss noted that Dr. Tupin had mentioned that one of the team's objectives in its second phase would be to create some new organizational structures. Dr. Tupin commented that, although those structures are not yet defined, the team intends to examine the way in which programs have developed in the University that affect activities at the hospital. These include clinical risk management and professional liability.

8. ACTIVITY AND FINANCIAL STATUS REPORTS ON HOSPITALS AND CLINICS

Vice President Gurtner commented that the University was able to negotiate an agreement with the federal government that will bring new monies to the University and that important legislation was put into place recently by the State Legislature that will ensure that the Medi-Cal program recognizes medical education as a legitimate cost of the program. In the coming year, the conversion of that change into ongoing support for the University, combined with changes in SB855 subsidies, will have significant beneficial financial impacts on the medical centers.

The meeting adjourned at 3: 15 p.m.

Attest:

Secretary