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UNITED STATES DISTRICT COURT
NORTHERN DISTRICT OF CALIFORNIA

SANTA ROSA MEMORIAL HOSPITAL, et)	Case No. 08-5173 SC
al.,)	
)	ORDER GRANTING
Plaintiffs,)	AMENDED MOTION FOR
)	PRELIMINARY
v.)	<u>INJUNCTION</u>
)	
DAVID MAXWELL-JOLLY, Director of)	
the California Department of)	
Health Care Services)	
)	
Defendant.)	
)	
_____)	

I. INTRODUCTION

This matter comes before the Court on Plaintiffs' Amended Motion for Preliminary Injunction. Docket No. 60 ("Am. Mot. for Prelim. Inj."). Plaintiffs are non-contract hospitals in the State of California. See Docket No. 7 ("Am. Compl.") ¶ 6. Defendant David Maxwell-Jolly ("Defendant"), Director of the California Department of Health Care Services ("Department"), filed an Opposition and Plaintiffs submitted a Reply. Docket Nos. 61, 64. The Court granted Defendant's Request for Leave to file a Surreply. Docket No. 67. Ordinarily, the Court would hold a hearing to determine the appropriateness of imposing injunctive relief. However, based on the facts of this case and the case law, the Court finds that the motion is suitable for decision without oral argument. For the reasons stated herein, Plaintiffs' Amended Motion for Preliminary Injunction is GRANTED.

United States District Court
For the Northern District of California

1 Rosa Memorial Hospital, St. Helena Hospital, Queen of the Valley
2 Medical Center in Napa, SRM Alliance Hospital Services (dba
3 Petaluma Valley Hospital), Central Valley General Hospital in
4 Hanford, San Joaquin Community Hospital in Bakersfield, Lancaster
5 Hospital Corporation, Fountain Valley Regional Hospital and
6 Medical Center, San Antonio Community Hospital in Upland,
7 Children's Hospital at Mission in Mission Viejo, Mission Hospital
8 Regional Medical Center in Mission Viejo, Saddleback Memorial
9 Medical Center in Laguna Hills and San Clemente, Orange Coast
10 Memorial Medical Center in Fountain Valley, Anaheim Memorial
11 Medical Center, Hoag Memorial Hospital Presbyterian in Newport
12 Beach, Heart Hospital of BK, LLC in Bakersfield, and John Muir
13 Health in Concord and Walnut Creek. Am. Compl. ¶ 6.³ On January
14 14, 2009, Plaintiffs moved for a preliminary injunction. Docket
15 No. 11. On February 23, 2009, the Court stayed this case pending
16 the Ninth Circuit's resolution of the same issues in other cases.
17 Docket No. 30. On September 9, 2009, the Court lifted the stay
18 and permitted Plaintiffs to file a new brief in support of an
19 amended motion for preliminary injunction. Docket No. 59.

20
21 **III. LEGAL STANDARD**

22 To warrant injunctive relief, a plaintiff "must establish

23 _____
24 Defendant agrees that Plaintiffs' claims concerning AB 1183 are
25 moot because those cuts have been temporarily enjoined. See Opp'n
at 2 n.2.

26 ³ According to Defendant, Fountain Valley Regional Medical
27 Center recently converted to contract-hospital status. Opp'n at 9.
28 If this claim is true, then the injunction granted in this Order
does not apply to that hospital.

1 that he is likely to succeed on the merits, that he is likely to
2 suffer irreparable harm in the absence of preliminary relief, that
3 the balance of equities tips in his favor, and that an injunction
4 is in the public interest." Winter v. Natural Res. Def. Council,
5 --- U.S. ---, 129 S.Ct. 365, 374 (2008); see also Am. Trucking
6 Ass'ns v. City of L.A., 559 F.3d 1046, 1052 (9th Cir.2009). "In
7 each case, courts 'must balance the competing claims of injury and
8 must consider the effect on each party of the granting or
9 withholding of the requested relief.'" Winter, 129 S.Ct. at 376
10 (quoting Amoco Prod. Co. v. Vill. of Gambell, Alaska, 480 U.S.
11 531, 542 (1987)).

12
13 **IV. DISCUSSION**

14 Plaintiffs seek to enjoin the implementation of AB 5's ten
15 percent reduction in the "allowable cost" reimbursement of non-
16 contract hospitals for inpatient services they provide to Medi-Cal
17 patients. Mem. of P&A in Supp. of Am. Mot. for Prelim. Inj. at 1.

18 **A. Likelihood of Success on the Merits**

19 The basis of Plaintiffs' lawsuit is that the Medi-Cal
20 reimbursement rate reductions violate federal law. Am. Compl.

21 ¶ 2. State reimbursement plans must ensure that payments are
22 consistent with efficiency, economy, quality of care, and access
23 to care. See 42 U.S.C. § 1396a(a)(30)(A) (hereinafter § 30(A)).
24 The Ninth Circuit interprets this federal requirement as follows:

25 [T]he Director must set hospital . . .
26 reimbursement rates that bear a reasonable
27 relationship to efficient and economical
28 hospitals' costs of providing quality services,
unless the Department shows some justification

1 for rates that substantially deviate from such
2 costs. To do this, the Department must rely on
3 responsible cost studies, its own or others',
that provide reliable data as a basis for its
rate setting.

4 Orthopaedic Hosp. v. Belshe, 103 F.3d 1491, 1496 (9th Cir. 1997).

5 The District Court for the Central District of California
6 already determined that non-contract hospitals were likely to
7 succeed on the merits of their claim that AB 5 conflicts with
8 § 30(A). Indep. Living Ctr. of S. Cal. v. Shewry, No. 08-3315,
9 2008 WL 3891211, at *2-5 (C.D. Cal. Aug. 18, 2008)(hereinafter
10 "Indep. Living Ctr. I"). The District Court found that:

11 [Section] 30(A) creates duties on behalf of the
12 Department, i.e., the duty to consider
13 efficiency, economy, and quality of care when
14 establishing reimbursement rates. . . . [W]hen
15 the State of California seeks to modify
16 reimbursement rates for health care services
provided under the Medi-Cal program, it must
consider efficiency, economy, quality of care,
and equality of access, as well as the effect of
providers' costs on those relevant statutory
factors.

17 Id. at *4. The District Court noted there was no evidence the
18 Department considered the relevant factors in making the ten
19 percent reduction. Id. Instead, "AB 5 itself suggests that the
20 only reason for imposing the cuts was California's current fiscal
21 emergency." Id.

22 On July 9, 2009, the Ninth Circuit affirmed these
23 determinations. Indep. Living Ctr. of S. Cal., Inc. v.
24 Maxwell-Jolly, 572 F.3d 644, 651-52 (9th Cir. 2009)(hereinafter

1 "Indep. Living Ctr. II").⁴ The Ninth Circuit determined that:

2 [I]t is clear that the Director [of the
3 California Department of Health Care Services]
4 violated § 30(A) when he implemented the rate
5 reductions mandated by AB 5. The Director
6 failed to provide any evidence that the
7 Department or the legislature studied the impact
8 of the ten percent rate reduction on the
9 statutory factors of efficiency, economy,
10 quality, and access to care prior to enacting AB
11 5, nor did he demonstrate that the Department
12 considered reliable cost studies when adjusting
13 its reimbursement rates. In the absence of such
14 cost data, the Director could not have complied
15 with § 30(A). . . .

16 Id. at 652.

17 Defendant suggests that this Ninth Circuit decision involved
18 different payment reductions than those that are currently before
19 the Court. Opp'n at 1. However, both the District Court and the
20 Ninth Circuit considered the rate reductions implemented by
21 section 14166.245, which are the reductions that apply to
22 Plaintiffs in this case. See Indep. Living Ctr. I, 2008 WL
23 3891211 at *4; see also Indep. Living Ctr. II, 572 F.3d at 649.
24 The District Court found that all petitioners, including non-
25 contract hospitals, demonstrated a likelihood of success on the
26 merits that the ten percent rate reductions implemented by AB 5
27 violated federal law. Indep. Living Ctr. I, 2008 WL 3891211 at
28 *4-5. The District Court also determined that most of the
petitioners, but not non-contract hospitals and managed care
plans, showed irreparable harm. Id. at *5-10. On appeal, the

⁴ Mr. Maxwell-Jolly replaced Sandra Shewry as the Director of
the California Department of Health Care Services on April 9, 2009.
Indep. Living Ctr. II, 572 F.3d at 649 n.2.

1 Ninth Circuit explicitly stated that "[u]nder the standards
2 established in Orthopaedic Hospital, it is clear that the Director
3 violated § 30(A) when he implemented the rate reductions mandated
4 by AB 5." Indep. Living Ctr. II, 572 F.3d at 652. The rate
5 reductions that apply to non-contract hospitals in section
6 14166.245 of the California Welfare & Institutions Code are part
7 of the rate reductions mandated by AB 5. Based on the Ninth
8 Circuit's decision, the Court finds that Plaintiffs are likely to
9 succeed on the merits of their claim that these rate reductions
10 violate federal law.

11 In his Opposition, Defendant points to three documents and
12 argues that "[w]ith these studies in mind, the Legislature
13 expressly considered hospital costs when it drafted AB 5." Opp'n
14 at 4.⁵ The first document is the Legislative Analyst's Office
15 ("LAO") Report analyzing the 2008-09 budget. Douglas Decl. ¶ 7,
16 Ex. D ("LAO Report").⁶ However, the District Court for the
17 Central District of California has already determined that "all
18 the Legislative Analyst's report shows is that such a report was
19 prepared. Respondent has not shown that the Legislature ever
20 reviewed or considered the concerns raised therein." Indep.

21
22 ⁵ This statement in Defendant's Opposition directly
23 contradicts the statement in Defendant's Surreply that "Plaintiffs
24 argue for the first time in their reply brief that the Legislature
25 (not DHCS) has the duty to study proposed Medi-Cal reimbursement
26 rates and provider costs before they are enacted." See Surreply at
27 2. It is Defendant who argued that the Legislature expressly
28 considered hospital costs when it drafted AB 5. See Opp'n at 4.

⁶ Toby Douglas, Chief Deputy Director for health programs at
the California Department of Health Care Services, filed a
declaration in support of Defendant's July 17, 2009 Supplemental
Brief. Docket No. 49.1.

1 Living Ctr. I, 2008 WL 3891211 at *4 n. 10. Similarly, here,
2 Defendant has presented no evidence that the Legislature or the
3 Department ever reviewed or considered this report prior to
4 setting the rate reductions that apply to Plaintiffs. Indeed,
5 nowhere in the LAO Report is there any analysis of non-contract
6 hospital costs. See LAO Report.

7 The second document is the 2007 California Medical Assistance
8 Commission ("CMAC") Annual Report. Douglas Decl. Ex. C ("CMAC
9 Annual Report 2007"). The Court finds that this report is
10 irrelevant. CMAC is the agency established for negotiating
11 contracts with managed care plans and hospitals under the Medi-Cal
12 program. Id. at 1. The report exclusively concerns contract
13 hospitals, not the non-contract hospitals who are Plaintiffs in
14 this case. See id. at 1-22. Douglas declares that "[t]he 2007
15 CMAC report would have been the most recent annual report
16 available for the Legislature to review when it enacted AB 5."
17 Douglas Decl. ¶ 6. Defendant presents no evidence that the
18 Department or the Legislature actually considered the report
19 before setting the ten percent reimbursement rate reduction at
20 issue in this case.

21 The third document is a November 2005 analysis by the
22 Department concerning a similar reimbursement rate reduction in
23 2004-2005. Douglas Decl. Ex. B ("November 2005 Analysis"). The
24 Douglas Declaration states that "[t]he November 2005 DHCS Rate
25 Analysis was a public document that would have been available for
26 legislators to review." Id. ¶ 5. Defendant presented no evidence
27 that the Department or the Legislature actually reviewed it. Even
28

1 if they did, this document does not consider the impact of AB 5 on
2 non-contract hospital costs. See November 2005 Analysis.

3 Defendant contends that the Department used the four-month
4 period between the enactment and implementation of AB 5 to
5 determine whether the reimbursement reductions satisfied the
6 requirements of § 30(A). Opp'n at 5-8. The Court finds that the
7 evidence presented is not sufficient to support this contention.
8 William Liu declares that the Department conducted an analysis of
9 the impact of section 14166.245 prior to its implementation. Liu
10 Decl. ¶ 4.⁷ However, the document submitted to support this claim
11 merely consists of annual estimates of recoupment collected by the
12 PIRL program and percentages of total reimbursement for non-
13 contract hospitals between 1999 and 2005.⁸ This document does not
14 support the contention that the Director relied on responsible
15 cost studies when adjusting the reimbursement rates at issue to
16 determine whether these reimbursement rate reductions were
17 consistent with efficiency, economy, quality of care, and access.

18 Gary Wong also declares that the Department analyzed whether
19 the reduced reimbursement payments would be reasonable relative to
20

21 ⁷ William Liu, Chief of the Disproportionate Share Hospital
22 Financing and Non-Contract Hospital Recoupment Section, Safety Net
23 Financing Division, of the California Department of Health Care
Services, filed a declaration in support of the Opposition. Docket
No. 61-2.

24 ⁸ "PIRL" stands for peer grouping inpatient reimbursement
25 limitation. Final Medi-Cal reimbursement for non-contract hospital
26 inpatient services is normally established at the PIRL, which is
27 the lesser of a hospital's (1) customary charges, (2) allowable
costs determined by the Department, (3) an all-inclusive rate per
discharge limitation, or (4) peer grouping rate per discharge
limiation. Liu Decl. ¶ 2.

1 hospitals' costs prior to implementation. Wong Decl. ¶ 5.⁹
2 However, Wong supports his claim by pointing to only two
3 documents. The first is the November 2005 Analysis that the Court
4 has already found inadequate to show that the Department complied
5 with its statutory obligations. See Wong Decl. Ex. A. The second
6 is a one-page, handwritten, summary comparison of how audited
7 allowable costs compared to reported costs for unidentified non-
8 contract hospitals between 2002 and 2005. See id. Ex. B. This
9 document is clearly inadequate to show the Department relied on
10 responsible cost studies to determine that the ten percent
11 reduction was consistent with efficiency, economy, quality of
12 care, and access. The Court finds the Liu and Wong declarations
13 and attached exhibits are not sufficient to show the Department
14 complied with federal requirements.

15 Furthermore, it is clear that the sole motivation for AB 5
16 was budgetary. The relevant code section begins by stating that
17 "[t]he Legislature finds and declares that the state faces a
18 fiscal crisis that requires unprecedented measures to be taken to
19 reduce General Fund expenditures" Cal. Welfare & Inst.
20 Code § 14166.245(a). The Ninth Circuit has already determined
21 that the record supported the District Court's determination that
22 the Medi-Cal reimbursement rate reductions contained in AB 5 were
23 based solely on state budgetary concerns. Indep. Living Ctr. II,

24
25 ⁹ Gary Wong, formerly employed as Health Program Audit Manager
26 1 in the Financial Audits Branch, Audits and Investigations
27 Program, of the California Department of Health Care Services filed
28 a declaration in support of Defendant's Opposition. Docket No.
61-4. See also Docket 17.5 ("Douglas Decl.") Ex. A Attachment E.

1 572 F.3d at 656. For this reason alone, the Court finds that AB 5
2 violates federal law. Id. Based on all of the foregoing, the
3 Court concludes Plaintiffs have shown a likelihood of success on
4 the merits.

5 **B. Irreparable Harm**

6 Dr. Michael L. Vaida declares that collectively Plaintiffs
7 will lose over \$13 million per year as a result of the AB 5 rate
8 cuts. Johnson Decl. Ex. 5 ("Vaida Decl.").¹⁰ Defendant objects to
9 Dr. Vaida's declaration and requests that it be stricken. Docket
10 No. 63 ("Def.'s Renewed Objections"). The Court may consider
11 inadmissible evidence on a motion for preliminary injunction so
12 long as the Court gives such evidence appropriate weight. See
13 Indep. Living Ctr. I, 2008 WL 3891211 at *2 n.5. The Court
14 therefore OVERRULES Defendant's objection to Dr. Vaida's
15 declaration and DENIES the request that it be stricken.

16 However, even if the Court did not accept Dr. Vaida's
17 calculation of the non-contract hospitals' losses, there can be no
18 dispute that the ten percent reimbursement rate reductions
19 implemented by AB 5 will result in monetary losses for Plaintiffs.
20 Defendant provides data indicating the reduction will result in
21 decreased revenues for Plaintiffs of between 0.1% and 4.2%,
22 depending on the hospital. See Opp'n at 9-10.

23 Ordinarily, monetary losses do not constitute irreparable
24

25 ¹⁰ Dean L. Johnson, attorney for Plaintiffs, filed a
26 Declaration in Support of the Amended Motion for Preliminary
27 Injunction. Dr. Vaida's declaration, which was previously filed in
28 in this case as Docket No. 48, pp. 62-65, is attached as Exhibit 5
to Johnson's Declaration.

1 harm. L.A. Mem'l Coliseum Comm'n v. Nat'l Football League, 634
2 F.2d 1197, 1202 (9th Cir. 1980). However, the Ninth Circuit
3 recently determined that reductions in Medi-Cal revenue payments
4 to hospitals constitute irreparable harm if a requested injunction
5 is not granted because the Eleventh Amendment sovereign immunity
6 of the Department bars hospitals from ever recovering damages in
7 federal court against the Department if they are successful on the
8 merits of their case. Cal. Pharm. Ass'n v. Maxwell-Jolly, 563
9 F.3d 847, 850-52 (9th Cir. 2009).¹¹ Accordingly, the Court finds
10 that Plaintiffs have shown irreparable harm.

11 Defendant accuses Plaintiffs of waiting too long to seek a
12 preliminary injunction and, as a result, Defendant claims that
13 Plaintiffs are not entitled to a finding of irreparable harm.
14 Opp'n at 8-9, 21. Here, however, the Court stayed this case
15 pending the Ninth Circuit's resolution of the same issues in other
16 cases. See Docket No. 30. Now that the Ninth Circuit has
17 clarified the standard of irreparable harm that applies in a case
18 where health care providers are challenging Medi-Cal reimbursement
19 rate reductions, the Court finds that Plaintiffs have shown

21 ¹¹ The Ninth Circuit's articulation of the irreparable harm
22 standard in California Pharmacists Association was made in the
23 context of deciding whether to issue a stay of Medi-Cal
24 reimbursement rate cuts that the District Court had declined to
25 enjoin. 563 F.3d at 849-50. The four factors considered by the
26 Ninth Circuit are the same as the four factors a District Court
27 must consider when ruling on a motion for a preliminary injunction.
28 See id. Furthermore, both a stay of a state action pending appeal
and granting a preliminary injunction in this context produce the
same result: both temporarily enjoin Medi-Cal rate reimbursement
reductions. Hence, the Court adopts the standard of irreparable
harm articulated by the Ninth Circuit in California Pharmacists
Association.

1 irreparable harm as a result of the ten percent rate reduction.

2 **C. Balance of Equities and Public Interest**

3 Defendant points out that California's fiscal situation
4 remains precarious. Opp'n at 22. The Court is mindful of the
5 budgetary difficulties facing the State of California. However,
6 the Ninth Circuit has already held with respect to AB 5 that
7 "[s]tate budgetary considerations do not . . . in social welfare
8 cases, constitute a critical public interest that would be injured
9 by the grant of preliminary relief. In contrast, there is a
10 robust public interest in safeguarding access to health care for
11 those eligible for Medicaid." Indep. Living Ctr. II, 572 F.3d at
12 659. Based on these considerations, the Ninth Circuit determined
13 the District Court did not abuse its discretion in concluding that
14 the balance of hardships and public interest weighed in favor of
15 enjoining implementation of the ten percent rate reduction
16 required by AB 5. Id.

17 Here, an AB 5 rate reduction is also before the Court, and
18 therefore the same considerations apply. While, as Defendant
19 points out, "an injunction would require policymakers to revisit
20 possible program cuts," Opp'n at 22, the Court must also take into
21 consideration the threat to the health of Medi-Cal recipients
22 created by a reduction in non-contract hospital reimbursement
23 rates, and the public interest in ensuring access to health care.
24 The Ninth Circuit has already determined that "it would not be
25 equitable or in the public's interest to allow the state to
26 continue to violate the requirements of federal law." Cal. Pharm.
27 Ass'n, 563 F.3d at 852-53. The Court finds that the balance of

1 equities and the public interest weigh in favor of granting the
2 injunction.

3
4 **V. CONCLUSION**

5 For the reasons stated above, the Court GRANTS the Amended
6 Motion for Preliminary Injunction. It is hereby ORDERED that, as
7 of the date set forth below, Defendant Maxwell-Jolly, Director of
8 the California Department of Health Care Services, is
9 preliminarily enjoined from continuing to implement and apply the
10 ten percent reduction in the "allowable cost" reimbursement of the
11 Plaintiffs for the inpatient services they provide to Medi-Cal
12 patients.

13 The Case Management Conference set for Friday, November 20,
14 2009, remains on calendar. The parties shall appear at 10:00 a.m.
15 in Courtroom 1, on the 17th floor, U.S. Courthouse, 450 Golden
16 Gate Avenue, San Francisco, CA 94102.

17
18 IT IS SO ORDERED.

19
20 Dated: November 18, 2009

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22 _____
23 UNITED STATES DISTRICT JUDGE
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