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UNITED STATES DISTRICT COURT

CENTRAL DISTRICT OF CALIFORNIA, WESTERN DIVISION

INDEPENDENT LIVING CENTER OF SOUTHERN CALIFORNIA, INC., a nonprofit corporation, *et al.*,

Petitioners,

SACRAMENTO FAMILY MEDICAL CLINICS, INC.; *et al.*,

Intervenors,

v.

TOBY DOUGLAS, Director of the Department of Health Care Services, State of California

Defendants.

Case No. CV 08-3315 CAS (MANx)

MEMORANDUM OF POINTS AND AUTHORITIES IN SUPPORT OF JOINT MOTION FOR APPROVAL OF SETTLEMENT AGREEMENT

[Notice of Motion and Joint Motion; Declaration of Craig J. Cannizzo in Support of Joint Motion for Approval of Settlement Agreement; and [Proposed] Order filed concurrently herewith]

Date: September 22, 2014
Time: 10:00 a.m.
Crtrm.: 5, Floor 2
Hon. Christina A. Snyder
Action Filed: April 22, 2008

CALIFORNIA PHARMACISTS ASSOCIATION, *et al.*, Plaintiffs, v. TOBY DOUGLAS, Director of the California Department of Health Care Services Defendant.	Case No. CV 09-722 CAS (MANx) Hon. Christina A. Snyder, Judge Presiding Action Filed: January 29, 2009
INDEPENDENT LIVING CENTER OF SOUTHERN CALIFORNIA, INC., *et al.*, Plaintiffs, v. TOBY DOUGLAS, Director of the Department of Health Care Services, State of California Defendant.	Case No. CV 09-382 CAS (MANx) Hon. Christina A. Snyder, Judge Presiding Action Filed: January 16, 2009
CALIFORNIA HOSPITAL ASSOCIATION Plaintiff, v. TOBY DOUGLAS, Director of the Department of Health Care Services, State of California Defendant.	Case No. CV 09-8642 CAS (MANx) Hon. Christina A. Snyder, Judge Presiding Action Filed: November 24, 2009

MEMORANDUM OF POINTS AND AUTHORITIES

I. INTRODUCTION

Plaintiffs and Intervenors (collectively, "Plaintiffs"), on the one hand, and the Department of Health Care Services ("DHCS") and the Director of DHCS, (collectively, "the Department"), on the other, jointly move the Court to approve the Settlement Agreement reached in the above-referenced cases. The Settlement Agreement was reached after six years of complex and exhaustive litigation, including multiple preliminary injunctions entered by this Court, numerous opinions by the Ninth Circuit Court of Appeals, complex regulatory proceedings, and ultimately, a United States Supreme Court decision that vacated most of the Ninth Circuit decisions and remanded the matter for further proceeding. After the Supreme Court's opinion was issued in February 2012, the parties engaged in continuous negotiations under the supervision of the chief Ninth Circuit mediator. As a result of these efforts, the parties ultimately negotiated a settlement which was executed in April 2014, and which the parties now present to the Court for approval.

The settlement was intensively negotiated by all parties and represents a fair and adequate resolution of these cases. Under the terms of the settlement, the parties have already dismissed their appeals from the preliminary injunctions issued in the cases, (§§ III.A.1, and § 1.16); and Plaintiffs agree, when this Agreement becomes effective, to dismiss the within actions with prejudice, (§ III.A.3), subject however to the Court retaining continuing jurisdiction to determine (1) motions for attorneys' fees by counsel for Plaintiffs, and (2) motions or proceedings by Plaintiffs to enforce the Agreement, up to and including January 1, 2016 (§ III.D.17). In return, under the settlement, the Department has agreed – either by release (§ III.B.2 (page 14), or by agreement § III.A.8 (page 13) – to forgo recoupment of any amounts paid out by the Department to Medi-Cal providers, pursuant to the preliminary injunctions previously issued by this Court, except with respect to "opt-out providers." In other words, when the settlement becomes effective, Plaintiffs

will give up their right to seek any further relief, and the state will give up its right to seek recoupment of funds that have already been paid pursuant to the preliminary injunctions, except with respect to "Claimed Excess Payments" for providers that "opt out" of the settlement. This preserves the status quo, and by any measure is fundamentally fair and equitable given the risk, expense, complexity and likely duration of further litigation if the settlement is not approved.

II. BACKGROUND

A. Original Medi-Cal Rate-Cut Legislation

The Court is familiar with the complex procedural and factual history of these actions, and the legislative enactments which they challenge, Assembly Bill X3 5 ("2008 AB 5"), Assembly Bill 1183 ("AB 1183"), and Assembly Bill X4 5 ("2009 AB 5").

B. Subsequent Legislation Impacting The Rate Cuts

The effective dates of certain of the payment reductions in these cases have been impacted or superseded by subsequent legislation.

First, the 10% outpatient payment reduction of 2008 AB 5 was superseded on March 1, 2009 by AB 1183, which imposed smaller payment reductions.

Second, Senate Bill 90 ("SB 90"), which was enacted effective April 13, 2011 eliminated the AB 1183 Reductions as to hospital inpatient services provided by Non-Contracting hospitals, for services rendered on or after April 13, 2011.

Another legislative enactment impacting the effective date of the challenged payment reductions is Section 93.5 of Assembly Bill 97 of 2011 ("AB 97"), which authorized the Department to reduce payments for various outpatient services and DP/NF services by ten percent, effective June 1, 2011 (the "AB 97 Reductions"). The instant settlement does not involve actions challenging the AB 97 Reductions.

C. The Supreme Court's February 2012 Ruling And Subsequent Ninth Circuit Mediation Efforts

On January 18, 2011, the Supreme Court granted certiorari with respect to the

various payment reduction lawsuits. Earlier, on November 18, 2010, the Centers for Medicare & Medicaid Services ("CMS") had disapproved various State Plan Amendments ("SPAs") related to the payment reductions, and the Department had requested reconsideration. Oral argument in the Supreme Court was conducted on October 3, 2011. However, following oral argument, CMS approved some of the pending SPAs, and the Department withdrew its request for reconsideration of some of its other SPAs. The parties subsequently submitted letter briefs to the Supreme Court regarding the effect on the applicable cases, if any, of these administrative developments.

The Supreme Court issued its decision on February 22, 2012. *Douglas v. Indep. Living Ctr. of S. Cal., Inc.*, 132 S.Ct. 1204 (2012). The Supreme Court held that the SPA decisions of CMS changed the procedural posture of the cases. *Id.* at 1209-10. The Supreme Court further held that, given the complexity of these cases, it would remand the cases back to the Ninth Circuit for further consideration of whether providers could maintain an action under the Supremacy Clause with respect to the payment reductions at issue. *Id.* at 1211. Thus, the Court vacated the Ninth Circuit decisions that had affirmed the various preliminary injunctions, and remanded the matter to the Ninth Circuit.

Following the Supreme Court's decision, the Plaintiffs in the various cases and the Department then engaged in lengthy settlement negotiations overseen by the chief Ninth Circuit mediator, Claudia Bernard. These mediation efforts were successful, ultimately resulting in execution of the instant proposed settlement on April 28, 2014.[1]

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[1] The Settlement Agreement is attached as Exhibit A to the Declaration of Craig J. Cannizzo in Support of Joint Motion for Approval of Settlement Agreement, filed concurrently herewith.

III. THE PROPOSED SETTLEMENT

A. General Provisions

First, pursuant to the Settlement Agreement, the parties have dismissed their various appeals in these actions. Then, after both this Court and CMS approves the Settlement, Plaintiffs will dismiss their actions with prejudice, subject to the Court retaining jurisdiction (1) to determine Plaintiffs' attorneys' fees motions and (2) to determine any motions by Plaintiffs to enforce the Agreement, up to and including January 1, 2016. In exchange, the Department will agree to forgo recoupment claims against Medi-Cal providers arising out of the preliminary injunctions in these cases, except with respect to "Claimed Excess Payments" for the following: (1) any current or prior hospital member of California Hospital Association ("CHA"), that, after notice sent after the Effective Date of the Settlement, nevertheless elects to opt out of the benefits of the Settlement (as specified in ¶¶ III.A.4 and 5); and (2) any provider that institutes a new suit or fails to dismiss a pending suit or administrative action against the State or Federal government, or officials in respect to the 2008 AB 5, 2009 AB 5, or AB 1183 Reductions, and (3) the plaintiff hospitals in the *Santa Rosa* or *North Bay* litigation (¶¶ II.19 and III.A.7). Each side is to bear its own costs, except for any Plaintiffs' attorneys' fees which may be awarded, if any.

Among other things, the agreement provides that the Settling Plaintiffs – which include not only individual providers but also associational plaintiffs who are acting as virtual representatives of the associations' members – will release state and federal entities "from any and all liability, derivative or otherwise," for all claims concerning or relating to the payment reductions, "excluding any claims that any individual Medi-Cal provider may have relating exclusively to the accuracy of the computation by DHCS of the reimbursement due to that provider under applicable law." (§ III.B.1.)

In turn, pursuant to § III.B.2, the Department will release the Settling Plaintiffs from liability relating to "DHCS's Claimed Excess Payments," meaning

payments made while challenged payment reductions were enjoined, but where DHCS ultimately obtained federal approval from CMS for those payment reductions (§ III.A.8).[2] In addition, pursuant to the Settlement Agreement, the Department has agreed to forgo recoupment of amounts paid as a result of various preliminary injunctions where the Department subsequently withdrew its request for SPA approvals. This covers various pharmacy and other outpatient provider payments during the period from July 1, 2008 through February 28, 2011, as well as certain hospital payments through December 31, 2010, or February 28, 2011, depending on the provider category. (See fn. 1, *supra*.)

The settlement will not be effective until fully approved by CMS, or, if only partially approved by CMS, the Department decides to nevertheless proceed and not recover monies from providers for the payment reductions for time periods discussed above. The date on which the settlement is effective is known as the "Settlement Effective Date." (§ II.24.)

B. Special Hospital Notice Provisions

Under the Settlement Agreement, the hospitals are required to forgo pursuing any further legal relief from the Medi-Cal payment reductions that were challenged in the applicable cases. In contrast with the other portions of these cases involving the outpatient payment reductions, this includes several hospital payment reductions that were enjoined only after they had been implemented for a period of time or

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[2]This includes, with some exceptions, all payments made as a result of injunctions of the AB 1183 Reductions for services rendered from March 1, 2011 through May 31, 2011, after which the successor legislation, AB 97, became effective. However, for hospital outpatient services and Non-Contract hospital inpatient services, the relevant dates of service are January 1, 2011 through April 12, 2011. Claimed Excess Payments also include payments made to small and rural Non-Contract hospitals for inpatient services while the 2009 AB 5 Reductions were enjoined, for dates of service of January 1, 2011 through April 12, 2011 and for DP/NFs for the period March 1, 2011 through May 31, 2011.

were never enjoined by this Court, some of which were statutorily eliminated several years later by SB 90 in 2011. Additionally, the association members of CHA are relatively few in number (approximately 450) and are readily identifiable. Because of these unique circumstances that are *only* applicable to hospital providers, the settlement is structured to provide special notice to hospitals, such that individual hospitals, that are not already an "opt-out provider", may choose not to accept the benefits of this settlement, and instead opt out and pursue claims on their own if they determine the settlement is not in their best interests.

Specifically, within 30 days of the Settlement Effective Date, the CHA is required to send a notice to all current members – and any hospital that was a member during any period on or after July 1, 2008 – advising them of the terms of the settlement (the "CHA Notice"). (§ III.A.4.) Within 45 days of when the CHA Notice is mailed, hospitals may opt out of the settlement by filing their own lawsuit challenging any or all of the payment reductions for any or all hospital services, and/or the federal government's approval of those reductions. If a hospital opts out, it is not required to release the State from any potential claims, and could seek retroactive relief with respect to the payment reductions. However, any such opt-out hospital would not get the benefit of the settlement, meaning that DHCS will have the right to seek recoupment of any Claimed Excess Payment from the hospital.

The CHA Notice must advise the hospitals of (a) the terms of the Settlement; (b) that they may "opt out" by timely filing a lawsuit in their own name; and (c) if a hospital does file such an individual action, then it will lose the benefits of the Settlement, and the Department will have the right to seek recoupment of any payment to that provider that constitutes or constituted a DHCS' Claimed Excess Payment. (§ III.A.4.) If CHA and DHCS cannot reach agreement on wording of the CHA Notice, any such dispute will be submitted to the Court for resolution. (*Id.*)

C. <u>Retention of Jurisdiction, and Attorneys' Fees</u>

Finally, the settlement also provides (§ III.D.17) that the Court shall retain

jurisdiction, after the agreed dismissal of the within actions, with respect to motions or proceedings by any named Plaintiff to enforce the Settlement Agreement; and with respect to any motion for attorneys' fees by any of the Plaintiffs or Plaintiffs' attorneys. Then, § III.C. provides that attorneys for Plaintiffs may seek an award of fees from the Department and/or the benefitted parties, including hospitals. Any such application must be filed no earlier than the Settlement Effective Date, and no later than 30 days after the Settlement Effective date.

IV. THE SETTLEMENT SHOULD BE APPROVED BECAUSE IT IS FUNDAMENTALLY FAIR, ADEQUATE AND REASONABLE

In deciding whether to approve a settlement agreement under which the court retains continuing enforcement jurisdiction, the criteria applied is whether it is "fair, adequate, and reasonable, as well as consistent with the public interest." *United States v. Lexington-Fayette Urban County Gov't*, 591 F.3d 484, 489 (6th Cir. 2010). As the Ninth Circuit has noted, "[s]ettlement is the offspring of compromise; the question . . . is not whether the final product could be prettier, smarter or snazzier, but whether it is fair, adequate and free from collusion." *Hanlon v. Chrysler Corp.*, 150 F.3d 1011, 1027 (9th Cir. 1998); *see also Officers for Justice v. Civil Service Comm'n*, 688 F.2d 615, 625 (9th Cir. 1982) ("The proposed settlement is not to be judged against hypothetical or speculative measure of what might have been achieved by the negotiators.").

The proposed settlement is the result of years of negotiation between counsel for the Plaintiffs and counsel for the Department. There is no question that the positions of the Plaintiffs and the Department were adverse, and that the settlement is the fruit of arm's-length negotiations. This is particularly true in light of the fact that the Department is a governmental entity which has defended these actions zealously, and which has dedicated substantial resources to advocating for its position in multiple state and federal fora, up to and including the United States Supreme Court. *See Hanlon*, 150 F.3d at 1026 (participation of governmental entity

weights in favor of approving settlement agreement).

The proposed settlement is fundamentally fair, adequate, and reasonable. By this settlement, providers will have secured gains they achieved in the litigation and will avoid the risk that would ensue if these actions were further litigated.

V. CONCLUSION

For all the above reasons, the parties jointly request that this Court approve the Settlement Agreement, subject to the retention of jurisdiction for the limited purposes described in the [Proposed] Order.

DATED: August 19, 2014

Respectfully submitted,
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By: /s/
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DATED: August 19, 2014

Respectfully submitted,
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