LOS MEDANOS COMMUNITY HEALTHCARE DISTRICT

SETTLEMENT AGREEMENT ANALYSIS AND FINDINGS

Prepared by G.L. Hicks Financial, LLC

Dated June 16, 2011

Overview:

This analysis and findings report has been prepared at the request of Los Medanos Community Healthcare District (the "District") in response to its desire to determine if a resolution of its Settlement Agreement dated September 10, 1998 (the "Settlement Agreement"), with the Office of Statewide Health Planning and Development ("Cal-Mortgage") can be resolved and terminated, and if such early termination would be financially favorable for the District.

The District constructed its acute care hospital facilities (the "Hospital") in 1979, and subsequently leased the Hospital and a skilled nursing facility to the Los Medanos Health Care Corporation (the "Corporation"). On March 1, 1990, the Corporation borrowed $11,080,000 in tax-exempt bonds (the "Bonds") that were insured by Cal-Mortgage, the proceeds of which were used to make improvements to the Hospital. Due to negative operating results, a receiver was appointed to run the Hospital on March 18, 1994. On April 1, 1994, Cal-Mortgage insured a $1,500,000 line of credit for the Corporation to pay for costs associated with final operations and closure of the Hospital, which closure occurred on April 28, 1994. The Corporation filed for bankruptcy on April 22, 1994, and the District later filed for bankruptcy on February 21, 1996, which bankruptcies were subsequently merged into one bankruptcy. On March 20, 1996, Cal-Mortgage filed a secured proof of claim for $10,640,000 with the bankruptcy court, which claim was later revised to a $4,430,000 secured claim ($1,400,000 of which is related to the lease of the Hospital to the County) and a $4,227,000 unsecured claim, resulting from Cal-Mortgage's guarantee of the defaulted Bonds.

An important provision contained in the Settlement Agreement requires the District to make certain payments to Cal-Mortgage and to the bankruptcy court in the event the District sells the Hospital during the term of the County Lease, including any extension of the lease by the County. Therefore, if the Hospital is sold during any time that it is leased to the County, the District must (i) repay all loans outstanding to Cal-Mortgage, (ii) repay the remaining balance of the $1,400,000 obligation relating to the lease of the Hospital to the County and (iii) turn over any residual amount remaining from the sale proceeds to the bankruptcy court to pay for all remaining claims of unsecured creditors.

On August 1, 1998, the District entered into a 20-year lease (through July 31, 2018) of the Hospital with Contra Costa County (the "County"), which lease had two five-year consecutive extensions available to the County to extend the lease for a total of 30 years (the "County Lease"). The County Lease required the County to pay annual rents as of August 15th of each year (rents paid in advance) at $100,000 per year through July 31, 2018. In order to exercise the first five-year lease extension, the County must provide the District with twelve months advance written notice of their intention to extend the lease through July 31, 2023. In order to exercise the second five-year lease extension, the County must provide the District with six months advance written notice of their intention to extend the lease through July 31, 2028. If the County elects to extend the lease for the first five-year extension, both the District and the County have six months to negotiate a new lease amount. If a new lease amount is not negotiated between the District and the County within six months, then the County has the option to withdraw its extension notice and terminate the lease. If the County elects not to terminate its extension notice, then both the District and the County must enter into binding arbitration in order to determine the fair market value rent during the five-year extension of the lease. A similar process is required should the County elect to extend the lease for a second five-year term, only the time frames for each action is less for the second extension than for the first. The County Lease also provides that the County has a 45-day option of first refusal to lease or purchase the Hospital from the District. The 45-day option commences after the District provides the County with other offers received by the District to either lease or purchase the Hospital by another party other than the County.

Simultaneous with the lease of the Hospital to the County, the District entered into an assignment of rents agreement with the County and Cal-Mortgage to assign all of the lease receipts relating to the County Lease to Cal-Mortgage and for all lease payments to be made directly from the County to Cal-Mortgage (the "Assignment Agreement"). The Assignment Agreement runs from August 1, 1998 to January 31, 2026, and covers all lease payments no matter the lease amount or the lessee. Furthermore, during the two-year period from August 1, 2018 through July 31, 2020, the District guaranteed a minimum lease payment to Cal-Mortgage of $500,000 annually, no matter if the Hospital is leased or not.

On May 1, 2000, the District entered into an amendment to the Settlement Agreement (the "Amendment Agreement") that, among other things, reaffirmed that the County had the first right of refusal to purchase the Hospital and set forth a methodology for the repayment of the $1,400,000 obligation referred to in the Settlement Agreement in the event the District were to sell the Hospital during the term of the County Lease. The methodology for repayment of the $1,400,000 requires that interest accrues on the obligation at 6.5% per annum from August 1, 1998 (the commencement date of the County lease), and is reduced by amounts paid to Cal-Mortgage pursuant to the Assignment Agreement.

Purpose of the Engagement:

The District engaged G.L. Hicks Financial, LLC ("G.L. Hicks") to review all documents relating to the Settlement Agreement, the Amendment Agreement, the County Lease, the Assignment Agreement, and various correspondence between the District, Cal-Mortgage and District counsel relating to the above-described documents (the "Pertinent Documents"). The District also authorized G.L. Hicks to negotiate with Cal-Mortgage in an attempt to determine the least amount that Cal-Mortgage would accept to terminate the Settlement Agreement. G.L. Hicks was also asked to prepare various cash flow analyses for the District to reflect differing scenarios with respect to the termination amount, the lease and/or sale of the Hospital. Finally, G.L. Hicks was requested to provide a final cash flow analysis assuming results of an appraisal conducted by CBRE CB Richard Ellis (the "Appraisal").

Findings:

Cal-Mortgage initially requested that the amount that it would accept to terminate the Settlement Agreement would need to be at least $1,900,000. After approximately three months of negotiations, Cal-Mortgage indicated that it would be willing to consider $1,600,000 to terminate the Settlement

Agreement. It is my opinion that the $1,600,000 termination price is the lowest that Cal-Mortgage is willing to accept as consideration to terminate the Settlement Agreement.

The cash flow analysis prepared based upon the CBRE CB Richard Ellis appraisal relating to a sale or lease of the Hospital property concluded the following:

1. Continuing to lease the Hospital, either to the County or to another party after termination of the County Lease, at the appraised fair market rental rate provides the greatest value to the District.

2. A lease of the Hospital, either to the County by way of its unilateral right to extend the County Lease for ten years subsequent to its expiration of July 31, 2018, or by way of a lease of the Hospital to another party in the event the County did not elect to extend the County Lease beyond July 31, 2018, would generate substantially more cash flow to the District if it were to terminate the Settlement Agreement for $1,600,000 than if it were not to terminate the Settlement Agreement for $1,600,000. The cash flow analysis based upon the appraisal's fair market net lease rate produces approximately $8,250,000 in additional cash flow to the District if it were to now terminate the Settlement Agreement for $1,600,000, than if it were not to terminate the Settlement Agreement. This positive cash flow represents approximately $3,473,380 in present value dollars if discounted at a 6% discount rate.

3. A sale of the Hospital (assuming the County does not extend the County Lease for an additional ten years) provides a positive cash flow of approximately $324,000 when terminated but a negative present value amount of approximately $283,000. Thus a sale of the Hospital would produce essentially a break-even result for the District should the County elect not to extend the County Lease for the additional ten years beyond its maturity. Keep in mind that if the District were to sell the Hospital when the County Lease was still in place, any residual amount remaining from the sale proceeds would be sent to the bankruptcy court to pay unsecured creditors, thus leaving significantly less or nothing for the District from the sale proceeds.

4. In my opinion it is unlikely the County will not elect to extend the County Lease after July 31, 2018. There are several reasons for this conclusion including: (i) the County is entrenched at the Hospital site and they have funded many improvements for the Hospital over the years so it meets their specific needs as a health clinic; (ii) the County would likely need to purchase a new facility or lease and make tenant improvements to another suitable facility; and (iii) its operations in Pittsburg are well established and it does not appear to have outgrown the Hospital. Please see the attached Analysis of Property Lease Scenarios providing cash flow analysis in support of the above findings.

Recommendation:

Based upon a review of the Pertinent Documents referenced above, the negotiated price at which Cal-Mortgage would consider termination of the Settlement Agreement, the outcome of the Appraisal and my opinion that the County would likely extend the County Lease beyond July 31, 2018, it is my recommendation that the District terminate the Settlement Agreement for $1,600,000 as soon as possible. I would suggest that the District look to fund the termination price with approximately $1,100,000 of its own cash reserves and fund the remaining balance of $500,000 through a bank loan with a local commercial bank using the County Lease payments and its tax revenues as sources of repayment for the $500,000 bank loan.

LOS MEDANOS COMMUNITY HEALTHCARE DISTRICT
ANALYSIS OF PROPERTY LEASE SCENARIOS

	Appraisal Lease		Appraisal Sale - A		Appraisal Sale - B		Lease Breakeven			
	Settlement Agreement		Settlement Agreement		Settlement Agreement		Settlement Agreement		Settlement Agreement	
	Terminated	Not Terminated	Terminated	Not Terminated	Terminated	Not Terminated	Terminated	Not Terminated	Terminated	Not Terminated
8/1/2011	($1,600,000)	$0	($1,600,000)	$0	($1,600,000)	$0	($1,600,000)	$0		
8/15/2011	100,000	0	100,000	0	100,000	0	100,000	0		
8/15/2012	100,000	0	100,000	0	100,000	0	100,000	0		
8/15/2013	100,000	0	100,000	0	100,000	0	100,000	0		
8/15/2014	100,000	0	100,000	0	100,000	0	100,000	0		
8/15/2015	100,000	0	100,000	0	100,000	0	100,000	0		
8/15/2016	100,000	0	100,000	0	100,000	0	100,000	0		
8/15/2017	100,000	0	100,000	0	100,000	0	100,000	0		
8/15/2018	1,143,752	0	0	(500,000)	0	(500,000)	150,000	(350,000)		
8/15/2019	1,143,752	0	9,450,000	8,726,260	11,830,000	11,106,260	150,000	(350,000)		
8/15/2020	1,143,752	0	0	0	0	0	150,000	0		
8/15/2021	1,143,752	0	0	0	0	0	150,000	0		
8/15/2022	1,143,752	0	0	0	0	0	150,000	0		
8/15/2023	1,143,752	0	0	0	0	0	150,000	0		
8/15/2024	1,143,752	0	0	0	0	0	150,000	0		
8/15/2025	1,143,752	0	0	0	0	0	150,000	0		
8/15/2026	1,143,752	1,143,752	0	0	0	0	150,000	150,000		
8/15/2027	1,143,752	1,143,752	0	0	0	0	150,000	150,000		
Total	$10,537,520	$2,287,504	$8,550,000	$8,226,260	$10,930,000	$10,606,260	$600,000	($400,000)		
Variance	$8,250,016		$323,740		$323,740		$1,000,000			
NPV*	$4,298,835	$825,455	$4,294,036	$4,576,749	$5,623,016	$5,905,728	($290,123)	($294,346)		
Variance	$3,473,380		($282,712)		($282,712)		$4,224			

* Net Present Value assumes a 6% discount rate.

Under both sale scenarios (Settlement Agreement Not Terminated) in 2019, the net proceeds from a sale assumes $723,740 payoff to Cal-Mortgage and no payment to unsecured creditors. This only applies if the County does not extend the lease and would be significantly less if the lease is extended.

This analysis assumes a termination price of $1,600,000 is negotiated to terminate the Settlement Agreement with OSHPD effective on August 1, 2011.