

**California Health Facilities Financing Authority (“Authority”)**  
**Agenda Item Five – Resolution No. 2011-03**  
**Downey Regional Medical-Center Hospital, Inc. – VCAP Request**

**Background**

The Authority issued \$68,845,000 in revenue bonds (the "Bonds") for the benefit of Downey Regional Medical-Center Hospital, Inc. (formerly known as Downey Community Hospital, hereinafter “Downey”) in September 1993. Downey applied a portion of the proceeds of the Bonds to refinance its acquisition of a facility known as Rio Hondo Hospital (“Rio Hondo”). Downey operated Rio Hondo as an outpatient facility until 1995 when Downey closed Rio Hondo. In 2002, Downey sold Rio Hondo to a private party for conversion to condominiums. At the time of the sale, Downey expected to spend the proceeds received from the sale of Rio Hondo for capital expenditures for its charitable purposes within two years of the sale of Rio Hondo as is permitted pursuant to the applicable provisions of the Internal Revenue Code and related regulations, in particular, Section 1.141-12 of the Treasury Regulations, and Downey has advised that Downey did in fact spend an amount in excess of the amount received from the sale of Rio Hondo within two years of the date of sale of Rio Hondo. In addition, Downey did redeem approximately \$4.5 million of Bonds in 2005. However, in April 2008, a flood occurred at Downey's principal hospital facility and a majority of Downey's records were lost. In addition, senior management has changed since the sale of Rio Hondo. As a result, Downey is unable to provide documentation indicating that all of the procedures required pursuant to Section 1.141-12 of the Treasury Regulations were followed.

To resolve situations of this type, the Internal Revenue Service provides a Voluntary Closing Agreement Program (“VCAP”). The VCAP Program requires the submission of certain information and execution of a closing agreement by the issuer of the Bonds. Therefore, Downey has requested the Authority, as issuer of the Bonds, authorize such actions as are necessary to enable Downey to resolve this situation through VCAP. Pursuant to the provisions set forth in its Loan Agreement with the Authority, including, without limitation, Section 4.2, Section 6.8, and Section 8.2 of the Loan Agreement, Downey will, of course, be responsible for the payment of any and all expenses incurred in connection with the VCAP Program and penalties levied, if any. In addition, Downey is required to indemnify the Authority pursuant to Section 8.3 of the Loan Agreement.

Staff concludes that it is desirable to authorize such actions as may be necessary pursuant to the VCAP Program to assist Downey to resolve the above-described situation. Downey is in the midst of Chapter 11 bankruptcy proceedings and is seeking to conclude that bankruptcy proceeding within the next several months<sup>1</sup>. Participation in the VCAP Program is necessary for Downey to secure bankruptcy exit financing as more specifically discussed in the next agenda item.

**Recommendation**

Staff recommends authorizing any and all actions as might be necessary in connection with the VCAP program for Downey’s Bonds.

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<sup>1</sup> Please note that any actions taken by Downey, even if approved by the Authority, will likely also be subject to approval of the bankruptcy court.