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 Sandra Shewry, Director of California  
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10 IN THE UNITED STATES DISTRICT COURT  
 11 FOR THE CENTRAL DISTRICT OF CALIFORNIA, WESTERN DIVISION

12 INDEPENDENT LIVING CENTER OF  
 13 SOUTHERN CALIFORNIA, a nonprofit  
 corporation; GRAY PANTHERS OF  
 14 SACRAMENTO, a nonprofit corporation;  
 GRAY PANTHERS OF SAN  
 15 FRANCISCO, a nonprofit corporation;  
 GERALD SHAPIRO, Pharm.D. doing  
 16 business as Uptown Pharmacy and Gift  
 Shoppe; SHARON STEEN, doing  
 17 business as Central Pharmacy; MARK  
 BECKWITH; MARGARET DOWLING;  
 18 TRAN PHARMACY, INC., a corporation,  
 doing business as Tran Pharmacy; and  
 19 JASON YOUNG,  
 20  
 21  
 22 SANDRA SHEWRY, Director of the  
 Department of Health Care Services of the  
 23 State of California; DEPARTMENT OF  
 HEALTH CARE SERVICES, a  
 24 Department of the State of California; and  
 DOES 1 through 50,  
 25  
 26 Respondents.

CV08-03315 CAS (MANx)

**RESPONDENT'S REPORT OF  
 COMPLIANCE WITH  
 AUGUST 18, 2008  
 PRELIMINARY INJUNCTION  
 ORDER**

Date: September 5, 2008  
 Time: 11:00 a.m.  
 Courtroom: 5  
 Judge: The Honorable  
 Christina A. Snyder

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1 Respondent Sandra Shewry, Director of the California Department of Health Care  
2 Services, hereby submits the declarations of Stan Rosenstein, Michael Kaufmann, and  
3 Dennis Dworman regarding Respondent's compliance with this Court's August 18,  
4 2008 Preliminary Injunction Order (Order).

5 As stated in the Rosenstein and Dworman declarations, Respondent believes that  
6 by September 5, 2008, the Medi-Cal claims processing system, excluding dental  
7 services, will be modified to stop the ten percent reduction with respect to all claims  
8 processed on or after that date with a date of service on or after August 18, 2008.  
9 (Rosenstein Decl., ¶ 9; Dworman Decl., ¶ 7.) It will then take Electronic Data  
10 Systems Corporation (EDS), the Department of Health Care Services' fiscal  
11 intermediary, until approximately September 24, 2008, to develop and implement  
12 computer changes to reprocess claims that were previously processed based on the  
13 ten percent reduction prior to September 5, 2008. (Dworman Decl., ¶ 10.) Based on  
14 an estimated volume of 7,275,000 claims to be reprocessed, it will take approximately  
15 8 weeks to reprocess those claims. (*Id.* at ¶ 12.) Thus, assuming that process begins  
16 on about September 24, 2008, it would be completed by the end of October 2008, as  
17 EDS' system is only capable of reprocessing up to 1 million claims per week. (*Id.*)

18 In addition, it is Respondent's belief that by the close of business on Tuesday,  
19 September 9, 2008, the necessary system programming changes to the claims  
20 processing system for Medi-Cal covered dental services will be completed, halting  
21 the ten percent payment reduction for claims processed on or after September 10,  
22 2008. (Kaufmann Decl., ¶ 5.) It will then take Delta Dental of California, the  
23 Medi-Cal fiscal intermediary for the claims processing system for Medi-Cal covered  
24 dental services, 3-4 weeks to reprocess the previously processed claims. (*Id.* at ¶ 6.)

25 At the August 28, 2008 hearing, the Court agreed to clarify the August 18, 2008  
26 Order with respect to pharmacies. (August 28, 2008 Transcript, p. 21, line 22, thru  
27 p. 23, line 6.) More specifically, the Court indicated that it believed the Ninth  
28 Circuit's July 11, 2008 Order found irreparable harm as to all pharmacy services, not

1 just prescription drugs. The Ninth Circuit in its July 11, 2008 Order, however,  
2 indicated that Petitioners "have demonstrated a high likelihood that the State's ten  
3 percent reduction in payments to Medi-Cal providers will cause serious irreparable  
4 injury to Medi-Cal beneficiaries while this case is pending, at least with regard to  
5 access to *prescription drugs*." (Ninth Circuit's July 11, 2008 Order, p. 4 (emphasis  
6 added).) In addition, the temporary injunction issued by the Ninth Circuit and then  
7 withdrawn applied only to "A.B. 5's ten percent reduction in the reimbursement rate  
8 for prescription drugs." (*Id.* at p. 5.) At the August 28, 2008 hearing, Respondent  
9 requested clarification of this Court's August 18, 2008 Order as to "pharmacies" since  
10 Petitioners' evidence of irreparable harm dealt only with prescription drugs, and the  
11 Ninth Circuit's July 11, 2008 Order referred only to Petitioners' evidence of access  
12 to prescription drugs. Also, the term "prescription drugs" does not apply to other  
13 services such as medical supplies that pharmacies provide to Medi-Cal recipients.  
14 There has been no evidence presented in this case with respect to whether the ten  
15 percent reduction was enacted in violation of the federal statute except with respect  
16 to prescription drugs.

17 The term "prescribed drugs" is defined in federal regulations to mean "simple or  
18 compound substances or mixtures prescribed for the cure, mitigation, or prevention  
19 of disease, or for health maintenance." (42 CFR § 440.120.) That definition certainly  
20 does not include other items that pharmacies may provide such as medical supplies.  
21 Medi-Cal regulations distinguish between "prescribed drugs" and "medical supplies."  
22 For example, title 22, California Code of Regulations sections 51313 and 51513 deal  
23 with drugs, and title 22, California Code of Regulations sections 51320, 51520, and  
24 59998 deal with medical supplies. As can be seen by comparing section 51513 to  
25 section 51520, the reimbursement methodology for drugs is totally different from the  
26 reimbursement methodology for medical supplies. Petitioners have not presented any  
27 any evidence in this case to challenge the reduced payments for medical supplies.  
28 Therefore, Respondent had no reason to present any evidence concerning its

1 assessment on whether reduced reimbursement for medical supplies complies with  
2 the federal statute. There is no evidence in the record at all concerning medical  
3 supplies. In summary, the term "prescription drugs" clearly does not encompass  
4 medical supplies or other services that pharmacies may provide. Moreover, federal  
5 Medicaid law is clear that the term "prescription drugs" does not include over the  
6 counter drugs provided by pharmacies. Specifically, 42 USC § 1396r-8, subdivision  
7 (k)(4) defines drugs that are provided over the counter as "nonprescription drugs."

8 Finally, *Lankford v. Sherman*, 451 F.3d 496 (8th Cir. 2006), cited by the Ninth  
9 Circuit in its July 11, 2008 Order, holds that State regulations regarding State funded  
10 only Medicaid services cannot be enjoined on the grounds that the regulation violates  
11 federal regulations. Here, the August 18, 2008 Preliminary Injunction Order enjoins  
12 enforcement of Welfare & Institutions Code § 14105.19(b)(1), which reduces  
13 payments for Medi-Cal fee-for-service benefits. Respondent respectfully informs this  
14 Court that the Medi-Cal program pays providers significant amounts for services that  
15 are not part of the federally approved State Medicaid plan or the federal Medicaid  
16 program.<sup>1/</sup> (Rosenstein Decl., ¶ 7.) These services include some dialysis services,  
17 total perienteral nutrition, certain mental health services, and pregnancy related  
18 services for certain eligibility categories. (*Id.*) Thus, these services are paid entirely  
19 with state funds, and they are not provided under the federal Medicaid program. (*Id.*)  
20 California also provides the full scope of Medi-Cal services to some immigrants on  
21 a state funded basis and not under the federal Medicaid program. Respondent  
22 respectfully informs this Court that in implementing the August 18, 2008 Preliminary  
23 Injunction Order, Respondent does not construe the injunction as applying to State  
24 funded only Medi-Cal services. In an effort to comply with this Court's August 18,

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27 1. For example, various services, such as prenatal services, are provided to  
28 undocumented aliens, and are not covered by the federally approved State Plan  
because they are not covered by the Federal Medicaid program. (Rosenstein Decl.,  
¶ 7.)

1 2008 Order, however, Respondent is taking the extraordinary measure of temporarily  
2 applying the injunction to even State funded only programs so that the ten percent  
3 reduction can be lifted on a more expedited basis. (Rosenstein Decl., ¶ 9.) Respondent  
4 is similarly taking the extraordinary action of at least temporarily stopping the ten  
5 percent reduction on services provided under non-Medi-Cal program. (*Id.*)

6 Petitioners allege that AB 5 is preempted by 42 U.S.C. § 1396a(a)(30)(A)  
7 (hereinafter § (a)(30)(A).) As this Court knows, § (a)(30)(A) sets forth that a State  
8 Plan must provide for payments to providers that comply with the factors of  
9 efficiency, economy, quality of care, and access. As such, § (a)(30)(A) only applies  
10 to services covered under the federally approved State plan for medical assistance,  
11 and the State only receives federal financial participation for services covered under  
12 the federally approved State Plan.

13 Respondent's understanding that the Order does not apply to State funded only  
14 Medi-Cal covered services because State funded only services are not subject to  
15 federal regulations is supported by the holding in *Lankford v. Sherman*, 451 F.3d 496  
16 (8th Cir. 2006), which was also cited by the Ninth Circuit Panel in this case. In  
17 *Lankford*, the plaintiffs, seeking injunctive relief, alleged that Missouri's regulation  
18 that eliminated Missouri's durable medical equipment program as a covered Medicaid  
19 service violated the comparability and reasonableness requirements of 42 U.S.C. §§  
20 1396a(a)(10)(B), (a)(17). *Lankford v. Sherman*, 451 F.3d at 500-501. Since the State  
21 defendant represented that it did not accept federal funds and used only state funds  
22 to provide the durable medical equipment benefits to Medicaid recipients, the Court

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1 found that the regulation did not violate the federal statutes. *Id.* at 506-07. Therefore,  
2 based on the above, Respondent does not construe the injunction as applying to State  
3 funded only Medi-Cal services.

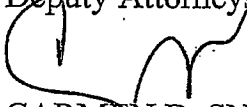
4  
5 Dated: September 4, 2008

Respectfully submitted,

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**DECLARATION OF DENNIS  
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Petitioners,

v.

22 SANDRA SHEWRY, Director of the  
 Department of Health Care Services of the  
 23 State of California; DEPARTMENT OF  
 HEALTH CARE SERVICES, a  
 24 Department of the State of California; and  
 DOES 1 through 50,

Respondents.

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1 DECLARATION OF DENNIS DWORMAN

2 I, DENNIS DWORMAN, declare as follows:

3 1. The following matters stated in this declaration are true of my personal  
4 knowledge.

5 2. I am the Regional General Manager for California Government  
6 Healthcare with Electronic Data Systems Corporation (EDS). EDS is the Medi-Cal fiscal  
7 intermediary for the Medi-Cal claims processing system, pursuant to contract with the  
8 Department of Health Care Services (DHCS), except for dental services. As the Medi-  
9 Cal fiscal intermediary, EDS is responsible for administering the claims processing  
10 system for paying all providers except dentists. This includes responsibility for making  
11 necessary system programming changes, as directed by DHCS. All decisions regarding  
12 the implementation date for programming changes are made by DHCS. Delta Dental is  
13 the fiscal intermediary for dental services covered by the Medi-Cal program. EDS has  
14 been the Medi-Cal fiscal intermediary since 1988. As Regional General Manager for  
15 California Government Healthcare, I have oversight for all aspects of EDS performance  
16 under the fiscal intermediary contract.

17 3. Assembly Bill 5 was enacted in February 2008 requiring DHCS to  
18 reduce payments for various services paid for under the Medi-Cal program and various  
19 non-Medi-Cal programs by ten percent effective for dates of service on or after July 1,  
20 2008. The programming changes necessary for EDS to implement the ten percent  
21 reduction were extensive. It took EDS approximately 1,200 person hours of labor to  
22 make the programming changes over the course of three months. As noted above, the  
23 claims processing system that EDS administers is also used for processing claims from  
24 providers under certain non-Medi-Cal programs that DHCS administers such as the  
25 California Children's Services (CCS), as well as payments to providers for certain  
26 services that are considered part of the state funded only Medi-Cal program. The ten  
27 percent payment reduction applied to services under these programs also. On June 23,

1 2008, the time-consuming process of making the necessary claims processing system  
2 changes for implementing the ten percent payment reduction was completed.

3 4. By Thursday, August 21, 2008, DHCS had notified EDS staff that the  
4 federal court had issued a preliminary injunction with respect to the ten percent payment  
5 reduction with respect to payments to various providers under the Medi-Cal program.  
6 DHCS staff then began working with EDS staff on the preliminary work necessary to  
7 comply with the court's preliminary injunction. Among the issues that needed to be  
8 addressed was how to stop the ten percent reduction for Medi-Cal payments made for  
9 services covered by the injunction but continue the reduction for payments made under  
10 non-Medi-Cal programs, such as CCS and the Genetically Handicapped Person's  
11 Program (GHPP). There was also an issue that DHCS was evaluating as to whether the  
12 court intended the injunction to apply to state funded only Medi-Cal services that were not  
13 paid for under the federal Medicaid program. And finally, DHCS was uncertain as to  
14 whether the court intended the injunction to apply to all Medi-Cal payments made to  
15 pharmacies or just payments for prescription drugs. Another issue impacting the amount  
16 of computer processing that would be necessary to fully comply with the injunction was  
17 whether the injunction applied to dates of service beginning July 1, 2008 or only dates of  
18 service on or after August 18, 2008.

19 5. DHCS advised EDS that it believes the injunction applies to Medi-Cal  
20 covered payments made to physicians, dentists, adult day health care centers,  
21 optometrists, clinics, and pharmacies with respect to prescription drugs. As I explained in  
22 my previous declaration in opposition to the motion for contempt, it is very important to  
23 understand that regardless of the date of service that the injunction takes effect, it is not  
24 possible to simply flick a switch and immediately pay to providers all the additional money  
25 they would be owed for all services back to the date that the injunction is effective.  
26 Regardless of what date the injunction is effective, there is a two step process. First, the  
27 ten percent payment reduction has to be stopped for claims processed in the future,

1 Second, previously processed claims have to be reprocessed to pay providers the  
2 additional money they are owed back to the date of service for which the injunction is  
3 effective. It can't all be done in one step with just one flick of a switch on the computer  
4 system. Whether the injunction applies to dates of service back to July 1, 2008 or only  
5 back to August 18, 2008 also impacts the process, especially with respect to step 2,

6           6. The first step of the process is to stop the ten percent reduction for  
7 prospectively processed claims. As explained in my declaration in opposition to the  
8 contempt motion, that process would take at least three weeks if we were going to  
9 program the system to stop the ten percent payment reduction only for federally funded  
10 Medi-Cal payments for physicians, optometrists, adult day health care centers, clinics,  
11 and only prescription drugs provided by pharmacies and continue the ten percent  
12 reduction for non-Medi-Cal programs such as CCS and GHPP, state funded only Medi-  
13 Cal services, and services such as medical supplies and nutritional supplements that  
14 pharmacies provide.

15           7. It is my understanding that on August 28, 2008, the federal court  
16 clarified that the injunction only applies to dates of service on or after August 18, 2008.  
17 This was an extremely important issue to get resolved before DHCS stopped the ten  
18 percent reduction on prospectively processed claims because the claims systems logic is  
19 set up to typically make changes in payment levels based on date of service. DHCS has  
20 now instructed EDS that in an effort to speed up the process of complying with the  
21 preliminary injunction, it wants EDS to stop the ten percent reduction as quickly as  
22 possible for all payments made to physicians, optometrists, adult day health care centers,  
23 clinics, and pharmacies for all services, including payments made under non-Medi-Cal  
24 programs such as CCS and GHPP and state funded only Medi-Cal services. By making  
25 this decision, the estimated time period of at least three weeks discussed above will not  
26 be required. By DHCS making the decision to stop the ten percent reduction to non-  
27 Medi-Cal programs, state funded only Medi-Cal programs, and all payments to

1 pharmacies, EDS believes that by September 5, 2008, the system will be modified to stop  
2 the ten percent reduction with respect to all claims processed on or after that date with a  
3 date of service on or after August 18, 2008, with one possible exception. The one  
4 exception concerns payments to clinics owned or operated by the County of Los Angeles.  
5 That issue is addressed in the declaration being filed by Stan Rosenstein.

6 8. Because of the decision DHCS is making to speed up compliance with  
7 the injunction on a prospective basis, it means that with respect to claims processed on  
8 or after approximately September 5, 2008, DHCS will be stopping the ten percent  
9 reduction with respect to some services that are clearly not covered by the injunction  
10 (e.g., non-Medi-Cal services) and some services for which the court may have not  
11 intended the injunction to apply (e.g., state funded only Medi-Cal and services that  
12 pharmacies provide other than prescription drugs).

13 9. It needs to be understood that for purpose of this declaration, the term  
14 "processing" of a claim means the system process of adjudicating a claim to determine if  
15 it can be approved for payment, the amount of money payable, and then sending the  
16 claim on for final payment processing. For purpose of this declaration, the term does not  
17 include the additional step of paying an approved claim, including sending a payment  
18 tape on to the State Controller's office and the time it takes for a check to be cut and  
19 mailed to a provider. For example, many claims processed prior to September 5, 2008  
20 will be paid after September 5. Also, many claims processed prior to September 5, 2008  
21 were adjudicated and sent on for final payment processing but have not yet been paid  
22 because of the lack of a state budget. Institutional providers, including some not even  
23 subject to the ten percent reduction (e.g., freestanding nursing facilities and contract  
24 hospitals) have not been paid for any services provided since July 1, 2008, because of  
25 the lack of a state budget. Claims for those providers are processed, meaning  
26 adjudicated and sent on for final payment processing, but have not yet been paid.  
27 Included among the institutional providers not being paid because of the lack of a state

1 budget are ADHCs and clinics. Claims for these services have been previously  
2 adjudicated based on applying the ten percent reduction, but they have not been paid yet  
3 because of the lack of a budget. When the state budget is ultimately passed, payments  
4 for claims that were previously processed based on the ten percent reduction but not yet  
5 paid, will finally be paid. Therefore, once the budget is finally enacted and payments are  
6 released on those claims processed prior to September 5, 2008, EDS will have to go  
7 back and pay those providers the additional money owed as part of the process  
8 described in paragraphs 10-11.

9           10. The process used to go back and reprocess previously processed  
10 claims is known as the erroneous payment correction (EPC) process. EDS is going to  
11 have to prepare more than one EPC because of the decision DHCS made to speed up  
12 the process of stopping the ten percent reduction on prospectively processed claims. An  
13 EPC is going to be needed to reprocess claims that were previously processed prior to  
14 September 5 to pay providers the additional money they are owed. Another EPC will be  
15 required to reprocess claims that were not subject to the injunction but for which the ten  
16 percent reduction was restored beginning September 5, 2008, so that DHCS can recoup  
17 excessive payments made to providers. It takes about 2 ½ weeks to develop and install  
18 computer changes for running an EPC to reprocess claims previously paid. This cannot  
19 be done until the ten percent payment reduction is lifted prospectively on the system  
20 because the process for selecting the claims to be corrected is dependent on the system  
21 changes having been made in the system before the selection process runs. So for  
22 example, assuming the ten percent payment reduction is stopped for claims processed  
23 on or after September 5, 2008, it will take EDS until approximately September 24, 2008  
24 to develop and implement computer changes for running an EPC to reprocess claims that  
25 were previously processed based on the ten percent reduction prior to September 5,  
26 2008. The EPC process that EDS manages on behalf of DHCS is only capable of  
27 reprocessing up to 1 million claims per week. Following are the tasks that EDS will have

1 to deal with after the ten percent payment reduction is stopped on prospectively  
2 processed claims on or about September 5, 2008.

3 11. It will take approximately 2 ½ weeks or until about September 24, 2008,  
4 to develop and have ready an EPC program to reprocess previously processed provider  
5 claims to pay providers covered by the Injunction the additional money owed for dates of  
6 service on or after August 18, 2008. Based on an estimated volume of 7,275,000 claims  
7 to be reprocessed, it will take approximately 8 weeks to reprocess those claims based on  
8 the 1 million per week limit. Thus, assuming that process begins on about September 24,  
9 2008, it would be completed by the end of October 2008.

10 12. Additionally, EDS will have to do the computer programming to restore  
11 the ten percent payment reduction for services that are clearly not subject to the  
12 injunction (e.g., non-Medi-Cal programs). Furthermore, assuming the court clarifies that  
13 it did not intend for the injunction to apply to state funded only services that are not  
14 covered under the federal Medicaid program, DHCS may ask EDS to develop a computer  
15 program to restore the ten percent reduction for those services. The computer  
16 programming involved in such a project could take several weeks. Also, if the court  
17 clarifies that it intended for the injunction only to apply to prescription drugs and not other  
18 services that pharmacies provide, then DHCS will ask EDS to develop a computer  
19 program to restore the ten percent reduction for the non-prescription drug services. The  
20 computer programming required for that project will take approximately three weeks.  
21 EDS will restore the ten percent reduction for some or all of the non-Medi-Cal programs,  
22 state funded only services, or non-prescription drugs, if DHCS directs it to do so. Then  
23 after restoring the ten percent reduction, EDS would have to develop an EPC program to  
24 go back and reprocess claims to recoup payments from providers. For example, EDS  
25 estimates that there could be 301,500 non-Medi-Cal claims that will have to be  
26 reprocessed after restoring the ten percent reduction in order for DHCS to recoup money  
27 from providers.

1 13. Because of the multiple programming projects necessary to comply  
2 with the Injunction and the various EPCs necessary to reprocess previously processed  
3 claims, there are other ongoing Medi-Cal projects that will have to be delayed based on  
4 the direction of DHCS. Moreover, because there has been no State Budget, the Medi-  
5 Cal program has not been making any payments for some Medi-Cal covered services,  
6 including providers that are not even subject to the ten percent payment reduction, such  
7 as certain long term care providers and contract hospitals. As soon as the Budget is  
8 signed, the claims processing system will be able to finally process payments for many  
9 providers that have been held up by the lack of a State Budget. Another over-all limit on  
10 the claims processing system is that it cannot process more than \$1 billion in payment  
11 weekly per claim type (for example, medical services, pharmacy, long term care, etc.)  
12 The huge amount of money that may have to be paid once the Budget is enacted could  
13 place another limitation on the time within which the system can be programmed to pay  
14 providers additional money owed pursuant to the Injunction.

15 14. It will take at least 1,000 person hours to complete the entire project of  
16 stopping the ten percent reduction prospectively, restore the ten percent reduction for  
17 some services, and then develop and implement the various EPC projects that will be  
18 needed to pay providers additional money on previously processed claims or recoup  
19 excessive payments not required by the Injunction. This may result in other important  
20 projects related to the administration of the Medi-Cal program being delayed based on  
21 the direction of DHCS.

22 I declare under penalty of perjury under the laws of the State of California  
23 that the foregoing is true and correct. Executed at Plano, Texas, this 4<sup>th</sup> day of  
24 September 2008.

25   
26 DENNIS DWORMAN  
27

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1 reduction should be stopped. That means that for claims processed after that date, the  
2 ten percent reduction would not be applied. By "processed," I mean the process of a  
3 claim being adjudicated by the claims system to determine whether it is payable and if so,  
4 the amount of payment, and then being sent on for payment processing. In other words,  
5 many claims processed prior to September 9, will be paid after that date. Those claims  
6 will have to be reprocessed for dates of service on or after August 18, 2008 pursuant to the  
7 process described in paragraph 6.

8           6. After the ten percent payment reduction is stopped on prospectively  
9 processed claims, it will be necessary for Delta Dental to go back and reprocess claims  
10 that were previously processed for dates of service on or after August 18 to pay dentists  
11 the additional amount of money they are owed based on the preliminary injunction. Now  
12 that we know the injunction only applies to dates of service on or after August 18, 2008,  
13 we have estimated that the number of claims that will have to be reprocessed at  
14 approximately 300,000. The claims processing system only allows us to pay a maximum  
15 of 100,000 reprocessed claims each week. We estimate that the first batch of  
16 reprocessed claims will be ready for payment September 18, 2008 and that the  
17 reprocessing of previously processed claims should be completed by approximately  
18 October 2, 2008. Delta Dental's ability to pay the additional money owed pursuant to the  
19 process described in this paragraph is subject to the State Budget situation.

20           I declare under penalty of perjury under the laws of the State of California  
21 that the foregoing is true and correct. Executed at Rancho Cordova, California, this 4<sup>th</sup>  
22 day of September 2008,

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MICHAEL B. KAUFMANN

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10 IN THE UNITED STATES DISTRICT COURT  
 11 FOR THE CENTRAL DISTRICT OF CALIFORNIA, WESTERN DIVISION

12 INDEPENDENT LIVING CENTER OF  
 13 SOUTHERN CALIFORNIA, a nonprofit  
 corporation; GRAY PANTHERS OF  
 14 SACRAMENTO, a nonprofit corporation;  
 GRAY PANTHERS OF SAN  
 15 FRANCISCO, a nonprofit corporation;  
 GERALD SHAPIRO, Pharm.D. doing  
 16 business as Uptown Pharmacy and Gift  
 Shoppe; SHARON STEEN, doing  
 17 business as Central Pharmacy; MARK  
 BECKWITH; MARGARET DOWLING;  
 18 TRAN PHARMACY, INC., a corporation,  
 doing business as Tran Pharmacy; and  
 19 JASON YOUNG,

20 Petitioners,

21 v.

22 SANDRA SHEWRY, Director of the  
 Department of Health Care Services of the  
 23 State of California; DEPARTMENT OF  
 HEALTH CARE SERVICES, a  
 24 Department of the State of California; and  
 DOES 1 through 50,

25 Respondents.  
 26  
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 28

CV08-03315 CAS (MANx)

**DECLARATION OF STAN  
 ROSENSTEIN RE:  
 RESPONDENT'S  
 COMPLIANCE WITH  
 AUGUST 18, 2008 ORDER**

Date: September 5, 2008  
 Time: 11:00 a.m.  
 Courtroom: 5  
 Judge: The Honorable  
 Christina A. Snyder

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DECLARATION OF STAN ROSENSTEIN

I, STAN ROSENSTEIN, declare as follows:

1. The following matters stated in this declaration are true of my personal knowledge.

2. I am employed by the California Department of Health Care Services (DHCS) as the Chief Deputy Director for health programs. In that capacity, I am in charge of administering the Medi-Cal program. Previously, I was Deputy Director for Medical Care Services. In that position I was also in charge of the State's Medi-Cal program. I have worked in various analytic and managerial positions in the Medi-Cal program for over 31 years. In my past and current positions, I have frequently testified before the Legislature and met with legislators concerning proposed legislation related to the Medi-Cal program and the budget for the Medi-Cal program.

3. DHCS was first notified at almost close of business on Tuesday, August 19, 2008, that on August 18, 2008, the federal court had issued a preliminary injunction requiring the State to cease applying the ten percent reduction for Medi-Cal payments for certain services. As will be explained in more detail below, DHCS determined that the only way to speed up its compliance with the injunction was to stop the ten percent reduction with respect to services that are not even subject to the injunction, such as services paid for under non-Medi-Cal programs. As a result of DHCS deciding to take this action, it is anticipated that the ten percent payment reduction will be stopped with respect to most services covered by the injunction with respect to claims that are processed beginning September 5, 2008.

4. On Wednesday, August 20, 2008, I met with various DHCS staff and management, including legal staff, to discuss the decision and its scope. DHCS attorneys reviewed the decision and provided their interpretation. As discussed in my declaration in support of a stay of the injunction pending appeal, DHCS concluded that the injunction appeared to apply to Medi-Cal payments for physicians, dentists,

1 optometrists, adult day health care centers, clinics, and prescription drugs. DHCS is  
2 uncertain as to which other services, if any, the court may have intended the injunction to  
3 apply. DHCS attorneys also advised that there was a major issue as to whether a  
4 federal court had jurisdiction to issue an order requiring a State to pay money  
5 retroactively for services provided prior to the time that the court has found a violation of  
6 law. The attorneys advised that they intended to seek clarification from the court that the  
7 injunction only applied to dates of service on or after August 18, 2008, when the court  
8 first determined that there was a violation of federal law. The attorneys also advised that  
9 they were seeking a request for a stay of the injunction pending appeal. In the meantime,  
10 the attorneys advised that DHCS needed to move forward with doing whatever was  
11 necessary to comply with the injunction as soon as possible if the court did not grant a  
12 stay.

13           5. By Thursday, August 21, 2008, DHCS was well underway in evaluating  
14 what would have to be done to comply with the injunction. DHCS contracts with two  
15 different Medi-Cal fiscal intermediaries, which are responsible for administering the  
16 claims processing systems for the Medi-Cal program. The Medi-Cal fiscal intermediary  
17 for dental services is Delta Dental. The Medi-Cal fiscal intermediary for other Medi-Cal  
18 covered services is Electronic Data Systems (EDS). In discussions on August 21 with  
19 both EDS and Delta Dental about the injunction, it was evident that significant  
20 administrative time and cost will be required to comply with the injunction. For example,  
21 after Assembly Bill 5 was enacted in February 2008, the programming changes that were  
22 required to implement the ten percent reduction in the EDS operated claims processing  
23 system required approximately 1,200 hours of labor over the course of three months.  
24 Typically we ask the Legislature for at least 3 months to implement a change that will  
25 involve making major changes to the claims processing system such as this. That is why  
26 the statute provided that implementation would not occur until July 1, 2008. The  
27 programming changes to implement the ten percent payment reduction were not

1 completed until June 23, 2008. Obviously then, the programming changes necessary to  
2 reverse the process cannot be done overnight. Both EDS and Delta Dental will have to  
3 make programming changes to their respective claims processing systems to stop the  
4 ten percent reduction.

5           6. In my declaration in opposition to the motion for contempt, I explained  
6 various issues that would delay our ability to comply with the injunction as quickly as the  
7 plaintiffs might desire. For example, one issue relates to the fact that the injunction  
8 clearly only applies to federally funded Medi-Cal payments that were reduced in  
9 accordance with Welfare and Institutions Code section 14105.19 (b)(1). The preliminary  
10 injunction does not apply to the ten percent reduction applied to payments under various  
11 non-Medi-Cal programs in accordance with Welfare and Institutions Code section  
12 14105.19(b)(2), such as the California Children's Services program (CCS) and the  
13 Genetically Handicapped Person's Program (GHPP). The claims processing systems  
14 that EDS and Delta Dental administer for Medi-Cal payments are also used to process  
15 claims for these other non-Medi-Cal programs. Programming the claims system to stop  
16 the ten percent reduction with respect to Medi-Cal payments for certain services (e.g.,  
17 physicians), but to continue the ten percent reduction for payments made for those same  
18 services under non-Medi-Cal programs such as CCS and GHPP is one of the things that  
19 lengthens, by at least 1 ½ weeks, the time it takes to program the system to stop the ten  
20 percent reduction with respect to Medi-Cal payments.

21           7. Another issue discussed in my declaration opposing the motion for  
22 contempt is the question of whether the court intended the injunction to apply to state  
23 funded only Medi-Cal payments. The Medi-Cal program pays providers significant  
24 amounts for services that are not covered by federal Medicaid law and thus, the federal  
25 government contributes no federal financial participation. The services are not covered  
26 by the federally approved State Plan. For example, certain services are provided on a  
27 state funded basis only, such as some dialysis services, nursing home care for

1 immigrants not eligible for federal funding, minor consent services, total perinatal  
2 nutrition, certain mental health services, and pregnancy related services for certain  
3 eligibility categories. These are examples of services that are simply not covered under  
4 the federal Medicaid program. Additionally, certain immigrants receive state funded only  
5 full scope Medi-Cal services. This includes qualified legal immigrants who have been in  
6 the country for less than five years. Federal Medicaid law does not cover the full-scope  
7 of Medi-Cal covered services that the State provides to persons in these immigrant  
8 eligibility categories. They are paid for by California on a state funded basis only. DHCS  
9 attorneys have advised that according to case law, federal Medicaid statutes do not apply  
10 to state funded only services that are not covered by federal Medicaid law. Thus, DHCS  
11 was uncertain whether the court intended for the preliminary injunction to apply to  
12 payments that California makes under its state funded only Medi-Cal program that are  
13 not even covered by federal Medicaid law. Programming the claims system to stop the  
14 ten percent reduction with respect to federally funded Medi-Cal payments for certain  
15 services (e.g., physicians), but to continue the ten percent reduction for payments made  
16 those same services on a state funded only basis by Medi-Cal would significantly  
17 lengthen, by a minimum of three weeks, the time it takes to program the claims system to  
18 stop the ten percent reduction with respect to payments that are covered by the federal  
19 Medicaid law.

20           8. Another issue discussed in my declaration opposing the motion for  
21 contempt and in my declaration in support of a stay was prescription drugs. While the  
22 injunction specifically says to stop the ten percent payment reduction for Medi-Cal  
23 payments to pharmacies, there is no discussion in the decision as to whether reduced  
24 payments for other services that pharmacies provide, such as nutritional supplements  
25 and medical supplies, violates the federal statute. There was also no discussion of  
26 whether irreparable harm would occur from a ten percent reduction in payments for the  
27 other services that pharmacies provide. In its July 11, 2008 ruling, the federal court of

1 appeals only issued an interim injunction with respect to "prescription drugs." Therefore,  
2 DHCS attorneys advised me that it was unclear whether the court intended the  
3 preliminary injunction to apply to payments made to pharmacies for all services or only  
4 for prescription drugs. Programming the claims system to stop the ten percent reduction  
5 with respect to Medi-Cal payments for prescription drugs, but continuing the ten percent  
6 reduction with respect to Medi-Cal payments for other services that pharmacies provide,  
7 such as medical supplies and nutritional supplements, would significantly lengthen, by a  
8 minimum of three weeks, the time necessary to program the claims system to stop the  
9 ten percent reduction with respect to payments for prescription drugs.

10           9. The State's attorneys advised that during a hearing on August 28, 2008,  
11 the court said it expected things to be done quicker than was being estimated in  
12 declarations filed by myself and by Dennis Dworman of EDS in opposition to the motion  
13 for contempt. Therefore, DHCS has decided that the only way to speed things up will be  
14 to stop the ten percent reduction on payments that are either clearly or arguably not even  
15 subject to the preliminary injunction. Specifically, directions have been given to EDS to  
16 program the claims system to stop the ten percent reduction on all payments, including  
17 those made under non-Medi-Cal programs such as CCS and GHPP, and state funded  
18 only Medi-Cal programs, for the specific providers identified in the injunction, which are  
19 physicians, optometrists, adult day health care centers, clinics, and pharmacies.  
20 Additionally, EDS has been instructed to stop the ten percent reduction with respect to all  
21 payments to pharmacies, including payments for services such as medical supplies and  
22 nutritional supplements for which the court made no findings in its ruling of August 18,  
23 2008. By taking this course, EDS estimates that by Friday, September 5, 2008, the  
24 claims system will have been programmed so that claims processed on or after that date  
25 for dates of service on or after August 18, 2008 will not have the ten percent reduction  
26 applied, with the exceptions discussed in paragraph 10.

27

1                   10. Directions have been given to Delta Dental to program its claims  
2 system to stop the ten percent payment reduction for dentists. Delta Dental has indicated  
3 that the ten percent reduction will be stopped on dental claims processed on or after  
4 September 10, 2008. Because unique payment rates are paid to outpatient clinics  
5 owned and operated by the County of Los Angeles, the DHCS Provider Enrollment  
6 Branch must make a special modification to the system to stop the ten percent reduction  
7 in payments for the LA County operated clinics. We estimate that change will be made  
8 so that the ten percent reduction will be stopped on claims for the LA clinics that are  
9 processed on or after September 11, 2008. Other than those two exceptions, we believe  
10 that the ten percent reduction will be stopped for the other services that DHCS  
11 understands are subject to the injunction with respect to claims processed on or after  
12 September 5, 2008. At this time, DHCS has not given any directions to EDS to stop the  
13 ten percent reduction on any other providers because it is uncertain as to which other  
14 providers, if any, the court intended the injunction to apply. As noted in my declaration in  
15 support of a stay, there was no evidence presented by the parties with respect to the  
16 impact of the ten percent reduction on other providers and the court made no findings of  
17 irreparable harm with respect to any other providers.

18                   11. By following the option discussed in paragraph 9, DHCS will be  
19 stopping the ten percent reduction for some services clearly not covered by the injunction  
20 and other services that the court may not have intended to be covered by the injunction.  
21 As explained by Dennis Dworman in his declaration, modifying the amount paid to  
22 providers for services provided on or after a specific date is always a two step process.  
23 Step 1 is to change how much is paid on claims that are processed on or after the date  
24 that a payment change is made in the system. Step 2 is to go back and reprocess  
25 previously processed claims to either pay providers additional money owed or to recoup  
26 money from the providers that was paid in excess. Thus, assuming the system is  
27 modified on September 5 with respect to prospectively processed claims, one of the

1 things that EDS will have to do is the programming work necessary to reprocess  
2 previously processed claims for dates of service on or after August 18, 2008. This is a  
3 labor and computer intensive lengthy process, as will be explained in the declaration of  
4 Mr. Dworman. Additionally, it will be necessary for EDS to program the system to restore  
5 the ten percent payment reduction for some services such as those provided under non-  
6 Medi-Cal programs and services provided by pharmacies other than prescription drugs,  
7 based on the court's ruling on Respondent's motion to alter or amend the preliminary  
8 injunction. Programming the system to restore the ten percent reduction for any of these  
9 services will also take time. In other words, once the ten percent reduction on  
10 prospective claims is stopped, EDS will have to program the system to restore the ten  
11 percent reduction on claims for services (e.g., such as non-Medi-Cal covered services)  
12 and then recoup excess payments that were made to providers in an effort to speed up  
13 our compliance with the injunction. Mr. Dworman will explain the time and cost involved  
14 in this effort.

15 I declare under penalty of perjury under the laws of the State of California  
16 that the foregoing is true and correct. Executed at Sacramento, California, this 4<sup>th</sup> day of  
17 September, 2008.

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19 STAN ROSENSTEIN

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