



*Mills-Peninsula
Health Services*

A Sutter Health Affiliate

1783 El Camino Real
Burlingame, CA 94010
650.696.5400

Peninsula Healthcare District
1783 El Camino Real
Burlingame, CA 94010
Attn: Donald E. Newman, M.D., Chair

Re: Restructured Relationship with Mills-Peninsula Health Services

Dear Dr. Newman:

This letter formally acknowledges Mills-Peninsula Health Services ("MPHS") is continuing its planning process, with input from the Peninsula Healthcare District ("District"), to plan and evaluate the construction of a facility to replace Peninsula Medical Center with a facility that meets state-mandated seismic standards. This planning process produced a Master Plan that was approved by the District, MPHS and Sutter Health, and an Environmental Impact Report has been filed and is currently in process with the City of Burlingame.

MPHS currently leases Peninsula Medical Center from the District pursuant to the Amended and Restated Lease between the parties dated as of January 25, 1985 (the "Existing Lease"). MPHS and the District anticipate that they would enter into an amendment to the Existing Lease (the "Interim Lease") for MPHS to continue operation of Peninsula Medical Center during construction of the new facility, and a new fifty (50) year ground lease (the "Ground Lease") to replace the Interim Lease once the new facility has been constructed. In addition to the Ground Lease, the parties anticipate entering into a Development Agreement pursuant to which MPHS would agree to construct and own a "state of art" replacement facility at the Peninsula Medical Center site that would conform with state-mandated seismic standards. Further, the parties anticipate entering into other agreements for MPHS to transfer certain properties, including medical office buildings, to the District. These transactions, together with the Interim Lease, the Ground Lease, the Development Agreement and other definitive agreements, shall collectively be referred to as the "Restructured Relationship." The existing litigation between the District, MPHS and Sutter Health would be dismissed with prejudice upon commencement of the Restructured Relationship if not earlier dismissed. The terms of this letter are intended to document discussions of the parties to date, but with the exception of Paragraphs B and C, the terms of this letter are not legally binding and enforceable except to the extent described in Paragraph E hereof.

A. Negotiations. Upon execution of this letter, the District and MPHS intend to diligently negotiate with the purpose of agreeing upon the terms of an Interim Lease, a Ground Lease, a Development Agreement and other definitive agreements (collectively, the "Agreements"); all as described in the Term Sheet attached hereto as Attachment 1 (the "Term Sheet"). District, MPHS and Sutter Health expect that the principal terms of the Agreements

shall substantially reflect the provisions of the Term Sheet. However, neither the Term Sheet nor this letter contains binding agreements of the District, MPHS or Sutter Health, except for the provisions of Paragraphs B and C which are binding. All tentative agreements shall become binding only upon satisfaction of the conditions described in Paragraph E.

B. Exclusive Negotiations. During the period from the date of this letter through December 31, 2004 (the "Negotiating Period"), District and MPHS agree to negotiate on an exclusive basis with each other for the transactions contemplated herein. Notwithstanding the foregoing, the parties agree to continue negotiations beyond December 31, 2004, so long as they are progressing in good faith and due diligence. Should either party determine that negotiations are not so progressing, they may, at any time after December 31, 2004, terminate the Negotiating Period, and this Letter of Intent, by delivering to the other written notice of intent to terminate negotiations. Such notice shall be effective upon delivery.

C. Authorization. District, MPHS and Sutter Health represent and warrant that the execution, delivery and performance of this letter has been duly authorized by their respective Boards of Directors or the appropriate Committees thereof.

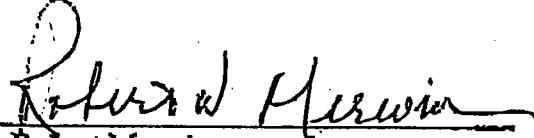
D. Legal Requirements. The terms of any Agreements entered into pursuant to this letter shall not include any provision which the general counsel of either District or MPHS determines, in good faith and relying on substantial legal authority, will violate or create substantial risk of violating any (i) of the state or federal antitrust laws; (ii) of the Medicare and/or Medicaid statutes or regulations; (iii) state or federal laws and regulations imposed upon tax-exempt entities or upon entities financed through tax-exempt bonds; (iv) of the Health Care District Law; (v) binding and enforceable contracts to which either District or MPHS is a party; or (vi) other state or federal law which governs the activities of either party.

E. Effect of Letter. This is a letter of intent only. It does not bind District, MPHS or Sutter Health to consummate the Restructured Relationship and no party shall be obligated to proceed with the Restructured Relationship unless each of the following conditions is satisfied: (i) definitive written Agreements are reached and consents obtained; (ii) each party's Board of Directors has approved the definitive written Agreements, which approval may be withheld at the sole discretion of any such Board; (iii) voter approval of the residents of the District has been received for the actions described in Section 7.B of the Term Sheet; and (iv) the definitive written Agreements have been executed by authorized representatives of each party thereto.

MPHS is excited by the opportunities presented by this Restructured Relationship. We look forward to continuing to work with you.

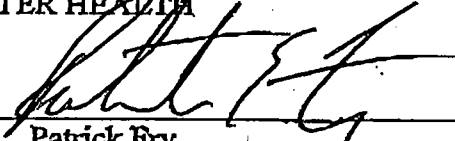
Sincerely yours,

MILLS-PENINSULA HEALTH SERVICES



By: Robert Merwin
Its: Chief Executive Officer

SUTTER HEALTH



By: Patrick Fry
Its: Executive Vice President and
Chief Operating Officer

September 10, 2004

Accepted and approved as of the ___ day of September 2004.

PENINSULA HEALTHCARE DISTRICT

Donald E. Newman, M.D.
Chair

Attachment 1

TERM SHEET

Restructured Relationship Between Peninsula Healthcare District and Mills-Peninsula Health Services

HISTORY

The Peninsula Healthcare District ("District") currently owns the site of the existing Peninsula Medical Center (1783 El Camino Real, Burlingame, California) (the "Existing Hospital Site") and Peninsula Medical Center.

In 1985, the District owned and operated Peninsula Hospital and Medical Center (known today as Peninsula Medical Center), and a predecessor of Mills-Peninsula Health Services ("MPHS") owned and operated Mills Hospital. Both hospitals were general acute care hospitals serving the residents of the District. The two parties sought to provide improved hospital services to residents of the District and greater efficiencies by merging the operations of the two hospitals (the "1985 Transaction").

To effect the 1985 Transaction, the District leased the Existing Hospital Site and Peninsula Medical Center to MPHS pursuant to the Amended and Restated Lease between the District and MPHS dated as of January 25, 1985 (the "Existing Lease"), and donated to a predecessor corporation related to MPHS (which later donated to MPHS) the following properties:

- (a) 1515 Trousdale Drive (land only);
- (b) 1791 El Camino Real (commonly known as the Blood Bank and Front Lawn);
- (c) 1730 Marco Polo Way (including access easement);
- (d) 1811 Trousdale Drive;
- (e) 1600 Trousdale Drive (land only);
- (f) 1848-50 El Camino Real; and
- (g) 1720 El Camino Real (50% only).

A protracted lawsuit over the legality of the Existing Lease and the adoption of the stringent SB 1953 seismic standards have prompted MPHS and the District to consider a new lease arrangement. The District and MPHS now share a mutual desire to establish a new and beneficial relationship centered on a long-term ground lease arrangement that would foster development by MPHS of a new state-of-the-art medical center.

The District has concluded that the merger of Peninsula Medical Center and Mills Hospital and the subsequent realignment of operations has been of substantial benefit to the healthcare needs of its community and the District desires to preserve this achievement. The District also believes that MPHS has been a successful and beneficial operator of Peninsula Medical Center and has embarked on several years of negotiations out of a desire to retain

MPHS as the operator of a new full service acute care hospital campus designed to meet the long-term healthcare needs of the community.

Since the 1985 Transaction, MPHS and its predecessors have expanded the scope and quality of the hospital services provided to the residents of the District, made significant capital updates and improvements to both Peninsula Medical Center and Mills Hospital, consolidated all general acute care services at Peninsula Medical Center and established Mills Hospital as a facility which provides rehabilitation and outpatient services, all while maintaining economic balance at a time when other hospitals owned or leased by healthcare districts were economically failing.

The Existing Lease from the District to MPHS of the Existing Hospital Site and Peninsula Medical Center will expire on January 31, 2015, at which time the existing facility, and the Front Lawn and Marco Polo parcels will revert to full ownership and control by the District.

Peninsula Medical Center will need substantial modification to comply with the SB 1953 seismic standards. If Peninsula Medical Center fails to comply with these standards, the law will require Peninsula Medical Center to cease operations as a general acute care hospital on January 1, 2013. Based on independent engineering studies, both MPHS and the District have concluded that compliance with these seismic standards is more efficiently and economically achieved by construction of a new facility rather than substantial reconstruction of Peninsula Medical Center.

Both the District and MPHS have expended substantial time and resources independently studying the strategic and land use options available to the community, leading to the conclusion of these Terms for a Restructured Relationship as the vehicle for bringing to this community a 50-year commitment for the operation of the new campus, with the provision of full time basic emergency services at the core of that commitment. The District believes that MPHS' strategic alliance with Sutter Health lends that organization's substantial health services network strength, financing ability and credibility to that commitment.

The District and MPHS seek to continue to provide health care services to the residents of the District for years to come by MPHS' construction and operation of a new facility. Toward that end, the District and MPHS have engaged in a planning process and produced a Master Plan that was approved by the District, MPHS and Sutter Health. An Environmental Impact Report ("EIR") has been filed and is currently in process with the City of Burlingame ("City"). A copy of the EIR is attached as Attachment 1-A. A copy of the site plan is attached for reference only as Attachment 1-B ("Site Plan").

MPHS is dedicated to the provision of general acute care health services, including full-time basic emergency services, to the residents of the District at the existing facility pending planning and construction of the new facility. Toward that end, MPHS has funded over \$6 million of aesthetic refurbishment to the existing facility so that it may appropriately serve the health care needs of the community until the new facility is constructed.

TERMS OF RESTRUCTURED RELATIONSHIP

1. Ownership and Lease of Properties.

A. Transfer of Properties. Promptly after Closing (as defined in Section 7, and includes the Voter Approval described in Section 7.B and Validation described in Section 7.D), MPHS and the District would sign an Interim Lease, a Ground Lease, a Development Agreement and other definitive agreements ("Definitive Agreements") under which MPHS would transfer to the District MPHS' interest in the following properties (the "Transferred Properties"):

- (1) 1515 Trousdale Drive (land only);
- (2) 1791 El Camino Real (commonly known as the Blood Bank and Front Lawn);
- (3) 1730 Marco Polo Way (including access easement);
- (4) 1811 Trousdale Drive;
- (5) 1600 Trousdale Drive (land only);
- (6) 1848-50 El Camino Real.

All Transferred Properties shall be transferred free and clear of all liens except for liens and leases in the ordinary course of business or existing at transfer from the District in the 1985 Transaction.

The District will terminate in a timely manner any leases with third parties of building space at 1515 Trousdale Drive and 1791 El Camino Real to allow demolition of such buildings for the construction of the new general acute care hospital to be built by MPHS (the "New Facility").

B. Ground Lease of New Peninsula Site. To construct the New Facility, MPHS will require, pursuant to the terms of the Ground Lease, the lease for 50 years of all of the District's real property necessary for the construction and operation of the New Facility, anticipated to be approximately 21 acres and to consist of the following properties ("New Peninsula Site"):

- (1) 1515 Trousdale Drive;
- (2) 1791 El Camino Real (commonly known as the Blood Bank and Front Lawn);
- (3) 1811 Trousdale Drive; and

(4) portion of 1783 El Camino Real (the Existing Hospital Site).

(See Section 5 for additional terms of the Ground Lease.)

After Closing, the District shall continue to lease to MPHS the Existing Hospital Site pursuant to the terms of the Interim Lease until the Start Service Date (defined below in Section 3), and then the New Peninsula Site shall be leased to MPHS pursuant to the terms of the Ground Lease.

C. District's Retained Property. The District will retain its property not necessary for the construction and operation of the New Facility, anticipated to be approximately 5 acres (the "District Controlled Land"). The District will make such portion of the District Controlled Land available to MPHS pursuant to one or more separate shorter-term leases should MPHS require additional surface parking or additional construction uses.

Upon demolition of Peninsula Medical Center and related structures and after the Start Service Date of the New Facility, the District would assume control of the District Controlled Land for use for health care purposes which are non-competitive with services or programs of MPHS located within the District. At least once annually during the term of the Ground Lease, MPHS would provide the District with a complete updated list of services or programs actually being provided by MPHS within the District (the "Existing Program List"). The District would not use District Controlled Land for purposes that are competitive with any service on the Existing Program List without the consent of MPHS, which consent shall not be unreasonably withheld. If MPHS does not respond within ninety (90) days to a District request to use District Controlled Land for a purpose which is competitive with a service on the Existing Program List, MPHS shall be deemed to have consented. Further, if the District-approved Definitive Agreements provide for a service or program that MPHS intends to commence at a specified future date (hereafter, an "Approved Future Service"), the District shall not, without the prior written consent of MPHS, which shall not be unreasonably withheld, use District Controlled Land for purposes which are competitive with any Approved Future Service, provided that construction of any facilities required for such Approved Future Service is commenced within three (3) years of the construction commencement date set forth in the Definitive Agreements, and that construction is completed expeditiously.

D. MPHS' Payment for MOB Property. MPHS shall retain ownership of 1720 El Camino Real and will pay to the District six million six hundred fifty thousand dollars (\$6,650,000) for a fifty percent (50%) interest. This fifty percent (50%) interest represents the ownership interest transferred from the District as part of the 1985 Transaction.

E. Property Use. The entire District property (consisting of approximately 26 acres), exclusive of 1730 Marco Polo Way, shall be subject to a deed restriction that the property shall be used only for health care and health care related purposes operated on a non-profit basis, and in the operation of an acute care general hospital, the operator of the hospital must offer the full range of hospital services, including reproductive services.

2. District's Oversight Role and Other MPHS Covenants.

A. Before and During Construction of New Facility. Two members of the District Board currently serve (and will continue to serve) on MPHS' Hospital Building Committee during the design phase of the construction project. MPHS will continue to provide quarterly status reports to the District on the project.

B. Maintenance of Services Obligations.

(1) Community Hospital Standard. MPHS shall operate the New Facility and services at a level of accessibility to patients and physicians, quality, technology and staffing that complies with law, regulations, accreditation, Medicare conditions and customary practices of comparable hospitals on a regional, statewide or nationwide basis during the term of the Ground Lease.

(2) Licensed General Acute Care Hospital. MPHS will maintain a general acute care licensed hospital with a 24/7 walk-in basic emergency room at the New Facility during the term of the Ground Lease.

(3) Maintenance of Acute Care and Emergency Services. MPHS will provide those clinical services at Peninsula Medical Center during the term of the Interim Lease and at the New Facility during the term of the Ground Lease as required under regulation for licensure as a general acute care hospital and basic level walk-in emergency services.

(4) Maintenance of Core Clinical Services. At the New Facility during the term of the Ground Lease, MPHS will maintain those clinical services listed on Attachment 1-C ("Clinical Services") unless: (a) the District and MPHS agree to no longer provide a service; (b) MPHS is otherwise required to comply with statute, regulation or order; or (c) the District and MPHS comply with the below process:

(a) MPHS Board of Directors approves of the termination of a service;

(b) MPHS consults with the District and the leaderships of both MPHS' nursing staff and professional staff;

(c) MPHS holds a minimum of two (2) public meetings to discuss termination of a service;

(d) The District approves of the termination of a service. The District's approval shall be sought if MPHS demonstrates one of the following:

(i) The service is economically infeasible to MPHS because the service's direct revenues cannot cover the expenses for providing that service and MPHS demonstrates it cannot afford to sustain these losses;

(ii) Quality is at risk or compromised because of low volume as demonstrated by nationally recognized standards; or

(iii) No community need exists for the service or another provider of that service or a new service demonstrates that it will meet community need.

The District and MPHS agree that the grounds for terminating a service should be construed reasonably and take into account the following:

(1) With regard to the economic reasons for terminating a service, MPHS' should use an objective standard to reference its earnings so that MPHS can objectively demonstrate that maintaining the service would not be economically feasible for MPHS. The District and MPHS shall submit verification of MPHS earnings to a mutually agreed upon third party neutral auditor if a dispute arises between the parties.

(2) With regard to quality as demonstrated by nationally recognized standards, the parties agree that standards developed and set forth by relevant national health care societies are acceptable recognized standards if reasonable and appropriate to apply in the setting at issue.

Any dispute as to termination of a service will be submitted to binding arbitration by an independent, nationally recognized accounting or healthcare management consultant, or by an AAA or JAMS arbitrator, or as otherwise mutually agreed by the parties. For example, if the District disagreed with MPHS' belief that one of the above factors to terminate a service exists with respect to the Clinical Service proposed to be terminated, the issue would be submitted to binding arbitration. If the arbitrator determined by a preponderance of the evidence that a factor to terminate a service existed with respect to the Clinical Service proposed to be terminated, MPHS could terminate such Clinical Service; if the arbitrator determined that a preponderance of the evidence did not support the existence of a factor to terminate a service with respect to the Clinical Service, MPHS could not terminate such Clinical Service, and MPHS could not request termination of the same Clinical Service for a period of eighteen (18) months from the date of the arbitrator's determination.

If a service may be or is terminated solely for financial reasons, the District may fund the continuation of this service or subsidize net losses incurred by MPHS for continuing to provide this service.

MPHS will provide for a new clinical service to be added to those services listed on Attachment 1-C and maintain this service subject to termination in accordance with the process set forth above at such time as the new service becomes a sustainable and significant service provided by MPHS.

If MPHS' obligations to provide services pursuant to this Section 2.B is prevented or delayed by reason of any act of God or any act of the District or third party outside of MPHS'

control or not MPHS' fault (including earthquake, natural disaster, terrorism, war, strike, lockout, labor trouble, lack of physician availability, inability to secure materials, restrictive governmental laws or regulations or similar force majeure events), the time for performance of the obligation will be extended for a period equivalent to the period of delay and performance of the obligations during the period of delay will be excused.

C. Charity Care. During the term of the Ground Lease, MPHS shall comply with its charity care policy which shall be consistent with MPHS' nonprofit charitable purposes. MPHS shall encourage, support, recognize and report charity care as set forth in its charity care policy. In addition, MPHS shall provide the District with an annual report setting forth the level of charity care provided by MPHS during the previous year. Further, MPHS shall participate in any regional San Mateo County cooperative planning process among hospital providers to address unmet charity care needs in San Mateo County provided that MPHS has the opportunity to be meaningfully involved in this planning process.

D. Medicare Private Room Coverage. The New Facility is projected to have private rooms except for specified services such as mental health (where semi-private rooms would assist in treatment). MPHS will not seek additional reimbursement from Medicare patients who stay in private rooms to fund the difference between the cost of a shared room paid by Medicare and the cost of a private room in the New Facility during the term of the Ground Lease.

3. New Facility.

A. Construction of the New Facility. MPHS will design, build, own and operate a newly constructed general acute care hospital on the New Peninsula Site. The New Facility would be built in conformity with seismic standards (California Health and Safety Code Section 130000 et seq.), at no District cost and in substantial conformity and compliance with the EIR. MPHS would own and operate the New Facility during the term of the Ground Lease.

MPHS would use its reasonable best efforts consistent with Sutter Health's ability to meet its financing obligations to complete construction of the New Facility by the date legally required by Section 130000 et seq.

Peninsula Medical Center will operate at substantially the same level of services before and during construction of the New Facility and until the Start Service Date of the New Facility.

B. Planning Process and District Approval. It is anticipated by the parties that the District review, and if acceptable to the District, approve the Restructured Relationship, including the EIR for the New Facility, and the Definitive Agreements. The District's approval will be contingent upon its opportunity to provide secondary approval of any material reduction in the size of the New Facility requested by the City and made by MPHS as part of the City's approval process. A material reduction would require the consent of the District, which shall not be unreasonably withheld. A material reduction for this purpose would be a reduction that exceeds fifteen percent (15%) in the number of beds of the New Facility or a significant change

in the Site Plan. A party may submit a dispute regarding a material reduction for this purpose to binding arbitration that follows the same arbitration proceedings as disputes under the Definitive Agreements. The arbitrator shall be instructed to take into account that a material reduction may be permitted if regulatory changes, market conditions or community health care needs warrant such changes, or such changes are necessary to obtain required regulatory permits or approvals. In addition, the Definitive Agreements should specify the parties' intent that the New Facility be sized in a manner consistent with projected needs and uses within the community and good business practices. In no event shall a reduction that exceeds fifty percent (50%) in the number of beds of the New Facility be permitted without the consent of the District.

C. Sutter Health Guaranty. Sutter Health will guaranty MPHS' performance of its obligations under the Development Agreement to construct the New Facility pursuant to a Guaranty Agreement with the District.

D. Financing of New Facility and Debt. MPHS will pay for the construction of the New Facility at no cost to the District.

MPHS will continue to be responsible for any debt related to financing construction or improvement of the Existing Facility. During the term of the Ground Lease, the District will not be responsible for payment of any debt related to the construction of the New Facility, including any debt secured by the New Facility and improvements or secured by the revenues of MPHS generated in connection with the operation of the New Facility.

MPHS' leasehold interest (as well as MPHS' ownership interest in the New Facility) may be used by MPHS as security for financings, including any done by or for the Sutter Health Obligated Group, but only after the first fifteen (15) years of the Ground Lease following the Start Service Date. MPHS' revenues may be used by MPHS as security for financings, including any done by or for the Sutter Health Obligated Group, at any time.

E. Demolition of Existing Facility. MPHS will conduct the demolition of the Peninsula Medical Center after the Start Service Date of the New Facility. MPHS will pay for the demolition of Peninsula Medical Center.

F. District's Rights to Purchase New Facility. District will have a right of first refusal to purchase the New Facility at then-current fair market value during the term of the Ground Lease upon MPHS' request to transfer or assign its interest in the Ground Lease to a non-Sutter Health affiliate. Fair Market Value shall be defined to take into account remaining term of the Ground Lease and factors appropriate to such determination. Notwithstanding the foregoing, MPHS shall not transfer or assign its interest in the Ground Lease to a non-Sutter Health affiliate without the consent of the District.

4. Interim Lease.

A. Amendment of Existing Lease. Upon Closing, the Existing Lease would be amended by the Interim Lease to cover the time period from Closing until the New Facility is operational (the "Start Service Date"). The lease rate during such period (the "Interim Period")

would be one dollar (\$1.00) per year. The maintenance obligations of the Existing Lease will continue during the Interim Period. The replacement obligations of the Existing Lease will be terminated as of the date of Voter Approval so that MPHS shall have no obligation to repair or rebuild Peninsula Medical Center while the New Facility is under construction.

B. Termination of District's Obligation to Purchase Assets. Any right or obligation of the District to purchase any of MPHS' assets on the closure of Peninsula Medical Center terminates upon Closing. These assets will continue to be owned by MPHS.

5. Ground Lease.

A. Term. The Ground Lease shall commence immediately upon Closing for the New Peninsula Site not subject to the Interim Lease and, for all other portions of the New Peninsula Site, an initial term of fifty (50) years commencing upon the Start Service Date of the New Facility. The Ground Lease shall also provide for an additional twenty-five (25) year renewal upon MPHS' request and upon the District's written consent, which shall not be unreasonably withheld, provided MPHS is not in default under the Definitive Agreements and MPHS has performed satisfactorily. For the renewal to be effective, MPHS shall give the District prior written notice of its intent to renew three (3) years prior to the expiration date of the Ground Lease. The terms of this renewal shall be on the same terms as the initial fifty (50) year term of the Ground Lease.

The parties shall meet and confer ten (10) years in advance of expiration of the initial term of the Ground Lease to discuss extension and renewal of the Ground Lease. Thereafter, the parties may renew the Ground Lease upon mutual agreement.

B. Rent. For the initial fifty (50) year term and any extension thereof, MPHS would pay the District an annual rent of one million five hundred thousand dollars (\$1,500,000); provided, however, that this amount shall be deferred by the District for any year that MPHS has negative net operating income. If deferred, MPHS shall repay such amount with interest at the then-prime rate in the subsequent year if MPHS has positive net operating income. Deferral by the District of payment of annual rent by MPHS for more than five (5) years shall constitute a breach of the Ground Lease. The District and MPHS shall submit verification of MPHS earnings to a mutually agreed upon third party neutral auditor if a dispute arises between the parties. The annual rent amount shall be adjusted for inflation every ten (10) years by the Consumer Price Index for the Bay Area.

C. Destruction of New Facility During Ground Lease Term. If the New Facility is partially or totally destroyed, MPHS will promptly make repairs to return the New Facility to service in a condition comparable to that before destruction (or MPHS could elect to demolish and reconstruct to produce a reconstructed facility comparable to the New Facility). During the first twenty-five (25) years of the initial fifty (50) year term, MPHS will have no right to reimbursement or refund from the District for cost of repairs or restorations upon the expiration of the Ground Lease. After the first twenty-five (25) years of the initial fifty (50) year term, if costs are not covered by insurance, the District will reimburse or refund to MPHS the book value of repairs or restorations upon the expiration of the Ground Lease.

D. Capital Improvements to New Facility During Lease Term. If, after the first twenty-five (25) years of the fifty (50) year term, MPHS seeks to make any capital expenditure for improvements or other capital assets integral to the operation of the New Facility that will have a useful life extending beyond termination of the Ground Lease, MPHS will seek the District's approval of the expenditure. If the District approves of the expenditure, the District will reimburse MPHS the book value of the improvement upon termination of the Ground Lease. If the District does not approve of the expenditure, the District will have no obligation to reimburse MPHS for such expenditure and MPHS will have no obligation to make the expenditure.

E. Transfer of New Facility Upon Expiration of the Ground Lease. MPHS will transfer the New Facility to the District free and clear upon the later of expiration of the initial term of the Ground Lease or, if this term is extended, the expiration of the final extended term, subject to:

(1) The District's obligation to reimburse MPHS for book value as of the date of termination or expiration of repairs or restorations made during the last twenty-five (25) years of the Ground Lease; and

(2) District's obligation to reimburse MPHS for book value as of the date of termination or expiration of District approved capital improvements made during the last twenty-five (25) years of the Ground Lease.

At year forty-seven (47) in the fifty (50) year term set for expiration without renewal, or three (3) years before the expiration date of any renewal, the District and MPHS will meet and confer to determine whether the District will purchase the equipment, furniture and non-integral assets owned by MPHS at the termination of the Ground Lease. MPHS may remove all equipment, furniture and other assets non-integral to the operation of the New Facility. Alternatively, MPHS and District may agree for the District to purchase some or all of these assets.

At the time of transfer and if requested by the District, MPHS will make available to the District bridge financing to fund the District's obligation to pay for repairs, restorations and capital improvements. Such financing will be with appropriate security (including all real and personal property (if permitted by law), all accounts, tax and other revenues) on then-current rates and terms charged by commercial banks for a period to end the earlier of three (3) years or until the District has refinanced the debt.

Prior to the transfer of the New Facility upon the expiration of the initial or extended terms of the Ground Lease, as applicable, the parties will negotiate in good faith to transition the New Facility to the District.

F. MPHS' Rights to Purchase Leased Premises. MPHS will have a right of first refusal to purchase any of the District's real property for then-current fair market value upon District's request to sell to a third party. MPHS' shall have no right of first refusal upon

voluntary or involuntary transfers by the District upon any dissolution of the District or upon any merger or consolidation of the District with another public entity.

Provided that MPHS is not in breach of the Definitive Agreements, MPHS will also have an option to purchase any of the leased premises for then-current fair market value upon termination of the Ground Lease, foreclosure of a lien against the District upon the leased premises, the District's filing for bankruptcy or dissolution, a determination by a court of competent jurisdiction that the lease term be less than fifty (50) years or the remaining term for any reason other than MPHS filing for bankruptcy. If MPHS exercises its option to purchase due to a court determination as noted above, MPHS shall purchase from the District, and the District shall sell to MPHS all of the properties constituting the New Peninsula Site, provided that the District transfers the New Peninsula Site and retains a reversionary interest that provides for the return of ownership of the New Peninsula Site at a time when the Ground Lease would have terminated under the Definitive Agreements.

G. Upon Termination of Ground Lease. Upon notice of termination of the Ground Lease for any reason and MPHS is not in default of the Definitive Agreements and does not exercise its option to purchase from the District the leased premises, if applicable, the District shall purchase the New Facility at then-current fair market value. The Ground Lease shall remain in effect until this purchase is effective. In no event shall the New Facility be transferred by operation of law or otherwise to the District prior to expiration of the initial term of the Ground Lease without payment to MPHS of the then-current fair market value of the New Facility. During this time period, MPHS may, but shall not be required to, perform the maintenance of services obligations set forth in Section 2.B. Prior to the sale of the New Facility (whether by exercise of District's option to purchase or otherwise), the parties will negotiate in good faith to transition the New Facility to the District.

6. Medical Office Buildings. The District would agree during the term of Ground Lease to rent office space to physicians at fair market value rental rates for medical office space of like quality in the area. First priority for such office space would be given to physicians on the MPHS Medical Staff, except for space at 1600 Trousdale Drive. The District would agree during the term of the Ground Lease to make available to MPHS space at 1600 Trousdale Drive at fair market value rental rates for office space of like quality in the area. In addition, the District would agree to give MPHS a right of first refusal to rent such space at such fair market value.

The District would have the opportunity to conduct reasonable due diligence on the medical office buildings immediately upon execution of the non-binding Letter of Intent. If the District determines that it no longer wishes to own one or more of the properties, it may market the property to third parties, provided that MPHS would have a right of first refusal to match any bona fide offer received by the District within thirty (30) days of receipt of a third party offer.

If MPHS did not wish to acquire such property, the District could sell such property to a third party for uses that are non-competitive with any service on the Existing Program List or any Approved Future Service.

7. Before Closing Can Occur. The following must occur prior to the consummation of the Restructured Relationship (the "Closing") for the Restructured Relationship to be effective:

A. Boards Approval. The District, MPHS and Sutter Health Boards of Directors will have approved of the Definitive Agreements and the terms of the Restructured Relationship.

B. Voter Approval. When mutually agreed, the District will place a measure on the ballot for submission to the voters of the District to seek approval of the Ground Lease and the other Definitive Agreements describing the terms of the Restructured Relationship. The approval of 50% (plus one) of the residents of the District who vote in the relevant election will be required ("Voter Approval"). MPHS will pay for reasonably incurred election costs incurred by the District as are billed to the District by the County of San Mateo.

C. Dismissal of Litigation. All current litigation between the District and MPHS will be dismissed with prejudice no later than immediately following Voter Approval.

D. Validation. A validation action will be instituted by the District with MPHS joined as an interested party in accordance with Section 860 et seq. of the California Code of Civil Procedure validating the Ground Lease and the other Definitive Agreements ("Validation"). The validation action must be final before Closing.

E. CEQA and Other Regulatory Approvals. Prior to Closing, MPHS shall have received no indication that all planning, environmental and other regulatory approvals required for the construction of the New Facility and demolition of Peninsula Medical Center will not be obtained.

F. Financing. MPHS will have obtained or arranged for the financing necessary to complete construction of the New Facility and related improvements.

G. Other Conditions Precedent to Closing. Other conditions precedent to Closing include:

- (1) No litigation is pending impacting the Restructured Relationship.
- (2) MPHS review and satisfaction with appropriate title policies.
- (3) District's compliance with the Subdivision Map Act with regard to the leased premises as reasonably required to implement the Ground Lease and Definitive Agreements.
- (4) Appropriate representations and warranties by the District and MPHS.

8. Enforcement of MPHS Promises.

A. Pre-Construction. After the effective date of the Interim Lease and prior to construction of the New Facility, the District may, after notice and reasonable opportunity to cure, enforce MPHS' promises under the Definitive Agreements as follows:

(1) Money and equitable remedies (i.e., remedies would be limited to actual compensatory or other monetary damages suffered by the District or equitable remedies that the District is entitled to bring under law and expressly excludes any right to terminate the Ground Lease or the other Definitive Agreements);

(2) Enforcement of Sutter Health's guarantee of MPHS' performance of its obligation to construct the New Facility under the Development Agreement; and

(3) If MPHS abandons the construction of the New Facility or elects not to build the New Facility, the Interim Lease shall be reformed to no longer obligate MPHS to build the New Facility, and the Ground Lease and any of the Definitive Agreements shall terminate. The District may choose to unilaterally fund and construct the New Facility but shall reimburse MPHS for its actual costs in the development of the New Facility and related matters should the District substantially utilize MPHS' project plans. If the District pursues this remedy, it shall be the exclusive remedy available to the District (i.e., (1) and (2) above shall not be available to the District).

B. Construction. During the term of the Interim Lease and after MPHS has broken ground on construction of the New Facility, the District may, after notice and reasonable opportunity to cure, enforce MPHS' promises under the Definitive Agreements as follows:

(1) Money and equitable remedies (i.e., remedies would be limited to actual compensatory or other monetary damages suffered by the District or equitable remedies that the District is entitled to bring under law and expressly excludes any right to terminate the Ground Lease or the other Definitive Agreements);

(2) Enforcement of Sutter Health's guarantee of MPHS' performance of its obligation to construct the New Facility under the Development Agreement; and

(3) If MPHS abandons the construction of the New Facility or elects not to build the New Facility, the Interim Lease shall be reformed to no longer obligate MPHS to build the New Facility, and the Ground Lease and any of the Definitive Agreements shall terminate. The District may choose to unilaterally fund and construct the New Facility but shall reimburse MPHS for its actual costs in the development of the New Facility and related matters should the District substantially utilize MPHS' project plans. If the District pursues this remedy, it shall be the exclusive remedy available to the District (i.e., (1) and (2) above shall not be available to the District).

C. After the Start Service Date. After the Start Service Date of the New Facility, the District may, after notice and reasonable opportunity to cure, enforce MPHS' promises under the Definitive Agreements as follows:

(1) Ordinary Defaults. Money and equitable remedies (i.e., remedies would be limited to actual compensatory or other monetary damages suffered by the District or equitable remedies that the District is entitled to bring under law and expressly excludes any right to terminate the Ground Lease or the other Definitive Agreements).

(2) Paramount Defaults. Upon a Paramount Default, the District may, upon its option to forego money and equitable remedies, terminate the Ground Lease. Upon termination of the Ground Lease by the District pursuant to this Section 8.C, the ownership of the New Facility ("Assets") shall automatically revert to the District, and the District shall be obligated to pay MPHS the then-current fair market value of MPHS' interest in the Assets. For purposes of this Section 8.C, fair market value is defined to take into account the remaining term of the Ground Lease (without unexercised extensions of the term of the Ground Lease) and the circumstances in effect at the time of valuation.

If requested by the District, MPHS will make available to the District bridge financing to fund the District's obligation. Such financing will be with appropriate security (including all real and personal property (if permitted by law), all accounts, tax and other revenues) on then-current rates and terms charged by commercial banks for a period to end the earlier of one (1) year or until the District has refinanced the debt.

Unless the District declares a default as set forth in this Section 8.C, the District shall have no right to early termination of the Ground Lease.

"Paramount Default" means any of the following so long as such event is caused by MPHS or Sutter Health:

(a) There is a declared payment default under the Master Indenture that causes immediate acceleration of all debt under the Sutter Health Obligated Group that results in foreclosure of a lien on the New Facility and MPHS has not satisfied such lien;

(b) MPHS files for dissolution;

(c) MPHS is insolvent;

(d) The Sutter Health Obligated Group is insolvent;

(e) MPHS' express written repudiation of its obligation to operate substantially all of the New Facility;

(f) MPHS' inability to operate substantially all of the New Facility and such inability is either sustained or reasonably expected to be sustained; or

(g) Sustained closure of substantially all of the New Facility.

A "Paramount Default" shall not occur under subsections (a), (c), (d) (f) or (g) of Section 8.C if MPHS' obligations pursuant to the Definitive Agreements are prevented or delayed by reason of any act of God or any act of the District or third party outside of MPHS' or Sutter Health's control or not MPHS' or Sutter Health's fault (including earthquake, natural disaster, terrorism, war, or similar force majeure events), the time for performance of the obligation will be extended for a period equivalent to the period of delay and performance of the obligations during the period of delay will be excused.

9. Future Development.

A. Required Consents. The District must consent to any new development by MPHS of the properties it controls as a tenant under the Ground Lease. MPHS must consent to any new development by the District on the District Controlled Property and any other properties the District received from MPHS.

B. Development Advisory Committee. The parties will form a Development Advisory Committee to review and explore all future development of the approximate twenty-six (26) acres owned by the District, including the properties leased to MPHS. The Committee shall be an advisory committee not subject to the Brown Act and shall be composed of two representatives appointed by each of the District and MPHS, who shall appoint the fifth representative. The parties' intent is that definitive language set forth the collaborative goal, attitude and tone of the Committee.

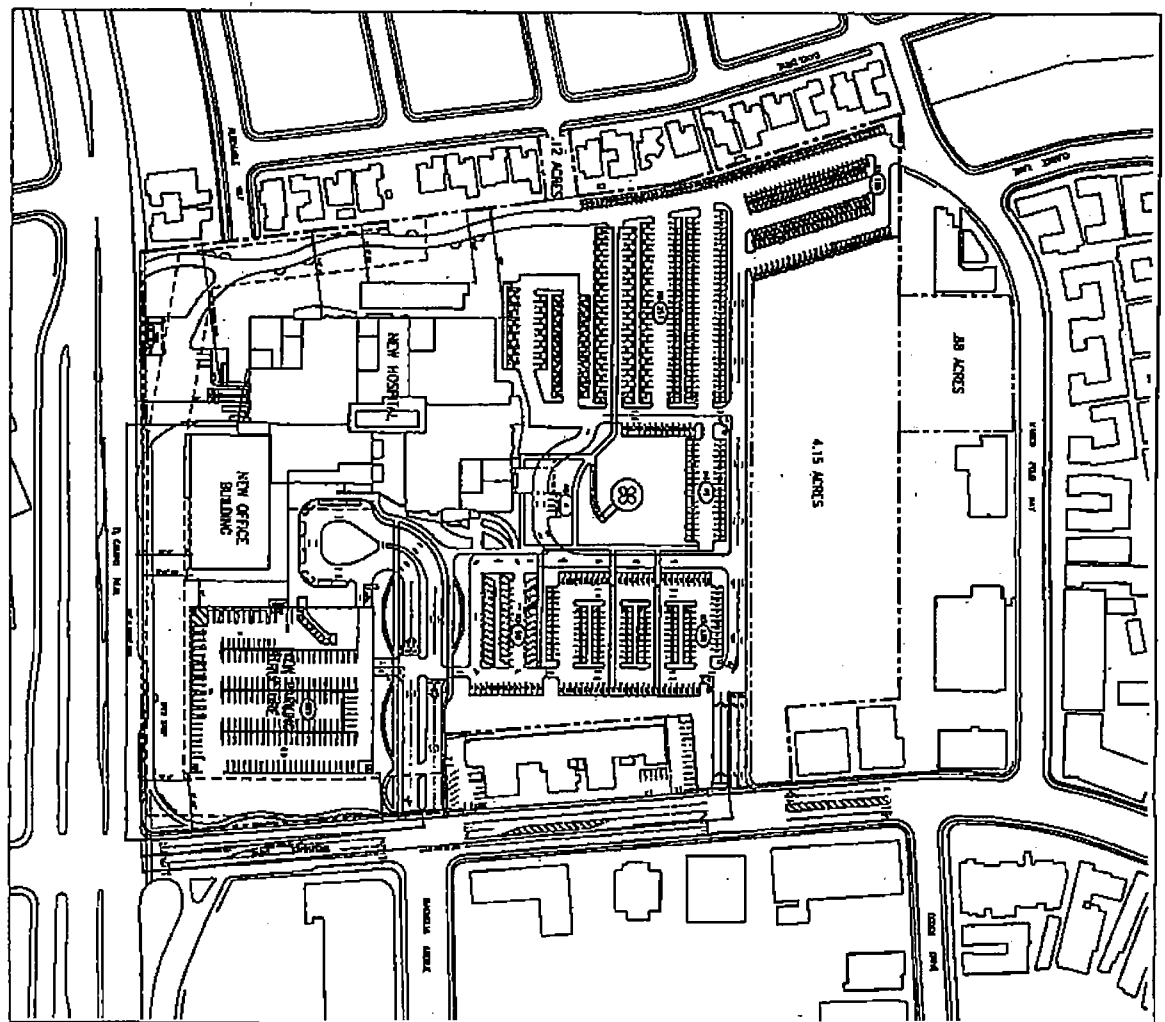
Attachment 1-A

Environment Impact Report

(Due to the size of the document, please find Attachment 1-A, Environmental Impact Report, as a separate document, not attached. The document is available on the District website.)

Attachment 1-B

Site Plan



LEGEND
 1. EXISTING PARKING
 2. NEW PARKING

NO.	DESCRIPTION	AREA (SQ. FT.)	AREA (ACRES)
1	EXISTING PARKING	100,000	2.30
2	NEW PARKING	1,000,000	23.00
TOTAL PARKING - 1.20 ACRES			



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A1.10
 NEW REFERENCED
 ALTERNATIVE

Attachment 1-C

Clinical Services

Intensive Care Services

Coronary
Medical
Neurosurgical
Pulmonary
Surgical

Newborn Care Services

Newborn Nursery Care
Premature Nursery Care

Obstetric Services

Abortion Services
Labor/Delivery/Post
Partum Services

Acute Care Services

Geriatric
Medical
Neonatal
Oncology
Orthopedic
Surgical

Surgery Services

Dental
General
Gynecological
Cardiac
Kidney
Neurosurgical
Ophthalmologic
Orthopedic
Otolaryngologic
Podiatry
Thoracic
Urologic
Anesthesia Services

Laboratory Services

*(Provided directly or
through contract)*

Diagnostic Imaging Services
(including invasive cardiology)

*(Provided directly or
through contract)*

Diagnostic/Therapeutic Services

*(Provided directly or
through contract)*

Mental Health

*(Provided either at
the New Facility or at any
other location within the
District. Does not include
substance abuse or
rehabilitation services.)*