

**Palomar Pomerado North County Health Development, Inc.  
Line of Credit**

**TO:** Board of Directors

**FROM:** Board Finance Committee  
Tuesday, October 25, 2005

**MEETING DATE:** Monday, November 14, 2005

**BY:** Bob Hemker, CFO

**Background:** As a newly formed entity of Palomar Pomerado Health (PPH), Palomar Pomerado North County Health Development, Inc. (Health Development), is in start-up mode. As such, certain cash flows were contemplated requiring cash infusion from PPH. The separation of legal entities requires this infusion to be separated and documented via a Line of Credit Agreement, in the requested form and documentation as per the attached.

The five-year *pro forma* warrants a not-to-exceed Line of Credit of \$1.6 million to cover the five-year period. It is expected that a cumulative draw on the line will result in this not-to-exceed amount rather than up-front draws.

**Budget Impact:** N/A

**Staff Recommendation:** Approval of the Line of Credit to Palomar Pomerado North County Health Development, Inc., as requested.

**Committee Questions:**

**COMMITTEE RECOMMENDATION:** The Finance Committee recommends approval of the Line of Credit to Palomar Pomerado North County Health Development, Inc., as requested.

**Motion:** X

**Individual Action:**

**Information:**

**Required Time:**

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**For discussion purposes only.**

**LINE OF CREDIT AGREEMENT**

**by and between**

**PALOMAR POMERADO HEALTH (“PPH”)**

**and**

**PALOMAR POMERADO NORTH COUNTY HEALTH DEVELOPMENT, INC.**  
**(“Health Development”)**

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**LINE OF CREDIT AGREEMENT**

THIS LINE OF CREDIT AGREEMENT (this "Agreement") is dated as of \_\_\_\_\_ 1, 2005, (the "Effective Date") by and between PALOMAR POMERADO HEALTH, a local health care district organized under the laws of the State of California ("PPH"), and PALOMAR POMERADO NORTH COUNTY HEALTH DEVELOPMENT, INC., a California nonprofit (pending) corporation ("Health Development"). PPH and Health Development are each sometimes referred to in this Agreement as a "Party" or, collectively, as the "Parties."

**RECITALS**

A. PPH, a local health care district organized under the California Local Hospital District Law (California Health and Safety Code § 32000 et seq.) (the "Law"), owns and operates healthcare facilities for the benefit of the communities within its boundaries.

B. Health Development, a nonprofit organization organized and operated to support PPH and its programs, is committed to its mission which is the enhancement of individual and community health through the obtaining of Grant Funding in support of PPH.

C. The Parties believe that it is in the best interests of the public served by PPH to facilitate the proper operation of Health Development so that it may carry out its mission.

D. Health Development desires to obtain from PPH certain funds, and PPH has agreed to provide such funds to Health Development to further the public purposes for which PPH and the Health Development operate, in accordance with the California Constitution and according to the terms and conditions set forth herein.

G. The Parties hereby reference the following additional agreements to which they are both parties:

- (i) Security Agreement dated \_\_\_\_\_, 2005, and attached hereto as Exhibit 2.1(b); and
- (ii) Business Associate Agreement dated \_\_\_\_\_, 2005, and attached hereto as Exhibit 4.2.

**AGREEMENT**

NOW THEREFORE, in consideration of the mutual covenants and agreements contained herein, the parties hereto agree as follows:

**ARTICLE I.**  
**LINE OF CREDIT**

**1.1 Line of Credit.** PPH shall make available to Health Development, and Health Development agrees to accept from PPH, a line of credit, the aggregate amount of which shall not exceed \_\_\_\_\_ Dollars (\$ \_\_\_\_\_) or a greater amount solely in PPH's discretion ("Line of Credit"), subject to the terms set forth in this Article III. The Line of Credit shall expire \_\_\_\_\_ (the "Credit Line Expiration Date"). This expiration date does not affect Health Development's repayment obligation.

**1.2 Advances.** PPH shall advance to Health Development amounts requested pursuant to Section 1.4 of this Article (each, an "Advance", and collectively, the "Advances"), from time to time prior to, but not including, the Credit Line Expiration Date. The aggregate amount of all outstanding Advances shall not exceed the Line of Credit. Notwithstanding the foregoing, both PPH's Chief Executive Officer and Chief Financial Officer and Health Development's Chair and Treasurer shall approve in writing Advance requests exceeding One Hundred Thousand Dollars (\$100,000).

**1.3 Use of Advances.** Health Development shall use the Advances for the following purposes only:

(a) For amounts approved by PPH in the capital and operating budgets of Health Development;

(b) For subsequent repayment to PPH in any given month when Health Development does not have sufficient funds to cover Health Development Expenses.

**1.4 Request and Delivery of Advances.** When Health Development desires to obtain an Advance, it shall deliver to PPH a notice in the form attached hereto as Exhibit 1.4 (the "Notice of Borrowing") at least three (3) Business Days prior to the date on which the Advance is to be paid (the "Proposed Funding Date"). The Notice of Borrowing shall specify the Proposed Funding Date (which shall be a Business Day), the amount of the requested Advance, and certify as to the satisfaction of each of the conditions set forth in Exhibit 1.4. "Business Day" shall mean any day which is not a Saturday, Sunday or a generally observed holiday for banks in the State of California.

**1.5 Contingencies to PPH's Payment of Advances.** PPH's obligation to make any Advances to Health Development under this Agreement shall be contingent upon the following:

(a) Documentation. Health Development's submission to PPH, in form and substance satisfactory to PPH, this Agreement, the Note (as defined in Section 2.1(a)), the

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Security Agreement (as defined in Section 2.1(b)), and such other documents and instruments as PPH may reasonably request, all duly executed by Health Development.

(b) Notice of Borrowing. Health Development's submission to PPH of a Notice of Borrowing in which Health Development certifies that as of the date of the Notice of Borrowing:

- (i) all of Health Development's representations and warranties contained in this Agreement shall be true, correct and complete in all material respects to the same extent as though made on and as of that date;
- (ii) no Event of Default (as defined in Exhibit 2.1(b)) shall have occurred and shall continue, or shall result from, making the Advance;
- (iii) no law or regulation shall prohibit, and no order, judgment or decree of any court, arbitrator or governmental authority shall purport to enjoin or restrain PPH from making the Advance; and
- (iv) no change having a Material Adverse Effect on Health Development, either individually or in the aggregate, shall have occurred since the Execution Date. "Material Adverse Effect" shall mean a material adverse effect upon Health Development's purpose, function, operation or status or upon PPH's security interest in the Collateral (as defined in Exhibit 2.1(b) attached hereto) or the priority thereof.

(c) Perfection. The Account described in Exhibit 2.1(b) of this Agreement shall have been established in a manner satisfactory to PPH, in its sole discretion, and PPH shall be satisfied that all steps shall have been taken necessary to create and perfect in favor of PPH a first priority security interest in the Account and all other Collateral described in such Exhibit 2.1(b).

**1.6 Promissory Note.** Health Development shall repay the Advances and accrued interest pursuant to the terms and conditions of the Note (as defined below). Health Development authorizes PPH to record on the schedule annexed to the Note, the date and amount of each Advance made by PPH, the Interest Rate (as such term is defined in the Note) when each Advance is made, and each payment or prepayment of the Advances, and agrees that all such notations shall constitute *prima facie* evidence of the matters noted. Health Development further authorizes PPH to attach to and make a part of the Note continuations of the schedule as necessary. No failure to make any such notations, nor any errors in making any such notations, shall affect the validity of Health Development's obligations to repay the Advances or Health Development's obligations under this Agreement, the Note, or any other document, contract or instrument delivered to PPH in connection with this Agreement (collectively, the "Line of Credit Documents").

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**ARTICLE II.**  
**PROMISSORY NOTE; SECURITY AGREEMENT; GUARANTEE**

**2.1 Health Development's Deliverables.** Concurrently with the execution of this Agreement, Health Development shall execute and deliver to PPH:

- (a) the secured promissory note in the form attached as Exhibit 2.1(a) (the "Note"); and
- (b) the security agreement in the form attached as Exhibit 2.1(b) (the "Security Agreement").

**2.2 Further Cooperation.** PPH and Health Development shall perform, or ensure the performance of, all actions and execute, or ensure the execution of, all documents necessary to perfect the security interests granted in the Security Agreement, as reasonably requested by PPH from time to time.

**ARTICLE III.**  
**TERM AND TERMINATION**

**3.1 Term.** This Agreement shall become effective on \_\_\_\_\_ (the "Effective Date"), and shall continue until \_\_\_\_\_ (the "Expiration Date"), subject to the termination provisions of this Agreement.

**3.2 Termination by PPH.** PPH shall have the right to terminate this Agreement upon the occurrence of any one or more of the following events:

- (a) Breach of this Agreement by Health Development where the breach is not cured within thirty (30) calendar days after PPH gives written notice of the breach to Health Development;
- (b) Breach by Health Development of the requirements under the Health Insurance Portability and Accountability Act of 1996 ("HIPAA") (as set forth in Exhibit 4.2);
- (c) Health Development is rendered unable to comply with the terms of this Agreement for any reason; or
- (d) Upon ninety (90) calendar days written notice without cause to Health Development in all other cases.

**3.3 Termination by Health Development.** Health Development shall have the right to terminate this Agreement according to the following terms and conditions:

- (a) Breach of this Agreement by PPH where the breach is not cured within thirty (30) calendar days after Health Development gives written notice of the breach to PPH or if the breach is not curable, then thirty (30) calendar days after Health Development gives written notice of the breach to PPH;

(b) Health Development is rendered legally unable to comply with the terms of this Agreement for any reason, in which case termination shall be coterminous with the date of such legal inability; or

(c) Upon ninety (90) calendar days written notice without cause to PPH in all other cases.

**3.4 Termination or Modification in the Event of Government Action.** If the Parties receive notice of any Government Action (defined below), the Parties shall attempt to amend this Agreement in order to comply with the Government Action. If the Parties, acting in good faith, are unable to agree to the amendments necessary to comply with the Government Action, or, alternatively, if either Party determines in good faith that compliance with the Government Action is impossible or infeasible, this Agreement shall be terminated ten days after one party gives notice to the other of such fact. For the purposes of this Section, "Government Action" shall mean any legislation, regulation, rule or procedure passed, adopted or implemented by any federal, state or local government or legislative body or any private agency, or any notice of a decision, interpretation, finding, or action by any governmental or private agency, court or other third-party which, in the opinion of counsel to PPH, because of the arrangement between the Parties pursuant to this Agreement, if or when implemented, would:

(a) revoke or jeopardize the status of any health facility license granted to PPH or any Affiliate (defined below) of PPH;

(b) prevent Health Development from being able to access and use the facilities of PPH or any Affiliate of PPH; or

(c) subject PPH, any Affiliate of PPH, Health Development, or any of their respective employees or agents, to civil or criminal prosecution (including any excise tax penalty under Internal Revenue Code Section 4958) on the basis of their participation in executing this Agreement or performing their respective obligations under this Agreement.

(d) For the purposes of this Section, "Affiliate" shall mean any entity which, directly or indirectly, controls, is controlled by or is under common control with PPH.

**3.5 Rights upon Termination.** Upon any termination or expiration of this Agreement, all rights and obligations of the Parties shall cease except those rights and obligations that have accrued or expressly survive such termination or expiration. Notwithstanding the above, upon termination of this Agreement by PPH and Health Development pursuant to Sections 3.2 and 3.3, respectively, of this Agreement, the outstanding principal amount of the Advances and all accrued but unpaid interest shall automatically become due and payable.

#### **ARTICLE IV.** **GENERAL PROVISIONS**

**4.1 Independent Contractor.** PPH is and shall at all times be an independent contractor with respect to Health Development in meeting PPH's responsibilities under this

Agreement. Nothing in this Agreement is intended nor shall be construed to create a partnership, employer-employee or joint venture relationship between PPH and Health Development.

**4.2 Compliance with HIPAA.** PPH and Health Development shall comply with the HIPAA requirements as defined and set forth in Exhibit 4.2. The HIPAA requirements shall survive the expiration or termination of this Agreement for any reason.

**4.3 Amendment.** This Agreement may be modified or amended only by mutual written agreement of the Parties. Any such modification or amendment must be in writing, dated, signed by the Parties and attached to this Agreement.

**4.4 Dispute Resolution.** In the event of any disagreement, dispute or claim (collectively, a "Dispute") arises between the Parties hereto with respect to whether an alleged breach hereof has or has not occurred, or with respect to any other matter related to or arising out of this Agreement, or the relationship or transactions contemplated hereby, the Dispute shall be resolved in accordance with the following procedures:

(a) **Meet and Confer.** In the event of a Dispute, either Party may give written notice to the other Party setting forth the nature of the Dispute (the "Dispute Notice"). The Parties shall meet and confer to discuss in good faith and attempt to resolve the Dispute within fifteen (15) days of the Party receiving the Dispute Notice. The representatives of the Parties shall meet at such date(s) and time(s) as are mutually convenient to the representatives of each Party within the 15-day period.

(b) **Arbitration.** Except as set forth below, any Dispute that cannot be resolved by the Parties under Section 8.4(a) within the 30-day meet-and-confer period, shall be submitted to final binding arbitration, as follows:

- (i) ***Designation of an Arbitrator.*** A single disinterested third party shall be selected by mutual agreement of the Parties. If the Parties are unable to mutually select an arbitrator within (15) days after each party notifies the other of its desire to arbitrate the Dispute, then the arbitrator shall be selected, and the arbitration shall be conducted, in accordance with JAMS's then -current Comprehensive Arbitration Rules and Procedures or Streamlined Rules of Practice and Procedure, as appropriate, depending on the amount in dispute.
- (ii) ***Venue.*** The arbitration shall be conducted in the County of San Diego, California, unless the Parties mutually determine that another venue would be more convenient.
- (iii) ***Arbitrator's Expenses and Fees.*** JAMS' administrative fees and the expenses and fees of the arbitrator shall be divided among the Parties equally. Each Party shall pay its own counsel fees, witness fees, and other expenses incurred.

**4.5 Assignment.** Except for assignment by PPH to an entity owned, controlled by, or under common control with PPH, neither Party may assign any interest or obligation under this Agreement without the other Party's prior written consent. Subject to the foregoing, this Agreement shall be binding on and shall inure to the benefit of the Parties and their respective successors and assigns.

**4.6 Attorneys' Fees.** If either Party brings an action for any relief or collection against the other Party, declaratory or otherwise, arising out of the arrangement described in this Agreement, the losing Party shall pay to the prevailing Party a reasonable sum for attorneys' fees and costs actually incurred in bringing such action, all of which shall be deemed to have accrued upon the commencement of such action and shall be paid whether or not such action is prosecuted to judgment. Any judgment or order entered in such action shall contain a specific provision providing for the recovery of attorneys' fees and costs incurred in enforcing such judgment. For the purpose of this Section, attorneys' fees shall include fees incurred in connection with discovery, post judgment motions, contempt proceedings, garnishment and levy.

**4.7 Authorized Persons.** Whenever any consent, approval or determination of a Party is required pursuant to this Agreement, the consent, approval or determination shall be rendered on behalf of the Party by the person or persons duly authorized to do so, which the other Party shall be justified in assuming means any officer of the Party rendering such consent, approval or determination, or the Party's board of directors.

**4.8 Choice of Law.** This Agreement shall be construed in accordance with and governed by the laws of the State of California, except choice of law rules that would require the application of the laws of any other jurisdiction.

**4.9 Compliance with Laws.** Health Development shall comply with applicable laws, ordinances, codes and regulations of federal, state and local governments, including laws that require Health Development to disclose any economic interest or relationship with PPH.

**4.10 Counterparts.** This Agreement may be executed in one or more counterparts, each of which shall be deemed to be an original, but all of which together shall constitute one and the same instrument.

**4.11 Entire Agreement.** This Agreement is the entire understanding and agreement of the Parties regarding its subject matter, and supersedes any prior oral or written agreements, representations, understandings, discussions or past practices between the Parties. No other understanding between the Parties shall be binding on them unless set forth in writing, signed and attached to this Agreement.

**4.12 Exhibits.** The attached exhibits, together with all documents incorporated by reference in the exhibits, form an integral part of this Agreement and are incorporated into this Agreement wherever reference is made to them to the same extent as if they were set out in full at the point at which such reference is made.

**4.13 Force Majeure.** Except with respect to obligations imposed with regard to payments to be paid by Health Development under this Agreement, neither Party is liable for

nonperformance or defective or late performance of any of its obligations under this Agreement to the extent and for such periods of time as such nonperformance, defective performance or late performance is due to reasons outside such Party's control, including acts of God, war (declared or undeclared), action of any governmental authority, riots, revolutions, fire, floods, explosions, sabotage, nuclear incidents, lightning, weather, earthquakes, storms, sinkholes, epidemics, failure of utilities, or strikes (or similar nonperformance or defective performance or late performance of employees, suppliers or subcontractors).

**4.14 Further Assurances; Good Faith.** Each Party shall, at the reasonable request of the other Party, execute and deliver to the other party all further instruments, assignments, assurances and other documents, and take any actions as the other Party reasonably requests in connection with the carrying out of this Agreement. In performing its obligations under this Agreement, each Party shall act in good faith.

**4.15 Indemnification.** To the extent that such acts or omissions are not covered by insurance, each Party shall indemnify, hold harmless and defend the other Party and its officers, agents or employees, against any loss or liability arising out of or resulting in any way from the acts or omissions of such Party or its own officers, employees or agents, except that any such obligation to indemnify and hold harmless shall be reduced by any amount of such loss or liability arising from the contributory acts or omissions of the indemnified Party and its owners, employees or agents. This obligation shall not be qualified or eliminated by an allegation or finding that the other Party or any of its personnel is responsible for a passively negligent act or omission. This section shall survive the termination of this Agreement. Headings. The headings in this Agreement are intended solely for convenience of reference and shall be given no effect in the construction or interpretation of this Agreement.

**4.16 Interruption of Services.** Notwithstanding any provision in this Agreement to the contrary, PPH shall not be liable to Health Development in damages or otherwise for any failure to advance any funds contemplated by this Agreement. This Agreement contemplates a close operating relationship between PPH and Health Development that will exist over a long period of time. Accordingly, in approving this Agreement and directing its officers to enter into this Agreement on its behalf, the Parties shall mutually review the performance of both Parties to this Agreement, identifying deficiencies in the performance of either or both Parties to this Agreement, developing (as necessary) a plan for addressing any such deficiencies, discussing potential modifications to the terms and conditions of this Agreement and the responsibilities of the Parties as set forth herein, reviewing the outstanding principal amount of Advances, including all accrued but unpaid interest thereon, made pursuant to this Agreement and addressing repayment of such amounts, and at the appropriate time addressing a plan for Health Development to attain self-sufficiency.

**4.17 Notices.** All notices or communications required or permitted under this Agreement shall be given in writing and delivered personally or sent by United States registered or certified mail with postage prepaid and return receipt requested or by overnight delivery service (e.g., Federal Express, DHL). Notice is deemed given when sent, if sent as specified in this Section, or otherwise deemed given when received. In each case, notice shall be delivered or sent to:

**If to PPH, addressed to:**

Palomar Pomerado Health

\_\_\_\_\_  
\_\_\_\_\_  
Attention: \_\_\_\_\_

**If to Health Development, addressed to:**

Palomar Pomerado North County Health Development, Inc.

\_\_\_\_\_  
\_\_\_\_\_  
Attention: \_\_\_\_\_

Either Party may provide for a different address by notifying the other Party of such change as provided for in this Section.

**4.18 Severability.** If any provision of this Agreement is determined to be illegal or unenforceable, that provision shall be severed from this Agreement, and such severance shall have no effect upon the enforceability of the remainder of this Agreement unless the purpose of this Agreement is thereby destroyed.

**4.19 No Third-Party Beneficiary Rights.** The Parties do not intend to confer and this Agreement shall not be construed to confer any rights or benefits to any person, firm, group, corporation or entity other than the Parties, including but not limited to the Personnel.

**4.20 Waiver.** No delay or failure to require performance of any provision of this Agreement shall constitute a waiver of that provision as to that or any other instance. Any waiver granted by a Party must be in writing to be effective, and shall apply solely to the specific instance expressly stated.

**4.21 Meaning of Certain Words.** Wherever the context may require, any pronouns used in this Agreement shall include the corresponding masculine, feminine, or neuter forms, and the singular form of nouns shall include the plural and vice versa.

[REMAINDER OF PAGE INTENTIONALLY LEFT BLANK]

**DRAFT-DO NOT SIGN**  
**For discussion purposes only.**

The Parties have executed this Agreement on the date written below (the "Execution Date").

PALOMAR POMERADO HEALTH,  
a California local health care district

Date: \_\_\_\_\_, 2005 **DRAFT-DO NOT SIGN** \_\_\_\_\_  
By: \_\_\_\_\_  
Its: \_\_\_\_\_

PALOMAR POMERADO NORTH COUNTY HEALTH  
DEVELOPMENT, INC.,  
a California nonprofit public benefit corporation

Date: \_\_\_\_\_, 2005 **DRAFT-DO NOT SIGN** \_\_\_\_\_  
By: \_\_\_\_\_  
Its: \_\_\_\_\_

**EXHIBIT 1.4**

**NOTICE OF BORROWING**

**[LETTERHEAD OF PALOMAR POMERADO NORTH COUNTY HEALTH  
DEVELOPMENT, INC.]**

[Address of Health Development]  
\_\_\_\_\_, 20\_\_

Re: Notice of Borrowing

To Whom It May Concern:

Please take notice that Palomar Pomerado North County Health Development, Inc., a California nonprofit public benefit corporation ("Health Development"), desires to borrow an Advance of \_\_\_\_\_ Dollars (\$\_\_\_\_\_) from Palomar Pomerado Health, a local health care district organized under the laws of the State of California ("PPH"), on \_\_\_\_\_, 20\_\_ (the "Funding Date"). Advance requests exceeding One Hundred Thousand Dollars (\$100,000) must be accompanied by signatures from PPH's Chief Executive Officer and Chief Financial Officer and Health Development's Chair and Treasurer.

Health Development hereby certifies that as of the date of this Notice:

- (a) all of Health Development's representations and warranties contained in the Management Services Agreement (the "Agreement") and all exhibits to the Agreement shall be true, correct and complete in all material respects to the same extent as though made on and as of that date;
- (b) no Event of Default (as defined in Exhibit 2.1(b) of the Agreement) shall have occurred and shall continue, or shall result from, making the Advance;
- (c) no law or regulation of general application shall prohibit, nor any order, judgment or decree of any court, arbitrator or governmental authority specifically naming Health Development and known to Health Development, shall purport to enjoin or restrain PPH from making the Advance; and
- (d) no change having a Material Adverse Effect on Health Development (as such term is defined in the Agreement), either individually or in the aggregate, shall have occurred since the Execution Date.

Sincerely,

\_\_\_\_\_  
Name: \_\_\_\_\_  
Title: \_\_\_\_\_

As Approved By

**PALOMAR POMERADO HEALTH,**  
a California health care district

Date: \_\_\_\_\_

\_\_\_\_\_  
By:  
Its: Chief Executive Officer

**PALOMAR POMERADO HEALTH,**  
a California health care district

Date: \_\_\_\_\_

\_\_\_\_\_  
By:  
Its: Chief Financial Officer

**PALOMAR POMERADO NORTH COUNTY HEALTH**  
**DEVELOPMENT, INC., a California nonprofit corporation**

Date: \_\_\_\_\_

\_\_\_\_\_  
By:  
Its: Chair

**PALOMAR POMERADO NORTH COUNTY HEALTH**  
**DEVELOPMENT, INC., a California nonprofit corporation**

Date: \_\_\_\_\_

\_\_\_\_\_  
By:  
Its: Treasurer

**EXHIBIT 2.1(a)**

**PROMISSORY NOTE**

[Place of Execution]

Not to Exceed \$ \_\_\_\_\_

**FOR VALUE RECEIVED**, Palomar Pomerado North County Health Development, Inc., a California nonprofit public benefit corporation ("Health Development"), promises to pay to the order of Palomar Pomerado Health, a local health care district organized under the laws of the State of California ("PPH"), the principal sum equal to the outstanding amount of Advances paid to Health Development pursuant to the Management Services Agreement by and between Health Development and PPH dated as of \_\_\_\_\_, 2005 (the "Management Services Agreement"). Unless otherwise defined in this Promissory Note (the "Note"), each capitalized term shall have the meaning given in the Management Services Agreement. The outstanding principal amount of the Advances provided to Health Development pursuant to the Management Services Agreement (the "Principal") shall not \_\_\_\_\_ Dollars (\$ \_\_\_\_\_)

**1. Advances of Principal; Interest.**

(a) Health Development hereby promises to pay to the order of PPH, at such place as PPH may from time to time designate in writing, in lawful money of the United States of America, the Principal and accrued interest thereon.

(b) Interest shall accrue on the Advances at a rate equal to **two and one-half percent (2.5%)** above the one (1) year LIBOR (the "Interest Rate"), computed annually on the basis of a 360-day year, and the number of days elapsed from the date each Advance is deposited into Health Development's Account until the outstanding Advances are repaid. Accrued interest shall be paid monthly in arrears on the first Business Day of each month. The interest rate shall be adjusted quarterly to reflect changes in the prime rate. The first (1st) Advance shall fix the prime rate for that calendar quarter. Any subsequent Advance in that quarter shall be assigned the same prime rate. Notwithstanding any other provision of this Agreement, the Interest Rate shall not exceed the maximum rate permitted by applicable law (the "Permitted Rate"). If any payments in the nature of interest exceed the Permitted Rate, as finally determined by a court of competent jurisdiction, any such amount in excess shall be considered payment of Principal and the Principal outstanding shall be reduced accordingly.

**2. Repayment.**

(a) Notwithstanding any other provisions of this Note, Principal, accrued interest, and other applicable fees, costs and charges ("Costs"), if any, owing on this Note shall be payable as follows:

(b) Repayment. Principal and accrued interest thereon shall be payable in sixty (60) equal monthly installments sufficient to fully amortize the unpaid balance of this Note. Principal and accrued interest thereon shall be payable on the first (1<sup>st</sup>) Business Day of each

successive calendar month beginning on the Credit Line Expiration Date and continuing until the earlier of (i) the date on which the Principal and all accrued interest thereon, and all Costs, if any, are paid in full, or (ii) the Maturity Date (as defined below). In all events, and subject to the remaining provisions of this Section 2, the entire then-outstanding balance of Principal and all accrued, unpaid interest thereon, and all Costs, if any, shall be due and payable by Health Development to PPH no later than the Maturity Date, the "Maturity Date" shall mean the date that is sixty (60) months from the Credit Line Expiration Date

(c) Application of Payments. Unless otherwise agreed in writing in advance by PPH, each payment or forgiveness with respect to this Note shall be credited as follows: first, against Health Development Expenses; second, against accrued and unpaid interest then due and owing; and third, against the Principal outstanding.

(d) Prepayment. Health Development shall have the right to prepay the Principal outstanding in whole or in part without penalty. Any partial prepayment shall be applied against the Principal outstanding and shall not postpone the due date or alter the amount of any subsequent monthly installment. Any amounts prepaid prior to the Credit Line Expiration Date may be reborrowed.

**3. Events of Default.** The termination for any reason of the Management Services Agreement or the occurrence of any Event of Default of the Management Services Agreement shall constitute an event of default ("Event of Default") under this Note.

**4. Acceleration.** If either an Event of Default (as defined in Exhibit 2.1(b) of this Agreement) occurs, or if this Agreement is terminated by either PPH or Health Development pursuant to Sections 3.2 and 3.3, respectively, of the Agreement, PPH may, at its option, declare the entire Principal outstanding, together with accrued interest and all other Health Development Expenses immediately due and payable to PPH; and PPH shall have all rights, powers and remedies available under the Line of Credit Documents, or accorded by law to a beneficiary or a secured party, including the right to resort to any or all of the Collateral or any other security for any of the obligations of Health Development. PPH may exercise its rights and remedies with respect to the Collateral without resorting or regard to other security or sources for payment. All rights, powers and remedies of PPH in connection with each of the Line of Credit Documents may be exercised at any time by PPH, and from time to time after the occurrence of an Event of Default, are cumulative and not exclusive, and shall be in addition to any other rights, powers or remedies provided by law or equity.

**5. Termination.** Upon the occurrence of an Event of Default or upon termination of the Agreement by PPH or Health Development pursuant to Sections 3.2 and 3.3, respectively, of the Agreement, the outstanding principal amount of the Advances, all accrued but unpaid interest and all other obligations of Health Development under the Agreement may automatically become, or may be declared to be, due and payable in the manner, upon the conditions and with the effect provided in the Agreement.

**6. Costs of Collection.** If PPH exercises its acceleration rights pursuant to this Note, in addition to the Principal outstanding and accrued interest thereon, PPH shall be entitled to collect all costs of collection, including reasonable attorneys' fees incurred in connection with the

protection or realization of collateral and PPH's reasonable collection efforts, whether or not suit on this Note or any foreclosure proceeding is filed. Any and all such costs and expenses shall be payable on demand and secured by the Security Agreement.

**7. Continuing Liability.** Following the occurrence of an Event of Default, Health Development's liability under this Note shall not be affected by PPH's pursuit or non-pursuit of any one or more of its rights, powers or remedies (including, without limitation, its option to accelerate the payment of this Note), regardless of the order in which or the extent to which PPH may pursue any of such rights, powers or remedies, it being understood that the liability of Health Development shall cease only upon satisfaction in full of all of Health Development's obligations arising under this Note and the Management Services Agreement.

**8. No Waiver.** No failure on the part of PPH to exercise any right or remedy under this Note, whether before or after a default, shall constitute a waiver of such right or remedy, and no waiver of any past default shall constitute waiver of any future default. No acceptance of a past due installment or other indulgence granted for time to time shall constitute a waiver of the right to insist upon prompt payment, be deemed to be a novation of this Note or as a reinstatement of the debt evidenced by this Note, or be construed to preclude the exercise of any right which PPH may have under law, by agreement or otherwise. PPH and each endorser or guarantor hereby expressly waive the benefit of any statute or rule of law or equity which would produce a result contrary to or in conflict with the foregoing. Health Development and endorsers of this Note consent to renewals and extensions of time at or after the maturity hereof, without notice, and hereby waive diligence, presentment, protest, demand and notice of every kind and, to the full extent permitted by law, the right to plead any statute of limitations as a defense to any demand under this Note.

**9. Waiver of Notice.** Health Development and each endorser or guarantor of this Note hereby (i) waives presentment, demand, protest and notice of presentment, notice of protest and notice of dishonor of this debt and any other notice respecting this Note, and (ii) agrees that PPH, at any time without notice to such party or such party's consent, may grant extensions of time, without limit as to the number or the aggregate period of such extensions, for the payment of any Principal of or interest accrued thereon.

**10. Choice of Law.** This Note shall be construed in accordance with and governed by the laws of the State of California, without giving effect to any choice of law or conflict of law rules or provisions that would cause the application of the laws of any jurisdiction other than the State. Health Development and each endorser or guarantor hereby submit to jurisdiction in said State for the enforcement of Health Development's obligations under this Note and all other Line of Credit Documents, and waive any and all rights under the laws of any other state to object to jurisdiction within such State.

**11. Amendments.** This Note may be modified or amended only by mutual written agreement of the Parties. Any such modification or amendment must be in writing, dated, signed by the Parties and attached to this Note.

**12. Assignment.** Health Development shall not assign, sell, transfer or delegate any of the Health Development's rights or duties under this Note without the prior written consent of

PPH. PPH may assign its rights and delegate its duties under this Note upon written notice to Health Development.

**13. Notices.** Any notice required or permitted to be given in this Note shall be given in accordance with the notices provision of the Management Services Agreement.

**14. Security.** This Note is secured by a first priority security interest granted by Health Development to PPH in the Collateral described in that certain Security Agreement of even date herewith (the "Security Agreement") by and between Health Development and PPH. All of the provisions contained in the Security Agreement are hereby made a part of this Note to the same extent and with the same effect as if they were fully set forth in this Note.

**15. Severability.** If any provision of this Note, in whole or in part, or the application of any provision, in whole or in part, is determined to be illegal, invalid or unenforceable by a court of competent jurisdiction, such provision or part of such provision shall be severed from this Note, and such severance shall have not effect upon the enforceability, performance or obligations of the remainder of this Note, including the remainder of such provision not determined to be illegal, invalid or unenforceable.

**16. Successors and Assigns.** The provisions of this Note shall inure to the benefit of and shall be binding upon the heirs, assigns, successors and representatives of Health Development and PPH, respectively. The term "Health Development" shall mean Health Development and each heir, successor, assign, and representative of Health Development as obligor of this Note. The term "PPH" shall mean PPH and each successor, assign, and representative of PPH as payee or holder of this Note.

[REMAINDER OF PAGE INTENTIONALLY LEFT BLANK]

**DRAFT-DO NOT SIGN**  
**For discussion purposes only.**

Health Development has executed and delivered this Note as of the date and at the place first above written.

**PALOMAR POMERADO NORTH COUNTY HEALTH  
DEVELOPMENT, INC.,**  
a California nonprofit public benefit corporation

\_\_\_\_\_  
By: \_\_\_\_\_  
Its: \_\_\_\_\_



**EXHIBIT 2.1(b)**

**SECURITY AGREEMENT**

THIS SECURITY AGREEMENT (this "Security Agreement"), executed and delivered as of \_\_\_\_\_, 2005, by PALOMAR POMERADO NORTH COUNTY HEALTH DEVELOPMENT, INC., a California nonprofit public benefit corporation ("Debtor"), for the benefit of PALOMAR POMERADO HEALTH, a local health care district organized under the laws of the State of California ("Secured Party").

**RECITALS**

A. Debtor and Secured Party desire to enter into this Security Agreement to grant a security interest to Secured Party in the Collateral, as hereinafter defined, to secure the performance of the obligations and duties of Debtor under the Agreement.

**AGREEMENT**

NOW THEREFORE, in consideration of the mutual covenants and agreements contained herein, the parties hereto agree as follows:

**ARTICLE I.**  
**COLLATERAL AND SECURITY INTEREST**

**1.1 Collateral and Grant of Security Interest.** Debtor hereby grants to Secured Party a security interest of first priority in the Collateral, as described in Attachment A, to secure the payment and performance of all indebtedness, liabilities and obligations of Debtor to Secured Party under the Agreement and repayment of the principal amount of the Advances (as defined in Section 3.2 of the Agreement) and accrued interest thereon. The security interest created by this Security Agreement shall attach immediately on execution of this Security Agreement by Debtor.

**1.2 Perfection and Priority.** Debtor shall take all action necessary to perfect the security interest granted to Secured Party in Section 1.1 of this Security Agreement. Secured Party's security interest in the Collateral is, and will continue to be, a first priority security interest which is free and clear of all liens, claims, security interest and encumbrances, except with respect to any liens, claims, security interest and encumbrances granted by statute or pursuant to any other agreement executed by and between Secured Party and Debtor. Secured Party shall have no duty to collect or protect the Collateral, nor to preserve rights against prior parties or any other rights pertaining to the Collateral. Secured Party shall perfect its security interest in the Account (as defined in Section 1.5 herein) by sending to the appropriate financial institution a letter in the form of Attachment B.

**1.3 Further Assurances.** Debtor shall, from time to time, at Debtor's expense, execute and file any financing or continuation statements, or amendments thereto, and other instruments, endorsements or notices, and take other actions, reasonably necessary or as Secured Party reasonably requests, in order to perfect and preserve the assignments and security interests

granted or purported to be granted by this Security Agreement. Debtor authorizes Secured Party to file one or more financing or continuation statements, and amendments thereto, relative to all or any part of the Collateral without Debtor's signature where permitted by law. Copies of any such statement or amendment shall promptly be delivered to Debtor. Debtor shall notify Secured Party of any change in Debtor's name, identity or corporate structure at least fifteen (15) days prior to any such change.

**1.4 Principal Place of Business.** Debtor's principal place of operation, where Debtor shall keep records regarding the Collateral, is located at \_\_\_\_\_ Debtor shall not relocate Debtor's principal place of operation without providing at least sixty (60)-days prior written notice to Secured Party.

**1.5 Business Deposit Account.** Debtor shall establish and maintain business deposit accounts ("Accounts") with \_\_\_\_\_, or such other financial institution as is mutually selected and approved in writing by Debtor and Secured Party (the "Depository Bank"). Debtor shall promptly deposit all donations and grants received by Debtor into the Account. If any Event of Default occurs, Secured Party may, by written notice to the Depository Bank, terminate Debtor's right to make any withdrawal from the Account and exercise any other right under this Agreement, at law, equity or otherwise applicable to the proceeds of the Account.

## **ARTICLE II.** **REPRESENTATIONS AND WARRANTIES**

Debtor makes the following representations and warranties to Secured Party, which shall be true and correct on and as of the date of this Agreement:

**2.1 Authorization and Validity.** This Security Agreement, and any other document, contract or instrument delivered to Secured Party in connection with this Security Agreement have been duly authorized by Debtor, and are legal, valid and binding agreements and obligations of Debtor, enforceable in accordance with their respective terms, except as limited by bankruptcy, insolvency, reorganization, moratorium or similar laws affecting creditors' rights generally.

**2.2 Governmental Consents.** No consent, approval, order or authorization of, or registration, qualification, designation, declaration or filing with, any federal, state or local governmental authority on the part of Debtor is required in connection with the consummation of the transactions contemplated by this Security Agreement.

**2.3 No Violation.** The execution, delivery and performance by Debtor of this Security Agreement, and any other document, contract or instrument delivered to Secured Party in connection with this Security Agreement, do not violate any provision of any law or regulation or result in a breach of or constitute a default under any contract, obligation, indenture or other instrument to which Debtor is a party or by which Debtor may be bound, except for any such breach or default which has been duly waived or consented to by all necessary parties.

**2.4 No Events of Default.** Debtor is not in default under any debt or obligation of Debtor and no event has occurred which would become an event of default under any such debt or obligation with or without the giving of notice, the lapse of time, or both.

**2.5 Collateral.** Debtor owns the property granted by it as Collateral to Secured Party free and clear of any and all liens, claims, charges, pledges, security interests, deeds of trust, mortgages and other encumbrances in favor of third parties, or any other arrangements having the practical effect of the foregoing, or preferential arrangements of any other kind.

**2.6 No Litigation.** There is no action, proceeding or investigation pending or threatened, or any basis therefor known to Debtor, that questions the validity of this Security Agreement or the right of Debtor to enter into this Security Agreement, or that would have, either individually or in the aggregate, a Material Adverse Effect. "Material Adverse Effect" shall mean a material adverse effect upon Debtor's purpose, function, operation or status or upon Secured Party's security interest in the Collateral. There is no judgment, decree or order of any court in effect against Debtor and Debtor is not in default with respect to any order of any governmental authority to which Debtor is a party or by which Debtor is bound.

**2.7 Existence and Authority.** Debtor is a public benefit corporation duly organized and validly existing in good standing under the laws of the State of California. Debtor has the power and authority, rights and franchises to own its properties and to carry on its operations as now conducted. Debtor has the power and authority to make and carry out this Security Agreement.

### **ARTICLE III.** **COVENANTS OF DEBTOR**

Debtor covenants that so long as any indebtedness, liabilities and obligations (whether direct or contingent, liquidated or unliquidated) of Debtor to Secured Party under the Agreement (including payment of Health Development Expenses or repayment of the principal amount of the Advances and accrued interest thereon) remain outstanding, and until payment and performance in full of all obligations of Debtor under this Security Agreement:

**3.1 Compliance with Laws.** Debtor shall comply with the requirements of all laws, rules, regulations and orders of any governmental authority applicable to Debtor or its operation.

**3.2 Performance and Compliance with Other Agreements.** Debtor shall perform and comply in all material respects with each of the provisions of each material indenture, contract and other agreement by which Debtor or any of its properties is bound.

**3.3 Taxes and Other Liabilities.** Debtor shall pay and discharge when due any and all indebtedness, obligations, assessments and taxes, both real or personal and including federal and state income taxes, which in the aggregate the nonpayment of which would have a Material Adverse Effect, except such as Debtor may in good faith contest or as to which a bona fide dispute may arise, so long as provision is made to the satisfaction of Secured Party for eventual payment thereof if it is found that payment is an obligation of Debtor.

**3.4 Notices to Secured Party.** Within ten (10) days after Debtor has actual knowledge of the occurrence of each such event or matter, Debtor shall give written notice to Secured Party of: (i) the occurrence of any Event of Default (defined below), or any condition, event or act which would become an Event of Default with or without the giving of notice; or (ii) the commencement, or threatened commencement (of which Debtor has received written notice) of any litigation, arbitration or other proceeding against Debtor involving a reasonably potential liability.

**3.5 Records and Reports.** Debtor shall maintain books and records pertaining to the Collateral in such detail, form and scope as is consistent with good business practice, ensure that such books and records reflect Secured Party's interest in the Collateral, and permit Secured Party or its agents to enter upon the premises of Debtor at any time and from time to time, during normal business hours and upon reasonable notice under the circumstances, and at any time at all on and after the occurrence of an Event of Default, for the purposes of inspecting and verifying the Collateral, and inspecting and/or copying (at Debtor's expense) any and all records pertaining to the Collateral.

**3.6 Change in Collateral.** Debtor shall not transfer or otherwise dispose of or encumber all or any part of the Collateral, without Secured Party's prior written consent; provided, however, that in the absence of an Event of Default under this Agreement Debtor shall be entitled to utilize the Collateral in the ordinary course of business for the payment of the debts and obligations of Debtor in accordance with the terms set forth in the Agreement and any agreements, documents and exhibits incorporated in or ancillary to the Agreement. Debtor shall give Secured Party thirty (30) days' prior written notice of any proposed change in the location of any Collateral or in the location of Debtor's place of operation, advise Secured Party promptly, in sufficient detail, of any change relating to the type, quantity or quality of the Collateral, or any event which could have an adverse effect on the value of the Collateral or on the security interests granted to Secured Party in the Collateral, and defend the Collateral against all claims and demands of all persons at any time claiming the same or any interest in the Collateral.

**3.7 Guaranties.** Debtor shall not agree to any guarantee or liability or become liable in any way as surety, endorser (other than as endorser of negotiable instruments for deposit or collection in the ordinary course of business), accommodation endorser or otherwise for, nor pledge or hypothecate any assets of Debtor as security for, any liabilities or obligations of any other person or entity, without Secured Party's prior written consent.

**3.8 Change in Purpose and Operation.** Debtor shall not make any substantial change in the present character of Debtor's purpose and operation, without Secured Party's prior written consent.

**ARTICLE IV.**  
**EVENTS OF DEFAULT**

**4.1 Events of Default.** The occurrence of any of the following shall constitute an "Event of Default" under this Agreement:

(a) Failure, breach or default in the performance of the obligations and duties of Debtor under the Agreement including the payment of Health Development Expenses or repayment of the Advances as provided in Section 3.6 of the Agreement;

(b) Debtor fails to perform or satisfy when due any obligation, agreement, covenant or condition contained in this Security Agreement, and with respect to any such default which by its nature can be cured, such default continues for a period of thirty (30) days from its occurrence;

(c) Any representation or warranty made by Debtor in connection with this Security Agreement or the Agreement proves to be false, incorrect or incomplete in any material respect when furnished or made;

(d) Any levy upon, seizure or attachment of any of the Collateral, or any other event or circumstance pursuant to which Secured Party ceases to have a valid and perfected first priority security interest in the Collateral;

(e) Debtor admits in writing its inability to pay its debts as they mature, or commences any voluntary proceedings under any bankruptcy, reorganization, arrangement, insolvency, readjustment of debt, dissolution, liquidation or other similar law of any jurisdiction;

(f) Any application or proceeding described in (d) above is filed or commenced against Debtor, and Debtor indicates its approval, consent or acquiescence thereto, or an order is entered adjudicating Debtor bankrupt or insolvent and such order remains in effect for thirty (30) days;

(g) Debtor transfers all or substantially all of its properties to, or merges with or into, any other entity; or

(i) Any change having a Material Adverse Effect on Debtor, or any other event or condition which Secured Party reasonably and in good faith believes impairs, or is substantially likely to impair either: (i) the prospect of payment or performance by Debtor of its obligations under this Security Agreement or the Agreement; or (ii) the rights and remedies of Secured Party under this Security Agreement or the Agreement.

**4.2 Remedies.** If an Event of Default occurs, Secured Party shall have all rights, powers and remedies available under this Security Agreement or the Agreement, or accorded by law to a beneficiary or a secured party, including the right to resort to any or all of the Collateral or any other security for any of the obligations of Debtor. Secured Party may exercise its rights and remedies with respect to the Collateral without resorting or regard to other security or sources for payment. All rights, powers and remedies of Secured Party in connection with this Security Agreement or the Agreement may be exercised at any time by Secured Party, and from time to time after the occurrence of an Event of Default, are cumulative and not exclusive, and shall be in addition to any other rights, powers or remedies provided by law or equity.

**4.3 Action on Collateral.** If any Event of Default occurs and continues, Secured Party may exercise with respect to the Collateral: (a) all the rights and remedies of a secured

party on default under the Uniform Commercial Code of the State of California (the "Code") (whether or not the Code applies to the affected Collateral); (b) all of the rights and remedies provided for in this Security Agreement or the Agreement; and (c) such other rights and remedies as may be provided by law or otherwise.

**4.4 Waiver.** Debtor waives (to the extent permitted by applicable law): (a) notice of the acceptance of this Security Agreement and all other notices, demands or protests to which Debtor might otherwise be entitled by law in respect to this Security Agreement, all other Line of Credit Documents or the Collateral; and (b) all rights of redemption, stay and/or appraisal which Debtor now has or may at any time in the future have under any rule of law or statute now existing or hereafter enacted.

**ARTICLE V.**  
**GENERAL PROVISIONS**

**5.1 Amendment.** This Security Agreement may be modified or amended only by mutual written agreement of the Parties. Any such modification or amendment must be in writing, dated, signed by the Parties and attached to this Security Agreement.

**5.2 Dispute Resolution.** In the event of any controversy or dispute related to or arising out of this Security Agreement, the Parties agree to meet and confer in good faith to attempt to resolve the controversy or dispute without an adversary proceeding. If the controversy or dispute is not resolved to the mutual satisfaction of the Parties within five (5) business days of notice of the controversy or dispute, the Parties agree to waive their rights, if any, to a jury trial, and to submit the controversy or dispute to a retired judge or justice pursuant to Section 638 *et seq.* of the California Code of Civil Procedure, or any successor provision, for resolution in accordance with Chapter 6 (References and Trials by Referees), of Title 8 of Part 2 of the California Code of Civil Procedure, or any successor chapter. The Parties agree that the only proper venue for the submission of claims is the County of San Diego, California, and that the hearing before the referee shall be concluded within nine (9) months of the filing and service of the complaint. The Parties reserve the right to contest the referee's decision and to appeal from any award or order of any court.

**5.3 Assignment.** This Security Agreement shall be binding on and inure to the benefit of the heirs, executors, administrators, legal representatives, successors and assigns of the Parties; provided, however, that Debtor may not assign or transfer its interest or obligations under this Security Agreement without the prior written consent of Secured Party. Secured Party reserves the right to sell, assign, transfer, negotiate or grant participation in all or any part of, or any interest in, Secured Party's rights and benefits under this Security Agreement, the Note and any other Line of Credit Document.

**5.4 Attorneys' Fees, Costs and Expenses.** Debtor shall hold Secured Party harmless from, and pay to Secured Party immediately upon demand, the full amount of all costs and expenses, including reasonable attorneys' fees, incurred by Secured Party in connection with: (i) Secured Party's administration of this Security Agreement or the Agreement (including any costs or other expenses incurred in establishing or maintaining the Collateral); (ii) the enforcement of Secured Party's rights and/or the collection of any amounts which become due to Secured Party

under the Agreement (including in connection with any bankruptcy, reorganization, or similar circumstance or proceeding); and (iii) the prosecution or defense of any claim, or action in any way arising out of or related to this Security Agreement, the Agreement or the transactions contemplated thereby, including without limitation any action for declaratory relief. Any judgment or order entered in such action shall contain a specific provision providing for the recovery of attorneys' fees and costs incurred in enforcing such judgment. For the purpose of this Agreement, "attorneys' fees" shall include fees incurred in connection with post judgment motions, contempt proceedings, garnishment, levy, and debtor and third-party examinations, discovery and bankruptcy litigation.

**5.5 Choice of Law.** This Security Agreement shall be construed in accordance with and governed by the laws of the State of California, except choice of law rules that would require the application of the laws of any other jurisdiction.

**5.6 Compliance with Laws.** Debtor shall comply with all applicable laws, ordinances, codes and regulations of federal, state and local governments, including without limitation laws that require Debtor to disclose any economic interest or relationship with Secured Party.

**5.7 Confidentiality.** Neither Party shall disclose this Security Agreement or any of its terms to any person or entity, other than its attorneys and accountants, without the prior written consent of the other Party, unless and only to the extent such disclosure is required by law.

**5.8 Counterparts.** This Security Agreement may be executed in one or more counterparts, each of which shall be deemed to be an original, but all of which together shall constitute one and the same instrument.

**5.9 Entire Agreement.** This Security Agreement (including all agreements incorporated herein by referenced or mentioned herein) together with the Agreement constitutes the entire understanding and agreement of the Parties regarding its subject matter, and supersedes any prior oral or written agreements, representations, understandings or discussions between the Parties. No other understanding between the Parties shall be binding on them unless set forth in writing, signed and attached to this Security Agreement.

**5.10 Exhibits.** The attached exhibits, together with all documents incorporated by reference in the exhibits, form an integral part of this Security Agreement and are incorporated into this Security Agreement wherever reference is made to them to the same extent as if they were set out in full at the point at which such reference is made.

**5.11 Force Majeure.** Neither Party is liable for nonperformance or defective or late performance of any of its obligations under this Security Agreement to the extent and for such periods of time as such nonperformance, defective performance or late performance is due to reasons outside such Party's control, including acts of God, war (declared or undeclared), action of any governmental authority, riots, revolutions, fire, floods, explosions, sabotage, nuclear incidents, lightning, weather, earthquakes, storms, sinkholes, epidemics, or strikes (or similar

nonperformance or defective performance or late performance of employees, suppliers or subcontractors).

**5.12 Headings.** The headings in this Security Agreement are intended solely for convenience of reference and shall be given no effect in the construction or interpretation of this Security Agreement.

**5.13 Notices.** All notices or communications required or permitted under this Security Agreement shall be given in writing and delivered personally, sent by United States registered or certified mail with postage prepaid and return receipt requested or by overnight delivery service (e.g., Federal Express). In each case, notice shall be delivered or sent to the address set forth for Debtor or Secured Party, as applicable, in the Agreement. Notice is deemed given when sent, if sent as specified in this paragraph, or otherwise deemed given when received.

**5.14 Severability.** If any provision of this Security Agreement is determined to be illegal or unenforceable, that provision shall be severed from this Security Agreement, and such severance shall have no effect upon the enforceability of the remainder of this Security Agreement, unless the purposes of this Security Agreement is thereby destroyed.

**5.15 No Third-Party Beneficiary Rights.** The Parties do not intend to confer and this Security Agreement shall not be construed to confer any rights or benefits to any person, firm, group, corporation or entity other than the Parties.

**5.16 Termination.** This Security Agreement and the security interest in Collateral created hereby shall terminate after payment and performance in full of all obligations arising under the Agreement. Upon such termination, the Collateral shall be released from the security interest hereby created, and Secured Party will execute and deliver to Debtor such documents as Debtor shall reasonably request to evidence such release.

**5.17 Waiver.** No delay, failure or discontinuance of Secured Party in exercising any right, power or remedy under this Security Agreement or the Agreement shall constitute a waiver of such right, power or remedy; nor shall any single or partial exercise of any such right, power or remedy preclude, waive or otherwise affect any other or further exercise thereof or the exercise of any other right, power or remedy. Any waiver, permit, consent or approval of any kind by Secured Party of any breach of or default under this Security Agreement or the Agreement must be in writing and shall be effective only to the extent expressly set forth in such writing.

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Secured Party and Debtor have executed this Security Agreement on the date first above written.

**SECURED PARTY**

**PALOMAR POMERADO HEALTH, a local California health care district**

By: \_\_\_\_\_  
Its: \_\_\_\_\_

**DEBTOR**

**PALOMAR POMERADO NORTH COUNTY HEALTH DEVELOPMENT, INC., a California nonprofit public benefit corporation**

By: \_\_\_\_\_  
Its: \_\_\_\_\_

**ATTACHMENT A TO EXHIBIT 2.1(b)**

**DESCRIPTION OF COLLATERAL**

Except to the extent the granting of a security interest is limited by application of law with respect to payments from governmental entities, all present and future right, title and interest of Debtor in and to: (a) donations and grants from all sources; (b) furniture, fixtures and equipment; (c) all monies from time to time on deposit in Debtor's business bank accounts as established in accordance with this Agreement; (d) documents; (e) insurance proceeds; (l) all books and records in respect to the foregoing; and (m) to proceeds of all the foregoing, whether now existing or hereafter acquired or arising (collectively, the "Collateral").

**ATTACHMENT B TO EXHIBIT 2.1(b)**  
**[LETTERHEAD OF PALOMAR POMERADO HEALTH]**

[Address of Bank]

\_\_\_\_\_, 20\_\_

Re: Notice of Security Interest in Account

Ladies and Gentlemen:

Please take notice that PALOMAR POMERADO HEALTH, a local health care district organized under the laws of the State of California (“PPH”), holds a security interest in a business deposit account, number at \_\_\_\_\_, maintained for PALOMAR POMERADO NORTH COUNTY HEALTH DEVELOPMENT, INC., a California nonprofit public benefit corporation (“Health Development”).

The security interest is held pursuant to that certain Security Agreement by and between PPH and Health Development, dated as of \_\_\_\_\_, 2005, a copy of which is enclosed.

Sincerely,

\_\_\_\_\_  
Name: \_\_\_\_\_  
Title: \_\_\_\_\_

**EXHIBIT 4.2**

**OBLIGATIONS UNDER THE HEALTH INSURANCE PORTABILITY AND  
ACCOUNTABILITY ACT OF 1996 ("HIPAA")**

PPH and Health Development shall execute a Business Associate Agreement which shall set forth the terms and conditions under which Protected Health Information ("PHI") that is created or received by Health Development from or on behalf of PPH will be used, disclosed and otherwise handled by Health Development, consistent with the following:

1. **Use of Protected Health Information.** Health Development shall use PHI only as expressly permitted by the Business Associate Agreement and for the purpose of performing its obligations under this Agreement or as otherwise required by law. Health Development shall not use PHI in any manner that would constitute a violation of HIPAA if done by PPH.
2. **Permitted Disclosures.** Health Development shall disclose PHI, only as expressly permitted or by the Business Associate Agreement and for the purpose of performing its obligations under this Agreement or as otherwise required by law. Health Development shall not disclose PHI in any manner that would constitute a violation of the HIPAA if done by PPH.
3. **Appropriate Safeguards.** Health Development shall implement appropriate safeguards as are necessary to prevent the use or disclosure of PHI other than as permitted or required by the Business Associate Agreement.
4. **Reporting of Improper Use or Disclosure.** Health Development shall notify PPH in writing of any use or disclosure of PHI that is not permitted or required by the Business Associate Agreement within two (2) days of becoming aware of such use or disclosure.
5. **Agents and Subcontractors.** Health Development shall require all of its subcontractors and agents that receive, use, or have access to PHI to agree to adhere to the same restrictions and conditions that apply to Health Development under the Business Associate Agreement
6. **Access to Records.** Health Development shall make their respective internal practices, books and records relating to the use and disclosure of PHI available to PPH for purposes of determining Health Development's compliance with the Business Associate Agreement or to the Secretary of the U.S. Department of Health and Human Services for purposes of determining PPH's compliance with the Privacy Rule.
7. **Access, Amendment and Accounting.** Health Development shall comply with requests by PPH regarding individuals' rights of access, amendment and to receive an accounting of the uses and disclosures of their PHI in accordance with processes and time frames which shall be set forth in the Business Associate Agreement.

8. **Security Rule Compliance.** Health Development shall (a) implement administrative, physical and technical safeguards that reasonably and appropriately protect the confidentiality, integrity and availability of electronic PHI, (b) ensure that any agent or subcontractor to whom it provides any electronic PHI agrees in writing to implement similar safeguards as those required of the Business Associate Agreement, and (c) report to PPH, in writing, any security incident of which it becomes aware within two (2) days of becoming aware of such security incident.

9. **Term of Obligations.** Health Development's obligations shall commence as of the compliance date of the effective date of this Agreement, and shall terminate when the Business Associate Agreement is terminated and all of the PHI is destroyed or returned to PPH.

10. **Effect of Termination.** Upon expiration or termination of this Agreement or the Business Associate Agreement for any reason, Health Development shall return or destroy all PHI that Health Development still maintains in any form and shall retain no copies of such PHI. If return or destruction is not feasible, as determined by PPH, Health Development shall continue to extend the protections discussed above to such information, and limit further use and disclosure of such PHI to those purposes that make the return or destruction of such PHI infeasible.

11. **Amendment.** The parties agree to take such action as is necessary to amend the Business Associate Agreement from time to time in order for PPH to comply with the requirements of HIPAA, and other applicable laws relating to the security or confidentiality of PHI.

12. **Interpretation of Obligations.** The obligations as set forth above shall be interpreted as broadly as necessary to allow PPH to implement and comply with its obligations under HIPAA . The parties acknowledge and agree that any ambiguity in the obligations set forth in the Business Associate Agreement shall be resolved in favor of a meaning that permits PPH to comply with its obligations under HIPAA .

13. **Definitions.**

- a. **"Privacy Rule"** shall mean the Standards for Privacy of Individually Identifiable Health Information, 45 C.F.R. Part 160 and Part 164, Subparts A and E, as amended from time to time, under HIPAA.
- b. **"Security Rule"** shall mean the Security Standards, 45 C.F.R. Part 160 and Part 164, Subpart C, as amended from time to time, under HIPAA.
- c. **"HIPAA"** shall mean 42 U.S.C. 1320d-1 *et seq.*, the Privacy Rule, the Security Rule, and the Standards for Electronic Transactions, 45 C.F.R. Part 160 and Part 162, all as amended from time to time.
- d. All other capitalized terms used, but not otherwise defined, in the Business Associate Agreement shall have the meaning set forth in the Privacy Rule and/or Security Rule as applicable.