DOCKET NO. : OAG 15-486-01

IN RE APPLICATION FOR ASSET PURCHASE	**:**	**OFFICE OF THE ATTORNEY GENERAL**
BY PROSPECT MEDICAL HOLDINGS, INC. OF	**:**	
EASTERN CONNECTICUT HEALTH NETWORK	**:**	
INC.	**:**	**MAY 25, 2016**

PROPOSED FINAL DECISION

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I. INTRODUCTION

The proposed asset purchase agreement between Eastern Connecticut Health Network, Inc., and its affiliates ("ECHN"), and Prospect Medical Holdings, Inc. ("PMH")(collectively, the "Applicants"), is the second Application by ECHN filed with the Office of the Attorney General (the "OAG") for its review pursuant to the Nonprofit Hospital Conversion Act, Conn. Gen. Stat. § 19a-486 et seq. (the "Conversion Act").

On June 4, 2014, ECHN submitted a proposed transaction with Tenet Healthcare Corp. ("Tenet") that was withdrawn by Tenet prior to the completion of the OAG's review under the Conversion Act. This Application comes 2 years afterwards.

The difficulties faced by hospitals in delivering quality healthcare services in a changing and increasingly challenging fiscal landscape have become, appropriately, a subject of national concern and debate. A number of forces in recent years have contributed to the financial challenges to local hospitals, including those in Connecticut. Against the backdrop of a changing regulatory and fiscal landscape at the federal and state level, the delivery of healthcare services remains a local issue of extreme importance to the communities in which nonprofit hospitals operate. These issues are no less true for ECHN than for any other community hospital or hospital system in Connecticut. It is in this context that ECHN has decided to sell substantially all of its assets to PMH. Its stated goal in making this decision is to ensure the continued existence of ECHN's facilities and services, to provide sufficient capital to enhance the facilities and services, and to integrate its operations with an established health care system that is prepared navigate the evolving health care system of the future. (Application of ECHN and PMH re a Proposed Asset Purchase Agreement, AG Docket 15-486-01, pp. 25-26; hereinafter, "App., p. __.)

Pursuant to the Conversion Act, the legislature has authorized the Attorney General to review and investigate proposed nonprofit to for-profit hospital transactions, to disapprove them if he finds that any of the criteria set forth in Conn. Gen. Stat. § 19a-486c(a) are not met, or to approve the transaction subject to any modifications or conditions that the Attorney General deems appropriate. Conn. Gen. Stat. § 19a-486b. Under the law, the Attorney General is required to assess both the procedural and financial fairness of the transaction and to protect and preserve the charitable assets of ECHN.

Contemporaneously with the OAG's review of the proposed Asset Purchase Agreement (the "APA"), the Office of Health Care Access, Department of Public Health ("OHCA"), has been reviewing the transaction to determine whether a certificate of need should be issued in this case and also whether OHCA's criteria in the Conversion Act have been fulfilled by the Applicants. In contrast to the Attorney General's focus, OHCA's review encompasses issues involving the impact of the proposed transaction on access to, and the quality of, health care in the ECHN service area.

As explained in detail below, we grant the Application with conditions necessary to conform the proposed transaction to the requirements of the Conversion Act. I would like to thank ECHN and PMH for their cooperation throughout this process. I would also like to thank the many witnesses, public officials, and members of the public who testified or commented on the proposed transaction in our proceedings. Last, I would like to thank my staff, Assistant Attorney General Henry Salton, head of the Health and Education Department, Assistant Attorney General Gary W. Hawes, and Paralegal Specialist Cheryl A. Turner for their diligent efforts on this matter.

II. EXECUTIVE SUMMARY

A. Standard of Review

Pursuant to the requirements of the Conversion Act, the OAG is required to review a proposed transaction for compliance with specifically articulated standards that were established by the legislature. § 19a-486c(a). In sum, these criteria require the OAG to make certain determinations: whether the nonprofit hospital's decision to sell its assets was reasonable, whether it chose the ultimate purchaser in an open and fair process, whether it received fair market value for its assets, whether the funds generated by the sale will be held by a charitable foundation that will use them for the promotion of healthcare in the nonprofit hospital's community, and whether use restrictions on any charitable asset held by ECHN will be preserved.[1]

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[1] Conn. Gen. Stat. § 19a-486c(a) provides in full:

The Attorney General shall deny an application as not in the public interest if the Attorney General determines that one or more of the following conditions exist:

(1) the transaction is prohibited by Connecticut statutory or common law governing nonprofit entities, trusts or charities;
(2) the nonprofit hospital failed to exercise due diligence in (A) deciding to transfer, (B) selecting the purchaser, (C) obtaining a fairness evaluation from an independent person expert in such agreements, or (D) negotiating the terms and conditions of the transfer;
(3) the nonprofit hospital failed to disclose any conflict of interest, including, but not limited to, conflicts of interest pertaining to board members, officers, key employees and experts of Waterbury Hospital, the purchaser or any other party to the transaction;
(4) the nonprofit hospital will not receive fair market value for its assets, which, for purposes of this subsection, means the most likely price that the assets would bring in a sale in a competitive and open market under all conditions requisite to a fair sale, with the buyer and seller each acting prudently, knowledgeably and in their own best interest, and with a reasonable time being allowed for exposure in the open market;
(5) the fair market value of the assets has been manipulated by any person in a manner that causes the value of the assets to decrease;
(6) the financing of the transaction by the nonprofit hospital will place the nonprofit hospital's assets at an unreasonable risk;
(7) any management contract contemplated under the transaction is not for reasonable fair value;

B. The Proposed Transaction

ECHN and PMH propose an asset purchase whereby ECHN will sell substantially all of its assets to PMH or one or more affiliates of PMH. Substantially all of the assets of ECHN will be transferred to PMH in exchange for $105,000,000, subject to certain adjustments.[2] The adjustments include a Net Working Capital reconciliation, reductions for the value of ECHN liabilities assumed by PMH, and adjustments for the value of any ECHN joint venture interest not assigned or transferred to PMH. Pursuant to the APA, PMH will also commit to spend not less than $75,000,000 on capital items over five years. (App., p. 23.)

PMH will continue to operate both Manchester Memorial Hospital ("MMH") and Rockville General Hospital ("RGH") as acute care hospitals for at least three years after the

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(8) a sum equal to the fair market value of the nonprofit hospital's assets (A) is not being transferred to one or more persons to be selected by the superior court for the judicial district where the nonprofit hospital is located who are not affiliated through corporate structure, governance or membership with either the nonprofit hospital or the purchaser, unless the nonprofit hospital continues to operate on a nonprofit basis after the transaction and such sum is transferred to the nonprofit hospital to provide health care services, and (B) is not being used for one of the following purposes: (i) For appropriate charitable health care purposes consistent with the nonprofit hospital's original purpose, (ii) for the support and promotion of health care generally in the affected community, or (iii) with respect to any assets held by the nonprofit hospital that are subject to a use restriction imposed by a donor, for a purpose consistent with the intent of said donor; or

(9) the nonprofit hospital or the purchaser has failed to provide the Attorney General with information and data sufficient to evaluate the proposed agreement adequately, provided the Attorney General has notified the nonprofit hospital or the purchaser of the inadequacy of the information or data and has provided a reasonable opportunity to remedy such inadequacy.

[2] The Application indicated that the purchase price would be either $105 million or $115 million, depending on whether ECHN obtained an assumable loan to finance certain of its outstanding bond liabilities. At the public hearing on this transaction, it was confirmed that ECHN had not acquired the loan, and the purchase price was going to be $105 million.

transaction closes.[3] Each hospital will maintain a local advisory board, and substantially all of the employees of ECHN and its affiliates will be offered employment by PMH or its affiliates. (App., p. 24.)

In addition, PMH will ensure that MMH and RGH maintain ECHN's current policies on charity care and indigent care or will adopt other policies that are at least as favorable to the ECHN community. (App., p. 32.)

After the closing, ECHN will establish a new charitable entity ("New Foundation") that will receive the net proceeds of the transaction and the appropriate charitable gift assets held by ECHN.

C. The Proposed Transaction Meets the Requirements of the Conversion Act Provided the Applicants Comply with the Attorney General's Modifications.

Based on our review of the record, all testimony provided at the public hearings, all exhibits provided pursuant to this review, and the standards set forth in § 19a-486c(a), we conclude that the proposed transaction meets the requirements of the Conversion Act, provided that ECHN and PMH comply with the modifications and conditions that are imposed herein.

1. Findings and Conclusions

First, we conclude that the process employed by ECHN in deciding to sell its assets to a for-profit healthcare services company reflects proper due diligence by ECHN's Board of Directors. The ECHN Board undertook an extensive process to explore potential strategic options and identify capital alternatives to address its weakening financial

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[3] At all times, a hospital must receive approval in the form of a Certificate of Need from OHCA before terminating inpatient or outpatient services offered by the hospital. See Conn. Gen. Stat. § 19a-638(a)(5).

position. The Board's efforts have been diligent and without conflicts of interests, and in our opinion, the Board has met their fiduciary obligations to ECHN.

Second, we conclude that ECHN will receive fair market value for its assets as a result of this transaction. Based primarily on the opinions of two independent financial valuation experts, the price negotiated for the sale of ECHN's assets equals or exceeds the price they would command in an open and competitive market.[4] This conclusion is buttressed by the fact that the process followed by the ECHN Board to select a purchaser was itself open and competitive.

Third, assuming compliance with the modifications and conditions set forth below, we conclude that the charitable assets of ECHN will be adequately protected and preserved after the proposed transaction closes. The charitable assets of ECHN, which have been held in trust for the public, will be held by the New Foundation and safeguarded for their specific charitable uses or to promote healthcare in the ECHN service area. We also conclude that a sum equal to the fair market value of ECHN's assets will be transferred to the New Foundation and will be restricted to charitable uses consistent with ECHN's

[4] The nonprofit hospital conversion review process provides the OAG with the opportunity to have two separate, independent financial experts review the proposed transaction for compliance with the provisions of § 19a-486c(a). The first expert opinion is required by § 19a-486c(a)(2)(C), which provides that the nonprofit hospital obtain a fairness evaluation from an independent person expert in such agreement. ECHN hired Duff & Phelps, LLC, for these purposes, and its opinion is in the record. In addition, § 19a-486c(c) allows the Attorney General to contract with a financial expert to assist in the review of the nonprofit hospital's compliance with the provisions in § 19a-486c(a). Through an RFP process, the OAG retained the services of Navigant Consulting, Inc., to provide an additional independent analysis of the APA.

original purpose and for the support and promotion of healthcare generally in the ECHN community.[5]

2. Modifications and Conditions

The General Assembly has assigned the OAG significant responsibility and flexibility to modify the terms of the proposed transaction, if necessary, to fulfill the statutory mandates of the Conversion Act and—in particular—to fulfill the Attorney General's statutory charge to serve the public interest in the protection of gifts, legacies or devises for public or charitable purposes. Conn. Gen. Stat. § 3-125.

Consequently, although we approve the APA, that approval is contingent on certain modifications and conditions that must be made to the proposed transaction to ensure that the interests of the public and the requirements of the Conversion Act are met. These modifications and conditions, which are more fully described in Section V of this decision, include the following:

1. The Applicants must ~~delete~~ revise the language in section 5.18(~~a~~b) of the draft APA submitted to the OAG ~~from the APA~~ so that any deferral is limited to no more than ten (10) years after closing.

2. The Applicants shall notify the OAG in writing of the closing date of the Asset Purchase as soon as reasonably possible after the date has been set. If the closing date changes, the Applicants shall notify the OAG in writing of the change as soon as reasonably possible.

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[5] As discussed in Section IV(H)(1) of this decision, the current estimate on the net proceeds to be transferred to the New Foundation is zero. In other words, after ECHN meets the obligations of its creditors and the provisions in the APA that require capital, there will be very little or nothing left over to transfer to the New Foundation.

3. The Applicants must submit to the OAG, within 30 days of closing, fully executed copies of the Asset Purchase Agreement, without schedules.

4. As soon as reasonably possible after the Applicants have agreed to a Final Closing Statement of the transaction, the Applicants must provide the OAG a final accounting of the transaction that sets forth the balance sheets of ECHN immediately prior to and after the closing and that provides a net proceeds analysis.

5. After the closing, ECHN ("Legacy ECHN") shall hold and protect all charitable gift funds and any net proceeds from the Asset Purchase in its possession until they are transferred to the New Foundation or other charitable organization by order of a court of competent jurisdiction.

6. Legacy ECHN shall report quarterly to the OAG regarding (1) any and all income received by Legacy ECHN post-closing, including, but not limited to, Medicare and Medicaid reimbursements, income from charitable assets held by Legacy ECHN prior to transfer to the New Foundation, and any additional charitable funds received, and (2) all expenditures for Legacy ECHN.

7. When the requirements of the indemnity reserve have been fulfilled, and if there remain any funds in the indemnity reserve, they shall be considered ECHN's net proceeds and be treated accordingly.

8. Any income or unrestricted gifts received by Legacy ECHN post-closing shall be considered net proceeds.

9. The New Foundation shall include paragraph 14 as set forth in the draft Certificate of Incorporation in the final Certificate of Incorporation of the New Foundation, requiring Attorney General approval for changes to paragraphs 2, 5, 8, and 14 of the Certificate of Incorporation.

10. Legacy ECHN must present to the Superior Court, in coordination with the OAG, a petition for equitable deviation and approximation to transfer the unrestricted endowments remaining after any appropriation of net appreciation to the New Foundation and to change the charitable purpose of the unrestricted endowments to the charitable purpose of the New Foundation.

11. Legacy ECHN must, in coordination with the OAG, include the restricted endowments remaining after any appropriation of net appreciation for the restricted purpose in the Superior Court petition for an equitable deviation order, provided that there shall be no appropriation of net appreciation for the Trotter, Baker and Schortman funds. With respect to the Trotter, Baker, and Schortman funds, Legacy ECHN must seek an order of approximation, in addition to one for equitable deviation, to adjust the funds' charitable purposes to ones that come as close as possible to the donor's original charitable intent.

12. Legacy ECHN must, in coordination with the OAG, include any special funds that still have money in them in the Superior Court petition for an equitable deviation and approximation order.

13. Legacy ECHN must, in coordination with the OAG and the third-party trustees, bring any third-party trusts in need of approximation before a court of competent jurisdiction for appropriate orders.

14. Legacy ECHN must, in coordination with the OAG, include the Life Insurance Policy in the Superior Court petition for an equitable deviation order.

15. Any net proceeds from this transaction, including the earnings therefrom, shall be transferred to and then held by the New Foundation and used only for the support and promotion of healthcare in the ECHN community. The net proceeds shall never inure

to the benefit of the for-profit hospital. The net proceeds shall forever be held by the New Foundation for the purposes articulated in the New Foundation's Draft Certificate of Incorporation, unless and until a court of competent jurisdiction orders otherwise.

16. The net proceeds held by the New Foundation shall be considered an endowment fund, as that term is defined in the Connecticut Uniform Prudent Management of Institutional Funds Act, Conn. Gen. Stat. § 45a-535 et seq. ("CUPMIFA").

III. PROCEDURAL HISTORY

On July 17, 2015, OHCA and the OAG received ECHN's certificate of need determination letter that set forth in summary fashion the terms of the APA between the Applicants.[6] Because the OAG determined that the APA required approval pursuant to § 19a-486 et seq., the OAG and OHCA on August 6, 2015, jointly sent the Applicants an Application Form regarding the APA.

The Applicants requested an extension of time to submit their Application, which both agencies granted, On October 13, 2015, the Applicants filed their Application for an Asset Purchase, which included 45 exhibits. Upon review of the Application, the OAG and OHCA determined that the Applicants' Application was not complete, and on October 30, 2015, it requested additional information from the Applicants. Before the Applicants had an opportunity to respond to the October 30 requests, the OAG and OHCA requested further information on November 12, 2015, related to the reports that PMH was up for sale. On November 23, 2015, the Applicants filed responses to the two sets of additional requests set forth by the OAG and OHCA. On December 11, 2015, OHCA issued one last set of

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[6] All docket documents referenced in this opinion can be found on the Attorney General's website: www.ct.gov/ag.

completeness questions, to which the Applicant responded on December 24, 2015. On January 13, 2016, the OAG and OHCA determined that the Application was complete. In order to ensure the completeness of the record, the OAG and OHCA took administrative notice of the record in the Proposed Asset Purchase of Greater Waterbury Health Network, Inc., by Prospect Medical Holdings, Inc., OHCA Docket No. 15-31217-486, OAG Docket No. 15-486-02 (the "GWHN/PMH APA").

Pursuant to Conn. Gen. Stat. § 19a-486e, the OAG and OHCA conducted two public hearings regarding the proposed Asset Purchase, one in Manchester and one in Rockville. The Manchester public hearing was held on March 29, 2016, at 2:00 p.m. at the Manchester Country Club in Manchester, Connecticut. The Rockville public hearing was held on March 30, 2016, at 2:00 p.m. at the Elks Club in Rockville, Connecticut. No person sought intervenor status for the hearings. Conn. Gen. Stat. § 19a-486a(g). All parties submitted pre-filed testimony for the hearings.

The hearings were presided over by representatives from both the OAG and OHCA. Deputy Attorney General Perry Zinn Rowthorn served as the hearing office for the OAG. Also on the panel for the OAG were Assistant Attorney General Henry A. Salton and Assistant Attorney General Gary W. Hawes. Kevin Hansted served as the hearing officer for OHCA. Also on the panel for OHCA were Kimberly Martone, Director for OHCA, Steven W. Lazarus, Associate Health Care Analyst, and Carmen Cotto, Health Care Analyst.

At the hearings, all parties adopted their pre-filed testimony, and all exhibits on the table of record were entered into the record. At both hearings, the Applicants presented full testimony and were subject to cross-examination by OHCA and the OAG. In addition, the hearing panel heard approximately 20 public comments and accepted written public comments. Subsequent to the hearings, the OAG receive one additional public comment.

The Applicants filed late-filed exhibits with OHCA and the OAG on April 20, 2016.

IV. FINDINGS OF FACT

Based upon the entire record of this Application, including all statements, testimony, and exhibits submitted by the Applicants, all public comments made at the hearing or submitted to the OAG in writing, the summary reports and exhibits submitted by the independent financial experts, and the record in the GWHN/PMH APA, we find the following.

A. Parties and other relevant corporate entities

ECHN is a not-for-profit health care system that serves 19 towns in eastern Connecticut including Andover, Bolton, Coventry, Ellington, Manchester, South Windsor, Tolland, Vernon, Willington, Ashford, Columbia, East Hartford, East Windsor, Glastonbury, Hebron, Mansfield, Somers, Stafford, and Union (the "Service Area"). ECHN was formed in 1995 when Manchester Memorial Hospital and Rockville General Hospital joined as partners.

ECHN's care network consists of a number of wholly owned entities: MMH; RGH; ECHN ElderCare Services, Inc.; Visiting Nurse and Health Services of Connecticut, Inc. ("VNHSC"); A Caring Hand, LLC; Clinically Integrated Network of Eastern Connecticut, LLC; Connecticut Healthcare Insurance Company; ECHN Corporate Services, Inc.; Medical Practice Partners, LLC; ECHN Enterprises, Inc.; Haynes Street Property Management, LLC; Eastern Connecticut Medical Professionals Foundation, Inc.; and ECHN Community HealthCare Foundation, Inc.

ECHN has ownership interests in a number of community based services including the following joint ventures: Evergreen Endoscopy Center, LLC; WBC Connecticut East, LLC; Aetna Ambulance Service, Inc.; Metro Wheelchair Service, Inc.; Ambulance Service of Manchester, LLC; Connecticut Occupational Medicine Partners, LLC; Eastern Connecticut Physician Hospital Organization, Inc.; Northeast Regional Radiation Oncology Network, Inc.; Tolland Imaging Center, LLC; Haynes Street Medical Associates, LLC; Haynes Street Medical Associates II, LLC; Evergreen Medical Associates, LLC; and Evergreen Medical Associates II, LLC

PMH is a Delaware corporation with its principal place of business located in Los Angeles, California. PMH is a healthcare services company that owns and operates thirteen acute care and behavioral hospitals located in Rhode Island, Texas, and California. PMH also owns a network of specialty and primary care clinics in each of its regions. Through PMH's medical group segment, PMH manages the provision of physician services to approximately 260,000 patients in Southern California, South Central Texas, and Rhode Island through a network of approximately 8,900 physicians.

PMH currently owns the following hospitals: Los Angeles Community Hospital; Los Angeles Community Hospital at Bellflower; Los Angeles Community Hospital at Norwalk; Southern California Hospital at Hollywood; Southern California Hospital at Van Nuys; Southern California Hospital at Culver City; Foothill Regional Medical Center; Nix Health (four campuses); Roger Williams Medical Center (RI); and Our Lady of Fatima Hospital (RI).

PMH aligns its hospitals and physicians under a model referred to as Coordinated Regional Care ("CRC"). CRC provides for clinical integration among hospitals, physicians and other medical, social and community providers working closely with strategic partner health plans and other payers under a value-based, global risk reimbursement payment system to achieve the triple aim of improved patient care and experience, better patient health, and lower costs.

B. ECHN's Fiscal Condition

ECHN's mission has been impeded since 2001 by various factors, including reduced reimbursement from government payors, limited access to the capital required to improve infrastructure and to recruit and maintain needed physicians, and mounting pension liabilities.

Starting in 2001, when ECHN lost more than $10 million, capital investments had to be deferred and long-term debt and pension liabilities continued to grow. The pension funding reforms of 2006 and the market crash of 2008 created additional financial problems for ECHN. Although ECHN took numerous steps to mitigate the losses from these events, it was still unable to make significant capital investments. ECHN's plans to expand and introduce new programs to help recruit physicians were also put off.

In addition to the financial challenges that ECHN faced at that time, federal and state regulation changed the landscape for health care provider reimbursements and tax burdens. These increased financial burdens over the period of ten years led the Board to consider affiliation options.

C. The Search for Solutions and Partners

In 2011 the ECHN Board authorized the establishment of a workgroup to evaluate whether benefits would be realized by affiliating with another health care system, or whether ECHN would better serve the community by remaining an independent system (the "Partnering Workgroup"). To assist the Partnering Workgroup in its evaluation, ECHN engaged The Chartis Group, LLC ("Chartis"), a national healthcare consulting firm.

In September of 2012, the Partnering Workgroup presented its initial findings to the ECHN Board. The Partnering Workgroup concluded that affiliation with a larger health system would better position ECHN to achieve its goals, and the Board agreed.

From November 2012 through April 2013, the Partnering Workgroup worked with Chartis to develop and conduct a request for proposal (RFP) process for potential partners. RFPs were mailed to three nonprofit health systems and three for-profit health systems. Based upon an initial review of four indications of interest and the conclusion that affiliation appeared to be the best alternative, the ECHN Board created the Transaction Committee to thoroughly evaluate the proposals for affiliation.

After proper due diligence by the Transaction Committee and consideration of the Transaction Committee's recommendation by the ECHN Board, the Board selected a proposed joint venture between Yale New Haven Health System ("YNHHS") and Vanguard Health Systems, Inc. ("Vanguard") as the purchaser of ECHN. Before being able to negotiate a definitive Asset Purchase Agreement, however, ECHN learned that Tenet Healthcare Corporation ("Tenet") was going to acquire Vanguard. The Transaction Committee then performed its due diligence with respect to Tenet and recommended to the Board that ECHN continue with the contemplated transaction. The Board voted to approve the Transaction Committee's recommendation.

ECHN and Vanguard began the regulatory approval process in the summer of 2014 and submitted their application to the OAG and OHCA on October 24, 2014, and filed responses to completeness questions on November 25, 2014. On December 11, 2014, Tenet informed ECHN that it was withdrawing its application for the acquisition of ECHN citing the proposed regulatory conditions that had been placed on its Application to form a joint venture with the Greater Waterbury Health Network, Inc. ("GWHN").[7]

While waiting to see if Tenet might return to Connecticut to pursue its acquisition of ECHN, the Board reaffirmed the need for ECHN to partner. To that end, and with the guidance of The Chartis Group, the Transaction Committee conducted a second RFP process. On February 6, 2015, RFPs were sent to the four systems that had expressed interest in partnering with ECHN and to two additional out-of-state systems that had approached ECHN with interest in an affiliation. ECHN received three responses.

While considering these proposals, two teams of Transaction Committee members and ECHN executives made visits to Los Angeles to tour PMH's management services organization that supports its independent physician practice associations (IPAs) and hospitals for risk-based contracting and population health management. The groups also toured Prospect's Southern California Hospital in Culver City and met with and interviewed representatives in the areas of governance, medical staff leadership, and administration from Prospect's Los Angeles Coordinated Regional Care Market.

Members of the Transaction Committee and ECHN executives also visited CharterCARE Health Partners' Roger Williams Medical Center in Providence, Rhode Island. CharterCARE Health Partners is PMH's coordinated regional care network comprised of Roger Williams Medical Center, Our Lady of Fatima Hospital, a skilled nursing facility, a regional cancer center, a rehabilitation center, a community primary care

[7] On December 11, 2014, Tenet withdrew its applications with respect to the Greater Waterbury Health Network, Inc., Saint Mary's Health System, Inc., Eastern Connecticut Health Network, Inc., and Bristol Hospital and Health Care Group, Inc.

center, a home health services company, an IPA, and a physician group practice based in Providence.

Based upon their due diligence with respect to all the proposals, the Transaction Committee chose to negotiate only with PMH in finalizing a proposed asset purchase agreement. After some of the open items in PMH's proposed APA were addressed through negotiations, the Transaction Committee unanimously recommended to the ECHN Board that it accept PMH's proposal to acquire substantially all of the assets of ECHN. After review, the Board unanimously approved the APA in substantially the form presented to them. The draft APA was then submitted to ECHN's Corporators for consideration. The ECHN Corporators approved the draft APA on July 29, 2015, with 165 voting in favor of the transaction and 4 against.

D. The Proposed Transaction

PMH or a PMH designated subsidiary (hereinafter, "PMH") will purchase substantially all of the assets of ECHN, including the properties, assets and businesses of, or ownership interests of ECHN affiliates. PMH will also purchase ECHN's interests in its or its affiliates' joint ventures.[8]

[8] The assets of ECHN Community HealthCare Foundation, Inc., will not be included in the assets purchased by PMH.

PMH will acquire real property, leased property, equipment, accounts receivable, and net working capital (*i.e.*, non-cash current assets less the value of all current liabilities) of ECHN and the ECHN affiliates. PMH will assume several key liabilities, including ECHN's unfunded pension liabilities, ECHN's health benefit plan for retirees, ECHN's captive insurer liabilities (*i.e.*, Connecticut Healthcare Insurance Company), and ECHN's workers' compensation obligations.

PMH will exclude some current ECHN liabilities that will then remain the responsibility of ECHN's residual corporation following the transaction ("Legacy ECHN"). For example, PMH will not assume liabilities that could arise from lawsuits or tax settlements based on pre-closing activities. ECHN will exclude certain of its assets from the purchase, including certain cash and cash equivalents of ECHN; all short-term and long-term investments, but excluding ECHN's investment interests in the joint ventures; board-designated, restricted, and trustee-held or escrowed funds (such as funded depreciation, debt service reserves, self-insurance trusts, working capital trust assets, and assets and investments restricted to use), beneficial interests in charitable trusts, and accrued earnings on all of the foregoing.

PMH will pay $105,000,000 subject to the Net Working Capital reconciliation, minus the amount of certain ECHN liabilities assumed by PMH (*e.g.* ECHN's unfunded pension obligations, captive insurer liability, capital leases, and the workers' compensation liability), minus asbestos abatement liability of up to $1,000,000, and minus, in the event that ECHN is unable to assign and transfer to PMH ECHN's interest in an ECHN joint venture, a dollar amount to be fixed in advance for each ECHN Joint Venture.

ECHN's proceeds from the APA will first be used to settle all of ECHN's bond liabilities and all of ECHN's other indebtedness not otherwise assumed by PMH. The remaining proceeds will next be used to fund an indemnity reserve for a period of at least three years (the "Reserve Period") following the closing of the transaction for payment of ECHN liabilities to PMH that may arise post-closing. Any proceeds that remain after settling bond liabilities, settling other indebtedness, and funding the indemnity reserve will be held by the residual ECHN corporation to be used for post-closing liabilities and wind down of operations. After expiration of the Reserve Period, any funds remaining in the Reserve and not used to pay claims will be transferred as directed by the Office of the Attorney General of the State of Connecticut with the expectation that such funds will be transferred to a nonprofit foundation and used to support charitable health related efforts in the ECHN Service Area.

After closing, PMH/ECHN, will develop a strategic capital plan with respect to the Hospital Businesses. PMH has committed to spend within five years of the closing not less than $75,000,000 (the "Commitment Amount") for the benefit of the Hospital Businesses and for the benefit of the Service Area of MMH and RGH. These expenditures may include: (i) capital projects, including routine and non-routine capital expenditures for the improvement of ECHN's facilities; (ii) development, expansion, or acquisition of a department, program, service or facility; (iii) upgrades or renovations generally; (iv) deferred maintenance items; and (v) capital expended in support of the recruitment of the hospitals' medical staff located in the hospitals' Service Area.

PMH will offer employment as of the closing to substantially all employees of ECHN and its affiliates who work at the hospital businesses, including employees on approved leaves of absence as of the closing. PMH will offer the hired employees salaries that are equal to their salaries as of the closing date and benefits packages that are comparable to those offered to similarly-situated employees at other hospitals operated by PMH. PMH will assume and honor ECHN's (and its affiliates') collective bargaining agreements.

For at least three years after the closing of the transaction, PMH will continue operating MMH and RGH in their current locations as acute care hospitals with emergency departments. Also, for at least three years after the closing of the transaction, PMH will maintain an ownership interest in ECHN's current post-acute care continuum of care network and require any wholly owned entity involved with such post-acute care continuum of care network to maintain appropriate service lines during such three-year period. PMH will also ensure that each Hospital maintains and adheres to ECHN's current policies regarding charity care, indigent care, community volunteer services and community benefits (or adopts other policies that are at least as favorable to the community as ECHN's current policies).

PMH will maintain and support financially ECHN's University of New England medical student and other health professions teaching programs, as well as ECHN's graduate medical education programs, while operating at a level not to exceed the Indirect Medical Education and Direct Graduate Medical Education caps that may be established by the Centers for Medicare and Medicaid Services.

Following the closing, MMH and RGH will each maintain an advisory board made up of community representatives, physicians on the respective hospital's medical staff, and the Chief Executive Officer of the respective hospital (the "Local Board"). Among other things, the Local Board will serve as a resource for PMH with respect to PMH's investment of the capital commitment, assist with maintenance and implementation of a strategic business plan for the Hospitals, make recommendations for medical staff credentialing at the Hospitals, review and make recommendations regarding the quality assurance program at the Hospitals, and assist in issues relating to accreditation for the Hospitals.

ECHN agrees to maintain an indemnity reserve in the amount of $4,500,000 for a period of three years after the closing date so that PMH will have meaningful recourse against ECHN for any potential indemnification claims. If certain claims arise during this three year period, the indemnification reserve may be extended, but not beyond the fifth anniversary of the closing date. The indemnification obligations of PMH's subsidiary buyer to ECHN are guaranteed by PMH.

E. The Charitable Assets of ECHN

Throughout its history, ECHN has received numerous charitable gifts, legacies and devises from generous individual donors and community fundraising efforts.[9] These gifts were given to one of four entities: Manchester Memorial Hospital, Rockville General Hospital, the ECHN Community HealthCare Foundation, Inc. (the "ECHN Foundation"), and ECHN Eldercare Services, Inc. As part of its Application, ECHN provided information and documentation of the charitable trusts and gifts of which its hospitals are the beneficiary or in which its hospitals claim an interest. Specifically, it provided copies of the gift documents themselves (Exhibit Q11-2 of the Application) and a spreadsheet (the "Gift Document Analysis"; Exhibit Q11-1 of the Application) that included a narrative description of each charitable gift, succession language where applicable, the name of the trustee of each gift, and a designation of whether each gift was an endowment and

[9] Manchester Memorial Hospital, Rockville General Hospital, the ECHN Community HealthCare Foundation, Inc., and ECHN Eldercare Services, Inc., hold all of ECHN's charitable funds. For the sake of our discussion, we will refer generally to funds as being held by ECHN.

restricted as to purpose. The value of all the charitable gifts as of March 30, 2016, was $23,116,006.

The OAG reviewed the Gift Analysis provided by ECHN for accuracy and completeness. In addition, the OAG questioned ECHN on the due diligence undertaken to identify all of the underlying gift documents for the charitable funds. The OAG is satisfied that ECHN has identified all the charitable funds in its possession and has met its burden to produce the underlying gift documents for each fund.

1. Manchester Memorial Hospital

We first catalog the charitable funds held by MMH.

a. MMH Unrestricted Endowments

Unrestricted endowments are charitable funds, the original gift instrument of which specifies that the sum donated is to be held and preserved as “principal,” as a “fund,” as an “endowment,” or directs that the sum be held and invested, or added to an existing endowment fund, and further specifies that the annual income earned on said principal be applied to the general purposes of the hospital.

The following gifts are unrestricted endowments held by MMH:[10] Blish (11-1.1), Carpenter (11-1.2), Chapman (11-1.3), Coates (11-1.4), Dart (11-1.5), House (11-1.6), Porter (11-1.7), Rice (11-1.8), Stanley (11-1.9), Strant (11-1.10), Strickland (11-1.11), Ellis (11-1.12), Pinney (11-1.13), Hohenthal (11-1.14), Cheney (11-1.15), Campbell Cheney (11-1.16), Dewey (Albert) (11-1.17), Dewey (Jane) (11-1.18), Gardner (11-1.19), Piper 1 (11-1.20), and Piper 2 (11-1.21). As of March 31, 2016, the total value of these restricted endowments was

[10]The numbers following the gifts represent the fund number as identified in the Application, Exhibit Q11-1.

$8,558,001.

b. MMH Endowments Restricted to Purpose

Endowments Restricted to Purpose are charitable funds, the original gift instrument of which specifies that the sum donated is to be held and preserved as "principal," as a "fund," as an "endowment," or directs that the sum be held and invested, but the purposes to which the income may be put are restricted and cannot be applied to the general purposes of the hospital. One of the most common restrictions on hospital gifts directs the funds to be used for free bed care, i.e., to use the funds on behalf of persons unable to pay for the hospital services provided (a "Bed Fund"). MMH holds six Bed Funds: Drake (11-1.22), Hills Preston (11-1.23), Boynton (11-1.24), Loomis (11-1.25), Cheney Disher (11-1.26), and Keeney (11-1.27). MMH's Bed Funds are valued at $541,728 as of March 31, 2016. MMH holds two additional endowments restricted to purpose: Trotter (11-1.28) (for the benefit of children patients) and Wright (11-1.29) (for the benefit of the fight against cancer). The Trotter and Wright funds have a total value of $6,629 as of March 31, 2016.

c. MMH Miscellaneous Funds

MMH has interests in two additional funds: Damato (11-1.30) and a life insurance policy (11-1.31). The Damato estate is an unrestricted gift, with an undetermined value at this time. The date of final distribution is unclear at this time due to the complexity of liquidating the assets in the estate, particularly the real estate assets.

The current value of the life insurance policy is $58,147.

The total value of gifts held by MMH as of March 31, 2016, is $9,164,514.

2. Rockville General Hospital

a. RGH Unrestricted Endowments

The following gifts are unrestricted endowments held by RGH: Bissell (11-1.32), Maxwell (11-1.33), Goodale and Risley (11-1.34), United German Society (11-1.35), Prescott (11-1.36), Maxwell (11-1.37), Smith (11-1.38), Doss (11-1.39), Wood (11-1.40), Henry (Maud) (11-1.41), Henry (Lenore) (11-1.42), Charter (11-1.43), Bilson (11-1.44), Belding (11-1.45), Bradley (11-1.46), Britton (11-1.47), Sprague (11-1.48), Doane (11-1.49), Keney (11-1.50), American Red Cross (11-1.51), Talcott (11-1.52), Maxwell (11-1.53), Metcalf (11-1.54), and Henry (11-1.55), As of March 31, 2016, the total value of these unrestricted endowments was $8,989,027.

b. RGH Endowments Restricted to Purpose

RGH holds eight Bed Funds: DAR (11-1.56), Prescott (11-1.57), Phelps (11-1.58), Winchell-Foster (11-1.59), Tucker (11-1.60), Whitlock (11-1.61), Sykes Phelps (11-1.62), and Kress (11-1.63). RGH's Bed Funds are valued at $288,358 as of March 31, 2016. MMH holds two additional endowments restricted to purpose: Baker Family (11-1.64) (for the upkeep and physical maintenance of the Hospital) and Schortmann (11-1.65) (for the operation or improvement of the maternity and nursery facilities of the Hospital). The Baker Family and Schortmann funds have a total value of $278,769 as of March 31, 2016.

c. RGH Miscellaneous Funds

RGH has interests in two charitable gift annuities, but one of the two joint annuitants has now lived beyond the projected life expectancy. The annuities are now contractual liabilities of the Hospital, and ECHN is looking to terminate these arrangements at fair value. Names of the original grantors have been withheld. (11-1.77 and 11-1.78).

The total value of gifts held by RGH as of March 31, 2016, is $12,374,200.

3. ECHN Community Healthcare Foundations, Inc.

a. Endowments

The ECHN Foundation holds several funds for the benefit of MMH and RGH. With respect to MMH, the ECHN Foundation holds the following unrestricted endowments: Burgess (11-1.79), St. Laurent (11-1.80), and Piper (11-1.81). The total value of these three gifts as of March 31, 2016 is $1,285,023. With respect to RGH, the ECHN Foundation holds the follow endowments with restricted purposes: Maxwell (11-1.82) (for the benefit of the normal maintenance and repair of the Maxwell Home and its grounds) and Risley Scholarship (11-1.83) (for the benefit of nurses' continuing education). The total value of these two funds as of March 31, 2016, is $282,289. The total value of funds held by the ECHN Foundation is $1,567,312.

b. Special Purpose Funds

The ECHN Foundation holds a dozen funds that are fully expendable but have restricted purposes. If ECHN does not deplete these funds for their intended purpose prior to the closing, they will remain with Legacy ECHN to be transferred to the New Foundation or another charitable organization to fulfill the fund's intended charitable purpose. The special funds are as follows: Avis Lloyd Tree of Life (11-2.1), Team Towanda (11-2.2), Employee Care (11-2.3), Breast and Cervical Cancer (11-2.4), Adult Ambulatory Administrative Education and Development (11-2.5), Purcell Golf Classic Trophies (11-2.6), Woodlake at Tolland Wishes Program (11-2.7), Van (11-2.8), Risley (11-2.9), Fields (11-2.10), and Woodlake: Resident Council (11-2.11). The total value of the special funds held by the ECHN Foundation is $9,979.

4. Trusts Held by Outside Trustees

All the charitable funds identified above are held and administered by ECHN.

There is a series of charitable gift funds, however, that are not held by ECHN but by outside trustees and for which ECHN holds the beneficial interest.

a. For the Benefit of MMH

There are seven funds held by outside trustees for the benefit of MMH: Barton (11-3.1), Clark (11-3.2), Morton (11-3.3), Robertson (11-3.4), Crowell (11-3.5), Ferguson (11-3.6), and Rogers (11-3.7).

b. For the Benefit of RGH

There are three funds held by outside trustees for the benefit of GWH: Dillon (11-3.8), Moxon (11-3.9), and Barton (11-3.10).

The market value of the corpus of the trusts held by outside trustees for the benefit of ECHN was $10,903,971 on March 31, 2016.

V. LEGAL ANALYSIS AND REQUIRED MODIFICATIONS

Conn. Gen. Stat. § 19a-486a *et seq*. directs that any nonprofit hospital that enters into an agreement to transfer a material amount of its assets or operations with an entity operated for profit must first obtain the approval of OHCA and the OAG. Any agreement made without these approvals is deemed void.

Conn. Gen. Stat. § 19a-486c mandates that the Attorney General shall disapprove a proposed sale of a nonprofit hospital to a for-profit entity as not in the public interest if he determines that one or more of nine conditions exist.[11] The Conversion Act, however, allows the Attorney General to approve an application while setting forth modifications and/or conditions that would bring the proposed transaction into compliance with the conditions in § 19a-486c. What follows, therefore, is the OAG's analysis and discussion of

[11] See footnote 1.

the statutory criteria in § 19a-486c and the modifications and conditions to the Asset Purchase Agreement that are necessary to satisfy those criteria.

A. The transaction is not prohibited by Connecticut statutory or common law governing nonprofit entities, trusts or charities.

Pursuant to Conn. Gen. Stat. § 19a-486c(a)(1), the Attorney General shall disapprove a proposed agreement if he determines that the transaction is prohibited by Connecticut statutory or common law governing nonprofit entities, trusts, or charities. Subject to the modifications and conditions set forth in Section II(D) of this decision, we conclude that the Asset Purchase is not prohibited by statutory or common law governing nonprofit entities, trusts, or charities.

B. ECHN exercised due diligence.

Pursuant to Conn. Gen. Stat. § 19a-486c(a)(2), the Attorney General is required to determine whether the nonprofit hospital exercised due diligence in four distinct areas. The phrase "due diligence" is not defined by the Conversion Act, but Black's Law Dictionary (6th ed. 1990) defines it as: "Such a measure of prudence, activity, or assiduity, as is properly to be expected from, and ordinarily exercised by, a reasonable and prudent man under the particular circumstances; not measured by any absolute standard, but depending on the relative facts of the special case." In short, therefore, we review the level of care and prudence that the ECHN Board exercised in deciding to enter into the APA with PMH.

Based upon our and our expert's review of the materials presented as a part of the ECHN and PMH Application and the testimony given at the public hearings, it is clear that ECHN undertook an extensive and diligent process to explore strategic options and to identify a capital alternative that would enable it to address its difficult financial position. ECHN has faithfully pursued its mission to ensure quality healthcare for the Manchester and Rockville communities. As noted in the findings of fact, ECHN's efforts began in 2011 with the establishment of the Partnering Workgroup and the hiring of Chartis. Every step that followed in ECHN's pursuit of a capital partner was reviewed by a Transaction Committee, the Board of ECHN, and for significant issues, the ECHN Corporators. ECHN pursued discussions with multiple strategic partners, evaluated a range of transaction structures, and explored multiple strategies to access capital. Our specific due diligence findings follow.

1. ECHN exercised due diligence in deciding to participate in the APA.

Pursuant to Conn. Gen. Stat. § 19a-486c(a)(2)(A), the Attorney General shall disapprove a proposed agreement if he determines that the nonprofit hospital failed to exercise due diligence in deciding to transfer its assets. The record reveals a compelling case for ECHN to transfer substantially all of its assets as a means to assure the long-term viability of MMH and RGH.

ECHN engaged in a decision-making process that was reasonable, thoughtful, and thorough. In short, its ultimate decision to transfer substantially all of its assets to PMH demonstrated due diligence under the circumstances. As noted in the findings of fact, ECHN pursued a range of strategic initiatives to address the hospital's financial constraints, aging facilities, and limited access to capital. Without a feasible alternative available, the ECHN Board reasonably concluded that the sale of its assets to another hospital system was an appropriate solution for long-term viability of the hospitals. We, therefore, conclude that ECHN exercised due diligence in deciding to transfer substantially all of its assets as a part of the APA.

2. ECHN exercised due diligence in selecting PMH for the Asset Purchase.

Pursuant to Conn. Gen. Stat. § 19a-486c(a)(2)(B), the Attorney General shall disapprove a proposed agreement if he determines that the nonprofit hospital failed to exercise due diligence in selecting the purchaser. Based on the record in this case, ECHN has established that it exercised due diligence in selecting PMH to purchase substantially all of its assets.

The full history of ECHN's search for a capital partner is described in detail in the findings of fact. With respect to the initiative that resulted in the APA with PMH, however, we conclude that ECHN took appropriate and considered steps to identify the best situation for MMH and RGH. ECHN conducted a second RFP process with the guidance of Chartis, delivering the RFP to six potential partners, including PMH. By mid-March in 2015, ECHN had received three proposals. The Transaction Committee reviewed the proposals and evaluated each in light of the selection criteria approved by the Board, including quality of care. The Transaction Committee then performed its due diligence with respect to the potential partners, reviewing financial, quality, and corporate compliance data for each of the potential partners. With respect to PMH, members of the Transaction Committee visited PMH's California and Rhode Island operations.

On June 22, 2015, the Transaction Committee voted unanimously to recommend acceptance of the PMH proposal. On June 25, 2015, the Board held a retreat during which it considered the proposals received from the potential partners, ultimately voting in favor of the PMH proposal. The draft APA was then sent to ECHN's Corporators for their review, who approved entering the transaction in overwhelming numbers.

On or about the beginning of February 2016, after the hospital conversion application process had begun with the OAG and OHCA, ECHN learned that recent

Medicare and Medicaid surveys at two of PMH's California hospitals (Los Angeles Community Hospital and Southern California Hospital at Culver City) had resulted in findings of Immediate Jeopardy by regulatory authorities at both hospitals. After learning about these determinations, ECHN appointed a Quality Evaluation Team that looked into the Immediate Jeopardy findings to determine whether the findings were sufficiently substantial to call into question PMH's fitness as a transaction partner. After a thorough investigation, the Quality Evaluation Team determined that "the recent compliance issues present isolated challenges that [PMH] has demonstrated a strong commitment to remediate through corrective actions that are already in progress." (Testimony of Joy Durin, Vice Chair, Board of Trustees, Chair, Transaction Committee, p. 3350.) This conclusion was shared with the Transaction Committee, approved by them, sent to the Board, and the board approved the recommendation. In addition to the investigation performed by the Quality Evaluation Team, ECHN negotiated a Quality Assurance Commitment with PMH that requires PMH to maintain ECHN's quality programs for at least two years following the closing of the transaction. In addition, it requires PMH to maintain quality assurance and performance improvement programs that are consistent with industry best practices and quality improvement programs as currently implemented in PMH's Rhode Island facilities. Based on the evidence presented to the OAG, we conclude that ECHN exercised due diligence in selecting PMH as its partner for the APA and in confirming that selection after PMH's Immediate Jeopardy findings came to light.

3. ECHN exercised due diligence in obtaining a fairness evaluation.

Pursuant to Conn. Gen. Stat. § 19a-486c(a)(2)(C), the Attorney General shall disapprove a proposed agreement if he determines that the nonprofit hospital failed to exercise due diligence in obtaining a fairness evaluation from an independent person expert in such agreements.

ECHN's fairness evaluation was conducted by Duff & Phelps, LLC ("Duff & Phelps"), who had no previous material relationship with any party to the transaction, except for having previously provided an independent fairness opinion regarding the proposed ECHN/Tenet transaction. In addition, no portion of Duff & Phelps fee was contingent on the conclusion expressed in the fairness opinion or on the successful consummation of the transaction.

Therefore, we conclude that the ECHN Board exercised due diligence in obtaining a fairness evaluation regarding the terms of the proposed APA from an independent entity expert in such agreements.

4. ECHN exercised due diligence in negotiating the terms and conditions of the APA.

Pursuant to Conn. Gen. Stat. § 19a-486c(a)(2)(D), the Attorney General shall disapprove a proposed agreement if he determines that the nonprofit hospital failed to exercise due diligence in negotiating the terms and conditions of the transfer.

Our review of the transaction leads us to conclude that ECHN exercised due diligence in negotiating most of the terms and conditions of the APA. As discussed below, we believe ECHN will receive at least the fair market value for its assets. In addition, ECHN negotiated a capital commitment of $75 million for the for-profit ECHN hospital system ("PMH/ECHN") over the next five years. Other highlights include PMH's retention of ECHN employees, the assumption by PMH of the unfunded pension liabilities, the formation of local advisory boards for each hospital, and PMH's commitment to maintain ECHN's current policies regarding charity care, indigent care, and community benefits.

One provision in the APA, however, stands out as unreasonable in light of the details of the transaction as a whole. Section 5.18 of the APA concerns PMH's $75 million capital commitment, and subsection (b) of this section provides as follows:

> *Notwithstanding the above capital commitment, in the event that any Legal Requirement is enacted or imposed by the State of Connecticut after Closing that discriminates against, or adversely affects a disproportionate number of for-profit hospitals and causes the Hospital Businesses to suffer a decline in EBITDA of more than ten (10) percent in any year, on a consolidated basis, then, Buyer may defer in its discretion the above capital commitment beyond the five-year period provided in Section 5.18(a) but only to the extent of the decline in EBITDA resulting from the discriminatory Legal Requirement. To the extent Buyer desires to defer the capital commitment as a result of a discriminatory Legal Requirement, (i) Buyer shall make available to the public reasonably detailed information to support Buyer's position (provided that in no event shall Buyer be required to disclose any information that is subject to a confidentiality or other similar arrangement) and (ii) Buyer shall consult with the Local Board to determine an alternate mutually agreeable timeframe to complete the capital commitment that is reasonable and appropriate in light of the changed circumstances caused by the new Legal Requirement.*

(Exhibit Q3-2, Asset Purchase Agreement, p. 182.)

Although PMH may wish to hedge against future changes in the legal landscape, it cannot hold the ECHN capital investment hostage by such a provision. To do so would render the $75 million capital commitment – a key term of the deal – subject to delay upon the future actions of legislators. Put differently, we believe that PMH must bear the risk of future legislation and not PMH/ECHN. The $75 million capital commitment is indeed a commitment, and the deadline by which it must be spent must be honored. Accordingly, as a condition to approval of the proposed transaction, the OAG requires that the Applicants modify the APA by ~~deleting~~ revising the language currently in section 5.18(b) ~~from the APA~~to limit any deferral to no more than ten (10) years after closing.

C. ECHN Disclosed Any and All Board Member, Officer, Key Employee, and Expert Conflicts of Interest With Respect to the APA.

Pursuant to Conn. Gen. Stat. § 19a-486c(a)(3), the Attorney General shall disapprove the proposed transaction as not in the public interest if he determines that the nonprofit hospital failed to disclose any conflict of interest, including but not limited to, conflicts of interest pertaining to board members, officers, key employees, or experts of ECHN, the purchaser, or any other party to the transaction.

The Applicants provided the OAG with individual conflict of interest statements for each relevant individual (board member, officer, etc.) employed by ECHN, its experts, and PMH. Each individual was required to respond to individual questions regarding possible financial, beneficial, and/or employment related conflicts of interest. If any of the questions were answered with anything other than an unqualified "No," the individual was required to attach an explanation to the statement. These statements were reviewed by the OAG and Navigant.

Section 5.03 of the APA requires PMH "to employ as of the Closing Date substantially all employees of Seller and its Affiliates who work at the Hospital Businesses." (Exhibit Q3-2, Asset Purchase Agreement, p. 171.) Therefore, employees of ECHN, including ECHN's officers and key employees, have been offered employment with PMH as a part of the transaction. This general provision, however, does not create a conflict of interest for the purposes of this statutory element.

After a careful review of all the conflict of interest responses, there do not appear to be any conflicts of interest with this proposed transaction that exist outside of the APA itself. In addition, no intervenor or other participant in the proceeding has offered any credible evidence that any conflict existed at any time during the negotiation of the APA.

Accordingly, we conclude that no conflicts of interest exist that would require disapproval of the APA.[12]

D. ECHN will receive fair market value for its assets.

Pursuant to Conn. Gen. Stat. § 19a-486c(a)(4), the Attorney General shall disapprove the proposed transaction as not in the public interest if he determines that the nonprofit hospital will not receive fair market value for its assets. For purposes of the Conversion Act, "fair market value" is defined as

> the most likely price that the assets would bring in a sale in a competitive and open market under all conditions requisite to a fair sale, with the buyer and seller each acting prudently, knowledgeably and in their own best interest, and with a reasonable time being allowed for exposure in the open market.

Conn. Gen. Stat. § 19a-486c(a)(4).

PMH has agreed to pay $105 million as compensation for substantially all of ECHN's assets. Two independent financial experts have reviewed the transaction to determine whether ECHN will receive fair market value for its assets, and both have concluded that the purchase price of $105 million equals or exceeds the fair market value of ECHN's assets.

As discussed above, ECHN retained Duff & Phelps to provide it with an independent valuation and fairness opinion regarding the transaction.[13] Duff and Phelps considered three principal methods of valuation: discounted cash flow, guideline company, and M&A

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[12] ECHN's process to ensure that no individual with a conflict of interest voted on this transaction was very thorough. Indeed, ECHN created a Conflict of Interest Task Force specifically for this purpose. The Board voted on all transaction-related resolutions pursuant to a two-step process to help ensure that any personal interest in any of the transaction decisions made would be eliminated.

[13] The OAG has previously concluded that ECHN exercised due diligence in selecting Duff & Phelps to perform the independent fairness evaluation on its behalf.

transaction. These approaches indicated that the fair market value of ECHN was well below the price PMH had agreed to pay for substantially all of the assets of ECHN. Duff & Phelps's mid-point estimate for ECHN, without the joint ventures, was $57.1 million. Duff & Phelps used a market and a capitalized cash flow approach to estimate the value of ECHN's joint ventures as $13.1 million. The total estimated fair market value for ECHN as determined by Duff & Phelps, therefore, is $70.2 million. As such, Duff and Phelps was able conclude in its fairness opinion that "the consideration to be received by [ECHN] in the Proposed Transaction is fair from a financial point of view to the Company." (Exhibit Q7-4, Duff & Phelps' Fairness Opinion Letter, p. 836.)

Navigant was hired though an RFP process to be the OAG's financial expert for the purposes of reviewing this transaction. Navigant has also concluded that ECHN will receive fair market value for the transfer of its assets.[14] In performing its fair market value analysis, Navigant considered the three generally accepted approaches to value: income, market, and cost. Navigant valued ECHN's assets as value-in-continued use, as part of a going concern. Based upon these valuation methods, Navigant estimated the total fair market value of ECHN, including the joint ventures, to be $63,750,000. Navigant's analysis supports the conclusion that ECHN will receive fair market value for the transfer of its assets.

Based on the independent financial assessments of two respected hospital valuation firms, and the lack of evidence to the contrary in the record, we conclude that ECHN will receive fair market value for its assets.

[14] Navigant's report is attached hereto as Exhibit A.

E. The fair market value of the assets has not been manipulated by any person in a manner that causes the value of the assets to decrease.

Pursuant to Conn. Gen. Stat. § 19a-486c(a)(5), the Attorney General shall disapprove the proposed transaction as not in the public interest if he determines that the fair market value of the nonprofit hospital's assets has been manipulated by any person in a manner that causes the value of the assets to decrease.

Navigant performed reviews of ECHN's financials and assets and found no indication that the fair market value of ECHN's assets had been manipulated. No intervenor or other participant in the proceeding has offered any evidence that the fair market value of ECHN's assets has been manipulated to artificially lower the payment price. Based on these factors, we conclude that the fair market value of ECHN's assets has not been manipulated.

F. The financing of the transaction will not place ECHN's assets at an unreasonable risk.

Pursuant to Conn. Gen. Stat. § 19a-486c(a)(6), the Attorney General shall disapprove the proposed transaction as not in the public interest if he determines that the financing of the transaction by the nonprofit hospital will place the nonprofit hospital's assets at an unreasonable risk. Consistent with the OAG's interpretation of this provision in *Sharon*, we interpret this statutory provision to require our examination of the proposed financing of the transaction to ensure that the APA does not "burden the for-profit entity with so much debt that the transferred assets of the former nonprofit hospital, albeit now operated for profit, will be placed at an unreasonable financial risk of closure or bankruptcy—an event that would result in a loss of healthcare for the affected community." *In re Sharon Hospital*, Docket No. 01-486-01, p. 64 (2001).

Based upon the record, we conclude that the financing of this transaction will not place ECHN's assets at risk. PMH confirmed on the record that the $105 million purchase price for ECHN's assets will be financed with operating cash from PMH. More specifically, PMH represented that it has the financial capacity to provide the necessary capital to purchases ECHN's assets without transaction-specific financing arrangements. After its review of the transaction, Navigant concluded that PMH will not incur any debt financing to consummate the transaction, and so, ECHN's assets would not be put at an unreasonable risk.

As such, we conclude that the assets of ECHN will not be placed at an unreasonable risk due to the financing of the transaction.

G. The management contract contemplated under the transaction is for reasonable fair value.

Pursuant to Conn. Gen. Stat. § 19a-486c(a)(7), the Attorney General shall disapprove the proposed transaction as not in the public interest if he determines that any management contract contemplated under the transaction is not for reasonable fair value. No management contract is contemplated under the APA. Accordingly, we conclude that this element of the analysis has been met.

H. Assuming compliance with the modifications imposed below, a sum equal to the fair market value of ECHN's assets is being transferred to the New Foundation to provide only for charitable health care services in the affected community.

Pursuant to Conn. Gen. Stat. § 19a-486c(a)(8), the Attorney General shall disapprove the proposed transaction as not in the public interest if he determines that:

> a sum equal to the fair market value of the nonprofit hospital's assets (A) is not being transferred to one or more persons to be selected by the Superior Court who are not affiliated through corporate structure, governance or membership with either the nonprofit hospital or the purchaser, unless the nonprofit hospital continues to operate on a nonprofit basis after the transaction and such sum is

> transferred to the nonprofit hospital to provide health care services, and (B) is not being used for one of the following purposes: (i) For appropriate charitable health care purposes consistent with the nonprofit hospital's original purpose, (ii) for the support and promotion of health care generally in the affected community, or (iii) with respect to any assets held by the nonprofit hospital that are subject to a use restriction imposed by a donor, for a purpose consistent with the intent of said donor.

This provision in the Conversion Act advances the important policy that the value of the nonprofit hospital be preserved for charitable healthcare purposes in the service area that the nonprofit hospital previously served. In addition, it restates the OAG's statutory responsibility to protect the public interest in the protection of gifts made for charitable or public purposes codified at Conn. Gen. Stat. § 3-125.

The language of Conn. Gen. Stat. § 19a-486c(a)(8) requires the OAG to assess several different issues in connection with the APA. We must first analyze, determine, and approve a value that is the "sum equal to the fair market value of the nonprofit hospital's assets." Second, we must analyze the nature and purpose of the entity to which that sum is being transferred. Third, we must determine and require that the transferred sum is used only for the statutorily identified charitable purposes. Last, we are required to inventory all gift documents and restricted charitable assets currently held by ECHN and identify any approximation and/or equitable deviation needs in connection with these assets.

1. *A Sum Equal to the Fair Market Value of ECHN is Being Transferred to the New Foundation.*

The term "fair market value" is used in several places in subsection (a) of § 19a-486c. As discussed in the OAG's *Sharon* decision, and more fully below, fair market value has two distinct meanings depending on which section of the Conversion Act the term is used.

Subsection (4) of § 19a-486c requires us to ensure that the nonprofit hospital receives fair market value for its assets. As discussed earlier, subsection (4) defines "fair market value" as the likely price that the assets would bring in a sale in a competitive and open market. Subsection (4) is looking for the gross asset value.

If fair market value were computed for purposes of subsection (8) as it is for subsection (4), though, the nonprofit hospital might be left transferring to a conversion foundation the proceeds of its sale, but leaving the nonprofit hospital no ability to pay off its liabilities post-closing with some portion of those proceeds. Such a result is nonsensical, because a primary goal of a nonprofit hospital's sale of assets is the extinguishment of corporate liabilities. For example, in the case of ECHN, its long-term bond debt will be paid off with proceeds from the sale of its assets.

The definition we use for fair market value for purposes of subsection (8), therefore, is more appropriately the price paid for the nonprofit hospital's asset minus the amount of its debt obligations and other liabilities that it will resolve using the proceeds of the proposed transaction. In other words, fair market value equals the net proceeds of the nonprofit hospital. *In re Sharon Hospital*, OAG Docket No. 01-486-01, p. 69 (2001). With respect to ECHN, the net asset value calculation must take into account all retained assets and liabilities, including, for example, cash, accounts receivable, any adjustment to the net working capital figure, its long-term debt, workers' compensation and medical malpractice liability relating to events occurring prior to closing, and any payor liabilities and obligations from reporting periods prior to closing.

Late Filed Exhibit 8 (App., p. 4261) sets forth the most current numbers on what proceeds will remain after netted with ECHN's liabilities. In short, this exhibit projects that nothing will remain after ECHN pays off its liabilities. In fact, it appears that ECHN will not even have sufficient assets to fund the indemnity reserve or to fully pay for its liabilities in excess of $77 million (the excess liability is currently tallied at $7,924,000), both obligations of ECHN. Given these numbers, we conclude that the sum that is equal to the fair market value of ECHN is currently zero.

However, the post-transaction nonprofit ECHN, Legacy ECHN, may receive funds after the close. For example, Legacy ECHN may receive reimbursements due from Medicare and Medicaid for the years prior to the closing. Also, Legacy ECHN will receive income from the unrestricted endowments during the time period between the close of the transaction and the Superior Court order that will transfer all charitable assets from Legacy ECHN to the New Foundation. Moreover, Legacy ECHN, including Legacy MMH and Legacy RGH, may receive charitable distributions from pending estates, i.e., the Damato estate. This income will initially be used to pay off ECHN's liabilities and to fund the indemnity reserve, both obligations of ECHN.[15] After these obligations are paid or funded, however, any funds remaining would constitute net proceeds.

Because the final net proceeds value of the nonprofit hospital cannot be precisely identified prior to the actual closing of the transaction, the determination of a sum equal to the fair market value for the purposes of subsection (8) must await a post-closing accounting. Accordingly, as soon as reasonably possible after the Applicants have agreed to a Final Closing Statement of the asset purchase, the Applicants must provide the OAG a final accounting of the transaction that sets forth the balance sheets of ECHN immediately prior to, and Legacy ECHN immediately after, the closing and that provides a net proceeds analysis, substantially similar to Late Filed Exhibit 8 with explanations of any changes to the figures. This requirement is a condition of approval for the proposed transaction.

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[15] Legacy ECHN could also use these funds to finance wind-down costs, but Exhibit 8 already includes a line item for "Post-closing Pool 'Wind Down' Funds." Regardless, Wind Down costs are an appropriate expense for Legacy ECHN.

Additionally, because Legacy ECHN will receive income post-closing that may constitute net proceeds, Legacy ECHN shall, as a condition to the OAG's approval of the transaction, report quarterly to the OAG regarding (1) any and all income received by Legacy ECHN post close, including, but not limited to, Medicare and Medicaid reimbursements, income from charitable assets held by Legacy ECHN prior to transfer to the New Foundation, and any additional charitable funds received, and (2) all expenditures for Legacy ECHN.

Last, if the transaction ultimately produces net proceeds, that amount will be transferred to the New Foundation for use consistent with the charitable purpose of the New Foundation.

2. The Nature of the Conversion Foundation Complies with the Conversion Act.

The Conversion Act requires that the net asset value of the nonprofit hospital be transferred to "one or more persons to be selected by the Superior Court who are not affiliated through corporate structure, governance or membership with either the nonprofit hospital or the purchaser, unless the nonprofit hospital continues to operate on a nonprofit basis after the transaction and such sum is transferred to the nonprofit hospital to provide health care services." Conn. Gen. Stat. § 19a-486c(8)(A). This provision prohibits improper affiliation with the new for-profit hospital.

ECHN has submitted a draft certificate of incorporation ("COI") and draft bylaws for the New Foundation. By these submissions, ECHN is proposing to create an "independent conversion foundation." This particular type of foundation is completely independent from both the nonprofit hospital and the for-profit purchaser and must be approved by the Superior Court. There can be no affiliation by corporate structure, governance, or membership.

The draft documents comply with the requirements of the statute. The New Foundation will have no corporate relationship with PMH/ECHN, and the governing members of the New Foundation will not contemporaneously serve in any governing position at PMH/ECHN or at any of its affiliates. In addition, any individual who serves as member of a governing board at PMH/ECHN must wait two years before serving on the governing board of the New Foundation. (Exhibit Q10-2, New Foundation Bylaws (Draft), pp. 917-18.) The New Foundation meets the affiliation requirements of § 19a-486c(8)(A).

The New Foundation will also be operated for the proper purposes, as set forth in the Conversion Act. Section 19a-486c(a)(8)(B) provides that the New Foundation must be operated:

> (i) For appropriate charitable health care purposes consistent with the nonprofit hospital's original purpose, (ii) for the support and promotion of health care generally in the affected community, or (iii) with respect to any assets held by the nonprofit hospital that are subject to a use restriction imposed by a donor, for a purpose consistent with the intent of said donor . . . ."

§ 19a-486c(a)(8)(B).

In its draft COI, the New Foundation lists it purposes as follows:

> (a) To maintain and improve the health of the residents of the area historically served by Eastern Connecticut Health Network, Inc., Manchester Memorial Hospital, Inc., and Rockville General Hospital, Inc., specifically, the nineteen communities of Manchester, Vernon (including Rockville), Andover, Ashford, Bolton, Columbia, Coventry, East Hartford, East Windsor, Ellington, Glastonbury, Hebron, Mansfield, Somers, South Windsor, Stafford, Tolland, Union, and Willington (the "Communities");
>
> (b) To support or conduct community health needs assessments and encourage and support efforts to improve the health of the Communities, including the poor, the elderly, the disabled, children, and other underserved and at-risk populations;
>
> (c) To support and engage in community projects, activities, and programs that will improve access to care and enhance the health of

> residents, including, but not limited to, preventative health programs and health education;
>
> (d) To solicit and accept additional funds to support the Corporation's purposes, and to make grants and provide financial and other support to other non-profit organizations engaged in activities that further the Corporation's purposes;
>
> (e) To support and promote the education and training of medical professionals and providers in the area;
>
> (f) To work cooperatively with Prospect Medical Holdings, Inc. ("PMH") to ensure and augment a network of affordable and accessible health and medical care in the region; provided, however, that the Corporation will not support programs operated by or for the direct benefit of PMH while it operates as a for profit entity; and
>
> (g) To engage in any lawful act or activity for which a corporation may be organized under the Revised Nonstock Corporation Act of the State of Connecticut in furtherance of the foregoing.

(Exhibit Q10-1, Certificate of Incorporation (Draft), pp. 911-12.) These purposes are consistent with the requirements in the Conversion Act.

3. *The Transferred Sum Will Be Used Only for the Statutorily Identified Charitable Purposes.*

ECHN currently predicts that it will have no net proceeds to transfer to the New Foundation after the closing. Should a subsequent accounting of the transaction reveal net proceeds, however, we must ensure that they will forever be used for their proper charitable purpose. The draft COI established the proper charitable purposes, but the primary mechanism to ensure that they will be used as such forever is the requirement that the New Foundation Board receive the consent of the Attorney General for the amendment of specific sections of the COI, specifically, paragraphs 2, 5, 8, and 14. In this way, the purposes of the New Foundation (paragraph 2 of the COI) cannot change unless the Attorney General agrees. Accordingly, as a condition to the Attorney General's approval of the Application, the New Foundation must include paragraph 14 in the draft COI in the final COI of the New Foundation, requiring Attorney General approval for changes to paragraphs 2, 5, 8, and 14 of the Certificate of Incorporation.

4. Description and Quantification of the Nonprofit Hospital's Charitable Assets to be Held by the New Foundation

Our final area of concern is to ensure that the charitable assets of ECHN, which have been held in trust for the public, are safeguarded and used for the promotion of healthcare in the area served by ECHN after the sale of its assets to PMH. We must also ensure that any restrictions contained in these charitable gifts and trusts are protected.

a. Purpose of Attorney General's Review of Charitable Gifts

A full analysis and review of ECHN's charitable gifts and trusts at this time is essential for several reasons. First, it permits us to fulfill our statutory obligation to ensure that all of ECHN's charitable gifts and trusts are used for a purpose consistent with the intent of the donor. In other words, this review ensures that ECHN's analysis and treatment of charitable funds in the Application correctly interprets the donors' charitable use restrictions. Second, it ensures that, with respect to the charitable gifts, no aspect of the transaction is "prohibited by Connecticut statutory or common law governing nonprofit entities, trusts or charities." Conn. Gen. Stat. § 19a-486c(a)(1). Finally, it provides subsequent holders of the funds, i.e., the New Foundation, with accurate information about whether and how the gifts are restricted under Connecticut law so that it can administer them in accordance with donor restrictions, charities law, the terms of the contractual agreements, and modifications required in this decision.

b. Documents Reviewed and Legal Standards

As part of the Application, ECHN provided a review and analysis of its charitable gifts and endowments. (Exhibit Q11-1, Detail on Specific Funds, p. 927-976.) ECHN was required to provide copies of the gift instruments (including wills, inter vivos trust agreements, and documentation of inter vivos gifts), to document the current values of the funds, and to describe the donor's restrictions or directives reflecting how the gift was to be used by ECHN. The purpose of the OAG's request was to obtain the information necessary to: (1) review the gift instrument for each of ECHN's gifts to determine whether its language would permit the gift to be transferred to another nonprofit, or whether a reverter clause or gift-over provision would be triggered by the sale of assets that would require the donation to revert to a different person, and (2) determine whether the donor restricted the use of a fully expendable gift, or the income earned on an endowment fund, to a particular charitable purpose set out in the gift instrument, for example, free beds, charity care, maintenance, a building fund, or research.

The OAG reviewed each charitable gift and its supporting documentation to confirm the accuracy of ECHN's conclusions regarding the proper charitable purpose of the fund and any spending restrictions on the fund.

c. Amount Stated by Hospital in Application

ECHN has stated that as of September 30, 2015, it held $23,356,291 in charitable assets, plus an additional $19,349 in special funds. Thus, according to its figures as of that date, a total of $23,375,640 in charitable gifts, less any net appreciation appropriated by the Board for use in connection with the transaction (App., p. 55.), would be transferred to the New Foundation. In addition, the value of trusts held by third parties for the benefit of ECHN was $10,809,693 as of September 30, 2015.

We asked ECHN to update the value of the funds as of March 31, 2016, in a late filed exhibit. As of that date, it held $23,106,027 in charitable assets, plus an additional $9,979 in special funds. Thus, according to its figures as of that date, a total of $23,116,006 in charitable gifts, less any net appreciation appropriated by the Board for use in connection with the transaction, would be transferred to the New Foundation.

d. ECHN's Charitable Gifts and Trusts.

The law on approximation, or cy pres, is well-developed in Connecticut. Indeed, the OAG brought an approximation action in the *Sharon* matter to address those charitable purposes that could no longer be fulfilled due to the sale of Sharon Hospital's assets. In that case, the court set forth the standards for approximation.

> In determining the construction of a charitable trust upon the failure of its stated purpose, the court applies the common law doctrine of cy pres, or approximation to as near as possible reflect the donor's intent. When it becomes illegal or otherwise impossible to carry out the terms of a charitable trust, rather than allow it to fail, the court will apply the doctrine of cy pres or approximation in order to carry out the charitable intentions of the donor as near as possible. "The rule of cy pres is a rule for the construction of instruments in equity, by which the intention of the party is carried out *as near as may be,* when it would be impossible or illegal to give it literal effect . . . The doctrine of cy pres may be applied without the consent of the donor." (Citations omitted; emphasis in original; internal quotation marks omitted.) *Carl J. Herzog Foundation, Inc. v. University of Bridgeport, 243 Conn. 1, 10 n.8, 699 A.2d 995 (1997).*

Blumenthal v. Sharon Hosp., Inc., 2003 Conn. Super. LEXIS 1657, 11-12 (Sup. Ct. 2003).

Also relevant to the conversion of a nonprofit hospital is the law on equitable deviation, which is similar to that of approximation but concerns the administration of a gift fund and not its charitable purpose. The equitable doctrine of deviation has been applied to preserve the "dominant [charitable] purpose by modifying what is described as [a] secondary purpose, often the method or means for carrying out the dominant purpose." 8 G. Bogart, Trusts and Trustees (2d Ed. Rev.Repl.1991) § 396, p. 330. Courts use this legal doctrine to order a change in the administration of a charitable fund from one charitable entity to another. Equitable deviation will be necessary in this case to move the charitable funds from ECHN to the New Foundation or another appropriate entity.

The Attorney General's office inventoried the gift documents in Section IV(E) in the Findings of Facts. Based upon this inventory and ECHN's and our analysis of these charitable gifts, we have determined that as a condition of approval, the following actions must be taken with respect to these funds.

i. Unrestricted Endowments.

An endowment fund is defined as "an institutional fund or any part thereof not wholly expendable by the institution on a current basis under the terms of a gift instrument." Conn. Gen. Stat. § 45a-535a(2). The institution that holds an endowment fund cannot fully expend such fund, but may only appropriate so much of an endowment's funds for expenditure or accumulation as the institution determines to be prudent for the uses, benefits, purposes for which the endowment fund is established. Unless stated otherwise in a gift document, the assets in an endowment fund are donor-restricted assets until appropriated for expenditure by the institution. Conn. Gen. Stat. § 45a-535c(a).

As a condition to the OAG's approval of the Application, Legacy ECHN must present to the Superior Court, in coordination with the OAG, a petition for equitable deviation and approximation to transfer these funds to the New Foundation or another appropriate entity and to change the charitable purpose of the unrestricted endowments to the charitable purpose of the New Foundation. This condition applies to all unrestricted endowments, whether held by MMH, RGH, or the ECHN Community Healthcare Foundation, Inc.

ii. Restricted Endowments

The Conversion Act requires the recipient of the hospital's gift funds to use assets that are subject to a use restriction imposed by a donor for purposes that are consistent with the intent of the donor. Conn. Gen. Stat. § 19a-486c(a)(8)(B)(iii).

With respect to ECHN's restricted endowments, most of the charitable purposes can be fulfilled even though the funds will not be held by a hospital. For example, a free bed fund, which is used to provide charity care at a hospital, can still be used to pay for hospital bills for indigent individuals. These funds will simply need to be transferred to the New Foundation; no change in charitable purpose is needed. There are, however, several restricted endowments that will need their charitable purposes adjusted by the Superior Court as a result of the sale of ECHN's assets to a for-profit entity.

The Thomas D. Trotter Fund was given for the benefit of pediatric patients. The Julia and Percy Baker Family Memorial Fund was given for the benefit of the upkeep and physical maintenance of RGH. The Faith S. Schortman Fund was given for the benefit of the operation or improvement of the maternity or nursery facilities at RGH. These three funds must be modified so that no charitable income benefits PMH/ECHN.

Accordingly, as a condition to the OAG's approval of the Application, Legacy ECHN must, in coordination with the OAG, include the restricted endowments in the petition for equitable deviation and approximation that will be presented to the Superior Court. With respect to Trotter, Baker, and Schortman, Legacy ECHN must seek an order of approximation for each fund, in addition to one for equitable deviation, to adjust the fund's charitable purpose to one as close as possible to the donor's original charitable intent.

iii. Special Funds

ECHN has categorized eleven (11) funds as special purpose funds. Similar to restricted endowments, these funds have a specific purpose for which they are used. Unlike the restricted endowments, however, these funds can be completely used up; they are fully expendable. Therefore, to the extent that there is any money remaining in a special fund at the time the transaction closes, that fund will need to be a part of the equitable deviation and approximation action in order to transfer it and adjust its charitable purpose, if necessary.

Accordingly, as a condition to the OAG's approval of the Application, Legacy ECHN must, in coordination with the OAG, include any special fund for which any funds remain in the petition for deviation and approximation that will be presented to the Superior Court.

iv. Trust Held by Outside Trustees.

The last category of funds that the OAG must address as part of its hospital conversion review responsibilities are those charitable assets held by third parties for which ECHN holds the beneficial interest. ECHN has identified ten third party trusts for which it holds the beneficial interest.

In each of the ten cases identified by ECHN, the sale of ECHN's assets will not affect the structure of the trust, i.e., will not require the transfer of the trust to another entity. What may be necessary, however, is a switch of the charitable beneficiary and an adjustment to the trust's charitable purpose. Also important in the third-party trust analysis is whether the donors have directed that the charitable funds go elsewhere or have given the third-party trustees the power to redirect the charitable funds themselves if ECHN were to sell substantially all of its assets. If not, then the trusts must be presented to a court for legal disposition. Consultation with the third-party trustees is necessary in these cases.

Under Connecticut charities law, a gift to one charity, with language providing for a substitution or gift over to another charity upon certain conditions, has long been valid. *See Colonial Trust Co. v. Waldron*, 112 Conn. 216, 233 (1930); *Christ Church v. Trustees*, 67

Conn. 554, 565-66 (1896). When a gift contains an alternate disposition of a fund in case of the failure of the bequest, the equitable doctrine of approximation does not apply. See *Hartford National Bank & Trust Co. v. Oak Bluffs First Baptist Church*, 116 Conn. 347, 351 (1933); *First Congregational Society of Bridgeport v. City of Bridgeport*, 99 Conn. 22, 31-32 (1903); 4 Scott, Trusts (4th Ed.) § 399.2, p. 495-96; Restatement (Second), 2 Trusts § 399, comment c. "The provision for a gift over upon failure of the charity negatives the existence of a general charitable intent, just as the absence of such a provision is evidence of such a purpose." *Connecticut Bank & Trust v. Cyril and Julia C. Johnson Mem. Hosp.*, 30 Conn. Supp. 1, 8 (1972), citing Bogert, Trusts and Trustees (2d Ed.) § 437, p. 426.

Accordingly, as a condition to the OAG's approval of the Application, Legacy ECHN must, in coordination with the OAG and the third-party trustees, bring any third-party trust in need of construction or approximation before a court of competent jurisdiction for appropriate orders.

v. Miscellaneous

The Life Insurance Policy (11-1.31) for which MMH is the beneficiary shall be included in the Superior Court petition for an order of equitable deviation if the insured is still living at that time. Otherwise, the distribution of the insurance proceeds shall be included in the net proceeds of the transaction and treated as such.

ECHN's portion of the distribution in the Damato estate (and any other unrestricted gift to ECHN), if distributed prior to the Superior Court order transferring ECHN's charitable assets to the New Foundation or other charitable organization, shall be included in the net proceeds of the transaction and treated as such.

vi. Future Interests

To the extent there are future charitable interests for the benefit of ECHN, the disposition of those interests will be addressed on a case-by-case basis by a court under the doctrine of approximation. Only when a future interest becomes a present interest can a probate or superior court determine to whom the remainder will pass or whether the gift will fail and revert to the donors' heirs-at-law. Therefore, any future interests that have not yet vested cannot be included in the Superior Court action to address the identified charitable funds.

5. ECHN Must Present the New Foundation and its Restricted Charitable Funds to the Superior Court for Approval and Approximation and Deviation Orders.

Although the Attorney General has approved the purposes of the New Foundation and the other provisions in the draft COI and bylaws, ECHN will be required to present the New Foundation to the Superior Court for its approval and will need to have the court enter orders of approximation and equitable deviation to transfer the charitable assets to the New Foundation, or other eligible entity. The Office of the Attorney General shall participate in this action.

I. ECHN and PMH Have Provided The Attorney General With Information And Data Sufficient To Evaluate The Proposed Joint Venture.

Pursuant to Conn. Gen. Stat. § 19a-486c(a)(9), the Attorney General shall disapprove the proposed transaction as not in the public interest if he determines that the nonprofit hospital or the purchaser has failed to provide the Attorney General with information and data sufficient to evaluate the proposed agreement adequately, provided the Attorney General has notified the nonprofit hospital or the purchaser of the inadequacy of the information or data and has provided a reasonable opportunity to remedy such inadequacy. The Applicants have provided all relevant information and sufficient data to evaluate adequately the proposed APA.

VII. CONCLUSION

The OAG therefore concludes that the Application for an asset purchase by PMH of substantially all of the assets of ECHN is hereby approved subject to the modifications and conditions listed herein.

Date: ____________________

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PERRY ZINN ROWTHORN
DEPUTY ATTORNEY GENERAL