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November 14, 2011

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**VIA HAND DELIVERY**

Office of the Attorney General
Attn.: Associate Attorney General Perry Zinn Rowthorn
55 Elm Street
P.O. Box 120
Hartford, CT 06141-0120

Commissioner of Public Health
Attn.: Melanie A. Dillon, Esq.
410 Capitol Avenue
Hartford, CT 06134

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**RE: Saint Mary's Health System, Inc. / LHP Hospital Group, Inc.'s Completeness Responses Set Three**

Dear Attorneys Rowthorn and Dillon:

As requested, Saint Mary's Health System, Inc. and LHP Hospital Group, Inc. hereby submit the attached responses regarding their Application for a proposed joint venture. One hard copy and one electronic copy have been hand delivered to each office.

Please date/time stamp a copy of the Responses and return it with our messenger.

If you have any questions or need anything further, please contact me at 860.509.6517. Thank you for your assistance in this matter.

Very truly yours,

**BROWN RUDNICK LLP**

Robert J. Anthony

Robert J. Anthony

cc: Commissioner Dr. Jewel Mullen, DPH
Kimberly Martone, Director of Operations, OHCA
Steven Lazarus, Associate Healthcare Analyst, OHCA
Gary W. Hawes, Assistant Attorney General, OAG
Rebecca Hurley, Esq., LHP

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**STATE OF CONNECTICUT**
**OFFICE OF THE ATTORNEY GENERAL**
**DEPARTMENT OF PUBLIC HEALTH**

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| **IN RE: SAINT MARY'S HEALTH SYSTEM, INC. AND LHP HOSPITAL GROUP, INC.'S APPLICATION FOR APPROVAL OF A JOINT VENTURE.** | : : : : | **November 14, 2011** |

## RESPONSES TO COMPLETENESS QUESTIONS SET THREE

Saint Mary's Health System, Inc. ("Saint Mary's") and LHP Hospital Group, Inc. ("LHP") (collectively, the "Applicants") hereby respectfully submit to the Attorney General and the Commissioner of the Department of Public Health the following responses and additional exhibits regarding their application for a proposed joint venture (the "Application" or "CON").

1. **Please provide a copy of the updated Fairness Evaluation requested in our previous deficiency letter dated September 20, 2011 ("the deficiency letter"). If an updated Fairness Evaluation is not available or not yet available, please explain why and state when it is expected to become available.**

Saint Mary's, Waterbury Hospital and LHP continue to negotiate the terms of the joint venture documents. These types of multiple party transactions are very complex and challenging, thus it takes considerable time to work through every aspect towards a resolution that satisfies all parties involved. Once the business and financial terms are agreed upon and sufficient due diligence has been completed, the Applicants will be in a position to provide a Fairness Evaluation. This is expected to occur at such time that the Saint Mary's Board of Directors is prepared to review and approve the transaction. As noted in response to Question 2 below, a specific timeframe has not yet been determined.

1. **Please provide us with LHP's overall plan and timeframe for the consolidation of the St. Mary's and Waterbury Hospital facilities and services into a new single facility.**

The consolidation plan impacting local hospital operations will not be an "LHP plan". Any consolidation plan implemented by the joint venture will have to be approved by the joint venture Board of Directors to which LHP will appoint 6 of 12 members. Thus, any such plan will require the approval of the not-for-profit voting block controlled by Saint Mary's and Waterbury Hospital. That board does not yet exist.

Having said that, the parties have been thinking through, in general terms, how the consolidation could be most efficiently carried out. This process will evolve over the coming months and more work will need to be done before such plans are finalized. What is clear at this point is that the duplication of services between Saint Mary's and Waterbury Hospital will be addressed in three distinct phases as outlined in the Applicants' response to Question No. 9 submitted to the Attorney General and the Commissioner of the Department of Public Health on October 11, 2011.

2. **In response to the deficiency letter, you stated that there are several issues that must be renegotiated between LHP and St. Mary's in order to accommodate the entry of Waterbury Hospital into a three-party joint venture. Please identify those issues and an expected timeframe for their resolution.**

In general, the issues that must be renegotiated in order to accommodate the entry of Waterbury Hospital into a three-party joint venture relate to governance rights, various matters regarding the proposed replacement hospital (including resolution of the issues relating to compliance with the Ethical and Religious Directives for Catholic Healthcare Services), and sales and transfers of interests between and among the members of the joint venture under various circumstances. In addition, the task force negotiating the transaction on behalf of Saint Mary's has raised a number of legal and technical issues relating to the draft definitive agreements associated with the Waterbury Hospital transaction that must be considered and resolved. Negotiating a complex transaction of this nature among three parties requires time and effort by a large number of individuals. The parties are in the process of discussing these issues and intend to work expeditiously to resolve them as soon as reasonably possible. An expected timeframe for resolution of these issues, however, cannot be determined at this time.

3. **In response to the deficiency letter, Saint Mary's has explained that clinical growth opportunities will result from the anticipated three-party joint venture. Please provide examples of these clinical growth opportunities.**

This is a process that will evolve over the coming months and more work will need to be done before plans are finalized. However, intuitively, the development of the replacement hospital will drive the purchase of a significant amount of new equipment. The consolidation of volumes at a single location will make it possible to upgrade technologies that will in turn drive new volume. As volumes are consolidated at the department level and new volumes are layered on top of existing volumes, the higher throughput at a single location will fuel the use of faster and more effective technologies.

4. **If the three-party joint venture moves forward, will the development of a new electronic medical records (EMR) system for Saint Mary's be coordinated with Waterbury Hospital.**

Yes, if the joint venture moves forward the development of a new EMR system for Saint Mary's will be coordinated with Waterbury Hospital.

**5. According to LHP's Consolidated Statements of Equity ending December 31, 2010, there is a retained deficit of $25,649,110. How long does LHP anticipate it will take to eliminate this deficit.**

LHP began operations in December 2007 and acquired its first hospital in February 2009. In considering how long it will take LHP to achieve positive retained earnings, it is useful to understand the composition of the retained deficit at December 31, 2010. Included in the current retained deficit are two extraordinary, non-recurring items:

- First, the current deficit includes $9,430,600 of start-up losses that were incurred from December 2007 through January 2009 prior to LHP acquiring its first hospital, Portneuf Medical Center in Pocatello, Idaho.
- Second, the current deficit includes a one-time $15,000,000 payment made in connection with the acquisition of the Portneuf Medical Center. The payment was made to Bannock County, Idaho, the former owner of the hospital in question, to establish a community fund to be used for, among other things, indigent care and care for prison inmates. Although the payment was clearly integral to the related asset acquisition, LHP's accounting group concluded that the more conservative accounting treatment was to expense the payment rather than capitalize it as part of the asset purchase price.

If LHP's retained earnings are normalized to eliminate these two non recurring items, its retained deficit at December 31, 2010 would approximate $1,218,500.

LHP's current forecast, which is an estimate that is subject to change based upon changes in economic and business conditions, calls for its existing hospitals to produce the following amounts of net income in the years indicated:

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| Year ended December 31, 2011 | $2,843,000 |
| Year ended December 31, 2012 | $16,336,000 |
| Year ended December 31, 2013 | $30,230,000 |
| Total estimated net income 1/1/11 – 12/31/13 | $49,409,000 |

Therefore, without considering additional hospital acquisitions and without normalizing LHP's December 31, 2010 retained deficit to remove the two extraordinary items, LHP anticipates that it will report positive retained earnings approximating $23,760,000 in its Consolidated Statement of Equity for the year ending December 31, 2013.

In addition to the earnings from its existing hospitals, LHP's current forecast includes earnings from the hospital joint ventures that LHP anticipates acquiring during 2012. If the net income from these acquired hospital joint ventures is included in forecasted earnings, LHP's forecasted net income in 2012, which forecasted income is an estimate that is subject to change based upon changes in economic and business conditions, approximates $110,000,000, resulting in approximately $84,350,000 in positive retained earnings at December 31, 2012.

6. **Your response states that "[t]he Parties have not yet prepared financial projections for the three-party JV that correspond to the financial projections for the LLC that were submitted with the Application on pages 272-274; however, the parties expect that the addition of Waterbury Hospital to the LLC will have a materially positive impact upon such projections." Please explain how the addition of Waterbury Hospital will have positive impact on the financial projections previously submitted by the Applicant and provide supporting documentation and evidence to substantiate this claim.**

There are several factors that support the notion that the addition of Waterbury Hospital will have a positive impact on the financial projections previously submitted. The first is the opportunity to eliminate a large portion of duplicative overhead expenses from the combined entity. The second, alluded to in an earlier response, is the decrease in the incremental operating costs at the department level afforded by the consolidation of existing volume into a single location. Thirdly, the additional volume driven by newer, more efficient and effective technologies will improve both outcomes and financial performance. Fourthly, the ability to move into a state-of-the –art medical facility designed around modern standards of care will greatly enhance employee productivity and efficiency when compared to the current situation where staff are having to make do with outdated and inefficient facilities that have been added to and modified over nearly a century. And finally, the ongoing elimination of the need for duplicative technology purchases and the corresponding underutilization of such technology will further drive financial performance improvement. Even absent the creation of only one physical location, the addition of Waterbury Hospital to the LLC will realize significant cost savings from joint purchasing, shared corporate, administrative and IT services, avoidance of duplicative clinical services, data sharing, streamlined and coordinated clinical processes. All of these factors are expected to have a positive impact on the financial projections.