

IN THE MATTER OF THE APPROVAL
OF THE SALE OF THE ASSETS OF ST.
MARY'S HOSPITAL, PASSAIC, N.J.
PURSUANT TO N.J.S.A. 26:2H-7.10, *et*
seq.

SUPERIOR COURT OF NEW JERSEY
CHANCERY DIVISION: PASSAIC COUNTY
DOCKET NO. PAS-C- 57-14

Civil Action

**BRIEF IN SUPPORT OF APPLICATION OF ST. MARY'S HOSPITAL,
PASSAIC, N.J. PURSUANT TO THE COMMUNITY
HEALTHCARE ASSETS PROTECTION ACT, N.J.S.A. 26:2H-7.11**

DRINKER BIDDLE & REATH LLP
A Delaware Limited Liability Partnership
600 Campus Drive
Florham Park, New Jersey 07932-1047
(973) 549-7000
Attorneys for St. Mary's Hospital, Passaic, N.J.

Of Counsel:

Frank F. Velocci, Esq.
Robert K. Malone, Esq.
Marita S. Erbeck, Esq.

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PRELIMINARY STATEMENT

St. Mary's Hospital, Passaic, N.J. ("St. Mary's" or the "Hospital"), seeks approval under the Community Healthcare Assets Protection Act ("CHAPA"), N.J.S.A. 26:2H-7.11(l), of the sale of substantially all of the assets of the Hospital, including related arrangements and transactions, by St. Mary's to Prime Healthcare Services – St. Mary's Passaic, LLC ("Prime St. Mary's"), a Delaware limited liability company (the "Transaction"). After extensive review, the Acting Attorney General has issued his report finding that the Transaction is consistent with the public interest under CHAPA, subject to conditions specified therein, and the Commissioner of Health (the "Commissioner") has issued a Certificate of Need for the Transaction pursuant to N.J.A.C. 8:33-3.3(a)(1), subject to conditions specified therein. St. Mary's and Prime St. Mary's have accepted all of the conditions.

The Transaction transfers a hospital subject to chronic operating losses to new ownership able to infuse fresh capital, on terms that require the new owners to operate an acute care hospital for at least five (5) years, to maintain all services and programs, and to retain substantially all of the Hospital's employees. Moreover, it will preserve the Hospital in service for the community. The Acting Attorney General has determined that the Transaction complies with the criteria of CHAPA and is in the public interest, and the Commissioner has determined that the Transaction will benefit the community by preserving St. Mary's as a general acute care hospital.

St. Mary's respectfully requests that the Court review the Transaction as expeditiously as possible. It is in the interest of the Hospital, its employees and the community to have this period of uncertainty come to an end and new ownership put in place to begin a new era for St. Mary's. Accordingly, it is respectfully requested that the Court issue the Order to Show Cause in accordance with Rule 1:6-3.

STATEMENT OF FACTS

A. Parties To The Transaction

St. Mary's is owned by a single corporate member, St. Mary's Health Corporation (the "Corporation"), a New Jersey not for profit corporation. Under the bylaws of St. Mary's, as its sole corporate member, the Corporation has certain reserved powers, including the right to sell the assets of St. Mary's in the Transaction.

St. Mary's is a 269-bed general acute care community hospital licensed by the New Jersey Department of Health ("DOH"). St. Mary's (a) engages in the business of delivering healthcare services to the public through the operation of an acute care hospital located at 350 Boulevard, Passaic, Passaic County, New Jersey and (b) owns and operates certain outpatient, ancillary and other healthcare businesses incident to the operation of the Hospital. These outpatient, ancillary and other healthcare businesses are currently owned by the Hospital and are included in the assets being purchased by Prime St. Mary's in the Transaction.

Prime St. Mary's is a wholly owned subsidiary of Prime Healthcare Services, Inc. ("PHS"), a Delaware corporation. PHS and its affiliate, Prime Healthcare Services Foundation, a 501(c)(3) public charity, collectively own and operate a total of twenty-five (25) acute care hospitals and more than 4,700 beds throughout California, Kansas, Nevada, Pennsylvania, Rhode Island and Texas.

B. Background To The Transaction

Founded in 1895 by the Sisters of Charity of St. Elizabeth, St. Mary's was established and operated to serve the public interest by providing medical and surgical treatment and care for sick, injured and infirm persons, regardless of their race, creed, nationality, or their financial ability to pay for such services. In March 2007, St. Mary's purchased the assets of Passaic Beth Israel Regional Medical Center ("PBI"), which had, just three years earlier acquired the General

Hospital Center of Passaic. Since the acquisition of the assets of PBI, St. Mary's is the only hospital remaining in the city of Passaic. It has been considered by the Hospital Alliance of New Jersey to be a "vital safety net critical access" hospital. St. Mary's has approximately 1,200 employees and more than 550 physicians on its medical staff.

In 2009, St. Mary's was forced to file for Chapter 11 bankruptcy protection. In 2010, St. Mary's became the first hospital in the state to successfully emerge from this position. During the years 2008 through 2010, in an effort to shed operating losses, St. Mary's divested its inpatient behavioral health services, emergency psychiatric service, a chronic dialysis unit, and medical primary care clinics.

St. Mary's has actively sought a capital partner since it emerged from bankruptcy. The deliberation process that the St. Mary's Board of Trustees (the "Board") followed with regards to the Transaction began in 2010 with the search for a "capital partner."

During 2010, the then current CEO of St. Mary's worked with the Board's Strategic Planning Committee to identify an organization that would be interested in either affiliating with or acquiring St. Mary's. As part of that process, 22 different organizations were contacted and given a copy of a Confidential Descriptive Memorandum. Of those contacted, only one, the for-profit Ascension Health System ("Ascension"), expressed interest in an affiliation. During calendar year 2011, St. Mary's had substantive discussions with representatives of Ascension which led to the execution of a Letter of Intent. On September 27, 2011, St. Mary's signed a Memorandum of Understanding with Ascension Healthcare Network ("AHCN"). This acquisition was to include St. Joseph's Regional Medical Center ("SJPMC"). In November 2011, a Memorandum of Understanding ("MOU") was signed by all three parties: St. Mary's, SJPMC, and AHCN. St. Mary's and SJPMC are sponsored by the same Religious

Congregation, the Sisters of Charity of St. Elizabeth. During 2011 and through the first half of 2012, representatives of Ascension, St. Mary's and SJRMC conducted due diligence and proceeded to develop an Asset Purchase Agreement that was expected to be signed by all three organizations in the summer of 2012 with the transfer of assets to Ascension anticipated to occur in early 2013. In August of 2012, quite unexpectedly, the Board of Trustees of SJRMC decided not to proceed. Given that Ascension's interest was to acquire both St. Mary's and SJRMC, discussions with Ascension ended almost immediately. Without the inclusion of SJRMC, AHCN was no longer interested in purchasing St. Mary's and the transaction between the parties fell through.

Immediately following the announcement, the capital partner selection process resumed. New key criteria were established by the Hospital's Strategic Planning Committee. In looking for a new capital partner, it was essential that St. Mary's remain an acute care hospital. The Strategic Planning Committee also preferred to find a capital partner that would adhere to the Catholic principles upon which St. Mary's was founded. Other key criteria included: addressing non-union pension obligations; long term debt in a manner satisfactory to the applicable State agencies; ability to invest capital in St. Mary's; and an ability to close quickly outside of a bankruptcy proceeding. St. Mary's sought a capital partner willing to acquire the Hospital outside of bankruptcy because management and physicians were concerned that a second bankruptcy in three years would have a negative effect on patients' willingness to choose St. Mary's for their healthcare needs. PBI filed for bankruptcy in 2006, the assets of which were acquired by St. Mary's, and therefore, this would have been the third bankruptcy experienced by a majority of the employees and physicians on the medical staff.

Beginning in late August 2012, St. Mary's started a new search for an organization with interest in affiliating with or acquiring the Hospital. There was considerable urgency due to the deteriorating financial condition of St. Mary's and the fact that internal projections indicated that St. Mary's would have run out of cash before the end of the calendar year. Eight different organizations responded to the search. The responses fell into one of three categories: (a) no interest, (b) interest only if the Proposed Transaction could be structured around a "prepackaged bankruptcy" and (c) interest in acquiring St. Mary's under a traditional purchase of assets structure.

The Board, in collaboration with the leadership of the medical staff, concluded that another bankruptcy would be problematic because of the impact it would have on patients and private practice physicians who would probably not understand the implications of a prepackaged bankruptcy and would focus on the fact that St. Mary's was once again filing for bankruptcy. As a result, discussions continued with the only two organizations that expressed interest in acquiring St. Mary's under the traditional purchase of assets structure, PHS and Hudson Holdco, a New Jersey based organization that operates hospitals in Hudson County, New Jersey. PHS and Hudson Holdco both operate as for-profit entities. No not-for-profit health system was willing to conduct due diligence on St. Mary's to even consider a purchase through a bankruptcy proceeding.

In early October 2012, a revised Term Sheet was developed, reviewed with the Board and provided to PHS and Hudson Holdco. These two interested parties were asked to submit best and final offers. On November 7, 2012, both organizations were invited to personally meet with the Board and present the basis for their selection as the acquirer of choice.

At a Board meeting held on November 27, 2012, the Board reviewed the best and final offers and by unanimous vote selected PHS as the acquirer of choice. Although both offers were very similar from a financial perspective, the Board selected PHS because it determined PHS, as an acquirer, will own and operate the Hospital in the best interest of the community and specifically, for the following reasons: (a) PHS's performance relative to its recent acquisition and operation of a Catholic hospital in Reno Nevada, St. Mary's of Reno, based on one-on-one discussions between St. Mary's Board Chair, Sr. Barbara Conroy and Sr. Maureen McInerney O.P., a representative of the sponsor of St. Mary's, Reno; (b) PHS's size, balance sheet and experience as an operator of twenty (20) hospitals across the country as of that date, including in neighboring Pennsylvania; (c) PHS's approach to managing inner city hospitals as described during their presentation to the Board on November 7, 2012; (d) PHS's ranking among the Top 15 Health Systems by Thomson Reuters in 2012, its hospitals routinely being ranked among the Top 100 Hospitals in the nation, and its hospitals being ranked among the Top Performers on Key Quality Measures by Joint Commission and Centers for Medicare and Medicaid Services patient satisfaction surveys.

On November 28, 2012, the Board approved execution of the Letter of Intent with PHS, which contemplated the transfer of ownership of St. Mary's to Prime St. Mary's.

C. The Structure of the Transaction

1. Terms and Purchase Price

St. Mary's executed a letter of intent with PHS on November 29, 2012. On January 29, 2013, St. Mary's, PHS and Prime St. Mary's entered into an Asset Purchase Agreement for the sale of substantially all of the assets of the Hospital (the "Original APA"), which was subsequently modified on three occasions: (a) to extend the termination date of the APA to

December 31, 2013 for consideration of an additional \$5 million (b) to extend the termination date of the APA to April 30, 2014 and (c) to extend the termination date of the APA to July 31, 2014 (the Original Agreement, together with these modifications, collectively, the “APA”). A copy of the APA is attached to the Verified Complaint filed contemporaneously herewith as Exhibit B. The APA provides that PHS intends to acquire substantially all of the assets and assume certain of the liabilities of the Hospital as documented on the Hospital’s Financial Statements for the month prior to the month during which the Proposed Transaction closes, including the tail coverage associated with the Hospital’s Professional Liability Insurance, for a total price of \$30 million plus a commitment to invest at least \$30 million in capital improvements with no less than \$15 million during the first two years, not including normal/routine equipment replacements. Exceptions include (a) religious artifacts that will be returned to the Sponsor, (b) the Hospital’s non-union pension obligations and (c) the New Jersey Health Care Facilities Financing Authority Hospital Asset Transformation Program Bonds Series 2007-1 and 2007-2 (collectively, “the Series 2007 Bonds”).

As described above, PHS and St. Mary’s modified the APA to reflect PHS’ agreement to provide an additional \$5 million to address the Hospital’s non-union pension issues. In addition, PHS provided an additional \$3 million of working capital to the Hospital in the event that it was needed.

2. Use of Proceeds

The proceeds from the sale of St. Mary’s will be used as follows: (a) \$5 million of unsecured working capital was advanced to the Hospital; (b) \$15 million will be paid to the State of New Jersey in return for a release of all obligations, liens and encumbrances associated with the Series 2007 Bonds; (c) \$750,000 to fund the wind down and termination costs associated

with St. Mary's, post-closing, including but not limited to Directors and Officers tail coverage, and the legal fees associated with terminating St. Mary's corporate structure; and (d) \$9.25 million, to address the Hospital's non-union pension issues. In the event that there are any funds remaining from the \$750,000 allocated to the wind down of St. Mary's, they will be made available to fund the non-union pension plan. Post-closing, St. Mary's does not anticipate retaining any assets or having any debts or liabilities remaining as obligations of the Hospital except those described above.

3. Employee Matters

Prime St. Mary's has reached agreements with the Hospital's unions: JNESO, District Council 1, IOUE, AFL-CIO ("JNESO") covering the technicians who work at the Hospital and the registered nurses at the Hospital (collectively, the "JNESO Employees") and Local 68 of the International Union of Operating Engineers, AFL-CIO, covering approximately 20 individuals who operate machinery in the Hospital.

In addition to other regulatory and contractual consents and approvals required to be provided for the closing of the Transaction, St. Mary's is required, under the federal Worker Adjustment and Retraining Notification Act and its New Jersey equivalent, the Millville Dallas Airmobile Plant Jobs Loss Notification Act (collectively, the "WARN Act"), to provide written notice to its employees at least sixty days prior to a transaction that constitutes a mass layoff under these laws. Accordingly, in anticipation of receiving the required regulatory and other approvals for the Transaction in March, St. Mary's issued notices on January 10, 2014, under the WARN Act, to employees of the Hospital anticipating a closing in March 2014. Thereafter, on March 17, 2014, April 17, 2014 and June 5, 2014, the Hospital issued subsequent WARN Act Notices to employees. There are approximately 1,200 employees of the Hospital who are

affected and thus received this notice either personally or by mail. Prime St. Mary's has agreed to retain substantially all of the current employees.

No corporate officer or trustee of St. Mary's or the Corporation has any financial interest in Prime St. Mary's or in the Transaction or the proceeds of the Transaction.

D. Review by the Department Of Health

On December 31, 2012, Prime St. Mary's submitted to the DOH an application for a Certificate of Need to transfer ownership of the Hospital pursuant to N.J.A.C. 8:33-3.3(a)(1) (the "CN Application"). DOH deemed the CN Application complete by letter dated December 19, 2013.

Public hearings with respect to the CN Application were held at Passaic High School on January 15, 2014 and at St. Clare Elementary School in Clifton, New Jersey on January 30, 2014. More than 300 people attended both meetings. Copies of the transcripts of these public hearings are attached to the Verified Complaint filed contemporaneously herewith as Exhibits C and D, respectively. Dozens of individuals spoke at the hearings, expressing their overwhelming support for the Transaction. These people included:

- Sister Barbara Conroy, Chair of the St. Mary's Board
- Edward J. Condit, Chief Executive Officer of St. Mary's
- Assemblyman Gary Schaer, 36th District
- Assemblywoman Marlene Caride, 36th District
- Dr. Alex D. Blanco, Mayor of the City of Passaic
- James Anzaldi, Mayor of Clifton
- Virginia Treacy, Executive Director of JNESO District Council 1
- Nicholas Lanza, Chief Financial Officer of St. Mary's

- Christina Hutchinson, Chief Nursing Officer and Chief Operating Officer of St. Mary's
- 15 practicing physicians
- 4 members of St. Mary's Board
- Robert Arnold, Senior Executive Director of Hamilton Plaza Nursing and Rehab Center
- Paula Klein, Director of Radiology and Imaging at St. Mary's
- Robert D'Ambola, Director of Safety Security and Emergency Management at St. Mary's
- Steven Rose, President of Passaic County Community College
- Michelle McWeen, Seton Hall Physician Assistant Program
- Ana G. Rivera, Catholic Family Community Services for Hispanic Information Center
- Lee Weiss, Pulse Medical Transportation
- 14 residents of Passaic and surrounding municipalities
- 3 representatives of other hospitals acquired by PHS

In addition, those who had questions or concerns regarding the Transaction were permitted to speak, including India Hayes-Larrier, a representative of New Jersey Citizen Action, an independent citizen watchdog coalition; 4 members of the public, 3 of which are from outside the state of New Jersey. Of the 55 speakers, only 5 speakers had questions or concerns.

On February 21, 2014, the State Health Planning Board reviewed the CN Application and the comments and concerns presented by the various individuals and organizations at the public hearings on January 15 and 30, 2014. As was the case at the January 15 and 30 hearings, there

was tremendous community support for the Transaction before the State Health Planning Board. The State Health Planning Board unanimously recommended approval of the Transaction, subject to certain conditions. A transcript of the State Health Planning Board hearing is attached to the Verified Complaint filed contemporaneously herewith as Exhibit E.

On June 13, 2014, DOH approved the CN Application. A copy of the Certificate of Need is attached to the Verified Complaint filed contemporaneously herewith as Exhibit F. Approval is subject to compliance with conditions initially recommended by the State Health Planning Board, including:

- To operate the Hospital as a general hospital for at least five (5) years;
- To establish a Community Advisory Group, independent Advisory Board and Local Governing Board;
- To retain substantially all of the current employees;
- To continue all clinical services and community health programs currently offered for at least five (5) years.

St. Mary's and Prime St. Mary's assent to all conditions recommended by the State Health Planning Board.

E. Review by the Attorney General

On December 31, 2012, in accordance with CHAPA, St. Mary's provided initial notice of the Transaction to the Attorney General's Office. In response to requests for further information, St. Mary's and Prime provided thousands of pages of additional information and documentation to supplement its initial CHAPA application, including evidence of the fair market value of the Hospital. By letter dated December 19, 2013, the Acting Attorney General deemed the initial CHAPA application complete.

On January 16, 2014, in accordance with N.J.S.A. 26:2H-7.11(f), a designee of the Acting Attorney General, in conjunction with a designee of the Commissioner of Health, conducted an open public hearing at Passaic High School. A transcript of the public hearing is attached to the Verified Complaint filed contemporaneously herewith as Exhibit G. As required by N.J.S.A. 26:2H-7.11(a)(1), notice of the public hearing was advertised in the Herald News, The Record and El Especial (in Spanish), three newspapers of general circulation in Passaic County. The following individuals and groups participated in the public hearing, expressing either their support for the Transaction or their questions and concerns, including Sister Barbara Conroy, Chair of the St. Mary's Board and Edward J. Condit, Chief Executive Officer of St. Mary's; Senator Paul Sarlo, 36th District (via written letter read by Mr. Condit); public officials from the City of Clifton, the City of Garfield, the City of Wallington and the County of Passaic; India Hayes-Larrier of the New Jersey Citizen Action; Renee Steinhagen, Executive Director of New Jersey Appleseed Public Interest Law Center; Ed Lyons, Executive Director of the United Passaic Organization; Joanne Green, Executive Director of the Mental Hospital Association of Passaic County; employees, physicians and patients of the Hospital; and various other members of the public. Of the 45 individuals that spoke at the hearing, 39 supported the Transaction.

In the Acting Attorney General's Report dated June 13, 2014, the Acting Attorney General concluded that the Transaction is in the public interest and should be approved by this Court subject to certain conditions in addition to those imposed by the Commissioner, including:

- The discretion to force the resale of the Hospital in the event of any material misrepresentation in regards to this Transaction;
- To continue to provide information to the Acting Attorney General concerning actions taken against Prime, its affiliates or its hospitals for a term of five (5)

years relating to, or any final resolution of, the investigation currently being conducted by the United States Department of Justice and the Office of the Inspector General into coding at Prime hospitals;

- That St. Mary's Hospital Foundation, which shall continue in existence, provide the Acting Attorney General with an annual report for a two-year period and file a separate application to seek judicial application of the *cy pres* doctrine to change its purpose or mission and the disposition of its donor-restricted funds¹; and
- That Trustees and senior management of the Hospital be prohibited from investing in Prime or its subsidiaries for a period of three (3) years following the Transaction.

See Verified Complaint, Ex. A. St. Mary's and Prime St. Mary's have accepted the foregoing conditions.

LEGAL ARGUMENT

I. THE PROCEDURAL REQUIREMENTS OF CHAPA HAVE BEEN SATISFIED

CHAPA requires that the Acting Attorney General and the Commissioner of Health conduct a public hearing. N.J.S.A. 26:2H-7.11(f). It also requires that any person who submitted written comments or made a statement at the public hearing be joined as a party to this proceeding. N.J.S.A. 26:2H-7.11(l). These procedural requirements have been satisfied.

After notice was published in three local newspapers, the Acting Attorney General held a public hearing that was conducted at Passaic High School on January 16, 2014. Each of the individuals who participated at the hearing or submitted written comments on the application will be served with copies of the pleadings in this case, as will the Acting Attorney General. The

¹ It is expected that at the time of the closing of the Transaction, the St. Mary's Hospital Foundation will have less than \$100,000 in donor-restricted funds.

Order to Show Cause further provides that individuals who submitted postcard comments on the transaction or signed petitions will be notified by ordinary mail, and through a legal notice in three Passaic County newspapers, of their right to appear and submit comments in this proceeding. The notice states that copies of the pleadings will be available for public review both at St. Mary's and on its website.

II. THE TRANSACTION IS CONSISTENT WITH BOTH CHAPA AND THE CHARITABLE PURPOSES OF ST. MARY'S HOSPITAL

At common law the Attorney General represents the public's interest in the compliance of charitable trusts and charitable corporations with their charitable obligations. *See Paterson v. Paterson General Hospital*, 97 N.J. Super. 514, 518-19 (Ch. Div. 167), *aff'd*, 104 N.J. Super. 472 (App. Div. 1969); *Trustees of Rutgers College v. Richman*, 41 N.J. Super. 259, 283 (Ch. Div. 1956). Accordingly, the Attorney General must be notified of any action involving a charitable corporation. R. 4:28-4(b); *see Matter of Estate of Yablick*, 218 N.J. Super. 91, 97-99 (App. Div. 1987). CHAPA requires the Attorney General to review any proposed sale of a nonprofit hospital, according to the statutory criteria, in furtherance of his common law power as the "protector, supervisor and enforcer of charitable trusts and charitable corporations." N.J.S.A. 26:2H-7.11.

The Chancery Division exercises the common law powers of the Chancellor to oversee charitable corporations and associations. *See Howard Savings Institution v. Peep*, 34 N.J. 494 (1961); *Sharpless v. Medford Monthly Meeting of Society of Friends*, 228 N.J. Super. 68 (App. Div. 1988); *Tp. of Cinnaminson v. First Camden National Bank & Trust*, 99 N.J. Super. 115 (Ch. Div. 1968). A nonprofit hospital is a charitable corporation subject to the Chancery Court's supervisory power. *Paterson General Hospital, supra*. After the Attorney General has reviewed

and approved a proposed sale of a nonprofit hospital, CHAPA requires judicial review and approval by this Court. N.J.S.A. 26:2H-7.11(l).

Historically, the Chancery Division has reviewed changes in the charitable purpose of a trust or corporation under the doctrine of *cy pres*. See, e.g., *See Peep, supra*; *Sharpless, supra*; *Paterson General Hospital, supra*. Under the doctrine of *cy pres*, if the accomplishment of the purpose of a charitable bequest, trust or corporation becomes impossible or impracticable, a court of equity may modify the terms of the charity to a related purpose consistent with the settlor's or incorporator's general charitable intent. See generally *Peep*, 34 N.J. at 500-02; *Sharpless*, 228 N.J. Super. at 74.

CHAPA particularizes the general doctrine of *cy pres* as applied to the sale of a nonprofit hospital to a for profit entity. It requires the Attorney General to investigate the proposed Transaction in order to determine whether "appropriate steps have been taken to safeguard the value of the charitable assets of the hospital and to ensure that any proceeds from the proposed acquisition are irrevocably dedicated for appropriate charitable health care purposes." N.J.S.A. 26:2H-7.11(b). Specifically, N.J.S.A. 26:2H-7.11(c) requires the Attorney General to determine:

- (1) Whether the acquisition is permitted under the "New Jersey Nonprofit Corporation Act," Title 15A of the New Jersey Statutes, and other applicable State statutes governing nonprofit entities, trusts or charities;
- (2) Whether the nonprofit hospital exercised due diligence in deciding to effectuate the acquisition, selecting the other party to the acquisition and negotiating the terms and conditions of the acquisition;
- (3) The procedures used by the nonprofit hospital in making its decision, including whether appropriate expert assistance was used;
- (4) Whether conflict of interest was disclosed, including, but not limited to, conflicts of interest related to board members of,

executives of and experts retained by the nonprofit hospital, purchaser or other parties to the acquisition;

(5) Whether any management contract under the acquisition is for reasonable fair value; and

(6) Whether the acquisition proceeds will be used for appropriate charitable health care purposes consistent with the nonprofit hospital's original purpose or for the support and promotion of health care and whether the proceeds will be controlled as charitable funds independently of the purchaser or parties to the acquisition.

Because the sale is to a for-profit purchaser, N.J.S.A. 26:2H-7.11(d) further requires the Attorney General to determine:

(1) Whether the nonprofit hospital will receive full and fair market value for its assets. The Attorney General may employ, at the nonprofit hospital's expense, reasonably necessary expert assistance in making this determination;

(2) Whether charitable funds are placed at unreasonable risk, if the acquisition is financed in part by the nonprofit hospital;

(3) Whether a right of first refusal has been retained to repurchase the assets by a successor nonprofit corporation or foundation if, following the acquisition, the hospital is subsequently sold to, acquired by or merged with another entity;

(4) Whether the nonprofit hospital established appropriate criteria in deciding to pursue a conversion in relation to carrying out its mission and purposes;

(5) Whether the nonprofit hospital considered the proposed conversion as the only alternative or as the best alternative in carrying out its mission and purposes;

(6) Whether the nonprofit hospital exercised due care in assigning a value to the existing hospital and its charitable assets in proceeding to negotiate the proposed conversion;

(7) Whether officers, directors, board members or senior management will receive future contracts in existing, new, or affiliated hospitals or foundations; and

(8) Any other criteria the Attorney General establishes by regulation to determine whether a proposed acquisition by any

person or entity other than a corporation organized in this State for charitable purposes under Title 15A of the New Jersey Statutes is in the public interest.

CHAPA also prohibits the trustees and managers from benefitting from the Transaction. N.J.S.A. 26:2H-7.11(j) and (k). Finally, it requires that the Commissioner determine that the sale “will not result in the deterioration of the quality, availability or accessibility of health care services in the affected communities.” N.J.S.A. 26:2H-7.11.

The Commissioner issued the Certificate of Need required by N.J.A.C. 8:33-3.3(a)(1) for the transfer of ownership of the Hospital on June 13, 2014. The Certificate of Need concludes that the transfer is necessary to avoid closure of the Hospital and that it will preserve access to health care services for the community including the medically indigent and medically underserved populations. Verified Complaint, Ex. F at 4. It also concludes that St. Mary’s could no longer sustain the operating losses. *Id.* at ¶¶ 4-5. The Certificate of Need is subject to the conditions, all of which St. Mary’s and Prime St. Mary’s have accepted.

As detailed in the Acting Attorney General’s Report, the statutory criteria of CHAPA have been complied with. In particular, the Acting Attorney General found (i) that St. Mary’s had acted with due diligence in both deciding to effectuate the sale and in selecting Prime as the acquiring party, (ii) that there were no conflicts of interest or self-dealing, (iii) that the purchase price obtained fair market value for the Hospital’s assets, (iv) that the financial terms did not place the Hospital’s charitable assets at risk, and (v) that the proceeds will be used for appropriate charitable health care purposes. As the Attorney General concluded:

... St. Mary’s is the last of three nonprofit hospitals in Passaic to find it impossible to remain financially viable. Based on the materials submitted to us as part of the CHAPA process, it is unlikely that the Hospital is capable of surviving as a standalone entity. If the Hospital and Prime fail to obtain all of the necessary regulatory approvals and consummate the Proposed Transaction, the Hospital will almost certainly file for bankruptcy and will

likely cease to operate in its current form. In that event the community will lose the health care services provided by the Hospital as currently constituted We are satisfied that the trustees reasonably exercised their fiduciary duty in selecting an acquirer who they believe will be the best able to maintain the Hospital as a going concern. We are satisfied that under the circumstances taken as a whole, the Proposed Transaction is in accordance with the factors set forth in CHAPA.

Thus, when the Proposed Transaction is viewed in its entirety, this Office finds that, under the totality of the circumstances, it appears to be in the public interest, and, accordingly, it receives our support, provided that we respectfully request that the Court incorporate the following conditions into its order approving the transaction.

Verified Complaint, Ex. A at 53-54.

The Report then sets out certain conditions in addition to those required by the Commissioner, including (1) the discretion to force the resale of the Hospital in the event of any material misrepresentation in regards to this Transaction; (2) to continue to provide information to the Acting Attorney General concerning actions taken against Prime, its affiliates or its hospitals for a term of five (5) years relating to, or any final resolution of, the investigation currently being conducted by the United States Department of Justice and the Office of the Inspector General into coding at Prime hospitals; (3) that St. Mary's Hospital Foundation, which shall continue in existence, provide the Acting Attorney General with an annual report for a two-year period and file an application to seek judicial application of the *cy pres* doctrine to change its purpose or mission and the disposition of its donor-restricted funds; and (4) that Trustees and senior management of the Hospital be prohibited from investing in Prime or its subsidiaries for a period of three (3) years following the Transaction. *Id.*

While CHAPA does not require this Court to follow the Acting Attorney General's recommendation, it should give great deference both to the Acting Attorney General's detailed examination of the Transaction and to the Commissioner's issuance, after an equally detailed

review, of a Certificate of Need for the transfer of ownership to Prime St. Mary's. The Transaction was entered after a competition among other potential buyers, for a purchase price far superior to the appraised fair market value of the Hospital's assets. None of the trustees or officers of the Hospital has any interest in the buyer or will receive any benefit from the Transaction. They have exercised their judgment of the best interests of St. Mary's with the due care and disinterest required by the Nonprofit Corporation Act, N.J.S.A. 15A:6-14. See *Johnson v. Johnson*, 212 N.J. Super. 368, 385 (Ch. Div. 1985); *Paterson*, 97 N.J. Super. at 527; *Leeds v. Harrison*, 7 N.J. Super. 558, 570 (Ch. Div. 1950).

Moreover, the Transaction is consistent with the charitable purposes of St. Mary's. Historically, the Hospital has had substantial operating losses and is not operating on a self-sustaining basis. The sale is for fair market value and the proceeds will be used for appropriate charitable health care purposes. Prime St. Mary's will be required to continue operating St. Mary's as a general acute care hospital for five years, to maintain all of the existing clinical services and community health programs at the Hospital, to provide charity care as required by N.J.S.A. 26:2H-18.64 and N.J.A.C. 8:43G-5.3(c), to hire substantially all of the present employees of the Hospital and to establish a Community Advisory Group, an independent Advisory Board and a Local Governing Board. Sale to Prime St. Mary's represents the only alternative that will maintain the Hospital as an acute care facility serving its community. Accordingly, this Court should approve the Transaction both under CHAPA, N.J.S.A. 26:2H-7.11(l), and under its common law power to oversee charitable corporations.

CONCLUSION

For the foregoing reasons, the Court should issue the Order to Show Cause initiating this proceeding and, on the return date provided therein, should enter judgment (i) declaring that the Transaction is in the public interest in accordance with the application requirements of the Community Healthcare Assets Protection Act, N.J.S.A. 26:2H-7.10 *et seq.*; (ii) granting approval of the sale of substantially all of the assets of St. Mary's Hospital, Passaic, N.J. to Prime Healthcare Services – St. Mary's Passaic, LLC; and (iii) for such other relief as the Court deems just and proper.

Dated: June 20, 2014

DRINKER BIDDLE & REATH LLP

By: 

Frank F. Velocci

Attorneys for St. Mary's Hospital, Passaic, N.J.