



DOCKET NO. : OAG 13-486-01

IN RE APPLICATION FOR JOINT VENTURE BETWEEN GREATER WATERBURY HEALTH NETWORK, INC., AND VANGUARD HEALTH SYSTEMS, INC. : OFFICE OF THE ATTORNEY GENERAL
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:
: DECEMBER 1, 2014

PROPOSED FINAL DECISION

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I. INTRODUCTION

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. The delivery of healthcare services also remains a quintessentially local issue of critical importance to the communities in which nonprofit hospitals operate. The City of Waterbury knows full well the challenges presented to its two acute care hospitals: Waterbury Hospital and Saint Mary's Hospital. In response to those challenges, both hospitals have chosen to partner with a for-profit entity with the goals of addressing the immediate capital needs of the hospitals and better integrating the delivery of healthcare services across networks.

The Nonprofit Hospital Conversion Act, Conn. Gen. Stat. § 19a-486 et seq. (the "Conversion Act"), requires the Attorney General to undertake a review whenever a transaction is proposed that would transfer a material amount of a nonprofit hospital's assets to a for-profit entity. Such a transfer is referred to as a "hospital conversion." The primary purpose of the Attorney General's review of hospital conversions is to protect the charitable assets of the nonprofit hospital and, in that sense, is an extension of the jurisdiction granted him in Conn. Gen. Stat. § 3-125 to protect the public's interest in gifts or other assets held for charitable or public purposes. This requires ensuring that the sale of a nonprofit hospital's assets is procedurally and substantively fair, and that the proceeds received for those assets are

themselves protected as charitable assets to be used for appropriate nonprofit purposes – here, the advancement of health in the Waterbury community.¹

The Office of the Attorney General (the “OAG”) has completed an extensive review of the proposed joint venture between Greater Waterbury Health Network, Inc. (“GWHN”), and Vanguard Health Systems, Inc. (“Vanguard”)(collectively, the “Applicants”). Tenet Healthcare Corporation (“Tenet”) is the corporate parent of Vanguard, and although not directly a party to the transaction under review, Tenet has appeared in this case and is subject to the modifications and conditions set forth herein.²

As explained in detail below, we grant the application subject to certain modifications and conditions necessary to conform the proposed transaction to the purposes of the Conversion Act. In issuing this decision, the Attorney General thanks the parties to the transaction, the intervenors and all others who participated in this review. The Attorney General extends special thanks and recognition to the citizens of the greater Waterbury area. It is understandable that many will have strong feelings about a transaction anticipated to bring substantial change to an institution integral to the fabric of their community for over a century.

¹ Because the Attorney General’s review centers on the protection of the charitable assets, his focus in reviewing the transaction does not generally encompass the running of the for-profit hospital that results from a hospital conversion. Contemporaneously with the OAG’s review of the Joint Venture, the Office of Health Care Access, Department of Public Health (“OHCA”), has reviewed the transaction to determine if a certificate of need should be issued in this case. OHCA’s review is also undertaken pursuant to the Conversion Act, but it examines the proposed transaction pursuant to a separate set of criteria set forth in the Act.

² The Saint Mary’s Hospital conversion review process is proceeding on a different schedule than the process in the GWHN matter. However, the public hearings for both cases were held on consecutive days so that all Waterbury related issues could be discussed publicly at one point in time.

Their attention to this transaction and input concerning it are especially valued and appreciated.

II. SUMMARY

A. The Conversion Act – An Overview

The Conversion Act authorizes 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 the Conversion Act are not met, or to approve the transactions subject to modifications that the Attorney General deems appropriate. Under the law, the Attorney General is required to assess the fairness of the transaction, both procedural and financial, and to protect and preserve the charitable assets of Waterbury Hospital.

The first and only transaction reviewed by the OAG under the Conversion Act concerned the sale of Sharon Hospital, *In re Sale of Sharon Hospital*, Docket No. OAG 01-486-01 (2001). Although the *Sharon* decision is over 13 years passed, it provides some precedential value for our analysis in this matter. Since the decision in *Sharon*, however, the Conversion Act has been amended several times. First, in 2004, the legislature added additional language regarding the type of entity that can hold the nonprofit hospital's charitable assets after the proposed transaction. We discuss that amendment in detail in Section V.

Second, in June of 2014, the legislature amended the Conversion Act to allow the Attorney General to "place any conditions on the approval of an application that relate to the purposes of sections 19a-486a to 19a-486h, inclusive." Public Act 14-168, sec. 10(b). However, the Attorney General previously had the power to approve a proposed transaction subject to

modification. Conn. Gen. Stat. § 19a-486b. We interpret the power to require modifications to the proposed transaction and the power to place conditions on the proposed transaction as identical. Nothing in the legislative history of Public Act 14-168 suggests an intent to expand upon the previously existing authority to approve transactions with modifications. Accordingly, we believe that the 2014 amendment did not enlarge the Attorney General's jurisdiction in his review of a hospital conversion.³

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. Conn. Gen. Stat. § 19a-486c(a).⁴ More specifically, the OAG shall deny an application if one or more of the following conditions exist:

- the transaction is prohibited by Connecticut statutory or common law governing nonprofit entities, trusts or charities;
- 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;
- 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;

³ Additionally, we interpret the 2014 amendment as allowing the imposition of conditions that relate only to the grounds for disapproval that the Attorney General is required to assess. Conn. Gen. Stat. § 19a-486c.

⁴ Our review pursuant to the Conversion Act does not include competition concerns that this transaction alone or together with others may raise. The Attorney General has separate statutory authority pursuant to the Connecticut Antitrust Act to consider any such concerns.

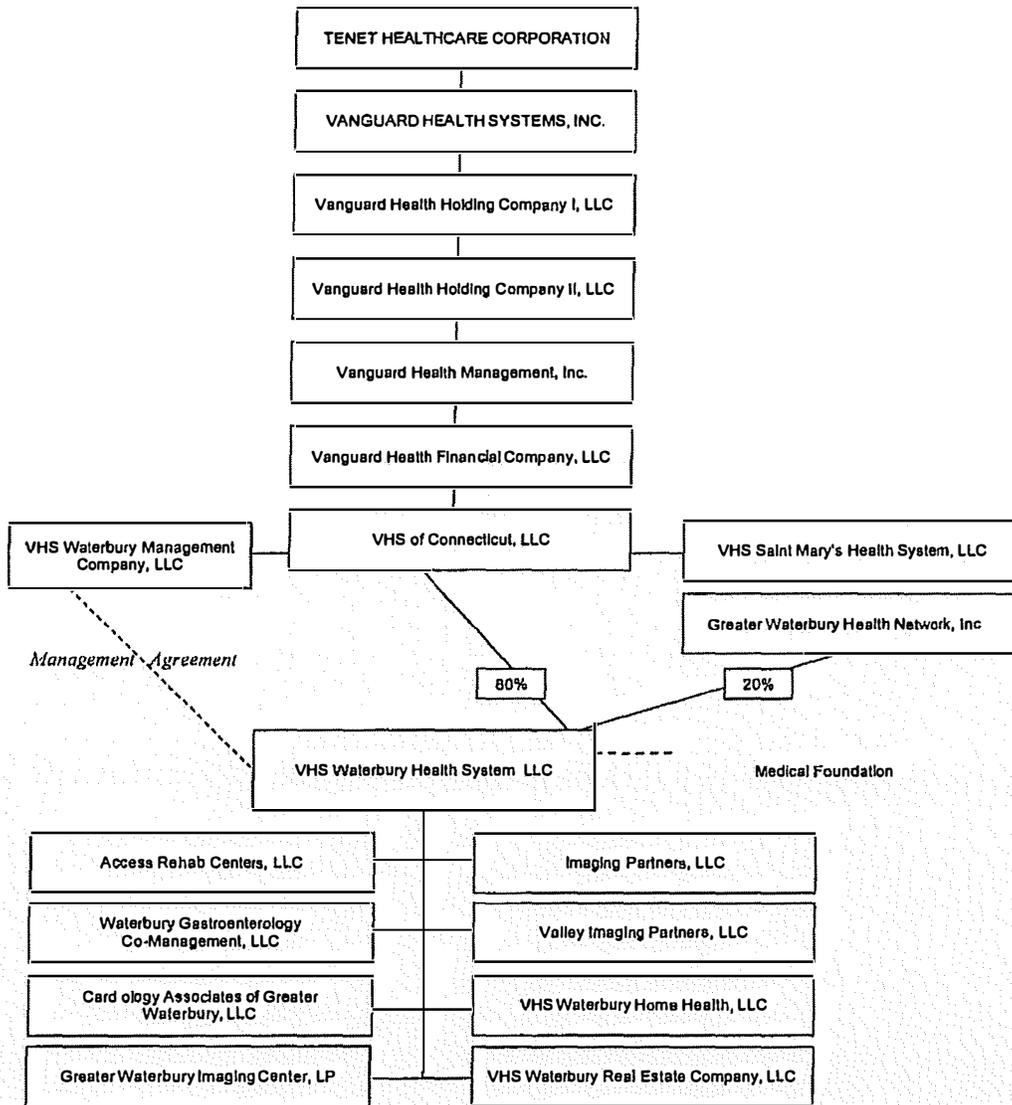
- the nonprofit hospital will not receive fair market value for its assets, which, for purposes of this subsection, means the most likely price that the assets would bring in a sale in a competitive and open market under all conditions requisite to a fair sale, with the buyer and seller each acting prudently, knowledgeably and in their own best interest, and with a reasonable time being allowed for exposure in the open market;
- 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;
- the financing of the transaction by the nonprofit hospital will place the nonprofit hospital's assets at an unreasonable risk;
- any management contract contemplated under the transaction is not for reasonable fair value;
- 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
- 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.

B. The Proposed Transaction

GWHN and Vanguard propose to form a for-profit joint venture (the "Joint Venture Hospital" or "JV Hospital") that, upon closing, will own substantially all of Waterbury Hospital's

assets, most significantly, the hospital itself. Substantially all of the assets will be contributed to the JV Hospital in exchange for a \$45 million payment from Vanguard and a commitment of the JV Hospital to expend no less than \$55 million on capital items and the development and improvement of ambulatory services in the greater Waterbury community within the next seven years.

The resulting ownership of the JV Hospital will be apportioned 80% to a Vanguard subsidiary and 20% to GWHN's surviving corporation, the Waterbury Hospital Foundation ("the WH Foundation"). GWHN/WH Foundation will purchase this 20% interest for a projected price of \$6.57 million. The following chart depicts the corporate organizational form of the Joint Venture post transaction.



In addition to the 20% equity interest in the JV Hospital, the WH Foundation will have a 50% representation on the JV Hospital's Board of Directors. Thus, the 20% equity interest in the JV Hospital will serve as both a potential source of income for the WH Foundation and a means of exercising influence – albeit limited – on the operations of the JV Hospital.

The JV Hospital will operate in accordance with the “community benefit standard” set forth in Internal Revenue Service Ruling 69-545, which requires the (i) acceptance of all Medicare and Medicaid patients, (ii) acceptance of all emergency patients without regard to ability to pay, (iii) maintenance of an open medical staff, and (iv) promotion of public health, wellness and welfare in the community through the provision of health care at a reasonable cost.

After the closing, GWHN’s surviving corporate entity, the WH Foundation, will continue with the primary purposes of serving as the holder of the 20% interest in the JV Hospital and managing and administering the charitable assets that it will possess post-closing.

C. Summary of Findings and Conclusion: The Proposed Transaction Meets the Requirements of the Conversion Act Provided the Applicants Comply with the Attorney General’s Modifications and Conditions.

1. Findings and Conclusions

Based on our review of the record and the standards set forth in § 19a-486c(a), we conclude that the proposed transaction meets the requirements of the Conversion Act, provided that GWHN, Vanguard, and Tenet comply with the modifications and conditions that are imposed herein.

First, we conclude that the process employed by GWHN in deciding to transfer its assets to a for-profit hospital to be run as a joint venture reflects reasonable and prudent due diligence by GWHN’s Board of Directors. The GWHN board reworked its management team to better equip it to conduct due diligence, sought out the advice of experts, and administered several RFP processes to evaluate and select a transaction partner—all in an effort to serve the

best interests of Waterbury Hospital and the provision of healthcare in the Waterbury community. The Board's efforts have been diligent, without conflicts of interests, and, in our opinion, have complied with its fiduciary obligations to GWHN.

Second, we conclude that GWHN will receive fair market value for its assets as a result of the proposed transaction. Based primarily on the opinions of two independent financial valuation experts, the price negotiated for the sale of GWHN's assets equals or exceeds the price those assets would command in an open and competitive market.⁵ This conclusion is buttressed by the fact that the process followed by the GWHN Board to select a capital partner was itself open and competitive.

Third, assuming compliance with the modifications and conditions set forth below, we conclude that the charitable assets of Waterbury Hospital will be adequately protected and preserved after the proposed transaction closes. The charitable assets of Waterbury Hospital, which have been held in trust for the public, will continue to be held by the WH Foundation and safeguarded for uses to promote healthcare in the Waterbury area. We also conclude that a sum equal to the fair market value of GWHN's assets will be maintained by the WH Foundation and will be restricted to charitable uses consistent with Waterbury Hospital's original purpose

⁵ The nonprofit hospital conversion review process provides the Attorney General 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. GWHN hired Principle Valuation, LLC, for these purposes, and its opinion and updated opinion are included 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 Attorney General retained the services of Navigant Consulting, Inc. ("Navigant Consulting"), to provide an additional independent analysis of the Joint Venture.

and for the support and promotion of healthcare generally in the Waterbury community.

Although the WH Foundation will have an equity interest in the JV Hospital going forward, the conditions required herein will adequately protect the charitable funds in its possession from inuring to the benefit of the for-profit joint venture or to Vanguard, or from being jeopardized by the activities of the for-profit hospital venture.

2. Modifications

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 purposes of the Conversion Act (§ 19a-486b), 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 Joint Venture, that approval is contingent on a number of modifications to the terms of the Joint Venture, and several conditions⁶ to the Joint Venture as a whole, that must be made or met 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, are as follows:

⁶ We use the terms “modification” and “condition” to signify those terms and situations that must be met before the OAG will approve the transaction. The OAG’s authority to approve the transaction with modifications has existed since the passage of the Conversion Act, pursuant to § 19a-486b. As previously stated, the recent addition of language that would allow conditions to be placed on the approval on an application (Public Act 14-168, Sec. 10(b)) does not alter that authority.

1. The Applicants shall notify the OAG in writing of the Closing Date of the Joint Venture within five days of such closing. All references to days in these Modifications and Conditions shall mean calendar days.
2. The Applicants must submit to the OAG, within 30 days of closing, fully executed copies of the Contribution Agreement, the Operating Agreement, and the Management Agreement.
3. Tenet, as the corporate parent of Vanguard, must guarantee each and every obligation of Vanguard as set forth in the Joint Venture.
4. The \$45 million purchase price for GWHN's assets must be financed with operating cash from Vanguard and Tenet.
5. The \$55 million capital commitment must be expended exclusively on projects that relate directly to the JV Hospital and add capital value to it, and not on projects that may benefit other hospitals or more generally the Waterbury area but not the JV Hospital directly. This modification, however, shall not be interpreted to restrict the capital expenditures to projects only on Waterbury Hospital's campus.
6. The JV Hospital shall not be relieved of its \$55 million capital commitment due to changes in federal or state law.
7. Vanguard and/or Tenet is prohibited from selling its interest in the JV Hospital until the full capital commitment has been expended, unless the capital commitment obligation is assumed by the purchaser.
8. The Applicants shall annually account to the OAG for the capital expenditures made to date in fulfillment of the \$55 million capital commitment in the Joint Venture.
9. When the requirements of the indemnity reserve have been fulfilled, and if there remain any funds in the reserve, they shall be added to the Net Charitable Assets⁷ and be treated as such.

⁷ "Net Charitable Assets" means the price paid for the nonprofit hospital's assets minus its debt obligations and the other liabilities it will address using the proceeds from the proposed transaction, which sum will ultimately be restricted as to use.

10. Should the WH Foundation ever cease to hold an equity interest in the JV Hospital, any funds received by the WH Foundation as compensation for its interest shall be added to the Net Charitable Assets and be treated as such.
11. The JV Hospital must provide the OAG, within 90 days of the closing, a final accounting of the transaction that sets forth the balance sheets of GWHN immediately prior to and after the closing, including an analysis of all adjustments post-closing and the resulting net cash assets figure for the WH Foundation. In addition, the Applicants and the JV Hospital must agree to be bound by any adjustments made by the OAG to this figure for purposes of restricting the Net Charitable Assets to charitable purposes only.
12. The Net Charitable Assets, including the earnings therefrom, shall be held by the WH Foundation and used only for the support and promotion of healthcare in the greater Waterbury community. The Net Charitable Assets shall never inure to the benefit of the for-profit JV Hospital. The Net Charitable Assets shall forever be held by the WH Foundation for their intended charitable purposes, unless and until a court of competent jurisdiction orders otherwise. The Net Charitable Assets cannot be used to satisfy any of GWHN's current liabilities that will remain with the WH Foundation.
13. The Net Charitable Assets held by the WH 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").
14. The WH Foundation must account for the Net Charitable Assets separately from other charitable assets in its possession.
15. GWHN must amend section 5(c) of the WH Foundation's draft Certificate of Incorporation ("COI") to read as follows (added language is underlined):

No part of the net earnings of the Foundation shall inure to the benefit of, or be distributable to, its officers, directors, trustees or other private persons, except that the Foundation shall be authorized and empowered to pay reasonable compensation for services rendered, to reimburse reasonable expenses incurred, to purchase goods and services at reasonable prices, but not from the JV Hospital, and to provide programs, services and other benefits, all in furtherance of the exclusively charitable, religious, educational, and/or scientific purposes of the Foundation set forth in Section 3, and to make distribution of its assets upon dissolution as provided for in Section 9.
16. GWHN must add a section 11 to the WH Foundation's COI to address modifications to

the COI. That section 11 shall include the following provision: “Any modifications to Articles 3, 5(c), 9, and 11 of the certificate of incorporation must receive prior written approval by the Attorney General, and, if necessary, additional approval by the Superior Court.”

17. The JV Hospital may not make a Capital Call to the WH Foundation and must remove the Capital Call option from the proposed Operating Agreement.
18. The Karl and Margaret Hallden Memorial Fund should be treated as an unrestricted endowment rather than an unrestricted fully expendable gift.
19. Unless provided for otherwise in the OAG Decision, all gift documents listed in the OAG’s Gift Analysis shall be held by the WH Foundation and shall continue to be used for the charitable purposes set forth by the donors.
20. The following charitable gift funds must be the subject of an approximation action to determine their proper disposition: Chase (3), Hayden (6), Heminway (7), Sarann B. Kazajian Memorial Fund (9), Kingsbury (11), Meigs (12), Merriman (13), Permanent Bed Fund (14), Flora S. Page and George W. Smith (15), Sperry (16), Terry (17), Various Gifts (18), Olive Rogers Warner (19), Bevans (23), Anderson (29), and Kingsbury (32).
21. The following four trusts with gift-over provisions must be the subject of a construction action to determine their proper disposition: Blakesley (30), Dayton (34), Sibilla Hellman Fund (37 and 38), and Kirk (41).

III. PROCEDURAL HISTORY

On January 22, 2013, the Department of Public Health, Office of Health Care Access (“OHCA”) and the OAG received GWHN’s certificate of need determination letter that set forth in summary fashion the terms of the Joint Venture between the Applicants.⁸ Because the OAG determined that the Joint Venture required approval pursuant to the Conversion Act, the OAG

⁸ All docket documents referenced in this opinion can be found on the Attorney General’s website: www.ct.gov/ag.

and OHCA on March 6, 2013, jointly sent the Applicants an Application Form regarding the Joint Venture.

On May 3, 2013, the Applicants submitted their Application for a Joint Venture, which included 21 exhibits. Upon review of the Application, OHCA determined that the Application was not complete, and on May 23, 2013, it requested additional information from the Applicants. On June 11, 2013, the Applicants filed responses to the additional requests set forth by OHCA. The OAG and OHCA determined, on July 1, 2013, that the Application was complete.

At approximately the same time that the Application was deemed complete, Tenet announced that it had entered into an agreement to purchase Vanguard but that Vanguard would maintain its existence as a separate corporate entity. The Applicants confirmed to OHCA and the OAG that the Tenet purchase of Vanguard would not alter the terms of the Joint Venture.

As a condition precedent to Vanguard's entering into the Joint Venture, Section 8.14 of the proposed⁹ Contribution Agreement between Vanguard and GWHN required the passage of a statutory amendment that would allow for the for-profit ownership of medical foundations: "The Connecticut legislature shall have amended the corporate practice of medicine statute to allow for-stock corporations and other for-profit entities, whether incorporated or organized in Connecticut or another jurisdiction, to own medical foundations that employ physicians." (In re

⁹ At this time, the agreement to form a joint venture, in all its parts, between Vanguard and GWHN is still just proposed. Pursuant to Conn. Gen. Stat. § 19a-486a(a), any agreement entered into prior to the OAG's approval shall be void.

Application for Joint Venture Between Greater Waterbury Health Network, Inc. , and Vanguard Health Systems, Inc. , AG Docket 13-486-01, Bates No. 128; hereinafter, “App., ___.”) This condition was asserted by the Applicants as necessary for the Joint Venture because its terms would, if approved, result in the for-profit ownership of Waterbury Hospital Inc.’s medical foundation.

A bill allowing the for-profit corporate practice of medicine was passed by the legislature at the end of the 2013 legislative session. On July 11, 2013, however, Governor Dannel P. Malloy vetoed that bill. Because the Application proposed a structure that was therefore not permitted under state law, the Applicants requested and received a number of extensions of time to supplement their application to modify or otherwise address the structure of the Joint Venture to bring it in compliance with Connecticut law.

In its 2014 session, the legislature took up the issue again, and on June 3, 2014, Gov. Malloy signed into law the “Act Concerning Notice of Acquisitions, Joint Ventures and Affiliations of Group Medical Practices,” which, among other things, permitted the for-profit ownership of medical foundations under certain conditions. Three days later, the Applicants filed their first supplement to the Application, which simply provided that the signed legislation addressed the issue of for-profit ownership of the medical foundation.

In the meantime, the OAG and OHCA became aware, generally, that Tenet was forming a partnership with Yale-New Haven Health Services Corporation (“YNHHSC”) and that the partnership was looking to work together in connection with various healthcare entities in Connecticut. In order to better understand that partnership and its possible impact on the

Application, the OAG and OHCA requested supplemental information of the Applicants, which the Applicants provided on June 27, 2014.

On July 2, 2014, the OAG and OHCA became aware of the proposed transaction between Tenet and Saint Mary's Health System, Inc. ("SMHS"). The OAG issued its first set of interrogatories and requests for production to the Applicants on July 28, 2014. Those interrogatories sought information concerning the Tenet/SMHS proposed transaction as it related to the Vanguard/GWHN application. The Applicants responded on August 18, 2014.

On August 29, 2014, the OAG issued its second set of interrogatories, to which the Applicants responded on September 5, 2014. On October 3, 2014, the OAG issued an additional set of interrogatories in connection with GWHN's gift document analysis. GWHN answered those interrogatories on October 24, 2014.

Three parties moved to intervene in this matter and requested status as either parties and/or intervenors: the Massachusetts Nurses Association (the "MNA"), Connecticut Health Care Associates ("CHCA"), and the Connecticut State Conference of the NAACP Health Committee and the Greater Waterbury Branch of the NAACP Health Committee (the "NAACP"). The MNA was granted intervenor status with limited rights. The CHCA was granted intervenor status with full rights. The NAACP was granted intervenor status with full rights.

The public hearing for the GWHN conversion was held on October 15, 2014, at 1:00 p.m. at the Courtyard by Marriot Waterbury. All parties and intervenors submitted pre-filed testimony for the hearing. The hearing was presided over by representatives from both the OAG and OHCA. Deputy Attorney General Perry Zinn Rowthorn served as the hearing officer for

the OAG. He was assisted by Assistant Attorney General Henry A. Salton and Assistant Attorney General Gary W. Hawes. Attorney Kevin Hansted served as the hearing officer for OHCA. Providing assistance to Attorney Hansted were Kimberly Martone, Director for OHCA, and Steven W. Lazarus, Associate Health Care Analyst.

At the hearing, all parties and intervenors, except one,¹⁰ adopted their pre-filed testimony, and all exhibits on the table of record were entered into the record, some over objection. All parties and intervenors presented testimony and were subject to cross-examination by OHCA, the OAG, and all others with rights of cross examination. After the testimony of the parties and intervenors, the hearing panel heard public comments, 23 in total. In addition, the OAG received nine additional public comments in writing.

The OAG closed its record on October 24, 2014, except for late filed exhibits from the Applicants. The Applicants filed late-filed exhibits with OHCA and the OAG on November 3, 2014, and November 5, 2104.

IV. FINDINGS OF FACT

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

¹⁰ On November 3, 2014, GWHN and Vanguard moved to strike the pre-filed testimony of Lauren M. Bates because it was not adopted at the hearing. On November 7, 2014, the OAG and OHCA denied the motion.

A. Parties and other relevant corporate entities

GWHN is a Connecticut non-stock, 501(c)(3) corporation and is the parent company and sole member of Waterbury Hospital, Inc. GWHN's mission is, "[t]o support and encourage the development of comprehensive, integrated, healthcare related services for the advancement of the health and well-being of the general public by providing financial, management and other assistance to its affiliates including Waterbury Hospital, Inc." (App., 6.)

Waterbury Hospital, Inc., in operation since 1890, is a 357-licensed bed (excluding bassinets) acute-care teaching hospital, which provides a full range of inpatient, outpatient and ancillary services in the city of Waterbury near the junctions of Route 8 and Interstate 84. In fiscal year 2012, Waterbury Hospital, Inc., admitted 11,399 inpatients, delivered 965 newborns, had 56,730 Emergency Department visits, and performed 2,544 inpatient surgeries and 4,920 outpatient surgeries.

Waterbury Hospital, Inc., itself, has interests in several affiliated entities. Alliance Medical Group, Inc. ("AMG") is a tax-exempt 501(c)(3) medical foundation and is wholly owned by Waterbury Hospital, Inc. AMG employs more than 100 physicians and health care providers practicing in emergency and internal medicine, pediatric and adolescent medicine, breast surgery, general surgery, endocrinology, pulmonary, rheumatology, infectious disease/travel medicine and sleep medicine.

The Greater Waterbury Imaging Center Limited Partnership is a Connecticut limited partnership formed to develop and operate a medical diagnostic imaging center. Waterbury Hospital, Inc., is a 64% general partner of the Imaging Center.

Access Rehab Centers LLC (“Access”) is owned by Waterbury Hospital (65%) and Easter Seal Rehabilitation of Greater Waterbury, Inc. (35%). It offers outpatient physical, occupational, and speech therapy to adults and children at ten locations. Access also provides physical therapy services on an inpatient basis to Waterbury Hospital.

Imaging Partners, LLC, is a limited liability company owned by Waterbury Hospital (85%) and a private radiology practice, Diagnostic Radiology Associates, LLC (15%).

Waterbury Gastroenterological Co-Management Company, LLC, is a limited liability company that was established to provide management services to Waterbury Hospital, Inc., in connection with Waterbury Hospital’s gastroenterology service line. Waterbury Hospital, Inc., is the sole Class H member of the LLC. The physician owners are Class P members.

Cardiology Associates of Greater Waterbury, LLC, is wholly owned by Waterbury Hospital. The practice is comprised of eight employed board certified cardiologists, three of whom are interventional cardiologists. The practice has approximately 20,000 active patients.

In addition to the above subsidiaries, Waterbury Hospital has two joint ventures with SMHS that provide specialty services: the Harold Leever Regional Cancer Center, Inc. (“HLRCC”) and the Heart Center of Greater Waterbury, Inc. (“HCGW”). Waterbury Hospital’s interests in the HLRCC and the HCGW will not be transferred to the JV Hospital as a part of the Joint Venture. Those interests will be retained by the WH Foundation.

With respect to GWHN’s subsidiaries, Greater Waterbury Health Services, Inc., is a wholly-owned subsidiary of GWHN. Currently, there is neither business activity nor assets in this subsidiary.

VNA Health at Home, Inc., (“VNA”) has been wholly owned by GWHN since 1996. “VNA is a home health care agency that provides skilled nursing care, speech, physical and occupational therapy, medical social work, and hospice care throughout the greater Waterbury region.” (App., 10.)

Greater Waterbury Management Resources, Inc. (“GWMRI”), a taxable corporation, is a medical service organization and is wholly owned by GWHN. However, there has been minimal activity in GWMRI since the formation of AMG, Waterbury Hospital’s medical foundation.

Valley Imaging, LLC (“Valley Imaging”) is owned by GWMRI (49%) and Diagnostic Radiology Associates, LLC (“DRA”) (51%). Valley Imaging offers open MRI Scanning services to outpatients in the service area.

The Children’s Center of Greater Waterbury Health Network, Inc. (“CCGWHN”), is wholly-owned by GWHN and will not be transferred to the JV Hospital. It will be retained by the WH Foundation.

Healthcare Alliance Insurance Company, Ltd. (“HAIC”) is a captive insurance company owned jointly by Griffin Health Services, Inc., Milford Health and Medical, Inc., and GWHN. Each has a third interest in HAIC. HAIC offers professional malpractice and general liability insurance coverage to its owners and members of their respective medical staffs. GWHN will not transfer its interest in HAIC to the JV Hospital. It will be retained by the WH Foundation

Vanguard is based in Nashville, Tennessee, and owns and operates 28 acute care and specialty hospitals with complementary facilities and services in Arizona, Illinois, Massachusetts, Michigan, and Texas. Vanguard is wholly owned by Tenet.

Tenet is an investor-owned, publicly traded company whose subsidiaries and affiliates operate regionally focused, integrated healthcare delivery networks. Tenet operates 80 hospitals and approximately 200 outpatient centers.

B. GWHN's Fiscal Condition

The evidence in the record reveals that GWHN has faced serious financial difficulties since the turn of the century. From 2006 through 2011, GWHN experienced five consecutive years of losses, ranging from \$2.5 million to \$17.8 million. In an effort to address its fiscal concerns, GWHN engaged Kaufman Hall in 2005 to evaluate the economics of consolidating Waterbury Hospital and Saint Mary's Hospital. Kaufman Hall concluded that even a consolidated institution would struggle financially. Despite this assessment, however, in 2006, Waterbury Hospital and SMH discussed the possibility of an affiliation between the hospitals. The collaboration never materialized.

In 2007, in response to the growing challenges facing the hospitals in Waterbury, OHCA conducted a special study of the status of healthcare services in the city. OHCA concluded that both hospitals were "in financial distress, had aged facilities, and lacked access to capital." (App., 21.) The options identified by the report were either to consolidate the two hospitals or to close Saint Mary's Hospital. Accordingly, discussions between the two hospitals resumed in 2007 and continued into 2008. However, the hospitals were not able to reach an agreement on terms or to secure sufficient capital to fund a possible merger.

Then, in 2008, a deep recession hit the United States. GWHN experienced lower healthcare utilization and, therefore, significant financial difficulty, which led to a default on its

bond covenants in 2009. As part of the subsequent negotiations with its bondholders, GWHN hired Price Waterhouse Coopers, LLC (“PWC”) to identify the challenges and risks for GWHN, to define operational improvements for GWHN, to define revenue cycle improvements, and to set physician initiatives. PWC recommended strategies for improving GWHN’s performance, but GWHN achieved only limited success in doing so.

In 2010 Kaufman Hall was once again retained, but this time with the purpose to identify near-term capital needs. Kaufman Hall identified over \$50 million in necessary capital improvements over the next five years to keep Waterbury Hospital operational. GWHN simply did not have access to such capital and could not secure it in the open market.

In late 2010, Waterbury Hospital refinanced its CHEFA debt in a private offering, but was nevertheless unable to stave off GWHN’s fiscal decline. GWHN’s financial difficulties and its serious capital needs resulted in its reconsidering its goal of remaining independent.¹¹

C. The Search for Solutions and Partners

“GWHN’s ability to achieve its mission and fulfill its long range plan had been impeded by limited access to capital, inadequate reimbursement from third party payors, aging facilities, an unfavorable payor mix, and an accrued pension liability.” (App., 20.) Beginning in 2011, the

¹¹ Also, in response to GWHN’s struggles, the Board ultimately realigned the GWHN executive team in 2011.

In the first six months, this new team reduced expenses by \$6 million, instituted service improvements, improved core measures, and made modest capital improvements as a result of the savings gained by successfully refinancing its tax exempt debt. However, these improvements were not enough to secure the long-term resources required to sustain the current health system.

(App., 21.)

GWHN Board took a series of deliberate steps to identify, evaluate and select a capital partner that ultimately resulted in its decision to approve the Joint Venture.

GWHN engaged a health care investment banker, Cain Brothers, to help assess the options available to address GWHN's capital needs. Cain Brothers has extensive experience advising nonprofit hospitals on strategic alternatives and knowledge of the Connecticut healthcare market. GWHN formed a task force specifically assigned to work with Cain Brothers to pursue a capital partner and formally explore strategic options.

In its first attempt to join forces with a capital partner, GWHN agreed to form a joint venture with LHP Hospital Group, Inc. ("LHP"), and SMHS that would have created a united health system in Waterbury with one new state-of-the-art hospital. The LHP joint venture agreement was the product of a process pursuant to which 14 prospective partners were approached and four written proposals were received. On August 23, 2012, the joint venture was submitted to both the OAG and OHCA for review pursuant to the Conversion Act, but it became clear as the review proceeded that there were significant impediments to the proposed joint venture. As a result, LHP terminated the proposed joint venture in August of 2012.

Immediately thereafter, the GWHN Board reconvened and directed Cain Brothers to seek new additional proposals from other prospective capital partners. Eleven parties were contacted for possible partnership. Two submitted proposals. This second process resulted in GWHN's selection of Vanguard as its capital partner and a joint venture as the preferred transaction.

In the fall of 2013, Vanguard was acquired by Tenet. Upon learning of the acquisition, GWHN met with Cain Brothers to learn about Tenet and to discuss the implications of the purchase. In addition, GWHN's CEO, the Board Chair, and the VP of medical affairs visited two of Tenet's hospitals that are similar in size to Waterbury Hospital to examine the company's approach to operating its hospitals.

In the spring of 2014, Tenet announced its intention to acquire the assets of SMHS. At that time, GWHN sought the advice of Cain Brothers and Principle Valuation LLC regarding the effect the SMHS transaction would have on the governance of the JV Hospital, the purchase price for GWHN's assets, and the other terms and conditions of the transaction. GWHN concluded that it continued to be satisfied with the proposed transaction.

D. The Proposed Transaction

GWHN and Tenet, through its wholly-owned subsidiary, Vanguard, have proposed to form VHS Waterbury Health System, LLC (the JV Hospital), a for-profit joint venture that will own and operate Waterbury Hospital. GWHN will contribute the assets of Waterbury Hospital, Inc., and certain affiliates to the JV Hospital in exchange for \$45 million and the commitment of the JV Hospital to expend no less than \$55 million on capital items in support of, among other things, the immediate capital needs of Waterbury Hospital, capital renovations at Waterbury Hospital, physician recruitment, and the development and improvement of ambulatory services

in the greater Waterbury community over seven years. GWHN will then purchase a 20% interest in the Joint Venture for a projected price of \$6.57 million.¹²

The \$45 million purchase price is subject to a potential working capital adjustment to the extent the net book value of the Hospital's net working capital varies from \$6.8 million as of the closing date. As of August 31, 2014, the book value of the GWHN's net working capital was approximately \$22 million.

Waterbury Hospital, Inc.'s entities that will be contributed to the Joint Venture are Waterbury Hospital, Inc.; Alliance Medical Group, Inc.; Greater Waterbury Imaging Center, LP; Access Rehab Centers, LLC; Imaging Partners, LLC; Valley Imaging Partners, LLC; Cardiology Associates of Greater Waterbury, LLC; VNA Health at Home, Inc.; and Waterbury Gastroenterological Co-Management Company, LLC (Class H members). GWHN will not contribute to the JV Hospital the following entities: the Harold Leever Regional Cancer Center; the Heart Center of Greater Waterbury, Inc.; the Children's Center of Greater Waterbury; and the Healthcare Alliance Insurance Co., Ltd.

As part of the transaction, the JV Hospital will assume certain liabilities, including accounts payable, accrued expenses, pension liability for Waterbury Hospital's cash benefit plan, asbestos abatement liability, and capital lease debt. GWHN will also retain certain liabilities, including long-term debt, workers' compensation, pension liability for the CHCA's defined benefit plan, and medical malpractice.

¹² The exact purchase price will be determined after the transaction closes because the purchase price is dependent upon the value of the liabilities that the JV Hospital will assume at the time of Close.

The JV Hospital will operate in accordance with the “community benefit standard” required of tax-exempt hospitals as set forth in Internal Revenue Service Ruling 69-545, including without limitation, the (i) acceptance of all Medicare and Medicaid patients, (ii) acceptance of all emergency patients without regard to ability to pay, (iii) maintenance of an open medical staff, and (iv) promotion of public health, wellness and welfare in the community through the provision of health care at a reasonable cost. The JV Hospital will also follow charity care and uncompensated care policies at least as favorable to patients as those currently maintained by GWHN.

Following the closing, the JV Hospital will be governed by a board of directors (the “JV Hospital Board”). The JV Hospital Board will have oversight and ultimate authority over the affairs of the JV Hospital. The JV Hospital Board will be composed of twelve (12) board members, six (6) of whom will be elected or appointed by GWHN and six (6) of whom will be elected or appointed by Vanguard. The JV Hospital Board can act only with an affirmative vote of a majority of the GWHN elected directors and an affirmative vote of the Vanguard elected directors.

The JV Hospital Board’s approval will be required for the following corporate acts, among others:

- modifying or discontinuing the provision of any Essential Service;
- adopting, modifying, or terminating any indigent care, charity care or conflict of interest policy;
- appointing a local Board of Trustees;
- changing the general character of the business anticipated to be conducted by the JV Hospital (it being understood and agreed that such business is the development,

ownership, and operation of health care related facilities and the delivery of health care services);

- approving the merger, consolidation, dissolution or Bankruptcy, or the sale of all or substantially all of the assets, of the JV Hospital; and
- establishing or changing the mission, values or purposes of the JV Hospital.

(App., 167.)

Pursuant to the Joint Venture, the JV Hospital Board would appoint a local Board of Trustees to oversee the operating activities of the Facilities. Six members of the Board of Trustees will be physicians from the active medical staff of Waterbury Hospital; the other six members will be local community leaders. The CEO of the JV Hospital is to serve as an *ex officio*, non-voting member of the Board of Trustees. The Board of Trustees will be responsible for:

(a) participating in the adoption of a vision, mission, and values statement for the Hospital Businesses; (b) participating in development and review of operating and capital budgets and facility planning for the Hospital Businesses and advising the Board of Directors with respect to the same (it being understood that ultimate authority for budgets and planning resides with the Board of Directors); (c) monitoring quality and performance improvement at the Hospital Businesses; (d) granting medical staff privileges and, when necessary and with the advice of counsel, taking disciplinary action consistent with the Hospital's Medical Staff Bylaws; (e) assuring medical staff compliance with Joint Commission requirements (with the advice of counsel); (f) providing advice and consultation regarding physician recruitment efforts; (g) fostering community relationships and identifying service and educational opportunities; and (h) performing such other activities and duties as may be directed or delegated to it by the Board of Directors.

(App., 169-70.)

The JV Hospital will enter into a management agreement (the "Management Agreement") with VHS Waterbury Management Company, LLC ("VHS Management"), pursuant to which VHS Management will perform financial, technical, managerial, and administrative

support services for the JV Hospital. The Management Agreement has an initial term of five years and will automatically renew for successive terms of five years each.

E. The Charitable Assets of Waterbury Hospital

Throughout its history, Waterbury Hospital, Inc., has received numerous charitable gifts, legacies and devises from generous individual donors and community fundraising efforts.¹³ As part of its Application, GWHN provided information and documentation of the charitable trusts and gifts of which it is the beneficiary or in which it claims an interest. Specifically, it provided copies of the gift documents themselves and a spreadsheet (the “Gift Analysis”) 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 use restricted and spending restricted. The value of all the charitable gifts as of September 30, 2014, was \$62,117,108.

The OAG has reviewed the Gift Analysis provided by GWHN and placed each gift in one of six different categories of documents. The first four groups include gifts that are held by Waterbury Hospital, Inc.: Restricted Endowments, Unrestricted Endowments, Restricted Fully Expendable Gifts (temporary restricted assets), and Unrestricted Fully Expendable Gifts. The two remaining groups—Trusts held by third party trustees and Future Interests—are not held

¹³ Waterbury Hospital, Inc., and not GWHN, holds all of Waterbury Hospital’s charitable funds.

by Waterbury Hospital, Inc. We have attached to our decision, as Exhibit B, the Gift Analysis, as modified by the OAG, and copies of the gift documents tabbed for references.¹⁴

1. Restricted Endowments

Restricted 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 a specific purpose such as free beds, indigent care, a building fund, or a particular program of the hospital.

The following gifts are restricted endowments:¹⁵ Anderson (1), At Risk Kids (2), Chase (3), Crozier (4), Fulling (5), Hayden (6), Heminway (7), Junior League Fund (8), Kazanjian Memorial Fund (9), Kazanjian Student Nurse Scholarship Fund (10), Kingsbury (11), Meigs (12), Nursing School Alumnae (13), Permanent Bed Fund (14),¹⁶ Flora S. Page and George W. Smith (15), Sperry (16), Terry (17), Various Gifts (18), and Olive Rogers Warner (19). As of September 30, 2014, the total value of these restricted endowments was \$10,896,213.

One of the restricted endowments, the Permanent Bed Fund, is comprised of 61

¹⁴ We include this exhibit in our decision to provide a definitive reference document for all gift documents held by Waterbury Hospital, Inc., at the time of the conversion.

¹⁵ The numbers following the gifts represent the tabs in Gift Analysis, attached hereto.

¹⁶ Although the Gift Analysis provided by GWHN does not provide a separate review of each bed fund, it did provide a list of the individual funds, with accompanying gift documents, from which it derived the value of the Permanent Bed Fund.

individual funds, created either through trusts or will bequests. Based on the responses to our discovery requests, we were able to determine that the Permanent Bed Fund contains the following funds: Adt (54), Benedict (55), Bristol (56), Bronson (57), Burdsall and Burritt Bed Fund (58), Edith & Melrose Burritt Bed Fund (58), Castle (59), Coffin (60), Curtis (61), Driggs (62), First Church Guild (63), Fitzsimons (64), Goss (65), Graves (66), Greenberg (67), Gross (68), Hart (69), Hill (70), Judson (71), Kazanjian (72), Kellogg (73), Kimble (74), Beth Kirk Memorial Fund (75), Henry and Bethia Kirk Fund (76), Margaret Kirk Bed Fund (77), Leavenworth (78), Lewis (79), Lott (80), Merchant (81), Helen Merriman Bed Fund (82), William Buckingham Merriman and Sarah Kingsbury Parsons Merriman Bed Fund (83), William Buckingham Merriman, Jr. Bed Fund (83), Charlotte B. Merriman (84), Minor and Northrop (85), Mitchell (86), Montague (87), Peck (88), Pomeroy and Hill (89), Poole (90), Powell (91), Rosemary (92), Scovill (93), Shipley (94), Skilton (95), C. Sanford Bull Memorial Fund (96), J. Richard Smith Memorial Bed Fund (96), Elizabeth L. Spencer (97), Julia V. Warner Spencer Fund (98), Julia V. Warner Spencer Memorial for Miss Emaline D. Warner Fund (98), Stiles (99), Stone (100), Swenson (101), Terry (102), Tuttle (103), Second Congregations Church (104), Wade (105), Oscar Warner (106), Welton (107), Whiton and Upson (108), J.H. Whittemore Endowed Room (109) and Julia S. Whittemore Memorial Room (110). The Permanent Bed Fund is valued at \$5,210,209 as of September 30, 2014.

2. 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 hospital’s “general purposes,” “general expenses,” “general fund,” or used “at the discretion of the board.”

The following gifts are unrestricted endowments: Brooker (20), Forester (21), and Karl & Margaret Hallden Memorial Fund (22). As of September 30, 2014, the total value of these unrestricted endowments was \$362,122.

3. Restricted, Fully Expendable Gifts

The third category includes restricted, fully expendable Gifts. These are funds not structured as endowments, and therefore fully expendable to be administered and used by the hospital for restricted purposes specified by the donor.

The following gifts are restricted, fully expendable gifts: Bevans (23) and Mayo (24). As of September 30, 2014, the total value of these unrestricted endowments was \$22,149.

4. Unrestricted, Fully Expendable Gifts

The fourth category of gift assets held by Waterbury Hospital, Inc. are Unrestricted Fully Expendable Gifts, which are not structured as endowments, and therefore fully expendable, to be administered and used by the hospital for its general purposes.

The following gifts are unrestricted fully expendable gifts: Crean (25), General Endowment Fund (26), Gift Annuity (27), and Pooled Income Fund (28). As of September 30,

2014, the total value of these unrestricted funds was \$2,144,025.¹⁷

5. Third Party Trusts

The fifth category of gift assets is Trusts held by third party trustees—trusts created and held by a third party, a portion of the annual income of which is designated for donation to Waterbury Hospital, Inc., to be used for one or more of its charter purposes. Within this category, there are two subsets: third party trusts with use restrictions and those without.

The following gifts are third party trusts with use restrictions:

The **Harriet S. Anderson Trust (29)** is currently held and administered by trustee Bank of America, and was established by a trust agreement, dated September 21, 1943. The agreement provides that upon the death of the last survivor of the initial beneficiaries of the trust, the net income shall be paid to Waterbury Hospital “to provide or assist in providing hospital care to deserving and needy residents of the City of Waterbury, Connecticut.” Waterbury Hospital, Inc. currently receives these funds.

The **Augustus M. and Albert J. Blakesley Fund (30)** is currently held and administered by trustee JP Morgan Chase, and was established by Article 26 of the will of Edyth A. Blakesley, dated March 8, 1961. Pursuant to Article 26, the rest, residue, and remainder of the estate of Edyth A. Blakesley passed to the trustee to be held in trust for the benefit of Waterbury Hospital “to be used by it as a Free Bed Fund for the benefit of members of The Second Congregational Church of Waterbury, Inc., who are considered by the Trustees of The Second Congregational Church of Waterbury, Inc., as worthy ill cases requiring financial assistance.” The will further provided that “[i]n the event that said The Waterbury Hospital shall be merged into or taken over by another private, nonprofit hospital, the said Trustee shall make payment to the successor corporation. In the event that the said The Waterbury Hospital shall terminate its existence the said Trustee shall have the power to send such income to such hospital, operating in the City of Waterbury, or serving the public of the City of Waterbury, as it may, in its judgment, select.” Waterbury Hospital, Inc. currently receives these funds.

The **Hopkins Memorial Fund (31)** is currently held and administered by trustee Bank of America, and was established under Article 7 of the will of Abbie C. Hopkins. Pursuant to Article

¹⁷ This value does not include the Crean fund as a value for that fund was not provided to us from GWHN.

7 of the will, the rest, residue, and remainder of the estate of Abbie C. Hopkins passed to the trustee to be held in trust for the benefit of a number of individual and corporate beneficiaries. The remainder of the net income was to be added to the principal and invested for a period of twenty years after the death of Abbie C. Hopkins. A provision of the will provided that, if at the termination of the twenty year period, a new Naugatuck Hospital had not been built, the net income from the fund would be given to Waterbury Hospital "for the purpose of providing accommodations and medical care and attention for the poor and needy residents of the Borough of Naugatuck aforesaid, with the understanding, however, that the surplus of said income, if any, may be used by The Waterbury Hospital aforesaid for its general uses and purposes." A new Naugatuck Hospital was not built. Waterbury Hospital, Inc. currently receives these funds.

The **Mary Kingsbury Bull Fund (32)** is currently held and administered by trustee Bank of America, and was established by a gift of U.S. Government Bonds from Edith Kingsbury and a trust agreement between Waterbury Hospital and the Colonial Trust Company, dated January 24, 1951. The gift summary memorializing the gift indicates that the gift was made to furnish and provide an endowment of the Children's Ward of Waterbury Hospital. Waterbury Hospital, Inc. currently receives these funds.

The **Warner Memorial Fund (33)** is currently held and administered by trustee Bank of America, and was established under Article 9 of the will of Oscar L. Warner, dated February 29, 1932. Pursuant to Article 9 of the will, the rest, residue, and remainder of the estate of Oscar L. Warner passed to the trustee to be held in trust for the benefit of his sister, Lucia B. Warner, for her lifetime. A provision in the will provided that after the death of Lucia B. Warner, the remainder of the net income was to be added to the principal and invested for a period of twenty years. At the termination of the twenty year period, if a new Naugatuck Hospital had not been built, the net income from the fund was to be given to Waterbury Hospital "for the purpose of providing accommodations and medical care and attention for the poor and needy residents of the Borough of Naugatuck aforesaid, with the understanding, however, that the surplus of said income, if any, may be used by The Waterbury Hospital aforesaid for its general uses and purposes." A new Naugatuck Hospital was not built during that 20 year period. Waterbury Hospital, Inc. currently receives these funds.

The following are third party trusts without use restrictions:

The **Almon B. Dayton Trust (34)** is currently held and administered by trustee Bank of America, and was established under Article 11 of the Will of Almon B. Dayton. Pursuant to Article 11, upon the death of his wife, one-fifth of the net annual income of the trust was to be paid to his niece, Marjorie D. Hitchcock Eller, for her lifetime. Upon the death of Ms. Eller, equal shares of her share of the net income were to be are paid annually in equal shares to

Waterbury Hospital, Waterbury Anti-Tuberculosis League of Waterbury, Inc., and Gaylord Farm Sanitorium, in perpetuity. Waterbury Hospital, Inc. currently receives these funds. The will provides that if Waterbury Hospital ceases to exist or relinquishes its corporate charter, or fails for any reason to function in the territory in which it is now located, its share of the income will pass to the Waterbury Foundation, Inc. to be used by the directors of the Foundation for religious or charitable purposes, preferably for some use similar to its use by Waterbury Hospital.

The **John Elton Trust (35)** is currently held and administered by trustee Bank of America, and was established under Paragraph 6 of the will of John P. Elton, dated November 29, 1946. Pursuant to a codicil to the will, dated June 26, 1947, \$100,000 was to be held in trust with the net income to be used, first, for the benefit of Otto Nilson and his wife, Elizabeth Deborah Steele Elton, and upon her death, for the benefit of Ida Johnson, and upon her death, for the benefit of Gustav Johnson. Upon the death of Gustav Johnson, the entire net income was to be given in equal shares to Waterbury Hospital and St. John's Parish of the Protestant Episcopal Church. Waterbury Hospital, Inc. currently receives these funds.

The **I. Kent Fulton Trust (36)** is currently held and administered by trustee Bank of America, and was established under Articles 10 and 14 of the will of I. Kent Fulton, dated October 2, 1939. Pursuant to Article 10, \$25,000 passed to the trustee to be held in trust for the benefit of Waterbury Hospital. Pursuant to Article 14, the rest, residue, and remainder of his estate was to be held in trust, first for the benefit of his wife, Elizabeth Warner Fulton, and, upon her death, for the benefit of his son, Wells Fulton. Upon the death of Wells Fulton, Waterbury Hospital was to receive one-sixth of the principal of the remaining trust to be placed in the trust that had been established in Article 10. A subsequent codicil, dated December 15, 1939, did not affect the bequest to Waterbury Hospital. Waterbury Hospital, Inc. currently receives these funds.

The **Sibillia Hellmann Fund (37 and 38)** is currently held and administered by trustee Bank of America, and was established under Article 4 of the will of Charles M. Hellman, dated June 13, 1955. Pursuant to Article 4, half of the estate of Charles M. Hellman passed to the trustee to be held in trust for the following beneficiaries: Ernest M. Meister, the wife of Charles M. Hellman (Rhoda Hellmann), Robert W. Mackey, Sophie Reichenbach Stage, Mary Reichenbach Parsons, and Julius Reichenbach. Upon the death of those beneficiaries, the remaining principal was to be renamed the Sibilla Hellmann Fund, and the income was to be divided equally between Waterbury Hospital and St. Mary's Hospital. Article 4 further provides: "In the event that either hospital goes out of existence, the entire net income shall be paid to the remaining hospital. If either hospital shall merge with another hospital and my Trustees believe that the corporation so formed carries out the purposes of the hospital so merged, then my Trustees shall pay one-half of the income to such amalgamated corporation, but if my Trustee believes that the amalgamated corporation does not carry out the purposes of the

hospital so merged and mentioned herein, then the entire income shall be paid to the remaining hospital.”

In addition, pursuant to Article 3 of the will of Charles M. Hellmann, the other half of the estate passed to the trustee to be held in trust for his wife, Rhoda M. Hellmann. Under that same Article, Rhoda Hellmann was further given the power of appointment over the corpus of the Article 3 trust estate. Rhoda Hellmann then exercised the authority granted to her under the will of Charles M. Hellmann under Article 6 of her will, dated November 11, 1969 as modified by codicils dated June 24, 1971, May 21, 1980 and May 23, 1980 by making several specific bequests to charitable organizations. Pursuant to Article 6, Section H, all of the rest, residue, and remainder of the property over which she held a power of appointment was to be passed in trust to the existing Sibilla Hellmann Fund in perpetuity to be divided equally between the Waterbury Hospital and St. Mary’s Hospital. Article 6, Section H further stated that if Waterbury Hospital was not an organization described in Sections 170 (a), 2055 (a) and 2522 (a) of the Internal Revenue Code or had ceased to exist when income was to be distributed to it, the trustee was instructed to distribute all of the income to St. Mary’s Hospital. If neither Waterbury Hospital nor St. Mary’s Hospital qualified under the abovementioned sections, the trustee was instructed to distribute the income to “such other organizations in the health care field as are described in said sections 170 (a), 2055 (a) and 2522 (a) as the Trustee shall select.” Waterbury Hospital, Inc. currently receives their share of these funds under the will of Rhoda M. Hellmann.

The **Frank Keeling Fund (39)** is currently held and administered by trustee Bank of America, and was established under Article 12 of the will of Frank Keeling, dated December 15, 1954. Pursuant to Article 12, the rest, residue, and remainder of the estate of Frank Keeling passed to a trustee to be held in trust for the benefit of Lillie Keeling Wurtenberg, Pauline T. Smith and Leita S. Hull. Upon the death of the last survivor, the original trust was terminated and a new trust was created, known as “The Frank Keeling Fund” for the benefit of Waterbury Hospital. Waterbury Hospital, Inc., currently receives these funds.

The **Jacob Keeling Fund (40)** is currently held and administered by trustee Bank of America, and was established under Article 10 of the will of Jacob Keeling, dated June 30, 1952. Pursuant to Article 10 of the will of Jacob Keeling, the rest, residue, and remainder of the estate of Jacob Keeling passed to a trustee to be held in trust for the benefit of Frank Keeling, Lillie Keeling Wurtenberg, Pauline T. Smith and Leita S. Hull. Upon the death of the last survivor, the original trust was terminated and a new trust was created, known as “The Jacob Keeling Fund” for the benefit of Waterbury Hospital. Waterbury Hospital, Inc. currently receives these funds.

The **Harriet Kirk Trust (41)** is currently held and administered by trustee JP Morgan Chase, and was established under Article 3 of the will of Harriet Kirk, dated June 15, 1942. Pursuant to Article 3, the rest, residue, and remainder of the estate of Harriet Kirk passed to the

trustee in trust, wherein Waterbury Hospital was to receive a 1/10 share. Article 3 further provided: "In the event that said corporation goes out of existence, then said income shall be divided equally among the other corporations and associations mentioned in Section B; but, if said corporation shall merge with any other corporation and my Trustee believes that the corporation so formed carries out the purposes of The Waterbury Hospital, Inc., then my Trustee shall pay the net income to such amalgamated corporation, but, if my Trustee believes that the amalgamated corporation does not carry out the purposes of The Waterbury Hospital, Inc., then the net income shall be divided equally among the other charitable and eleemosynary corporations and association mentioned in Section B. Waterbury Hospital, Inc. currently receives its share of these funds.

The **George B. Lambe and Harriet Welton Lambe Endowment Fund (42)** is currently held and administered by trustee Bank of America, and was established by a trust agreement, dated July 12, 1923, between George R. Lamb and The Colonial Trust Company, and an unsigned trust agreement between Waterbury Hospital and The Colonial Bank and Trust Company. The July 12, 1923 agreement provided that upon the death of George Lamb, or his wife, the trust terminated and the corpus of the trust was given to Waterbury Hospital as part of a permanent endowment to the Hospital. Waterbury Hospital subsequently entered into a trust agreement with Colonial Bank and Trust Company, whereby Colonial Bank became the trustee of the endowment fund.

The **Henry H. Peck Trust (43)** is currently held and administered by trustee Bank of America, and was established under Article 18 of the will of Henry H. Peck, dated June 12, 1918. Pursuant to Article 18, the rest, residue, and remainder of the estate of Henry H. Peck was to be divided into four equal shares. One share was to be held in trust for the benefit of Waterbury Hospital. A second share was to be held in trust for the benefit of Lucy A. Peck. Upon the death of Lucy A. Peck, her share would be added to the trust previously established under Article 18 for Waterbury Hospital. Waterbury Hospital would receive the remaining two shares if Clarence P. Bradley, the nephew of Henry H. Peck, predeceased him without issue, and Harriet E. Bradley, sister of Henry H. Peck, predeceased him. Waterbury Hospital, Inc. currently receives its share of these funds.

The **Francis A. and Florence A. Poole Fund (44)** is currently held and administered by trustee Bank of America, and was established under Article 9 of the will of Edith F. Poole, dated April 11, 1928. Pursuant to Article 9, following the death of the last survivor of the beneficiaries named in her will, the trust that had been created for their benefit would continue to be held by the trustee, minus a \$10,000 distribution of the principal of the trust fund to be given directly to Waterbury Hospital pursuant to Article 8 of her will to be known as the "Francis A. and Florence A. Poole Fund." The net income of the Article 9 trust was to be divided equally between the Second Congregational Church and Waterbury Hospital. Waterbury Hospital

currently receives its share of these funds.

The **Howard Easton Smith Fund (45)** is currently held and administered by trustee Bank of America, and was established under Articles 11 and 12 of the Will of W. Easton Smith, dated May 31, 1944. Pursuant to Article 11, should any of the organizations named in Articles 8 (Waterbury Visiting Nurses Association), 9 (Waterbury Day Nursery Association) or 10 (Boy Scouts of America) that received the net income from trusts held by the trustee “dissolve, terminate or cease to carry on their corporate purposes,” the income is, instead, to be paid to Waterbury Hospital. Pursuant to Article 12, the rest, residue, and remainder of the estate of W. Easton Smith was to be paid over, in the case of Waterbury Hospital and St. John’s Parish of the Protestant Episcopal Church, or held in trust, in the case of Waterbury Visiting Nurses Association, Waterbury Day Nursery Association, and Boy Scouts of America and divided proportionally between the organizations. Waterbury Hospital currently receives its share of these funds.

6. Future Interests

A final category of charitable assets is Future Interests, where gifts are either held in charitable remainder trusts (including charitable remainder unitrusts or annuity trusts, held by outside banks or trustees, in which the Hospital has no current income or principal interest) or provided as contingent remainders in wills. The future interests held by third party trustees are as follows:

The **Natalie M. Dodd Trust (49)** is currently held and administered by trustee JP Morgan & Co., and was established by an amended trust agreement between Natalie M. Dodd and Morgan Guaranty Trust Company of New York, dated May 18, 1976, and Article 4 of the will of Natalie M. Dodd, dated May 18, 1976. Pursuant to Article 4 of the will of Natalie M. Dodd, the rest, residue, and remainder of her estate passed to the trustee. Pursuant to the amended trust agreement, dated May 18, 1976, Waterbury Hospital receives 15 percent of the principal from trust under two scenarios: (1) upon the death of Natalie M. Dodd if Paul G. Heroux and his wife, Lynn D. Heroux, do not survive her and (2) upon the deaths of Paul G. and Lynn D. Heroux if they do survive Natalie M. Dodd.

The **Fenn Trust (50)** is currently held and administered by trustee Stanhope Fenn Cunningham, and was established under Article 5 of the will of J. Lincoln Fenn, dated October 23, 1950. Pursuant to Article 5, upon the death of all of the named beneficiaries in the will, Waterbury Hospital will receive one-fifth of the rest, residue, and remainder of the estate of J.

Lincoln Fenn to be added to its principal fund and “that only the income be used for the general purposes” of the Hospital.

The **Gibson Trust (51)** is currently held and administered by trustee JP Morgan Chase, and was established under the will of Donald F. Gibson, dated September 24, 1983.¹⁸ After the death of his wife, Ann J. Gibson, Waterbury Hospital will receive 6.67 percent of a portion of the principal of a trust created under Article 3 of the will. Pursuant to Article 4 of the will, Waterbury Hospital will receive 6.67% of one-half of a different trust that was created for the benefit of Ann J. Gibson and a number of other beneficiaries following their deaths.

The **Snowden Trust (52)** is currently held and administered by trustee Comerica Bank, and was established by a trust agreement between Wilma A. Snowden and Bank of Boston, dated October 25, 1984, and amendment dated December 27, 1990. Pursuant to the amended trust agreement, after the death of Wilma A. Snowden and the death of several named beneficiaries, the trustee will pay over to Waterbury Hospital one-ninth (1/9) of the remaining balance of the trust.

The **Stoughton Trust (53)** is currently held and administered by trustee Bank of American, and was established under Article 7 of the will of Kenneth T. Stoughton, dated June 13, 1977. Pursuant to Article 7, pursuant after the death of Paul L. Baraby, the trustee shall pay over to Waterbury Hospital the entire corpus of the remaining trust “to be added to the equipment fund, in memory of my beloved wife, Katherine Thornton Stoughton.”

The identified future interests that are not held by a third party trustee are as follows:
Lenners (46), Pecka (47), and Queor (48).

V. LEGAL ANALYSIS AND REQUIRED MODIFICATIONS

As explained above, the Conversion Act 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. With particular respect to the Attorney General’s

¹⁸ The will is dated September 24, 1985, but the witness affidavit is dated September 24, 1983.

review, the Conversion Act requires that he shall disapprove a proposed sale of a nonprofit hospital to a for-profit entity as not in the public interest if he determines the existence of one or more of nine criteria specified in § 19a-486c. The Conversion Act, however, permits the Attorney General to approve an application while setting forth modifications that would bring the proposed transaction into compliance with Act – that is, with modifications designed to cure the failure to meet the criteria specified in § 19a-486c. What follows, therefore, is the OAG’s analysis and discussion of the statutory criteria in § 19a-486c and the modifications to the Joint Venture that are necessary to address 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 V.H.4.e of this decision, we conclude that the Joint Venture is not prohibited by statutory or common law governing nonprofit entities, trusts, or charities.

B. GWHN 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 GWHN Board exercised in deciding to enter into the Joint Venture with Vanguard.

Based upon our and our expert’s review of the materials presented as a part of the GWHN application, it is clear that GWHN undertook an extensive and diligent process to explore strategic options and to identify a capital alternative that would enable it to address its deteriorating financial position and continue its mission of providing quality healthcare to the Waterbury community.¹⁹ GWHN’s efforts extended over a ten-year period, from 2005 to 2014, and included consultation with two experienced healthcare investment banking firms in Kaufman Hall & Associates and Cain Brothers, as well as the nationally recognized healthcare consulting firm of PricewaterhouseCoopers. GWHN 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. GWHN exercised due diligence in deciding to participate in the Joint Venture.

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 the assets of GWHN. The record supports the reasonableness

¹⁹ Navigant Consulting’s report is attached hereto as Exhibit A.

of the decision by GWHN to transfer substantially all of its assets as a means to assure the long-term viability of Waterbury Hospital.

GWHN engaged in a decision-making process that was reasonable, thoughtful, and thorough. In making the ultimate decision to transfer its assets, GWHN demonstrated due diligence under the circumstances. As noted in the findings of fact, GWHN pursued a broad range of strategic initiatives to address the hospital's operating losses, aging facilities, and limited access to capital. It sought a range of options including a merger with SMHS, an operational restructuring and realignment, and a private placement in the bond market. After a decade of failed alternatives, the GWHN Board reasonably concluded that an appropriate solution to provide long-term viability of the hospital was a sale or joint-venture with a for-profit operator. We, therefore, conclude that GWHN exercised due diligence in deciding to transfer its assets as a part of the Joint Venture transaction.

2. GWHN exercised due diligence in selecting Vanguard as a Joint Venture partner.

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, GWHN has established that it exercised due diligence in selecting Vanguard as its partner in the Joint Venture.

The full history of GWHN's difficult search for a capital partner is described in the findings of fact. With respect to the initiative that resulted in the Joint Venture with Vanguard, however, GWHN took appropriate and deliberate steps to identify the best situation for Waterbury Hospital. GWHN retained Cain Brothers to solicit possible capital partners. It

reviewed Cain Brothers's solicitation process, the nature and capabilities of the parties contacted for a possible partnership, and the terms of all proposals received. GWHN also spent considerable effort on its choice to seek a joint venture transaction rather than a straight sale of assets.

In addition, GWHN met with Cain Brothers and legal counsel upon learning that Vanguard was being acquired by Tenet, to discuss the implications of the acquisition. Subsequently, the Waterbury CEO, Board Chair, and VP of Medical Affairs visited Good Samaritan and Saint Mary's Hospitals in West Palm Beach, Florida, to better understand Tenet's approach to operating its hospitals. During this August 2013 visit, the Waterbury representatives toured the facilities, met with their counterparts at these hospitals, and also met with physicians and board members of these hospitals.

Although we recognize—and in no way discount—the concerns raised by the intervenors about Tenet, none was sufficiently concrete or proximate to compel the conclusion that the GWHN Board failed to exercise due diligence in selecting a purchaser of its assets. GWHN's due diligence was comprehensive and included consideration of Tenet's regulatory compliance and corporate citizenship history. Moreover, consistent with the fact that the OAG's review under the Conversion Act pertains generally to the protection of charitable assets, we considered whether GWHN reasonably evaluated Tenet's financial wherewithal to comply with the negotiated terms of the transaction, and it did. Last, OHCA's jurisdiction and review encompasses the purchaser's role in the delivery of healthcare services in the Waterbury area going forward.

GWHN exercised due diligence in selecting Vanguard as its partner for the Joint Venture and in confirming that selection after Tenet's purchase of Vanguard. Because Tenet purchased Vanguard subsequent to the Application being submitted to our office, however, we require as a condition of our approval of the proposed Joint Venture that Tenet, as the corporate parent of Vanguard, guarantee the performance and satisfaction of each and every obligation of Vanguard as set forth in the Joint Venture.

3. GWHN 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 (also known as a "fairness opinion") from an independent person expert in such agreements.

GWHN sought a firm to perform its independent fairness evaluation through an RFP process. From the three proposals received, GWHN selected Principle Valuation LLC ("Principle Valuation") to perform the fairness opinion. Principle Valuation has extensive hospital valuation experience regarding valuations to meet regulatory compliance needs. In addition, neither Principle Valuation nor its staff members have any known conflicts of interest with the parties to the transaction or to the transaction itself. Lastly, Principle Valuation's fees for its services were not dependent on the opinion it rendered.

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

4. GWHN exercised due diligence in negotiating the terms and conditions of the Joint Venture.

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.

GWHN retained Cain Brothers to evaluate the proposals it received from potential capital partners and to negotiate key elements of the proposals with the prospective partners. GWHN then evaluated the competing proposals and chose Vanguard as a capital partner. In addition, as a result of GWHN's deteriorating financial position, GWHN was able to renegotiate the initial capital terms of the deal, increasing the purchase price from \$25 million to \$45 million and reducing the capital commitment from \$75 million to \$55 million. Most importantly, we note that GWHN had limited leverage for negotiations given its deteriorating financial condition but was able to negotiate a transaction that recapitalized Waterbury Hospital to stabilize current operations and provide a source of capital for long term growth.

C. No GWHN Board Member, Officer, Key Employee, or Expert Has a Conflict of Interest With Respect to the Joint Venture.

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 GWHN, the purchaser, or any other party to the transaction. We conclude that no conflicts of interest exist that would require disapproval of the Joint Venture.

The Applicants provided the OAG with individual conflict of interest statements for each relevant individual (board member, officer, etc.) employed by GWHN and its experts and Vanguard. Later, Tenet provided conflict of interest statements to the OAG. 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.

After a careful review of all the conflict of interest responses, there do not appear to be any conflicts of interest relating to the proposed transaction among board members, officers, key employees, and experts retained by GWHN, Vanguard, or Tenet. 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 Joint Venture. Accordingly, we conclude that no conflicts of interest exist that would require disapproval of the Joint Venture.

D. GWHN 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).

Vanguard has agreed to pay \$45 million as compensation for GWHN's contribution of substantially all of its assets to the JV Hospital. Two independent financial experts have reviewed the transaction to determine whether GWHN will receive fair market value for its assets, and both have concluded that the purchase price of \$45 million equals or exceeds the fair market value of GWHN's assets.

As discussed above, GWHN retained Principle Valuation to provide it with an independent fairness opinion regarding the transaction.²⁰ Principle Valuation considered the three principal methods of valuation: the Cost Approach (Adjusted Book Value Approach), the Market Approach, and the Income Approach. With respect to the market based value approach to valuation, Principle Valuation used both a Guideline Company Approach and a Guideline Transaction Approach. After considering the strengths and weaknesses of each approach, and assigning a representative weight to each of the approaches, Principle Valuation derived an overall weighted value for GWHN's assets of \$27.8 million. As such, Principle Valuation was able to conclude in its fairness opinion that the \$45 million given as consideration for GWHN's assets is fair from a financial point of view to GWHN.

Navigant Consulting, Inc. ("Navigant Consulting"), was hired through an RFP process to be the OAG's financial expert for the purposes of reviewing certain aspects of the proposed

²⁰ The OAG has previously concluded that GWHN exercised due diligence in selecting Principle Valuation to perform the independent fairness evaluation on its behalf.

transaction. Navigant Consulting has also concluded that GWHN will receive fair market value for the transfer of its assets. In performing its fair market value analysis, Navigant Consulting also considered the three generally accepted approaches to value: income, market, and cost. In addition, Navigant Consulting concluded that GWHN and its assets should be valued under the premise of “value-in-place” and not as a “going concern.”²¹

The value-in-place premise of value was also consistent with the premise of value assumed in Principle Valuation’s fairness opinion analysis of GWHN on a standalone basis as evidenced by the absence of positive projected cash flow in its discounted cash flow method.

Navigant Consulting performed an independent fair market valuation of GWHN’s real and personal property and added this to GWHN’s current net working capital balance as of August 31, 2014. Under this analysis, and including only a working capital figure of \$6.8 million, Navigant Consulting concluded that GWHN will contribute assets valued at \$44,300,000 in exchange for the purchase price of \$45,000,000. Navigant’s analysis supports the conclusion that GWHN will receive fair market value for the transfer of its assets.

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

²¹ The premise of value-in-place assumes that the Hospital’s assets are in place, but not as part of a going-concern business enterprise. Furthermore, this premise of value assumes that all assets will continue to be used in the manner for which they were originally intended, which assumption is consistent with Vanguard’s stated intent to operate Waterbury Hospital as a general acute care hospital with similar levels and types of services.

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.

Both independent financial experts have concluded that the fair market value of the nonprofit hospital's assets has not been manipulated. Principle Valuation performed reviews of GWHN's financials and assets and found no indication that the fair market value of GWHN's assets had been manipulated. Navigant Consulting also conducted a thorough review of GWHN's assets and financials and concluded that the fair market value of GWHN's assets had not been manipulated.

No intervenor or other participant in the proceeding has offered any evidence that the fair market value of GWHN's assets has been manipulated to artificially lower the payment price. Based on these factors, we conclude that the fair market value of GWHN's assets has not been manipulated.

F. The financing of the transaction will not place Waterbury Hospital'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 Joint Venture 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.” *Sharon*, p. 64.

Additionally, as set forth in the Joint Venture, the WH Foundation is choosing to invest a projected \$6.57 million of its net assets to purchase a 20% interest in the JV Hospital. The OAG has a direct interest in protecting the value of the net assets because under certain of the provisions in the proposed Operating Agreement, the WH Foundation may choose to relinquish—or Vanguard may choose to purchase—the WH Foundation’s 20% interest in the Joint Venture. Should either of those options be exercised, the fair market value of the 20% equity interest in the JV Hospital at that time will become a cash asset of the WH Foundation. If this occurs, those funds will become restricted Net Charitable Assets as if they had been included as part of the net assets at the time of the conversion transaction.²²

Based upon the record, and subject to the conditions and modifications discussed below, we conclude that the financing of this transaction will not place GWHN’s assets at risk. Vanguard and Tenet have confirmed on the record that the \$45 million purchase price for GWHN’s assets will be financed with operating cash from the Vanguard/Tenet Health System. There will be no debt financing of the purchase price. As such, the assets of GWHN will not be

²² Conditions regarding GWHN’s net assets from the proposed transaction are discussed below.

placed at an unreasonable risk due to the financing of the transaction. To ensure the protection of GWHN's assets, however, we require as a condition of our approval of the proposed transaction that the \$45 million purchase price for GWHN's assets must be financed with operating cash from Vanguard and Tenet.

The other concern of the OAG regarding the security of GWHN's assets going forward, however, involves the \$55 million capital commitment of the JV Hospital. The Applicants state that the JV Hospital is committed to expend no less than \$55 million on capital items and the development of improvement of ambulatory services in the greater Waterbury community within seven years of closing.

Based upon testimony at the hearing, we understand that this capital commitment is an obligation of the Joint Venture and will be financed from either the operating cash of the Joint Venture or the line of credit that will be established for the benefit of the Joint Venture. In addition, we learned from testimony at the hearing that the capital commitment is not viewed by Tenet necessarily as committed or intended exclusively for the benefit of the JV Hospital. Although certain facility and equipment capital needs of the JV Hospital will be met by the use of this investment, the applicants have not committed to using all of it for such purposes and, instead, appear to anticipate that some portion of the capital commitment may be used more generally to benefit healthcare in the Waterbury community, e.g., "to invest in additional services throughout the community—ambulatory, physician recruitment, etc.—so that \$55 million commitment is not limited to the four walls of the hospital." (Testimony of Trip Pilgrim, Hearing Transcript, p. 135; hereinafter "Pilgrim, ____".) This more expansive conception of the capital

commitment, while perhaps worthy, does not comport with the terms of the deal negotiated by GWHN.

Relatedly, while discussing Vanguard's and Tenet's capital commitments to Saint Mary's Hospital, Tenet's representatives testified that the \$85 million capital commitment set forth in Tenet's Asset Purchase Agreement with SMHS is regarded by Tenet as including the \$55 million capital commitment in the Joint Venture with GWHN. Tenet explained: "So there's 85 million in capital commitment that's maxed out by Tenet. There's \$85 million of capital investment that is going to be made in this time frame in Waterbury, Connecticut, for facility improvement, renovations, life safety issues, ambulatory platform, physician recruitment." (Pilgrim, 147-148.) Given these and other comments during the hearing, it is clear that Tenet intends to treat the GWHN and SMHS transactions as resulting in a common owner of two distinct hospital campuses, with a common capital commitment. (Pilgrim, 112.)

However, this characterization is inconsistent with the interests of the WH Foundation, which mandate a different conception of the \$55 million capital commitment. The WH Foundation will maintain its 20% ownership interest in the JV Hospital, which means that it has a claim to 20% of the fair market value of the JV Hospital going forward. In other words, the \$55 million capital commitment that GWHN negotiated is partly (20%, or \$11 million) its own investment in the JV Hospital. GWHN clearly would not have negotiated an agreement to spend its own cash from operations, or to borrow on a line of credit on which it is obligated, to benefit any entity other than the JV Hospital. In other words, the \$55 million capital

commitment to Waterbury Hospital was a key term of the consideration received by GWHN in this transaction, and it must be honored.

The independent expert opinions support this conclusion. In its fairness opinion, Principle Valuation identified the capital commitment as a key element of the transaction. “[The JV Hospital] will make a commitment to spend \$55,000,000 in capital or other approved commitments to the Hospital Business over a seven year time frame.” (App., 741.) Of note is Principle Valuation’s reference that the investment would be made to the “Hospital Business” and not to improve healthcare in the Waterbury area more generally. Additionally, Navigant Consulting’s financial valuation of GWHN emphasized the dire capital needs of Waterbury Hospital: “There is a backlog of routine capital expenditures that need to be made, along with renovations to the aging building infrastructure, and strategic capital needed to improve the operations of the Hospital.” (Navigant Consulting Report, p. 51.) The JV Hospital needs the \$55 million capital investment, and the evidence in the record supports the conclusion that the \$55 million capital commitment provision requires that the capital expenditures would be spent exclusively for the direct benefit of the JV Hospital.

Therefore, as a condition of approval of the proposed transaction, we require that the following conditions be met in connection with the \$55 million capital commitment: The \$55 million capital commitment must be expended to add capital value exclusively to the JV Hospital. The JV Hospital must receive the direct capital benefit from the \$55 million because it will either be spending its own cash from operations or be borrowing from its line of credit,

both of which are expenditures of the JV Hospital. Those expenditures cannot benefit another corporate entity.

In addition, despite the terms of the proposed Operating Agreement, Vanguard will not be relieved of its \$55 million capital commitment if the federal or state legal landscape governing the JV Hospital changes in the future. Section 2.7 of the proposed Operating Agreement provides:

The Company shall commit to expend not less than \$55 million dollars on capital items and the development and improvement of ambulatory services in the greater Waterbury community by not later than seven (7) years after Closing. Notwithstanding the above capital commitment, in the event that any legal requirement is enacted or imposed after the Closing Date that discriminates against, or adversely affects a disproportionate number of, for-stock hospitals or other for-profit health care entities, or causes the Company to suffer a material decline in consolidated earnings before interest, taxes, depreciation and amortization on a consolidated basis, then the Company shall be relieved of its obligation to provide the above capital commitment and shall be required to consult with the Board of Trustees to determine an alternate mutually agreeable capital commitment of the Company that is reasonable and appropriate in light of the changed circumstances caused by the new legal requirement.

Although Vanguard may wish to insure against future changes in the legal landscape, it cannot hold the JV Hospital's capital investment hostage by such a provision. To do so would render the \$55 million capital commitment – a key term of the deal – illusory, subject to evaporation upon the future actions of legislators. Put differently, in the terms of the Conversion Act, we believe that the nonprofit hospital's assets, and the promised investment in them, should not bear the risk of future legislation. The \$55 million capital commitment is indeed a commitment, and it must be honored. Accordingly, the OAG requires that the

Applicants modify section 2.7 of the proposed Operating Agreement to delete the second sentence of the section.

Vanguard and/or Tenet is prohibited from selling its interest in the JV Hospital until the full capital commitment has been expended, unless the capital commitment obligations, including this one, are passed on to the purchaser. This condition follows from the OAG's interest in assuring that the nonprofit hospital's assets are not put at risk and also that the charitable funds are preserved. In the event that Vanguard or Tenet decides to divest itself of the 80% interest in the JV Hospital, the OAG must ensure that the capital commitment has been met or that the obligation is passed on to the purchaser. In short, a change of ownership will not change the JV Hospital's \$55 million capital commitment.

So that the OAG can confirm that the conditions set forth here relating to the capital commitment have been met, the OAG requires that the Applicants annually account to the OAG for the capital expenditures made to date in fulfillment of the \$55 million capital commitment in the Joint Venture.

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. Both independent financial experts have determined that the management contract is within a

reasonable range of fair market value, and no contrary evidence exists in the record.

Accordingly, we conclude that the proposed management contract is for reasonably fair value.

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

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.

Conn. Gen. Stat. § 19a-486c(a)(8).

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 Joint Venture. 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 GWHN and identify any approximation and/or equitable deviation needs in connection with these assets.

1. A Sum Equal to the Fair Market Value of Waterbury Hospital is Being Transferred to the Conversion Foundation.

The term “fair market value” is used in several places in subsection (a) of § 19a-486c. As discussed in the *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.

By contrast, subsection (8) of the statute requires that a sum equal to the fair market value of Waterbury Hospital’s assets be transferred and preserved for charitable healthcare purposes. In this context, though, fair market value is calculated somewhat differently than it is for purposes of subsection (4). This is because fair market value is determined under subsection (4) without taking into account the nonprofit hospital’s liabilities—that is to say, as the gross asset value. If fair market value were computed for purposes of (8) as it is for subsection (4), the nonprofit hospital might be left transferring to a conversion foundation the proceeds of its sale, having those proceeds restricted for charitable purposes only, but leaving

the foundation no ability to pay off its liabilities post-closing. Such a result is nonsensical, because a primary goal of a nonprofit hospital's sale of assets—as pointedly exemplified here—is likely to be to extinguish corporate liabilities. For example, in the case of GWHN, both its long-term bond debt and pension obligations will be resolved with proceeds from the sale of its assets.²³

The definition of fair market value for purposes of subsection (8), therefore, is more appropriately the price paid for the nonprofit hospital's assets minus the amount of its debt obligations and other liabilities it will resolve using the proceeds of the proposed transaction. In other words, fair market value equals the net asset value of the nonprofit hospital. *Sharon*, p. 69.²⁴ With respect to GWHN, the net asset value calculation must take into account all retained assets and liabilities, including 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, any payor liabilities and obligations from reporting periods prior to closing, and the CHCA pension obligation.

In the context of the Joint Venture, however, there are two allotments of net assets that will not be available immediately for their intended charitable purposes but should be added to

²³ Another way to understand this calculation is to view the retained liabilities as a direct result of the provision of health care services, and therefore, the payment of these liabilities is consistent with one of the acceptable uses of charitable foundation funds under the statute: "for the support and promotion of health care generally in the affected community." § 19a-486c(a)(8)(B)(ii).

²⁴ The net asset value of GWHN becomes the Net Charitable Assets, which are to be used only for the support and promotion of health care in the greater Waterbury community. The Net Charitable Assets and the restrictions thereon are discussed in detail below.

the sum of net assets if they become available. First, the Joint Venture requires the WH Foundation to maintain an indemnity reserve to satisfy any indemnification obligations it may have in connection with the transaction. The indemnity reserve will be funded from the WH Foundation's net assets. As such, when the requirements of the indemnity reserve have been fulfilled, and if there remain any funds in the reserve, they shall be added to the net asset value of GWHN and restricted identically.

Second, as discussed above, GWHN will purchase its 20% equity interest in the JV Hospital with net assets. Accordingly, should the WH Foundation ever cease to hold an equity interest in the JV Hospital, any funds received by the WH Foundation as compensation for the fair market value of its interest in the JV Hospital shall be added to the net asset value of GWHN and restricted identically.

Because the final net asset value of the nonprofit hospital cannot be precisely calculated prior to the actual closing of the transaction, the determination of the fair market value for the purposes of subsection (8) must await a post-closing accounting. Accordingly, a condition of approval for the proposed transaction is that the Applicants must provide the OAG, within 90 days of the closing, a final accounting of the transaction that sets forth the balance sheets of GWHN immediately prior to and after the closing, including an analysis of all adjustments post-closing and the resulting net cash assets figures for the WH Foundation. In addition, Vanguard and GWHN must agree to be bound by any adjustments made by the OAG to this figure for purposes of restricting the assets to charitable purposes only.

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.” § 19a-486c. For the purposes of this decision, we refer to the recipient of the net assets and the charitable gifts generally as a “conversion foundation.”

There are two options for a conversion foundation under the Conversion Act. The first type of conversion foundation that can hold the charitable assets of the nonprofit hospital going forward is 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. It has no affiliation by corporate structure, by governance, or by membership. § 19a-486c(a)(8)(A). This type of conversion foundation was the only kind permissible under the law when the OAG issued its decision in *Sharon*.

In 2004, the legislature amended the Conversion Act to permit another type of conversion foundation, which is codified in the “unless” clause in § 19a-486c(a)(8)(A): “. . . 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.” This provision allows the nonprofit hospital, in essence, to function as a charitable foundation and to hold charitable assets as long as it continues to operate on a nonprofit basis. We refer to these

types of conversion foundations as “continuing conversion foundations.” To qualify as a continuing conversion foundation under the statute, therefore, a nonprofit hospital must maintain its corporate existence after the transaction, continue to qualify for nonprofit, tax-exempt status, and continue to serve the healthcare needs of the community in which it previously existed.

A continuing conversion foundation does not have to meet the same statutory requirements as an independent conversion foundation. First, it does not need to comply with the anti-affiliation provisions regarding structure, governance, and membership. Additionally, a continuing conversion foundation does not need to be approved by the superior court, as would an independent conversion foundation. Neither of these requirements are set forth in the “unless” clause. The continuity of structure and governance of the nonprofit hospital and its nonprofit purpose and identity provide adequate assurance that it will continue to serve the healthcare needs of the community.

Because a continuing conversion foundation does not require approval by the superior court, however, does not mean that the OAG lacks authority to ensure that its charitable assets are properly protected. First, the Conversion Act specifically provides that the Attorney General “may place any conditions on the approval of an application that relate to the purposes of [the Conversion Act].” § 19a-486b(b). As explained above, the OAG’s role in a Conversion Act review encompasses the protection of charitable assets. Conditions relating to that purpose, therefore, are authorized under the Conversion Act.

In addition, though, independent of the Conversion Act, the Attorney General has jurisdiction to protect the public's interests in gifts made for charitable or public purposes. See Conn. Gen. Stat. § 3-125. It is pursuant to this jurisdiction that the OAG can require modifications to the structure of a continuing conversion foundation.

We now turn to the specifics of the conversion foundation anticipated in this Joint Venture. The Applicants have proposed that Waterbury Hospital, Inc. will retain its corporate identity and will continue to operate as a nonprofit organization, albeit as a hybrid—one part a conversion foundation and the holder of charitable assets, and one part a 20% equity interest member of the JV Hospital. Specifically, GWHN will merge into Waterbury Hospital, Inc., and then Waterbury Hospital, Inc. will restructure itself and change its name. The responsibilities of the WH Foundation are proposed to be as follows:

- To participate as the 20% owner of the JV;
- To manage the charitable assets remaining and to receive the investment income of those charitable assets held by third parties and restricted to use by the Hospital;
- To ensure that the JV conducts hospital operations in a manner consistent with the “community benefit standard” set forth in IRS Revenue Ruling 69-545;
- To manage the remaining assets and liabilities, including the Harold Leever Regional Cancer Center; the Heart Center of Greater Waterbury, Inc.; the Children’s Center of Greater Waterbury; and the Healthcare Alliance Insurance Co., Ltd.;
- To support charitable health related activities in the community in addition to those that will continue to be provided through the JV’s operation of the hospital in accordance with the community benefit standard; and
- To provide economic support for health care by accessing grants and using funds to purchase services from health care providers.

The initial question, therefore, is whether GWHN’s proposed nonprofit organization meets the standards of the Conversion Act.

The WH Foundation clearly does not qualify as an independent conversion foundation under the statute because it maintains multiple affiliations with the nonprofit hospital and the purchaser. With respect to corporate structure, the WH Foundation is a 20% equity owner of the JV Hospital. With respect to corporate governance, the WH Foundation seats six members on the JV board. With respect to membership, the WH Foundation is a class B member of the JV Hospital. The WH Foundation must therefore qualify as a continuing conversion foundation to be approved.

GWHN has submitted a draft COI and draft bylaws for the WH Foundation. As noted above, Waterbury Hospital, Inc. will not dissolve after the transfer of assets to the JV Hospital. Rather, it will continue its existence as the WH Foundation and, among other things, will serve the healthcare needs of the Waterbury community. The WH Foundation will also maintain its nonprofit status as a hospital pursuant to section 170(b)(1)(A)(iii) of the Internal Revenue Code because of its role as a member of the JV Hospital. We conclude, therefore, that the WH Foundation qualifies as a continuing conversion foundation.

However, as discussed in the following section, the OAG will require amendments to the draft COI to approve the transaction.

3. Certain Protections are Necessary to Ensure that the Full Net Asset Value is Protected for Use by the WH Foundation for Charitable Healthcare Purposes.

Even though the WH Foundation qualifies as a continuing conversion foundation, there exist issues concerning the protection of charitable assets that must be addressed if the proposed transaction is to be approved. The Conversion Act requires that the net asset value of

the nonprofit hospital that is transferred to the WH Foundation be used “[f]or appropriate charitable health care purposes consistent with the nonprofit hospital’s original purpose [or] for the support and promotion of health care generally in the affected community” Conn. Gen. Stat. §§ 19a-486c(a)(8)(B)(i) and (ii). Accordingly, as a condition of approval of the proposed transaction, the OAG requires that a sum equal to the net asset value of the nonprofit hospital shall be held by the WH Foundation as charitable assets to be used only for the support and promotion of health care in the greater Waterbury community.²⁵ These assets, and the earnings therefrom (the “Net Charitable Assets”), shall never inure to the benefit of the for-profit JV Hospital and shall forever be held by the WH Foundation for their intended charitable purposes, unless and until a court of competent jurisdiction orders otherwise. Moreover, because this sum ultimately takes into account all outstanding liabilities of GWHN, the net assets cannot be used to satisfy any of the current liabilities that will remain with the WH Foundation.²⁶

In addition to the use restriction set forth above, and as a condition to the OAG’s approval of the Joint Venture, the net charitable assets held by the WH Foundation shall be

²⁵ These assets and the net earnings therefrom may not be used for the administrative costs of the WH Foundation. They are to be used exclusively for their charitable purpose. The WH Foundation will receive unrestricted income from the gift documents that can be used for its administrative costs.

²⁶ As noted above, any funds remaining in the indemnity reserve shall be added to the net charitable assets. In addition, if the WH Foundation’s interest in the JV Hospital is bought out, the proceeds from that sale should also be added to the net charitable assets.

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.

We must note that the WH Foundation may receive funding from other sources that will not be subject to the above charitable restrictions. These restrictions relate only to the Net Charitable Assets. The WH Foundation, therefore, must account for the Net Charitable Assets separately from other of its assets. And, of course, because it is a tax-exempt organization, the WH Foundation will need to comply with the IRS’s restrictions on the use of its funds regardless of the OAG’s conditions set forth herein.

As additional support for the requirement that these charitable assets remain separate from and do not benefit the JV Hospital, the OAG requires the following two modifications to the WH Foundation’s draft COI.

First, GWHN must amend section 5(c) of the draft COI to read as follows (added language is underlined):

No part of the net earnings of the Foundation shall inure to the benefit of, or be distributable to, its officers, directors, trustees or other private persons, except that the Foundation shall be authorized and empowered to pay reasonable compensation for services rendered, to reimburse reasonable expenses incurred, to purchase goods and services at reasonable prices, but not from the JV Hospital, and to provide programs, services and other benefits, all in furtherance of the exclusively charitable, religious, educational, and/or scientific purposes of the Foundation set forth in Section 3, and to make distribution of its assets upon dissolution as provided for in Section 9.

Second, GWHN must add a section 11 to the COI concerning modifications to the COI, which shall include the following provision: “Any modifications to Articles 3, 5(c), 9, and 11 of

the certificate of incorporation must receive prior written approval by the Attorney General, and, if necessary, additional approval by the Superior Court.” Because GWHN has submitted a draft COI in its Application, approval of the transaction is conditioned upon the receipt of a COI in final form.

Our final concern with respect to protecting the charitable assets of the WH Foundation concerns the right of the manager to call for additional capital contributions from the members of the JV Hospital (a “Capital Call”) to fund the working capital needs of the JV Hospital, as set forth in section 3.2 of the proposed Operating Agreement. The WH Foundation’s assets will fall into one of two main categories. They will either be retained cash assets that are designated for use to address the retained liabilities or will be restricted charitable assets. If the retained cash assets are already designated for use to pay off liabilities, and they will be, then the only funds available to fulfill a Capital Call would be charitable assets. Such a circumstance would be unacceptable.

The primary reason that GWHN sought a capital partner in the first place was that it lacked access to capital to meet its needs going forward. Indeed, Vanguard pointed to its access to both the equity and debt markets as one of the key advantages it would bring to the provision of healthcare in the Waterbury area.²⁷ It is difficult to believe that Vanguard should ever need to turn to the WH Foundation for additional capital to run the JV Hospital. And it

²⁷ “What is the difference between being investor-owned and not-for-profit? We can access the equity markets. We also access the debt markets, but it gives us the kind of flexibility that we need to be able to sustain upturns, downturns in the economy” (Pilgrim, 60.)

appears that in the Tenet joint ventures in which such a provision has existed, it never has: “in the other joint ventures that we have done across the country, we’ve never had a capital call.” (Pilgrim, 153.)

What makes the Capital Call even more problematic is its ability to reduce the WH Foundation’s representation on the Board of the JV Hospital. If the WH Foundation is unable to meet the manager’s Capital Call, which is foreseeable in light of GWHN’s current capital shortage, Vanguard has the option to contribute nonetheless, and “the relative Percentage Interests of the members shall be adjusted to reflect the Capital Contributions actually made by the Members.” (App., 159.) If the WH Foundation’s percentage interest slips below 20%, its representation on the Board drops from 50% with a block voting requirement²⁸ to a maximum of 25% without block voting. As such, the Capital Call provision, through the relative percentage interest of the members, has the power to undercut a primary goal of GWHN; namely, sufficient Board representation to ensure a continuing community engagement with the JV Hospital.

This provision risks putting GWHN in the untenable position of *either* contributing charitable assets to the for profit JV Hospital *or* protecting those assets by refusing a capital call at the cost of reducing its control and ownership interests in the JV Venture received as consideration in this transaction. Based upon these significant concerns with the existing

²⁸ In Section 5.1(c) of the proposed Operating Agreement provides that for an action to constitute an action of the board, a majority of both 6 member groups (the WH Foundation members and the Vanguard members) must affirmatively approve the action.

option of a Capital Call, and the unlikelihood that it would ever be exercised, the OAG requires that the Applicants remove the Capital Call option from the proposed Operating Agreement as a condition of approval of the Joint Venture.

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

Our final area of concern is to ensure that the charitable assets of Waterbury Hospital, Inc., which have been held in trust for the public, are safeguarded and used for the promotion of healthcare in the area served by Waterbury Hospital after the sale of GWHN's assets to Vanguard. 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 Waterbury Hospital'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 the WH Foundation retains all of Waterbury Hospital's charitable gifts and trusts to which it is entitled under the statute. Second, this review ensures that GWHN's analysis and treatment of charitable funds in the Application correctly interprets the donors' charitable use restrictions so that the donations may remain with the WH Foundation subject to any "use restriction imposed by a donor, [and] for a purpose consistent with the intent of said donor." Conn. Gen. Stat. § 19a-486c(a)(8)(B)(iii). Third, 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 the WH 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, GWHN provided a review and analysis of its charitable gifts and endowments. GWHN 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 Waterbury Hospital. The purpose of the OAG's request was to obtain the information necessary to: (1) review the gift instrument for each of Waterbury Hospital's gifts to determine whether its language would permit the gift to remain with the WH Foundation, or whether a reverter clause or gift-over provision would be triggered by the Joint Venture that would require the donation to revert to the donor's heirs-at-law or pass to another charity selected by the donor or the trustee; 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, such as free beds, charity care, maintenance, a building fund, or research.

c. Amount Stated by Hospital in Application

GWHN has stated that as of September 30, 2014, the WH Foundation would retain approximately \$60,221,161 in charitable assets, plus an additional \$1,895,947 in endowment

funds. Thus, according to its figures, a total of \$62,117,108 in charitable gifts will remain with the WH Foundation.²⁹

d. GWHN's Charitable Gifts and Trusts.

We have inventoried the gift documents in section 5 in the Findings of Facts. Generally, of the funds being held by Waterbury Hospital, (1) 19 funds are classified as Restricted Endowments, with a value of \$10,896,213; (2) 3 funds are classified as Unrestricted Endowments, with a value of \$362,122; (3) 2 funds are classified as being Restricted Fully Expendable Gifts, with a value of \$22,149; and (4) 4 funds are classified as Unrestricted Fully Expendable Gifts, with a value of \$2,144,025.³⁰ There are 16 trusts held by outside banks, with a value of \$48,692,599.³¹ The Hospital classified 8 gifts as future interests, with no current value. That inventory provides the basis for our analysis in this section, in which we discuss a few corrections to the Gift Analysis provided by GWHN and the proper disposition of the gifts under the circumstances of this case.

²⁹ As previously discussed, the WH Foundation will receive GWHN's net assets to be used exclusively for charitable healthcare purposes. An exact figure for net assets must await a final account post-close.

³⁰ In Gift Analysis provided by GWHN, Olive Rogers Warner (19) and Gift Annuity (28) appeared to be improperly classified as unrestricted and held by a third party trustee, respectively. Upon further review, however, we determined that the erroneous classifications were scrivener's errors, and treated them as they should have been classified: Olive Rogers Warner (19) as restricted, and Gift Annuity (28) as being held by Waterbury Hospital.

³¹ Although there are 16 trusts, 17 gift documents exist to fund those trusts because two wills, those of Charles Hellmann and Rhoda Hellmann, made bequests in trust to the Sibilla Hellmann Fund.

- i. The Karl and Margaret Hallden Memorial Fund should be characterized as an unrestricted endowment.

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 only may appropriate for expenditure or accumulate so much of an endowment fund as the institution determines to be prudent for the uses, benefits, purposes and during 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 part of the documentation supporting the Karl and Margaret Hallden Memorial Fund (22), GWHN provided the will of Karl W. Hallden, dated July 26, 1967, a letter from Colonial Bank, trustee of the testamentary trust created by Karl W. Hallden, dated December 20, 1985, a Consent to Distribution Agreement between Waterbury Hospital and Colonial Bank, as trustee, dated June 1, 1986, and a partially executed agreement between Waterbury Hospital and Colonial Bank, dated September, 1986.

Pursuant to Article 3 of the will of Karl W. Hallden, the rest, residue, and remainder of his estate passed to the trustee to be held in a revocable trust for the benefit of his wife, Margaret M. Hallden, for her lifetime. The will also gave the trustee “all powers necessary” to make any changes to the trust for the tax benefit of Margaret M. Hallden. One of these changes was to terminate the trust. Both the July 1985 letter and the Consent to Distribution

Agreement contain an explanation for the termination of the trust and subsequent distribution of the assets of the trust. Specifically, Waterbury Hospital, Inc. was to receive 37.5% of the assets of the trusts “to be held . . . as an endowment fund and the income only to be used for the general purposes of [Waterbury Hospital].”

Waterbury Hospital, Inc. received its share and, thereafter, entered into an agreement with Colonial Bank whereby Colonial Bank would be the agent of the Karl and Margaret Hallden Memorial Fund. The agreement further stated: “It is understood that the title to all property shall remain in [Waterbury Hospital], and that all stock certificates shall be issued, and registered bonds, if any, shall be registered, in the name of [Waterbury Hospital] . . . [Waterbury Hospital] may withdraw any and all property held under this Agreement, at any time upon reasonable notice to Colonial.”

Although Conn. Gen. Stat. § 45a-535d in CUPMIFA does permit an institution acting as trustee for an endowment fund to delegate to an external agent the management and investment of the fund, nothing in CUPMIFA indicates that the institutional trustee does not remain the owner of the funds. Indeed, such a conclusion would be in direct contravention to the language of the contract between Waterbury Hospital, Inc. and Colonial Bank. Because Waterbury Hospital, Inc. remains the trustee of the Karl and Margaret Hallden Memorial Fund, and its use of the Fund is limited to income only, it should be characterized as an unrestricted endowment.

- ii. Except as set forth below, all gift documents listed in the OAG's Gift Analysis can continue to be held by the WH Foundation and can continue to be used for the charitable purposes set forth by the donors.

The Conversion Act requires a conversion foundation 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). The OAG's Gift Analysis sets forth these gift assets, along with their intended charitable purpose.

Accordingly, as a condition of our approval of the Joint Venture, the following gift documents listed in the OAG's Gift Analysis must be held by the WH Foundation and must be used for the charitable purposes set forth by the donors: Anderson (1), At Risk Kids (2), Crozier (4), Fulling (5), Junior League Fund (8), Sarann B. Kazanjian Student Nurse Scholarship Fund (10), Nursing School Alumnae (13), Brooker (20), Forester (21), Hallden Memorial Fund (22), Mayo (24), Crean (25), General Endowment Fund (26), Gift Annuity (27), and Pooled Income Fund (28).

In addition, the WH Foundation will continue to receive the income from the following trusts held by third party trustees: Elton (35), Fulton (36), Frank Keeling (39), Jacob Keeling (40), Lamb (42), Peck (43), Poole (44) and Smith (45).

- iii. All funds for which it will become illegal to fulfill the donor's charitable intent after the close of the Joint Venture must be the subject of an approximation action.

Based upon our analysis of the gift documents and the language contained therein, we conclude that there are several charitable funds that, given the sale of GWHN's assets, will no

longer be able to fulfill their charitable purpose and, therefore, cannot simply be applied as they have in the past. Accordingly, as a condition of approval, these funds must be presented to the superior court as part of an approximation action so that the court may determine the best alternative use of the funds.

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).

The approximation analysis must be applied to the following gifts, which are held by Waterbury Hospital: Chase (3) [used to underwrite the Henry S. Chase Outpatient Center "Chase Clinic"], Hayden (6) [bed fund], Heminway (7) [bed fund], Sarann B. Kazajian Memorial Fund (9) [medical and surgical equipment], Kingsbury (11) [bed fund], Meigs (12) [medical care at hospital], Merriman (13) [defray expenses of personnel of Clinical and Pathological

Laboratories to attend scientific meetings], Permanent Bed Fund (14) [bed fund], Flora S. Page and George W. Smith (15) [bed fund], Sperry (16) [bed fund], Terry (17) [bed fund], Various Gifts (18) [bed fund], Olive Rogers Warner (19) [bed fund], and Bevans (23) [hospitalized children].

In addition, the following trusts held by third party trustees are also subject to an approximation action: Anderson (29) [hospital care] and Kingsbury (32) [services to children in ER, special care and newborn nurseries].

iv. Four trusts with gift-over provisions must be the subject of a construction action in superior court.

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 doctrine of cy pres, or the equitable doctrine of approximation, does not apply.³² 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,

³² Cy pres is defined as the “equitable doctrine under which a court reforms a written instrument with a gift to charity as closely to the donor’s intention as possible, so that the gift does not fail. Black’s Law Dictionary (9th ed. 2009). The doctrine of approximation is well established in Connecticut law. See, e.g., *Lockwood v. Killian*, 179 Conn. 62 (1979); *Ministers & Missionaries Ben. Bd. v. Meriden Trust & Safe Deposit Co.*, 139 Conn. 435 (1953); *Seymour v. Attorney General*, 124 Conn. 490, 498-499 (1928).

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.

In the case of Waterbury Hospital, Inc., there are seven funds, six of which are held in trust by outside banks, that contain gift-over provisions. Two of those seven gifts, Hopkins (31) and Warner (33), are not implicated by the Joint Venture.³³ One fund held by Waterbury Hospital, the Pooled Income Fund (28), also has succession language that is not triggered by the Joint Venture.³⁴ The following remaining gifts contain succession language that could be triggered by the Joint Venture: Blakesley (30), Dayton (34), Sibilla Hellman Fund (37 and 38), and Kirk (41). In short, each of these trusts includes language that is ambiguous under the circumstances of this case, and depending on the interpretation of that language, might trigger a gift over provision in the trust. For example, the will created by Almon B. Dayton directs that if Waterbury Hospital “*shall cease to exist or shall relinquish its corporate charter, or shall fail*

³³ Both the wills of Abbie C. Hopkins and Oscar L. Warner direct that the trustee of the Hopkins Memorial Fund pay to Waterbury Hospital the net income of the trust “for the purpose of providing accommodations and medical care and attention for the poor and needy residents of the Borough of Naugatuck.” The wills further provide that should Naugatuck Hospital be built, the income will, instead, be paid to Naugatuck Hospital. As Naugatuck Hospital has not been built, these gift-over provisions are not implicated in this sale.

³⁴ The trust agreement provides: “If at the time of severance of the remainder interest the Hospital is not a public charity (an organization described in clauses (i) through (vi) of Section 170(b)(1)(A) of the Code), the amount severed shall be paid to an organization selected by the governing board of the Hospital that is a public charity.” Because the WH Foundation will be a public charity as described in Section 170(b)(1)(A), the gift-over provision is not triggered.

for any reason to function in the territory in which it is now located, its share of the income” (Emphasis added.)

As discussed above, Waterbury Hospital, Inc., shall continue to exist as a continuing conversion foundation, despite changes to its name and structure. It will be an equity holder of another, for-profit corporate entity that is currently applying for a new CON with OHCA. Clearly, however, its existence as a direct provider of health care as a licensed hospital will cease.

The key question is whether the hospital shall continue to exist in a manner that is consistent with the intent of donors of charitable funds. “All estates granted for . . . [any] charitable use, shall remain to the uses to which they were granted, *according to the true intent and meaning of the grantor*, and to no other use whatever.” (Emphasis added.) Conn. Gen. Stat. § 47-2, the Statute of Charitable Uses. “Any charitable trust or use . . . shall forever remain to the uses and purposes to which it has been granted *according to the true intent and meaning of the grantor* and to no other use.” (Emphasis added.) Conn. Gen. Stat. § 45a-514, the Statute of Charitable Trusts. The question is, therefore, what was the donor’s intent behind the words in the trust.

The law on will construction is well-established. “The construction of a will presents a question of law to be determined in light of the facts which are found by the trial court or are undisputed or indisputable.” *Hershatte v. Colonial Trust Co.*, 136 Conn. 588, 596 (1950). “The cardinal rule to be followed in constructing a will is to find and effectuate the intent of the testator. In seeking that intent, the court looks first to the will itself and examines the words

and language used in the light of the circumstances under which the will was written. *Dei Cas v. Mayfield*, 199 Conn. 569, 572 (1986).

Therefore, as a requirement for approval for the Joint Venture, these four trusts must be presented to the superior court for the interpretation of their gift-over terms.

v. Future Interests in Open Estates

According to the Gift Analysis provided to the OAG, there are four estates pursuant to which Waterbury Hospital, Inc., might receive charitable gifts: Crean (25), Pecka (47), Lenners (48) and Queor (49). According to a letter, dated June 11, 2012, from Attorney Matthew McCormack, co-executor of the estate of Thomas P. Crean to the Director of Finance at Waterbury Hospital, the \$10,000 bequest to Waterbury Hospital made under Article 7 of the will of Thomas P. Crean was completed. Consequently, GWHN must treat the Crean bequest as an unrestricted fully expendable gift and include it in the list of charitable trusts and gifts that can be legally transferred to the WH Foundation.

The Pecka (47), Lenners (48) and Queor (49) estates are still open and pending in Probate Court. If the probate of these estates is completed and if the court orders the distribution of funds to Waterbury Hospital, Inc., before the closing date of the Joint Venture, then those funds will remain with the WH Foundation. If the estates are still open at the closing of this transaction, then the decision about how to apply the bequests and remainder interests must be decided by the court under the equitable doctrine of approximation.

In addition, Waterbury Hospital, Inc., also has future interests in trusts that would be

held by third party trustees: Dodd (49), Fenn (50), Gibson (51), Snowden (52), and Stoughton (53). Similar to the gifts in which Waterbury Hospital, Inc., has a future interest, if GWHN's future interest in these trusts matures prior to the Joint Venture's closing, then that income will remain with the WH Foundation. If those interests have not matured by the closing, then the decision about how to apply the bequests and remainder interests must be decided by the court under the equitable 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, the foregoing future interests cannot, at this time, be included in the list of charitable trusts and gifts that can be legally transferred to the WH Foundation.

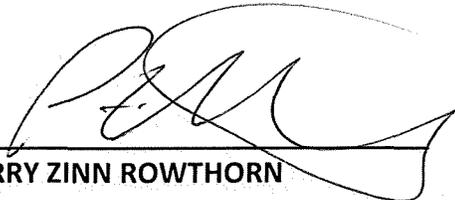
I. GWHN, Vanguard, And Tenet Have Provided The Attorney General With Information And Data Sufficient To Evaluate The Proposed Joint Venture.

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 Joint Venture.

VII. CONCLUSION

The OAG therefore concludes that the Application for Joint Venture between the Greater Waterbury Health Network, Inc., and Vanguard Health Systems, Inc., is hereby approved subject to the modifications and conditions listed herein.

Date: 12/1/2014



PERRY ZINN ROWTHORN
DEPUTY ATTORNEY GENERAL