



May 26, 2020

Attorney General William Tong  
Office of the Attorney General  
165 Capitol Avenue  
Hartford, CT 06106

Dear Attorney General Tong,

We write regarding hospital chain Prospect Medical Holdings' pending change in ownership. Safety net hospital chain Prospect Medical Holdings operates seventeen hospitals in five states, including three hospitals in Connecticut: Waterbury Hospital, Manchester Memorial Hospital, and Rockville General Hospital.<sup>i</sup>

Prospect is owned by private equity firm Leonard Green & Partners. Since Leonard Green acquired Prospect in 2010, the private equity firm and minority owners have drawn \$658 million dollars in fees and dividends from the company even its hospitals suffered operating challenges, substantially underfunded pensions, and regulatory scrutiny. Prospect has reported that Leonard Green is selling its now majority stake in Prospect to Prospect's management for \$10 million<sup>ii</sup>—a fraction of what it acquired Prospect and many of its hospitals for.

Prospect's hospitals currently have some of the lowest quality ratings from the Centers for Medicare and Medicaid Services—all but one have received one or two stars, the lowest quality ratings from CMS.<sup>iii</sup> In Connecticut, state regulators placed Prospect's three hospitals under review last year for deteriorating conditions that place patients in "immediate jeopardy."<sup>iv</sup> In Rhode Island, Prospect-owned hospitals' pensioners are suing Prospect for allegedly hiding the pension plan's poor health to shield its own liability from regulators.<sup>v</sup>

Prospect saw its EBITDA decline dramatically in recent years, from \$142 million in 2015 to \$17 million in 2018. Prospect's EBITDA margin dropped from 10.8% in 2015 to just 0.6% in 2018.<sup>vi</sup> In addition, Prospect faced \$260 million in unfunded pension liabilities as of September 2018.<sup>vii</sup>

Yet since Leonard Green acquired Prospect in 2010, the private equity firm and other owners have collected approximately \$658 million in fees and debt-funded dividends from the hospital company.<sup>viii</sup>

The \$457 million dividend the Leonard Green-led investment group collected in 2018 directly contradicted a commitment Prospect made to state regulators. In their consideration of Prospect's conversion of the CharterCARE hospitals in Rhode Island from non-profit to for-profit in 2014, the Rhode Island Office of the Attorney General and the State Department of Health made note of previous dividends the company had paid to investors, stating that Prospect had assured the regulators that it did not intend to make additional dividend distributions.<sup>ix</sup> Prospect paid the \$457 million dividend to its ownership group just four years later.

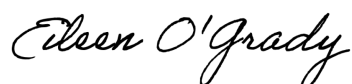
Last year, in an effort to pay down some of the existing \$1.1 billion debt it had accrued in part to fund dividends, Prospect sold much of its hospitals' real estate to health care REIT Medical Properties Trust and leased it back, adding additional lease obligations for Prospect's balance sheet.<sup>x</sup> Moody's analysts in July 2019 noted that the transaction did not merit a change in the company's B3 credit rating and negative outlook, as it "does not address the company's continuing operating challenges and lease-adjusted leverage will likely remain high."<sup>xi</sup>

Prospect subsequently shut down all of its health care facilities in Texas, laying off nearly 1,000 workers.<sup>xii</sup> It then sold the downtown hospital real estate to a hotel developer.<sup>xiii</sup>

It is inappropriate for a private equity firm to draw hundreds of millions of dividends from a safety net hospital chain, especially given the company's operating challenges and the hospitals' poor quality ratings.

We ask that your office decline to approve Prospect Medical Holdings' proposed change of ownership until Leonard Green & Partners returns the fees and dividends it collected from Prospect to ensure the hospitals and health care workers have as many resources as possible to respond to the COVID-19 pandemic.

Sincerely,



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<sup>i</sup> <https://pmh.com/hospitals/#map>

<sup>ii</sup> Change in Effective Control Application submitted by Prospect CharterCARE to State of Rhode Island Department of Health, Center for Health Systems Policy and Regulation. Submitted February 19, 2020. Accessed May 5, 2020. [https://drive.google.com/file/d/1vYdWVfRgKHQ3u\\_thgjz0qZA7UuPfFWBS/view](https://drive.google.com/file/d/1vYdWVfRgKHQ3u_thgjz0qZA7UuPfFWBS/view)

<sup>iii</sup> CMS Hospital Compare, accessed March 2020. <https://www.medicare.gov/hospitalcompare/search.html>

<sup>iv</sup> <https://www.courant.com/news/connecticut/hc-news-waterbury-hospital-prospect-medical-protests-20190602-hqc3yulngngwnd6qftmeiogdsq-story.html>

<sup>v</sup> <https://www.modernhealthcare.com/article/20180622/NEWS/180629970/lawsuits-allege-fraud-conspiracy-in-insolvency-of-st-joseph-health-services-of-rhode-island-plan>

<sup>vi</sup> <https://pestakeholder.org/wp-content/uploads/2020/05/UPDATE-Leonard-Green-Prospect-Medical-Dividends-PESP-051420.pdf>; Prospect Medical Holdings Consolidated Financial Statements as of and for the Years Ended September 30, 2018 and 2017. Prospect Medical Holdings Consolidated Financial Statements as of and for the Years Ended September 30, 2016 and 2015.

[https://drive.google.com/file/d/1vYdWVfRgKHQ3u\\_thgjz0qZA7UuPfFWBS/view](https://drive.google.com/file/d/1vYdWVfRgKHQ3u_thgjz0qZA7UuPfFWBS/view)

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- vii <https://pestakeholder.org/wp-content/uploads/2020/05/UPDATE-Leonard-Green-Prospect-Medical-Dividends-PESP-051420.pdf>; Prospect Medical Holdings Consolidated Financial Statements as of and for the Years Ended September 30, 2016 and 02015. [https://drive.google.com/file/d/1vYdWVfRgKHQ3u\\_thgjz0qZA7UuPfFWBS/view](https://drive.google.com/file/d/1vYdWVfRgKHQ3u_thgjz0qZA7UuPfFWBS/view)
- viii <https://pestakeholder.org/wp-content/uploads/2020/05/UPDATE-Leonard-Green-Prospect-Medical-Dividends-PESP-051420.pdf> ; [https://www.moodys.com/research/Moodys-downgrades-Prospect-Medical-Holdings-Incs-CFR-to-B3-outlook--PR\\_397518](https://www.moodys.com/research/Moodys-downgrades-Prospect-Medical-Holdings-Incs-CFR-to-B3-outlook--PR_397518)
- ix See: State of Rhode Island Department of the Attorney General, CharterCARE/Prospect Final Decision, (pg. 48). <http://www.riag.ri.gov/documents/5-16-14AGFinalDecision.pdf>; and Department of Health, Committee of the Health Services Council, Submitted May 2014 (pg. 22) <https://drive.google.com/file/d/0B9lx-sHDAL9qRmJPWmd1MXNpbEk/view>
- x <https://www.businesswire.com/news/home/20190715005786/en/Prospect-Receive-1.55-Billion-Investment-Medical-Properties>
- xi [https://www.moodys.com/research/Moodys-Prospect-Medicals-sale-leaseback-improves-liquidity-however-operating-challenges--PR\\_405116](https://www.moodys.com/research/Moodys-Prospect-Medicals-sale-leaseback-improves-liquidity-however-operating-challenges--PR_405116)
- xii <https://www.ksat.com/news/2019/11/06/last-nix-health-care-facility-in-san-antonio-set-to-close/>
- xiii <https://www.sacurrent.com/the-daily/archives/2020/01/03/hotel-company-purchases-downtown-san-antonios-historic-nix-hospital-building>

## UPDATE: Leonard Green-led ownership collected \$658 million in dividends and fees from Prospect Medical Holdings despite challenges, commitment to regulators to forgo dividends

Private equity firm Leonard Green & Partners owns Prospect Medical Holdings, a safety net hospital company that owns 17 hospitals in 5 states.<sup>1</sup>

Leonard Green acquired Prospect in December 2010 in a \$363 million leveraged buyout.<sup>2</sup> At the time, Prospect was a five-hospital community health system in Southern California.<sup>3</sup> Over the course of Leonard Green's ownership, Prospect bought hospitals in Connecticut, New Jersey, Pennsylvania, Rhode Island, and Texas.

Since 2010, the Leonard Green-led ownership group has drawn \$658 million dollars in fees and dividends from the company even as the hospitals suffered operating challenges, substantially underfunded pensions, and regulatory scrutiny.<sup>4</sup> Prospect's hospitals currently have some of the lowest quality ratings from the Centers for Medicare and Medicaid Services—all but one have received ratings of one or two stars, the lowest quality ratings assigned by CMS.<sup>5</sup> In late 2019 Prospect permanently shuttered all of the facilities in Texas, claiming it was unable to find a buyer for the hospital system.<sup>6</sup>

Of the \$658 million collected from Prospect, at least \$400 million appears to have gone to Leonard Green & Partners and its affiliates.<sup>8</sup>

Now, Leonard Green is selling its majority stake in Prospect to the company's management for just \$10 million<sup>9</sup>—a fraction of what it acquired Prospect and many of its hospitals for. Four years ago, in April 2016, *The Wall Street Journal* reported that Leonard Green was exploring a sale that might have valued Prospect at as much as \$1 billion.<sup>10</sup>

### FEES AND DIVIDENDS PAID TO LEONARD GREEN AND OTHER PROSPECT OWNERS

TYPE	DATE	AMOUNT
Annual \$1 Million Management Fee	2011-2019	\$9,000,000
Ivy Holdings Merger Transaction Fee	2010	\$4,441,000
Dividend	2012	\$88,000,000
Dividend	2013	\$100,000,000
Dividend	2018	\$457,000,000
<b>Total</b>		<b>\$658,441,000</b>

Sources: SEC filings and Prospect Medical Holdings, Inc. Consolidated Annual Financial Statements.<sup>7</sup>

*“Prospect’s management and representatives have given assurances that this [2013 dividend] was a one-time event and that there are no plans to make a similar distribution in the foreseeable future.”*

Rhode Island Attorney General decision, May 16, 2014

# UPDATE: LEONARD GREEN-LED OWNERSHIP

## 2018 DIVIDEND CONTRADICTED COMMITMENT TO RHODE ISLAND REGULATORS

The \$457 million dividend the Leonard Green-led investment group collected in 2018 directly contradicted a commitment Prospect made to state regulators. In their consideration of Prospect's conversion of the CharterCARE hospitals in Rhode Island from non-profit to for-profit in 2014, the Rhode Island Office of the Attorney General and the State Department of Health made note of the 2012 and 2013 dividends<sup>11</sup> stating that Prospect assured the regulators that it did not intend to make additional dividend distributions. The Attorney General's decision states: "Prospect's management and representatives have given assurances that this was a one-time event and that there are no plans to make a similar distribution in the foreseeable future."<sup>12</sup> At the same time, the Rhode Island Department of Health noted, "PMH [Prospect Medical Holdings] has represented that there are no intentions to make additional distributions."<sup>13</sup>

Prospect paid out the \$457 million debt-financed dividend to its owners four years later.<sup>14</sup>

## DECLINING FINANCIAL PERFORMANCE AT PROSPECT MEDICAL HOLDINGS

The Leonard Green & Partners-led ownership group collected the 2018 dividend despite declining financial performance at Prospect Medical Holdings.

### Operating Challenges

Prospect has faced substantial operating challenges in recent years.

Prospect's revenue grew by more than 2.3x between 2015 and 2018, likely due to its acquisition of three hospital systems in 2016. However, the company's EBITDA for the same period declined dramatically, from \$142 million in 2015 to \$17 million in 2018—an 88% decrease. Its EBITDA margin shrank from 10.8% in 2015 to just 0.6% in 2018.<sup>15</sup>

Cash on hand declined from \$65.9 million in 2015 to just \$7.7 million as of September 30, 2018.<sup>16</sup>

### Underfunded Pensions

Prospect's hospitals' pensions were substantially underfunded as of September 30, 2018 – the company faced \$260 million in unfunded retirement benefit obligations.<sup>17</sup>

Between 2016 and 2018, the funded ratio of the Prospect Medical Holdings' pension funds fell from 68.3% funded to 60.7% funded.<sup>18</sup>

In addition, the pension for Prospect's CharterCARE hospitals in Rhode Island, which is not included in these figures, is currently the subject of ongoing litigation. In 2018, pensioners filed a class action lawsuit against Prospect and other defendants for allegedly hiding the pension plan's poor health to shield its own liability from regulators. A year before, the plan's managers put the fund in receivership and cut benefits 40% across the board. Several other defendants in the suit have settled, but as of April 2020 Prospect has not settled.<sup>19</sup>

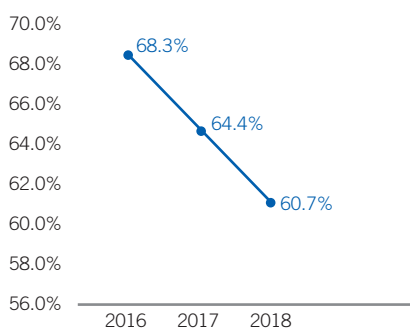
In connection with its acquisition of Crozer-Keystone Health System in Pennsylvania, Prospect planned to terminate the pension within the five-year period after acquiring it (i.e. by July 2021):

"Company will liquidate, fully fund and satisfy, and pay all benefits owed to participants and beneficiaries of the plan by providing lump sum distributions to participants, purchas-

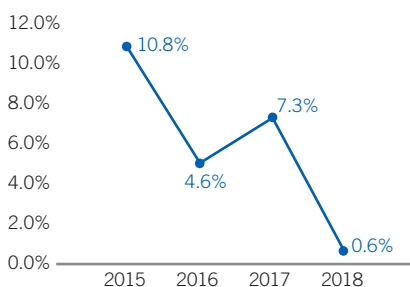
ing annuities for participants who do not elect a lump sum distribution."<sup>20</sup>

Prospect has made modest contributions to the pensions in recent years. In 2018, the company issued \$1.2 billion debt to refinance existing debt, reduce the underfunded pension liability, and pay a dividend to shareholders. Of the money the company raised, it contributed just \$40 million to the pension while paying a \$457 million dividend to Leonard Green and other owners.<sup>21</sup>

### FUNDED RATIO OF PROSPECT MEDICAL HOLDINGS' PENSION FUND



### PROSPECT MEDICAL HOLDINGS EBITDA MARGIN



# RAIDING THE SAFETY NET: LEONARD GREEN & PARTNERS SEEKS TO WALK AWAY FROM PROSPECT MEDICAL HOLDINGS AFTER COLLECTING \$570 MILLION IN FEES AND DIVIDENDS



## INTRODUCTION

In December 2010, Los Angeles-based private equity firm Leonard Green & Partners acquired Prospect Medical Holdings, then a five-hospital community health system in Southern California.<sup>1</sup> Under Leonard Green's ownership, Prospect expanded into Pennsylvania, New Jersey, Connecticut, Rhode Island, and Texas. By July 2019 it operated 20 hospitals and more than 165 clinics.<sup>2</sup>

While Leonard Green substantially grew the company through acquisitions, it has faced a number of operating challenges. Almost every hospital the private equity firm has acquired is now beset with problems, from regulatory scrutiny to system-wide facility closures.

In the meantime, Leonard Green has extracted hundreds of millions of dollars in fees and dividends from Prospect.

Leonard Green is now quietly exiting its stake in Prospect. It leaves in its wake numerous struggling, and in some cases, closing, health facilities.

Some of Prospect's hospitals—including East Orange General Hospital,<sup>3</sup> the Eastern Connecticut Health Network,<sup>4</sup> Crozer-Chester Medical Center and Delaware County Memorial Hospital<sup>5</sup>—are safety net hospitals, which are obligated to provide care to patients regardless of their insurance status. Leonard Green's raiding of safety

## KEY POINTS

- Private equity firm Leonard Green & Partners acquired Prospect Medical Holdings in 2010.
- Leonard Green and other owners have extracted \$570.44 million in fees and dividends from Prospect since they took over the company.
- Each of the health systems Prospect has acquired under Leonard Green's ownership has struggled:
- In Texas, Prospect is closing health system Nix Health in its entirety as of November 2019. Nearly 1,000 health care workers in San Antonio will lose their jobs.
- In Connecticut, state regulators have placed Prospect's three hospitals under review for deteriorating conditions that place patients in "immediate jeopardy." One of the hospitals received the lowest possible quality rating from the US Centers for Medicare and Medicaid and the others received the second lowest.
- In New Jersey, Prospect attempted to unload the hospital it acquired just three years into a five-year commitment. It had committed to \$50 million in investments in the facilities and had reportedly invested only \$26 million when it announced its intention to sell.
- In Pennsylvania, Prospect refused to pay millions of dollars it had committed to establish a community health charity as part of the transaction to acquire the Crozer-Keystone Health System. It also withheld school district property tax payments and allegedly failed to pay required pension benefits to hospital workers.
- In Rhode Island, Prospect-owned hospitals' pensioners are suing Prospect for allegedly hiding the pension plan's poor health to shield its own liability from regulators.
- As of November 2019, Leonard Green is quietly walking away from its stake in Prospect and selling its 61% stake to the minority owners for \$12 million—just 1.4% of what it acquired Prospect and many of its hospitals for.
- Several of Prospect's hospitals are safety net hospitals, which are obligated to provide care regardless of patients' inability to pay. Leonard Green's raiding the company is especially troubling given the service the hospitals provide to poorer patients.
- As private equity firms continue to invest in health care, stakeholders may look to Leonard Green's track record with Prospect as an example of the risks associated with private equity investment in the industry.



# RAIDING THE SAFETY NET

net hospitals is especially troubling given the service the hospitals provide to poorer patients.

As private equity investment in health care continues to grow, consumers, advocates, regulators, and other stakeholders may look to Leonard Green's tenure with Prospect as an example of the risks associated with private equity investment in the sector.

## LEONARD GREEN'S OWNERSHIP

Leonard Green & Partners, through its fund Green Equity Investors V, acquired Southern California-based Prospect Medical Holdings in December 2010 in a \$363 million leveraged buyout, including the assumption of \$158 million in debt.<sup>6</sup>

Leonard Green owns a 61.3% stake in Prospect. Prospect's founders, Samuel Lee and David Topper, together own almost all of remainder.<sup>7</sup>

Since Leonard Green acquired Prospect and its five California hospitals, it has expanded into Pennsylvania, New Jersey, Connecticut, Rhode Island, and Texas:

- **February 2012:** Nix Health System—San Antonio, Texas.<sup>8</sup>
- **September 2013:** CharterCare Health Partners joint venture—Rhode Island.<sup>9</sup>
- **May 2016:** East Orange General Hospital—East Orange, New Jersey.<sup>10</sup>
- **July 2016:** Crozer-Keystone Health System—Delaware County, Pennsylvania.<sup>11</sup>
- **August 2016:** Eastern Connecticut Health Network—Connecticut.<sup>12</sup>

## Fees and Dividends

Leonard Green has extracted hundreds of millions of dollars in fees and dividends from Prospect.

Per the December 2010 Management Services Agreement between Prospect and Leonard Green, Prospect pays Leonard Green an annual management fee of \$1 million for "management, consulting and financial planning services" and reimburses Leonard Green for its related expenses up to \$50,000 annually.<sup>13</sup>

Prospect's Board of Directors, which is controlled by Leonard Green,<sup>14</sup> may approve additional fees paid to Leonard Green "for services rendered in connection with major transactions from time to time." Under those terms, Prospect paid Leonard Green an additional \$4.4 million for fees associated with corporate restructuring in 2010.<sup>15</sup>

In November 2012, Prospect paid its owners a \$100 million dividend.<sup>16</sup>

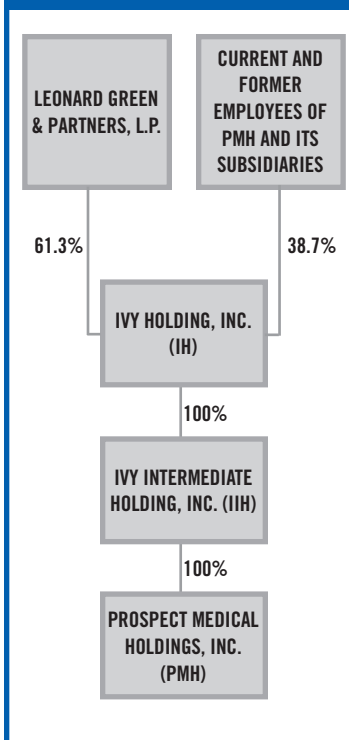
In January 2018, Prospect proposed a \$1.2 billion loan to reduce the underfunded pension liability and fund a roughly \$600 million dividend to shareholders.<sup>17</sup> However, after credit rating agency Moody's announced the move would result in a credit downgrade, the company restructured the loan and reportedly reduced the proposed dividend to \$457 million.<sup>18</sup> It is unknown whether Prospect has reduced its underfunded pension liability, though at its Rhode Island hospitals it is currently being sued by pensioners for allegedly breaching its pension obligations.<sup>19</sup>

In March 2019, Moody's downgraded Prospect's credit rating again, noting "very high financial leverage... and a history of failing to meet projections." Moody's noted that "Since completing a debt-funded sponsor dividend in early-2018, Prospect's leverage has increased significantly."<sup>20</sup>

## Sale-Leaseback Deal

In June 2019, Prospect initiated a \$1.55 billion sale-leaseback deal with Medical Properties Trust in which it sold its real estate to the health care REIT and leased it

**FIGURE 1: Relationship of Leonard Green to PMH**



Source: Prospect Medical Holdings submission to Connecticut Office of the Attorney General

*In March 2019, Moody's downgraded Prospect's credit rating again, noting "very high financial leverage... and a history of failing to meet projections."*

# RAIDING THE SAFETY NET

## FEES AND DIVIDENDS PAID TO LEONARD GREEN AND OTHER PROSPECT OWNERS

TYPE	DATE	AMOUNT
Annual \$1 Mil Management Fee	2011-2019	\$9,000,000
Ivy Holdings Merger Transaction Fee	December 2010	\$4,441,000
Dividend	November 2012	\$100,000,000
Dividend	February 2018	\$457,000,000
<b>Total</b>		<b>\$570,441,000</b>

back. The deal included all of its properties in Pennsylvania, Connecticut, and California.<sup>21</sup>

While the funds from the real estate sale allowed Prospect to pay down some of the existing \$1.1 billion debt it had accrued to fund the dividend it paid to Leonard Green a year prior, it also added significant additional lease obligations to Prospect's balance sheet. Moody's analysts pointed out that transaction did not merit a change in the rating agency's negative outlook, as it "does not address the company's continuing operating challenges and lease-adjusted leverage will likely remain high."<sup>22</sup>

It is unknown whether Leonard Green also was paid a transaction fee by Prospect as a result of the sale-leaseback deal.

### Leonard Green Walks Away from Prospect for \$12 Million

On November 4, 2019, Prospect submitted a notification to Connecticut regulators advising them that Leonard Green is selling its stake in Prospect to the minority owners. Sam Lee, CEO of Prospect, and David Topper, president of Prospect, will become Prospect's sole shareholders. In a statement, Prospect said it would take between 3-6 months for Leonard Green to fully exit the company.<sup>23</sup>

Prime Healthcare, a for-profit hospital system operating 45 hospitals in 14 states, reportedly offered to buy Prospect for \$50 million two weeks after Prospect notified state regulators of Leonard Green's intention to exit. Prime noted that Leonard Green was selling its stake for just \$12 million, and its offer of \$50 million reflects its belief that the company holds "substantially higher value." A Prospect representative reportedly said that it had signed a "binding agreement" with Leonard Green and could not consider other options for sale.<sup>24</sup>

Leonard Green's walking away from Prospect for \$12 million is puzzling considering it acquired Prospect and then the Connecticut, Pennsylvania, and Rhode Island health systems for approximately \$885 million.<sup>25</sup> The price for Prospect's Texas and New Jersey health systems was not disclosed. That means that Leonard Green appears to be selling its 61% stake in Prospect for just 1.4% of what the private equity firm and other owners acquired Prospect and many of its hospitals for. In addition, the sale price is negligible in comparison to the \$570 million in fees and dividends Leonard Green and other owners already collected from the health care provider.

Leonard Green had previously attempted to sell Prospect at least twice, without success—in 2015<sup>26</sup> and in 2018.<sup>27</sup>

*Leonard Green's walking away from Prospect for \$12 million is puzzling considering it acquired Prospect and then the Connecticut, Pennsylvania, and Rhode Island health systems for approximately \$885 million.<sup>25</sup>*



# RAIDING THE SAFETY NET

## TEXAS

In February 2012, Prospect acquired Nix Health System for an undisclosed amount. Nix was comprised of five primary facilities in San Antonio: Nix Medical Center, Nix Specialty Health Center, Nix Alamo Heights, Nix Primary Care Center and Nix North Orthopedic Center, as well as other physician offices.<sup>28</sup>

In April 2013, Prospect acquired Community General Hospital in Dilley, Texas to incorporate into the Nix Health system.<sup>29</sup> It closed the hospital in October 2016.<sup>30</sup>

In August 2019, Nix Health announced a series of closures that ultimately resulted in the complete closure of all Nix Health facilities.<sup>31</sup> Nix cited a “decline in community demand” for acute care services at its downtown hospital.<sup>32</sup>

On November 6, Nix submitted a final disclosure to the Texas Workforce Commission reporting that the closures would result in 972 layoffs.<sup>33</sup> The final facility closure took place on January 4, 2020.<sup>34</sup>

Prospect said it would host a job fair for affected workers.<sup>35</sup> It auctioned off medical equipment, valued at \$800,000, in December 2019.<sup>36</sup> It sold its 90-year-old downtown building in San Antonio to InnJoy Hospitality, which will likely convert the building into a hotel. Terms of the deal were not disclosed but according to public records, InnJoy borrowed \$19 million to finance the transaction.<sup>37</sup>



## CONNECTICUT

In August 2016, Prospect acquired three Connecticut hospitals: Waterbury Hospital, Manchester Memorial Hospital, and Rockville General Hospital. The hospitals sold for a combined \$335 million. As a condition for approving the transaction, the Connecticut state Department of Public Health's Office of Healthcare Access required Prospect to hire an independent monitor to track the facilities' compliance with state regulations and quality standards for at least two years. In response to community concern over possible closures, Prospect was also required to keep all services and facilities open for at least three years.<sup>38</sup>

By the monitoring agreement's expiration in fall 2019, health inspectors and regulators had found numerous issues at the hospitals.

Health inspectors cited both Waterbury and Manchester hospitals for conditions that placed patients in “immediate jeopardy.” According to the Centers for Medicare and Medicaid, immediate jeopardy means “serious injury, harm, impairment, or death as a result of a provider's, supplier's, or laboratory's noncompliance with one or more health and safety requirements.”<sup>39</sup>

Waterbury in particular has raised concern for regulators and the community: The Joint Commission on Hospital Accreditation in Spring 2019 cited Waterbury for 43 areas in which it must improve, from basic hygiene and infection control to fire drills, medications, patient discharge instructions, assessing patient's pain levels, suicide prevention methods and the accuracy of patient records.<sup>40</sup>

Waterbury has a one-star quality rating, the lowest rating, from U.S. Centers for Medicare and Medicaid. Rockville and Manchester are rated two stars.<sup>41</sup>

Because of the numerous citations at the hospitals, the monitoring agreement set to expire September 30, 2019 has been extended for an additional 18 months.<sup>42</sup>

## NEW JERSEY

Prospect took over East Orange General (EOGH) after the hospital filed for bankruptcy in 2016. East Orange General Hospital is East Orange, New Jersey's largest private employer and Essex County's only independent, fully accredited, acute-care hospital.<sup>43</sup> In its letter of intent filed as part of its application to the state to acquire the hospital, Prospect made a non-binding commitment to provide in excess of \$50 million in operational and capital investments over 5 years after the acquisition.<sup>44</sup>

# RAIDING THE SAFETY NET



In May 2019, three years after acquiring the hospital, Prospect began looking to sell it. As of May 2019, it had reportedly invested \$26 million.<sup>45</sup>

On June 30, NJ Gov. Phil Murphy signed a measure to earmark \$7.5 million of the state budget for the hospital. As of October 2019, the hospital had not collected the funds.<sup>46</sup>

EOGH reportedly filed paperwork with the state in July 2019 claiming that a change in ownership and restructuring from a for-profit to a non-profit is the only way to keep the hospital open. According to NJ Spotlight, the application “provides no detail on how exactly nonprofit status would be financially beneficial, but it notes the change would enable the hospital to better engage with community leaders, access funding currently off-limits and save on prescription drugs.”<sup>47</sup>

## PENNSYLVANIA

In July 2016, Prospect acquired Crozer-Keystone Health System in Pennsylvania. At the time of the acquisition, the system included five hospitals—Crozer-Chester Medical Center, Delaware County Memorial Hospital, Springfield Hospital, Taylor Hospital, and Community Hospital—and a network of outpatient and urgent care centers.<sup>48</sup> Prospect has since sold Community Hospital.<sup>49</sup>

Prospect has come under fire for failing to meet the terms of the acquisition of Crozer-Keystone Health System.

At the time of the acquisition, Prospect said it would make \$200 million in investments in the system over five years, keep the five Crozer-Keystone hospitals open and that it would assume Crozer-Keystone's outstanding pension liability.<sup>50</sup>

Prospect also committed to pay \$56.6 million for the establishment of a nonprofit county-wide health foundation,

the Crozer-Keystone Community Foundation. Despite its commitment, Prospect initially paid only \$32.9 million into the fund. The dispute went to arbitration, and in November 2017 an arbitrator ruled that Prospect still owed the foundation \$23.7 million.<sup>51</sup>

Prospect also refused to pay approximately \$480,000 in property taxes to the local school district on its Springfield Hospital property. When it bought the hospital system it claimed that a 1994 agreement between the hospital, the township, and the local school district applied to Prospect and released it from an obligation to pay taxes. The hospital was a nonprofit when it had entered into the agreement. When that argument failed, Prospect argued that it should not have to start paying taxes until the beginning of the next fiscal year, not from the date it acquired the hospital. A panel of Commonwealth judges ruled that Prospect was indeed to required to pay taxes from the date it acquired the hospital, and Prospect appealed.<sup>52</sup> The Springfield school board and district sued Prospect in August 2018 for still failing to pay the property taxes.<sup>53</sup> The case was settled in October 2018.<sup>54</sup>

## RHODE ISLAND

In 2014, Prospect entered into a joint venture with CharterCare Health to acquire a health system that includes Roger Williams Medical Center and St. Joseph Health Services of Rhode Island, including Our Lady of Fatima Hospital. Prospect paid about \$45 million for its 85% stake in the joint venture. The hospitals now operate as for-profit entities.<sup>55</sup>

Prospect and the hospitals' previous owners have been embroiled in a years-long dispute with pensioners dispute over the hospitals' dramatically underfunded pension plan.

In 2017 managers of the pension plan attempted to put the pension in receivership and cut benefits 40% across the board, claiming it could not pay its 2,700 beneficiaries. In

# RAIDING THE SAFETY NET



2018 the pensioners filed class action lawsuits against 14 defendants including Prospect. The pensioners claim to have only learned of the underfunding when the receivership request was filed.<sup>56</sup>

The suit accuses Prospect of hiding the pension plan's poor health to shield its own liability from regulators, alleging that "Saint Joseph Health Services of RI, the Prospect Entities, and other Defendants violated ERISA, committed fraud, breached their contractual obligations, violated their duty of good faith and fair dealing, and otherwise acted wrongfully."<sup>57</sup>

Prospect argued that it never intended to oversee the pension in the first place, touting that it has invested more than \$100 million in the state and preserved jobs by keeping the hospitals open.<sup>58</sup>

Several defendants have settled, resulting in settlement with the pension of \$4.5 million and \$11.9 million in October 2019.<sup>59</sup> As of January 2020, Prospect has not settled.<sup>60</sup>

## CONCLUSION

Leonard Green appears to have added little value to Prospect Medical Holdings. Meanwhile, it extracted millions of dollars in "management" fees, loaded the company with debt to pay out hundreds of millions of dollars in dividends, and then sold off much of Prospect's real estate to pay down that debt, adding significant lease liabilities to the health care provider's balance sheet.

Within weeks of announcing the complete closure of its Texas health system and amid the layoff of nearly 1,000 hospital employees, Leonard Green is seeking to exit its stake in Prospect. Beside the mass closures in San Antonio, Leonard Green leaves behind a legacy of declining quality of care in Connecticut, financial distress in New Jersey, financial disputes in Pennsylvania, and a lawsuit by distressed pensioners in Rhode Island.

Leonard Green's raiding of \$570 million in fees and dividends from Prospect is especially troubling given the role of Prospect's hospitals in providing a safety net to uninsured patients.

Leonard Green's gamble with Prospect should serve as an example of the risks of private equity investment in the health care industry.





# RAIDING THE SAFETY NET

## Endnotes

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# RAIDING THE SAFETY NET

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