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Suite 400  
Los Angeles, CA 90025

REDACTED

March 21, 2014

**Via E-Mail**

Geoffrey Ligibel, Director  
Houlihan Lokey  
123 North Wacker Drive, 4th Floor  
Chicago, IL 60606

Dear Mr. Ligibel:

This letter sets forth the non-binding intent of Prospect Medical Holdings, Inc. ("Prospect") with respect to a proposed transaction in which Prospect, or a designated subsidiary, would acquire the assets that comprise the businesses of St. Francis Medical Center and St. Vincent Medical Center (collectively "Southern California Hospitals") and their subsidiaries. The purchase shall include all real property (including medical office buildings) associated with the Southern California Hospitals as well as the Saint Vincent's Dialysis Center. The following represents the basic framework of our proposal and, if acceptable to Southern California Hospitals and Daughters of Charity Health Systems ("DCHS"), shall serve as a basis for a more formal Asset Purchase Agreement ("APA").

Pursuant to your request in the process letter, the following is an outline of our proposal:

**1. Description of Potential Acquiror**

Prospect provides quality, cost-efficient and coordinated healthcare services through our hospitals, clinics and physician networks in Southern California and San Antonio, Texas. We are purchasing two additional hospitals, a SNF and large freestanding clinic in the State of Rhode Island. One of the hospitals in Rhode Island is a Catholic hospital where we have agreed to abide by the Ethical and Religious Directives of the Catholic Church and maintain the Catholic identity of the hospital. We expect this transaction to close by June 1, 2014. Following the acquisition of these facilities, Prospect will generate over \$1 billion in annual revenues.

We conduct our business operations through two complementary segments: the hospital segment and the medical group segment. Through our hospital segment, we own and operate seven acute care and behavioral hospitals, with a total of approximately 1,056 licensed beds, and a network of 18 specialty and primary care clinics. Our hospitals are located in diverse population areas within Southern California and Texas and maintain significant market positions in the areas they serve. All of our facilities provide a comprehensive range of services tailored to their specific communities, including other area hospitals, physicians and health plans. We believe that our proven model has a number of competitive advantages, including a data-driven and cost-efficient platform that has enabled us to provide quality care to patients.

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Through our medical group segment and hospitals, we manage the provision of physician services to approximately 210,000 enrollees of Health Maintenance Organizations (“HMOs”) in Southern California through a network of approximately 3,300 primary care and specialty physicians. Based on our enrollment, our medical groups have a significant presence in Southern California and have long-term capitated contracts with nearly all major HMOs operating in the region. Under the capitated model, an HMO pays our medical groups a stable and predictable per-member-per-month rate, or a “capitation” payment, for which the medical groups assume responsibility for providing all required physician services for those enrollees.

We operate both our facilities and medical groups by applying highly disciplined, data-driven management to the provision of quality care to our patients. Through the in-depth analysis and application of various operational and financial metrics, we have been able to achieve a highly efficient cost structure across a diverse mix of payors and have been able to adapt to economic and regulatory changes. We believe the most cost-efficient and quality driven providers will succeed in this rapidly changing economic and regulatory environment. Furthermore, we believe the coordination of our facilities and medical groups creates an efficient healthcare delivery system that positions us well for the future of healthcare delivery.

## **2. Assets to be Acquired.**

As stated above, Prospect proposes to form new entities to purchase all of the tangible and intangible assets of St. Francis Medical Center, St. Vincent Medical Center and the assets of their respective subsidiaries (to the extent legally transferrable). We anticipate that the assets to be transferred include all real and personal property associated with St. Francis Medical Center, St. Vincent Medical Center, including the medical office buildings referred to as Huntington Park Medical Office Building, Maywood Medical Office Building, St. Vincent Professional Office Building and Ocean View Pavilion. The purchase would include all of the assets of St. Vincent’s Dialysis Center. We also anticipate that such purchase includes the assets of the medical practices of the physicians associated with the Medical Foundation, but only to the extent that such physicians are practicing at the Southern California Hospitals. We further anticipate that the employment agreements of the physicians employed by the Medical Foundation and related to the Southern California Hospitals would be assumed by a medical group affiliated with Prospect.

## **3. Treatment of the Medical Foundation**

Please see response to #2 above,

## **4. Amount and Form of Consideration**

Assuming that the balance sheet related to the Southern California Hospitals at closing would be free of all debt and cash, Prospect is prepared to offer a range between \$270 - \$300 million (based on financial statements as presented in the Confidential Information Memorandum) for the assets as described above.

## **5. Working Capital Assumption**

Prospect expects that the working capital of the Southern California Hospitals (excluding cash) to be at historical levels at Closing.

## **6. CBA Agreements and Non-Union Employee Retention**

Prospect anticipates to assume existing collective bargaining agreements. Furthermore, Prospect expects to offer employment, subject to customary pre-employment screenings, to substantially all employees of the Southern California Hospitals, including respective management, active, and in good standing, at the time of the closing of the transaction.

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**7. Post Retirement Obligations**

We note that the defined benefit plans at the Southern California Hospitals are Church Plans. As you know, for-profit entities, cannot assume Church Plans. In Rhode Island, Prospect faced a similar issue with respect to its transaction involving a Catholic hospital. Through cooperation and negotiations we were able to resolve the issue to the satisfaction of all parties. As such, we believe that we have experience in resolving issues related to Church plans and would be pleased to discuss possible solutions with DHCS as we move forward in the transaction.

**8. Treatment of other Agreements**

Subject to diligence, Prospect anticipates accepting assignments of the contracts related to the business, and the assets of the Southern California Hospitals.

**9. Sources of Capital**

Prospect is backed by Leonard Green & Partners, one of the largest private equity funds. We anticipate that Prospect would fund this transaction through a combination of cash on hand, debt and equity.

**10. Anticipated Operating Plan and Capital Commitment**

We recognize that meeting the long-term needs of the Southern California Hospital's service area would require constant evaluation of the market to identify needed services to enhance growth. Growth strategies begin with a detailed assessment of the market to identify opportunities to add or expand healthcare services. Service lines would be identified and evaluated. Working with the management team, we will identify and prioritize the growth initiatives that make the most sense. It would be our objective to initiate growth initiatives for the benefit of the surrounding communities and the Southern California Hospitals so long as that care can be delivered in a high quality and financially responsible manner.

Prospect will work with medical staff of each hospital to ensure that physicians maintain an active presence at the facilities and are kept informed and provided with necessary assistance during the transition planning phase, and are encouraged to maintain their medical practices within the community. Furthermore, we believe that the delivery of quality healthcare services depends in part on quality physicians. It is our intention to attract and recruit quality physicians in order to form and implement our CRCP model.

We will commit to make the necessary capital expenditures to deploy our CRCP model. We plan to commit sufficient funds in order to maintain and improve the physical plant and equipment at the Southern California Hospitals. Finally, we plan to commit sufficient capital to implement a physician engagement plan to align the incentives of physicians and each of the Southern California Hospitals.

**11. Community Service and Charity Care.**

Prospect recognizes the importance of community service and charity care within the communities served by the Southern California Hospitals. Prospect is proud of its institutional tradition of providing charity care to uninsured and the under-insured members of its hospital communities. Subject to diligence, Prospect will adopt each of the respect Southern California Hospital's charity care policies and will operate its charity care program in accordance with federal and state laws. Prospect will continue to provide medically necessary services to the surrounding communities served by Seller. Furthermore, subject to further diligence, Prospect anticipates supporting community outreach programs.

**12. Process and timing**

Due to the limited amount of data provided in the Confidential Information Memorandum, Prospect will need access to additional information as typical in the normal course of a sale process. Attached is a schedule of additional information that we would like to review prior to submitting a binding proposal, provided however, we reserve the right to request additional information as necessary. We anticipate conducting final confirmatory due diligence and negotiating an APA along a parallel path. Assuming timely receipt of the requested information, we anticipate that final confirmatory diligence and execution of the APA will occur within 60 – 90 days. We would then close the transaction as soon as possible after receiving the necessary regulatory approvals.

**13. Due Diligence**

Please see response to #12, above.

**14. Specific Contingencies to Closure**

This non-binding Indication of Interest has been approved by Prospect's senior management. Execution of an APA and completion of a transaction will require approval by the Prospect Board of Directors. Furthermore, the closing of the proposed transaction is subject to satisfactory completion of due diligence at Prospect's sole discretion, and any other customary governmental/regulatory approvals. We expect that we would obtain board approvals upon the completion of the due diligence and negotiation of the final draft of an APA. We believe that all such approvals will be obtained within the time frames specified above. We also intend to pursue all regulatory and governmental approvals as soon as possible.

**15. Other Parties**

We do not anticipate any third parties to participate in the consummation of the transaction. We anticipate that a transition services agreement maybe appropriate for a brief period of time.

**16. Contact information.**

We have not yet engaged any third parties to assist in the transaction. As we move forward, and identify such third party advisors , we will inform you of the same immediately.

We recognize that choosing a buyer involves more than financial considerations and legal structures. Our proposal is about preserving and enhancing a community resource in a way that honors DCHS stated mission and vision.

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Prospect is unique in the market place and is uniquely positioned to meet the challenges of ever changing healthcare environment and thrive under healthcare reform. Although noted above, we believe it is important to reiterate that what distinguishes Prospect in the marketplace is its proven ability to effectively and profitably manage risk, capitation, and bundled payments on behalf of our hospitals and medical groups while at the same time delivering a high quality of care. This unique structure allows managed care plans to focus on marketing; physicians to focus on patient care; and Prospect to coordinate medical management that ensures quality and efficiency.

This indication of interest is confidential and subject to the terms and conditions of our Confidentiality Agreement dated February 12, 2014.

The contacts for questions regarding our indication of interest are as follows:

Steve Aleman, Chief Financial Officer [REDACTED]

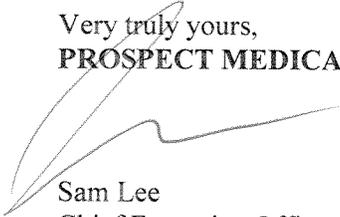
Frank Saidara Vice President [REDACTED]

(Messrs. Saidara and Aleman can be reached at [REDACTED]).

If you have any questions, please feel free to contact Messrs. Aleman, Saidara, or me.

We look forward to working with you.

Very truly yours,  
**PROSPECT MEDICAL HOLDINGS, INC.**



Sam Lee  
Chief Executive Officer

FS:fs  
Enclosures