

Executive Summary

Daughters of Charity Health System (“**DCHS**”) respectfully requests the Attorney General’s approval to transfer control of the health facilities comprising its hospital system (the “**Health Facilities**”) to Prime Healthcare Services, Inc. (“**Prime**”) under Section 5914 of the Nonprofit Corporation Law (the “Consent Statute”). Approval of this application is in the public interest.

When the California Legislature passed the Consent Statute in 1996, it gave the Attorney General the power and duty to protect access to health care services when control of nonprofit health facilities changes. The legislature encouraged the Attorney General to do so with regard for the preservation of health care access that for-profit health care operators can contribute to the state’s health care system. This transaction directly meets that purpose. The DCHS’s hospitals include some of California’s essential safety net providers. DCHS is in financial distress and expects to be out of operating cash by the middle of 2015. At that time it will face repayment of \$125 million in bridge financing that it obtained through the California Statewide Communities Development Authority in July and August 2014 for operating expenses. In the absence of this transaction, many of those liabilities will go unpaid and closure of one or more of the DCHS hospitals is likely. Closing hospitals causes substantial health care deficits in the communities served. The exercise of the Attorney General’s discretion to prevent such health care deficits from occurring will achieve a fundamental goal of the Consent Statute.

Consent to the transaction does not merely avoid negative impacts; the transaction merits consent for a number of positive outcomes and potentials. It offers to strengthen the DCHS health facilities by bringing them into a large, well-resourced hospital system offering economies of scale, turn-around experience and committed capital. Prime’s patient care scores on national measures objectively demonstrate strong quality and patient satisfaction. Prime has committed to invest at least \$150 million of much-needed capital to revitalize the DCHS facilities. Prime has promised to keep acute care services open without any restriction on the type or level of medical services provided by the health facilities after the closing. Prime has committed to continue charity care at historical levels and to fund pastoral services.

The transaction with Prime would also enable the DCHS Board to meet one of its foremost goals: to find a successor to assume and fund the DCHS pension plans covering over 16,000 present and former DCHS employees. Of DCHS’s four final bidders, one, favored by United Healthcare Workers West (UHW), staked the funding of the pension plans entirely on its ability to manage the DCHS Health Facilities to profitability, and offered no backstop for the pensions. That bidder’s proposal put the pensions at risk of being decimated if the turn-around failed. The remaining two proposals required DCHS to retain one of the pension plans. Prime alone offered its full worth (\$2.3 billion) to support the funding of the pension plans of DCHS. Prime also committed to preserve health care jobs, to abide by DCHS severance policies and commitments, to continue consistent benefits programs and to assume all existing union contracts.

At closing Prime will fund the repayment of DCHS’s two state bond issues. In addition to pension obligations, these liabilities to bondholders of the California Statewide Communities Development Authority represent the largest debts of DCHS, and they will be fully satisfied. Again, the bidder favored by UHW intended to leave a major portion of these bonds outstanding over bondholder-voiced objections.

The financial strength and operational capabilities of Prime set it apart in comparison to the other final bidders. Prime will take the DCHS Health Facilities into a major existing health system, with all the support functions and established capabilities such an enterprise brings to the task of stabilizing and sustaining these health care assets. No other final bidder presented such wherewithal. Indeed, the bid supported by UHW was markedly deficient: it proposed in essence nothing more than a management services contract at a cost to DCHS of \$24 million year for the services of three executives without a track record of working together in California health care or the resources of an existing health system. That proposal left the fate of DCHS's liabilities, including pensions and payment of the 2005 bondholders, hanging solely on the management company's ability to turn around the existing operations of the DCHS Health Facilities. Moreover, in contrast to Prime's agreement to take full risk for the pensions, that bidder risked only a limited investment in the new management company and sought to fund the cash requirements of DCHS going forward by borrowing against DCHS assets and requiring a cash contribution at closing from DCHS affiliates. Significantly, unlike the other three bidders, it also refused to provide a substantial deposit if selected to protect DCHS against failure to close. Despite important and valuable support for this bidder from UHW, these infirmities caused its final proposal to fall short of the fiduciary goal that DCHS's board set at the outset: a successor whose financial and operating strength, experience and legal commitment in the judgment of the DCHS Board best promises to meet those major obligations and, above all, preserve ongoing access to health care services.

DCHS is submitting the following extensive and detailed application materials in order to demonstrate that the process followed by DCHS was full and fair and that the final decision by the DCHS Board was based on careful deliberations and the objective merits of the Prime proposal in comparison with other final substantive offers. The terms and conditions of the agreement with Prime are fair and reasonable, with substantial protections for the interests of DCHS prior to closing such as a \$40 million deposit as surety for Prime's performance of its obligations under the agreement. The process of seeking a qualified successor securely established the fair value of the Health System by using extensive marketing efforts conducted over eight months by the members of an experienced professional firm who maintained a strictly level playing field for buyers. This transaction avoids significant negative effects on the availability and accessibility of health care services in the communities served by the DCHS health facilities. Most importantly, it was the strongest among the final proposals and promises to secure a viable future for the DCHS Health Facilities.