New Jersey
Appleseed

April 30, 2010

Jay Ganzman, DAG
New Jersey Dept. of Law and Public Safety
Hughes Justice Complex
P.O. Box 080
Trenton, NJ 08625-080

Re: Fair Market Valuation of Meadowlands Hospital and Medical Center

Dear Mr. Ganzman:

I am writing to you, at this time, to urge your office to consider retaining "reasonably necessary expert assistance in making [the] determination" whether Liberty Healthcare System, Inc. ("LHS") "will receive full and fair market value for its assets" upon the sale of Meadowlands Hospital and Medical Center ("MHMC") as the Attorney General is authorized to do pursuant to the Community Healthcare Assets Protection Act (CHAPA), N.J.S.A. 26:2H-7.11(d)(1).[1] We are making this request after our preliminary review of the initial documents filed by LHS with your office has raised several concerns about the process undertaken by LHS to sell MHMC, the entities selected to purchase and/or operate the hospital and the proposed structure and terms of the transaction.

[1] In addition to making this determiniation, we understand that the Attorney General must also consider whether LHS exercised due care in assigning a value to the existing hospital and its charitable assets in proceeding to negotiate the proposed sale to a for-profit entity. N.J.S.A. 26:2H-7.11(d)(6).

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Unlike the process followed by Salem Memorial Hospital when it sold itself to Community Health Systems, Inc., and Atlantic Health System when it sold Mountainside Hospital to Merit Health System -— both out-of-state for profit hospital systems, -- it does not appear that the board of LHS retained an expert to find a buyer through a public Request for Proposal process. Indeed, other than retaining a lawyer to advise the board as to its fiduciary obligations, it does not appear that experts were retained to develop a strategic sales plan, assist the board in establishing appropriate selection criteria to differentiate among entities that may respond to a Request for Proposal, or undertake a fair market value analysis prior to accepting offers to purchase. Rather, our preliminary review indicates an explicit effort to keep the sale of MHMC private, and to use a lobbyist to find potential purchasers. Such a private, closed process raises concerns that the actual fair market value of the hospital has not been received.

Other aspects of this transaction raise similar concerns:

First, it seems that the fair market analysis that was submitted by LHS in its application to justify the proposed purchase price was performed around the time LHS had already entered into preliminary negotiations with Meadowlands Hospital Acquisition LLC ("MHA").

Second, it is not clear that the operating losses that MHMC only started experiencing in the third quarter of 2008 after years of profit (and which ballooned in December 2008 through 2009) justify a low operational value to be assigned to the hospital. In fact, the proposed purchaser in the Certificate of Need application has projected significant increases in patient volume (the primary reason identified by LHS for the losses starting in 2008) and projected revenue at a level that would render the hospital profitable within months of purchase. The projections offered by the purchaser seem to indicate that the goodwill and reputational value of MHMC as an operating entity are certainly worth more than indicated in the FMV analysis submitted.

Third, we have questions as to the role the budget item "Due to Affiliates," which represents working capital advances from LHS to MHMC, played in the fair market valuation of MHMC. Around the time the analysis was performed, the "Due to Affiliates" item on the MHMC balance sheet had increased more than four-fold in the 18 months from December 2007 to June 2009. The basis of this increase needs to be explored. Furthermore, the treatment of this item seems to have changed. For the first time in 2008, "Due to Affiliates" appeared on the MHMC unaudited financials as a *current* liability (in contrast to a long term liability); as a result, MHMC's current ratio, a key measure of liquidity, suddenly appeared to be unfavorable. However, the audited financial statement for 2008 (only recently available) restores this budget item to a long term liability. We urge the Attorney General to investigate the amount and treatment of this budget item in light of its affect on the operating value of MHMC.

Fourth, from the materials presented it is unclear whether the closing of Greenville Hospital (GH) in April 2008, the transformation of the MHMC Board into an advisory board to LHS, and the renegotiation of the Capital One loans for which MHMC and GH were jointly and severally liable adversely impacted the valuation of MHMC and played a significant role in LHS's decision to sell MHMC rather than try to turn it around itself. It is our understanding that when Greenville closed, Meadowlands became responsible for the full amount of the loans; however, we do not know whether that responsibility and/or subsequent decisions to allocate the loans between the two entities and to renegotiate the terms of the loans were reflected in the valuation of MHMC.

In addition, we question why the real estate entity purchasing the hospital is only paying $10 million dollars if it is guaranteed to receive $4.3 million in rent per year. That is, we assume that the expected rental stream generated from real property should be reflected in the purchase price of that property. Accordingly, we have serious concerns that the real estate value of the hospital is being seriously underestimated.

There are several other aspects of this transaction that also raise our concern that the full fair market value of MHMC is not reflected in the purchase price of the hospital and that the community's interest in the hospital's charitable assets has not been properly protected. LHS has not negotiated the creation of an independent conversion foundation that could also receive any endowment funds LHS holds and administers on behalf of MCMS; LHS has agreed to lend MHA $5 million representing one-third of the purchase price; LHS has not retained a right of first refusal in the event that MHA decides to close the hospital, sell it or reduce any services(a likely event given the failure of LHS to negotiate a commitment to keep the hospital as a full service acute care facility for any period of time, in contrast to the commitments received upon the conversion of Salem, Mountainside and Bayonne Hospitals); and LHS has agreed to pay over $3 million in transaction fees to be deducted from the $15 million purchase price, representing 20% of the purchase price.

Under these circumstances, we urge the Attorney General to exercise its authority under CHAPA and retain a second independent appraisal of MHMC.

Sincerely yours,

Renée Steinhagen

Cc: Mayor Michael Gonnelli
Assemblyman Vincent Prieto
HPAE