

**BUSH GOTTLIEB SINGER LÓPEZ  
KOHANSKI ADELSTEIN & DICKINSON  
A Law Corporation**

David Adelstein  
David Ahdoot  
Daniel Bush  
Robert A. Bush  
Pamela Chandran  
Erica Deutsch  
Peter S. Dickinson+  
Ira L. Gottlieb\*  
Joseph A. Kohanski\*  
Robert Kropp, Jr.  
Miriam López  
Marissa M. Nuncio  
Hope J. Singer\*  
Melvin Yee

500 North Central Avenue  
Suite 800  
Glendale, California 91203  
Telephone (818) 973-3200  
Facsimile (818) 973-3201

November 24, 2010

**File No:**  
11097-20005

**Direct Dial No.:**  
(818) 973-3206  
DBush@BushGottlieb.com

\* Also admitted in New York  
+ Also admitted in Nevada

**VIA E-MAIL AND CERTIFIED MAIL**

Dr. Mark Horton  
Director  
California Department of Public Health  
1615 Capitol Avenue, MS 0512  
Sacramento, CA 95814

Re: Prime Healthcare Services Acquisition of Alvarado Hospital

Dear Dr. Horton:

This office represents the Service Employees International Union, United Healthcare Workers-West ("SEIU-UHW" or the "Union"). We write to express serious concerns with respect to Prime Healthcare Services, Inc.'s ("Prime") recent acquisition of Alvarado Hospital in San Diego, CA, from its previous owner Plymouth Health. We understand that Prime has failed to submit a Change of Ownership application and is currently operating the hospital without a license in violation of state law.

This failure to submit a Change of Ownership application constitutes an egregious and deliberate attempt to circumvent the efforts by the California Department of Public Health ("CDPH") to protect the public health and well-being of California residents through the regulation and licensing of healthcare facilities. As you know, the CDPH is launching a joint investigation with the Department of Health Care Services, Audits and Investigations Unit into Prime's extremely high septicemia rates and has determined that it will not grant any Change of Ownership applications submitted by Prime until all investigations have been concluded.

In an obvious effort to circumvent the licensing process, Prime has callously and cynically thumbed its nose at the CDPH and the people of this State. We request that the CDPH immediately initiate legal action against Prime for operating a hospital without a license.

**I. Factual Background**

Prime is a privately held for-profit company that, with Alvarado Hospital, operates 14 acute care hospitals, 13 in Southern California, and one in Redding, California. SEIU-UHW represents over

## VIA E-MAIL AND CERTIFIED MAIL

Dr. Mark Horton  
November 24, 2010  
Page 2

1,000 Prime employees at four hospitals and is engaged in a labor dispute with the company. As part of the 2.2 million-member Service Employees International Union (SEIU), the largest union of healthcare workers in the United States, the Union is a key advocate of protecting public health and public funds dedicated to healthcare.

An SEIU-UHW analysis of Medicare billing records for 2008 in over 2,900 U.S. hospitals found that Prime-operated hospitals have alarmingly high septicemia rates, rates that are considerably higher than any other health system in the United States. The report offers two possible explanations for these extreme septicemia rates: that they are evidence of either substantial Medicare fraud and/or a distressing breakdown in the quality of care. The Union's analysis was reported on by the Los Angeles Times and California Watch as well as other media outlets.

### A. Ongoing Investigations Into Prime

Alarmed by the SEIU-UHW report's findings, and in response to requests by lawmakers, federal and state regulators have launched several investigations into Prime's practices.

Two U.S. Congressmembers from California, Henry Waxman, Chairman of the House Committee on Energy and Commerce and Pete Stark, Chairman of the Subcommittee on Health, House Committee on Ways & Means requested in a July 1, 2010 letter that the Inspector General of the federal Health & Human Services Department conduct an investigation into Prime's practices. That letter describes the SEIU-UHW report as "potentially demonstrat[ing] a pattern of fraudulent billing of Medicare program and/or extremely high rates of blood infections among Medicare patients treated at Prime-operated hospitals."

According to the Los Angeles Times, in response to the letter by Congressmembers Waxman and Stark, the Health and Human Services Department has launched a federal probe into Prime.

State Senator Elaine Alquist, Chair of the Senate Health Committee, in an August 17, 2010 letter to the CDPH, calls the SEIU-UHW report's findings "deeply concerning," and requests "most urgently" that the Department launch an investigation into Prime. She further requests that **"until all of these investigations are complete, I request that you withhold approval of any additional facility licenses for Prime or Prime-related entities."** (emphasis in original).

Joining Senator Alquist, Assemblymember Bill Monning, Chair of the Assembly Health Committee, requested in a September 8, 2010 letter to CDPH, that the Department launch an investigation and "withhold any additional facility licenses for Prime or Prime-related entities."

As you know, in response to these concerns, the CDPH has notified lawmakers that it is launching its own investigation into what the Department has characterized as "great concerns that there could be a significant health care and infection control issues within Prime Healthcare Services hospitals and/or potential up-coding for the purposes of overbilling," and has agreed to withhold granting any Change of Ownership application until the investigations are completed.

## VIA E-MAIL AND CERTIFIED MAIL

Dr. Mark Horton

November 24, 2010

Page 3

The Los Angeles Times article also reports that the state attorney general's office has already initiated a criminal investigation into Prime and that, separately, Medi-Cal auditors are conducting an inquiry into Prime and have flagged \$2.8 million in questionable expenses. In addition, Prime recently paid out \$1.2 million to settle a lawsuit filed by the California Department of Managed Healthcare that alleged that Prime illegally put thousands of emergency room patients in the middle of billing disputes with their insurers.

### **B. Prime's Acquisition of Alvarado Hospital**

On November 17, 2010 Prime announced the acquisition of Alvarado Hospital from Plymouth Health. Alvarado Hospital is a general acute care hospital licensed under Alvarado Hospital, LLC. Plymouth Health, LLC is listed as having a 100% ownership interest. The license is scheduled to expire effective December 31, 2010.

In its own press release, Prime makes abundantly clear that it has purchased the hospital, labeling the transaction as an "acquisition" of the hospital, stating that it "will continue to operate" and "has no intention of closing" the hospital, and that Prime "also owns and operates" another nearby hospital. Prime's press release quotes Prem Reddy, Prime Healthcare's Chairman of the Board, as stating that Prime is "pleased that Plymouth Health elected to sell Alvarado to Prime Healthcare." (Prime's press release is available on its website, [http://www.primehealthcare.com/primestyle/shtm/news/news\\_2010\\_4.shtm](http://www.primehealthcare.com/primestyle/shtm/news/news_2010_4.shtm)). Prime's website now lists Alvarado as one the fourteen hospitals owned and operated by Prime. (See, <http://www.primehealthcare.com/primestyle/shtm/hospitals.shtm>).

Yet, despite the fact that Prime has become the new owner and operator of Alvarado Hospital, the company failed to provide notice to the CDPH of this purchase and has not submitted a Change in Ownership application, in violation of state law. See 22 CCR 70125 (CDPH must be provided at least 30 days notice prior to any change of ownership of a healthcare facility); 22 CCR 70105 (a new hospital license is required upon a change of ownership).

Indeed, Prime has structured its acquisition of Alvarado Hospital for the very purpose of seeking to avoid the licensing requirements. While Prime has purchased Alvarado Hospital, it elected to retain Alvarado Hospital LLC as the existing business form by acquiring all of the membership interests in the LLC. Thus, while Prime is the sole owner and operator of the hospital, the name of the license holder – Alvarado Hospital LLC – has not changed. In an email to Kathleen Billingsley dated November 17, 2010, Prime representative Suzanne Richards baldly asserts that this acquisition has not resulted in a change of ownership but simply a "change of information as the licensee" and Prime is therefore not required to apply for a new hospital license.

Given the grave concerns raised by lawmakers and regulators about Prime's practices, it is perhaps no surprise that the company has made such a concerted effort to avoid regulatory scrutiny. Prime's attempt, however must fail; its actions serve to emasculate the regulatory

**VIA E-MAIL AND CERTIFIED MAIL**

Dr. Mark Horton  
November 24, 2010  
Page 4

authority of the CDPH and fly in the face of the meaning and purpose of the Health and Safety Code's licensing requirements.

**II. Prime's Acquisition of Alvarado Constitutes a Change of Ownership Requiring a New License**

As you know, as part of the CDPH's mandate to ensure the health and well-being of California residents, the Department is responsible for licensing and certifying health facilities. The license application process is triggered for new facilities as well as when there is a change in ownership at an existing licensed facility. Cal. Health & Safety Code §§1253,1298; 22 CCR 70105.

Analysis of related federal and state law as well as a review of the legislative intent behind the licensing provisions of the Health & Safety Code leads to an obvious and compelling conclusion: when one entity purchases a hospital from another entity and assumes complete operational control of that hospital, a change of ownership results, requiring that the new owner submit a Change of Ownership application prior to operating the hospital.

**A. Alvarado Hospital LLC Has Been Terminated As A Matter of Law**

Both state and federal tax law have developed definitions that demarcate when existing partnerships and limited liability companies are terminated and new companies or partnerships are created. In doing so, these provisions establish when a change of ownership occurs.

Under Internal Revenue Code 26 U.S.C. §708(b)(1)(B), partnerships, including LLC's will be considered terminated if "within a 12-month period there is a sale or exchange of 50 percent or more of the total interest in partnership capital and profits." While the entity's name and Employer Identification Number remain the same, the tax code considers the old entity terminated and a new one created. 26 C.F.R. §§1.708-1(b)(4)(i)-(iii); 26 C.F.R. §301.6109-1(d)(2)(iii).

Similarly, California state tax regulations treat as a "change in ownership," when one business form, including a corporation, acquires "direct or indirect ownership or control of more than 50 percent of the total interest in partnership or LLC capital and more than 50 percent of the total interest in partnership or LLC profits." 18 CCR §462.180(d)(1)(B); *see also* Cal. Rev. & T. Code §64(c)(1).

In this case, Prime itself has asserted that it has purchased 100% of the membership interests in the Alvarado Hospital LLC and has assumed complete operational control of the Hospital. Therefore, Alvarado Hospital LLC owned by Plymouth Health has been terminated and a change of ownership has occurred with the creation of new LLC, under the same name, owned by Prime. As required by the Health and Safety Code and regulations, Prime was obligated to submit a Change of Ownership application before operating Alvarado Hospital.

## VIA E-MAIL AND CERTIFIED MAIL

Dr. Mark Horton  
November 24, 2010  
Page 5

### **B. The Health and Safety Code**

The Health & Safety Code provides that no person or entity shall “operate, establish, manage, conduct, or maintain” a hospital without obtaining a license from the CDPH. Cal. Health & Safety Code §§1253,1265 1298. The statute further defines “manage” to mean “to assume operational control of the facility.” Health & Safety Code §1265(l). The Code of Regulations further provides that an individual or entity cannot “advertise by any means that it operates a hospital” without obtaining a license. 22 CCR 70103. Finally, when ownership of a licensed facility changes hands, the new owner must submit an application for a new license. 22 CCR 70105; Health & Safety Code §1298.

Prime now owns Alvarado Hospital, has assumed operational control of the hospital, and is advertising and holding itself out as the owner and operator of the Hospital. Prime is thus the new owner of the hospital and is obligated to submit a Change of Ownership application. Prime has failed to do so and is operating Alvarado Hospital without a license.

Moreover, the very purpose of the licensing regime necessitates treating Prime’s purchasing of Alvarado as a change of ownership requiring a new license. Hospital licenses are required to protect the public health by ensuring that only reputable and responsible applicants who have the ability to comply with health facility laws and regulations are permitted to operate hospitals. *See, e.g., California Bill Analysis, A.B. 330, CA B. An., A.B. 330 Sen., 8/29/2005.* To aid the CDPH in carrying out its licensing responsibilities, the Health and Safety Code outlines numerous factors that the CDPH must consider in determining whether to grant a license. Health & Safety Code §1265.3.

The license application process includes extensive documentation concerning whether the applying entity and the individuals behind that entity, have the experience and character to operate a hospital. For example, the applying entity must provide an organizational chart of the owning entity and its parent entity, if applicable, including a list of owners, directors, board members and officers, as well as a list of anyone with 10% or more ownership interest. *See CDPH’s General Acute Care Hospital Application Request Letter and Instructional Checklist, October 1, 2010.* The CDPH is also authorized to deny a license if the applicant or members of the applying entity with more than 10% beneficial ownership interest in the applicant have been convicted of certain crimes. Health & Safety Code §1265.1.

Given that the licensing process centers around the bona fides of the applicant, it should come as no surprise that hospital licenses are not transferrable and that upon a change of ownership, the new owner must submit a new license application. 22 CCR 70125; 22 CCR 70105. If this were not the case, the licensing process could be easily avoided by simply acquiring a facility that has already been licensed. Granted, facilities must renew their licenses, but as you know, the renewal licensing application process is far less stringent or comprehensive than the initial licensing process or the Change of Ownership application.

**VIA E-MAIL AND CERTIFIED MAIL**

Dr. Mark Horton  
November 24, 2010  
Page 6

Prime's attempt to avoid the Health and Safety Code's licensing requirements in its acquisition of Alvarado Hospital should be seen for what it is: a brazen attempt to undermine the authority of the CDPH and avoid scrutiny of its extremely questionable and dangerous business practices. If Prime's contention that its acquisition of Alvarado Hospital is not a change of ownership is not challenged, the Health and Safety Code's licensing requirements upon a change of ownership will be eviscerated and anyone, regardless of their criminal records or lack of bona fides will be able to own and operate a hospital by carefully structuring its purchase of the hospital as the acquisition of the membership interests of the licensed entity as Prime has done here. The CDPH cannot permit this to happen.


**III. Requested Action**

We urgently request that the CDPH take immediate action against Prime's continued operation of Alvarado Hospital without a license. Specifically, we request that your Department, pursuant to Health & Safety Code §1290, refer the matter to the District Attorney for prosecution, and bring an action to enjoin Prime from continuing to operate the Hospital without a license as authorized by Health & Safety Code §1291. We note that upon verifying the facts in such a complaint, the court, as a matter of right, is required to issue the injunction. *Id.*; *see also Universal Life Church, Inc. v. State of California*, 158 Cal.App.3d 533, 539 (Ct.App. 1984) ("respondents entitled to an injunction as a matter of right").

Although we believe that Prime's action constitute a straight-forward violation of the Health and Safety Code's prohibition against operating a hospital without a license, at the very last CDPH should withhold renewing the existing license for Alvarado Hospital once it expires on December 31, 2010 at least until the ongoing state and federal investigations into Prime have completed. If CDPH has already granted a renewal of this license, we request that the Department immediately take action to revoke the hospital license.

Sincerely,

Bush Gottlieb Singer López  
Kohanski Adelstein & Dickinson  
A Law Corporation

  
Daniel Bush

cc: Jerry Brown, California Attorney General  
Dave Regan, President SEIU-UHW