

Hearing date: November 18, 2020 at 11:00 a.m.

STATE OF RHODE ISLAND
PROVIDENCE, SC.

SUPERIOR COURT

In re:

CharterCARE Community Board; St. Joseph
Health Services of Rhode Island; and Roger
Williams Hospital

C.A. No. PC-2019-11756

**LIQUIDATING RECEIVER'S PETITION FOR INSTRUCTIONS REGARDING
INDEPENDENT COUNSEL FOR THE CATEGORY A DIRECTORS
OF PROSPECT CHARTERCARE, LLC**

Thomas S. Hemmendinger (the "Liquidating Receiver") hereby petitions this Court for instructions regarding the Category A Directors of Prospect CharterCARE, LLC, on the following grounds:

1. On January 17, 2020, this Court appointed the Liquidating Receiver as permanent liquidating receiver of CharterCARE Community Board ("CCCB"), St. Joseph Health Services of Rhode Island ("SJHSRI"), and Roger Williams Hospital ("RWH") (collectively, the "Legacy Hospital Entities").
2. CCCB is the parent of SJHSRI and RWH. Until June 20, 2014, SJHSRI owned and operated Our Lady of Fatima Hospital in North Providence, Rhode Island, and RWH owned and operated Roger Williams Medical Center in Providence, Rhode Island (the "Local Safety-Net Hospitals").
3. On June 20, 2014, the Legacy Hospital Entities closed on a transaction involving the sale of the Local Safety Net Hospitals to subsidiaries of Prospect CharterCARE, LLC. In connection with the transaction, among other things, CCCB received a 15% membership interest in Prospect CharterCARE, LLC and certain additional rights (collectively, the "Hospital Interests"). The Hospital Interests include the right to an upward adjustment to CCCB's membership interest based on any failure by the majority member Prospect East Holdings, Inc. to

make \$50 million in capital contributions to the hospitals (the “Long-Term Capital Contribution”) for certain capital projects on or before June 20, 2018.¹

4. Prospect CharterCARE, LLC’s June 20, 2014 operating agreement (the “LLC Agreement”) provides for an eight-member board of directors, CCCB has the right to appoint four (the “Category A Directors”), and Prospect East Holdings, Inc., the majority member, has the right to appoint four (the “Category B Directors”).

5. As more fully set forth in the amended and supplemental complaint in *CCCB v. Lee*, C.A. No. PC-2019-3654, pending before this Court, the Category A Directors who were in place when this Court appointed the Liquidating Receiver had breached their fiduciary duties to Prospect CharterCARE, LLC. Therefore, the Liquidating Receiver sought, interviewed, and researched candidates to replace those existing Category A Directors.

6. Once this process was completed, on July 22, 2020, the Liquidating Receiver appointed James H. Aceto, CPA, William J. Lynch, Esq., James P. Riley, and Marc Weinberg, M.D. as the Category A Directors. The Liquidating Receiver selected these gentlemen for their integrity, skills, commitment to supporting the long-term success of Prospect CharterCARE, LLC and the local hospitals, and commitment to the communities that these hospitals serve.

7. However, since shortly after the new directors were appointed, Prospect CharterCARE, LLC and its counsel have used improper and unwarranted means to prevent the Category A Directors from communicating with the Liquidating Receiver or others and from performing their duties or exercising their rights. Some of these actions are manifest attempts to muzzle and intimidate the Category A Directors. All of these actions violate this Court’s stay against

¹ As of the date of this petition, Prospect East has failed to establish that it has funded the Long-Term Capital Commitment.

interference with the Liquidating Receiver's administration of receivership property.²

8. In the face of this misconduct by Prospect CharterCARE, LLC, the Category A Directors have engaged Matthew T. Oliverio, Esq. and his firm Oliverio & Marcaccio LLP (collectively, "Independent Counsel") to advise them, to represent them before this Court, and to represent them in any disputes with Prospect CharterCARE, LLC, any other Prospect entities, or any other persons associated with a Prospect entity.

9. The Liquidating Receiver believes that it is essential to the liquidating receiverships that the Category A Directors have their own legal counsel, and that Independent Counsel is well-suited to serve this role.

10. The Category A Directors have asked the Liquidating Receiver to pay the fees and expenses of Independent Counsel in the first instance, and have agreed to assist the Liquidating Receiver in recovering such payments under the indemnity provisions in the LLC Agreement or under other legal or equitable principles.

11. The Liquidating Receiver believes that the request and undertaking of the Category A Directors is fair and reasonable, and will provide a net benefit to the liquidating receiverships.

WHEREFORE, the Liquidating Receiver prays that this Court:

(a) Authorize and instruct the Liquidating Receiver to pay the fees and expenses of Independent Counsel, reserving to the Liquidating Receiver the right to seek recovery of all such amounts from Prospect CharterCARE, LLC and others.

(b) Award to the Liquidating Receiver such other and further relief as this Court deems

² The details of Prospect's wrongful actions, the Category A Directors' compliance with all of their obligations as directors, and the good-faith efforts of the Category A Directors and the Liquidating Receiver are set forth in the Liquidating Receiver's objection to the Prospect entities' motion to adjudge the Plan Receiver in contempt (copy without exhibits attached hereto as Exhibit A).

In re CharterCARE Community Board et al.

C.A. No. PC-2019-11756

appropriate.

Respectfully submitted,

Date: November 6, 2020

/s/ Thomas S. Hemmendinger
Thomas S. Hemmendinger #3122
Liquidating Receiver
Brennan, Recupero, Cascione, Scungio &
McAllister, LLP
362 Broadway
Providence, RI 02909
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CERTIFICATE OF SERVICE

I hereby certify as follows:

- 1) On November 6, 2020, I electronically filed the foregoing document. This document is available for viewing and/or downloading from the Rhode Island Judiciary's Electronic Filing System.
- 2) The following parties received electronic notice: any parties entered to be notified through the Electronic Filing System.
- 3) The document was served by United States Postal Service, postage prepaid, on the following persons: see separate certificate of service.

/s/ Thomas S. Hemmendinger
Thomas S. Hemmendinger

Exhibit A
**(Liquidating Receiver’s Objection to
Prospect Entities’ Motion to Adjudge Plan
Receiver in Contempt—without exhibits)**

Hearing date: October 9, 2020 at 11:00 a.m.

STATE OF RHODE ISLAND
PROVIDENCE, SC.

SUPERIOR COURT

ST. JOSEPH HEALTH SERVICES OF
RHODE ISLAND, INC

v.

ST. JOSEPH'S HEALTH SERVICES OF
RHODE ISLAND RETIREMENT PLAN, as
amended

C.A. No. PC-2017-3856

**LIQUIDATING RECEIVER'S OBJECTION TO THE PROSPECT ENTITIES' MOTION
TO ADJUDGE PLAN RECEIVER IN CONTEMPT**

Thomas S. Hemmendinger (the "Liquidating Receiver") hereby objects to the motion (the "Contempt Motion") by Prospect Medical Holdings, Inc., Prospect East Holdings, Inc., and Prospect CharterCARE, LLC (collectively, the "Prospect Entities") to adjudge Stephen Del Sesto (the "Plan Receiver"), the permanent receiver of the St. Joseph Health Services of Rhode Island Retirement Plan, in contempt.

The Contempt Motion not only seeks to hold the Plan Receiver in contempt, but it also seeks an order requiring the Liquidating Receiver to (1) withdraw his objection to the Prospect Entities' pending application to the R.I. Department of Health for approval of an effective change in control and (2) "cease instructing the Category A Directors to supply [the Receivers] with documents and information relevant to the pending litigation[.]" Contempt Motion, p. 9.

The Contempt Motion has no basis in fact or law, and counsel for the Prospect Entities must have known that when they signed and filed the Contempt Motion.

Statement of Facts

On January 17, 2020, this Court appointed the Liquidating Receiver as permanent

liquidating receiver of CharterCARE Community Board (“CCCB”), St. Joseph Health Services of Rhode Island (“SJHSRI”), and Roger Williams Hospital (“RWH”) (collectively, the “Legacy Hospital Entities”).

CCCB is the parent of SJHSRI and RWH. Until June 20, 2014, SJHSRI owned and operated Our Lady of Fatima Hospital in North Providence, Rhode Island, and RWH owned and operated Roger Williams Medical Center in Providence, Rhode Island (the “Local Safety-Net Hospitals”).

On June 20, 2014, the Legacy Hospital Entities closed on a transaction involving the sale of the Local Safety Net Hospitals to subsidiaries of Prospect CharterCARE, LLC. In connection with the transaction, among other things, CCCB received a 15% membership interest in Prospect CharterCARE, LLC and certain additional rights (collectively, the “Hospital Interests”).

Prospect CharterCARE, LLC’s June 20, 2014 operating agreement (the “LLC Agreement”) provides for an eight-member board of directors, CCCB has the right to appoint four (the “Category A Directors”), and Prospect East Holdings, Inc., the majority member, has the right to appoint four (the “Category B Directors”). Therefore, each director is a “constituency director” for the member who appointed him or her.¹

The LLC Agreement also contains a conflict of interest policy (the “LLC Conflict Policy”) and obligated Prospect CharterCARE, LLC to adopt it for its directors and certain employees. Exhibit A hereto. This is the only operative conflict of interest policy for Prospect CharterCARE. Prospect CharterCARE, LLC has not identified any other applicable conflict policy, nor has it identified any confidentiality requirement other than what is contained in the

¹ A “constituency director” is one who is appointed by a particular owner of the company. E. Norman Veasey and Christine T. Di Guglielmo, “How Many Masters Can a Director Serve? A Look at the Tensions Facing Constituency Directors,” 63 Bus. Law. 761 (May 2008) (hereinafter, “Veasey”).

LLC Conflict Policy.

In 2017, at the request of SJHSRI, this Court appointed Stephen Del Sesto (the “Plan Receiver”) as receiver of the Plan. On June 18, 2018, after an investigation by Wistow, Sheehan & Loveley, PC (“Special Counsel”), special counsel to the Plan Receiver, the Plan Receiver and certain Plan participants as putative class representatives sued the Legacy Hospital Entities, various Prospect entities, various Roman Catholic organizations, and others to recover damages for the benefit of the Plan and its participants. (*Del Sesto et al. v. Prospect CharterCARE, LLC et al.*, C.A. No. 18-cv-00328-WES (D. R.I.), and *Del Sesto et al. v. Prospect CharterCARE, LLC et al.*, C.A. No. PC-2018-4386 (R.I. Super.)).

In 2018, subject to approval by this Court and the U.S. District Court for the District of Rhode Island, the Legacy Hospital Entities, and the Plan Receiver, and the putative class-action representatives entered into a Settlement Agreement dated as of August 31, 2018 (the “Settlement Agreement”), under which, among other things, CCCB agreed to hold the Hospital Interests in trust for the Plan Receiver on account of the Plan Receiver’s claims against the Prospect Entities and others in the litigation described above.

This Court and the U.S. District Court each approved the Settlement Agreement. This Court’s November 16, 2018 order approving the Settlement Agreement states as follows:

The Petition for Settlement Instructions is granted, and the PSA [Proposed Settlement Agreement] may be filed with the Federal Court at an appropriate time for approval. The PSA is approved for purposes of this proceeding, subject to the following two conditions: (1) the Receiver refrains from exercising any rights under the PSA prior to the federal court’s determination of whether to approve the PSA; and (2) until such time as the determination in condition 1 is made, then, prior to implementing, or directing that CCCB implement, any rights, whatsoever, in favor of the [Plan] Receiver (or the Plan) derivative of CCCB’s rights in CCF [CharterCARE Foundation] or PCC [Prospect CharterCARE,

LLC], the [Plan] Receiver must provide all parties, including but not limited to the Objectors, with twenty (20) days written notice. All prior Orders remain in full force and effect.

This Court's permanent order appointing the Liquidating Receiver authorized and directed the Liquidating Receiver "to hold and administer the Hospital Interests in trust solely for the benefit of the Plan Receiver according to and subject to the terms of the Settlement Agreement, including but not limited to prosecution of CharterCARE Community Board v. Samuel Lee, et al., PC-2019-3654." The permanent order also directed the Liquidating Receiver to perform the Legacy Hospital Entities' obligations under the Settlement Agreement:

7. That the Liquidating Receiver on behalf of the Petitioners shall perform and continue to perform their obligations under the Settlement Agreement, . . .

Without having assumed the Settlement Agreement, the Liquidating Receiver has been performing all of the Legacy Hospital Entities' current obligations under it.

The permanent order appointing the Liquidating Receiver also contains the following injunction:

9. That . . . the interference with the Liquidating Receiver's taking possession of or retaining possession of any such property [i.e., property of the Legacy Hospital Entities], . . ., by any of such parties aforesaid, other than the Liquidating Receiver designated as aforesaid, or the termination of services relating to the [Legacy Hospital Entities], without obtaining prior approval thereof from this Honorable Court, in which connection said Liquidating Receiver shall be entitled to prior notice and an opportunity to be heard, is hereby restrained and enjoined until further Order of this Court. However, (1) this injunction shall neither restrain nor enjoin the Plan Receiver and his attorneys and agents in any way concerning Hospital Interests, and the Plan Receiver and his attorneys and agents are authorized to take such steps as they deem

appropriate to protect such Hospital Interests . . .

On March 11, 2019, CCCB commenced a civil action in this Court (C.A. No. PC-2019-3654, hereafter “*CCCB v. Lee*”) against Prospect East Hospital Advisory Services, Prospect CharterCARE, LLC, the directors of Prospect CharterCARE, LLC, Prospect East Holdings, Inc., Prospect Medical Holdings, Inc., various affiliates of theirs, and a number of individual and entity John Does, seeking, among other things:

(a) Specific performance of the entity defendants’ obligations to fund the Long Term Capital commitment, both derivatively and non-derivatively.

(b) Specific performance of the entity defendants’ contractual and statutory obligations to provide access to the business and financial records of Prospect CharterCARE, and information concerning the funding of the Long Term Capital Commitment, including sufficient information for CCCB and the Plan Receiver to evaluate the put option and determine whether to exercise it.

(c) Specific performance and damages against the individual defendants, Prospect East, and Prospect Advisory for breach of fiduciary duty and for aiding and abetting the breach of fiduciary duty, both derivatively and non-derivatively.

(d) Damages and other relief under the Uniform Fraudulent Transfer Act (now the Uniform Voidable Transactions Act) for transfers related to distributions from various Prospect entities and related to obligations incurred to secure the financing that funded those distributions.

(e) Declaratory relief, including the reformation of the LLC Agreement to give CCCB sufficient time to decide whether to exercise the put option.

In November 2019, various Prospect entities applied to the Rhode Island Department of Health for approval of an effective change in control of the Prospect CharterCARE subsidiaries that operate the Our Lady of Fatima Hospital and Roger Williams Medical Center. As of February 19, 2020, the Prospect entities resubmitted their applications. These Prospect entities also applied to the Rhode Island Attorney General for approval of the effective change in control under Rhode Island’s Hospital Conversion Act.

The Liquidating Receiver and the Plan Receiver learned of these applications only in March 2020.

According to all of these applications, the current owners of the local Prospect entities' ultimate parent company are Samuel Lee, David Topper (through a family trust), and various private equity funds and investors.² The applications seek approval of transactions that would result in Messrs. Lee and Topper owning 100% of the ultimate parent company in exchange for Prospect Medical Holdings—not Lee or Topper—paying the private equity investors almost \$12 million plus an undisclosed amount required to buy out certain options.

After the receivers and Special Counsel reviewed and investigated the applications on April 9, 2020 the Liquidating Receiver and the Plan Receiver timely objected and asked the Department of Health to deny the applications on several grounds, including:

(a) The applications are materially incomplete. For example, they fail to disclose material litigation, including *CCCB v. Lee*, in which Mr. Lee, Mr. Topper, and various Prospect entities are defendants.

(b) The applications misrepresent and fail to disclose material terms of the proposed change in control transactions, including the price to buy out the options referred to above.

(c) The proposed transactions fail to identify any benefit to the paying entity, Prospect Medical Holdings, Inc. This entity is also a guarantor of Prospect East's Long-Term Capital Commitment. Therefore, consummation of the change in control transactions would impair the Prospect entities' ability to fund that commitment.

(d) The applications misrepresent the financial condition of Prospect CharterCARE, Prospect Medical Holdings, and the Prospect CharterCARE subsidiaries who own Our Lady of Fatima Hospital and Roger Williams Medical Center (Prospect CharterCARE SJHSRI, LLC and Prospect CharterCARE RWMC, LLC). For example:

(1) According to financial statements submitted with the applications, these entities do not have sufficient current assets to fund their operations, much less the

² Messrs. Lee and Topper are defendants in *CCCB v. Lee*.

amounts described in the change in control transactions.

(2) These entities are guarantors of loans that were used in part to fund at least \$457 million in dividends to owners of Prospect Medical Holdings, including Lee and Topper.

On April 21, 2020, based on the Prospect applications to the regulators, the receivers' investigation thereof, and other investigations, the Liquidating Receiver and the Plan Receiver filed a First Amended and Supplemental Complaint in *CCCB v. Lee*. The amended and supplemental complaint adds facts and causes of action uncovered in these investigations.

On July 21, 2020, the Department of Health's Health Services Council commenced its hearing on the Department of Health applications on July 21, 2020. At the hearing, Special Counsel spoke on behalf of both Receivers in opposition to the applications. The Receivers were treated as members of the public as to their objections. The Health Services Council recessed its hearing and will continue it at a later date, tentatively October 13, 2020.³

As more fully set forth in the amended and supplemental complaint in *CCCB v. Lee*, the Category A Directors who were in place when this Court appointed the Liquidating Receiver had breached their fiduciary duties to Prospect CharterCARE, LLC. Therefore, the Liquidating Receiver sought, interviewed, and researched candidates to replace those existing Category A Directors. Affidavit of Thomas S. Hemmendinger, hereinafter "Liq. Receiver Aff.," ¶ 10 (Exhibit C hereto).

Once this process was completed, on July 22, 2020, the Liquidating Receiver appointed James H. Aceto, CPA, William J. Lynch, Esq., James P. Riley, and Marc Weinberg, M.D. as the

³ The Department of Health and the Attorney General have extended the deadline for their decisions on the Hospital Conversion Act application to November 5, 2020. Their decision was based on questions about the financial impact of the covid-19 pandemic on the local hospitals, the delay in the Prospect entities providing documents to the Department and to the Attorney General, the implications of certain Prospect transactions, and unanswered questions about the proposed transaction.

Category A Directors. Liq. Receiver Aff. ¶ 10. The Liquidating Receiver selected these gentlemen for their integrity, skills, commitment to supporting the long-term success of Prospect CharterCARE, LLC and the local hospitals, and commitment to the communities that these hospitals serve. Liq. Receiver Aff. ¶ 11.

In his communications the new Category A Directors, the Liquidating Receiver shared information and documents related to the governance of Prospect CharterCARE, LLC and to the Liquidating Receiver's concerns about the financial condition of Prospect CharterCARE, LLC and its subsidiaries. Liq. Receiver Aff. ¶ 12. The Liquidating Receiver also made it clear to the new directors that they should not take the Liquidating Receiver's claims on faith, but should make their own independent determinations and take such actions as they deemed consistent with their duties and rights as directors. Liq. Receiver Aff. ¶ 13.

At no time did the Liquidating Receiver ask the Category A Directors to share with the Liquidating Receiver, the Plan Receiver, or Special Counsel any confidential information or documents they obtained in the course of their service as directors. Liq. Receiver Aff. ¶ 14.

In fact, each Category A Director has acknowledged both his fiduciary duty to Prospect CharterCARE, LLC and his duty to keep certain information and documents confidential. For example, on August 25, 2020 at the Category A Directors' request, the Liquidating Receiver wrote to Prospect CharterCARE, LLC's chief executive officer Jeffrey Liebman, copied to its counsel Mark Russo, Esq. as follows:

The new directors acknowledge that they owe a fiduciary duty to Prospect CharterCARE, LLC. The same is true for the Category B Directors and for all officers.

...

The new directors understand that, subject to applicable law that

requires or permits disclosure to protect the interests of the entity, a director may not, on his or her own, disclose information that is covered by a valid (i) privilege held by the entity or (ii) obligation not to disclose confidential information. In particular, a director may not share the entity's litigation strategy with the entity's opponent in litigation.

Exhibit B hereto (August 25, 2020 letter from the Liquidating Receiver to Jeffrey H. Liebman).⁴

Further, last month the Category A Directors fully complied with the LLC Conflict Policy, including its confidentiality provisions, by completing, signing and submitting their conflict of interest disclosures to Prospect CharterCARE, LLC. Exhibit B hereto (September 25, 2020 email from the Liquidating Receiver to Miriam Cauley, Esq.—without attachments).

The LLC Conflict Policy includes confidentiality provisions. Exhibit A hereto, p. 1. In September 2020, each Category A Director formally accepted these by completing the disclosure form attached to the 2011 policy and submitting it to Prospect CharterCARE, LLC.

The Category A Directors sought in good faith to obtain information and documents to which they have an absolute right, that is:

- 1) Proposed dates and times for an initial meeting of the Category A Directors with CEO Jeffrey Liebman (first requested August 25, 2020).
- 2) An agenda for such initial meeting (first requested August 25, 2020).
- 3) Year-to-date financial reports on Prospect CharterCARE, LLC and its subsidiaries (first requested August 25, 2020).
- 4) The revised financial statements submitted to the R.I. Attorney General and the R.I. Department of Health on August 11 (first requested August 25, 2020).
- 5) The documents authorizing and justifying the pending Hospital Conversion Act and Change

⁴ Exhibit B hereto is, collectively, the relevant correspondence between the Liquidating Receiver or the Category A Directors, on the one hand, and Prospect CharterCARE, LLC or its counsel, on the other.

in Effective Control applications from the perspective of Prospect CharterCARE, LLC and its subsidiaries (first requested August 25, 2020), each of which applications was signed by Dr. Liebman.

- 6) The schedule for Prospect CharterCARE, LLC board meetings (first requested August 25, 2020).
- 7) Copies of any policies or codes governing all directors or officers (first requested August 25, 2020).
- 8) Confirmation that the Category A Directors are covered by Prospect CharterCARE, LLC's directors and officers liability insurance policy to the same extent as all other directors (first requested August 25, 2020).
- 9) A copy of the directors and officers liability insurance policy (first requested August 25, 2020).
- 10) Copies of the minutes of all Prospect CharterCARE, LLC board of directors meetings since June 20, 2014 (the date on which Prospect CharterCARE, LLC and its subsidiaries took ownership and management of Our Lady of Fatima Hospital and Roger Williams Medical Center—the "Local Safety-Net Hospitals"), including all minutes of any and all executive sessions during that same period, with any appropriate redactions for discussion of litigation strategy in the cases involving either the plan receiver or the liquidating receiver (first requested September 8, 2020).

Exhibit B hereto (October 5, 2020 email from the Liquidating Receiver to Mark Russo, Esq.).

Notwithstanding these facts, since shortly after the new directors were appointed, Prospect CharterCARE, LLC and its counsel have used improper and unwarranted means to prevent the Category A Directors from communicating with the Liquidating Receiver or others and from performing their duties or exercising their rights. Some of these actions are manifest attempts to intimidate the Category A Directors. All of these actions violate the stay in paragraph 9 of the order appointing the Liquidating Receiver.

For example, as of the date of this objection, despite requests dating back to August 25, 2020, Prospect CharterCARE, LLC has given the Category A Directors only item on this list: a

September 11, 2019 conflict of interest policy for “Covered Staff.” Exhibit B hereto (August 31, 2020 email from Sheila Capobianco, September 2, 2020 email from Miriam Cauley, Esq., and September 4, 2020 email from Ms. Cauley). This 2019 policy applies by its own terms only to employees and medical staff. This leaves the LLC Conflict Policy as the only possibly applicable policy.

Prospect CharterCARE, LLC has compounded its failure to provide requested and necessary information and documents by attempts to muzzle and intimidate the Category A Directors. For example:

Since August 6, 2020 Prospect CharterCARE, LLC has tried to prevent the Category A Directors from communicating with the Liquidating Receiver or his counsel.

Prospect CharterCARE, LLC has without explanation continued to insist that the Category A Directors submit to a conflict of interest policy that does not even apply to them.

Prospect CharterCARE, LLC has effectively refused to accept the Category A Directors’ tender of the required disclosures and acceptance of confidentiality provisions under the 2011 policy that does apply to them.

Prospect CharterCARE, LLC has tried to force the Category A Directors to agree to an unconscionable, unwarranted, and unnecessary confidentiality agreement.

Prospect CharterCARE, LLC, probably with the involvement of its lawyers, made demonstrably false statements to (a) the broker for the directors and officers liability policy, putting coverage in jeopardy (see September 18, 2020 letter from Lockton Insurance Brokers to Frank Castro at Prospect Medical Holdings, Inc.) and (b) the Category A Directors (see Miriam Cauley’s September 20, 2020 email to the directors).

Prospect CharterCARE, LLC, through counsel, has made demonstrably false allegations that the Category A Directors intend to seek information and documents to pass on to me as liquidating receiver.

Exhibit B hereto.

In the face of all these facts, the Prospect Entities filed the Contempt Motion.

Argument

I. The Prospect Entities have presented no evidence—because none exists—to support their allegation against the Liquidating Receiver.

B. The Plan Receiver has not directed the Liquidating Receiver to do what the Liquidating Receiver has done.

The Prospect Entities allege that “beginning in July of 2020 the Plan Receiver and Special Counsel also directed the Liquidating Receiver to replace four directors of PCC [Prospect CharterCARE, LLC] and to seek to use the newly appointed directors to obtain documents and information to benefit the Plan Receiver and the Liquidating Receiver in the various lawsuits that they filed against the Prospect Entities . . .” Contempt Motion, p. 2 and pp. 7 - 8.

However, the only evidence they produce to support this allegation is the Liquidating Receiver’s July 22, 2020 letter appointing the new Category A Directors. Contempt Motion, Exhibit E. This letter says nothing about information, documents or the Liquidating Receiver’s purposes in appointing the new directors.

In fact, neither the Plan Receiver nor Special Counsel has ever demanded, directed, or instructed the Liquidating Receiver to do or refrain from doing anything in his capacity as Liquidating Receiver. Liq. Receiver Aff. ¶ 9. Nor would the Liquidating Receiver have accepted any such instruction. Liq. Receiver Aff. ¶ 9.

B. The Category A Directors would not give confidential information or documents to the Liquidating Receiver or others, and the Liquidating Receiver has not tried to get them to.

The Prospect Entities also allege that “PCC [Prospect CharterCARE, LLC] was and

remains concerned that the newly appointed directors are using their position to obtain documents and information to benefit the Plan Receiver and the Liquidating Receiver in the various lawsuits that they have filed against the Prospect Entities.” Contempt Motion, p. 8.

This professed concern is utterly baseless, and the Prospect Entities *do not even try to cite any evidence for it*.

In truth, as shown by undisputed evidence, the Liquidating Receiver has never sought to use the Category A Directors to obtain information to which he is not entitled. Liq. Receiver Aff. *passim*. Further, the Category A Directors have acknowledged and agreed to their responsibilities.

Therefore, the Contempt Motion has no basis in fact.

II. The Liquidating Receiver may continue to exercise his rights and remedies as the minority member in Prospect CharterCARE, LLC.

A. The 20-day notice does not even apply to the Liquidating Receiver, so it imposes no restrictions on the Liquidating Receiver’s actions.

The Prospect Entities make backhanded claims that the Liquidating Receiver has violated the 20-day notice requirement in this Court’s November 16, 2018 order. Contempt Motion, pp. 2, 5 – 6, and 7.

However, by its terms, the notice requirement does not apply to the Legacy Hospital Entities. Further, the Court entered the November 2018 Order more than a year before the Liquidating Receiver’s appointment, and the Court has not made the notice requirement applicable to the Liquidating Receiver.

Moreover, as demonstrated above, the actions the Liquidating Receiver has taken have been on his own, and not at the direction of the Plan Receiver or Special Counsel. This is also the case for any actions the Liquidating Receiver has taken jointly with the Plan Receiver, such as

objecting to the CEC application and offering assistance to the regulators in their investigations of the CEC application and the Hospital Conversion Act application.

B. The Liquidating Receiver has been, and may continue to, pursue his rights and remedies.

The only relevant order governing the Liquidating Receiver's actions is the January 17, 2020 order appointing him permanent liquidating receiver. The Liquidating Receiver has acted within the scope of his authority. The Liquidating Receiver has also reported to this Court on his actions described in this objection, and the Court has approved those actions.

Therefore, the Liquidating Receiver may continue to pursue his rights and remedies as the minority member of Prospect CharterCARE, LLC.

III. The Category A Directors have the right to communicate with the Liquidating Receiver and others.

Under Rhode Island law, each manager of a limited liability company owes a fiduciary duty to the company. R.I. Gen. Laws § 7-16-17(a) ("A manager shall discharge his or her managerial duties in good faith, with the care that an ordinarily prudent person in a similar position would use under the circumstances, and in the manner the manager reasonably believes to be in the best interests of the limited-liability company."). The manager of a limited liability company is "a person . . . designated by the members of a limited-liability company to manage the limited-liability company." R.I. Gen. Laws § 7-16-2(19).

Under Prospect CharterCARE, LLC's 2014 LLC agreement, its affairs are in the hands of a "manager" (Prospect Medical Holdings or one of its affiliates) and of a board of directors, made up of the Category A Directors (appointed by CCCB) and the Category B Directors (appointed by Prospect East Holdings, Inc.).

Therefore, the members of Prospect CharterCARE, LLC's board of directors owe a

fiduciary duty to Prospect CharterCARE, LLC.

On entity law questions where Rhode Island courts have not ruled, they often look to Delaware case law for guidance. See, e.g., *Bove v. Community Hotel Corp. of Newport, Rhode Island*, 105 R.I. 36, 41–42, 249 A.2d 89, 93 (1969) (Delaware’s case law “are generally considered to be the leading ones in the field”).

To the best of the Liquidating Receiver’s knowledge, Rhode Island’s courts have not ruled on the rights and duties of a “constituency director” or the owner who appointed him or her. Therefore, it is appropriate for this Court to look to Delaware law on to subject.⁵

Under Delaware law, each constituency director owes his or her fiduciary duty to the LLC and to the members. *Veasey*, 63 Bus. Law. at 767. In the case at bar, this applies equally to the Category A Directors and the Category B Directors.

If the interests of the members and the LLC differ, the business judgment rule determines the director’s duties. *Id.* For example, if the appointing member seeks long-term profitability rather than short-term gain, its constituency directors are entitled to seek long-term value, even if the other member seeks only short-term gain. *Veasey* at 767-68 (quoting the American Law Institute’s PRINCIPLES OF CORPORATE GOVERNANCE).

In the case at bar, the Category A Directors are entitled to work for the long-term survival and success of Prospect CharterCARE, LLC, even though the Category B Directors may seek the opposite.⁶

⁵ While the *Veasey* article concentrates on corporations, shareholders, and directors, it recognizes that the principles set forth in the article apply also under “[a]lternate entity laws” such as a limited liability company act. *Veasey*, 63 Bus. Law. at 775.

⁶ Based on the allegations in the amended and supplemental complaint in *CharterCARE Community Board et al. v. Samuel Lee et al.*, C.A. No. PC-2019-3654 (R.I. Super.).

IV. The Category A Directors may advocate in the Board of Directors for any action that they reasonably believe is in the best long-term interests of Prospect CharterCARE, LLC, the local hospitals, and the communities they serve.

A constituency director “should be permitted to promote and vote in favor of the sponsor’s interest, so long as the board is aware of those interests and the entire board is involved in the decisionmaking process.” Veasey, 63 Bus. Law. at 771. This is especially the case where, as is the case with the Category A Directors, the constituency directors do not constitute a majority of the board. *Id.* at 773.

For such advocacy to take place, it is obviously essential that the constituency director and his or her sponsor communicate with each other—subject of course to the director’s duty to keep certain matters confidential. *Id.* at 775.

In the case at bar, the Category A Directors have acknowledged their fiduciary duty to Prospect CharterCARE, LLC, and there is no risk that they will disclose confidential information to the Liquidating Receiver. Therefore, the Liquidating Receiver may provide information and documents to the Category A Directors and ask them to make inquiries on matters of concern and to pursue such actions as the Category A Directors deem consistent with their rights and duties as directors. These actions include advocacy for policies and decisions to promote Prospect CharterCARE, LLC’s success in achieving the long-term growth and success of the company and of the Local Safety Net Hospitals.

V. Prospect CharterCARE, LLC has violated the injunction in this Court’s order appointing the Liquidating Receiver.

As noted above, on January 17, 2020, this Court issued an injunction against “ the interference with the Liquidating Receiver’s taking possession of or retaining possession of any [property of the Legacy Hospital Entities]” (January 17, 2020 appointment order, ¶ 9). All

counsel of record in the liquidating receivership, including counsel for the respective counsel of record for the Prospect Entities were served with this order when it was entered. Further, A copy of the order was included with the Liquidating Receiver's appointment of the Category A Directors on July 22, 2020, copied to Messrs. Halperin and Russo.

Therefore, Prospect CharterCARE, LLC has knowingly violated this Court's injunction.

VI. The Prospect Entities' request that the Liquidating Receiver withdraw his objection to the regulatory applications violates Rhode Island's Anti-SLAPP law.

Rhode Island's Anti-SLAPP law protects a person's legitimate exercise of his or her constitutional rights to petition the government and to speak on matters of public concern. R.I. Gen. Laws § 9-33-2.

In objecting to the regulatory applications, the Liquidating Receiver is merely exercising those rights. Because the Prospect Entities have produced no evidence to contradict this basic fact, their request that the Liquidating Receiver withdraw his objection violates the Anti-SLAPP law.⁷ Therefore, the Liquidating Receiver is entitled to reasonable attorneys' fees and appropriate damages.

VII. The Contempt Motion violates Rule 11.

Under Rule 11 of this Court's Rules of Civil Procedure,

The signature of an attorney, self-represented litigant, or party constitutes a certificate by the signer that the signer has read the pleading, motion, or other paper; that to the best of the signer's knowledge, information, and belief formed after reasonable inquiry

⁷ The Plan Receiver's objection to the Contempt Motion establishes this in greater detail from the Plan Receiver's perspective. The Plan Receiver's arguments apply equally to the Liquidating Receiver, and the Liquidating Receiver adopts them. The Liquidating Receiver also joins in the other grounds for the Plan Receiver's objection to the Contempt Motion to the extent they also apply to the Liquidating Receiver.

the pleading, motion, or other paper is well grounded in fact and is warranted by existing law or a good faith argument for the extension, modification, or reversal of existing law, and that the pleading, motion, or other paper is not interposed for any improper purpose, such as to harass or to cause unnecessary delay or needless increase in the cost of litigation. . . . If a pleading, motion, or other paper is signed in violation of this rule, the court, upon motion or upon its own initiative, may impose upon the person who signed the pleading, motion, or other paper, a represented party, or both, any appropriate sanction, which may include an order to pay to the other party or parties the amount of the reasonable expenses incurred because of the filing of the pleading, motion, or other paper, including a reasonable attorney's fee.

R.I. SUPER. R. CIV. P. 11.

As shown above, not only does the Contempt Motion fail to be “well grounded in fact”, it does not even include basic facts to support the Prospect Entities’ requests for relief. Therefore, counsel for the Prospect Entities has violated Rule 11, and the Liquidating Receiver is entitled to reasonable attorneys’ fees.

Conclusion

For these reasons, this Court should deny the Contempt Motion, award to the Liquidating Receiver the reasonable expenses incurred because of the Contempt Motion, including reasonable attorneys’ fees, damages under the Anti-SLAPP law, and award to the Liquidating Receiver such other and further relief as this Court deems appropriate.

Respectfully submitted,

Date: October 6, 2020

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CERTIFICATE OF SERVICE

I hereby certify as follows:

- 1) On October 6, 2020, I electronically filed the foregoing document. This document is available for viewing and/or downloading from the Rhode Island Judiciary's Electronic Filing System.
- 2) The following parties received electronic notice: any parties entered to be notified through the Electronic Filing System.
- 3) The document was served by United States Postal Service, postage prepaid, on the following persons: see separate certificate of service.

/s/ Thomas S. Hemmendinger
Thomas S. Hemmendinger