Hearing Date: February 18, 2010 at 2:30 p.m. (EST)

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UNITED STATES BANKRUPTCY COURT
SOUTHERN DISTRICT OF NEW YORK

In re:	
SAINT VINCENTS CATHOLIC MEDICAL CENTERS OF NEW YORK d/b/a SAINT VINCENT CATHOLIC MEDICAL CENTERS, et al.,	Chapter 11
	Case No. 05-14945 (CGM)
Debtors.	(Jointly Administered)

RESPONSE OF SVCMC TO (I) THE MEDMAL TRUST MONITOR'S MOTION FOR AN ORDER HOLDING SVCMC IN CONTEMPT FROM THE CONFIRMATION ORDER AND GRANTING REMEDIAL RELIEF AND (II) THE STATEMENT OF SUPPORT AND JOINDER IN MOTION OF THE COMMITTEE OF INTERNS AND RESIDENTS/SERVICE EMPLOYEES INTERNATIONAL UNION

TO: THE HONORABLE CECILIA G. MORRIS,
UNITED STATES BANKRUPTCY JUDGE:

Saint Vincents Catholic Medical Centers of New York d/b/a Saint Vincent Catholic Medical Centers and certain of its affiliates ("SVCMC"), through their undersigned counsel, hereby submit this response (the "Response") to: (A) the motion (the "Motion")[1] of the MedMal Trust Monitor (the "Trust Monitor") for entry of an order

[1] Capitalized terms used herein but not otherwise defined shall have the meanings ascribed to them in the Motion.

(i) holding SVCMC in civil contempt of the Confirmation Order, (ii) directing SVCMC's immediate compliance with its past due obligations owed to certain medical malpractice trusts (the "MedMal Trusts") formed under the plan of reorganization confirmed in these cases in 2007 (the "Plan") under the Confirmation Order, Chapter 11 Plan and MedMal Trust Agreements, (iii) entering judgment against SVCMC in the amount of $10 million for alleged actual damages, (iv) enjoining SVCMC from making any further transfer of any asset or encumbering any asset unless and until such time as SVCMC complies with its past due obligations, and (v) directing SVCMC to provide the Monitor with a full accounting of SVCMC's assets, liabilities, current cash position and all payments previously made or to be made to creditors; and (B) the Statement of Support and Joinder in Motion (the "Joinder") of the Committee of Interns and Residents/Service Employees International Union ("CIR"). In support of the Response, SVCMC respectfully represents as follows:

PRELIMINARY STATEMENT

SVCMC is undergoing a liquidity crisis impacting its current business operations. These difficulties stem, in part, from the wider economic crisis affecting New York State and the Country as a whole. Notably, because of its payor reimbursement mix, SVCMC is dependent upon Medicare and Medicaid reimbursements for its revenues – which have suffered multiple cuts in the last two years as the State and Federal governments face unprecedented deficits. Coupled with SVCMC's low private insurance reimbursement rates and its high level of unreimbursed charity care, SVCMC's revenues are strained.

In this context, late last week, SVCMC met with the Trust Monitor to discuss the issues underlying the Motion. At that meeting, the Trust Monitor expressed concern that, in light of SVCMC's difficulties in funding the MedMal Trusts, the ongoing allowance and payment of medical malpractice claims threatened to deplete the trusts' assets and jeopardized the trusts' continuing ability to pay all such allowed claims over time. SVCMC appreciates the concerns facing the Trust Monitor and the medical malpractice claimants whose interests he represents. Accordingly, SVCMC requested, and the Trust Monitor agreed, that (i) the hearing now scheduled for February 18, 2010 should be treated as a status conference to allow the Trust Monitor's concerns over how the current trust res should be applied to current and future claims to be presented to the Court, and (ii) the parties' respective arguments concerning the substantive relief requested in the Motion, if necessary, be deferred to a later date. SVCMC remains willing to work with the Trust Monitor to address how SVCMC and the MedMal Trusts can and should liquidate and pay medical malpractice claims in light of SVCMC's financial status.

Therefore, although SVCMC believes that there is no basis to grant the relief requested in the Motion, this Response does not present a detailed substantive response to the Trust Monitor's legal arguments. Instead, it principally seeks to apprise the Court of SVCMC's current financial difficulties and the steps it and others are taking to address them.

<u>RESPONSE</u>

<u>Status Report: SVCMC's Current Financial Condition</u>

1. Founded by the Sisters of Charity over 160 years ago, SVCMC operates the only remaining Catholic-sponsored, acute-care hospital network in New

York City. Its core business centers around St. Vincent's Hospital Manhattan (the "Hospital"), located in the Greenwich Village section of Manhattan, which serves as the academic acute-care medical center for New York Medical College. The Hospital is the primary medical center on the West Side of Manhattan from 58th Street south to Battery Park — an area that includes over 250,000 residents, over 900,000 private sector workers and millions of tourists — and offers the only Level One Trauma Center below 114th Street on the West Side of Manhattan. Recognizing the importance of the institution, in December 2006, the New York State Commission on Health Care Facilities in the 21st Century determined that the Hospital is "essential" to the healthcare needs of the West Side of Manhattan.

2. SVCMC and its then debtor-affiliates emerged from Chapter 11 in the summer of 2007 with over $700 million of financial and contractual debt. After emergence, SVCMC took significant steps to improve its operations, reduce costs and increase revenues. Despite these efforts, however, SVCMC has remained burdened with tens of millions of dollars in annual debt service and other payment obligations under the confirmed plan of reorganization (the "Plan"). These obligations, along with continuing declines in private payor and Medicaid reimbursement rates, a historic operating footprint and workforce that are no longer properly matched to the current state of the Hospital's business and the profound effects of the recent economic downturn, caused SVCMC to experience substantial operating losses in each of 2008 and 2009 resulting in a severe cash crisis in the end of 2009. SVCMC began exploring various business transactions with other healthcare providers to allow SVCMC to restructure its operations and

enhance profitability and to preserve the Hospital as an acute care facility on the lower West Side of Manhattan.

3. In an effort to address its problems directly, in late January 2010, SVCMC appointed Mark E. Toney as its Chief Restructuring Officer, and retained the firm of Grant Thornton to act as crisis managers. Working with senior management and the Board, Mr. Toney and the Grant Thornton team are now actively pursuing SVCMC's strategic and tactical options, including devising a business plan, identifying liquidity generating initiatives, negotiating with potential acquirers of various non-Hospital assets, and overseeing all aspects of the restructuring process. In addition, as has been reported in the press, earlier this month, in response to the financial crisis confronting SVCMC, New York State Governor David Paterson formed a "Task Force" of state and federal elected officials, The Department of Health, unions, and key lenders to explore alternatives to preserve the operations of SVCMC on the Lower West Side of Manhattan. The Task Force has been engaged in the restructuring process, having met in person or by phone on nearly a daily basis since its formation two weeks ago.

4. At the same time the Governor formed the Task Force, in order to address certain near-term liquidity issues, New York State and General Electric Capital Corporation ("GE Capital"), as agent for itself and TD Bank, N.A., as co-lender, SVCMC's principal secured lender, arranged an $8 million emergency loan to allow the Hospital and its affiliates to make payroll during the first week of February. Since then, the State and GE Capital have extended a further $6 million loan to sustain SVCMC's immediate operations. While these infusions of capital have temporarily preserved SVCMC's ability to meet its direct operating needs, additional financing will be required

to allow SVCMC to continue operating while it explores long term business solutions. SVCMC may likely be forced to file for protection under Chapter 11 in the near future to address its need for a financial and operational restructuring.

The Trust Monitor's Motion

5. At the end of August 2009, as a result of its cash shortage and increasing financial problems, SVCMC was unable to make a $10 million periodic payment (the "Payment") to the MedMal Trusts. Lacking the cash flow to make such a substantial "legacy" (i.e., contractual Plan obligation) payment from operating revenues, SVCMC entered into discussions with the Trust Monitor concerning alternative methods of payment. Over a period of months, the parties discussed the potential for selling an apartment building in New York City on which the MedMal Trusts held a junior lien (the "Staff House") and using a portion of the net sale proceeds to make the Payment. However, because the anticipated sale proceeds were less than the amount of the senior lien, the contemplated sale required a refinancing of the senior mortgage and the allocation of increased debt to another asset (the real property underlying SVCMC's behavioral health facility in Harrison, New York). The transaction also required the consent of GE Capital. Given SVCMC's deteriorating financial condition, however, this transaction could not be brought to a successful conclusion in the later part of 2009.[2]

6. In response to SVCMC's inability to make the Payment, the Trust Monitor has filed this Motion, seeking to hold SVCMC in civil contempt for failing to

[2] SVCMC and its relevant affiliate are still pursuing the sale of Staff House with the proposed purchaser. Any such sale would no longer involve a complicated refinancing and reallocation of debt, but rather a simple paydown of the secured lender. It is not anticipated that the net sale proceeds will be sufficient to pay fully the senior mortgage and, therefore, there would not be available proceeds for the MedMal Trusts' junior liens.

make the Payment in August 2009 and, on that basis, seeking assorted relief, including (i) the entry of a judgment for $10 million, (ii) an accounting, and (iii) an injunction against the Hospital's making of any payments of any kind pending its making of the Payment.

7. As noted at the beginning, SVCMC reserves its rights to address the merits of the Motion at the proper time, if necessary. However, SVCMC briefly notes that the Motion lacks merit for a variety of reasons, including the following:

- It asserts claims for failure to comply with the payment provisions of the Plan, various implementing agreements and mortgages. Since the Plan was confirmed by order of the bankruptcy court and became effective more than two years ago, these claims are contractual in nature and do not sound in civil contempt. *In re Victory Markets, Inc.*, 221 B.R. 298, 303 (B.A.P. 2d Cir. 1998). *See also* Collier on Bankruptcy ¶ 1129.01[1] (Alan N. Resnick & Henry J. Sommer eds., 16th ed.) ("As to agreed provisions, the plan is a contract between the proponent and those bound by it"). The proper method to assert these claims is through a claim for breach or foreclosure of the MedMal Trusts' liens (subject to any intercreditor requirements due to the junior nature of the MedMal Trusts' liens).

- To the extent that the MedMal Trust Monitor seeks to recover money or property, or to obtain equitable relief such as an injunction or an accounting, he has improperly proceeded by motion. In the bankruptcy court, such relief is only available in the context of an adversary proceeding. See Fed. R. Bankr. P. 7001(1), (9).

- The MedMal Trust Monitor fails to state a claim for civil contempt in any event. Not only has SVCMC failed to violate any clear directive of the confirmation order, but its failure to make the Payment was clearly the result of its inability to pay rather than disregard of its obligations. Indeed, SVCMC and the MedMal Trust Monitor expressly sought to negotiate alternative means for SVCMC to make the Payment from asset sale proceeds and not from operating revenues. Although ultimately unsuccessful, these discussions belie any assertion that SVCMC has flouted a judicial directive.

- The MedMal Trust Monitor is mistaken when he suggests that approximately $18.6 million in distributions in the third and fourth quarters of 2009 were preferential payments. In fact, none of

> SVCMC's general assets were used to pay these legacy claims under the Plan. Rather, these amounts were paid from collateral proceeds or trust fund proceeds resulting from: (i) a settlement entered into by the litigation trust, the proceeds of which were received by the trustee of that trust, not SVCMC, and distributed by the trustee in accordance with the waterfall set forth in section 1.78 of the Plan and (ii) the proceeds of the liquidation of certain notes that were secured by a lien created by the Plan for the benefit of general unsecured creditors and distributed to such creditors in satisfaction of that lien.

<u>Related Concerns of the MedMal Trusts</u>

8. Because the MedMal Trusts are an important constituency of SVCMC, on February 11, 2010, SVCMC met with the Trust Monitor and his counsel to discuss the substance of the Motion and provide him with information concerning the current status of SVCMC's operations and financial condition, discussed above. At that meeting, the Trust Monitor expressed concern that the missed Payment and SVCMC's financial condition will adversely impact the continued operation of the MedMal Trusts. In particular, the Trust Monitor expressed concern that the continued settlements and payment in full of allowed medical malpractice claims could consume all of the current assets of the MedMal Trusts, leaving them unable to pay future claims as and when they become allowed. The Trust documents do not contemplate the situation in which payments made on a "first settled, first paid" basis could deplete the trust funds to the potential detriment of future settled and allowed claims.

9. SVCMC and the MedMal Trust Monitor agreed that these concerns relating to the equitable treatment of all holders of allowed claims against the MedMal Trusts – both current and future claim holders – should be brought to the attention of the Court. SVCMC requested, and the Trust Monitor agreed, that the hearing of the Motion would most productively be treated as a status conference, at

which the parties could inform the Court of the issues facing SVCMC, the issues affecting the MedMal Trusts, as well as potential procedural responses to those issues to protect the interests of current and future holders of allowed claims against the MedMal Trusts.

10. The parties also agreed that litigation of the Motion itself, if necessary, should be deferred for approximately 45 days to allow SVCMC's financial condition and operating strategy to be clarified, including through the work of the Governor's Task Force, as it analyzes options for SVCMC's continued business and healthcare operations. Should litigation of the Motion become necessary, however, SVCMC expressly reserves the right to submit a supplemental pleading fully articulating the various bases for its objection to the relief requested in the Motion.

CONCLUSION

11. For the foregoing reasons, SVCMC respectfully requests that the Court (i) hold a status conference on February 18, 2010 to address the concerns expressed by the MedMal Trust Monitor concerning the operations of the MedMal Trusts, (ii) defer a substantive hearing on the Motion for approximately 45 days, to an appropriate date on the Court's calendar, and (iii) grant SVCMC such other and further relief as the Court deems just and proper.

Dated: New York, New York
February 16, 2010

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